Written evidence submitted by the Institute of Directors (IoD)

Inquiry: Jobs, Growth, and Productivity after Covid-19

We appreciate the opportunity to participate in this inquiry. We regularly receive feedback from our members on the Coronavirus pandemic and the economic recovery. As this is an evolving issue, please find below a snapshot of responses to some of your questions. We will continue to provide regular updates.

About the IoD

The IoD was founded in 1903 and obtained a Royal Charter in 1906. It is an independent, non-party political organisation of approximately 20,000 members. Its aim is to serve, support, represent and set standards for directors to enable them to fulfil their leadership responsibilities in creating wealth for the benefit of business and society as a whole. The membership is drawn from right across the business spectrum, with 70% consisting of directors from small and medium-sized enterprises (SMEs).

Jobs, growth and productivity

How much difference can government policy make to economic growth?

Government policy can play an important role in developing the pre-conditions to support directors to drive business growth, job creation, and innovation. Loan, grant, and regulatory support over the past year has enabled many businesses to weather the pandemic and restrictions, and equally, policy can help bolster firms as they attempt to reopen, rescale, and rehire during the recovery.

Around 40% of our members feel lower employment taxes (such as employer's NICs), and business tax reliefs would be the best way to support the UK's economic growth over 2021 and 2022. Meanwhile one-third would prioritise investment in the UK's digital infrastructure and business investment incentives to support the wider economic recovery.

What are the causes of the gap in the UK's level of productivity compared to other advanced economies, and why has productivity growth been persistently weak in the aftermath of the 2007-09 financial crisis?

The high concentration of banking and financial sector activity in the UK economy, and the sectors' slow recovery over the past decade, was a key factor behind subdued productivity growth since the 2008 financial crisis, relative to peer nations. More broadly, this period has also been characterised by low levels of both private and public sector investment in skills (e.g. retraining, digital skills, management skills), capital (e.g. plant, machinery and infrastructure), and innovation (e.g. tech adoption), all of which underpin productivity growth.

Around 40% of our members feel digital and physical infrastructure investments would be the best way to drive productivity growth, compared to around one-third who would prioritise a reduction in the regulatory burden, improvements to the skills system, and support for R&D.

How successful has the Government's pandemic response been in protecting jobs to date, and how can it help reduce and mitigate the economic scarring effects of the pandemic going forward?

The Coronavirus Job Retention Scheme has provided significant support for our members and has helped many businesses to retain staff. That said, inevitably, some firms have had to make redundancies, including for roles their organisations will need in the future.

The risk of long-term unemployment rises the longer economic activity remains subdued. This means ongoing efforts to support businesses' cashflow, alongside fresh initiatives to drive-up investment and start-up activity, would be paramount in limiting the chance of long-term unemployment. As the economy reopens further, firms will also naturally be looking to make vacancies and restaff.

Targeted employment initiatives can also provide support to at-risk groups. At this stage it is still relatively early to judge the effectiveness of the programmes in the Government's Plan for Jobs, though our members are broadly supportive of them. One-third are likely to hire workers under the Kickstart Scheme, while around 30% are more likely to hire apprentices and almost 40% are more likely to hire a young trainee, given the incentive packages announced.

Over the longer-term the pandemic has accelerated many business trends which are likely to shift the demand for certain skillsets. This could have implications on the ability of the unemployed to find work, particularly those in sectors most impacted by lockdowns. Digital skills will be more in demand as firms have digitised their business models, and with greater impetus behind the 'green economy', workers with a knowledge of the sector will increasingly be sought. This means raising access to retraining tools is just as important for existing employees as it is for the young and currently unemployed.

Additionally, helping businesses to adjust to Brexit, scale, and align to new industrial trends can help drive growth, and avoid scarring. Firms will need more support to adjust to Brexit, and to redraw their supply chains. The March Budget was also lacking in significant support for UK scale-ups. While the country has become a hub for digital and fintech start-ups, skills and financial barriers have prevented the development of anything close to the Silicon Valley titans, which holds back the UK's productive potential. As the host of the UN's COP26 summit this year, the UK's green agenda could also do with more fleshing out, which can help drive innovation and grow the UK's renewable sector.

What policies are effective in helping people to reskill, move between occupations and sectors and take advantage of new opportunities? How could these be best implemented in the aftermath of the pandemic, and as technological developments such as artificial intelligence change the nature of work?

The pandemic has highlighted the challenges facing the UK's skills system. Unemployment has increased, swathes of the workforce have been placed on furlough, and the pandemic has led to industrial shifts which have accelerated demand for new skillsets. Developing the skill system, with an emphasis on retraining, reskilling, and lifelong learning, will be crucial to stave off the effects of long-term unemployment and to support the UK economy's economic adjustment. This is even more crucial as businesses adjust to the new immigration system, and as international labour movement remains restricted by covid-19 border restrictions.

While the broader skills and apprenticeship framework is being developed, the Government could, for example, introduce a temporary retraining credit incentive to allow SMEs to fund their retraining needs during the recovery, with a particular emphasis on digital and green skills, management and leadership competencies, and other professional training. The emphasis would be on quickly driving up engagement with specific retraining programmes in skillsets vital for the post-pandemic economy.

Raising access to digital, management, leadership, and 'green' skills training is needed to support productivity in time-constrained SMEs and the broader adjustments needed for the post-pandemic economy. Lengthy courses pose a significant opportunity cost for small firms in particular, and so access to shorter modular courses, online training, peer-to-peer learning, mentoring, and coaching style programmes would be beneficial. As such, the Government ought to consult on extending and funding the Apprenticeship Levy to a broader "training levy" to allow it to be spent on upskilling and developing more in-demand skills. Indeed, many Levy paying firms are sitting on unspent funds.

