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A new UK policy institution for growth and productivity - a blueprint

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A new UK policy institution for growth and productivity - a blueprint

CHAPTER TEN

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"Recent years have seen a multitude of growth strategies and plans seeking to address the UK's growth problems, aimed at boosting investment, innovation and its diffusion... but a high degree of policy churn has prevented these strategies and plans from having an effect."

The UK has experienced 15 years of poor productivity performance relative to its own past and relative to its peers. Analysis of the UK's productivity problem points towards many contributing factors, discussed in this volume. Addressing the UK's productivity crisis is urgent if the UK is to see sustainable increases in living standards once more, particularly given the headwinds of fiscal constraints and demographic change. Here we argue for a dedicated, independent policy institution, that is unwaveringly focused on finding solutions to the productivity problem. Crucially, such an institution would help with the politics of making difficult long term decisions.

Average annual growth in labour productivity (GVA per hour) in the decade before the financial crisis was around 2%, but has averaged less than 0.5% in the years since. The GDP growth that we have seen since the financial crisis has been largely accounted for by an increase in labour supply which is not expected to continue in the years ahead.

Analysis of the UK's productivity problem points towards many contributing factors, notably chronic private and public sector underinvestment in tangible and intangible assets including skills, a lack of diffusion of productivity-enhancing technologies and practices (between firms and between places), and highly centralised policy-making at the same time as fragmented execution.[1]

While the UK economy has comparative advantages in services and certain areas of high value manufacturing,[2] it appears that these are not being fully exploited. Indeed, much of the productivity slowdown since the financial crisis occurred in 'knowledge economy' sectors which are considered UK strengths.[3]

The productivity gaps between London and the UK's largest cities are also bigger than in comparator countries, and one of the critical routes to improving productivity performance at the national level will involve improving the productivity of our largest cities.[4] The evidence suggests that a higher productivity future will need to see more economic dynamism than in recent years.[5]

Against this background, contemporary challenges also point to an urgent need for increased investment, innovation and structural change - in particular with regard to the UK's legal commitment to meet net zero greenhouse gas emissions by 2050. The Climate Change Committee estimates that additional annual investment will need to rise to £50 billion by 2030 (largely in electricity, buildings and surface transport),[6] and most of this is expected to come from the private sector.[7]

A strategic approach to this investment must consider how to capture the associated growth opportunities,[8] and implies an accelerated and more purposeful approach to 'green' industrial policy.[9] Ongoing technological change, including the rise of generative AI, together with an ageing society, Brexit and geopolitical shifts, also imply a more strategic approach to growth is needed.

The UK therefore stands at a critical juncture. Under significant fiscal pressure following the pandemic and the energy crisis, and in the light of demographic shifts, the government will find it increasingly difficult to increase public spending in response to these challenges. This implies scarce resources will need to be used more productively, and policy levers pulled effectively to catalyse significant amounts of private capital.[10]

Recent years have seen a multitude of growth strategies and plans seeking to address the UK's growth problems, aimed at boosting investment, innovation and its diffusion. Some of these emphasise the need to do so in a manner that is consistent with sustainability and inclusiveness.[11]

But a high degree of policy churn has prevented these strategies and plans (and associated policies) from having an effect, and from being properly evaluated. Crucially, this churn causes uncertainty for businesses (in already uncertain times given recent shocks and global trends) which dampens the incentives for investment.

Such churn applies at a high level (e.g. the UK's Industrial Strategy was launched in 2017, and abandoned in 2021),[12] across core areas of business policy such as corporate tax (with changes every year since 2010[13]) and with respect to detailed policies (e.g. the Growth Voucher Programme, and Help to Grow: Digital, both of which lasted around a year) and support for key technologies (e.g. reversals on carbon capture, usage and storage competitions[14]) or transitions (the recent delay of key net zero targets for cars and homes[15]).

