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Championing better work and working lives

UNLOCKING BUSINESS IMPROVEMENT

Overcoming obstacles to workplace productivity growth

Policy paper

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Policy paper

Unlocking business improvement: overcoming obstacles to workplace productivity growth

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1 Introduction

The long-running debate about how to boost UK productivity has occupied successive governments, with agreement only that it's a complex problem of many dimensions.

As the UK seeks to recover from the pandemic and to 'level up' and boost growth across the country, the question of how best to catalyse the productivity improvements required to achieve this comes into sharp focus once more – not least because of rising skill and labour shortages that risk holding back economic recovery, and the Government's ambition of transitioning the UK to a high-wage, high-skill economy.

The Government's strategy for meeting this challenge is set out in its Plan for Growth, which outlines proposals to boost investment and improve policy in three key areas:

1. infrastructure
2. innovation
3. skills.

Although there's broad consensus that these are key priority areas, there's growing evidence that improvements to physical infrastructure and increased R&D investment – coupled with support for key high-tech sectors – are unlikely to be sufficient to achieve the Government's ambitions.

Similarly on skills, while plans to reform further education and put employers at the heart of the system are both welcome and necessary, the Plan for Growth has clear fault lines:

- Its narrow focus on a few high-tech industries means there's little attention paid to addressing the productivity deficit that exists within every sector of the economy – including those sectors which employ the biggest proportion of workers, such as services, hospitality and care.
- There is a lack of a credible strategy to encourage and enable more firms, particularly SMEs, to invest in the technology, people management capability and workforce development required to achieve economy-wide improvements in productivity. This is necessary to create more high-wage, high-skilled jobs; address high levels of overqualification and skills mismatch; and boost incremental firm-level innovation, which, evidence suggests, is just as important to economy-wide innovation as more radical or disruptive innovation generated by investment in R&D and the work of scientists and engineers.

The Government does acknowledge the importance of broadening the adoption of technology across the economy and the role of improving management capability in enabling this in its Plan for Growth and UK Innovation Strategy. However, its proposals to achieve this through its Help to Grow Management and Help to Grow Digital schemes, as well as via the existing business support infrastructure, fall far short of what is required. For example, its £300 million Help to Grow Management scheme will potentially help up to 30,000 business leaders of small and medium-sized enterprises (SMEs) over three years, representing a very small fraction of the almost 1.4 million SMEs that employ people in the UK.

Current government policy on growth and innovation fails to recognise how difficult it is to encourage business leaders and managers to engage in business improvement, as well as the type of flexible, high-quality support needed to achieve this.

This paper highlights the various reasons why employers too often fail to invest in technology, management capability, and skills development, and the difficulty of achieving business improvement even when business leaders do accept the need for action.

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To address this, there's the need for a long-term strategy that goes beyond limited small-scale interventions to one that seeks to enhance the business environment and supports business productivity improvement at a regional, sectoral and national level. The paper sets out key recommendations on the policies and investment needed to underpin this type of strategy.

Summary of recommendations for government

- Establish a UK Productivity Commission to develop strategy and policy on improving business productivity growth.
- Invest £60 million in a bespoke, integrated business support consultancy service providing SMEs with up to two days of free support a year through the Growth Hub network in England.
- Commission a review of sector-based institutions, such as Sector Skills Councils and other sector skills bodies, with a view to improving support for key industries.
- Reform the Apprenticeship Levy into a more flexible training levy to boost employer investment in skills and engagement with the further education (FE) system.
- Double Acas's annual budget to £100 million a year to enable it to further develop its people management advisory services to employers as part of a more progressive labour market enforcement system.
- Invest an estimated £100 million a year to increase the number of labour market enforcement inspectors to one per 10,000 workers.
- Sponsor the creation of a Business and Productivity Forum to help disseminate good practice, guidance, training and professional qualifications.
- Require the Financial Reporting Council to work with key stakeholders to develop best practice guidance to improve the consistency and quality of workforce reporting.

We explore these recommendations in depth throughout this paper.

2 Unlocking UK-wide business improvement

The UK Government has set out the ambition to build back better after the pandemic and address regional inequalities through 'levelling up' economic growth and opportunity. More recently, Prime Minister Boris Johnson has highlighted the need for the UK to transition to a high-wage, high-skill economy that relies less on immigration to address skill and labour shortages. Whether these ambitions can be realised will ultimately depend on increased economy-wide productivity growth.

Productivity growth can help offset the skill and labour shortages that surfaced during 2021 as the economy started to recover from the worst effects of the pandemic – shortages that, longer term, are likely to become more of a challenge due to the UK's ageing workforce and more restrictive immigration policy.

Enhanced productivity (for example, through investment in technology and improvements in management capability to boost worker output relative to inputs/hours worked) can play a part in helping the UK towards its target of creating a net-zero emission economy by 2050.

While there have been welcome signs of economic growth during 2021, the strength and sustainability of recovery is uncertain – not least because the revival in activity is driven to a very large degree by an increase in household consumption. In contrast, exports and,

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in particular, levels of business investment – both of which could potentially help boost productivity – remain well below pre-pandemic levels.

Furthermore, longstanding factors that have contributed to low UK productivity growth continue to hold the UK back. These include the:

- long tail of low-productivity firms across all sectors (linked to low firm-level investment in skills)
- poor diffusion of new technology beyond the best-performing companies.

