

Investing in Prosperity – Launch of the LSE Growth Commission Report

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Professor Craig Calhoun

Chair, LSE

LSE events Suggested hashtag for Twitter users: **#LSEgrowth**





Growth
Commission



Philippe Aghion
Tim Besley
John Browne
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Chris Pissarides
Nick Stern
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Investing for Prosperity

Skills, Infrastructure and Innovation
Report of the LSE Growth Commission

in partnership with

**INSTITUTE
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CENTRE for ECONOMIC
PERFORMANCE

**Twitter
Hashtag
#lsegc**

THANKS TO OUR FUNDERS....



Knowledge
Exchange
HEIF 5

SET UP (IN JAN 2012)

IN PARTNERSHIP WITH THE INSTITUTE FOR GOVERNMENT

- Co-Chairs Tim Besley & John Van Reenen
- Financed by HEIF 5 and ESRC
- Commissioners:
 - Philippe Aghion
 - Lord John Browne
 - Francesco Caselli
 - Sir Richard Lambert
 - Rachel Lomax
 - Lord Nick Stern
 - Nobel Laureate Chris Pissarides



WHY AN LSE GROWTH COMMISSION?

- Focus on long-term structural issues beyond debates about austerity
- Numerous reports on growth
- Focus on evidence (report short but “feeder” reports in detail on website)
- Commissioner background: academics from UK and overseas, but also business & policy-makers
- Political economy: why things have not been fixed before? What institutions could be built to last?

NO STONE UNTURNED



GROWTH



British Chambers of Commerce

THE CASE FOR A BRITISH BUSINESS BANK
SEPTEMBER 2012

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Dr. Keith Marshall
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BUSINESS
GOOD FOR
BRITAIN

INTRODUCTION & SUMMARY

- **Optimistic story, UK has many assets**
 - Rule of law, flexible labour market, competition, universities, openness
 - Reversal of relative decline in last 3 decades
- **...But deficits**
 - Policy instability
 - Growth not inclusive: Inequality
- **Leads to failure of long-term investment**
 - Human capital (especially bottom third)
 - Infrastructure (especially transport & energy)
 - Private investment & Innovation
 - Low productivity
- **Wanted: A Manifesto for Growth**

MODUS OPERANDI

- Commissioner Meetings
- Evidence sessions
- Written Evidence
- Background documents
- Report
- Follow on ...?

INTRODUCTION & SUMMARY

- **Human Capital**
 - Improve teaching through freer entry & more exit
 - Flexible ecology to deepen academy system
 - Reduce disadvantage by information, inspection
- **Infrastructure**
 - New institutional architecture of Infrastructure Strategy Board, Infrastructure Planning Commission & Infrastructure Bank
- **Investment & Innovation**
 - Increase retail banking competition
 - Business Bank