An attempt to strengthen institutions for growth and productivity with the establishment of the independent Industrial Strategy Council by a Conservative government was short-lived, although the Labour Party has proposed relaunching it and placing it on a statutory footing.[16]

Our argument is that a dedicated policy institution, that puts productivity at the heart of the growth agenda, is a key part of the answer. In this chapter, we build on arguments made by the LSE Growth Commission,[17] the Economy 2030 Inquiry,[18] and The Productivity Institute,[19] setting out how a well-designed growth and productivity institution would improve the formulation, implementation and staying power of effective pro-productivity policies. Crucially, such an institution would help with the politics of making difficult decisions where positive outcomes are likely to be felt over the long term.

But even if we agree that such an institution would be valuable, there are questions around its focus, role and institutional design. Many drivers of productivity are long-term, uncertain and intertwined. They are influenced by national, devolved nations', regional and local government as well as external, global factors.

Nevertheless there is precedent that the UK can learn from. In fact the UK stands out amongst a group of 20 other OECD countries for not having some such policy institution. The UK commissions that have taken place have usually involved academics and other key stakeholders and been external to government.

Moreover, growth policy in the UK stands out amongst other core areas of economic policy (including. fiscal, monetary, competition and climate policies) for not having stronger, independent institutions governing it. Lessons from dedicated productivity institutions overseas, and economic policy institutions at home, provide a set of principles that can shape the design of a new growth and productivity institution in the UK. These lessons are summarised in the following sections before we set out key considerations and suggestions on focus, role and institutional design.

At this point we are not prescriptive about the name of a new institution, though we argue that it would be desirable for this to reflect a focus on productivity. Henceforth, we refer generically to a new Growth and Productivity Institution (GPI) for the UK.

"Even if we agree that such an institution would be valuable, there are questions around its focus, role and institutional design."

Lessons from overseas

It is only relatively recently that several OECD countries have established productivity bodies. Typically these are called commissions, boards or councils. Broadly speaking, these institutions aim to highlight the importance of productivity for economic performance, to strengthen understanding about the drivers of productivity, and to provide guidance to governments on policies to strengthen productivity. Today, around 20 pro-productivity institutions operate across the OECD area with Australia's Productivity Commission (founded in 1998) the oldest. From 2010 onwards, several other OECD countries (New Zealand, Denmark, Mexico, Norway and Chile) also established commissions, and these were followed by many EU countries after a recommendation of the EU Council in 2016.

Key features

Table 1 (overleaf) summarises key features of the institution, set-up and reporting framework for 11 of the 20 pro-productivity institutions in the OECD area (for which there is sufficient information). While the missions of the 11 are similar, typically focusing on productivity analysis and advice, the variety in institutional arrangements demonstrates that governments have taken different decisions on how these commissions work and the advice they want them to provide.

In most countries the institutions are independent advisory bodies consisting of three to 12 members, typically appointed by the government. In some countries (Chile, France and Germany) membership mainly consists of academics, possibly supported by government officials.

Other countries (Denmark and Ireland) involve representatives from business and trade unions or draw on expertise from business, as in New Zealand. In contrast, in some countries (Netherlands and Portugal), they are mainly composed of government officials and are closely linked to Economics or Finance Ministries. Institutions often have their own research teams, but also use existing research, for instance from the academic community.

In practice these institutions play a variety of roles: informing the national productivity debate; developing evidence and analysis on productivity growth and its drivers; providing policy recommendations; and contributing to policy discussions nationally or internationally. The bulk of their work has focused on the 'direct' drivers of productivity, such as investment, human capital, innovation, digitalisation and business dynamics.

However they are starting to tackle new questions such as: the rationale for a more focused or targeted innovation policy (New Zealand); resilience and strategic dependencies (Germany); the role of health for productivity (Australia); or policies linked to data and artificial intelligence (Australia, Germany, Ireland). They undertake little work on macroeconomic policy, financial markets and competition policy, possibly as such issues are already addressed by other institutions. Also, few of the commissions have explored the regional dimensions of productivity.

The wide range of issues covered suggests that many pro-productivity institutions take a broad view of their mandate. In taking on such a wide range of issues, important questions emerge related to policy coordination across different parts of government.

