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BusinessLDN submission to the government's 'Invest 2035' green paper

The UK's modern industrial strategy
November 2024

BusinessLDN speaks for over 170 leading businesses in London, spanning a wide range of economic sectors. We strive to make London the best city in the world in which to do business, working with and for the whole UK.

We called for and are helping to develop the Mayor's London Growth Plan, essentially a local industrial strategy, and welcome the opportunity to help shape the government's modern industrial strategy for the UK.

There is much to like in the proposed approach to the modern industrial strategy, including:

- The pledge for policy and regulation to be consistent over time;
- Deliberately playing to the UK's strengths; and
- London earmarked for a key role as a global, urban powerhouse.

Our submission recommends:

- Using the industrial strategy as the governing thought for the Government's growth mission, driving systems thinking across all parts of government and ensuring that policymaking across government is aligned.

- Ensuring that the identified sectors don't 'box in' growth opportunities.

- Focusing on the factors that determine investment location decisions to help target the barriers to investment.

- Optimising the critical cross-cutting enablers of growth, especially people & skills, data, infrastructure, regulation & tax.

The industrial strategy should be used as the governing thought for the government's growth mission, driving 'systems thinking' across all parts of government and ensuring that policymaking across government is aligned…

The government should be more explicit that the industrial strategy will be the governing thought for its growth mission, embedding the growth objective across all of government and its extended regulatory bodies.

That should start with more clearly defined end goal success measures that the industrial strategy will be judged against. These could include, for example, GDP growth, foreign direct investment flows and global impact indicators.

The government should then use the industrial strategy to drive a 'systems thinking' approach right across government. This would require a commitment that all subsequent policy decisions across government will be aligned in service of the industrial strategy goals and priorities. Live examples of where this would result in a change in behaviour include the development of Sustainable Aviation Fuels, which are being championed by the Department for Transport, and yet the supply of available feedstocks is not currently prioritised by the Department for Environment, Food &

Rural Affairs in setting the UK's waste hierarchy. As another example, HM Treasury is currently consulting on reform of business rates without reference to the industrial strategy and a proposed approach that would transfer more of the burden to many of the identified growth sectors.

Care must be taken to ensure that focusing on the identified sectors doesn't 'box in' growth opportunities…

Important elements to the modern industrial strategy are (1) backing growth sectors, but equally important is (2) optimising the horizontal enablers across the economy, which are also important sectors in their own right.

The sectors that the government has identified are all areas where London and the UK have significant strengths and considerable growth potential. But there are important considerations in finalising the sectors to get behind and the approach taken to achieve this:

- It's vital that the industrial strategy attaches equal weight to the 'enabling sectors' in our economy that are intrinsic to the success of the identified growth sectors. Examples that stand out include international connectivity, which is critical for both trade and the movement of talent in a services-driven, island nation economy. Industrial logistics - from supply chain management through to technology & automation - will play a fundamental role in determining the success of the growth sectors and most other leading economies regard it as a core sector. The higher education sector also plays a hugely significant role in supporting both the skills and innovation agendas that so many high-growth sectors depend.

- Insights from our work on 'London as a place to invest' emphasise the importance of not inadvertently sending up a "not wanted here" message to international investors considering investment in a product or service outside of the designated growth sectors, so the messaging of such an approach requires handling with care.

- The industrial strategy is by nature designed to drive long-term thinking. In identifying and supporting the growth sectors of today, it's important that the approach remains open to innovation and emerging sectors. Much of the UK's success in recent years has been derived from combining areas of strength, so for example FinTech, MedTech and EdTech. There is a danger that using a SIC code approach risks missing what sectors look like in the modern economy. Thinking about the fusion of sectors might be one way to think about how emerging sectors and technologies feature in a modern industrial strategy.

- Local growth plans should focus on areas of local strength, as opposed to trying to fit a 'cookie cutter' national strategy. Further devolution should help a focus on the conditions to optimise growth in local economies. Business Improvement Districts are a good example of how hyper-devolution can work in practice and ensure a focus on what really makes a difference for local businesses.

Stepping into the shoes of boards and investors and focusing on the factors that determine investment location decisions will help to target the barriers to investment…

BusinessLDN's research into 'London as a place to invest' has identified the key 'investment location factors' that swing investment decisions. They include:

- The over-riding message is that London's real strength is the breadth & depth of its marketplace. This includes the range of talent and skills that mean whatever or whoever you need, it's available here. It's vital that a modern industrial strategy continues to promote this diversity of ecosystem.

- There is a big need to restore the UK's reputation for policy and regulatory stability, especially in the eyes of long-term investors. Of course, the policy environment must be attractive but equally important is the ability to "price it in" over the duration of the investment. Similarly, international investors emphasise that political signalling to answer the "am I wanted here" question counts for a lot and that a single front door to government for international investors is important to cut through departmental silos.

