



## Select Committee on Economic Affairs

### Corrected oral evidence: Employment and Covid-19

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3 pm

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Members present: Lord Forsyth of Drumlean (The Chair); Baroness Bowles of Berkhamsted; Lord Burns; Viscount Chandos; Lord Fox; Baroness Kingsmill; Lord Livingston of Parkhead; Lord Monks; Lord Skidelsky; Lord Stern of Brentford; Lord Tugendhat.

Evidence Session No. 12

Virtual Proceeding

Questions 97 - 104

### Witnesses

I: Professor Paul Nightingale, Director of Special Projects, UK Research and Innovation; James Heywood, Head of Welfare and Opportunity, Centre for Policy Studies; Professor Richard Jones, Chair in Materials Physics and Innovation Policy, University of Manchester.

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## Examination of witnesses

Professor Paul Nightingale, James Heywood and Professor Richard Jones.

Q97 **The Chair:** Professor Nightingale, James Heywood and Professor Jones, welcome to the Economic Affairs Committee for this first session. May I begin by asking you to introduce yourselves?

**Professor Paul Nightingale:** I am director of special projects at the ESRC, which is part of UKRI. UKRI is a non-departmental public body investing in innovation and research. Today, I will be speaking on behalf of UKRI and not as an independent expert. UKRI is currently undergoing the spending review, and some of the things I will talk about will be subject to that final settlement, so there will be a degree of uncertainty in my answers.

**James Heywood:** I am head of welfare and opportunity at the Centre for Policy Studies, a think tank here in Westminster.

**Professor Richard Jones:** I am a professor of materials physics and innovation policy at the University of Manchester.

Q98 **The Chair:** Perhaps I could direct the first question to James Heywood. The Chancellor has indicated that he will “always balance the books”. First, is he right to do so? Secondly, what would be an appropriate timeframe in which to do so?

**James Heywood:** It would be concerning if a Chancellor of the Exchequer was not making that statement. The question is how realistic it will be in the immediate future. Of course, the emergency measures that have had to be put in place and the drastic reduction in tax revenue will mean that, this year, borrowing will possibly be as much as £350 billion. We assume that much of that borrowing will fall away after the immediate crisis is over and the economy recovers. There has been some complacency from some about the extent to which that will happen. Some people think the economy will simply bounce back. If it does, of course, the public finances will be fine.

There is a question about how much lasting economic damage there will be. Some fiscal implications will be permanent, because although the measures that have been announced were emergency measures, a lot of them will politically be difficult to get rid of. There will probably be permanent significantly higher spending on health and social care. It will be very difficult for the Government to reverse in full a lot of the welfare measures that have been introduced. Those are permanent fiscal commitments which the Government will be looking at having to meet. There will be a lot of work to be done. Equally, if the Government start pulling the rug from under the economy before we are back on our feet, it could end up having a detrimental effect on the recovery.

In our paper with Sajid Javid, we said that, as a rough rule of thumb, once the economy and real GDP had recovered to their pre-crisis level, balancing the current budget—excluding investment spending—after

three years would be reasonable. I suspect that would mean not having a balanced current budget by the end of this Parliament.

**Professor Richard Jones:** Over the past decade, predictions about how quickly the deficit would close have consistently failed to be met, as a result of the long-running failure of productivity growth to resume since the global financial crisis. It is important to recognise that the problems with productivity that have been present for the past decade have not gone away due to this immediate crisis. After we recover from this crisis, there is still an issue about how to restore productivity growth, to create the GDP growth that would allow the deficit to be closed by increasing the productive capacity of the economy.

Q99 **Baroness Bowles of Berkhamsted:** How significant would increased R&D spending be in supporting the economic recovery and increasing resilience in the UK economy?

**Professor Richard Jones:** Spending on R&D will have a direct effect as a stimulus. It constitutes wages and purchases of goods and services that will have the same short-term stimulating effect as any other kind of public spending. The more interesting question is the extent to which those investments can support productivity growth. Again, that is a longer-term issue about what the economy will look like after the immediate crisis has been overcome.

The relationship between R&D and productivity is complicated. We have some estimates from econometrics, from the work of Haskel and others, suggesting rates of return of about 20% on public investment in R&D, but it will depend on what kind of R&D and where it is spent. Where are you on the continuum from basic research to translation? Are you spending money in places that are already prosperous and with high productivity? Currently, R&D spending is strongly concentrated in London and the south-east.