Impact

It is difficult to assess formally the impact these institutions have on the national productivity debate, on policy development and implementation, and ultimately on productivity growth. The Australian government has accepted and implemented many of the recommendations of the Australian Productivity Commission (notably in the areas of industry assistance and economic policy, with a more mixed record on social and environmental policy), and the economic benefits (in terms of higher productivity and lower prices) of resulting reforms have been pointed out.[21] New Zealand's commission notes that: "The influence of our work may only emerge over long timeframes, and it may be challenging to directly identify and attribute it to our work."[22]

Table 1: Overview of key Productivity Commissions in the OECD area

INSTITUTION	ESTABLISHED	TYPE OF INSTITUTION	MISSION	LOCATION
Australia Productivity Commission	1998	Standing inquiry body	Promoting productivity-enhancing reforms	Independent, reports to executive and Parliament
Belgium National Productivity Board	2019	Independent advisory body	Examine development of productivity and competitiveness	Independent structure, reports to trade unions and employers' organisations
Chile National Commission for Evaluation and Productivity	2015	Independent advisory body based on presidential decree	Analyse and recommend on policies for productivity and well-being; evaluate regulations and policies	Independent (tacit), reports to the president and government
Danish Economic Council	2017	Independent advisory body (multi-stakeholder)	To analyse productivity and competitiveness	Independent, provides advice to Danish policy makers
Finnish Productivity Board	2021	Independent expert body	Monitor productivity and competitiveness and conduct independent evaluations	Independent expert body linked to Ministry of Finance, reports to government
French National Productivity Council	2018	Independent advisory body of academic economists	Analyse productivity and competitiveness and policies that affect them	Independent, non-partisan advisory body reporting to the Prime Minister and Minister of Finance
German Council of Economic Experts	2019	Independent academic advisory body	Analyse developments in the field of productivity and competitiveness	Independent, provides advice to German policymakers
Ireland National Competitiveness and Productivity Council	2018	Independent council established by government (multi-stakeholder)	Analyse policy and developments in the field of productivity and competitiveness	Independent council, reports to Prime Minister and government
Netherlands Productivity Board	2017	Independent economic research agency	Gain understanding of factors driving productivity growth	Independent agency, part of Ministry of Economic Affairs and Climate Policy
New Zealand Productivity Commission	2011	Standing inquiry body	Improved well-being, improved productivity	Independent, reports to Parliament
Portugal Productivity Council	2018	Joint temporary structure	Monitoring policies related to productivity and support discussion	Joint economic structure of Ministry of Finance and Ministry of Economy

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Lessons from UK institutions

As set out by the LSE Growth Commission in 2017, the UK has strong frameworks governing monetary, fiscal and competition policy. Objectives are defined and enshrined in law, while independent experts play a role in offering advice and in some cases taking policy decisions. The remit of such bodies is transparent, with justifications for their advice presented in statutory publications, and such arrangements have the potential to improve stability and promote external scrutiny.

These institutional features are set out in Table 2 overleaf, which also includes the institutions for infrastructure and climate policy. These provide useful lessons concerning complex areas where many policy levers are relevant, and where outcomes are long-term, requiring significant supply side reform and investment.

While the roles and remits vary from decision-making powers (Bank of England MPC and Competition and Markets Authority) to advisory and monitoring roles (Office for Budget Responsibility, Climate Change Committee and the National Infrastructure Commission), there is a general consensus that previous policy failures such as short-termism, time-inconsistency and accountability failures justify independent decision making or analysis in these areas.

Most of these examples are statutory bodies (i.e. established through legislation) with the exception of the National Infrastructure Commission, which is an Executive Agency of HM Treasury.

As a non-governmental statutory body, accountable to both Parliament and the Chancellor, the OBR is considered to have enhanced the credibility of the UK's economic and fiscal reporting and instilled greater fiscal discipline around government budgets.

The value of the OBR forecasts which accompany fiscal events was brought into stark relief by the fact that a forecast was not requested at the time of the disastrous 'mini-budget' in September 2022. The unfunded tax cuts this included led to market chaos, policy reversals and the departure of the Prime Minister and Chancellor.

