

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

About The Centre for Inclusive Trade Policy

The Centre for Inclusive Trade Policy, a centre of excellence for innovative trade policy research, is the first Centre dedicated to trade policy to be funded by the Economic and Social Research Council. The Centre is built on the precept that trade policy should be inclusive in both policy formulation and outcome. Our aim is to build permanent capacity by developing a community of scholars and practitioners with the knowledge, skills and mutual understanding to develop robust trade policy in a changing world. Led by the University of Sussex, the Centre is comprised of universities from across the whole of the UK - including from the University of Nottingham, the University of Strathclyde, Queen's University Belfast, Cardiff University and the University of Cambridge - and beyond, along with non-academic partners working on trade.

<https://citp.ac.uk/>

UK Trade Policy Observatory

The UK Trade Policy Observatory (UKTPO) is an independent expert group that initiates, comments on and analyses trade policy proposals for the UK, and trains British policymakers, negotiators and other interested parties through tailored training packages. The University of Sussex has the largest collection of academic expertise on the world trading system in the UK, with specialists on trade policy, trade law and trade politics and European law and economy. The team includes experts in economics, international relations and law.

The need for an Industrial and Trade strategy.

1. The UK is an open economy with the value of exports and imports as a share of GDP around 60-65%. The success of UK businesses depends considerably on competitiveness in export markets which in turn depends on access to imported intermediate goods and services. Hence successful Industrial Policy (IP) requires also focussing on trade and trade policy.
2. Driven by serious concerns about growth, the green and digital transitions, and economic security, IP interventions by other countries have risen dramatically in recent years. 'Strategic competitiveness' is the most commonly cited objective, revealing that industrial policy is increasingly outwardly oriented. The policy environment is substantially different to even 3-5 years ago and the UK needs a long-run strategic response. The UK needs to decide on the extent of alignment (or not) to EU policy on open strategic autonomy, and to formulate strategies to strengthen its competitive position notably in digital and green global value chains.
3. The key **objectives** of IP include: growth; broader societal considerations (eg. environment), and economic security. Economic growth is typically central, and there may be trade-offs between this and the other objectives. The **rationale** for IP is that without intervention, businesses, due to some form of 'market failure', may not make socially optimal decisions with regard to the preceding objectives. A further argument sometimes made is the need to respond to those actions taken by others.
4. The UK does not currently have either an industrial strategy or a trade strategy. Instead, there are a series of documents on specific issues (advanced manufacturing, critical imports, batteries...). This lacks coherence.

Recommendation: Both an **industrial strategy**¹ and a **trade strategy** are needed in order to provide a consistent, evidence-based, framework for policy. The former would

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

focus on key long-run objectives for the shape of the UK economy and articulate the priorities with regard to growth, social considerations and economic security. It should explain why intervention is necessary and the forms of acceptable (and unacceptable) interventions. Elements of industrial policy (e.g. the Advanced Manufacturing Plan) are then the specific actions to support that strategy. Analogously a **trade strategy** provides a framework for how trade policy can support the domestic policy objectives, detail the key constraints and trade-offs, and outline and provide supporting evidence for the priorities therein.

5. Good policy – industrial and trade requires a solid evidence base, transparency, and the means for independent scrutiny and advice.

Recommendation: We recommend the establishment of an independent Board of Trade to provide independent analysis of UK trading performance, and trade policy and how the latter supports UK industrial policy.

6. The most efficient policies are those that directly address the issue (market failure). As there are many forms of market failure, and a range of non-economic objectives, which vary across firms, industries and time – it is hard to provide general policy recommendations. The answer to whether a policy is justified and what is the best policy is: ‘it depends’. While this might seem unhelpful, it is important. It reveals that (a) there is no blanket justification for IP intervention, (b) the form of intervention will be case specific; (c) with a wide range of interventions the need for policy coherence via an Industrial Strategy document is all the more important.

7. In November 2023, the Chancellor announced 5 priority sectors: *advanced manufacturing, green industries, life sciences, creative industries and digital technology*. While going beyond manufacturing is welcomed, there is little underpinning explanation for these choices, nor consideration of the importance of services for the UK economy. Shortly after, the Government published the Advanced Manufacturing plan (AMP) listing detailed interventions in key industries (automotive, aerospace, life sciences, green industries, chemicals, and semi-conductors). However, this is not a strategy document nor really a plan. There is little justification of *why* policy should be focused on these sectors, little discussion of *what* interventions are needed, nor of the *coherence* of any such policy measures. Greater transparency about the evidence base and thus the need for different forms of intervention is desirable.