R&D spending has a significant role, but one needs to correct various imbalances that have arisen in the system. It is particularly interesting to look at where the private sector invests in R&D. At the moment, public sector R&D should very much have the aim of trying to crowd in more private sector investment. Looking at the balance between public sector R&D and private sector R&D across the country, and where there are regional imbalances, is quite a good way to proceed.

**Professor Paul Nightingale:** I agree with what Richard said. There is an additional bit where investing in R&D has allowed the UK to have a much more science-intensive response to the pandemic. The academic community in the UK responded very quickly when the emergency started. It engaged very closely with government. UKRI was able to step forward to support that activity through a rapid response urgency call, which has funded a significant amount of research across the sciences to support government. That has fed through into policy support, better data and medical interventions, such as helping to find therapeutics, and investment in vaccines, which will be very important for addressing it.

I agree with Richard's point. The evidence is that, in the longer term, investment in R&D leads to increased economic growth. Alongside the evidence he suggested, BEIS presented evidence from some consultants about the impact of increasing investment in R&D in the R&D road map. That suggested that, consistent with the research that Richard cited, you would get about a two-times return. If we increase R&D in line with government spend, the research suggests that GDP will grow by between 1.2% and 1.4% over 15 years. In concrete terms, that means that, if we add an additional £15 billion to R&D, we would expect an additional £30 billion of GDP growth and 80,000 additional jobs.

Richard is absolutely right that we should not think that you just turn a lever and growth happens naturally. Our ability to turn public investment into productivity growth depends significantly on downstream investment by firms that is expensive and persistent. Alongside that investment in increasing the amount of research, subject of course to a spending review, the ESRC is investing significantly in a productivity programme of research to increase our ability to understand and direct research so that it generates the best outcomes for the UK.

**Baroness Bowles of Berkhamsted:** Is that where the industrial strategy comes in?

**Professor Paul Nightingale:** It will be feeding into and supporting the industrial strategy.

**Baroness Bowles of Berkhamsted:** It feeds into and supports the industrial strategy. It is not a question of making the industrial strategy help out where the R&D investment goes in. Is it not a bit chicken and egg?

**Professor Paul Nightingale:** I am sorry, I do not follow the question.

**Baroness Bowles of Berkhamsted:** If you are trying to make your spending in R&D give you maximum productivity, I agree that it has to fit within an industrial strategy, but the two do not necessarily automatically mesh, do they, unless you make them?

**Professor Paul Nightingale:** There is a need to make sure that the investments that you make in public sector research match the needs of UK industry and the UK Government. That is a very important part of it.

**Baroness Bowles of Berkhamsted:** Do we need any changes to the industrial strategy that you can think of, or that the other witnesses can think of?

**Professor Paul Nightingale:** UKRI is effective in making sure that the R&D we support is aligned with the needs of industry.

**Professor Richard Jones:** It is a very important point. As soon as one accepts that the state will take a part in supporting downstream research—research in collaboration with industry—it has to be informed by a strategy. That strategy needs to be clearly articulated and it will

inform the kinds of investments you make. There is a lot of good to be said about the 2017 industrial strategy, but it is always worth looking at these things again.

The industrial strategy has to consider the long-term goals of the British state; the aims that, not just this Government, but following Governments will not be able to achieve unless they have the research and innovation to support them. I would put into that category the net zero target. It is a very demanding target and it will take substantial innovation to realise at a reasonable cost. That is a very obvious area. Perhaps more work could be done on the industrial strategy and then the appropriate investments could be made to follow it up.

There is also a spatial aspect to industrial strategy. Economically, the UK is a very divided country. Large parts of it are not fulfilling their potential. If we look at fiscal balances across the UK, only London, the South-East and East Anglia have a positive fiscal balance. Many parts of the country ought to have more productive economies. Thinking about how one can support increased productivity in those lagging regions is, again, a vital part of industrial strategy. In that case, it will come about both from mapping what the existing industry clusters are in those areas and asking how they can be strengthened, and from seeing where there is a realistic prospect of developing new industry clusters that reflect the existing endowments of those parts of the country.