The Economic Story of the UK

Human Capital

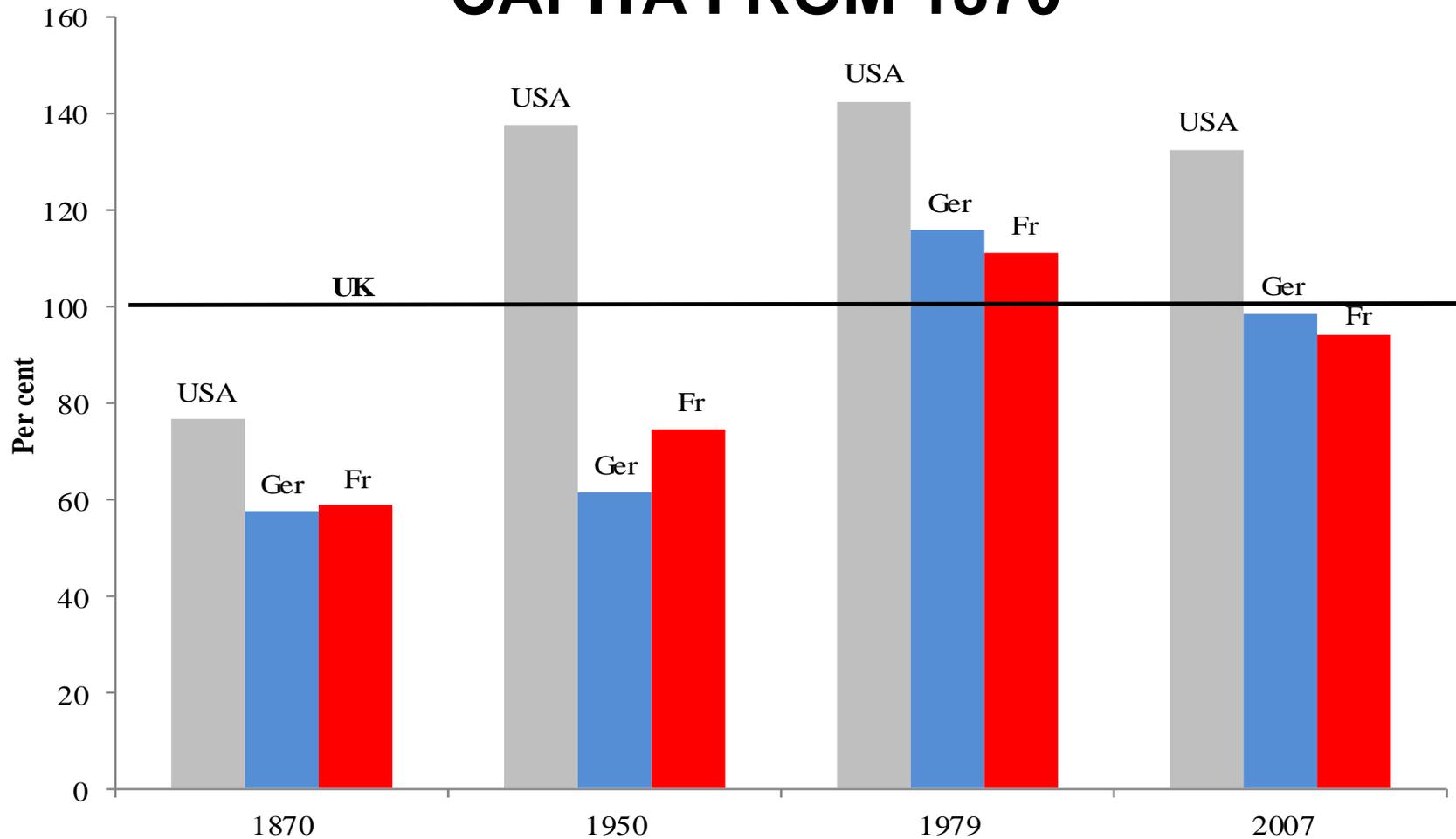
Infrastructure

Innovation & investment

Measuring Progress

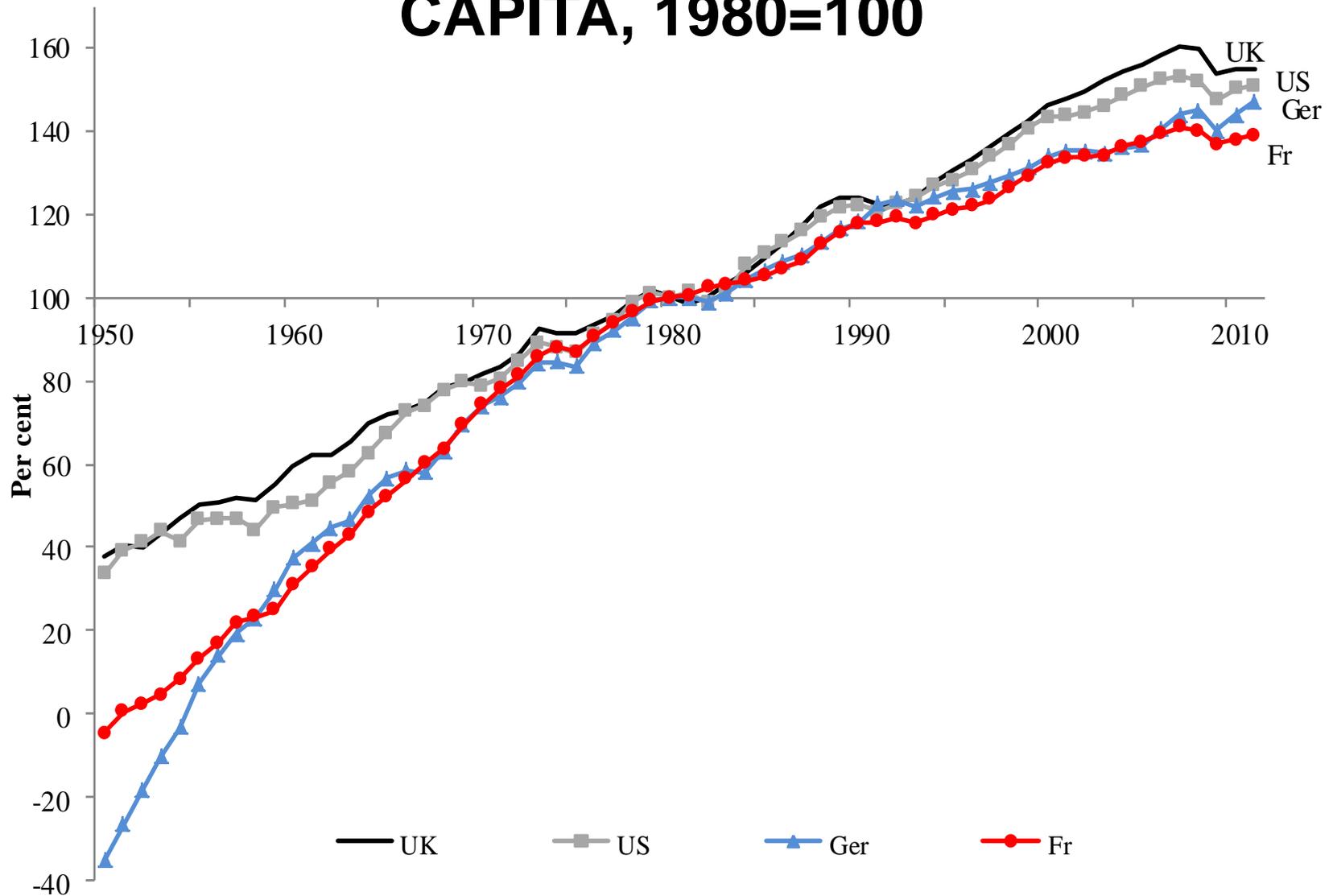
Conclusions

DECLINE AND REBOUND: RELATIVE GDP PER CAPITA FROM 1870



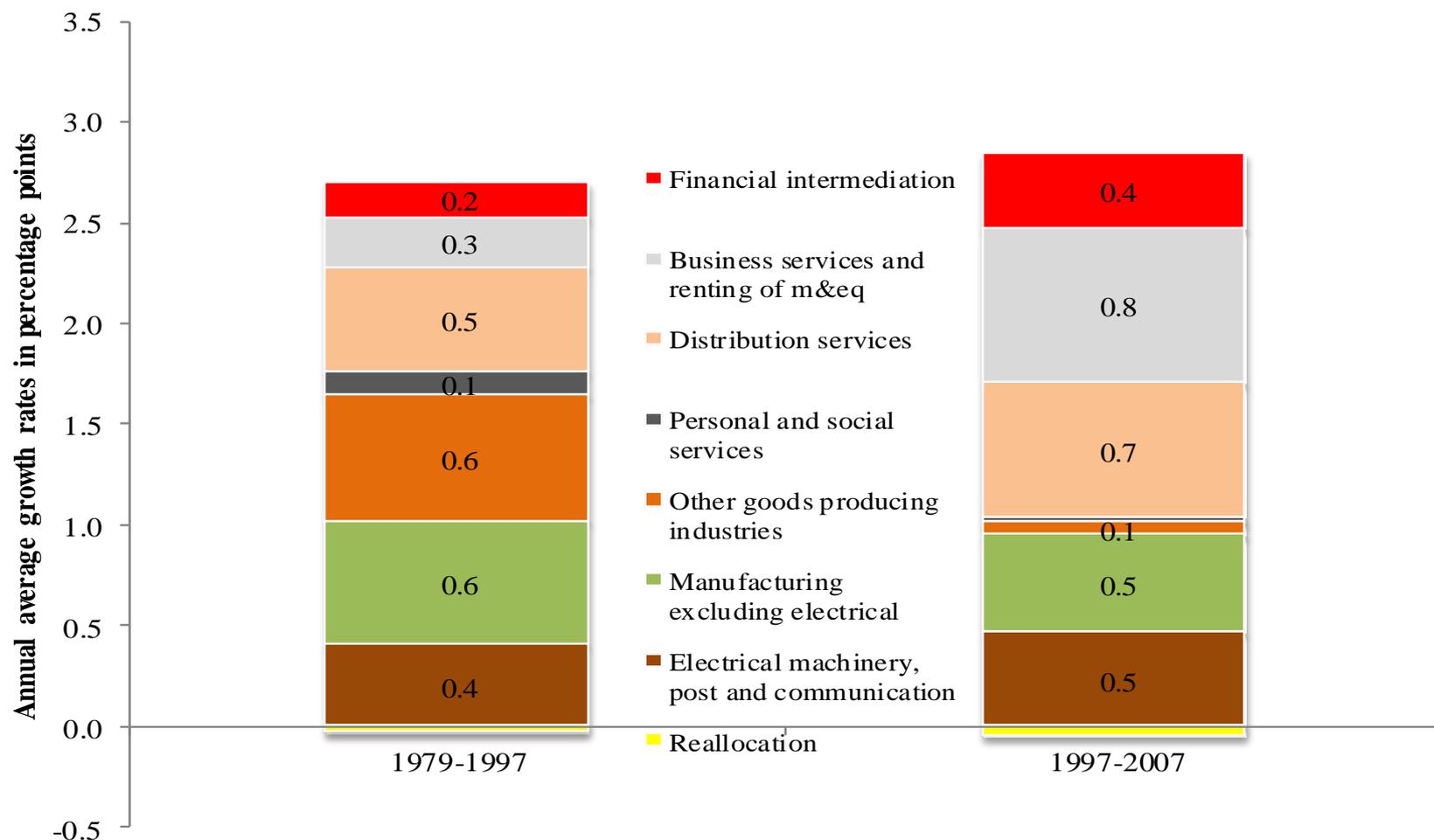
Source: LSE Growth Commission

A REVERSAL OF MISFORTUNE, GDP PER CAPITA, 1980=100



Source: LSE Growth Commission

PRODUCTIVITY GROWTH (GDP PER HOUR) : IT WASN'T ALL FINANCE



Source: LSE Growth Commission

WHAT WORKED

- **Policy Changes**

- Tougher competition through privatization; independent regulators; competition policy
- Flexible labour markets through reforms to employment services, benefits & union law
- Increases in university education (5% had degree in 1980 compared to 31% in 2011)
- Openness to FDI & immigration

