

Raising the bar

Business priorities for
industrial strategy one year on



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Foreword



Last year the CBI made the case for a twenty-first century industrial strategy for the UK. We argued that in addition to improving the underlying business environment, the government should adopt a more strategic approach to championing key sectors where the UK has competitive advantage and sees future opportunities for growth.

That case has now been won. Government’s commitment to developing and implementing a long-term industrial strategy in partnership with business last September represented a welcome sea change in approach, and aligned us with other competitor countries.

We now have a once-in-a-generation opportunity to get industrial strategy right. Overall, business is positive about the direction of travel, but clear too that much more work is needed to consolidate and build on the steps that have already been taken.

And we need to raise the bar. Last summer the UK showed the world what it can achieve by delivering the 2012 Olympic Games. That ambition and drive is what we must now harness as we look to rebalance our economy through the implementation of our industrial strategy, positioning us for long-term growth and success in the global economy.

To achieve this we must move further and faster to improve the competitiveness of the overall business environment to ensure the UK stays ahead of its competitors as a place to do business. We must continue to champion key sectors of our economy, refining how we use targeted policy interventions to remove barriers to growth. And as this report highlights specifically, we should now focus in on building stronger supply chains to underpin the success of those key sectors.

We also need a shift in emphasis from words to action. If industrial strategy is to amount to more than just rhetoric and deliver long-term results, it must be viewed as a whole of government priority, not just one for the business department. It must continue to be driven and championed by business. And it must be underpinned by further action to strengthen cross-party consensus and lift the agenda out of the political arena.

One year on, business is now ready and willing to do more.

John Cridland
CBI director-general

Executive summary

Maintaining momentum on industrial strategy is crucial to securing prosperity through private sector growth and positioning UK businesses for long-term success in the global economy. This means moving further and faster to improve the competitiveness of the overall business environment, continuing to champion key sectors of the economy and refining how we use targeted policy interventions to support them, and taking action to build stronger supply chains that underpin those sectors. To deliver this change going forward business and government must focus on implementation to ensure words are translated into practical action.

The CBI’s 2012 report *Playing our strongest hand* argued that action to develop a coherent industrial strategy is needed to bolster investment and strengthen Britain’s global role as a trading nation. One year after government committed to developing such an industrial strategy in partnership with industry, this report provides the CBI’s perspective on the progress made and priorities for the future. It follows a series of CBI policy briefs on the automotive, construction and professional and business services sectors: in the near future we will also produce a sector plan for our world-beating creative industries.

Our research highlighted the need to move further and faster to ensure the UK remains an attractive place to do business. Creating a competitive business environment is at the heart of a successful industrial strategy, but right now companies surveyed by the CBI are divided about whether they think conditions for business will improve or not in the next five years (51% confident, 48% not confident). Going forward we need to benchmark ourselves regularly against international competitors and focus attention on areas where we are falling short – including access to finance and infrastructure quality.

In addition, government must continue to focus on how it uses targeted policy interventions in support of key sectors. Business supported the decision to work with eleven sectors on developing sector strategies and forming sector councils, with a commitment of £1.6bn to support this. There are positive examples of where a more targeted approach is now being employed, especially in backing

innovation and boosting exports. But with 63% of businesses surveyed saying the government is not strategic in how it uses the policy and funding levers at its disposal to underpin UK competitive advantage, it is clear more should be done – especially with regard to procurement, skills, regulation and tax incentives, and encouraging cluster development.

But above all else, targeted action to strengthen the supply chains underpinning key sectors should now be prioritised. If we rise to this challenge and act to boost supply chain capabilities, the benefits for the UK could be significant, with the potential to increase economic value captured here; for example, the offshore wind sector has the potential to capture 60% of the overall value of investment into the sector by 2030, but at the moment only around one third of the contracts secured for new developments come from the UK. Action should be focused on improving understanding of supply chains to help target weaknesses and reinforce strengths, promoting existing initiatives to support supply chain development, and encouraging and incentivising supply chain collaboration.

Finally, with 60% of businesses surveyed by the CBI still unclear about what the UK’s industrial strategy is looking to achieve, we must do more to consolidate this agenda through effective implementation. This requires action to secure buy-in to industrial strategy from across the whole of government, to strengthen cross-party commitment for the agenda and ensure business takes the lead in pushing it forward.

Research methodology

Our analysis and recommendations have been compiled with the assistance of CBI members including CEOs and Vice-Chancellors, and trade associations representing key sectors. We also undertook a short survey to garner wider business reviews. The survey received 193 responses from companies across a range of sectors, including all the eleven industrial strategy sectors.

‘Maintaining momentum on industrial strategy is crucial to securing prosperity through private sector growth and positioning UK businesses for long-term success in the global economy’

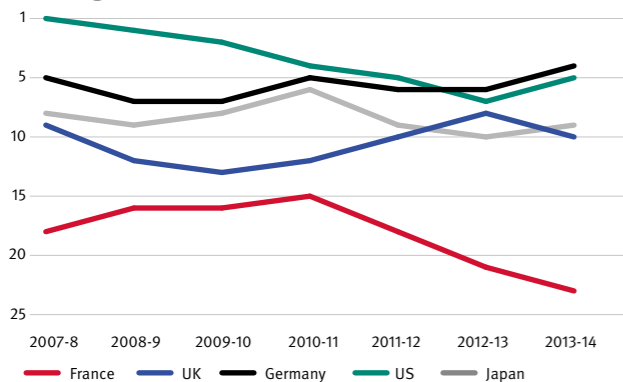
Recommendations

- 1 Government should ensure the UK’s performance on all the key business environment indicators identified by the CBI is assessed as strong or average relative to our competitors by 2020 through regularly benchmarking progress and using this to guide policy and implementation priorities
- 2 Government should reinforce and strengthen use of targeted policy interventions to champion key sectors, focusing in particular on procurement, sector specific skills initiatives, regulation and tax incentives, and encouraging cluster development
- 3 Government should work with sector councils to build up the evidence base on supply chains through supply chain mapping and exploring options for gathering better information on use of local content
- 4 Government should work with sector councils to develop a more targeted approach to attracting inward investment to plug supply chain gaps through UKTI, alongside promoting UK supply chain strengths to inward investors
- 5 Government should commit to funding the Advanced Manufacturing Supply Chain Initiative (AMSCI) for the long-term and focus attention on encouraging greater participation from a wider array of sectors and businesses
- 6 Sector councils and trade associations should work with government on raising awareness of existing support for supply chains and share best practice on sector-specific initiatives
- 7 Government should explore incentives for encouraging greater supply chain collaboration on issues including skills, innovation, access to finance and exporting
- 8 From 2014, the government should include objectives related to industrial strategy in all relevant departmental business plans to improve cross-government delivery of industrial strategy priorities
- 9 All political parties must engage in an active dialogue with business to identify industrial strategy priorities for the next parliament, alongside manifesto commitments to take forward the positive progress made to date
- 10 Business must take ownership of sector council work plans and develop KPIs against which progress can be measured
- 11 Business should consider providing more industry-sponsored secondees to support the work of sector councils and officials in delivering work plans and initiatives

1 Despite progress, we need to move further and faster to ensure the UK business environment remains internationally competitive

In the face of rising global competition from developed and emerging market economies, we need to move further and faster to ensure the UK remains one of the most competitive places in the world for business. Opinion among business is currently split on whether they think the UK business environment will become more attractive in the next five years. Action is therefore needed to reinforce and build on our business environment strengths (eg headline rate of corporation tax) and to address where we lag behind competitor countries (eg access to finance and quality of infrastructure).