Looking again at the industrial strategy is a good thing, and I know the Government are planning to do it. They should look at goals, sectors and spatial aspects, and that should be connected with any increase that arrives in the R&D budget.

**The Chair:** This has stimulated a number of people.

**Lord Skidelsky:** This is a public finance follow-up question from both the Chair's question and the question you have just answered. It is addressed to James Heywood primarily, although anyone else is very welcome to answer. When you talk about balancing the books, do you distinguish capital spending and current spending? Which particular book is to be balanced? You suggested that it should be over three years. Does that include both? That is the first question.

The second question is: how do you judge the necessary scale of the stimulus that is required to get the economy back to full production?

**James Heywood:** On the first part of your question, I specified that, when I was talking about balancing the books, I was talking about the current budget. It is reasonable for the Government to borrow modest sums for productive capital investment. The fiscal plans the Government had in place before the crisis were gradually to reduce the debt to GDP ratio while running a small current budget surplus, or at least a balanced current budget, and borrowing for the Government's infrastructure plans. If within five or six years the Government are able to get back to that position, and we have the same fiscal position that we were in before but

with a higher debt, we assume that we will be able to manage the higher debt because at the moment the markets are being very kind and interest rates are good, but we should not be unaware of the fact that there is increased risk to the public finances from that increased debt.

On the stimulus question, it is not just about the amount of money; it is about how it is being spent. That speaks to the other question that we were talking about. It is as much about where the money is being directed, and about systems and incentives, as it is about the scale of the amounts of money that are being pumped in. The Bank of England will have a huge role to play if there continue to be liquidity problems in the economy, but as far as the long-term productive capacity of the economy is concerned, ultimately, if the Government were simply to say, "We will create X million jobs overnight", that is not an economic plan for 20 or 30 years' time. It might help with the immediate employment crisis, but it is not a sustainable approach to economic management.

**Lord Fox:** Professor Nightingale and Professor Jones both referred to the strategy of investing in the golden triangle of Oxford, Cambridge and London. As regards bangs for buck, how much economic activity, how much productivity, does a pound spent within that golden triangle generate versus outside the golden triangle? While I can support the aims, I wonder whether the forces of economics are still putting the money into that golden triangle.

**Professor Paul Nightingale:** We do not have an exact answer to that, but there is research we can draw on to inform our strategy about where we invest. Traditionally, the UKRI has had an excellence-based focus to our investment, where we try to be agnostic about place. There are some investments where we take place into consideration. Some UKRI activity is funded through Innovate UK, which has a significant place focus. We have research funded through the Arts and Humanities Research Council, which attempts to support clusters.

The issue in locating research is the extent to which the spillovers—the economic benefits of that research—are localised. There, the research is quite complicated and it is very difficult for economists to unpick. It suggests that a lot of those benefits are localised, but the extent of the localisation differs in different areas. Some of the localised benefits are very localised, within five kilometres. Others extend to 85 kilometres, and others extend to local areas in the United States that are larger than the UK. We need to be nuanced in our understanding of what local is.

The other issue is that firms that invest in R&D are often highly capable and will reach out around the world for the best research there is. If they need a piece of research, their local university may not necessarily be the university that provides it. Our view is that we should support excellence in research but take into account the regional inequalities and the broader inputs to productivity growth and economic development, particularly in left-behind areas that may not necessarily be R&D based. The economy around Cambridge is very R&D intensive and, typically, will draw directly on the research that goes on there, but there may be other

parts of the UK that have economies that are behind the technological frontier, and, there, the key issue may be the diffusion of existing technology, or topics we will come on to later, such as skills, where we need to support research.

**Professor Richard Jones:** Cambridge is a fantastic economy, but there is an issue about capacity constraints in existing places. If you put too much more R&D money into Cambridge, nobody would be able to get around the city or afford to live there. There is also evidence that there are potential spillovers that are currently not being realised. I accept completely the argument about agglomeration; it would be wrong to disperse R&D spending over the entire country. But there is evidence that there are places that have quite strong private sector R&D economies where the Government are not co-investing. A key example is Cheshire, which has remarkably high R&D intensity from the private sector and very little from the public sector. Parts of the east Midlands are in the same category. I would agree on the importance of agglomeration benefits, but say that we could have more agglomerations than we have currently.