Recommendation: A successful industrial policy (and AMP) needs to identify existing and potential areas of strength (ranging from advanced manufacturing to education, financial or businesses services) and explain the objectives, why intervention is needed, and justify the forms of intervention.

8. Modern IP is also defensive, such as the desire to reduce import dependency on China (which has gained prominence as direct supplier to the UK in products such as computers and communication equipment) but also more broadly in sectors yielding high rents or thought to be critical bottlenecks. Such interventions are driven by a mix of geo-political tensions, concerns about forced labour practices, and the perceived success of China in using state subsidies to boost exports. Others argue that global supply chains have in recent years operated with remarkable flexibility, and intervention is not needed.

¹ Industrial has connotations of manufacturing and goods, so a better term might be a ‘growth’ strategy.

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

9. Value chain trade consists of complex networks of intermediate input trade flows, exports/re-exports, and therefore rarely connect the UK directly with a particular producing country. Hence, a considerable fraction of UK imports from the EU are mined and refined (in the case of critical minerals) or assembled (advanced manufacturing) elsewhere, notably in China. Similarly, many UK exports are used as an intermediate input by firms abroad.
 - a. The AMP pays insufficient attention to the importance of international trade for advanced manufacturing in terms of both imports, exports and the complexity of modern supply chains using both goods and services.
 - b. Production systems are so interconnected that it may make little sense to promote sectors as a whole, given the diversity of sources of parts and components.
 - c. Relatedly, MNEs play a central role in trade networks and their ability to rapidly reallocate trade from across destinations should be considered.
 - d. Engaging with and incentivising the private sector seems paramount: from stimulating investment to securing access to key raw materials and components.
 - e. Reducing import dependency may have unwanted side effects, e.g: restrictions on imports of solar panels may induce more domestic production but will reduce take-up and thus impact on climate change objectives.
 - f. Massive subsidies (as with Inflation Reduction Act in the US) can have a major impact on investment levels and structures but cannot easily be copied.
 - g. The UK should strive to maintain close alignment with the EU, to facilitate trade and investment flows, especially in emerging areas such as green and digital GVCs.

9.1 Recommendation: The complex nature of interdependent value chains should be taken into account – both with regard to resilience/vulnerability and with regard to the impact of industrial and trade policy on UK firms.

10. A business environment conducive for a strong manufacturing sector needs an efficient supply of services. The government should identify those related services that are necessary to boost productivity along all areas of the value chain; and the eco-system of services needed for exporting. Broadly, these include distribution, logistics, marketing, sales, after-sale services, IT, back-office support, and management.²
11. Investment Zones attempt to promote industrial clusters where a university linked R&D base already exists. These policies have only sometimes succeeded. Initial conditions needed for success are complex, and risk displacing employment elsewhere. Freeports are a variant of Investment zones with the ability to defer payment of import duties until they are exported or sold on into the rest of the UK. There is very little to encourage industrial regeneration from this deferral of duty payment. The areas designated do include some interesting projects, notably in the area of wind turbines, green hydrogen and carbon capture and storage. However, the freeport policy, as such, did not create these activities and is unlikely to be the main element in promoting them.

² Trading Services for a Circular Economy, Ministry for Foreign Affairs of Finland and the International Institute for Sustainable Development, October 2020, <https://www.iisd.org/system/files/2020-10/trading-services-circular-economy.pdf>

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

Economic security:

12. Economic security potentially conflicts with the UK's trade policy objectives. Policy tools for economic security, such as export controls, investment screening, subsidies for reshoring and friend-shoring, tend to intensify government interventions and disrupt international trade and investment activities. In a world with rising industrial policy protection there is a risk that economic security is used too easily as a justification for intervention. . Geopolitical pressures are already impacting on [35% of UK importers and reshaping their supply chains](#). Economic security measures that interfere with UK companies' operations, need to be resisted and where introduced need careful justification.
 - 12.1 **Recommendation:** Commitment to an open and outward looking economy, the rules based world trading system, and providing policy certainty to business should be core principles.
 - 12.2 **Recommendation:** To retain balance between economic security and trade policy, the government should clarify the scope of intervention based on economic security and the areas of priority. Policy measures should be based on business needs, including those of SMEs, such as providing information and analysis relating to geopolitical risks and interventionist trade measures likely to affect global supply chains. The government should also provide information on UK's trade partners' economic security policy (e.g. China-related policy decisions) and existing bilateral and plurilateral arrangements relating to economic security. This could help UK companies avoid adverse effects and reshape their short-midterm trade and investment strategies.
13. Numerous countries have introduced 'economic security' policies, with varying approaches, scope, priorities and policy measures. Sharing information and improving transparency through bilateral and plurilateral collaboration is crucial to avoid unintended consequences to UK business. Also, collective international actions to economic threats, such as [G7 initiative to foster resilience to economic coercion](#), would be more effective than for the UK to act alone. Collective international actions should be well defined and be extended beyond G7.
 - 13.1 **Recommendation:** The UK Government should make clear that 'weaponisation' of global trade should be avoided as [fragmented world trade does not lead to economic prosperity](#). To that end, the UK government should analyse how the WTO could contribute to economic security governance and take a lead in promoting discussions at the WTO, and through bilateral and plurilateral cooperation.

Critical Raw Materials

14. The Critical Minerals Strategy of 2022, the Critical Minerals Refresh of 2023 and the Critical Imports and Supply Chains Strategy of 2024 clarify the UK Government's intention to utilise a host of policies to maintain its economic security and resilient CRM supply chains. However, the UK needs to identify where it wants to position itself in Critical Raw Materials (CRM) value chains and where there may be a need for intervention, and justify the forms of intervention.
15. CRM access should be consistent with domestic policy supporting the development of competitive downstream manufacturing industries. For example, if the UK wants to

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

make EVs for export markets such as the United States, it should understand the U.S. IRA implications of sourcing CRMs from countries that the United States does not have trade agreements with. While recognising the difficulties of so doing, the UK should negotiate with the United States to minimise impact on UK firms.

16. Most UK imports of critical materials from supplier countries appear to flow through the EU. Additional trade barriers with the EU bloc could have unintended consequences concerning the sourcing of the critical raw materials, even if the EU is not a major supplier.

16.1 **Recommendation:** Reducing trade barriers with the EU should be a priority

17. Existing agreements and MoUs with resource rich countries are limited without legally binding obligations. They may signal diplomatic understanding between two countries' but do not guarantee access.³ There are two options. First, create legally binding obligations on trade in CRMs, such as WTO+ prohibitions on export restrictions and taxes. However, these may breach multilateral trade rules on discrimination. Second, closer value-chain integration with supplier countries through longer term investments and knowledge transfer.

17.1 **Recommendation:** The UK should analyse the effectiveness of existing partnership agreements with resource-rich countries, and consider:

a. Collaboration: There is scope for UK support to investors to strike firm-level deals with mining and processing companies e.g. in African resource-rich economies, preferably those that are already vertically integrated. Entering into joint ventures with local companies have benefits of crossing unexpected or latent entry barriers and building long-term trust.

b. Technology and knowledge transfer to CRM abundant lower income countries through the supply of CRM-related professional services. From the perspective of industrial policy for inclusive trade, supporting the transfer CRM-related knowledge could enhance local capabilities.

17.2 **Recommendation:** Uphold the highest Environmental, Social and Governance (ESG) standards in CRM sourcing and assist resource-rich nations in meeting those standards, while minimising impacts on competitiveness. For example, the US offers performance-based grants to U.S. companies/mining entities sourcing critical minerals from Congo who support the integration of local companies and artisanal miners into the global supply chain.⁴ Another option is to create a fund to incentivise finance mining related investments in resource-rich countries, with financing conditional upon ESG compliance and environmental and social impact disclosures, and to provide technical assistance in exploration activities.

18. The UK should (continue to) participate in multilateral groupings to develop and harmonize ESG standards. It should consult with industry to understand the difficulties and where needed provide training on how to meet those standards. To avoid a zero-sum game, such policies need coordination with other countries, and the UK should

³ Task & Finish Group Report on Industry Resilience for Critical Minerals, 2023, https://assets.publishing.service.gov.uk/media/6585b37aed3c3400d3bfe0d/the-task-_finish-group-report-on-industry-resilience-for-critical-minerals.pdf.