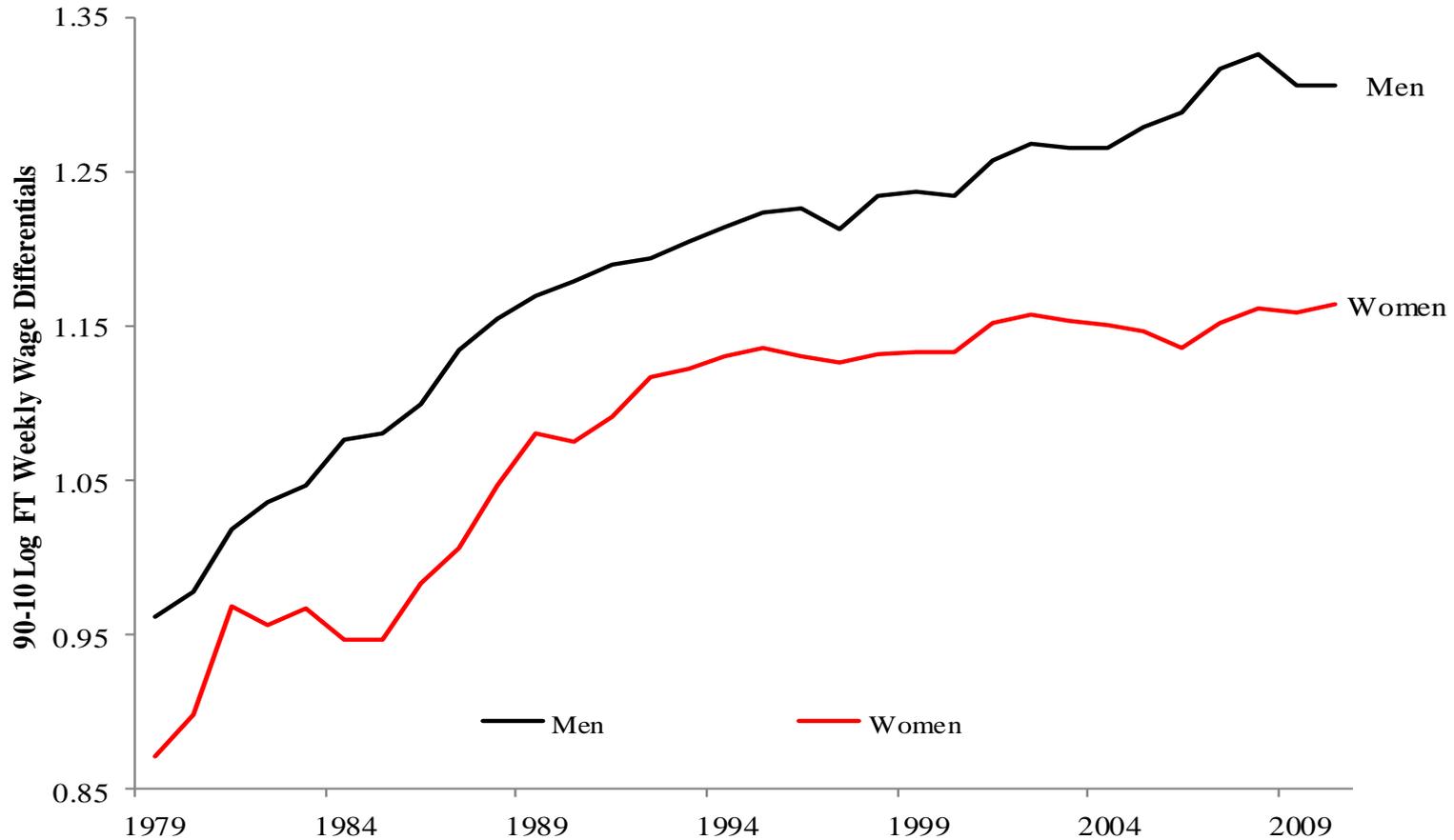
- **Independent bodies – experts & political resilience**

- Competition Commission & OFT
- NICE
- Bank of England MPC
- OBR
- MAC, LPC, NPRB, CCC

WHAT DIDN'T WORK

- Policy failures (procrastination, reversals)
 - Short-term political horizons
 - Adversarial politics causes tinkering, rebranding, reversals
 - Lack of independent expert advice & evaluations
 - Populist pressure
- Outcome is high uncertainty & low investment in long-term assets

THE INEQUALITY CHALLENGE: GROWING WAGE DIFFERENCES



Source: LSE Growth Commission

The Economic Story of the UK

Human Capital by JOHN VAN REENEN

Infrastructure

Innovation

Measuring Progress

Conclusions

WHY HUMAN CAPITAL MATTERS

- **Strong relationship between skills & growth**
 - We focus on schooling age 4-18
 - *Quality* not just *quantity* of schooling matters
 - Teaching most important input
 - “Double Dividend” of increasing human capital of disadvantaged: boosts growth & reduces inequality
- **Some UK problems**
 - Mediocre test scores (e.g. OECD PISA)
 - “Long tail” of underachievement
 - Stronger link between disadvantage and low academic achievement than in other countries

1. 'FLEXIBLE ECOLOGY' FOR SCHOOLS

- Make the system work better to spread better teaching practices
 - Greater school **autonomy**
 - Strengthened **accountability** (Ofsted Inspection; information; curriculum)
 - Wider parental **choice**
 - **Flexibility** for good schools to grow
 - School-level expansion
 - *Sponsored* academies. Leadership & governance. Takeover of struggling schools

2. TACKLING DISADVANTAGE

- Current system leads to focus on average (e.g. floor targets) & not “long tail” of disadvantage
 - **Information** on performance across the distribution (e.g. League Tables must show progression of disadvantaged kids)
 - Ofsted **Inspection** criteria reflect this information
 - Revise floor **targets** (to avoid incentives to target only “marginal” children around threshold)
 - Expansion of **sponsored** academies in disadvantaged areas

3. IMPROVING TEACHER QUALITY

- Key finding: hard to predict which teachers will be good in advance; but can discover after classroom experience
- **Proposals:**
 - Expansion of *Teach First* (top graduates)
 - Wider intake and more rigorous selection at end
 - Probation period extension (e.g. 2 to 4 years)
 - Sharing best practice (e.g. London Challenge)

4. SUPPLEMENTARY PROPOSALS

- Financial support for disadvantaged via pupil premium (PP) rising £600 to £900, but targeting issue
 - “PP Plus”: pupils can keep some PP themselves if attendance & performance improvements 14+ (cf. EMA, an evaluation success story)
- **Apprenticeships**
 - Quality too low. Employer control & incentives
- **Pre-School**
 - Children’s Centres; Family-Nurse partnerships

WHY HAVE PROBLEMS PERSISTED?