- Profit-based taxes aren't raised proactively as a big factor. Headline rates of corporation tax need to be ballpark competitive so as not to raise a red flag over the UK. But boards and investors see through this and look at the overall tax burden. The section on taxation in the industrial strategy green papers seems to downplay cost-based taxes which in reality feature more prominently, with business rates highlighted as an area in need of urgent attention, along with the costs of employment for labour-intensive industries.

- London and the UK have developed a 'chicken and egg' problem with low rates of growth. Multi-national firms are not surprisingly pivoting their investments towards higher growth markets such as the US and India. This in turn means that the UK is missing out on productivity-enhancing, high-growth investment opportunities. So, whilst the industrial strategy is inherently long-term in nature, it's important that the government's wider economic policy includes some 'quick wins' to help break out of this low growth trap.

- London's role as a global, urban powerhouse means that it attracts talent from across the UK and from around the globe. Capital cities are often costly places. But the cost of living has now become a significant factor in attracting and retaining talent, even for middle-management and senior roles. Housing is clearly a big component part of this. Seeing through proposed reforms to tackle both planning delays and unpredictability will help developers get to investable decisions quicker.

The industrial strategy should place emphasis on the critical cross-cutting enablers of growth, especially people & skills, innovation, data and infrastructure…

Putting emphasis on the cross-cutting enablers of growth is critical to supporting the identified growth sectors, but also to maintaining the breadth and depth of marketplace that makes London a global, urban powerhouse.

Skills shortages continue to be a barrier to firms' growth ambitions. The skills that businesses most see a demand for in the coming years are for advanced digital skills, sector-specific technical skills and transferable skills. Ensuring that the skills system is demand-led and highly responsive to employer need is the best way to meet current and future skills need. Ways in which this can be done include ensuring that Skills England re-commits to the partnership model underpinning the

Local Skills Improvement Model; devolving National Careers Service funding to London and other Mayoral Combined Authorities; and ensuring collaboration between Skills England and the Migration Advisory Committee with an evidence-based approach to migration policy. More broadly, the industrial strategy should encourage a joined-up approach across government to meeting the labour market needs, aligning policy right across the Department for Education, the Department for Work & Pensions, HM Treasury, the Department for Business, the Home Office and the Ministry for Communities, Housing & Local Government.

Continued investment into Research & Development and investment into universities as a source of innovation and driver of growth in their regions is very important.

Data is intrinsic to the modern economy and supports all of the identified growth sectors. Boosting the capacity around data centres by putting them on an equivalent status to other critical national infrastructure, and tackling the fragmented approach to data sharing that exists across local authorities would be important steps the government could take to improve data-based decision making.

High quality infrastructure is vital for any modern economy and critical to the success of the identified growth sectors. A recent WPI Economics study on behalf of Manchester Airports Group found that established sectors - including financial services, the creative industries and real estate - are particularly reliant on international connectivity for their success. The study also highlighted similar dependency on global connectivity for a number of fast-growing sectors, including advanced manufacturing, life sciences, fintech and advanced digital. Because of the importance of international connectivity, we believe there is a strong case for aviation being a specific foundational sub-sector.

Steps that the government can take to boost the quality of infrastructure across the UK include creating certainty in the project pipeline, and ensuring it includes projects of sufficient maturity and scale; establishing the funding models for new privately funded infrastructure; and encouraging the development of city prospectuses, drawing on the experiences of London & Partners and Opportunity London in marketing the capital.

More detail on these points is set out in the annex, where we provide specific responses to questions 7-9 focused on people & skills, questions 12-13 focused on data, questions 14-16 focused on infrastructure & energy and question 19 on economic regulation & competition.

<u>Annex: responses to specific questions in the Industrial Strategy consultation</u>

Q7. What are the most significant barriers to investment? Do they vary across the growth-driving sectors? What evidence can you share to illustrate this?

The main body of our submission identifies the critical factors driving investment location decisions. These include maintaining a breadth & depth of marketplace, restoring a reputation for policy & regulatory stability, maintaining competitive cost-based taxes, being attractive to globally-mobile talent and breaking out of a 'low growth trap' that is making companies turn to higher-growth markets to invest in.

On taxation, we believe that cost-based taxes such as business rates are an influential factor, with the current rates making UK infrastructure a relatively less attractive asset class to invest in resulting in investment going overseas.

On skills, the BusinessLDN-led London Local Skills Improvement Plan (LSIP) survey published in March 2024 identified barriers to growth that relate to people and skills:

- The majority (57%) of participants cite a low number of suitable applicants with required skills as a primary driver of recruitment challenges,

- A lack of work experience is flagged as the number one reason for unsuitability of job applicants, with two thirds of participants (67%) highlighting it as an issue, ahead of a lack of qualifications (59%) and lack of required attitude, motivation or personality (58%).