Exhibit 1 World Economic Forum competitiveness rankings, 2007/08 to 2013/14



As the CBI argued in its 2012 report *Playing our strongest hand*, creating an attractive business environment is at the heart of a successful and coherent UK industrial strategy. To ensure we continue to make progress, government should commit to regularly benchmarking our performance against key business environment indicators and use this as a basis for guiding policy and implementation priorities to ensure we rise up the global rankings relative to our competitors.

The UK business environment remains competitive, with some positive steps taken to improve our global standing further...

Competitiveness rankings from the World Economic Forum reveal the UK's standing has improved in recent years, but a dip for 2013/14 highlights we cannot afford to be complacent (Exhibit 1).¹

Digging below headline figures, however, it is positive to see data showing we are performing well relative to our competitors on some business environment indicators. This is reflected in a new scorecard developed by the CBI which assesses the UK's performance against key indicators, with a comparable assessment for selected competitor countries provided as context (Exhibit 2).

'...creating an attractive business environment is at the heart of a successful and coherent UK industrial strategy'

Theme	Indicator	UK	France	Germany	US	Japan	World leader
Education and Skills	PISA ranking ³	25	22	20	17	8	Shanghai, China
Research and innovation	Quality of science research institutions ⁴	3	13	6	5	9	Israel
	R&D expenditure, % of GDP ⁵	1.8	2.2	2.9	2.8	3.3	Israel
Infrastructure	Quality of overall infrastructure ⁶	28	6	10	19	14	Switzerland
Energy costs	Industrial electricity prices ⁷	8.5	7.7	9.4	4.2	12.3	US
Tax competitiveness	Headline corporation tax rate, % ⁸	23	33.3	29.6	40	38	Russia, Turkey, Saudi Arabia
	Effective marginal tax rate, % ⁹	22.3	17.9	18.2	23.2	27.0	Italy
Regulatory burden	Burden of government regulation ¹⁰	45	130	56	80	81	Singapore
Access to finance	Ease of access to loans ¹¹	82	41	46	17	33	Qatar
Investment and trade	Openness to trade (trade to GDP ratio), % ¹²	47.2	47.6	75.7	24.8	28.3	Hong Kong

■ Strong performance relative to other countries
 ■ Average performance relative to other countries
 ■ Poor performance relative to other countries

The scorecard has been compiled to reflect key factors determining the attractiveness of the UK's business environment. The data in the scorecard is wide-ranging, drawing on figures from organisations such as the World Economic Forum, World Bank and OECD, with detail on sources set out in the references. It represents a snapshot in time only, based on the latest official figures available.

The CBI's assessment is based on relative performance compared to other countries on key indicators and has been determined according to the following rules:

- For ranked variables, countries are green if they fall in the top ten, yellow if between 11-20 and red for anything above 20
- For all other indicators, the assessment has been made based on where countries sit relative to the mean of the indicator.

On indicators such as businesses taxes and research & innovation the UK is performing well at present. Indeed, where the UK performs best is in the quality of its science and research institutions, where we are ranked third according to the World Economic Forum (WEF).

The indicators are revised on a regular basis and we believe that the government has taken a number of positive steps that should help to push up the UK's performance over time. These include reducing the headline rate of corporation tax, refocusing export support through UKTI, increasing spending on innovation, improving the R&D tax credit and introducing the Patent Box which has been credited with unlocking investment by companies such as GSK (**case study 1**). These actions should help the UK to consolidate its position on tax competitiveness and improve its standing on indicators such as openness to trade.

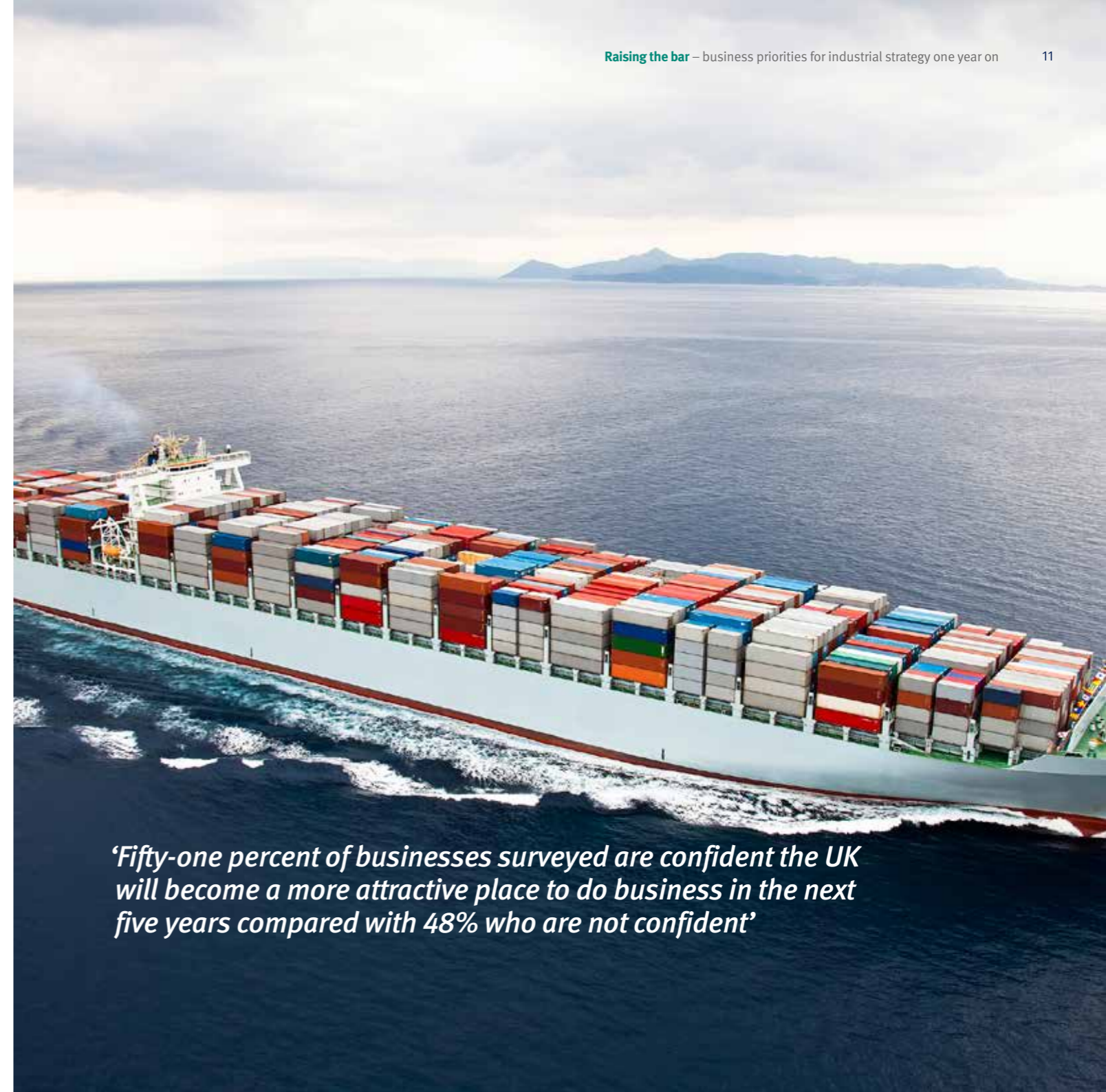
Case study 1 **GSK and the Patent Box**¹³