The announcement of a Lifelong Loan Entitlement for all individuals is a welcome step, and we welcome further consultation on its operation and function. Our preferred approach would be to create a 'shadow personal allowance', or another form of tax relief, to incentivise engagement with qualifying lifelong learning courses or programmes. This could, for example, be offset against an individual's income tax liability provided they have paid for a course. As such, any loan offering should be designed to consider the most effective incentive and repayment structures to support take up. Indeed, developing a lifelong learning offer would be particularly invaluable for freelancers, sole traders, and the self-employed who may not be able to access training given their employment status and would otherwise have to rely on their own personal finances.

Is the Government doing enough to encourage corporate investment?

The investment incentives, including the Help to Grow scheme for SMEs and the capital allowance 'super deduction', which were announced at the Budget were welcomed by our members. But further incentives, covering more organisations and investments, are much-needed to drive-up investment across the corporate community. Indeed, the repairing of balance sheets and ongoing uncertainty will continue to restrain business investment more generally.

Around 40% of our SME members were considering applying for funding via the Help to Grow scheme to support their investment in digital technology and management skills. Meanwhile a further 25% of our members, who do not qualify for the scheme due to their small employee numbers, said they would also be interested in support under the scheme.

Almost one-third of members said the 'super deduction' incentive would increase their investment plans over the coming 24 months, while around two-thirds expected it to result in no change to their investment plans. While this incentive would seem generous on the surface, for many large businesses its interaction with the proposed hike in corporation tax could likely detract from the incentive to bring investment plans forward (see **Figure 1**).

Over 1 in 3 of our members consider business investment incentives as a priority for the economic recovery. While some firms were able to make investments in digital technology to support their adjustment to coronavirus, many are aware of what investments they need to make but are unable to execute decisions due to poor cashflow. Extending incentives, like the digital vouchers under the Help to Grow scheme, for more firms to make investments in existing digital technology (e.g. cloud computing and data tools) and potentially also in green endeavours (e.g. products that reduce carbon footprint or improve sustainability), can help capitalise on the current digital, and green, moment for the UK, which can drive the recovery and productivity gains.

Figure 1

Scenario 1: Company using super deduction before April 2023

assume 100k investment (which receives 130% 'super deduction')

@ 19% corporation tax

tax saving

= 19% * (100K * 130%)

= 24.7k

Scenario 2: Company using normal annual investment allowance after April 2023

assume current annual investment allowance remains (allows 100% write-down up to 1m till Dec '21)

assume 100k investment (which receives 100% 'AIA deduction')

@ 25% corporation tax

tax saving

= 25% * (100K * 100%)

= 25k

Is the "Plan for Growth" an adequate replacement for the "Industrial Strategy"?

While the "Plan for Growth" is a broadly welcome development, it is important to note that the chopping, changing, and rebranding of the UK's long-term growth agenda can negatively impact business engagement with its component policies and initiatives. Indeed, a clear coherent economic plan can support business leaders in their own long-term planning, but many are yet to digest what opportunities the new plan holds for their organisations and are mainly keen for more details on the precise measures and timeframes behind the various 'plans'.

Furthermore, the loss of the Industrial Strategy Council, which was an important institution in providing long-term accountability and oversight on the Government's strategy, risks discouraging long-term business planning and investment decisions. While the ISC lacked the legal status and tools to act as a check and balance on supply-side policy, the IoD believes a similar independent institution, with more teeth, is necessary.

Is the UK well placed to take advantage of future technological breakthroughs and translate them into economic opportunities?

The UK suffers from the weak diffusion of best practice technology throughout the business community. Indeed, many UK SMEs lag other advanced nations in their adoption of even existing digital technologies. By helping small organisations get onto the ladder of digital investment, and by supporting the diffusion, and application, of best practice in technology from leading firms and R&D, the UK can be better placed at taking advantage of future technological breakthroughs.

Macroeconomic policy

What are the roles of monetary policy and fiscal policy in stabilising the business cycle and promoting growth in the post-pandemic economy?/What evidence is there on the relationship between the scale of the public debt and economic growth?

Currently, the risks of a high national debt and deficit appear to be low. Interest rates are at a historic low, keeping borrowing costs down, and yield curves are also largely anchored downward in the long-run. Indeed, the UK Government has a critical window now to continue to support the economic recovery with tax reliefs, spending, and investment.

Over 80% of our members believe the Government should, for the time being, prioritise stimulating economic growth over reducing the deficit/level of debt. Businesses will be a key driver for economic growth next year and beyond as they look to rescale, innovate, and take staff back on. Fiscal consolidation, particularly in the form of tax hikes on investment and entrepreneurial activity, risks choking off the UK's recovery. Furthermore, by inducing weaker economic growth, and thus lower tax revenues, a move to raise taxation now could make deficits and debt more unsustainable in the long-run.

Is a return of inflation a risk to the economic recovery?

Our member surveys show that around 57% of business leaders expect costs to be higher in the coming 12-months compared with the previous year, which may be indicative of forthcoming inflation. Many of these higher costs are being driven by reopening expenses, rehiring/taking staff off furlough, paying back debt and deferrals, limited spare capacity, and Brexit adjustment, and as such we expect a natural pick-up in price levels during this period of economic recovery. While this may just be transitory, it is important that business costs, emanating from tax, regulation and other fees, are kept low to help support firms to develop margins and to keep a lid on inflation.

Tej Parikh

Chief Economist

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