Plan for Growth: aims and challenges

Against this backdrop, the Government's strategy for kick-starting a sustainable and inclusive UK recovery as it emerges from the pandemic is set out in its recent Plan for Growth. To a large degree, the key elements of the plan are very similar to previous approaches adopted by successive governments to try and catalyse productivity and unlock greater economic growth. These can be summarised under the three main pillars in the Plan for Growth:

1. **Greater investment in infrastructure**
   The Plan for Growth sets out proposals to increase capital spending – for example, on roads, rail and green technologies, while supporting city and regional investment in infrastructure projects.
2. **Greater investment in innovation**
   Plans to increase innovation centre mainly on increasing R&D investment and supporting certain high-tech sectors, such as life sciences, fin tech, and the digital and creative industries.
3. **Plans to try and boost the supply of skills to the economy**
   The Government's priority is to improve the further education and training system, including through much greater employer engagement with colleges and universities, as well as by making tweaks to some aspects of apprenticeship policy.

These three key areas for investment and public policy reform are critical to help boost UK growth and competitiveness. Major infrastructure investment is of course crucial to ensuring that our businesses of the future will have the transport, energy, waste, water and digital networks they'll need to thrive, while R&D investment will help generate the cutting-edge ideas, advanced and green technologies that can help power our economy and transform our society. These are crucial investments in the country's future.

However, whether greater investment in our physical infrastructure and R&D in themselves will create the game-changing productivity benefits the UK economy needs is highly debatable. Similarly, the planned supply-side changes to skills policy fail to address arguably more substantive problems. These include falling employer investment in skills, high levels of skills mismatch, and overqualification and poor use of skills within too many firms because of inadequate HR and people management capability.

These have been the 'go to' areas of policy and big-ticket investments used to try and boost growth by successive governments over the last two decades, with little evidence that they've been sufficient to transform our productivity growth or tackle economic inequalities.

A growing body of evidence suggests that the benefits of massive spending on physical infrastructure and breakthrough technology will fail to be optimised unless there's also greater investment in support to boost adoption of technology and improve firm-level management capability across all sectors. Furthermore, it's arguable that innovation, which

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happens incrementally within firms across the economy, is as important as major research and development breakthroughs, with the quality of people management being central to organisational innovation.

Likewise, the levelling-up agenda will be badly undermined if people growing up in poorer regions have to continue to move to wealthier areas to find higher-skilled, higher-paid jobs as a result of a narrow focus on productivity and innovation.

3 Investing in technology and management capability

Analysis by former Bank of England Chief Economist Andy Haldane and the OECD has highlighted that productivity growth will be strongly linked to the appetite firms have for investment in new technologies like AI and robotics.

Furthermore, greater investment in new technology by UK employers will also be needed to compensate for the UK's ageing working population and prevent skills and labour shortages. McKinsey's report, *A Future That Works: Automation, employment and productivity*, observes: *'While much of the current debate about automation has focused on the potential for mass unemployment, predicated on a surplus of human labor, the world's economy will actually need every erg of human labor working, in addition to the robots, to overcome demographic aging trends in both developed and developing economies.'*

However, investment in technology alone is unlikely to lead to productivity growth without complementary investment in management capability and workforce development. Employees need to be managed effectively and develop new skills if business investment in technology is to be optimised to boost productivity and wages.

Improving management capability is critical

Haldane's detailed analysis of the UK's productivity problems highlighted a lack of management capability as one reason for poor adoption of new technology and slow technological diffusion to the long tail of low-productivity firms in the UK. The 2019 Government-sponsored *Business Productivity Review* noted: *'Good management is often the key enabler to driving up firm-level productivity and can be the stepping stone to businesses adopting other productivity improvements such as digital adoption and better working practices.'*

Analysis by the OECD also identifies low managerial quality as a key factor in curbing the rate of adoption of new technologies. Recent work by the NIESR on productivity in some low-wage industries shows that, for the most part, it's not the differences in capital investment or labour quality (qualification level) that accounts for productivity gaps with other major economies but, rather, 'total factor productivity' – which captures everything else in the workplace, including managerial competence, work organisation and skills development.

The importance of management capability to firm-level productivity was further highlighted by findings from the Office for National Statistics (ONS) Management Practices survey of 25,000 firms published in 2017.

Analysis of the data found a significant positive link between the presence of more formal management practices and productivity. The study also found that people management practices – including performance reviews, managing underperformance, training and

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promotion – were the management practices most correlated with productivity. The improvement of people management practices is also central to efforts to improve workers' job quality and wellbeing and create more flexible and inclusive workplaces.

CIPD research shows that the quality of firms' people management capability among line managers will significantly determine:

- how inclusive they are
- the motivation levels, overall wellbeing and job satisfaction of the workforce.

It's not just the presence of HR policies that matters, but how they are applied that determines their overall effectiveness. The role of the line manager is critical in this.

This growing body of evidence underlines the critical importance of improving management capability in order to catalyse and optimise the greater business investment in new technologies and workforce skills required to boost the nation's productivity. It's also crucial to enable the creation of more high-skilled jobs and address skills mismatch and high levels of overqualification in the UK by international standards.

The Government's Plan for Growth and accompanying innovation strategy do both recognise the need to improve management capability to support the wider adoption and optimisation of productivity-enhancing new technology across the economy. To address this issue, the Government has pledged to invest £500 million in its Help to Grow Management and Help to Grow Digital schemes. However, while these are welcome initiatives, they are too small-scale to make a significant difference.

For example, the £300 million Help to Grow Management programme will only help 30,000 business leaders over three years, which is highly unlikely to have much impact on overall UK productivity given almost 1.4 million SMEs employ people in the UK.

4 Business support via LEPs and Growth Hubs

The other way the Government intends to support firms to build management capability and support technology adoption is through reforming LEPs (Local Enterprise Partnerships), and improving the quality and access to business support schemes they deliver through Growth Hubs.

The Government hopes these changes, combined with the business support services offered through Be the Business (discussed below), Scottish Enterprise agencies, the Welsh Government and Invest Northern Ireland, will be sufficient to tackle the UK's management capability and technology adoption deficit.

However, a closer examination of the business support offered at a local level – for example, through LEPs in England – suggests that there'll need to be very significant improvements to the services available to firms if they're to achieve what's expected of them.