**Lord Stern of Brentford:** I declare that I am a member of the Prime Minister's Council for Science and Technology and I led the report to the Prime Minister on net zero by 2050, which we discussed earlier this year.

I am worried that there is a rather strong narrowness in your answers, and I want you to comment on that. There is narrowness as regards the outcomes on GDP and productivity measured by GDP when we know that well-being matters enormously in relation to R&D—mental health being one clear example, and there are many more. There is narrowness in relation to the role of the service sector. We are an 80% service economy, and, even if you look narrowly at exports, it is still pretty largely services, or perhaps ballpark close to 50:50.

You seem to be talking about R&D in a very technical, narrow manufacturing-oriented way when that is only a very small part of the economy, and therefore a small part of productivity. You broadened it to levelling up, infrastructure and net zero, and those are, of course, important, but the other aspects of narrowness as regards well-being and the service sector are also very important. Would you like to comment on that?

**Professor Richard Jones:** Those are very valid points, and having a good sense of the structure of the economy is quite important.

**Lord Stern of Brentford:** May I say that those are not footnotes but major stories?

**Professor Richard Jones:** It is important to recognise that the service sector contains many different things, and I am not totally sure it is helpful to think about it as a single thing. It has some of the highest productivity parts of the economy, in knowledge-intensive business

services, and some much lower sectors in hospitality, and I am not totally sure that it is helpful to consider those things together.

There is a very interesting question about how much knowledge-intensive business services themselves depend on sectors such as ICT and manufacturing, which we would think of as conventionally high technology. The importance of manufacturing could be bigger than its share of GVA would indicate, because it supports a range of high-productivity, knowledge-intensive business services, that count in the service sector. The kinds of trends that we have seen in business where some functions of manufacturing businesses are unbundled to become free-standing parts of the service sector are important, too.

One also has to look at where productivity growth comes from. Technological progress is very uneven; some sectors have very fast productivity growth and others have much less productivity growth. There is a very interesting question about how much you focus on sectors that are relatively small but can deliver fast productivity growth, as against smaller gains in much bigger sectors.

But I take your point. For example, health and social care is a massively important and very big part of the economy. Relatively small improvements in productivity there would be good for the economy, and for some of the wider things you are talking about.

**Lord Monks:** This is a question about how well the country's economic models are geared to supporting innovation and R&D. Corporate debt levels are high, while investment in R&D and skills is comparatively low. That has disappointing consequences for productivity in general. Fortunately, there are exceptions. Mr Heywood, do you have any observation that you would like to make on that point?

**James Heywood:** It is true that the UK, while strong in many ways in the science and innovation field, is very focused on its universities. Some other countries are a lot better at joining up the academic side of research and development and industry. It is worth noting that, while our overall R&D spend as a percentage of GDP is lower than the OECD average, the ratio of public to private investment is roughly the same as the OECD average. That suggests that in what Richard was talking about—leveraging in investment from the private sector as we look to increase the public sector spend on research and development—we need to ensure that we take the private sector along with us. As Paul said, it is not just a case of turning a tap on and suddenly we will get the benefits.

There is a perfectly good economic case for the Government to have a role in those things, because ultimately there are huge spillover effects from research and development spending, but the people doing it are not necessarily capturing the gains. There is a need to create an ecosystem between the public sector and the private sector in research and development.

**Baroness Kingsmill:** Mine is a slightly challenging question and it relies



a lot on what Lord Stern was asking. I have a sense of *déjà vu*. We have been talking about low productivity in the UK for years and years, and we have also been talking about R&D being the answer to that. I am beginning to wonder whether R&D is an industry in itself and that the productivity that arises from it is among the academics. I would like you to give me a little more clarity as to how R&D improves productivity in the real economy.

**Professor Richard Jones:** This comes back to the point that R&D is not a single thing. You may well think that giving more money to professors in Manchester University just supports professors in Manchester University. That is why I focused on translational R&D and on making sure that the R&D supported by the Government crowds in private sector R&D and leads to new goods and services that create value and deliver other benefits, and that it provides the new technologies that allow us to decarbonise the economy without a big impact on our living standards, and delivers sustainable and humane health and social care.