GSK has credited the introduction of the Patent Box, which applies a 10% corporation tax rate to profits attributed to patents, as having transformed the way it views the UK as a location for new investment. As a result, the company has recently announced a series of more than £500m investments in the UK, creating up to 1000 new jobs in the supply chain.

...but the UK lags behind its competitors on a number of important business environment indicators such as access to finance and infrastructure quality...

While the overall trend in terms of the UK's competitiveness is positive, the scorecard highlights variable performance relative to our competitors on a number of indicators, including access to finance and infrastructure quality. On infrastructure quality, the UK currently ranks behind Saudi Arabia and Barbados, while on access to finance it trails Indonesia and Taiwan.

Even where performance is assessed as good based on official figures, further data paints a more disappointing picture. For example, while the UK's research and knowledge base is strong, the capacity of business to develop and absorb new research and technology is much weaker, while the proportion of the UK's GDP spent on R&D remains below that of Japan, the United States, Germany and France. Where performance is assessed as bad however, it is important to acknowledge that this is a judgement relative to competitors; for example, the PISA rankings we have used to grade our education and skills system (England and Wales only) do not indicate that the overall system is poor, simply that we are not doing as well compared to our key competitors.



'Fifty-one percent of businesses surveyed are confident the UK will become a more attractive place to do business in the next five years compared with 48% who are not confident'

Businesses' views on how they think the UK ranks on key indicators also provides useful colour to this analysis. Data from the CBI's industrial strategy survey revealed that 72% of companies felt the UK was poor or very poor with regard to overall regulatory burden

on business, which chimes with official rankings. That said, it is unsurprising we perform poorly relative to many emerging market economies with less developed regulatory regimes, and should acknowledge that we are now ranked higher than France, the US,

Exhibit 3 Snapshot of CBI policy recommendations aimed at improving the competitiveness of the UK business environment

Education and skills

- Route apprenticeship funding directly through employers and consider the merits of an apprenticeships tax credit run through PAYE
- The Department for Education and Ofsted should require schools to deliver a broader set of educational outcomes, which go beyond the merely academic to include the wider behaviours and attitudes of young people

Infrastructure

- Speed up delivery of the National Infrastructure Plan, prioritising flagship projects such as the A14 expansion, the M4 relief road and improving surface access to airports
- Develop a long-term strategy for digital infrastructure and communications to be overseen by Infrastructure UK

Energy costs

- Enshrine the Energy Bill in law and bring forward secondary legislation to provide businesses with the certainty they need to invest in the energy sector

Tax competitiveness

- Reduce the burden of employer National Insurance Contributions
- Introduce a capital allowance for infrastructure
- Cap business rates at 2%

Regulatory burden

- Maintain and build on the flexibility which makes the UK's labour market competitive, including reform of employment tribunals and modernising the legal framework for industrial relations

Intellectual property

- Ensure the UK has a recognised IP and copyright framework that supports rights holders and which is responsive to the changing nature of the digital economy

Access to finance

- Take action to increase the supply of alternative sources of finance in the UK – in particular, equity investment

Export support

- Introduce a New Markets Incentive – a targeted tax credit to underpin exploratory export activity by SMEs

Japan and Germany, our main developed economy competitors. More problematically however, 45% of companies think the UK is poor or very poor in terms of access to finance, and 80% said the same about energy costs,¹⁴ which are disproportionately impacting energy intensive industries at present.

Disappointingly, government progress in addressing some of these challenges has been lacklustre. Delivery of major infrastructure projects has been too slow and cumbersome, with the UK's complicated planning system acting as a persistent barrier to new developments. Similarly, slow progress on electricity market reform is acting as an impediment to new investment.

Against this backdrop, businesses surveyed by the CBI are currently divided on whether they think the UK is likely to become a more attractive place in which to do business over the next five years with 51% confident or very confident and 48% not confident.

...so action is now required by the government to drive improvement, alongside regular benchmarking of the UK's performance to assess progress and guide priorities

Policy interventions from the government to further improve the UK business environment must now be prioritised. The CBI has worked with its members to develop policies across a range of indicators such as infrastructure, tax competitiveness, regulatory burden and access to finance, which we believe should be actioned as soon as possible to push the UK further up the global rankings (**Exhibit 3**). For example, these include introducing a new markets incentive to support export activity by SMEs, a capital allowance for infrastructure and considering the introduction of an apprenticeships tax credit.

'Policy interventions from the government to further improve the UK business environment must now be prioritised'

As the government takes forward industrial strategy in partnership with business, monitoring the UK's performance against the CBI's key indicators will be important to assess whether progress is being made towards improving the competitiveness of the overall business environment. The CBI believes this exercise should be undertaken on a regular basis and the results used by the government to guide future policy and implementation priorities, with the aim of ensuring that the UK performance is assessed as strong, or at worst, average, relative to our competitors on all measures by 2020.

Recommendation

Government should ensure the UK's performance on all the key business environment indicators identified by the CBI is assessed as strong or average relative to our competitors by 2020 through regularly benchmarking progress and using this to guide policy and implementation priorities

2 To champion key sectors effectively, we need to place a continued focus on use of targeted policy interventions

Government must continue to focus on use of targeted policy interventions to champion the UK's industrial strengths. One year after setting out plans to develop an industrial strategy in partnership with business, some progress has been made in aligning and concentrating action in support of sectors where we have competitive advantage and see strategic opportunities in the future. The government's decision to focus attention on eleven industrial sectors (**Exhibit 4**) – including automotive, offshore wind, and the information economy – and to work with them to develop long-term strategies represents a sea-change in approach. For other sectors, it is also positive that government has committed to providing differing levels of support, with some industries such as chemicals and defence also working closely with BIS and other departments on identifying key priorities.