By contrast, it has been argued that UK infrastructure decision-making might have benefitted if the National Infrastructure Commission had been on a statutory footing – as was the original intention.[24]

"As a non-governmental statutory body the OBR is considered to have enhanced the credibility of the UK's economic and fiscal reporting."

Table 2: Examples of Institutions in other areas of UK economic policy

INSTITUTION	ROLE	TYPE OF INSTITUTION	MANDATE OR GUIDELINES	LEGISLATION	TRANSPARENT PUBLICATION
Bank of England's Monetary Policy Committee (MPC)	Decision-maker	Public body, answers to Parliament (HoC Treasury Committee)	Inflation target	Bank of England Act 1998, Bank of England and Financial Services Act 2016	Monetary Policy Reports
Office for Budget Responsibility (OBR)	Oversight	Non departmental body	Examine and report on the sustainability of the public finances	Budget Responsibility & National Audit Act 2011. Charter for Budget Responsibility	Economic and Fiscal Outlook (EFO) (accompanying fiscal events). Fiscal risks and long term projections
Competition and Markets Authority (CMA) Board	Decision-maker	Non ministerial department	Duty to promote competition for the benefit of consumers	Competition Act 1998, Enterprise Act 2002, Enterprise and Regulatory Reform Act 2013, Subsidy Control Act 2022	Merger inquiry findings. Market investigation findings
Climate Change Committee	Oversight and advice	Non departmental body	Advise the UK and devolved governments on emissions targets and to report to Parliament on progress made (incl. adaptation)	Climate Change Act 2008	Progress reports. Carbon budgets. Other reports on net zero and adaptation
National Infrastructure Commission	Oversight and advice	Executive Agency, sponsored by Treasury	Provide government with impartial, expert advice on major long-term infrastructure challenges		National Infrastructure Assessment (once in every Parliament). Monitoring reports. Specific studies

Source: Builds on Table 3.1 in LSE Growth Commission; see: UK Growth: A New Chapter, LSE, 2017.

The Industrial Strategy Council (ISC) set up in 2018 (and disbanded in 2021) had some desirable institutional features and was focused on key drivers of growth and productivity.

While not a statutory body, which would have required legislation to close it, it was an independent advisory group within the Department for Business, Energy and Industrial Strategy (BEIS). Its remit was to develop metrics to monitor and evaluate implementation of the 2017 Industrial Strategy White Paper, producing regular progress reports as well as studies on relevant topics.

The remits of the existing institutions included in Table 2, and others (e.g. other regulators, the British Business Bank and the UK Infrastructure Bank), shape and inform growth policy and outcomes in the UK.

But there is a gap in the institutional framework governing UK growth and productivity policies. We note that the proposals set out below are general principles for any government seeking to set up a new GPI – whether in the form of a resurrected ISC (which, in that case, should be stronger and have a broader remit), or an entirely new institution.

Rather than duplicate efforts and analysis with other pre-existing institutions, a new GPI could play a coordinating role. For example, it would complement the Office of Budget Responsibility's work, drawing upon its analyses on the fiscal outlook, but contributing insights on the longer-term productivity impact of government policies or other trends such as technological change.

While the Climate Change Committee advises on and monitors progress towards net zero, the new institution could identify how policies for net zero interact with the need for investment, innovation and economic dynamism for growth – setting out clearly where there are synergies or trade-offs and how to address these.

"Rather than duplicate efforts and analysis with other pre-existing institutions, a new Growth and Productivity Institution could play a coordinating role."

Key considerations

Focus and scope

It is important to be clear about the focus and scope of a newly-launched GPI. 'Productivity' needs to be at the heart of its remit. While many other factors will be critical for the economic future of the UK, including the impacts of climate change and demographic shifts, productivity growth will account for the lion's share of GDP growth and income growth over the next decade.

How broadly should productivity be linked to other key policy domains? One option is to focus on the direct drivers, including investment (such as physical, human and intangible capital provided by public and private sector organisations) and technological change, notably the diffusion of knowledge and technology across firms and regions.