On the point about the relationship between R&D and productivity, the UK was a very R&D-intensive economy in 1980. The R&D intensity of the economy fell substantially through the 1980s and 1990s to its current value. It has been bouncing along at about 1.7% of GDP since the 2000s. Productivity growth was quite high until the global financial crisis, and then it stopped. It is not the case that we have been increasing the R&D intensity of the economy, and productivity has not been responding. In fact, you could make the opposite argument. The economy has become a lot less R&D intensive, and it has also become an economy with much lower productivity growth.

**The Chair:** I am sorry to cut you off, but we have an hour, with seven questions and quite a lot of ground to cover. I think the point has been made. Do you want to add anything, Professor Nightingale?

**Professor Paul Nightingale:** No, we can move on.

Q100 **Lord Burns:** In the general climate of low interest rates, there is a lot of support for more infrastructure spending, and I do not want to question that at this point. Given the long lags involved in most infrastructure investment, is it realistic that it can make much of an impact in the short term to aid recovery? Which investment programmes do you feel should be brought forward and which would have the biggest short-term effect?

**James Heywood:** You are absolutely right that, much as it is very easy for politicians to talk about shovel-ready projects, people in the Treasury will tell you that they are few and far between, We can think in particular about how long some of our rail investment projects have been going on. It is difficult to get those things off the ground quickly enough for them to have the sort of short-term impact on the economy that we would be looking for.

There are a few things that can be done. We can look, for example, at roads—new roads, no; but resurfacing roads, very much so. That is the

sort of thing you can do relatively quickly. Similarly, there has been talk about retrofitting homes, which would also advance the Government's green agenda, and could create quite a lot of jobs.

**Professor Richard Jones:** The challenge of getting to net zero is massive. There are many investments that need to be made. Some of the immediate employment benefits of those are probably overstated, but they ought to be done.

**The Chair:** Professor Nightingale, can you answer Lord Burns's question?

**Professor Paul Nightingale:** I have nothing to add.

**Lord Stern of Brentford:** Again, there is a question of narrowness in the understanding of the meaning of infrastructure. Essentially, infrastructure enables other activities to take place. From that point of view, there are quite a lot of things that could be done very quickly, and I would like you to comment on those—for example, making cities much more friendly to cyclists and pedestrians, which is crucial for health and for the drive to net zero. Some of that is labour intensive and some of it can be done quickly. Restoring degraded land can be done quickly; indeed, the climate change committee has made some interesting recommendations on that.

It would be very good if you could comment on the kinds of infrastructure activities that are much more labour intensive and can be done quickly alongside those others, which are also very important but are much bigger and more capital intensive.

**The Chair:** I see two of the witnesses nodding in agreement, so presumably we can deal with this point quite quickly.

**Professor Paul Nightingale:** UKRI does not have a position on infrastructure policy, but we fund a number of academic teams that work on infrastructure policy, and, having spoken to them, they would agree with Lord Stern's opinions.

**Professor Richard Jones:** I think the examples that Lord Stern mentioned are good ones. You could add fast broadband more widely, charging infrastructure for cars and the retrofitting of houses. There are a number of examples.

**James Heywood:** The only thing I would add is the caveat that we need to be particularly careful about transport infrastructure. It looks as though Covid will have a long-term impact on the structure of our economy, particularly on the way urban areas and commuting work. We need to ensure that we make investments that are good for productivity long term and are value for money for the taxpayer.

**The Chair:** Having been stuck for 20 minutes in Park Lane because of the extension of the cycle lanes, I am not absolutely persuaded that productivity always follows from these things.

**Lord Stern of Brentford:** May I come back, Mr Heywood—

**The Chair:** Lord Stern, I want to move on because we do not have much time.

**Lord Stern of Brentford:** I do not agree anyway.

Q101 **Viscount Chandos:** How can the Government's training and skills vision, for instance their ambitions for more institutes of technology and lifelong learning, be aligned with the UK's research and innovation framework? To what extent are those ambitions threatened by financial challenges to the universities relating to Covid-19? Professor Nightingale, is that one for you to kick off with?

**Professor Paul Nightingale:** I think it is. UKRI welcomes the new focus on training and skills. As we mentioned earlier, the ability of the UK economy to generate value from its R&D system depends on a whole series of other things. There are significant problems in many areas of skill development in the UK that we need to address. If we develop a new technology in an R&D lab, it will depend on users being able to use it and on their skills. We are concerned that, if those skills are not in place in the rest of the economy, we will not get the full benefits of any investment in R&D. It is part of the overall ecosystem.

