Firing up the post-COVID economy: How to be “pro-business” in the 2020s

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The UK’s economic model has displayed numerous shortcomings for many years. It is time for a new approach. A social market-based pro-enterprise agenda is the strongest foundation for a successful and sustained post-Brexit and post-pandemic economy that is also able to weather the headwinds of technological change.

KEY POINTS

- The prevailing liberal market economy (LME) model has, despite the claims of its proponents, failed to create a “pro-business” environment.
- Despite relatively light regulation and cuts to corporation tax over the past four decades, UK businesses lag behind those in peer economies in terms of levels of innovation and investment. A non-trivial proportion of domestic businesses display a lack of ambition, with a considerable number not interested in growth at all and a smaller fraction of UK businesses scaling-up rapidly, compared to other advanced economies.
- The LME model has failed to deliver because it does not sufficiently prioritise key measures determining business outcomes and over-prioritises low tax and light regulation.
- The 2018 Business Perceptions Survey produced by the Department for Business, Energy & Industrial Strategy showed just 16% of businesses reporting the level of tax as the greatest challenge they faced, falling to just 2% for large businesses with 250 or more employees. For large companies, attracting and retaining customers, complying with regulation and staff recruitment and retention were all cited as much more important factors.
- Improving aspects of the business environment – such as public service quality, infrastructure and skill levels – may require higher rates of taxation, including corporate taxation, to support the necessary government expenditure.
- A new economic model, based on social market principles, would improve business performance and in turn economic prosperity – striking a better balance between taxation, institutional quality and public investment in measures that are beneficial to businesses.

THE NEED FOR CHANGE

An economy grappling with numerous challenges

The UK economy is at a critical juncture. The Coronavirus pandemic has seen growing demands for a larger, more activist state, not just now but as part of a longer-term readjustment of the economic settlement. The pandemic has highlighted the deficiencies of the UK's benefits and health and social care systems in providing support to those in need, necessitating greater government spending on a sustained basis - and a strong economy to generate the tax revenues to support such spending.

Further, the pandemic is set to lead to permanent job losses in sectors such as retail, where lockdowns have accelerated the demise of the traditional high street as shoppers increasingly shift online. There are calls for government to expand its role in the labour market through measures such as supporting retraining opportunities and, as the SMF recently argued, acting as an employer of last resort by creating a Universal Jobs Guarantee.[1]

In addition, suggestions are circulating that the UK needs to take a more strategic approach to industry[2] [3] and public services, in order to ensure society and the economy are more resilient in the face of future "shocks". This will require changes which are likely to involve more spending, perhaps through state aid and public procurement channels.

In addition to the pandemic, the UK left the transition arrangement that it had with the EU on the 31st of December last year and began a new bilateral relationship based on the EU – UK Trade and Cooperation Agreement.[4] Brexit is likely to result in some long-term changes in the UK's trade patterns as the UK's trade arrangements evolve. It also means that the UK will have considerably more autonomy over policy levers across a wider range of areas than it did within the EU.[5]

Unfortunately, discussion to date over how policy might change in order to boost the UK's GDP per capita levels over the long run has often failed to reflect the complexity of the factors that drive long-term prosperity, including finding the best ways in which business can be helped to bring about such economic improvement. Instead, much of the public discussion has frequently devolved into an unhelpful polarisation between those pushing for ever greater tax cuts and indiscriminate liberalisation on the one hand, and those who see the market as something to be tolerated at best, and rarely acknowledged as beneficial for society.

Further, the UK, like all countries, is experiencing the headwinds of technological transformation.[6] The so-called "Fourth Industrial Revolution" is likely to create considerable economic disruption over the coming decades as existing industries change as a result of technology - some will grow, others may shrink and perhaps a proportion will wither away, while new ones emerge.[7]

Finally, the UK's problem of relative economic underperformance in recent decades, compared to previous periods of UK post-war economic history and comparable countries, remains an unresolved challenge.

Between 1961 and 2019, the average annual growth in GDP per capita in the UK was 1.9%.[8] This average figure, however, hides a steep drop-off in GDP per capita growth in the UK, in the early 2000s. This decline in the growth rate is highlighted in Figure 1.

It has also been widely noted that the UK workforce is considerably less productive than peer economies. Per hour worked, British employees produce less economic output than peers in the US, Germany, France and Italy. Productivity on this measure is lower than the average for the G7 group of countries.[9]

These demands on the public purse come at a time when the national debt is the highest it has been in peacetime, raising questions about the viability of more deficit financing and how the existing debt accrued as a result of the crisis might be paid back.

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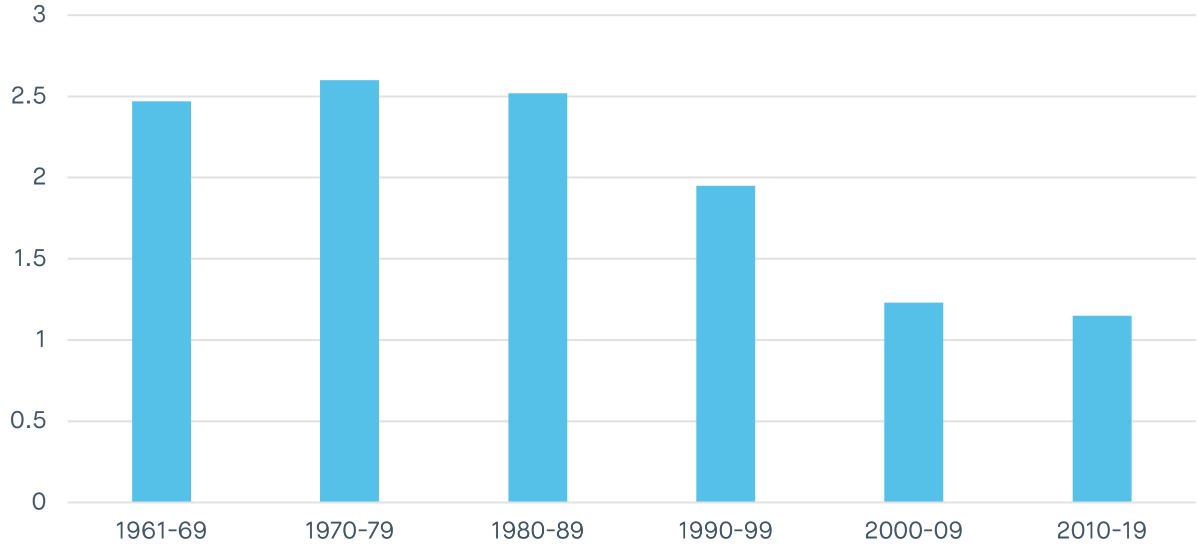
Figure 1: Average annual GDP-per-capita growth rate in each decade between 1961 and 2019 (%)



Source: World Bank

ADDRESSING THESE CHALLENGES

How best to deal with this plethora of challenges facing the UK? A big part of the answer must be "high quality" economic growth. This means something other than a post-pandemic return to the comparatively low productivity growth the UK has experienced in recent decades. Rather, the UK needs a step-change in productivity growth, which would in turn translate into higher living standards.