But while the work undertaken to produce sector strategies has seen commitments to adopting a more targeted approach in some areas such as innovation and exports, 63% of businesses surveyed for this report still said that government is not strategic in how it uses the policy and funding levers at its disposal to underpin UK competitive advantage. This is not about more money for business in the majority of cases, but the way in which funding is prioritised and used, and the extent to which structures and policy interventions align to target support at key strengths. In particular, the CBI believes more could be done to support key sectors through targeted action in areas such as skills, public procurement, tax and regulation and the development of business clusters.

Exhibit 4 The 11 HMG industrial strategy sectors

- Aerospace
- Agri-tech
- Automotive
- Construction
- Education
- Information economy
- Life sciences
- Nuclear
- Oil and gas
- Offshore wind
- Professional and business services

Progress in supporting innovation and exports in key sectors is being made...

While the UK is still early in the process of developing its industrial strategy there are already good examples of where a more targeted approach to championing key sectors is starting to feed through into practical action. This is the case in particular with regard to backing innovation and boosting exports.

'Sixty-three percent of businesses surveyed said that government is not strategic in how its uses policy and funding levers to underpin UK competitive advantage'

'...targeted support for exports from key sectors needs to be placed at the heart of the UK's approach to industrial strategy'

Backing innovation and commercialisation of key technologies

Reflecting CBI calls, in some sectors there is evidence of the government adopting a more strategic approach to backing innovation and commercialisation of key technologies over periods that align with business investment timeframes. For example, a £1bn commitment matched by business for a new Aerospace Technology Institute with funding spread over seven years will further enable the aerospace sector to develop technologies for the next generation aircraft it needs to remain globally competitive.¹⁵ Similarly, a £500m commitment also matched by business for an Advanced Propulsion Centre spread over ten years should help position the UK as a world leader in low-carbon vehicle engine technologies.¹⁶

In addition to funding research into 'eight great technologies', the government has also rightly acknowledged the increasingly important role played by the Technology Strategy Board (TSB) in supporting innovation and commercialisation of technology. For example, support for the information economy, offshore wind, life sciences and agri-tech sectors through the emerging network of TSB funded Catapult Centres has the potential to drive the development and commercialisation of new innovative products and technologies over time in areas such as smart cities, renewable energy, stratified medicine and precision farming. The commitment

of an additional £185m from 2015-16 to help the TSB achieve its mission as called for by the CBI was therefore a welcome development, but the agency's funding levels should be kept under review to ensure it is properly resourced beyond 2016.

Providing targeted support for exports

The CBI's report *The only way is exports* argued that targeted support for exports from key sectors needs to be placed at the heart of the UK's approach to industrial strategy.¹⁷ Further work will be needed over time to realise this ambition, but there are already indications of a positive shift in focus. For example, the professional and business services strategy outlined a commitment to strengthen UKTI support for businesses in the sector to access high growth markets.¹⁸ The education sector strategy also committed to establish a new BIS/UKTI unit – Education UK – to support UK education institutions access £3bn-worth of overseas contract opportunities by 2020.¹⁹ This is a model that has already been used in the healthcare sector and could potentially be adapted to other priority industrial strategy sectors.

...but government should do more in areas such as skills, procurement, tax and regulation and developing business clusters

The government needs to build on its use of targeted policy interventions to reinforce our strengths across sectors. To do this it will be necessary to share best practice, and there is a role for the

newly established Industrial Strategy Council to help encourage and facilitate this. Beyond the progress made in backing innovation and exports in key sectors to date, the CBI believes there is scope for more targeted interventions focused on skills, procurement, tax and regulation, and developing business clusters.

Addressing sector skills shortages

The majority of the sector strategies highlight skills shortages – and especially STEM and higher level skills – as a challenge to competitiveness and growth, with both structural reforms to the skills system and a greater focus on sector-specific initiatives required.

Case study 2 Elutec University Technical College and Ford²¹

Ford is supporting Elutec, a new University Technical College for East London and Essex specializing in engineering, design and technology, which will open in September 2014. Elutec will see Ford employees developing and delivering curriculum modules alongside visits for students to Ford's Dagenham Diesel Centre and the Ford Dunton Technical Centre in Essex, providing students with an insight into the careers available in the automotive sector.

While not a substitute for long-term reform, more can be done to support key industries to access a sustained pipeline of skilled talent in near term. For example, action to better align immigration policy with the needs of the key industrial strategy sectors could help (eg through a more responsive and competitive system which can meet the need for high-level scarce skills – particularly in engineering and specialist areas where there is a shortage). Similarly, the government can encourage and work with sectors to ensure more companies take advantage of existing mechanisms that can help business to address skills shortages. The UKCES Employer Ownership of Skills Pilots are starting to enable a more targeted approach to addressing sector skills challenges, with £67m funding awarded to 34 successful business bids in the scheme's first round.²⁰ University Technical Colleges also present a good opportunity for companies in key sectors to shape the type of vocational and technical education provided to 14-19 students, as the example of Ford supporting a UTC in East London demonstrates (**case study 2**).

To underpin a truly demand-led skills system however, government and business must devise a simpler skills funding system that empowers employers to bring in provision directly addressing their needs. As the recent CBI report *Tomorrow's growth: new routes to*

'...success in developing thriving clusters depends on local decision-makers targeting support at sectors and activities where a locality has competitive strength'

higher skills highlights, action to develop the market in higher skills provision through better collaboration between businesses and higher education on 'learn-while-you-earn' courses could help to meet demand in key sectors.²² Government can also work more strategically with sectors on both careers advice and boosting uptake of STEM subjects by young people, both of these themes highlighted in a number of sector strategies.

Driving innovation through public procurement

The government procures £227bn on goods and services each year and needs to ensure that it is using this effectively to drive innovation.²³ Across a number of sectors, the publication of long-term procurement pipelines has been a welcome development, providing companies with greater visibility of future contract opportunities.²⁴ But in many cases there is only limited detail available. At this point, it is also too early to evaluate whether they are having the desired impact on business investment decisions.

But more can be done to use public procurement as a tool to stimulate business confidence and spur innovation. For example, the construction sector has highlighted the potential to be more ambitious in this regard, focusing on the specification of bid criteria to promote more innovation by industry, and providing clearer guidance on how whole life costs are taken into account in value for money considerations.

Overall, to ensure the UK's approach to public procurement is consistent with the wider industrial strategy aims, Government should take advantage of the new EU procurement regulations as they are transposed into UK law to simplify existing procedures and to encourage more cost-effective public procurement which fosters innovation in industry.