An example would be some recent work that was done by the Royal Society looking at the acceptability of Covid vaccines. It found that the main determinant of whether people in the UK would accept a vaccine was their level of numeracy. We know that, even on basic skills, something like half the population of the UK, according to government surveys, have numeracy levels equivalent to primary school level. There is a significant need to upgrade skills throughout the economy.

In our work, we think of it as a ladder of capability development that goes from very basic skills that are accumulated in formal educational settings and in informal settings, particularly work. They accumulate through basic numeracy skills, basic skills, skills in the workplace, management practices, the ability to diffuse and adopt technology and the ability to innovate. Only at the very top are the R&D-intensive innovation parts of that capability ladder that we are particularly interested in supporting.

We are very supportive of that work. It comes across most clearly in the work that UKRI is doing on the place agenda and trying to make sure that we support all the regions of the UK. Many of the most left-behind regions are not R&D intensive but could still benefit from the sort of research that we fund. It has been pushed down through the UKRI board that we need to take strong consideration of that in our strategy, and we will be seeking to align it with the government strategy on skills.

**Professor Richard Jones:** The premise of the question is absolutely correct. We have tended to think of skills as a supply problem, but we need to address the demand side. It is characteristic of places that are left behind that their economies are often stuck in a bad equilibrium,

where there is no demand for skills, there is no innovation, and there are low-productivity businesses.

We need to think about innovation and skills together. Innovation provides the demand side of the skills equation. Creating a more innovative economy will create demand for those skills. We then need to be in a place to satisfy that demand. That needs more collaboration than we have seen before between the university sector, the FE sector and agencies that promote innovation.

To be blunt, it is not made easy. The relationship between the Department for Education and the Department for Business, Energy and Industrial Strategy could be better on that. It may be easier to drive at the level of city regions, or possibly devolved nations, where a more holistic view could be taken. Innovation and skills need to be coupled much more closely than they have been in the past.

**Q102 Lord Fox:** We have talked about infrastructure and training. The Resolution Foundation recommended investing in retrofitting and social care to create new jobs quickly. I am not necessarily asking you to comment on that, but what other government direct investment could rapidly create jobs as a policy for the now? A lot of what we have talked about seems to be very long term. How do we do stuff now?

**James Heywood:** We have already covered the immediate question of which bits of government investment spending can create jobs quickly. As for policies that the Government need to be looking at, so far, a lot of the emphasis has been on protecting people's jobs. I hope that at some point the Chancellor will look, for example, at the employer's national insurance system and make some temporary changes there to incentivise hiring.

As far as possible, we need to make sure that we leave the market to do what it does best, and not to see it purely as the Government spending money and creating jobs. The Government should do that if there are things the Government need to do. If the Government decide there is a need for more people in the social care sector because there is a capacity issue, they should do that, but they should not do it just for the sake of creating jobs.

**Lord Fox:** The only lever you suggested the Government can use to get the private sector into this is national insurance. What else should the Government be doing to lubricate the process?

**James Heywood:** There are plenty of other things the Government could look at. For example, they need to look at the way that capital investment is treated for companies via the corporation tax system. We should also be addressing the fact that the business rate system means that companies are penalised if they invest in their properties. If companies are looking at changing their business model as a result of changes in the economy, it would be nice if they were not penalised by the tax system for doing that.

**Professor Paul Nightingale:** UKRI as a research funder does not have a position on that question, but we fund a lot of researchers who have been looking at it and drawing international evidence together. A number of studies have been summarised on a website that the ESRC and UKRI have funded on Covid and the economy, and I direct you to their responses there.

**The Chair:** Lord Fox is looking for more immediate things that could be done to deal with the large numbers of people who will be looking for jobs in the next few months.

**Professor Richard Jones:** There is an issue about the short-term damage which the current crisis will cause to innovation systems. I am thinking particularly of aerospace. Aerospace is a very important sector for many local economies and has been badly hit. It supports a lot of very high-productivity jobs. It is worth the Government thinking about how some of those specific sectors can be supported, be it the aerospace or automotive sectors.

One also has to consider that, if there is a disorderly Brexit, it will have a significant impact on sectors such as chemicals, which are a very innovative part of the economy in otherwise left-behind parts of the country. Thinking about short-term support for those sectors is another important aspect.