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Improvements needed to the business support services available to firms

CIPD research evaluating the Strategic Economic Plans and the Skills and Employment Plans of 15 Local Enterprise Partnerships found that there was, overall, very little focus on raising management capability at a regional level, and limited available help for firms to improve their practices.

Exceptions included evolving efforts – for example, in Manchester, Liverpool and London, creating local good employer charters as a way of championing the importance of people management and development. However, such initiatives take time to gain traction and require effective marketing and business support services to boost wider uptake and impact beyond the 'good' employers that are naturally attracted to such initiatives.

A more recent research report published by the Gatsby Foundation into the provision and quality of business support services provided through LEPs via the Growth Hubs found extreme variability in both the scope and scale of business support services. Furthermore, the research found no clear pattern in the nature of the business support offered in an area relative to local economic need. It also showed huge variety in the budget and delivery model for business support services.

The analysis identified the two nationally funded programmes designed to boost SME productivity and growth which are typically promoted via the Growth Hub network:

1. The BEIS Business Support Helpline, which provides a phone and web-chat service to assist with basic enquiries, often signposting to Growth Hubs and other services.
2. Be the Business, a publicly funded initiative designed to help organisations improve their productivity, established in 2018, provides online resources (such as tools and digital learning courses) on leadership, voluntary mentoring (by experienced business managers), and online peer networking. Since it was set up in 2018, only about 15,000 business leaders across England have benefited through its formal programmes where available, which suggests its capacity to support economy-wide improvements in management capability and technology adoption will be extremely limited.

5 Lack of co-ordination undermines FE reforms

The Gatsby report also highlights a lack of co-ordination across the LEP network of:

- 'demand-side' business support (designed to improve management capability and business innovation)
- 'supply-side' skills policy (designed to ensure workers have the skills businesses require).

For example, it found typically poor links between Growth Hubs and local FE colleges, and limited evidence that Growth Hubs prioritise skills and workforce development (with some exceptions, such as the Greater Manchester Skills brokerage). The analysis suggests that most FE engagement with employers is transactional, involving tasks like placing apprentices, and does not involve dialogue about their business model or strategic growth ambitions.

'Pump-priming' business support

A system that really puts employers at the heart of the further education provision should include 'pump-priming' business support to help firms depending on their particular needs:

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- upgrade their business growth strategies
- improve their people management and development capability
- adopt and optimise the benefits of new technology.

This type of improved business support would:

- help firms establish the type of workforce skills development they need to boost growth and productivity
- enable employers to engage more strategically with education providers on their skills requirements as they evolve
- dovetail with the work of any new college business centres as they emerge
- help many more firms engage far more meaningfully with the further education system
- support the development of functioning local skills ecosystems, which can help create higher-skilled and better-quality jobs by better matching the supply of skills and the demand for skills, combined with a much stronger focus on improving how skills are utilised in the workplace.

It is hoped that the BEIS-led review of national and local business support – including through the Growth Hubs – recommends greater investment in business support on management capability and technology adoption, and improved co-ordination between demand- and supply-side skills policy. In addition, there needs to be a more consistently delivered and standardised business support offer that recognises the common obstacles that businesses across all sectors face in taking steps to try and boost their productivity, growth and competitiveness.

6 The journey to change will be different for every firm

The type of business support on offer – and how it's delivered – is also likely to be critical to its success. Business change won't always be strategic; it'll sometimes start with a more transactional requirement in response to a specific problem. However, the value of this sometimes basic first step to business improvement should not be underestimated, as it can get business leaders and managers thinking differently about the business and its priorities. Even small changes – to management practices, for example – can have significant positive effects in their own right.

This point has come through from a number of CIPD-run pilot programmes providing an amount of free (up to two days per firm), high-quality HR consultancy support for small firms. It was also referenced by the Government's 2019 Business Productivity Review, which observed: *'Relatively basic practices such as implementing management best practice and making best use of technology are likely to have a big impact in businesses with low productivity.'*

Holistic business support consultancy service needed

The CIPD pilots showed that the transactional people management support typically needed by small firms (such as ensuring there are written terms and conditions of employment or job descriptions in place) can have a positive impact on performance. For example, owner-managers were more likely to report their organisation being *better* or *much better* than similar firms in their sector on measures of workplace relations, labour productivity and financial performance after using the People Skills HR support service

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than they were prior to using it. The People Skills service was also flexible, providing both transactional and more transformational support (such as management training) depending on what intervention/s were needed in relation to the maturity of the firm.

These pilots highlighted that a flexible, consultancy model of business support is particularly valued by owner-managers of small firms because:

- it's easy to access
- it provides a bespoke diagnosis of the key business challenges small firms face
- it develops targeted, context-specific support or training.

In contrast, off-the-shelf business support offers with fixed curriculums and/or those requiring lengthy time investment on the part of business leaders and managers (to either access or benefit from) are unlikely to be as attractive.

Of course, besides providing firms with access to high-quality HR and people development support, there's also a need to provide support and expertise on other key areas firms need to invest in to boost productivity, such as digital technology and automation. However, whether firms understand – and take steps to address – their skills development needs (to ensure their people are trained to fully utilise new technology) will also depend on their people management and development capability.

This is why the CIPD believes there's a need for an integrated business support consultancy service encompassing advice on business models and product market strategies, people management and development, digital technology, AI and automation. This would be delivered in England through the Growth Hubs, providing SMEs with up to two days of free consultancy support, which would be promoted by key stakeholders and trusted networks like local councils, chambers of commerce and sector and professional bodies. The high-quality – but limited – free support would be designed to 'pump-prime' the market and boost demand among more employers for greater investment in management capability, technology and workforce skills development.

