

*Gordon Brown has expressed concern over the UK's poor record on productivity. Evaluate the policies the government can use to improve the UK's international competitiveness. (60 marks)*

*Government investment on infrastructure has suffered from decades of under-investment. In terms of government investment as a percentage of GDP, the UK has consistently underperformed in comparison to its main competitors, lagging behind all other G7 countries (USA, France, Germany, Japan, Italy and Canada) from 1980 - 1999. This legacy of underinvestment can be seen in our transport infrastructure for example. Total transport investment has been falling in real terms as a percentage of GDP since the early 1990s. Increased economic activity and rising incomes have generated more demand for both private travel and the increased transport of goods and services. A combination of insufficient investment and rising demand for travel has resulted in increasingly congested roads, inadequate public transport and services and an overcrowded and unreliable rail network. Improvements to infrastructure are clearly required. Therefore one way in which the Government can improve infrastructure is by increasing the amount of money spent on roads and rail for example, which would have positive multiplier effects to many firms and individuals, however this extra spending would have to be financed by higher taxes, which in reality is not a political ideal. However, infrastructure is not only roads and railways; the UK is doing well in a new type of infrastructure, the internet, which is part of e-commerce and strong levels of communication between businesses (even on a world wide basis). This is significant because digital technologies are a key enabler of a modern knowledge driven economy, such as the UK. If UK businesses lag behind its competitors in adopting digital technology, the UK will be unable to take advantage of the opportunities provided, such as giving businesses the opportunity to make improvements to their internal processes, shorten their supply chains and reduce the cost of processing transactions. More generally, there is potential to lower search costs by increasing access to, and lowering the cost of, information for both business and consumer (closer to perfect information/knowledge). However, this increase in communications infrastructure can have its disadvantages, especially on a knowledge/service economy such as the UK. What has been found is that firms that were based in the UK have moved over to lower cost countries such as India, who have an educated workforce (supply side policy) and relatively lower wages. Because of the simplicity and lower costs of moving these types of operations, such as internet design and telephone*

operators, there is an ongoing outflow of jobs to these lower cost, lower wage countries.

Another policy which the government can adopt to address the poor productivity and to improve the level of UK international competitiveness, is an improvement of the skills gap that the UK is said to have relative to other advanced OECD countries (of which there are 29). Even more serious for competitiveness is the shortfall in vocational qualifications, especially at the intermediate level. These problems are compounded by a shortage of skilled managers, as revealed by studies undertaken for the Skills Task Force. Germany, for example, has good vocational training from its government and businesses and can therefore benefit from a more developed and flexible workforce which is, therefore, more productive. This is significant because workers need to be equipped with sufficient skills to take advantage of opportunities from innovation and adaptation to keep the business competitive. This policy, which is in use, means that the government is committed to ensuring that the UK competes for the best skilled workers in the world market, by reviewing the work permit scheme, the government has made high skilled jobs, such as in ICT part of the shortage list and therefore employers can find it easier to arrange work permits. Also to combat this skills gap, the government can implement a policy of increased and better vocational training by, for example, introducing this type of training into universities. However, this would have relatively small time lags (in comparison to other supply side policies).

The latest international comparisons show UK R&D performance falling even further behind our main international rivals. This has consequences not only for our ability to develop innovative ideas but also to adopt and adapt ideas developed overseas. Evidence in the previous point on skills suggests that an important constraint on improving the commitment to innovation may be managerial attitudes and quality. In the UK, overall, services perform very well on innovation spending, on average spending more than their European counterparts, and services spend more on innovation than manufacturers, who are performing poorly against other comparative countries (i.e. G7). Part of this lack of investment in R&D stems from the UK based culture of short-termism whereby managers are more inclined to satisfy shareholders in the short run, as opposed to looking to long term aspects. Because of this the UK has suffered from decades of under-investment. Business expenditure on fixed capital per worker still compares poorly with other G7 countries.

Finance may be a constraint for some companies but workforce skills, the quality of management and attitudes to risk seem to be more of a problem.

R&D is significant because successful innovative new products or processes require not just business expenditure on R&D but also expenditure on design, training, marketing and equipment. To address this problem the government can/is using/introducing a number of measures to stimulate investment in innovation and R&D. Such measures include reforms to capital gains tax, new enterprise management incentives and the tax credit scheme for small firms' research. Consideration is also being given to proposals to extend the R&D tax credit to beyond small firms. In addition, for companies to make the most of science and technology (which in the UK is strong and is being strengthened further through international collaboration in R&D) the UK needs more people who are skilled technically as well as being skilled in management and entrepreneurship. The government is providing additional funding for Science Enterprise Centres to teach science, engineering and technology graduates business and managerial skills. However, time lags will be involved here, and this can be shown by data indicating that R&D is still under developed in the UK in comparison to other first world countries.