- The skills firms are most lacking in are sector specific technical skills (cited by 52% of respondents), followed by cross-cutting transferable skills (43%), basic digital skills (34%), green skills (25%), basic math skills (25%) and English skills (25%).

- Looking to the future, businesses see advanced digital (54%) and sector specific technical skills (47%) as the most needed over the next two to five years.

Beyond these headline findings, we believe that a lack of clear demand signals in key areas, such as in green skills and retrofitting, is a barrier to developing the supply side of skills provision. Employers frequently cite time and cost as barriers to training, especially for SMEs. This is compounded by rigid funding models and the inaccessibility of provision for many.

Q8. Where you identified barriers in response to Question 7 which relate to people and skills (including issues such as delivery of employment support, careers, and skills provision), what UK government policy solutions could best address these?

There are various policy solutions that the government could deploy to address some of these people and skills issues that are a barrier to investment and growth. They include:

- Ensuring that the skills system is equipped with the tools to respond to employer skills needs, for example by ensuring that Skills England recommits to the model of partnership between government, industry and educators that has been successful in the LSIP.

- Aligning national policy and delivery with local priorities, where Skills England also has an important role to play in co-ordinating between national and local/regional skills needs.

- Devolving National Careers Service funding to London and other Mayoral Combined Authorities so that they are able to better shape the service for local people.

- Delivering a joined-up approach to skill development and migration policy, by ensuring that the planned collaboration between Skills England and the Migration Advisory Committee, supports the needs of the labour market, especially in the growth-driving sectors, through an evidence-based approach to migration policy. In practical terms this could mean expanding the Youth Mobility Scheme and ensuring that visa costs and health surcharges are internationally competitive.

Q9. What more could be done to achieve a step change in employer investment in training in the growth-driving sectors?

Measures that would help achieve a step change in employer investment in training include:

- Championing a strong Higher Education sector in driving growth in key growth sectors, such as life sciences, digital and tech.

- Reforming the Growth and Skills Levy. The government's plans to transform the Apprenticeship Levy into a more flexible Growth and Skills Levy, with £40m to help deliver new shorter and foundation courses in 'key sectors' is welcome. Business engagement with Skills England, the new body set up to co-ordinate on skills needs, on the detail of these new courses, is vital. The government should also publish a roadmap towards the more flexible Growth & Skills Levy to boost uptake and avoid a chilling effect on investment in training during the transition.

- There's a huge issue for digital & tech skills in that the pace of change and the skills needed is far outstripping demand. Facilitating more employer-provider collaboration, including industry led training such as workforce exchange partnerships and industry certification of training should be priorities.

- Ensuring that Skills England speeds up the development of new qualifications, including in modular training, to reflect more nimble employer needs.

- Bringing forward the rollout of the Lifelong Learning Entitlement as stated in the Budget to stimulate the market for modular training, including in key areas like green, digital and transferable skills.

- Providing clear demand signals in areas like clean energies. The lack of demand signals from central government on green skills for example are often barriers to investing in a stable green skills pipeline. In key green policy areas such as retrofit, the lack of government policy, or constantly change targets dampens ultimate employer demand, which acts as a barrier to developing the skills supply side. Clear long-term transition plans, targets and KPIs around Net Zero transition would help overcome this.

Q12. How can the UK government best use data to support the delivery of the Industrial Strategy?

Steps that the government can take to best use data to support the delivery of the Industrial Strategy include:

- Drawing on lessons from the trailblazer Data for London programme, to gain insights on data projects, methods and information governance will help get the National Data Library off to the races.

- Focusing the proposed National Data Library on helping to anticipate future trends and driving public-private partnerships to tackle major policy challenges such as mapping the spread of EV chargers and improving air quality.

- Ensuring that the AI Opportunities Action Plan explicitly harnesses the role of data.

- Boosting the capacity around data centres, by putting them on an equivalent status with energy, water, transportation, health, financial services, telecommunications, and emergency services as critical national infrastructure.

Q13. What challenges or barriers to sharing or accessing data could the UK government remove to help improve business operations and decision making?

Barriers to sharing or accessing data that the government could help remove include:

- Tackling the fragmented approach to data sharing that exists across local authorities. Currently, each local authority has the autonomy to decide what data to share, making it challenging to put together a whole picture at the same standard or level of granularity. For example, for the same data request submitting under FOI, some council(s) will respond quickly and provide comprehensive data in good formats, while another may refuse at the first instance.

- A quid pro quo for the growth of data enabled policy, especially relating to AI, is likely to be greater levels of scrutiny, more risk reporting and so on. Any fresh regulations arising as a result must strike a balance between being safe and smart, otherwise there’s a risk they crowd private sector investment out rather than in.