There is likely to be a sectoral or technological (which could be termed 'industrial strategy') element, broadly defined as policies that seek to influence the structure of the economy,[25] and an outward focus on global trends and how the UK interacts with the world will also be necessary. Indeed, the UK's Industrial Strategy Council sought to evaluate government progress across both economy-wide 'horizontal' areas (e.g. skills, innovation) and more specific or 'vertical' objectives (sectors or 'missions').

A GPI should have a broader scope than the Industrial Strategy Council, and should also deal with investment and growth-related issues around trade, foreign direct investment, regulation and competition, planning, 'levelling up', and potentially also net zero and climate change adaptation.

However, the risk of too wide a scope is that the new institution would be thinly spread and fail to supply the detail needed to formulate actionable policy. Given the experience elsewhere, it seems likely it would draw in and coordinate related topics even where these were not explicitly in its remit.

Given those arguments, we recommend a primary focus on the direct drivers of growth and productivity (investment in physical, intangible and human capital), while considering the origin of these drivers (which sectors, places, technologies should be in focus). Specific topics for inquiry could be chosen by government in consultation with the institution's leadership. This would not exclude the possibility of including other domains, but in such cases the institution could rely on the expertise of others and focus on how to connect those themes to design an integrated policy framework. It could therefore also play a coordinating role in good policy design, a role largely absent in the formal UK governance structures.

In other words, the GPI should prioritise areas based on evidence about what drives productivity. The institution should also explicitly consider ensuring that productivity growth is compatible with environmental sustainability and inclusivity,taking into account a UK-wide, devolved nations and regional perspective. One key role of the institution could be to highlight where synergies and trade-offs exist and how they might be addressed, particularly in the short-term.

It would also be important to keep the remit of the GPI high-level and non-contested, so that it could survive changes in political priorities. From this perspective it might not be sensible to link overall objectives of this institution to a specific part of a government's growth agenda – though this will shape priority areas for inquiry.

Remit

There are a number of options for the specific role of a new GPI, with various features that could add value to current policy frameworks. A key feature would be to provide the long-term expertise and capacity needed to conduct analysis that can inform pro-productivity policy recommendations and reporting. This is particularly important given the career structures in the civil service which incentivise frequent moves.

More specifically, the GPI would have the ability, capacity and legitimacy to:

- Conduct inquiries into priority areas agreed with government. Focus on well-defined problems that can be addressed by policy, allowing space for policy entrepreneurs to generate ideas, and supporting policy makers in translating those into detailed, careful, thoughtful, and thorough policy design to make the policies work. The outcome of these inquiries should be actionable and evidence-based recommendations.
- Monitor and evaluate policies against key defined objectives – the implementation of pro-productivity policies, proximate outcomes (e.g. investment as a share of GDP) and ultimately productivity.
- Produce high quality data and reports on productivity and its drivers, based on an understanding of the literature, data and institutional history of the UK and other relevant comparators. This should be a combination of regular reporting on key metrics, and bespoke reports based on specific issues or inquiries. A microeconomic understanding of the drivers of productivity, and barriers to investment (including within firms) will be crucial, as well as how this translates to macro outcomes. Access to non-economic expertise will also be required in many areas (e.g. planning and regulation).

Given that productivity growth is shaped by many areas of policy at national, devolved nations and regional levels, and by the actions of industry, the third sector and civil society, **stakeholder consultation, coordination and communication** should be a key feature. This will improve the legitimacy of recommendations and reports, which should be based on consultation as well as research and analysis, as well as their salience in the public debate. In this way, a key role of a new institution would be to provide a focal point that facilitates policy action.

Data and metrics will be crucial, and a GPI could build capacity in constructing and linking relevant micro-datasets, working with academics and data providers (the ONS, but also government departments, international institutions such as the OECD, and private sector data providers), and using these to monitor and report on trends and evaluate policies where possible. The institution might also advise government on which metrics should be used for monitoring progress.

Evaluation of the GPI itself, against its stated objectives and remit as set out in its mandate, will also be necessary to maximise legitimacy. This will require a robust theory of change along with metrics for monitoring and evaluation. This could build on work by the Economic and Social Research Council (ESRC) in assessing its academic productivity investments (acknowledging shared objectives of providing robust analysis and information, shaping policy and ultimately improving productivity).