The CIPD's People Skills pilots showed there's very little deadweight associated with this type of support, with a large majority of the participating firms never having invested in professional HR support previously. The pilots also showed that providing a limited amount of free support can help encourage firms to invest further once they'd experienced the value of capability-building.

This type of business support would also enable and encourage more businesses to engage meaningfully with their local further education college to help shape the design of training courses and qualifications to address skills mismatch and create more high-skilled roles in local communities. This is key to improving opportunity and 'levelling up'.

The CIPD estimates that such a holistic, integrated business support consultancy service based on the flexible People Skills delivery model could be established in England in every Growth Hub at an overall cost of about £60 million a year and could service up to 40,000 firms annually in England alone. Properly promoted, the service could, over five years, potentially reach up to 200,000 businesses. Consequential funding for Scotland (£5.8 million a year), Wales (£3.4 million a year) and Northern Ireland (£2 million a year) would enable investment in similar interventions in the devolved nations.

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However, significant further steps need to be taken to boost demand for this service and incentivise and enable more firms across the economy to invest more time and resources in management capability, technology and workforce development.

Recommendations

- Invest £60 million in a bespoke, integrated business support consultancy service providing SMEs with up to two days of free support a year through the Growth Hub network in England.
- Provide consequential funding for Scotland (£5.8 million a year), Wales (£3.4 million a year) and Northern Ireland (£2 million a year) to enable investment in similar interventions in the devolved nations.

7 Why firms don't invest in improving performance

One of the difficulties all business support services face in helping firms improve their management practices is a lack of demand for these services among companies – even if they're very low cost or free.

This is because of what can be described as 'demand-side' inertia. It's often held that, if investing in management capability and skills development was so valuable to firms, they'd of course do it for themselves. Too often this does not happen.

There are a number of reasons for this demand-side market failure:

1 Firms often over-rate their productivity

CIPD research into firm-level productivity shows that business leaders typically over-rate their organisation's productivity relative to peers, with the majority believing their organisation is already more productive than competitors. This false confidence is likely to undermine organisations' appetite for investment in new technology or in improving people management and workforce skills development.

2 People management issues are often overlooked

Even when business leaders are looking to improve or invest in their business, they may not accurately recognise the weaknesses in management capability that need to be addressed. For example, people management issues are often overlooked or under-prioritised even though the evidence suggests these are the management practices most correlated with enhanced firm-level productivity. The Government's 2019 Business Productivity Review noted that *'UK SMEs compare particularly unfavourably internationally on people management, which is the factor most correlated to productivity. Leadership and management practices therefore represent one of the greatest opportunities for firm-level productivity growth in the UK.'*

However, CIPD research shows that small-firm owner-managers often don't understand why they need to develop their people management skills until they've had their first conversation with an experienced HR consultant. Too often, business leaders and managers

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lack awareness of the people factors underlying poor business performance. This means they typically only ever reach the point of looking for help when they hit a significant problem or crisis – such as a major staff conflict, employee absence issue or tribunal claim against them.

Owner-managers of small firms are also very time- and resource-poor; they struggle to find the capacity and money to invest in business improvement activities even if they do recognise the need to.

3 Sustainable change is hard to achieve

Even when business leaders want to take action to upgrade their business strategies and invest in new technology, management capability or workforce development, achieving sustainable change is difficult to achieve. The 2019 Business Productivity Review, jointly undertaken by the Department for Business, Energy and Industrial Strategy (BEIS) and HM Treasury, summarised the steps firms need to go through to initiate and embed change through the four stages of the business change cycle:

1. realisation that a change is needed
2. assessment of the costs of change and associated outcomes, quality and value of change, and of the business support available to help identify solutions
3. navigation of the business support environment to find advice, or new services and products, to deliver the desired change
4. embedding the change in the business to realise the benefits, which may require strong leadership and staff training.

This process underlines how difficult achieving sustainable business change and improvement is, and why it simply won't happen for most firms without significant assistance.

Together, this analysis suggests there needs to be a coherent national strategy to improve the business environment and build greater demand among many more employers to invest in business improvement that goes beyond a place-based approach.

8 Sector-based support to boost productivity

A key element of this strategy would be to develop stronger sector institutions to collectively engage and support employers within industries facing similar challenges in productivity, growth and workforce issues, such as skill or labour shortages.

CIPD analysis of ONS data (Figure 1) shows a wide spectrum of productivity performance between the lowest-performing and highest-performing companies within every sector. This data shows clearly the productivity growth potential that could be achieved across the economy if the productivity performance of bottom quartile firms within every sector across the UK could be raised to at least the median level of their industry.

Analysis by the recently abolished Industrial Strategy Council emphasised the need for government to take steps to boost productivity at a sector level, including among large, low-pay service sectors like retail, hospitality and care. It concluded: *'Services matter and require policy attention due to their sheer scale, their often-lagging productivity, and the difficulties they face in the aftermath of the Covid-19 outbreak. But they are also crucial because of their increasing importance to the manufacturing industry, their growing export potential, and the significant non-quantifiable benefits they provide (e.g. care sector's role in wellbeing, or creative industries' role in UK's international soft power).'*