Q14. Where you identified barriers in response to Question 7 which relate to planning, infrastructure, and transport, what UK government policy solutions could best address these in addition to existing reforms? How can this best support regional growth?

Policy solutions that could help remove barriers to planning, infrastructure and transport include:

- Developing a fundable long-term project pipeline backed up by government support in the form of guarantees and risk sharing approaches.

- Providing certainty over deliverability, skills capacity and capability.

- Ensuring that the forthcoming 10-year infrastructure strategy, due to be published with the 2025 spending review, includes a credible project pipeline, free from regulatory intervention and changes to the scope of projects, which damage investor confidence.

- Ensuring that the new infrastructure pipeline gives the private sector the certainty it needs to make decisions and begin to scale up supply chains in advance of demand.

- Establishing innovative funding models - such as the regulated asset base model applied to the Thames Tideway Tunnel and the Contracts for Difference for offshore wind - and providing clarity to the private sector on what these models will look like.

- Concluding the major projects review and the infrastructure strategy to unlock wider investment plans currently in a holding pattern.

- Reducing business rates would make infrastructure a more attractive asset class to invest in.

Q15. How can investment into infrastructure support the Industrial Strategy? What can the UK government do to better support this and facilitate co-investment? How does this differ across infrastructure classes?

The steps that the government can take to support and facilitate co-investment include:

- Continuing to build investor confidence through certainty of the project pipeline, and by capacity-building for project delivery.

- Ensuring sufficiently available projects to invest in at a sufficient level of maturity and scale.

- Boosting understanding of the different kinds of capital looking for a home, for example in relation to pensions, the different nature of annuities (long-term) vs balance sheet (short term) and aligning these with different types and stages of investment projects.

- Encouraging the development of city prospectuses, which clearly spell out the investment opportunities in a given geography and are supported by knowledge of the origins of private capital, drawing on the experiences of London & Partners and Opportunity London in marketing the capital.

- Prioritising the establishment of funding models for new privately provided infrastructure, building on the success of the model employed by Thames Tideway Tunnel and the Contracts for Difference for offshore wind.

- Devolving powers to London Government and other City Regions to enable the delivery of new infrastructure to boost growth and unlock development, such as the power to use Tax Increment Financing for new transport projects which will also have a benefit in terms of crowding in development around new connectivity.

Q16. What are the barriers to competitive industrial activity and increased electrification, beyond those set out in response to the UK government's recent Call for Evidence on industrial electrification?

Additional barriers to competitive industrial activity and increased electrification that the government could help to tackle include:

- Boosting grid capacity and infrastructure: the current grid capacity is limited and the relevant infrastructure can be considered outdated which constrains large-scale electrification, especially for industrial processes which may be more resource heavy. Connection delays (as outlined in the UK government's recent Call for Evidence on industrial electrification*)* is a common barrier that adds time and costs to already expensive and difficult to deliver projects.

- Removing regulatory uncertainty: as with all decarbonisation efforts, the lack of consistency and certainty in decarbonisation policies and regulatory frameworks discourage large scale investment from the private sector, which would otherwise help accelerate delivery and drive growth.

- Addressing skills shortages: the lack of skilled workforce to implement and maintain electrification of localised or central energy systems.

- Providing further incentives to address high upfront costs: initial capital investment is required to transition from existing fossil fuel methods to electrified technologies, such as large-scale heat pumps. The costs are prohibitive and, coupled with the regulatory uncertainty mentioned above, or the lack of green financial incentives such decisions are very hard to make.

- Tackling supply Chain gaps: the lack of necessary equipment, which would render the electrification of a system more efficient (i.e. batteries etc.) can lead to delays, increased costs and dependency on imports from external markets.

Q19. How can regulatory and competition institutions best drive market dynamism to boost economic activity and growth?

- Since its creation, the UK's system of economic regulation has brought significant benefits to the economy and broader society. It has driven greater efficiency in utilities, improved service to customers and attracted significant volumes of new private investment.

- The regulatory approach should incentivise network companies to maximise the utilisation of their networks today and to prioritise network investment where it is needed most. This will support a robust and resilient utility network which is fit to the challenge of meeting London's growth for the benefit of the whole UK, as well as keeping costs as low as possible to the consumer.

- It is also important that the framework is incentive-based, particularly in encouraging the proliferation of low-carbon technologies; that appropriate planning for net zero is done at both local authority level and UK-wide, that the two are coordinated, and that regulatory frameworks are adaptive to enable additional investment to be unlocked if required within a regulatory period – which is often the case for the water and energy sectors.

- In the digital sector, the market should be characterised by sustainable competition rather than fragmented sub-scale operators. The UK needs national-scale wholesale competition to secure future progress and generate the right conditions to accelerate innovation and development in full fibre, which continues to lag where we need to be in London and across the UK.