> "A microeconomic understanding of the drivers of productivity and barriers to investment will be crucial."

Institutional design

The following principles should guide the design of a new GPI:

- Independence to ensure credibility, and create some distance from political priorities

- Embedded long-term focus, insulated (to the extent possible) from short-term issues and policy churn

- Some flexibility, such that ongoing work and inquiries can be shaped by new developments (e.g. shocks) or changes in government or political realities

- Ability to impact on government machinery and create political leverage, facilitating the political process and creating an environment to solve difficult long-term problems.

Given the multiple policy domains that ultimately impact productivity, it seems most appropriate to set up the GPI as a non-departmental body, reporting to the Cabinet Office. While the objectives and remit of the organisation would be set by the government and Parliament, this would allow the institution to work across relevant policy domains and government departments.

Clearly HM Treasury has a large stake in growth and productivity policies and frameworks (including fiscal policy, structural policies and public sector productivity), whereas other departments relate to specific drivers (for example, innovation, education, infrastructure, regional dimensions or trade). These connections with government departments could be reflected in the composition of a Ministerial Group reviewing the work of the GPI and providing political leverage. A group of civil servants could support the institution on specific topics.

For longevity and accountability, the GPI should be a statutory body, accountable to Parliament. Parliamentary approval is critical to assure longevity and safeguard expertise by committing to the institution while allowing for flexibility to repurpose its formal objectives as required. As the legislation to establish a new body could take time, it may be advisable to start with a simpler non-statutory structure while obtaining buy-in and commitment. This could also facilitate experimentation to see what works while legislation is in progress.

Following good practice elsewhere, the GPI itself could consist of between six and 12 independent commissioners. Depending on the degree of stakeholder coordination, some commission positions may be allocated to independent experts, possibly representing specific constituencies, such as business and workers. Representation from outside London, particularly from devolved nations and regions with the most potential to contribute to productivity growth, will also be needed. The Chair should be fully independent with a strong public profile and well-recognised expertise, analytical capacity and convening power.

To be effective, the GPI will need to be well-resourced. In addition to an administrative support team, it will be necessary to have a strong analytical team, working on a well-defined research agenda determined by the priorities as set by the commissioners, in consultation with government.

The research team may be supported by other research entities outside government or policy analysis teams within government, collaborating as needed. However, reports and analysis should be developed independently, approved by the GPI, presented to both government and Parliament, and with a statutory requirement for government to respond on a committed timetable and set out how it will take forward the policy recommendations (or why it will not).

Conclusion

This chapter has set out the case for a new GPI in the UK and outlined how it might be designed. Would the UK's growth and productivity performance in recent years have been better had this type of institution existed? We think so, encouraged by the evidence from well-established commissions overseas, such as those in Australia and New Zealand.

Given the breadth of policy areas which are potentially influenced by productivity-related interventions, a more coordinated and long-term approach to policy with a pro-productivity focus can be expected to have a positive impact on growth. The need for such a coordinated and comprehensive approach for pro-productivity policies is even more urgent in the light of the consecutive economic shocks from the EU referendum vote, the pandemic and the energy crisis. An independent, enduring institution with the expertise and credibility to shape pro-productivity policy would contribute to the ability of policy makers to take decisions that may not be immediately popular but are in the long-term interests of the nation.

Key takeaways

Addressing the UK's productivity problem requires increased long-term investment in physical, human and intangible capital, and a new Growth and Productivity Institution (GPI) would help to ensure that the appropriate policies are in place to achieve this.

Such a body, placed on a statutory footing to ensure it survives political churn, would provide independent expertise and credibility to shape effective, coordinated and lasting pro-productivity policy.

Through conducting inquiries into key areas, monitoring and evaluating policy, and regular reporting to Parliament, combined with extensive stakeholder consultation, coordination and communication, a new GPI would help with the politics of making difficult decisions where positive outcomes are likely to be felt over the long term.

Experiences setting up similar institutions in other advanced economies, and independent institutions in other areas of policy in the UK provide lessons for the design of a new GPI in the UK.

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