In this paper, we argue that achieving such ends will require the UK to jettison its laissez-faire economic strategy and the liberal market economy (LME) model that was built to implement it, and which has dominated the UK's political economy for the past forty years. The LME approach has failed to live up to the expectations many had of it. It has not, for example, enabled UK businesses to deliver the kinds of aggregate productivity gains that those who support a LME approach argue can only be obtained through free markets. Further, substantial reductions in corporate tax rates have not translated into greater levels of investment and innovation in the UK.

The importance for business in a new economic model

For the UK economy to emerge strongly from the downturn created by COVID-19, prosper outside the EU, successfully ride the wave of technological change associated with the Fourth Industrial Revolution *and* reverse its recent historical economic underperformance, we argue that business needs to play a leading role. An alternative to the LME model, far from being anti-business, must do all it can to promote entrepreneurship, innovation by businesses and competition among businesses.

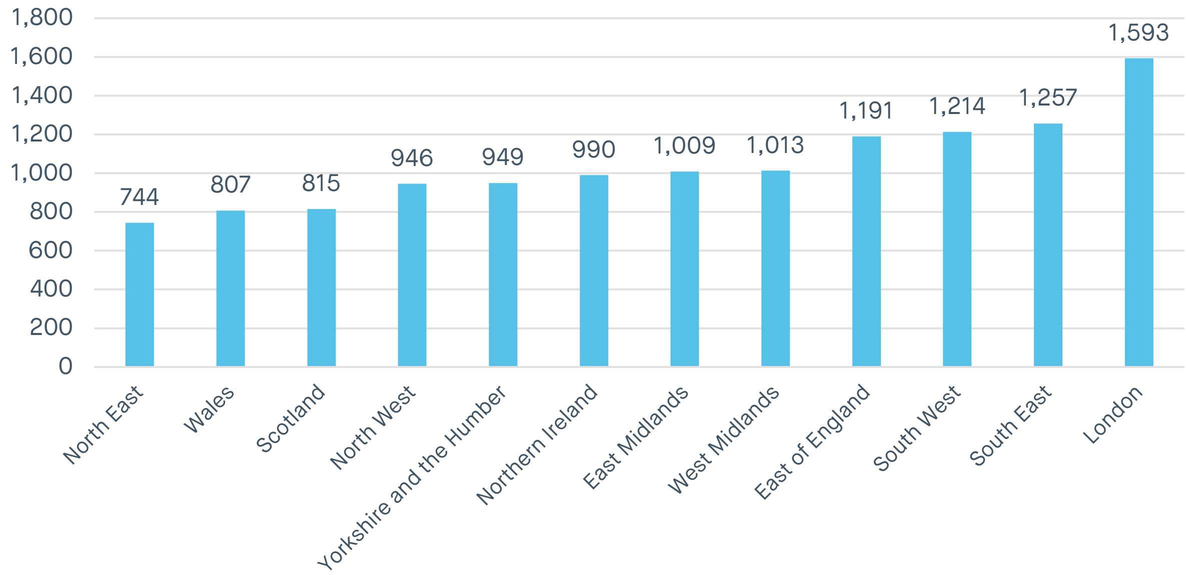
The private sector employs more than 80% of the UK's workforce. With potentially hundreds of thousands of jobs set to disappear in the retail sector, city centre economies affected by the rise of remote working, automation leading to job losses and adjustments in export patterns (courtesy of global growth trends and new trade arrangements), business will be required to generate new jobs. Not least in the fast-growing and high-value industries of the future. For that to happen, the UK needs a more competitive business community, spurred on through a genuinely "pro-enterprise" business environment, based upon a more sophisticated understanding - than the dominant LME approach - of what such an environment entails.

The risk of business being overlooked as we emerge from COVID-19

Despite the importance of private enterprise to economic success, and the purported centrality of business to the LME approach to the economy, much of the discussion about the economic recovery from COVID-19 and the post-Brexit economy has focused on the case for a larger and more active state, rather than the need to boost business dynamism and deliver a step-change in the UK's aggregate labour productivity growth trajectory, which would help resolve some of the dilemmas that are facing the Government – such as how to balance the deficit and growing national debt, expand the state and improve public services. The British Academy's "The COVID Decade" report is a good example of this tendency.[16] While the report is an important contribution to the debate about UK society after the COVID-19 crisis, the private sector and how prioritising business-led growth could contribute to overcoming many of the social challenges that it discusses, is treated as a second-order issue.