- Difficulties/complexity in measuring performance
 - political and media focus on average
- Changes to give perception of policy change & differentiation (reflects adversarial political culture)
- Vested interests

SUMMARY ON HUMAN CAPITAL

- People are key resource: we have failed to unlock talent
- More flexible school model helps spread good practice & gives incentives to improve
 - Need to help disadvantaged for growth reasons (not just social justice)
 - Best way is to improve teaching
- Complementary proposals on financial support, post-school & pre-school
- Huge potential gain if reforms can raise quality

The Economic Story of the UK

Human Capital

Infrastructure by NICK STERN

Innovation

Measuring Progress

Conclusions

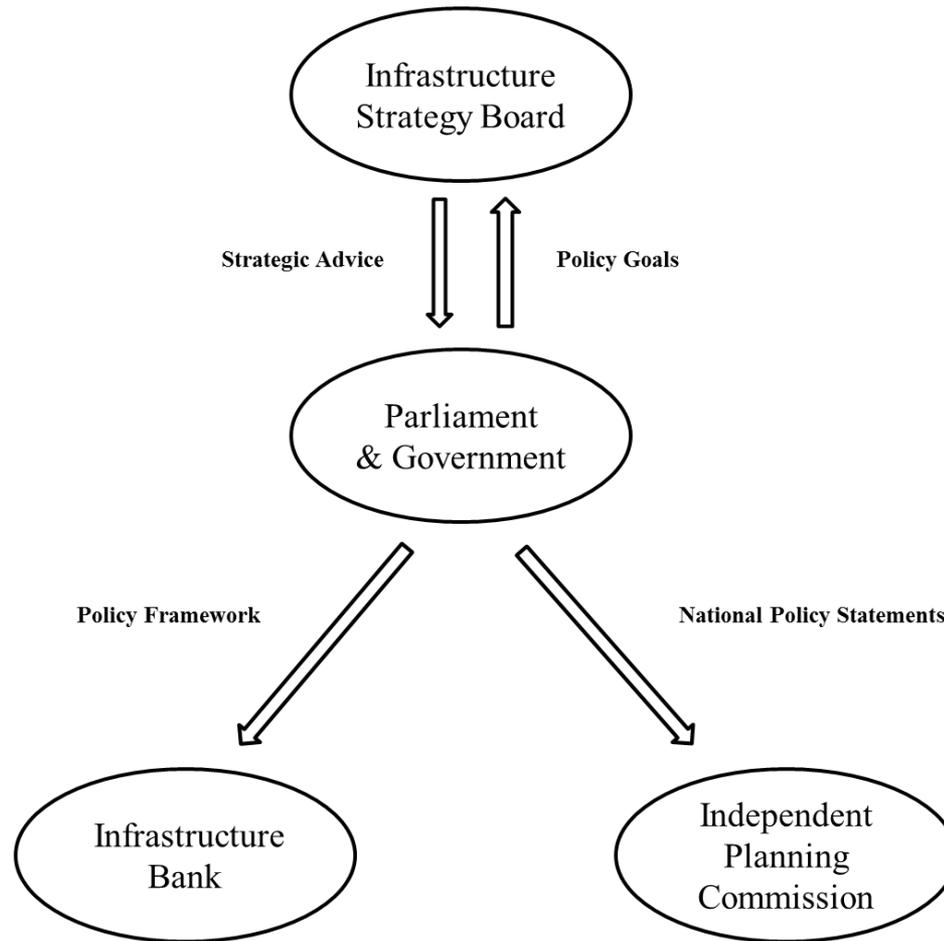
INFRASTRUCTURE

- **Problem areas**
 - Transport (roads, aviation, rail)
 - Energy
- **Government induced policy risk**
 - Lack of clear sense of strategy – uncertainty
 - Vacillation in and politicisation of policies and projects
- **Rigid planning framework**
 - Rationale with little economic content
 - Limited scope to share benefits
- **Rigid and misleading public accounting conventions**

NEW INSTITUTIONAL ARCHITECTURE

- **Infrastructure Strategy Board**
 - Independent expert advice
 - Accountable to Parliament
 - Foundation for cross-party consensus
- **Infrastructure Planning Commission**
 - Delivery – planning implications
 - Share benefits of development
 - No ministerial veto
- **Infrastructure Bank**
 - Reduce policy risk to encourage private sector investment
 - Develop sector-specific skills in new areas
 - Catalytic/multiplier effects on private investment

PROMOTING CONFIDENCE AND TRANSPARENCY



OTHER PROPOSALS

- **Fiscal targets should recognise assets, not just debt**
- **Road pricing / RAB model for new national roads**
- **Housing**
- **Broadband**

**“HS2 cost rises £2bn in
12 months”**

Financial Times, 28th January 2013

**“Power shortage risks by
2015, Ofgem warns”**

BBC News Business, 5th October 2012.

**“Third runway at Heathrow?
Beijing builds an airport with
seven”**

The Times, 15th January 2013

The Economic Story of the UK

Human Capital

Infrastructure

Innovation by RICHARD LAMBERT

Measuring Progress

INVESTMENT AND INNOVATION

- **Low investment as a share of GDP**
 - heavily weighted towards property and buildings
- **Weak intangible investment**
 - Low R&D and patent intensity
 - Weak commercialisation
 - Poor management quality
- **Financing gaps affecting start-ups and SMEs**
- **Aggravated by lack of skilled labour and infrastructure investment**

PROBLEMS IN UK CAPITAL MARKETS

- **Short-termism**
- **Lack of competition in retail banking**
- **Lack of economies of scale in SME financing**
- **Excessive reliance on debt**

PROPOSALS

- **Increase competition in retail/SME banking**
 - Account switching; banking license
 - Referral to Competition & Markets Authority
- **Business Bank to focus on innovative start-ups**
 - Independent board
 - Focus on innovation investments
 - SME securitisation
- **Other Proposals**
 - Voting linked to length of holding shares
 - Implement Vickers in spirit & letter
 - Allowance for Corporate Equity
 - Industrial Strategy
 - Management