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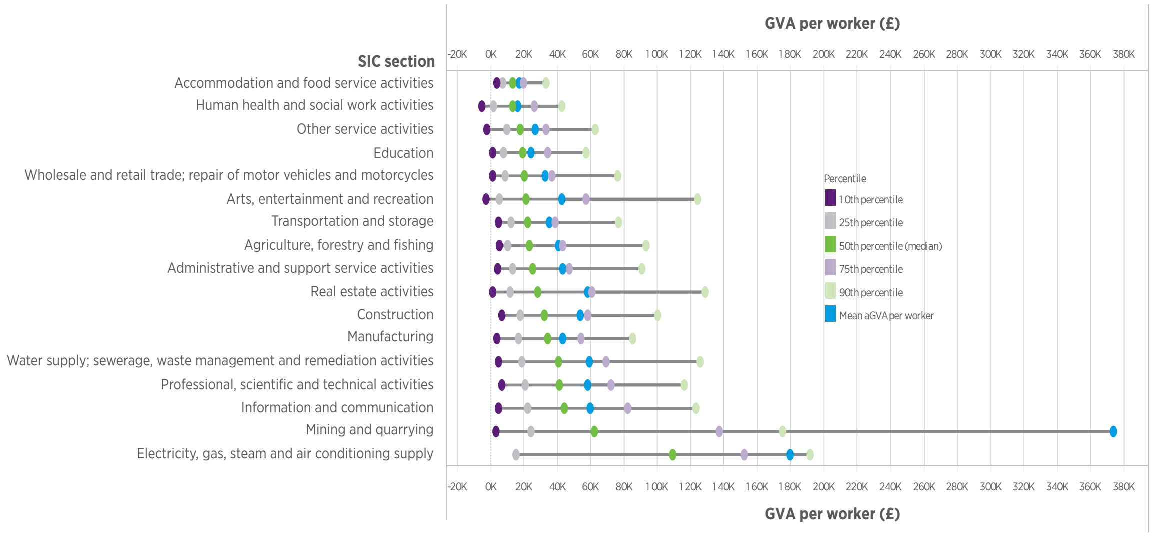
Figure 1: Average labour productivity and percentiles by industry sector, firm weighted, current price, 2018



Source: ONS (2020) – Firm-level labour productivity estimates from the Annual Business Survey (ABS): summary statistics.
Data has been sorted on the median (blue dot).

This point is also made in a recent paper by the Institute for Government, *Productivity: Firing on all cylinders*. Its author, former government adviser Giles Wilkes, cautions that the Government should resist the temptation to put all their emphasis on the cutting-edge industries of the future. He observes that, *'There may be good economic and other reasons to bring special attention to technological challenges, but technological intervention can play only a small part in addressing the productivity gap. At least as important will be steps to lift the performance of less productive service industries, such as retail, administration, hospitality and transport. Innovation is just as relevant to these sectors as any other.'*

Sector bodies can help highlight common areas where there need to be greater investment and capability-building among employers across an industry, such as how to address current and future workforce skills and management capability issues. They could also play an important role in signposting employers to their nearest place-based source of business consultancy support, which would help build demand for these services and boost the number of firms that benefit.

Effective sector bodies that meaningfully engage large numbers of organisations can also support the Government's ambition to put employers closer to the heart of the FE system and join up supply- and demand-side skills policy. However, as discussed above, this requires organisations to have a more sophisticated understanding of their skills development needs in the context of changes to business strategy or investment in technology, or in response to external factors like increasing skill or labour shortages.

Review sector institutions to understand what works (and what doesn't)

Forthcoming CIPD research exploring how firms in a number of low-wage sectors are trying to address skill or labour shortages shows that very few are planning to invest in technology in response to these challenges. In addition, they are often not utilising progressive HR and people management practices – for example, to make their recruitment practices more inclusive or to create more flexible working practices to boost

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their ability to attract and retain a more diverse workforce. Without external support, these firms simply don't have the capacity or knowledge to invest more strategically in technology or people management practices.

Currently, the sector institutions that support different industries are highly varied, ranging from those based on the now-defunct Sector Skills Councils and groups of employers linked to the previous government's sector deals. The level of professional support and the degree of meaningful employer engagement provided through these bodies inevitably varies.

To address this, there should be a review of these sector institutions to understand where they work well, and where the weaknesses and gaps are. This review should:

- consider the core function the services sector bodies should provide, and the sectors that most require this type of institutional support
- investigate whether they require additional public funding to allow them to play a strategic role in building sector-wide capability through stimulating greater investment in management and workforce development and wider adoption of new technology.

Key upgraded sector bodies could then be set targets to raise overall productivity within their industry, with government support contingent on them having a focus on developing people management and development capability and supporting technology adoption.

Recommendations

The Government should commission a review of sector-based institutions such as Sector Skills Councils and other sector skills bodies with a view to improving support for key industries.

9 Enhancing the labour market enforcement system

Another central leg of a coherent strategy to boost economy-wide improvements to firm-level productivity should be a much more progressive labour market enforcement system. This would focus as much on supporting firms to comply with regulation and raising employment standards overall, as it would on holding employers accountable for breaches through penalty notices and fines.

This view is supported by evidence from recent research by the Warwick Institute for Employment, which shows a link between job quality and productivity and also finds that this correlation is stronger for bad work and poor productivity. It suggests that the focus on productivity initiatives should be on lifting more poor-quality work closer, at the very least, to the average level.

A reformed labour market enforcement system is the ideal vehicle for this purpose, with the scope to influence employer behaviour across the economy. A recent CIPD research paper, *Revamping Labour Market Enforcement in the UK*, outlines the reforms needed to achieve this and ensure that the forthcoming creation of a Single Enforcement Body (SEB) meaningfully improves the system.

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Specifically, it sets out of a range of recommendations on the changes needed to transform the system to one that:

- significantly improves how employment rights are enforced (including increasing the number of labour market enforcement inspectors to one per 10,000 workers)
- supports compliance by providing enhanced advice and support on people management so that fewer employers breach employment regulation due to a lack of knowledge or capability.