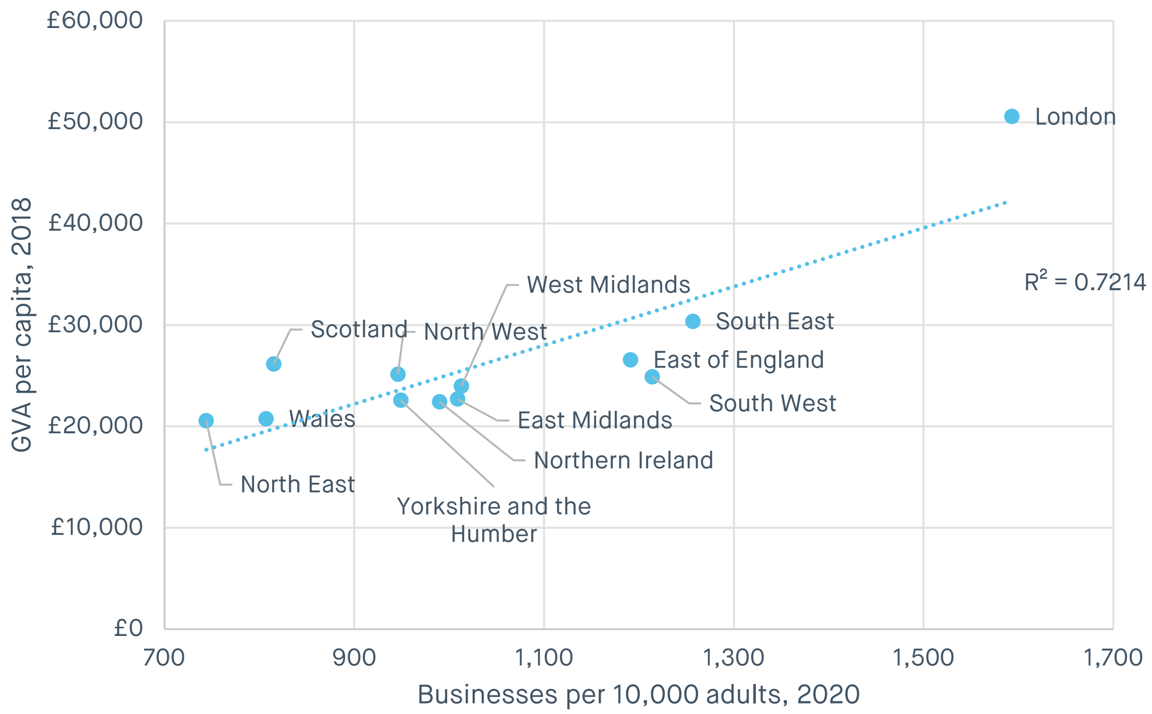
Another example of the relative under-attention given to the private sector in the debate over the UK's post-COVID crisis recovery is the emphasis on moving some of the central civil service to the regions and nations of the UK.[17] While a potentially positive move if done with care,[18] [19] the policy is asymmetrical. There is comparatively less emphasis on bolstering the private sector in those regions with complementary measures of similar ambition to invigorate the business environment that can encourage business-led growth in those same parts of the country. This is despite a clear correlation between, for example, regional levels of entrepreneurship and local level economic performance, as illustrated in the charts below.

Figure 2: Businesses per 10,000 adults, 2020



Source: BEIS business population estimates

Figure 3: Gross value added (GVA) per capita versus business density, by region



Source: SMF analysis of BEIS business population estimates and ONS regional economic accounts

Why is the role of businesses in delivering economic prosperity being given such short shrift? Perhaps, in part, this reflects growing doubt about the long-term success of Britain's purported "pro-business" LME model. Its supporters believed such an economy - where businesses are "set free" - would generate the best environment for entrepreneurs and businesses to thrive in. Yet, its overall record in delivering sustained prosperity is a mediocre one that falls short of what its adherents claimed it would deliver.[20]

Certainly, the balance of evidence across a number of key dimensions that influence business success - and in turn economic growth - suggests there are good reasons for such doubts. Despite four decades of dominance by an ostensibly "business friendly" policy approach:

- Entrepreneurs and businesses have failed to invest sufficiently in **human**[21] [22] and **physical**[23] capital on a sustained basis, which has constrained the competitiveness of individual businesses and has, in turn, held back economy-wide productivity and wage growth.
- Many enterprises operate with comparatively **poor quality management**.[24] This is a persistent failure in British capitalism, hindering successful entrepreneurship and firm growth.
- In some markets, competition is not intensive enough, leaving the UK with many sectors that are **less dynamic** than they could be and domestic industries operating more inefficiently **compared to other countries**.[25] [26]

- A non-trivial proportion of domestic businesses display a **lack of ambition**, with a considerable number not interested in growth at all and a smaller fraction of UK businesses **scaling-up rapidly**, compared to other advanced economies.[27] [28]
- Other than a handful of sectors, private sector innovation levels (measured through **R&D** expenditure, **patents** and **technological adoption**) typically lag behind innovation in firms in other countries.[29] [30] [31]

A case study of the quintessential LME policy for business-led growth: Corporation Tax reform

The approach to Corporation Tax reform of successive governments since the mid-1980s has been emblematic of the LME orthodoxy about how to create a "pro-business" environment, which facilitates high-levels of business-led productivity growth over the longer-term.

Corporation Tax reform was a central element of the "supply-side" reforms at the heart of the transformation of the UK's political economy in the 1980s, from its post-war mixed economy (sometimes referred to as "Butskellism" or the post-war consensus) model to a LME regime.[32] Corporation Tax was introduced by the Wilson Government in the 1960s.[33] The trend in company tax policy, until the Lawson reforms in the 1980s, was for higher headline rates but generous allowances and exemptions for activities such as capital investment. This approach was turned on its head by the Chancellor Nigel Lawson, who pursued a policy of cutting the rates and broadening the corporate tax base (i.e. reducing the number and generosity of allowances and reliefs).[34] [35]

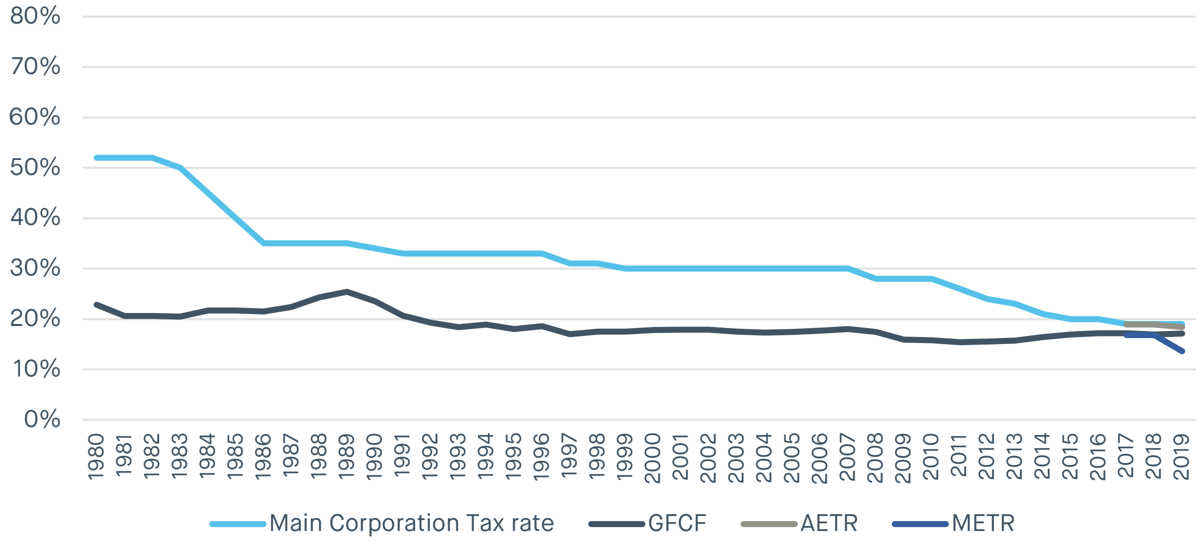
Until the Budget of March 2021, the approach to Corporation Tax implemented by Lawson when Chancellor of the Exchequer under Margaret Thatcher, remained the received wisdom in policymaking circles. Its influence is reflected in the way subsequent governments of all colours did not challenge the fundamentals of the approach established in the 1980s. Rather, their policies towards Corporation Tax were consistent with the underlying assumptions of and broad direction set by the Lawson reforms.