⁴ Alexandra Wexler and Yusuf Khan, In Quest for Battery Metals, U.S. Takes On Cobalt's 'Inconvenient Truth', Wall Street Journal (August 24 2023), <https://www.wsj.com/business/in-quest-for-battery-metals-u-s-takes-on-cobalts-inconvenient-truth-80dd8cab>.

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

stress the importance of multilateral cooperation. UK investors will not be incentivised to meet ESG standards at higher costs if doing so puts them at a disadvantage to other investors not bound by similar standards. An important element of the multilateral cooperation is to promote the need for transparency regarding reporting of the industrial policies being pursued by other countries. The UK could also explore joint investment opportunities with allies where the buyer's market appears saturated.

19. The UK Government may need to support investment in R&D to explore manufacturing of higher value and technically complex tech products in which it could build its own competitive advantage.
 - 19.1 **Recommendation:** The government should leverage talent at its leading universities to study and develop new green technologies that would reduce reliance on CRMs.
20. Given the increasing regulatory and legal compliance issues confronting firms, the UK should leverage its existing position as an [arbitration-friendly jurisdiction](#) to establish itself as a hub of environmental law and regulatory practice.

Net Zero:

Total greenhouse gas emissions:

21. Net-zero targets and industrial policy both focus on production within the UK which is clearly significant. However, for climate change the issue is less what gases are emitted from within the UK but what is emitted arising from UK consumption. The climate consequences of emissions are the same regardless of where they are made. Although the UK has cut emissions strongly since 1990, increasing amounts of emissions have been expended on goods imported into the UK. DEFRA (2024) reports that in 2020, of the emissions embodied in UK consumption, very nearly 60% came from imported goods.⁵
22. The CBAM converts the ETS from a production to a consumption base but covers only a subset of the sectors covered by the latter.
 - 22.1 **Recommendation:** In future industrial policy, focusing only on UK production risks missing the point of climate policy completely. Any such policy must be accompanied by policies to manage imported emissions not only for the climate's sake but for the sake of ensuring that UK output, jobs, incomes etc. are not put at a disadvantage by more emissions-intensive imports.

Electric vehicles:

23. Competition from China in electric vehicles will be intense. Any policy designed to support UK production by attenuating such competition will raise the price of such vehicles and set decarbonisation back materially. Before embarking on such policies, the government needs to be clear (not merely to wish) that the supported industry will eventually become competitive, including having access to critical materials for constructing batteries and other components. Unless this is ensured, policy would be better to accept Chinese largesse in supplying important tools for achieving net-zero at lower cost than the UK could manage itself. Resources would be better employed focusing on sectors in which the UK has a more obvious comparative advantage.

⁵ Department for the Environment, Food and Rural Affairs (2024) *Carbon footprint for the UK and England to 2020*, <https://www.gov.uk/government/statistics/uks-carbon-footprint/carbon-footprint-for-the-uk-and-england-to-2019>

Written evidence submitted by the Centre for Inclusive Trade Policy and UK Trade Policy Observatory (IPO0067)

Environmental services:

24. Industrial policy is traditionally thought to pertain only to industry and the support of manufacturing jobs, but this is a mere historical accident. The UK is a professional services superstar.

24.1 **Recommendation:** Among the sectors that it might focus resources on is environmental services – research, development, design and management. To the extent that support to services would help to solve market failures in those sectors, it could equally apply to them.

25. Merely asserting the presence of market failures is not sufficient to justify intervention. The failures must be identified and understood, and policy designed to address them in an efficient manner. Intervention may not actually be necessary – the sector may be able to ‘look after itself’. But making room for it to do so by not diverting resources elsewhere would still count as a policy.

25.1 **Recommendation:** One area of active policy would be negotiating suitable market access abroad for UK professionals and their firms – e.g. via mutual recognition of professional qualifications or liberal inward investment policies in those markets. Doing this could also be badged as an industrial policy in the sense of focusing on a sector and seeking to enhance its productivity and reach.

26. Relatedly, the UK will not be able to provide sufficient services to satisfy both domestic and export demand, and so provisions must be made for UK firms to import services from abroad to achieve net-zero at least cost.