On the latter point, the key recommendations are that the Government should:

- Double Acas's budget to boost its ability to advise small employers and individuals on people management, workplace conflict and employment rights. SEB inspectors should be allocated on a regional as well as sectoral basis to work locally with Acas and local business advisers (for example, accountants) to ensure that local employers and their staff are made fully aware of relevant employment legislation and rights and are supported to deliver them effectively. Acas advisers could also refer employers to a new integrated consultancy service situated in every Growth Hub to continue their business improvement journey.
- Give Acas the resources to provide a free annual HR 'MOT' to small firms with fewer than 50 staff. This could potentially reduce their liability in any subsequent claim against them at an employment tribunal. However, this would need to be consulted on and developed.
- Reinstate the ability for employment tribunals to make wider recommendations to employers to improve their people management practices; this should cover all aspects of employment rights – not just equality issues. The employer would be required to work with Acas or a professionally qualified HR adviser to improve their people management practices. The SEB or other relevant enforcement body, such as the HSE or EHRC, would be responsible for following up these orders to monitor compliance, with power to fine employers not meeting their obligations.

The carrot and stick of progressive labour market enforcement

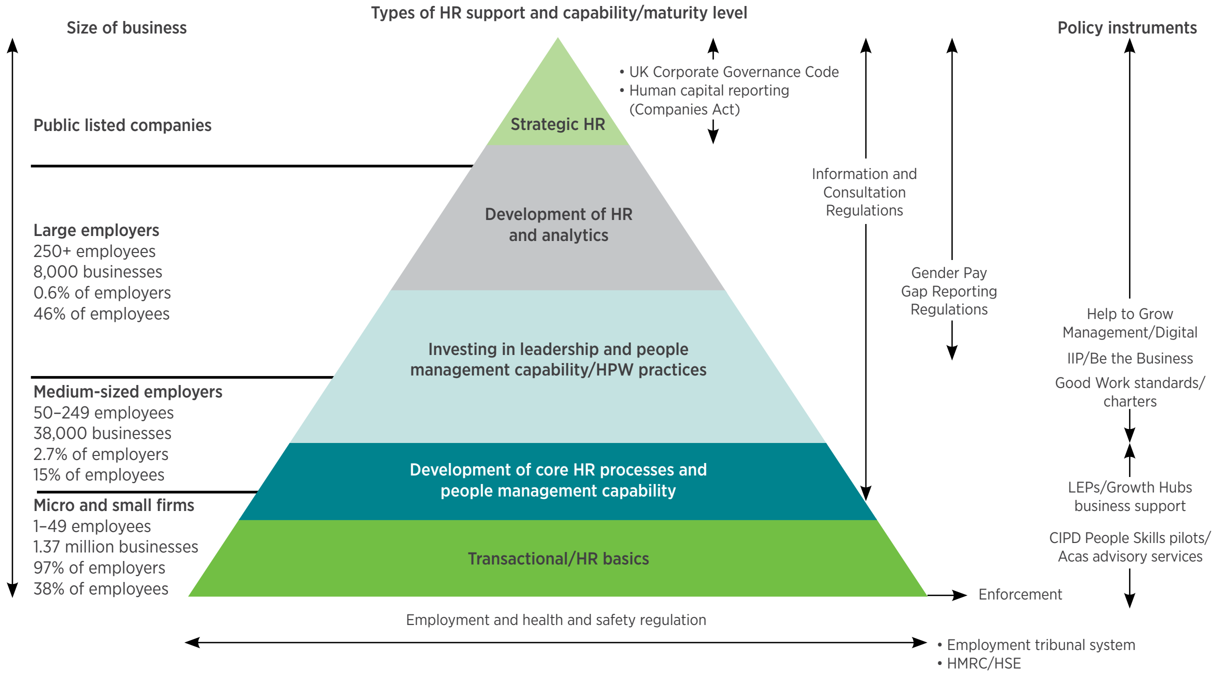
A progressive labour market enforcement system, as described above, has the potential to both significantly help boost demand among employers for investment in people management capability over time and reduce the proportion of workers whose employment rights are breached. This is because it combines the carrot of the provision of a limited amount of free high-quality advice and support, and the stick of the threat of enforcement action and fines if action is not taken. It's also likely to have more reach across the economy than any other policy mechanism for improving firms' management capability (see Figure 2).

Acas advisers could also play a role in referring employers to an improved business support consultancy service provided via the Growth Hubs to encourage them to continue their business improvement journey.

This model, based on insights from the CIPD's People Skills HR pilots, indicates that the level of HR capability within firms varies depending on their size and maturity, and, consequently, so do their business support needs. This highlights the need for policy-makers to consider in a much more nuanced way the type of business support offered, and how it's delivered if it's to be effective.

The CIPD's HR support pilots for small firms, referenced previously, suggests that a focus on supporting small firms to comply with employment regulation is likely to have

Figure 2: Improving job quality and workforce productivity



productivity benefits. They found that typical people management capability in most small firms employing up to 50 people is very low, with indications that many struggle to comply with some aspect of employment regulation. The findings from the pilots suggested that the provision of basic HR support, such as ensuring there were written terms and conditions of employment and consistent processes for recruiting staff, could help support improvements to firm-level performance. Furthermore, this type of transactional support can help owner-managers start to think more strategically about how they recruit, manage and develop staff. Professor Carole Atkinson, who led the evaluation of the pilots, observed in a recent paper that the *'HRM needs of SMEs may often be basic, but their resolution can be transformational, and stimulate a more strategic orientation towards HRM issues'.*

Recommendations

- The Government should increase the number of labour market enforcement inspectors to one per 10,000 workers.
- The Government should double Acas's annual budget to £100 million a year to enable it to further develop its people management advisory services to employers.

10 Improving workforce reporting quality

Improving the labour market enforcement system is likely to have the greatest effect on the behaviour of those SMEs that have no – or limited – HR and people management capability. However, an economy-wide strategy to boost investment in management capability and workforce investment needs to reach and influence larger firms as well. Policy to enhance the standard of workforce reporting can play a role in encouraging

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larger firms, which have more sophisticated HR capabilities, to invest more effectively in their workforces.

Human capital management (HCM) information is key to businesses identifying which workforce investments will drive long-term value for different stakeholders – including their employees, as well as managing risks to both staff and the business linked to the poor management of people.