Corporation Tax reform: little impact on long-run business investment performance or productivity

A key expectation of the proponents of ever-lower Corporate Tax rates was that less profit taken by the tax authorities would mean higher returns on business investment and more revenues available for competitiveness enhancing investment in business assets such as machinery and equipment. However, as noted in detail by Andrew O'Brien in a report published by the SMF last year,[36] there is scant evidence that the UK has seen a significant improvement in capital investment behaviour in response to such rate cuts and the broadening of the base (see charts below).

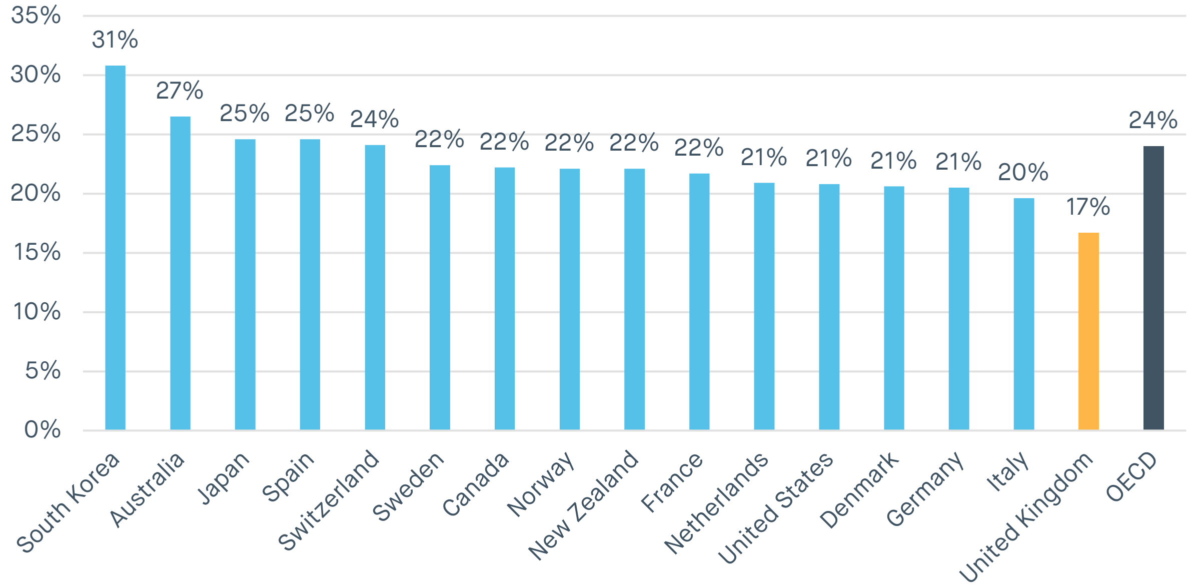
In 1980, investment, measured by gross fixed capital formation (GFCF), was 22.8% of GDP. Since then, GFCF peaked in 1989 at 25.4% of GDP. From the 1990s, GFCF has tended to vary between 18% and 15% of GDP. In 2019, GFCF was 17% of GDP. In the UK, GFCF is a lower proportion of GDP than a range of peer economies such as France and Germany, despite a relatively more "favourable" corporate tax regime.

Figure 4: Trend in the UK's main corporate tax rate and GFCF as a percentage of GDP, 1980 to 2019



Source: World Bank, OECD and Tax Foundation

Figure 5: Average GFCF as a percentage of GDP in select countries, 1997 to mid-2017

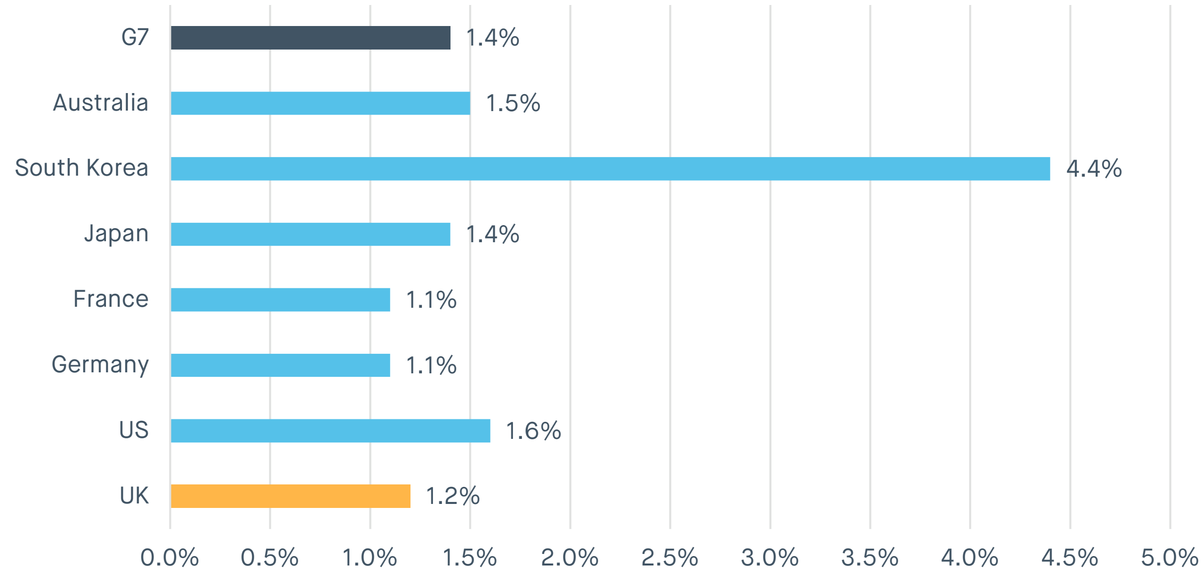


Source: ONS analysis of OECD data

The consequences of the underwhelming investment response by the UK business community to the policy of sustained Corporation Tax cuts is evident in the UK's comparatively lacklustre labour productivity growth figures and the decade-on-decade fall in GDP per capita growth rate discussed earlier.[37]