Addressing regulatory barriers and employing targeted tax changes

Businesses in key sectors have highlighted the need to focus greater attention on ensuring their activities are not impeded by excessive or poor quality sector-specific regulation. For example, the professional and business services sector has highlighted concerns around the regulatory burden impacting on the sector as a whole, and selected sub-sectors such as legal services.

On a more positive note, over the last year targeted tax changes have been introduced by the government to the benefit of selected sectors such as automotive and the creative industries (**Exhibit 5, page 18**). There is potential to undertake more of this type of activity however, where it can be shown to encourage investment and nurture competitive advantage.

Exhibit 5 Examples of targeted tax changes

- While not identified as an industrial strategy sector by the government, various sub-sectors which make up the UK's creative industries now benefit from a 25% tax relief introduced from April this year. Presently, these tax-breaks apply to film, animation and high-end television programmes produced in Britain
- The introduction of two new company car tax (CCT) bands from 2015 will help to stimulate the market for ultra-low emissions vehicles. In future, CCT rates will also be announced three years in advance giving more long-term certainty to industry.

Developing business clusters

The benefits associated with developing business clusters has been highlighted in a number of sector strategies, including automotive and offshore wind. As the CBI and recent interim findings of the review into universities and growth by Andrew Witty²⁵ have both argued, success in developing thriving clusters depends on local decision-makers targeting support at sectors and activities where a locality has competitive strength.

To be effective this necessitates close collaboration between Local Enterprise Partnerships (LEPs), universities, businesses and other local partners.

If the UK is to foster effective clusters, central government will also need to play a role in aligning national industrial strategy priorities with incentives that exist to encourage local economic development. For example, government can encourage LEPs to collaborate with local partners as they develop bids to secure funding from the new Local Growth Fund. It will also need to maintain sufficient oversight of LEP priorities to avoid duplication of effort in supporting sectors at a local level.

Recommendation

Government should reinforce and strengthen use of targeted policy interventions to champion key sectors, focusing in particular on procurement, sector specific skills initiatives, regulation and tax incentives, and encouraging cluster development

3 To increase economic value captured in the UK, we need to build stronger supply chains

As the UK progresses its industrial strategy, action to strengthen the supply chains underpinning our strongest industrial sectors should be prioritised. The potential benefits of boosting supply chain competitiveness and capabilities are significant, helping us to capture more value from investments at home, as well as ensuring more UK content is included in the products and services that are exported overseas. For example, the offshore wind supply chain has the potential to capture 60% of the overall value of investment into the sector by 2030,²⁶ but at the moment only around one third of the contracts secured for new developments come from the UK.²⁷

To capitalise on opportunities for growth, government and business must focus on improving their understanding of supply chains and the capabilities of UK suppliers, using this information to reinforce strengths and address weaknesses. Existing government support schemes for supply chain development must also be promoted to a wider array of industries and businesses to improve take up, while greater supply chain collaboration on issues such as skills, innovation, access to finance and exporting should be actively encouraged and incentivised.

Focusing on key sectors has highlighted the importance of strong supply chains to the competitiveness of UK industry...

A number of the sector strategies have highlighted the importance of supply chains to their long-term competitiveness. These findings have been reinforced by our survey; 78% of businesses that

responded identified supply chain development as important or very important to the long-term growth prospects of their sector.

Indeed, supply chains are a critical component of the UK's industrial ecosystem, providing a secure, responsive resource for companies, and making the UK an attractive place for global businesses to base their operations. They are often highly complex networks comprising small, medium and large suppliers, manufacturers, and retailers, involved in the production, handling and distribution of a particular product. In this respect, the CBI has been a consistent champion of the UK's medium-sized companies, which form a critical part of many supply chains, arguing that action to unblock the growth potential of these firms could deliver an additional £20bn to the UK economy by 2020.²⁸

While supply chains are structured differently across sectors, it has become clear that adapting a narrow sectoral focus to supply chain development is insufficient due to the interconnectedness of industries. To illustrate this, there are many manufacturing supply chain companies that provide components to both the automotive and aerospace sectors, such as GKN, the UK-based global engineering group, while Sheffield Forgemasters supplies components to the oil and gas, nuclear and offshore wind sectors.

Similarly, companies in 'foundation sectors' – including chemicals, steel and electronics – are also constituents of supply chains in a broad range of high value sectors. For example, Tata Steel produces steel for companies in the automotive, oil & gas, nuclear, offshore

‘The potential benefits of boosting supply chain competitiveness and capabilities are significant’

wind and construction sectors. Therefore, ensuring that UK foundation sectors remain competitive will have a positive impact throughout the supply chains of the priority industrial strategy sectors they serve.

...but UK supply chains face significant challenges

Over the past few decades, persistently strong sterling and low production costs in developing economies have had the effect of weakening UK supply chains, with a detrimental impact on the competitiveness of some of our key industries.²⁹ There will always be a degree of import dependency as some countries will be able to produce inputs needed by domestic producers more efficiently. But supply chains underpinning our key sectors face several challenges, which mean they are not as well positioned to secure as much business at home and overseas as they potentially could be.

The CBI has identified a number of recurring themes and common weaknesses impacting supply chains across sectors, such as skills, innovation and technology, access to finance and transparency. These themes are consistent with those identified in the eleven sector strategies and addressed in the previous chapter, but each theme manifests itself into sector-specific supply chain challenges which require focused and targeted action (**Exhibit 6, page 21**):

Skills: Many suppliers struggle to access the skills they need, and particularly high level and niche technical skills. For example, there is an insufficient pipeline of skilled workers in the UK automotive sector to support a growing, increasingly technology-focused industry. Similarly, many small and medium-sized businesses lack the management capabilities and skills needed to upscale their operations and to explore new markets.

Innovation and technology: UK suppliers lower down the supply chain are often not willing or able to advance their technology. For example, work through the Aerospace Growth Partnership has highlighted the need for UK suppliers to engage earlier in the product development process or risk losing out on opportunities to foreign competitors.³⁰

Access to finance: Some suppliers face difficulties in accessing the financial capital they need to respond to increasing demand, harming overall productivity in the supply chain. A good example is the UK offshore wind sector, where a problem in accessing finance hinders the ability of suppliers to scale up to satisfy demand.