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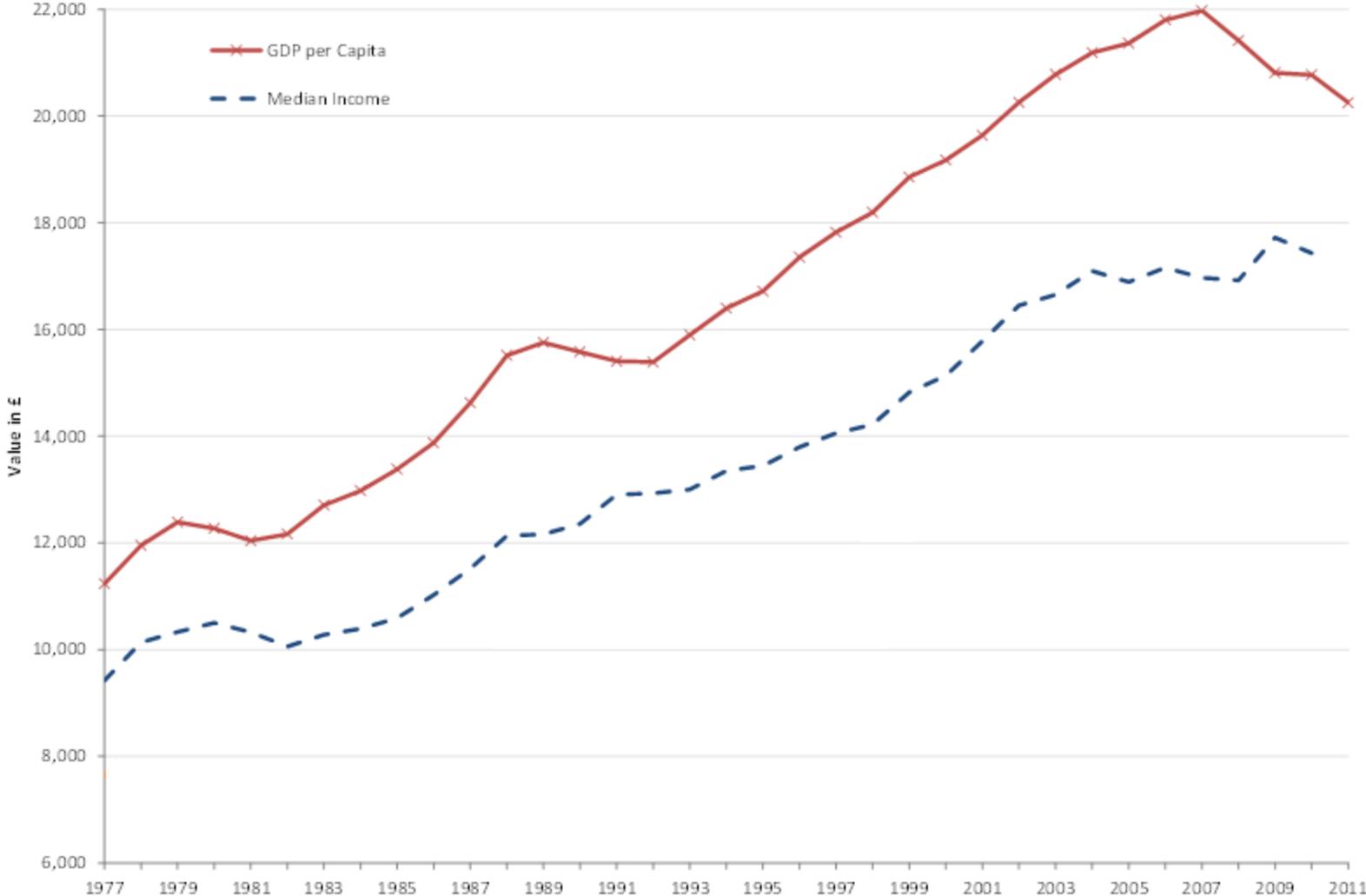
**Measuring Progress by FRANCESCO
CASELLI**

Conclusions

MEASURING PERFORMANCE

- Important to define criterion for success: growth of what?
- Exclusive focus on GDP not helpful
 - Goes up even if most people are left behind
 - Measures production not income
- Proposed: greater focus on Median Household Income
 - Captures what happens in the core of the population
 - Measures income
 - Focuses on families
- Recommendation: direct statistical agencies to devote more effort and resources to providing timely and accurate measures of MHI

MEDIAN INCOME AND GDP PER CAPITA



Source: ONS

The Economic Story of the UK

Human Capital

Infrastructure

Innovation

Measuring Progress

Conclusions by RACHEL LOMAX

POLITICAL ECONOMY OF GROWTH

- **The problems are well known - why don't we tackle them more effectively?**
- **The fundamental weakness: failure to create a stable policy framework for long term investment**
 - Short term policy horizons
 - Adversarial politics
 - Amplified by 24/7 media
 - Privately owned infrastructure

OUR APPROACH

Build institutions that put politics in the right place

- Making strategic choices
- Setting high level objectives
- Holding executive bodies to account

supported by

- More capability at the centre of government
- A bipartisan commitment to evidence based policy

Effective action requires sustained cross party commitment:

- to tackle the key problems holding back long term growth
- to develop the institutions needed to create a stable long term policy framework