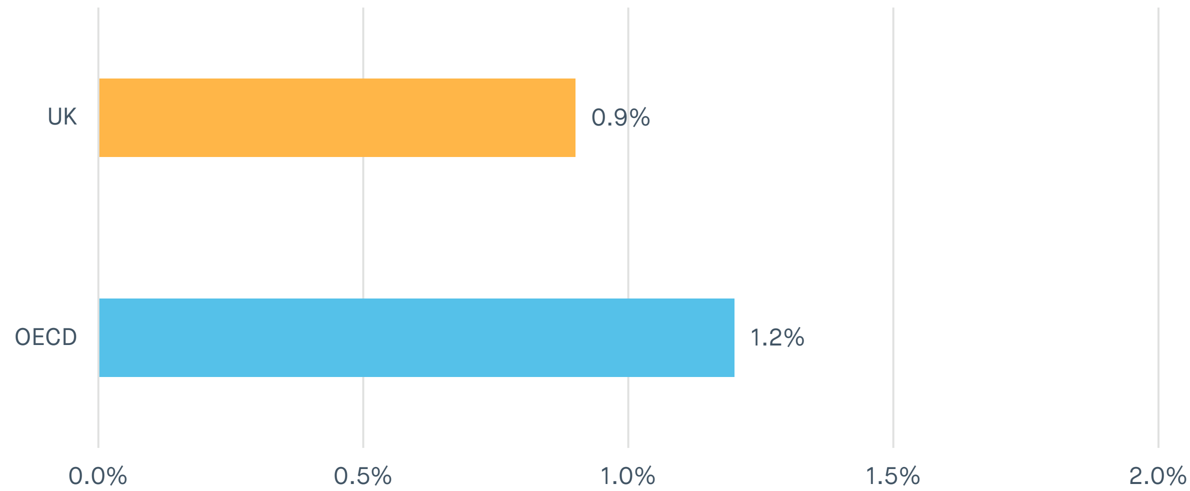
Across the period 1995 to 2019, the UK's average labour productivity growth increased by 0.2 percentage points less, per year, than the G7 average. The pattern is also visible in OECD comparative data, which shows that between 2001 and 2019,[38] the average annual labour productivity growth of the OECD countries was 0.3-percentage points higher than it was in the UK.

Figure 6: Average annual labour productivity[39] growth in the UK and selected countries, 1995 to 2019



Source: OECD

Figure 7: Average annual labour productivity[40] growth in the UK and among OECD countries, 2001 to 2019



Source: OECD

Time to admit the experiment did not work on the scale it was expected to

Corporate tax reform has largely failed to encourage UK businesses to invest at “global frontier” levels and consequently it has made a negligible difference to aggregate labour productivity growth in the UK relative to other industrialised countries. It has made little contribution to sustaining GDP per capita growth rates at close to their historic average.

Admitting this is the first step towards improving the business environment for UK entrepreneurs and firms. After the catharsis that will come with acknowledging the shortcomings of the dominant approach of the past 40 years, the job of identifying and implementing better policies to achieve the consistently higher levels of business-led growth needs to begin.

Why the LME approach to business-led growth has failed to deliver

The range and complexity of the drivers of business growth

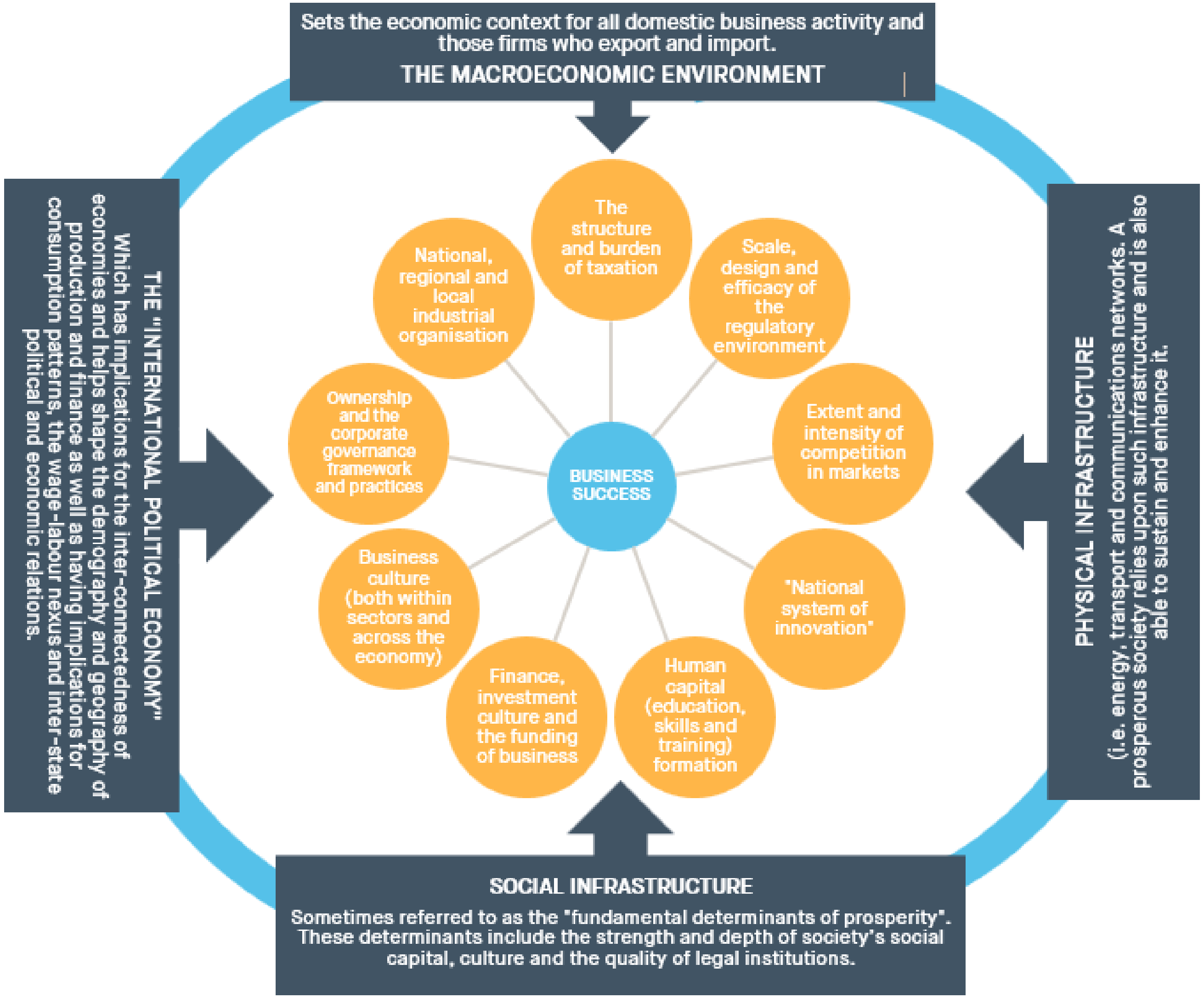
A key reason why the dominant LME policy approach of the last forty years has fallen short of generating the business-led productivity growth its supporters claimed it would is that it relies on a partial understanding of what drives business competitiveness and dynamic markets.