‘Seventy-eight percent of businesses identified supply chain development as important or very important to the growth prospects of their sector’

Exhibit 6 Supply chain challenges in selected industrial strategy sectors

Aerospace ³¹	UK suppliers not effective at incorporating new products and technology improvements Lack of visibility in supply chain beyond immediate suppliers Shortage of skilled engineers and low levels of industry investment in skills and training
Automotive ³²	Some key capabilities and capacity no longer available in the UK – particular shortage of UK-based tier one automotive suppliers Skilled employees needed to replace retiring workers – expected replacement demand of 48,000 new jobs between 2010 and 2020 Restricted access to finance – particularly tooling finance – constraining supply chain growth
Construction ³³	Collaboration in the UK supply chain is low and has led to fractures between construction design and management Low levels of innovation, particularly investment in R&D, inefficient processes, and limited knowledge sharing and technology transfer
Life sciences ³⁴	SMEs struggle to secure financing for R&D and as a result find it hard to develop and commercialise medical innovation in the UK Smaller firms lack business and management skills
Offshore wind ³⁵	Shortage of tier one equipment suppliers – particularly turbine manufacturers – based in the UK Technology deployment low preventing full utilisation of R&D capability Problems accessing finance hinders ability of UK supply chain to scale up quickly to meet demand Engineering and managerial skills gaps
Oil & gas ³⁶	Relatively low levels of investment in R&D and engagement with UK academia to develop and commercialise new technologies Enhanced global competition has resulted in skills shortages, particularly in smaller companies Supply chain firms required to post a performance bond after being awarded a large contract, as a guarantee work will be delivered as agreed
Nuclear ³⁷	Investment in new capability and capacity difficult to finance through conventional market instruments High average age of existing nuclear workforce likely to result in more skills gaps developing over the coming decade

Exhibit 7 Examples of supply chain growth opportunities

Aerospace	The civil aerospace sector is forecast to grow strongly, generating opportunities worth billions of pounds for UK suppliers. Global forecasts for the period to 2031 estimate a requirement for over 27,000 new passenger aircraft worth circa \$3.7tn, 24,000 business jets worth \$648bn and 40,000 helicopters worth \$165bn. ⁴¹
Automotive	80% of the component types for vehicle assembly operations could be procured from domestic suppliers, amounting to £3bn worth of unfulfilled opportunities for the UK supply chain. At present only 36% of the proportion of content in the UK vehicle supply chain is sourced from domestic businesses. ⁴²
Offshore wind	The UK offshore wind supply chain has the potential to capture around 60% of the overall value of investment in the sector over the period to 2030 – supporting 41,000 jobs. ⁴³ At present however, companies based here are only securing about one third of the contracts to supply components, build and install new UK offshore wind developments. ⁴⁴
Nuclear	The nuclear supply chain has the potential to capture £25bn (44%) of expenditure on new build projects to 2030 and a sizeable chunk of overseas business as well. ⁴⁵ The construction of a new plant at Hinkley Point could see up to 57% of the contracts associated with its construction going to UK suppliers. ⁴⁶

Fragmentation: Some UK supply chains suffer from fragmentation. For example, while there are some large businesses in the UK construction sector, the majority of firms employ less than ten people and 37% of contracting jobs are self-employed.³⁸ CBI analysis of the sector identified fragmentation of different elements of the supply chain as one of the key barriers to innovation and collaboration on the use of new technologies. Similarly, the fragmented structure of the agriculture industry is a barrier to uptake of scientific research, with farm businesses not taking the opportunity to explore commercial application of new R&D technology.³⁹

Lack of transparency: Lack of transparency along supply chains can also be problematic, as is the case in the UK aerospace sector. This is partly explained by the complexity of the industry, where each sale of an aircraft powered by Rolls-Royce engines currently supports approximately 3,000 companies in the supply chain.⁴⁰ Nonetheless, larger companies that don't have a clear view of their supply chain below immediate suppliers risk not having a full appreciation of the risks they may be exposed to.

The opportunities for growth in supply chains are significant...

If targeted action is taken to address supply chain weaknesses and reinforce strengths, the opportunities for growth are significant. As the examples from the aerospace, automotive, offshore wind and nuclear sectors highlight, the scale of unfulfilled potential and the size of the prize are both enormous (**Exhibit 7**). In automotive alone, analysis from the Automotive Council has uncovered £3bn worth of unfulfilled growth opportunities for UK suppliers, estimating that total spend in the UK could increase from £11bn in 2011 to £21.5bn in 2016.⁴⁷

The potential spill over impact on jobs in related manufacturing, enabling and foundation sectors could be substantial, alongside increased demand for products and services from other sectors. For example, it has been estimated that should the UK nuclear supply chain secure 44% of the contracts awarded as part of the new nuclear build programme, the indirect multiplier effects could result in total Gross Value Added (GVA) of almost £28bn to the UK economy as a whole.⁴⁸

Recent global trends in manufacturing also suggest some companies may be looking to repatriate supply chains to the UK that have drifted to lower cost economies. While evidence on re-shoring is mainly anecdotal at present there are high profile examples to point to. For example, John Lewis recently announced it is looking to repatriate textile manufacturing to the UK from foreign factories, with a target to increase sales of UK products by at least 15% by 2015.⁴⁹

Potential explanations for any emerging trend of supply chain repatriation include rising labour, energy and transport costs in emerging markets such as China, as well as greater concern from businesses about quality control and supply chain risks and responsiveness. Indeed, a recent study estimates that the trend towards re-shoring could see manufacturing employment in the UK increase by as much as 100-200,000 over the next decade alone.⁵⁰ As a result, there could be significant benefits in terms of UK jobs and growth if government and business can capitalise on this trend and encourage supply chain repatriation through targeted policy and funding interventions.

Business and government both have a role in boosting UK supply chains

To boost capabilities of domestic supply chains both business and government need to act. One year into the industrial strategy programme, further work on supply chains is now required, and as a starting point, the CBI believes attention should be focused on three core areas:

1 Improving understanding of supply chains to help target weaknesses and reinforce strengths

There is an urgent need to build a better understanding of supply chain dynamics and structure within and across different sectors. Supply chain mapping – while often challenging – can be a useful tool for highlighting strengths and identifying weaknesses in the supplier base. The Automotive Council has already attempted to map the automotive supply chain in the UK, while the new oil and gas sector council has committed to doing the same. There are also good examples of where individual companies or groups of companies are developing supply chain mapping tools that others could learn from. For example, Toyota Motor Europe is developing a supply chain mapping tool to provide a comprehensive database of supplier location and function (**case study 3, page 24**).

Government and business should also explore how to build up a more detailed understanding of the use of local content in the delivery and on-going maintenance of major industrial and construction projects. For example, in the offshore wind sector Government is looking for developers to produce a supply chain plan. While the process is still to be developed it is likely they will need to set out how a development project will encourage a diverse supply chain and support innovation and skills development.