**Lord Livingston of Parkhead:** I want to pick up on something that James Heywood said in response to Lord Fox's question. Is not one of the challenges that there are sectors—social care was mentioned—where the issue is not creating more jobs but rather, in social care, the fact that there are probably between 100,000 and 200,000 jobs that people wish to have filled but cannot find candidates for? That may be true in a number of sectors. I am interested in the mismatch. Creating jobs for a sector if there are no applicants does not do a lot. Do you have any thoughts on that?

**James Heywood:** Absolutely. The point I am making is that social care policy, of which the management of the social care workforce is an element, should not be seen as part of employment policy and wider economic policy, because, ultimately, if you are using it simply as a job creation mechanism, it is not sustainable. If they are not jobs which the Government think they need, if those are not people the Government think they need to be employing in the long term, that is not an appropriate way for the Government to use their money. That is all I am saying. If the Government look at it and say, "We need a lot more people in the social care sector and we have not been putting the money in", and that kills two birds with one stone, as it were, it is perfect.

**Lord Stern of Brentford:** To pick up on what James Heywood was saying, most people would agree there must be a better reason than merely creating jobs. It is a question about timing and unemployment. If there are a lot of things that we know we have to do, does it not make sense to bring them forward to a period of unemployment? We probably

have to expand our care sector, given the ageing of the population. There is a lot of strain on it now, so bringing that forward makes sense. In addition to what you were talking about, there is a timing question that I think is important. It applies also to some of the net zero stories.

The second thing is to avoid the destruction of skills. We saw the destruction of skills on a grand scale in the 1980s and we are seeing some of that now. Surely avoiding that destruction should come into what you do immediately about jobs.

**James Heywood:** When we talk about the scarring effects of unemployment, we usually distinguish between two separate issues. The first is the job match loss; there is a benefit from people having an existing relationship with an employer. The Coronavirus Job Retention Scheme was all about preventing that loss. Secondly, there is the impact of people losing contact with the labour market and losing the skills involved with doing their job day to day, and so on.

It is absolutely right, and I do not disagree in any way, that even a short period of extremely high unemployment will have a catastrophic impact on the lives of large numbers of people and on the economy as a whole. The major question for the Chancellor is what he will do about that. Ultimately, it will not be as simple as saying, "Let's give everybody a job". These are very complicated questions, which, unfortunately, the Chancellor will have to wrestle with over the next year or two and beyond.

I do not have any simple answers, but it is at least worth pointing out that some of the work the Government have been doing on increasing DWP capacity, to make sure that people coming out of jobs get back into them as quickly as possible, for those there are jobs for, is a very good thing.

Q103 **Baroness Kingsmill:** We have talked about the left-behind areas quite a lot. Are there any emergency measures you can think of that are not necessarily related to Covid-19? Covid-19 is not the only cause. Those areas have been left behind for some years and it is nothing to do with Covid in some senses. How does the levelling-up agenda tie in with all the emergency measures that may be necessary for reigniting the high street or city centres?

**Professor Richard Jones:** A key feature of the left-behind regions is that they are not very resilient. Even if the damage of Covid is not particularly focused on left-behind regions, their lack of resilience and the lack of people's financial resources make it likely that, whatever damage Covid does, it will be exacerbated in those regions.

**Baroness Kingsmill:** What I was trying to say is that the two are not always connected and that the measures we need to introduce for left-behind areas are not necessarily the emergency measures stimulated by Covid, but more systemic ones.

**Professor Richard Jones:** Left-behind regions have a foundational economy. Health and social care is obviously a very important part of those economies. Focusing measures on those things is important.

Another way forward, perhaps picking up from a previous question, is where one can combine employment schemes with built-in training. The attractiveness of both retrofitting houses and social care is just that: you could think of those as areas where people could be trained to move into a different sector at the same time as the opportunities arose. Beyond that, there is a lot of work to be done in building up the productive economies of left-behind regions, but that is a long-term problem rather than a response to the crisis.