The liberal market policy orthodoxy puts its faith in the largely uninhibited market almost always finding the optimal outcome and relegates to the status of minimal importance, the many complexities and subtleties that play a role in contributing to entrepreneurship and business success and, in turn, long run economic development.

The upshot of having such a perspective is that the policy prescriptions which are considered the most effective i.e. that will ensure a prosperous society, are ones that maximise the scope of the market and avoid encumbering the freedom and initiative of private actors and minimise distortions of the "natural" operation of the market.

However, such an approach will always disappoint because, as economic history teaches, entrepreneurship and business competitiveness in particular, and therefore economic growth more generally, is a more complex phenomenon. For example, there is a good deal of historic contingency involved and a multiplicity of factors, such as the characteristics of entrepreneurs and business leaders or a firm's internal organisation and capacities. Others relate to the composition and nature of the business environment in which entrepreneurs and businesses operate and how the environment enables and constrains commercial plans and activities – such as the quality of infrastructure, public services and the skill levels in the workforce. Some of the key influences on entrepreneurs and firms are set out in Figure 8.[41] [42] [43] [44] [45] [46] [47]

Figure 8: Elements of the business environment that enable and constrain entrepreneurship and business competitiveness

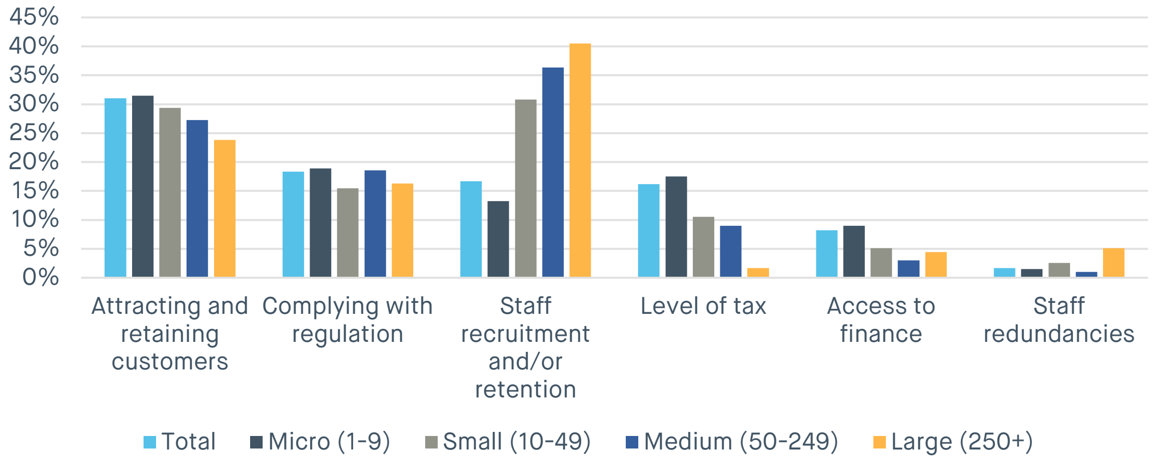


Sources: SMF analysis

The wide range and complexity of the factors which influence business success are frequently reflected in business surveys which find that there are often – indeed usually – greater concerns than levels of corporate taxation. The 2018 Business Perceptions Survey produced by the Department for Business, Energy & Industrial Strategy showed just 16% of businesses reporting the level of tax as the greatest challenge they faced, falling to just 2% for large businesses with 250 or more employees. For large companies, attracting and retaining customers, complying with regulation and staff recruitment and retention were all cited as much more important factors.

Given that higher levels of corporate taxation could be used to tackle these challenges – for example through public investment in skills and infrastructure - businesses (especially large ones) may be willing to accept such a trade-off. A new economic model, departing from the prevailing LME model, should aim to strike a better balance between levels of taxation and the other factors that are crucial for creating an environment that is supportive of business, entrepreneurship, innovation and competition.

Figure 9: Greatest challenge affecting business, by business size in terms of number of employees



Source: BEIS Business Perceptions Survey 2018

Policy that reflects the complexity of business growth

Policymakers need to develop a more nuanced understanding than that which LME model adherents offer, if they are to adopt a new economic strategy based upon a more dynamic business community, in order to shift the UK, sustainably, onto a higher growth trajectory, with stronger productivity growth rates underpinning it.

Only with a more sophisticated analysis and outlook - incorporating the multiplicity of interlinked variables that enable business success - can policymakers develop an environment that is optimally calibrated for business competitiveness.

Continuing with the flawed analysis and simplified prescriptions of the advocates of laissez faire approaches, as typified by the UK's recent history of Corporation Tax reform, would only result in "more of the same" of what the UK had before the COVID crisis and Brexit.

THE CASE FOR A SOCIAL MARKET APPROACH TO BUSINESS

Three ways forward for the UK business environment

There are signs that government is starting to take notice of the shortcomings of the prevailing economic model. The March 2021 Budget saw the Chancellor Rishi Sunak announce the first Corporation Tax *rise* in almost 50 years, with the main rate increasing to 25% from April 2023.[48] This was complemented by the creation of a "super deduction" for capital investment and a reintroduction into the system of a lower small firms rate, for profits below £50,000.[49] This heralds a shift away from the dominant (until March 2021) orthodoxy that ever lower corporate tax rates are needed to drive economic growth and encourage business investment.