For example, data on the demographic profile of the workforce at different levels – on training and development, recruitment and staff turnover costs, and employee engagement, linked to information on firm performance – can indicate where and how investment in people can add value.

This type of information can give investors key insights into whether boards view the workforce as a strategic asset, and how value is maintained, and risks mitigated.

Just as importantly, this information can provide workers with information on the:

- extent to which an employer values their workforce
- steps taken to improve inclusion and diversity
- steps taken to invest in their training and development and wellbeing.

The importance of this type of information was also highlighted in the Financial Reporting Council's (FRC) report on corporate culture, which explored how organisations can create cultures that ensure employees have effective voice and can speak out on their concerns, and support sustainable performance.

Unfortunately, the quality of external workforce reporting among UK-based publicly listed companies is, overall, mediocre at best, despite some exemplary companies. A recent assessment of workforce reporting among FTSE firms by the FRC's Reporting Lab highlighted that there was a lack of consistent disclosure on workforce matters, and that a gap remains between the reporting investors are looking for and what is being disclosed.

The CIPD is currently working in partnership with the Pensions and Lifetime Savings Association on a project exploring the quality of workforce reporting post-COVID-19 and how to improve this area of practice. What seems clear is the need for guidance to ensure greater consistency of reporting to ensure that essential data – for example, on the diversity and make-up of the workforce; employee relations and wellbeing; reward; training and development – is always presented.

Recommendations

The Financial Reporting Council should work with key stakeholders to develop best practice guidance to improve the consistency and quality of workforce reporting.

11 Skills policy reform

This paper has primarily been concerned with the demand side of skills:

- how to raise employer demand for investment in skills and improve people management and development capability to ensure people's skills are used more effectively in the workplace.

It's highlighted why this is so important in the context of the Government's Skills for Jobs white paper to meet the objective of putting employers at the heart of the further education system. It's also suggested the business support improvements needed to make this happen.

However, it's clear there's also a need for significant changes to the supply side of skills policy to improve workplace productivity. Although there is not space here to explore skills policy in detail, two areas in particular require urgent attention in the context of a strategy to improve workplace productivity:

1 Improved careers advice and guidance

Effective careers advice can ensure that there's a better fit between the qualifications and skills people have and the jobs available, which evidence finds can help improve productivity. For example, the OECD has found *'that the UK could improve its productivity by 5% or more if it reduced the level of skills mismatch to that of high performing international competitors'.*

However, despite its importance, evidence suggests that the quality of careers advice and support for young people in the UK is inadequate. Forthcoming CIPD research shows that the overall quality of careers advice and guidance for about half of young people while at school is either poor or non-existent. It also found that, while most young people received support on applying for university, only 3% received help to understand the labour market, jobs and salaries. Likewise, just 1% received support or help on applying for an apprenticeship while at school, even though a majority of those who went on to attend university said they would have been open to this route instead.

To address this, the CIPD is calling for the Government to invest an additional £23 million a year to ensure that all year 11 students have had at least one face-to-face career guidance session. Evidence suggests that the longer-term return on this investment would be significant. Research commissioned by the Careers and Enterprise Company suggests that, for each £1 the Government invests in personal guidance, it should be confident of recouping at least £3 and, most likely, much more.

2 Apprenticeship Levy reform

There's a pressing need to reform the Apprenticeship Levy into a more flexible training levy to encourage and enable employers to use the funding for a wider range of skills development and training, as well as apprenticeships.

CIPD analysis finds that the Apprenticeship Levy has failed on every measure, with data showing that, since its introduction, there's been a reduction in total apprenticeship starts and in the number of apprenticeships going to young people. There's also been a fall in the number of small firms using apprentices and in overall employer investment in training, which the levy was supposed to boost.

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CIPD research suggests that a more flexible training levy would help:

- boost employer investment in skills
- foster employer engagement with further education colleges
- support workplace productivity improvements.

Data from the CIPD's summer 2021 *Labour Market Outlook* survey of 2,000 employers found nearly three in ten (28%) large employers with 250 or more staff reported that this change would boost their engagement with FE providers. Levy flexibility would help employers fund their employees through training in further education colleges, as many technical and vocational courses are not apprenticeships. This change would ensure funding is better tailored to both employer and learner needs, and help meet the ambition of the Government's Skills for Jobs white paper to put employers at the heart of the skills system.

Previous CIPD survey data finds that this policy change would support efforts to improve firm productivity. This showed that nearly half of large employers report that reforming the levy to a more flexible training levy would help them improve workplace productivity and business performance to either a great (23%) or moderate extent (23%). Just 13% of large firms employing 250 or more staff said that reforming the levy in this way would have no impact on productivity or performance.

Recommendations

- Reform the Apprenticeship Levy into a more flexible training levy.
- Government to invest an additional £23 million a year to ensure that all year 11 students have had at least one face-to-face career guidance session.

12 Developing a coherent UK productivity strategy

This paper has set out the case for a long-term strategy to enhance business improvement and workplace productivity and the type of policies that would underpin this.

Given that different areas of policy – such as innovation, economic growth, employment, labour market regulation, and skills (both supply- and demand-side) – are interdependent, this strategy would need to be informed by the Government with input from different departments and key external stakeholders to ensure that a systemic approach is adopted.

Data from the OECD demonstrates that policy decisions that are well informed by evidence and analysis, and underpinned by community understanding, are more likely to be successfully implemented and to achieve good outcomes than those that are not. However, in the UK, *'the policymaking and implementation framework is institutionally complex and frequently changes with the political cycle'*, according to conclusions in a new paper, *The UK's Industrial Strategy: Learning from the past?* The paper goes on to observe that, *'rigorous evaluation of evidence and a subsequent mechanism for learning from outcomes are not institutionally embedded into the process. The practice of engaging*

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stakeholders and incorporating consultations from expert groups and relevant interests is done haphazardly, with little understanding as to how the information derived from these discussions are actually incorporated into the policymaking process.'