In addition, more information on use of local content in different sectors could be useful for identifying where UK suppliers are currently uncompetitive and the steps that need to be taken to

Case study 3 **Toyota Motor Europe and supply chain mapping**⁵¹

A Supply Chain Mapping (SCM) tool is being developed by Toyota Motor Europe with the aim to create a new online automotive community that will become an industry standard. Jaguar Land Rover and Aston Martin are also involved in the project while other OEMs are watching with interest. The tool aims to provide a complete database of supplier location and function, using data gathered from the OEMs about their suppliers. Tier 1 suppliers are then invited to provide information about their supply chains to build up a more detailed map of second and third tier suppliers. Potential benefits to Toyota include early visibility of financial and environmental risks to production, enabling joint proactive planning with suppliers to mitigate the risks of any potential incident

ensure they are best positioned to win business in the future. The challenge however, is to ensure that the costs to business associated with collating such information do not outweigh the benefits.

Building up the evidence base will help to inform how Government and business can be more targeted in the interventions they make to support supply chain development. In particular, the CBI believes this could help inform a more strategic approach from UKTI to plugging supply chain gaps through inward investment into key

sectors where it is realistic and competitive for production to take place in the UK. The new offshore wind and automotive inward investment organisations are positive examples of where this approach is being trialled, with both these organisations looking to sell the UK as a place to invest for key suppliers. Concurrently, there is a role for UKTI to be more strategic in packaging up the strengths of our supplier base, where they exist, and promoting them overseas to attract major investments.

Recommendation

Government should work with sector councils to build up the evidence base on supply chains through supply chain mapping and exploring options for gathering better information on use of local content

Recommendation

Government should work with sector councils to develop a more targeted approach to attracting inward investment to plug supply chain gaps through UKTI, alongside promoting UK supply chain strengths to inward investors

‘Supply chain mapping...can be a useful tool for highlighting strengths and weaknesses in the supplier base’

2 **Promoting existing initiatives to support supply chain development**

Action is also needed to raise awareness of existing schemes which can strengthen supplier competitiveness, including the Regional Growth Fund, Advanced Manufacturing Supply Chain Initiative (AMSCI), Technology Strategy Board and UK Export Finance. In particular, awareness among small and medium-sized supply chain companies about what is currently on offer is not as good as it could be. For example, 69% of SME exporters are unaware of UKTI and two thirds of medium-sized firms are unaware of UK Export Finance.⁵²

Improved promotion and awareness-raising should be accompanied by the continuation and expansion of schemes providing valuable support for UK supply chain development. In particular, the government should promote and build on the success of AMSCI, which is adopting a flexible approach to addressing barriers to supply chain growth. The scheme is well regarded by businesses who have participated, providing grants and loans to support research and development, skills training and capital investment. It’s also a vehicle by which government can encourage new suppliers and foreign investors to establish or strengthen their presence in the UK. Going forward, particular focus should be placed on encouraging participation from a wider selection of industries and companies than at present so that support extends to other high-value sectors.

Case study 4 **GROW: Offshore Wind**⁵³

GROW: Offshore Wind is a new service funded by the Regional Growth Fund and provided by the Manufacturing Advisory Service in collaboration with partners including Grant Thornton and Renewable UK, focused on supporting small businesses in the supply chain to increase their capacity and new players to enter it. The service will provide technical and commercial advice around how to gain business in the growing offshore wind market. This could include support to access finance, with project and business planning or advice on positioning to win contracts.

Business would also like to see the scheme placed on a more permanent footing, with a longer-term funding commitment. Up to £125m funding was available in AMSCI Rounds 1 and 2 and an additional funding of £120m was announced in the 2012 autumn statement for a further two competitions, but there is a strong argument to increase the funding available, and to extend this support beyond the current Parliament.

Finally, more can be done to promote sector-specific initiatives with businesses, as well as share best practice across sectors. Sector strategies which have committed to developing and promoting a number of supply chain initiatives could provide useful lessons and actions for other sectors to replicate. Examples include the Offshore Wind Supply Chain Growth Programme (GROW), which is providing technical and commercial advice to small businesses in the supply chain to help increase their chances of securing contracts for new offshore wind development projects (**case study 4**).

‘Sixty-nine percent of SME exporters are unaware of UKTI and two thirds of medium-sized firms are unaware of UK Export Finance’

Recommendation

Government should commit to funding the Advanced Manufacturing Supply Chain Initiative (AMSCI) for the long-term and focus attention on encouraging greater participation from a wider array of sectors and businesses

Recommendation

Sector councils and trade associations should work with government on raising awareness of existing support for supply chains and sharing best practice on sector-specific initiatives

3 Encouraging and incentivising greater supply chain collaboration

Action should also be taken to encourage and incentivise greater collaboration between larger companies and their suppliers in areas such as skills, innovation, access to finance and exports. For example, the recently published Next Manufacturing Revolution report argues that in manufacturing sectors, improved supply chain collaboration, particularly on technology development and resource efficiency, could play a part in delivering significant efficiencies that have the potential to create 300,000 new UK manufacturing jobs and a 24% reduction in CO2 emissions.⁵⁴

Large companies have a particularly important role to play in managing and shaping their supplier base, partnering with suppliers to bring their products through to market, ordering ahead of production to ease cashflow and by giving their supply chains long-term visibility of future commercial opportunities. As the example of Skanska working with suppliers demonstrates, there are positive examples of supply chain collaboration already happening, in other areas such as sustainability (**case study 5**).

Greater collaboration and information sharing between small and medium-sized suppliers can also make a difference. The CBI’s work on medium-sized businesses has highlighted the benefits

Case study 5 Skanska and the Supply Chain Sustainability School⁵⁵

A Supply Chain Sustainability School has been founded by Skanska in partnership with Kier, Lend Lease, Morgan Sindall, Sir Robert McAlpine, Willmott Dixon. and Aggregate Industries, and supported by funding from CITB-ConstructionSkills. The school provides construction suppliers and subcontractors with free support and practical advice on how to improve their knowledge of sustainability practices. The school has plans to reach 80% of the UK supply chain over the next five years, leading to improved performance in sustainability across the whole of the construction sector in the UK.

associated with peer-to-peer knowledge sharing and prompted the establishment of a network of ‘M-Clubs’, which allow medium-sized companies to network, share experiences and receive expert advice on how to maximise their role in supply chains and fulfil their prospects for business growth.

In addition to promoting and sharing best practice, government should also work closely with business to explore what incentives could be introduced to drive further collaboration across UK supply chains in a range of areas. One such area is access to finance, which is critical for helping foster further supply chain development. Corporate balance sheets should not be seen as a panacea to the access to finance challenge for small and medium-sized companies – such collaboration only works when it is a sound investment for the large and smaller firm – but to see if there is scope to do more here, the CBI is exploring what incentives, if any, can be used to increase collaboration on access to finance within supply chains, looking in particular at supply chain finance and corporate venturing.