Developments at the international level, such as the recent discussions among G7 members over minimum corporate tax rates, suggest there is a shift in opinion underway - among some policymakers in some of the biggest economies in the world - about the direction in which corporate tax rates should go in the future.[50] Suggesting that, over the next few years, the UK's recent changes are unlikely to be considered unusual in the international policy landscape.

Supporters of the existing LME orthodoxy have been vocal in their criticism of the Chancellor's plans for raising the main rate of Corporation Tax. This includes the former Chancellor George Osbourne, who argued that such a move "sends the wrong signal".[51] Others, who also warned against such a policy change, argued that increasing the rate would worsen the UK's already relatively ungenerous (by international standards) treatment of investment by businesses.[52]

Assuming, despite the criticism from its natural supporters, the Government sticks with its corporate tax plans, it suggests that reducing tax rates (and the assumptions behind such a policy about the best way to optimise the business environment) are no longer going to be a central feature of a wider LME model for encouraging entrepreneurship, investment and business success in the UK.

If the UK is moving away from a laissez-faire economic strategy, it raises the question: what should a new "pro-business" approach look like? There are, in in our view, three ways forward for policymakers:

1. **Build upon the existing policy orthodoxy and extend the UK's existing LME model – "Laissez Faire 2.0".** This might include winding back the April 2023 corporation tax increase once the public finances are put on a more sustainable footing. However, there seems little basis on which to believe that this approach will deliver better results than it already does.
2. **Construct a "new social market economy" that embodies the more nuanced understanding of the business environment and the drivers of business competitiveness above.** Such a settlement provides for a stronger basis on which to generate (compared to recent decades) high rates of business-led

productivity (and consequent GDP per capita) growth in the UK. However, such a change would require a significant re-orientation of the UK's current political economy, away from the LME model and the construction of a new approach based upon social market principles.

3. **Reheat (in an updated form) the post-war model of political economy: neo-Butskellism.** The growth and productivity data from 1950 to 1973 suggest that this approach – which involved a much greater role for the State, including through nationalisation of multiple industries - was successful until the early 1970s when it somewhat ran aground.[53] The early 21st Century is a different context to the post-war decades. How a reversion to an approach that emerged in a different era would succeed in the 21st Century is a considerable uncertainty and raises viability challenges for any attempt to revive the post-war model (albeit in a revised form).

The differences between the approaches are summarised in Figure 10.

Figure 10: Three policy approaches to business-led growth in the 2020s

Laissez-faire 2.0	New social market economy	Neo-Butskellism
A preference for lower taxes over higher public spending and a lightly regulated business environment - maximising the freedom of market actors - including a laissez-faire approach to market structure and competition and the balance of power between capital and workers and the commodification of labour.	A preference for public spending over lower taxes, and tax reform linked to clear social benefits, along with a balanced regulatory environment for businesses, that aims to ensure markets are competitive, market power is minimised, market failures are corrected, and limit the commodification of labour.	A preference for public spending over lower taxes and extensive constraints on and interventions in the business environment limiting the freedom of markets (and businesses in those markets), including the use of socialised ownership to restrict the scope for markets to operate, the nurturing of countervailing power to that of capital and strong constraints on the commodification of labour.
Market determination of the UK's business demography, industrial structure and economic geography.	Direct and indirect intervention to help shape the UK's business demography, industrial structure and economic geography.	State directed (or at least partially directed) determination of the UK's business demography, industrial structure and economic geography.
Minimum public investment levels, maintaining necessary public institutions but relying on private sector leadership for the bulk of the investment in assets such as human capital, machinery and equipment, intangible assets, innovation and physical infrastructure.	High public investment levels, with an active public sector investing in human capital and social and physical infrastructure and supporting private sector investment in assets such as machinery and equipment, intangible assets and innovation.	High public investment levels, with the public sector providing the bulk of the investment in human capital, innovation and social and physical infrastructure. The private sector retains more autonomy over investment in business assets such as machinery and equipment and IP.
Minimal legal framework around private ownership of capital, little interest in the structure of ownership or how capital is	A legal framework that regulates the ownership, structure and uses of capital to maximise social benefit and not	Extensive legal intervention exerting considerable control over the private ownership of capital and how it is structured

utilised by those who own it, a high degree of autonomy in business-investor relations and the allocation of capital resources. Including leaving the financing of businesses to be determined, primarily, by private institutions and individuals.	just private returns, including direct and indirect interventions in the market for financing business.	and used, along with state owned assets replacing private ownership in some "important" areas. Including directly financing businesses instead of leaving that, primarily, to private institutions and individuals.

A social market approach is needed to maximise business-led productivity (and GDP-per-capita) growth

It is only change at the system level that will deliver a sustained step-change in productivity growth and a significant increase in the UK's GDP per capita levels. The system change required is the building of the "new social market economy" model, based upon the insights and principles of the social market. Only a dismantling of the current LME and the construction of a new model will deliver sufficient improvement in economic performance and ultimately national prosperity. This is because social market principles recognise the complex relationships between the factors that drive business competitiveness and look to ensure that they are optimised for economic success.

Creating a new "social market" orthodoxy for business-led growth

In order to develop a social market economy that will generate higher levels of business-led productivity growth, there will be a need to build a new and compelling narrative and policy programme around the importance of enterprise in driving up long-term per capita prosperity growth.

The first step towards change requires policymakers to shift their mindset and recognise the comparative failure of the LME model to transform the UK's long-term productivity and economic growth performance and, consequently, that the optimal business environment for the future is not one based upon the Laissez-faire 2.0 option. The UK's relative economic decline under Butskellism – which saw the country dubbed the "Sick Man of Europe" – also suggests something different from a reversion to the Post-War consensus is needed.

Policymakers need to embrace the more complex reality of business growth - something the high priests of global capitalism at the World Economic Forum (WEF) have done. The WEF, for example, has noted that businesses value a multiplicity of other factors – above, for example, low taxes which typify the LME model - when deciding on what to do.[54]

POLICY DIRECTIONS: BUILDING THE "NEW MIXED (SOCIAL MARKET) ECONOMY"

If policymakers embrace a new model for the UK's political economy, they will realise that contrary to the "received wisdom" on which the current LME model is based, a higher tax economy is not necessarily an "anti-business" policy stance. If implemented sensitively, such an approach to the business environment can be explicitly "pro-business", if those taxes help improve it.