**Professor Paul Nightingale:** You are absolutely right to highlight that it is a complicated relationship. Research that we have funded has looked at where the impact of Covid is, and it is not necessarily in left-behind or rich areas. Places such as Crawley have suffered because of the decline in air traffic; Gatwick has been particularly hit. Younger people and people who do not have secure work, and people in particular sectors such as hospitality, are being hit the most, and they are found across the country. The two things, as you say, need to be understood in a nuanced way.

In the left-behind areas, we are looking in our spending review to do a range of activities that will try to tie together at local level things that have previously been kept apart. The problems of left-behind places are different for different left-behind places. They depend on skill levels, demographics and geography. In our spending review we will be looking to set up a series of innovation centres to support local economies. That will include, in some places, very basic skills. It will include support for local government to link national and local data to inform policy and make it better fit the local needs of areas. It will be the diffusion of pre-existing technology and support for improving management practices to boost local firms in those areas. Only for a small number of those areas will it link into the broader R&D-intensive work that we support.

Q104 **Lord Livingston of Parkhead:** We have talked quite a bit about which sectors and where geographically the Government should promote. I would be interested to hear from the witnesses about how. How can the Government promote private sector expenditure, particularly at a time when the private sector can see lots of risk but perhaps little return? What methodologies would you recommend that the Government should look at to promote the private sector, whether it be corporates, private equity, venture capital or the like?

**Professor Richard Jones:** One of the most important ways the Government can support the private sector is by buying stuff from it. There is a very long-running argument about the need to use public procurement more intelligently. That is still important.

**Lord Livingston of Parkhead:** Do you mean by focusing on the UK, or that the types of products they procure encourage further investment?

**Professor Richard Jones:** It is about a procurement policy more focused on supporting companies, particularly innovative companies, in developing new products. It is about making the health service a better customer, less focused on immediate cost savings and more focused on supporting companies as they develop new products. That is one way. There are other ways that involve supporting translational research, working in partnership with companies. The work of Innovate UK, on which Paul can comment more, and the Catapult Centres all have a role. Those are some of the ways.

I would not focus on venture capital. Venture capital is interesting and important, but it is relatively small as the economy goes, and it is very focused on London and the south-east. It is also already very well supported by the Government, to an extent that people perhaps do not realise; the amount of direct government funding going into venture capital is not an insignificant part of the whole. There should certainly be more venture capital outside London and the south-east, and it would be nice if it supported a wider range sectors. On the other hand, it is very hard to make money in that sector, and one would not want to overemphasise it.

**Professor Paul Nightingale:** May I provide an alternative view to Richard's on venture capital? In the United States, it is very clear that venture capital is extremely important in the development of technology. There is research that suggests that about a third of the market capitalisation of US stock markets is made up of firms that were backed previously by venture capital. It has a very significant effect there. Although it is a relatively small part of the portfolio of investment—Richard was right to call it a tiny part—its impact is disproportionate, and it is an area that we should be supporting. Richard is absolutely right; it is an area that we support in the UK.

**Lord Livingston of Parkhead:** James Heywood, do you have any suggestions on how government should encourage private sector investment?

**James Heywood:** I would raise two things. I mentioned one in passing, which is the way the tax system treats capital investment by private firms. We are one of the least competitive tax systems in the world when it comes to that. We currently have a temporarily high annual investment allowance of £1 million. That is due to fall back to £200,000 at the end of this year. If the Government do nothing to address that, it will become less advantageous for companies to make capital investments after December than it is at the moment, which seems bizarre to us, but it is true.

Secondly, at the moment the tax system incentivises debt-financed investment versus equity-financed investment, which has probably contributed to the fact that we have a particularly debt-laden corporate sector. I would look at addressing that as well.

**Lord Livingston of Parkhead:** We definitely raised the first issue with



the Chancellor—the capital allowance system—so thank you very much for that.

**The Chair:** James, when you said you would address the debt issue, does that mean that you would not make debt allowable against corporation tax?

**James Heywood:** I would look at reducing the amount of companies' debt costs that they can offset against their tax bills.

**The Chair:** Reducing it in what way?

**James Heywood:** By reducing the EBITDA, as it is called in the lingo. It is simply saying that, instead of 30%, you can offset 20%. It is quite easy to do if the Government want to do it.

**The Chair:** We have run out of time. I apologise for pushing the pace, but there was a lot of ground to cover. I am very grateful to you, Professor Jones, Professor Nightingale and James Heywood, for giving evidence. That concludes our first session.