‘Large companies have a particularly important role to play in managing and shaping their supplier base’

Recommendation

Government should explore incentives for encouraging greater supply chain collaboration on issues including skills, innovation, access to finance and exporting



‘The real test will be whether the UK’s approach to industrial strategy adds up to more than the sum of its parts’

4 Government and business must work together effectively to cement the UK’s industrial strategy over the long term

One year on, business and government must now maintain momentum on industrial strategy in order to deliver lasting change, building on the commitments that both sides have made since the launch in September 2012. This means government taking bold steps to realise an effective cross-government approach to delivery, and business and sector councils improving their ability to drive forward implementation of policy actions and initiatives. To secure wider buy in from across the business community, action is also needed to further strengthen the political consensus on industrial strategy so companies can engage with the agenda safe in the knowledge that there is a commitment to it which spans the political cycle.

Early signs suggest we’re moving in the right direction, but the real test will be whether the UK’s approach to industrial strategy adds up to more than the sum of its parts and is delivered as a coherent package over a sustained period of time. With 60% of businesses surveyed by the CBI stating that they were unsure about what UK industrial strategy is seeking to achieve, further work is needed by the government partnering with business to translate shared goals into practical reality.

Action to secure whole of government buy-in and strengthen political consensus on industrial strategy is critical

As the CBI argued in its 2012 report *Playing our strongest hand*, for a UK industrial strategy to deliver for business over the long term, a whole-of-government approach to implementation with buy-in from all relevant departments and agencies is a prerequisite. Policies and funding decisions made about energy, infrastructure, skills, and competition or related to specific sectors and technologies need to reinforce and complement each other. At the moment this is not always the case.

Indeed, businesses from across a range of sectors continue to report frustration that government departments are not sufficiently joined up and continue to pursue policies in isolation. During the interviews conducted when researching this report, many business leaders expressed the view that while a renewed focus on industrial strategy is welcome and long overdue, it has felt so far like a Department for Business, Innovation and Skills (BIS) project rather than a whole-of-government agenda.

For example, the Aerospace Industrial Strategy, which on the whole was a successful partnership between industry and government, was characterised by considerable wrangling between BIS and HM Treasury right up to the last minute on funding commitments. While business does not underestimate the scale of the challenge involved in delivering more effective cross-government

‘Sixty percent of businesses surveyed stated that they were unsure about what a UK industrial strategy is seeking to achieve’

coordination of policies, taking action to enable a more joined up approach is paramount, both to ensure consistent implementation of industrial strategy across departments, and to bolster business confidence in the capacity of the industrial strategy programme to deliver for them.

In this regard, the newly-established Industrial Strategy Council can play an important role in holding government and business to account on overall coordination and implementation. Co-chaired by business secretary Vince Cable and the chancellor of Warwick University, Richard Lambert, the council brings together ministers, senior civil servants, business chairs of the sector councils, as well as the CBI and the TUC. To improve the overall coordination of policies and activities across government departments, there is a strong case for the council to include representatives from HM Treasury, the Foreign and Commonwealth Office, the Department for Energy and Climate Change and other relevant departments.

To encourage a truly whole of government approach however, departments also need to be incentivised to align their activities with wider industrial strategy priorities. From next year, specific objectives written into departmental business plans to support industrial strategy would be a good way to start doing this (eg around specific policies, championing sector priorities or nurturing a particular technology). This should help to drive cross-government coordination and delivery, with ministers held firmly to account for their departments’ performance each year.

Political consensus is also crucial to improving business confidence in the ability of the industrial strategy to establish a long-term framework for securing private sector growth in the UK. A consensus is starting to emerge, but business will be looking for commitment from the main political parties in their upcoming election manifestos to build on the industrial strategy structures and initiatives that have been established in this parliament. Industrial strategy should be taken out of the political cycle to the extent that this is possible, with cross-party agreement on the overall direction of travel and the long-term priorities for key sectors that have been identified through engagement with business.

Recommendation

From 2014, the Government should include objectives related to industrial strategy in all relevant departmental business plans to improve cross-government delivery of industrial strategy priorities

Recommendation

All political parties must engage in an active dialogue with business to identify industrial strategy priorities for the next parliament, alongside manifesto commitments to take forward the positive progress made to date

Business also needs to up its game and focus unremittingly on delivery

Business must also play a leading role in driving the industrial strategy agenda forward, working on a cross-party basis to identify industrial strategy priorities for the next parliament and securing commitment to delivery from political parties in Westminster and the devolved administrations. This is especially important for the eleven sectors that have worked in partnership with Government to develop sector strategies and are committed to delivering specific long-term actions.

Some sectors such as the aerospace and automotive sectors already have well-established sector councils and strong relationships with government that predated the decision to develop an industrial strategy. The key lessons from these sectors are that partnerships with government should develop organically and from the bottom up to secure the necessary buy in from across business. This can take time to achieve. Firms also need to grow the confidence to engage openly with government officials and each other – even where they are competitors – about the major long-term challenges they are facing as a sector and how they can be addressed.

Many of the eleven priority sectors are only just starting out on this journey and this difference in maturity is reflected in the nature and content of the various sector strategies. Where partnerships

between business and government were not well established, the result tended to be a more prescriptive approach with less business oversight of the strategy as it was developed.

Strengthening sectoral leadership and ambition in these sectors will therefore be crucial to driving effective implementation going forward. The importance of this is exemplified by the 90% of businesses responding to our survey, who identified sector leadership as important or very important for the future growth and competitiveness of their sector in the UK.

While the formation of sector councils is an important step towards delivering more effective sector leadership and ambition, they should not be viewed merely as an end in themselves. As strategies are implemented, individual sectors need to establish the objectives, goals and an approach taken to these councils that works most effectively for them. No one template should be readily applied.

Business also needs to ensure it sets the priorities of sector councils, and takes responsibility for driving them forward and identifying new issues to address in the future. To guide this, each sector council should flesh out key performance indicators (KPIs) as a priority against which progress can be measured on a regular basis, building on the actions and basic KPIs set out in sector strategies.

‘Ninety percent of businesses surveyed identified sector leadership as important or very important for the future growth and competitiveness of their sector’

Furthermore, in both the automotive and aerospace sectors, use of industry-sponsored secondees into BIS have proven effective in helping to drive forward the sector’s priorities. They can act as a conduit between government officials and business, helping to drive forward agreed policy actions and initiatives. As work plans and KPIs are developed, other sectors should also consider whether committing similar resource might be useful.

Finally, with a general election due in 2015, business also needs to be at the forefront in making the public case for industrial strategy, being clear about its priorities, and areas that require attention to ensure that momentum is maintained over the long term. The CBI will do its part here, continuing to promote the need for industrial strategy and holding both government and business to account for delivery of an agenda that is crucial to the UK’s long-term prospects for balanced, sustainable growth.

Recommendation

Business must take ownership of sector council work plans and develop KPIs against which progress can be measured

Recommendation

Business should consider providing more industry-sponsored secondees to support the work of sector councils and officials in delivering work plans and initiatives

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September 2013
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