What might bringing-into-existence the "new mixed (social market) economy" require policymakers to do? This briefing note is not the place for laying out a detailed manifesto for delivering the new model of political economy for the UK. However, a sense of direction in which policy would need to go in, is offered below.

Key to the "new mixed economy" approach to business-led growth is "getting the basics right". This involves reviving and modernising the country's "social infrastructure"[55 56 57] and as part of that effort, enhancing the UK's state capacity. This will require a comprehensive upgrade programme that will place the UK at the "global frontier" of institutional quality and administrative capability i.e. on a par with counties like Singapore, Denmark and Switzerland. Countries consistently ranked near or at the "global frontier" across multiple international quality and capacity benchmarks.

The more active state of the "new mixed economy" requires a more effective state. The national and local government bureaucracy needs to become genuinely transparent, easy for entrepreneurs and businesses to interact with, actively helpful to enterprise in many areas and agile in the face of change.

Strategic goal – shift to the insitutional quality and state capacity "global froniter"

Rebuild the UK's "social infrastructure" and move the UK to the international "frontier" of institutional quality and administrative capacity, through a 10-year programme of renewal.

Alongside improved institutional quality and enhancing state capacity the "new mixed economy" model will also only succeed with clarity in economic policy aims. A key part of this will be setting ambitious development goals for the country. This is an approach that has found considerable success in countries like Singapore, Taiwan and South Korea.[58 59]

Such an approach has long been thought unsuitable for mature industrialised economies. However, it is an approach that continues, overall, to work effectively in advanced economies (such as Singapore) that have the public and private capacity to deliver on them.

The setting out of ambitious but achievable development goals creates a degree of transparency and accountability around economic policymaking. As such, the approach galvanises policy and delivery efforts towards clear outcomes.

Strategic goal – an annual growth ambition

Establish an annual GDP per capita growth ambition (e.g. 1.9% - the average growth rate for the UK between 1961 and 2019) and outline a multi-year plan for the economy, so that by the end of the decade the UK will be averaging GDP per capita growth of 1.9% on a sustained basis.

As part of the system change to a “new social market economy” model, the basis for business taxation needs to be re-cast and based upon a new settlement between business, society and the state, whereby societally desirable activities that are often under-supplied by private actors (because the private benefits that accrue from them are not as great as the social benefits that accumulate) will attract support.[60] These ”desirable activities” include, investing in human capital, expenditure on machinery and equipment, sharing the proceeds of firm growth with employees and increasing rates of innovation. As the SMF put it in a report last year, “corporate tax cuts should be dependent on businesses doing the right thing” - rather than a general expectation.[61] Pro-business should, ultimately, be shorthand for pro-good business.

At the same time, commercial behaviours by business that are detrimental should be discouraged. Extensive re-balancing and simplification of the system would be, in our view, necessarily part of the quid pro quo of re-shaping the system around the “new settlement”. Equally essential are complementary reforms to other taxes that impact businesses and their investment decisions, such as Business Rates.

Strategic goal – a new business tax settlement for state, business and society

Re-cast the foundations of the business tax system in the UK, through a new settlement between the state, business and society that establishes its guiding principles.

Innovation is a key driver of business success and, consequently, in increasing long run prosperity. The environment for business in the “new social market economy” would be calibrated to foster high levels of innovation. The construction of a better “National Innovation System” (NIS) would be integral to the new model. NIS describes the set of actors and institutions (and the associated incentives facing, and competences of, those actors and institutions) within a country that contribute to the creation of technologies and the development and diffusion of “technological learning”.[62]

The reformed NIS would:

- Ensure the UK had leading-edge technological infrastructure in-place.
- Improve the UK’s record in commercialising innovation and capturing more of the economic value that is generated by such innovation.
- Facilitate more effective technological diffusion throughout the economy and society, enabling the business community to take advantage of the availability of better technologies.

The more aggressively interventionist and capable state of the “new social market economy” model would provide the public backing for businesses to innovate, be an active player in the market for technologies and build the networks and institutions needed to support private sector innovation.

Strategic goal – creating a better National Innovation System

Reduce the weaknesses in the UK's existing NIS, through overhauling the innovation eco-system. This will require substantial increases in public and private investment in R&D and policymakers to think in more joined-up ways about how a range of areas – some not typically directly associated with innovation policy – interlink with innovation and where policy and performance need to improve to better support it. These include, among others, education, taxation, industrial and technology policy, procurement, the insolvency framework and devolution. It will also require more effective networks and institutions aimed at helping diffuse technology through the UK economy, utilising public resourcing and other interventions such as the state being a more pro-active participant in the market for technologies.

The new social market economy would limit the commodification of labour and preserve dignity in the workplace. As well as the state providing access to lifelong learning and improved adult education services[63], there is scope for employee ownership to be at the heart of the new economic model, giving workers a genuine stake and say in business – a real third way distinct from state ownership of business (under Butskellism), the LME models tendency to leave a large proportion of the workforce disempowered. Recent SMF research has shown that employee ownership could boost business performance and significantly bolster the financial resilience of UK households.[64]

Strategic goal – broaden ownership of business to establish a share-holding democracy of economic stakeholders.

Establish an Employee Ownership Commission, tasked with developing the necessary institutional support needed to generate wider rates of employee ownership. This includes reviewing business access to support and advice on employee ownership, financial support, marketing of employee ownership and identifying and removing barriers to employee ownership.

Lastly, a pro-business social market economy would aim to make markets more competitive, creating stronger incentives for businesses to innovate, reduce prices and improve the quality of goods and services. Under the LME model, too many markets in the UK are dominated by a small number of large companies. That alone would not be problematic, if these large firms were intensely competing over market share. But often they are not; as the SMF has noted, customer switching rates are low in sectors such as telecoms and banking, undermining the ability of the free market to improve outcomes for customers.[65]

Maintaining this status quo is, in our view, "anti-business" as it limits the ability of new entrants to compete and gain market share. The social market economy model would recognise the numerous instances in which the LME fails to deliver competitive pressures and would explore the role of interventions to introduce such pressures. This includes through technology-based solutions (such as automatic customer switching services)[66] and having local or central government suppliers acting as competitors in markets such as energy.[67]

Strategic goal – make Britain's markets the most competitive in the world

Establish the position of Minister for Competition and Consumers, to ensure competition is prioritised across government and considered by policymakers in all relevant departments and agencies. barriers to employee ownership.

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