LSE

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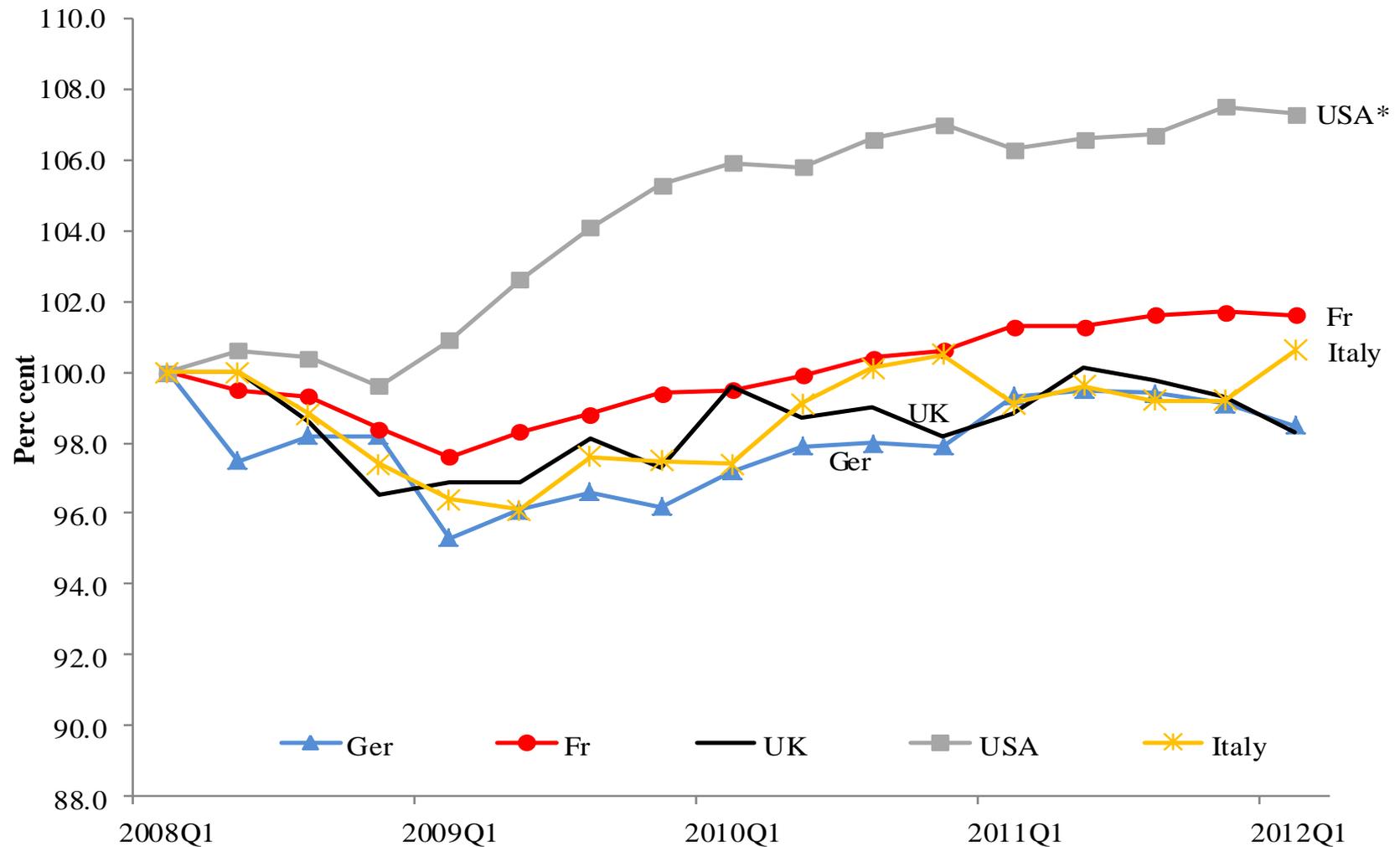
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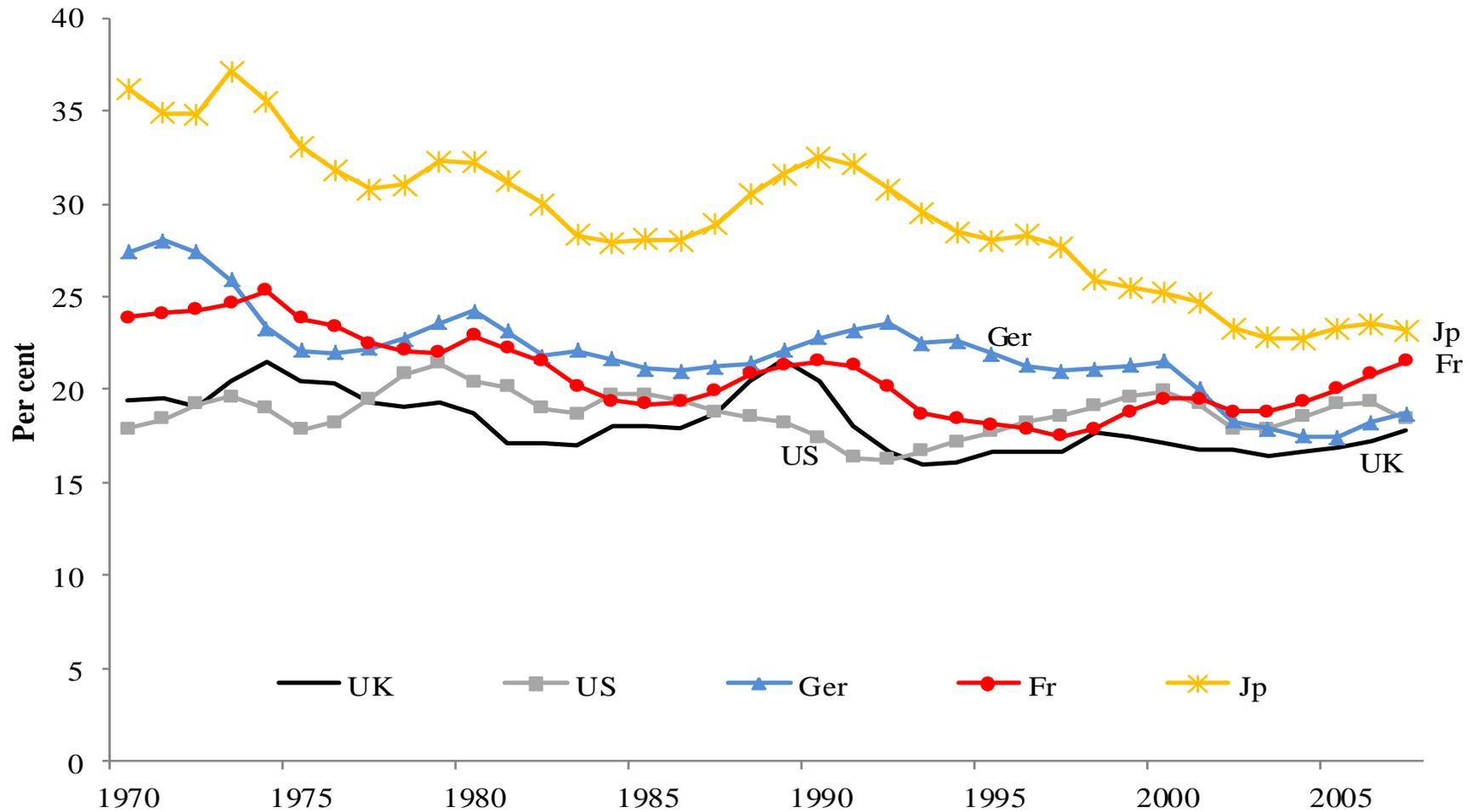
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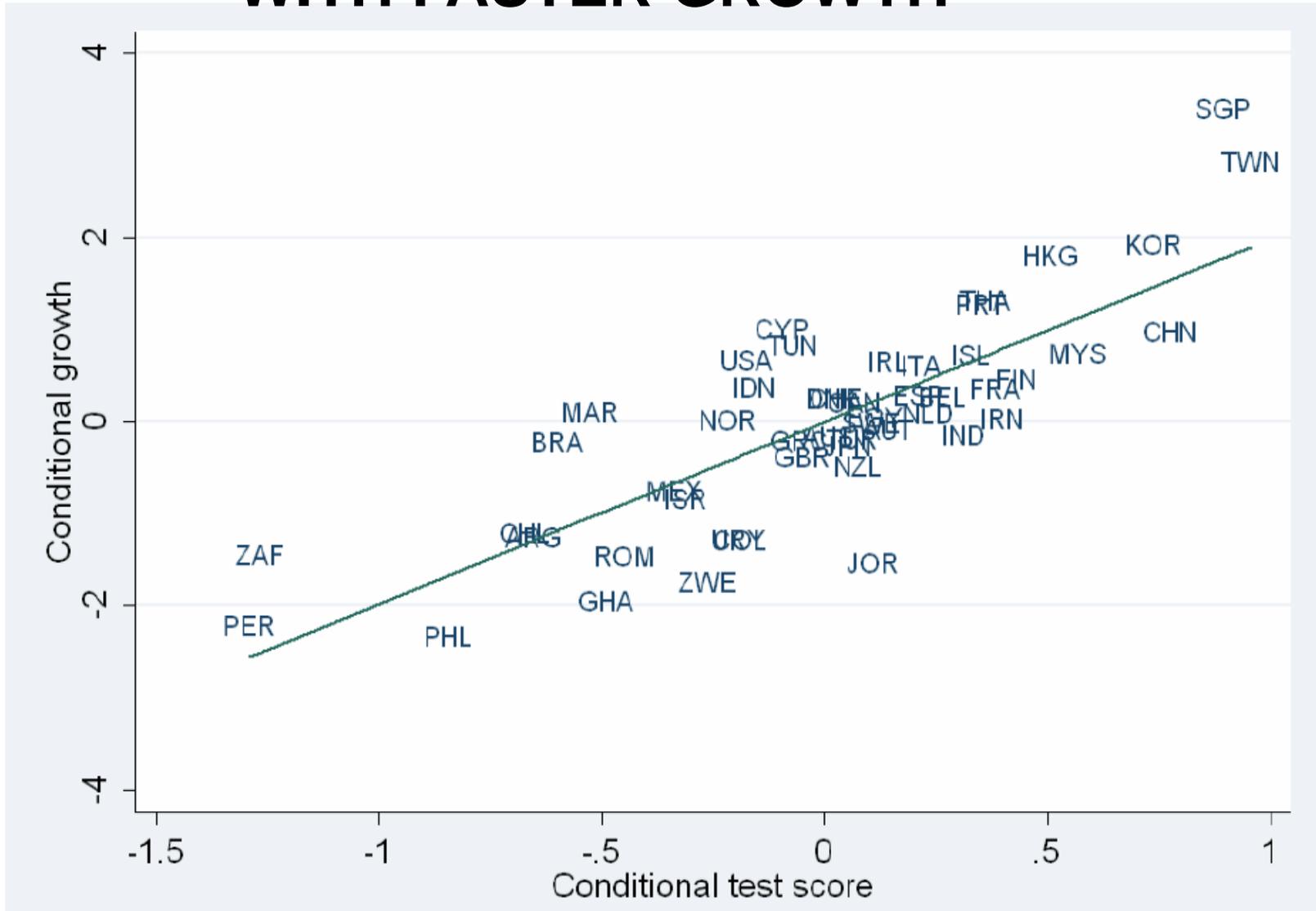
GDP PER HOUR: THE PRODUCTIVITY PUZZLE (IN US)



INVESTMENT (GFCF) OVER GDP



BETTER COGNITIVE SKILLS ASSOCIATED WITH FASTER GROWTH



Source: Hanushek & Woessmann (2012)

WHAT WON'T WORK

- **Right**
 - Ever smaller state
 - Ever more de-regulation
- **Left**
 - More redistribution (less inequality desirable but not generator of growth)
 - More regulation e.g. ever higher minimum/Living Wage
- Short-run policies for austerity or stimulus & leave long-run to look after itself

INVESTING FOR PROSPERITY

REPORT OF THE LSE GROWTH COMMISSION



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