Consequently, to address these weaknesses, there's a strong case for the development of a UK Productivity Commission to ensure that strategies and policies to improve the country's productivity are developed with input from across government and other key stakeholders. This would combat the risk of policy development happening in political or departmental silos and improve systemic thinking about both challenges and solutions over longer time horizons than the political cycle. To function effectively, it would need to be independent of government but have a ministerial sponsor and established for the long term, with terms of reference jointly agreed by government and members of the commission.

The Productivity Commission's first task, once established, would be to undertake a broad review of policies that are material to productivity, and develop an economy-wide strategy to boost productivity growth.

Disseminating best practice

The creation of a Productivity Commission and a coherent strategy to enhance business improvement and workplace productivity, underpinned by the right policies and investment, would dovetail well with a more co-ordinated drive to improve and disseminate good practice.

This could be developed through the formation of a Business Productivity Forum, which would:

- represent business bodies, professional institutions and associations, and trade unions
- have a core purpose of supporting the work of the Productivity Commission.

Collectively, bodies like the Confederation of British Industry, the British Chambers of Commerce and the Federation of Small Business, together with organisations like the CIPD and Association of Chartered Certified Accountants, reach and influence hundreds of thousands of businesses every year.

They can highlight the business case for greater investment in new technology, management capability and workforce skills, and provide the knowledge on how to do this through guidance and training and embedding professional qualifications and standards.

The development of a Business Productivity Forum could help these bodies collectively collaborate and work together with the Government on evidence-based productivity growth priorities to maximise impact and prevent duplication of effort.

This forum, supported by a small government-funded secretariat with a rotating chair drawn from members, could be used to feed into public policy development at an early stage, and to collectively agree priorities and joint campaigns to improve practice.

Recommendations

- The Government should establish a UK Productivity Commission to develop strategy and policy on productivity growth.
- The Government should sponsor the creation of a Business Productivity Forum to help boost productivity and disseminate good practice.

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13 Conclusions

This paper suggests that there needs to be a major rethink in how to boost productivity growth in the UK. It highlights evidence showing why the current narrow focus on boosting investment in infrastructure and R&D and in certain high-tech sectors and industries is unlikely to be sufficient in itself to boost overall productivity or address regional economic inequalities.

A growing body of evidence suggests that unless far more firms improve their management capability (particularly on people management) or invest in technology or workforce skills development, efforts to lift the country's productivity will continue to face a strong headwind. Greater investment in these areas is also key to:

- supporting economy-wide innovation
- creating better-quality and higher-paying jobs
- fostering flexible and inclusive workplaces.

The Government's Plan for Growth and accompanying innovation strategy both identify the importance of improving productivity and innovation across the economy by supporting improvements to management capability and the adoption of new technology. But its policies to achieve this are small-scale and inadequate relative to the challenge. Likewise, its proposals on further education reform, while positive, fail to address more substantive failings in the skills system.

At the heart of the challenge of addressing firm-level productivity is how hard it is to encourage, incentivise and enable businesses at scale – particularly, but not exclusively, SMEs – to take steps to improve their productivity.

A combination of complacency, lack of knowledge about their own weaknesses (with people management a particular Achilles' heel), and a lack of time and resources, act to prevent too many business leaders from investing in (and improving) their companies. Even where there is the recognition of the need to act and the will to do so, achieving meaningful improvement is very difficult to achieve without effective support.

To address this, the paper concludes that there's the need for a UK-wide productivity strategy to enhance the business environment and build greater demand among many more employers to invest in the management capability, skills and technology needed to boost performance.

It suggests that the creation of a Productivity Commission could help inform the development of a more cohesive workplace productivity strategy and policies. This type of body could ensure there is a more systemic approach to addressing the UK's productivity challenge which recognises the interdependence of policies on innovation, economic growth, employment, employment relations, labour market regulation and skills.

The paper makes some specific policy recommendations on the type of policies that would be required to underpin this strategy and to drive demand for more employers to invest in business improvement. These include the development of enhanced, accessible and flexible business consultancy support at a regional level and improved sector-based support to increase employers' capability and appetite for business improvement.

Perhaps the greatest lever to address the demand-side failure by firms to invest more in people management is through a revamped labour market enforcement system with a much stronger focus on supporting employers to comply with regulation and driving up employment standards. Evidence suggests that fairly basic changes to employers'

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people management practices to support compliance with employment regulation can in themselves help increase firm productivity.

The recommendations would require additional investment from the Government of around £200 million a year. However, the potential return is high over time. The Business Productivity Review estimated that boosting the productivity of the UK's small and medium-sized businesses to match that of Germany could add up to £100 billion to our economy. The Institute for Government has estimated that the productivity slowdown between 2008 and 2018 equates to a loss to the UK economy of £300 billion, highlighting the potential value of even marginal improvements to workplace productivity across the economy.

Policy-makers are comfortable making big bets on productivity-enhancing investments in physical infrastructure, such as the £100 billion latest estimated cost of HS2, or increasing R&D spend to 2.4% of GDP. The analysis in this paper suggests that there is an equally strong case for additional, relatively small-scale investment to help raise firm-level productivity across the economy. There would need to be a long-term commitment to a workplace productivity strategy, given that significant benefits would be unlikely to be realised for at least five to ten years; however, this would be a shorter timeframe than the return on many investments in major physical infrastructure

The alternative is that the Government simply waits and relies on enhanced R&D investment paying dividends in the form of game-changing scientific or technological breakthroughs or the potential benefits of projects such as HS2 starting to come through in the 2030s. Given UK governments have broadly relied on the same ingredients to boost productivity growth for the last two decades with disappointing returns, it could be a long, unproductive wait.

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