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HOW CAN THE NEW GOVERNMENT WORK WITH BUSINESS TO DELIVER MISSIONS?

DISCUSSION PAPER

ANDREW O'BRIEN

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15 Whitehall, London, SW1A 2DD
T: 020 3878 3955
hello@demos.co.uk
www.demos.co.uk

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FOREWORD
BY TOBY PELLEW

The recent General Election has delivered the biggest change to the UK's political landscape for a generation and with it, a fundamental shift in how business will engage with policy makers moving forward.

The government's primary challenge is to deliver higher levels of economic growth, increase investment in public service and improve living standards across society. Labour has long spoken about how 'mission-driven government' will help achieve this and partnership with business to deliver the missions has been a centrepiece of the policy.

At Headland, we are powered by collaboration. In our recent report, the Collaborative Corporate, we proved that businesses benefit from a 'collaborative advantage' if they are able to strengthen their relationships with stakeholders, including government, through shared transformational goals.

We are very pleased to be partnering with Demos which takes this thinking a step further. Partnership in Practice outlines barriers and potential policy options that the new government will need to address to create a supportive environment for collaboration between the public and private sectors, in order to deliver the missions.

It is clear that to meet the ambitions of Keir Starmer's administration, we need a new framework where government genuinely partners with the private sector to understand the motivations of shareholders, business leaders and investors; and at the same time, where businesses are honest about their strengths and weaknesses and what can be achieved. That framework does not yet exist, despite warm words on both sides.

This paper is the starting point for a discussion about how to address this gap. In the coming weeks, we will be establishing the British Partnership Council, bringing together government, businesses and other experts to understand how we can put the shared desire for partnership into practice. We look forward to updating on our findings soon.

Toby Pellew

Partner and Head of Public Affairs

Headland

EXECUTIVE SUMMARY

The new government is pursuing a different approach to governing, what it calls "mission-driven government". Key to achieving this is a strong partnership with business, because without the resources and expertise of the private sector, it will not be possible to deliver the missions.

However, this has been something that UK Governments have struggled to achieve for several decades. For example, for every pound of government investment spent, business invests around £3. In contrast, Germany and France both achieve levels of business investment at **double the rates achieved by the UK.** If the UK could match French levels of ratios of government/business investment, the UK would leap from the worst performing country to the second best performing country in terms of investment.

This is partnership in practice.

We have identified six barriers that need to be tackled in order to encourage stronger partnership working:

1. Lack of coherent long term plan for the economy
2. Policy instability
3. Ineffective incentives
4. Cultural immaturity
5. Excessive short-termism in business
6. Lack of shared institutions

In order to address these barriers, we have identified six policy options that a new government should explore:

1. Publishing a Medium Term Economic Strategy
2. 'Policy Locks' to tackle policy instability
3. A comprehensive review of tax incentives
4. Conditionality to create new expectations of business
5. An updated Companies Act
6. A new shared institutional architecture

Getting the environment for partnership between government and business will require changes on both sides. Businesses need to become more collaborative and think about the wider interests of society. Government will need to be more deliberative in the way that it develops policy and commits to long term plans.

Demos, supported by Headland, will be convening a series of roundtables through our *Business Partnership Council.* This will bring together government, businesses and other experts to understand how we can put the shared desire for partnership into practice.

This paper is a contribution to begin that conversation and to lay out how mission-driven government can be made reality in partnership with business.

A NEW APPROACH TO GOVERNMENT AND BUSINESS PARTNERSHIP

Everyone in politics, business and academia agrees on one thing: We need to achieve higher levels of economic growth in the UK economy over the next decade if we want to significantly improve living standards and increase investment in public services.

The central question is how?

At the core of the new government's approach is what it calls 'mission-driven government'.

According to the Labour Party's General Election Manifesto, "[m]ission-driven government means raising our sights as a nation and focusing on ambitious, measurable, long-term objectives that provide a driving sense of purpose for the country."[1] Prior to the election, Demos has been engaging with Labour and other experts to understand how mission-driven government can be delivered, with a particular focus on partnership with business.

Supported by Headland, we have developed the following discussion paper on the key challenges, barriers and policy options that the new government needs to consider in resetting the relationship with UK plc.

This paper will inform our new *Business Partnership Council* as it seeks to convene government, business and other stakeholders to understand how we can put the aspiration for greater partnership working into practice. The Council will be meeting over the Autumn 2024 and publishing further papers related to some of the urgent challenges and opportunities confronting policy makers.

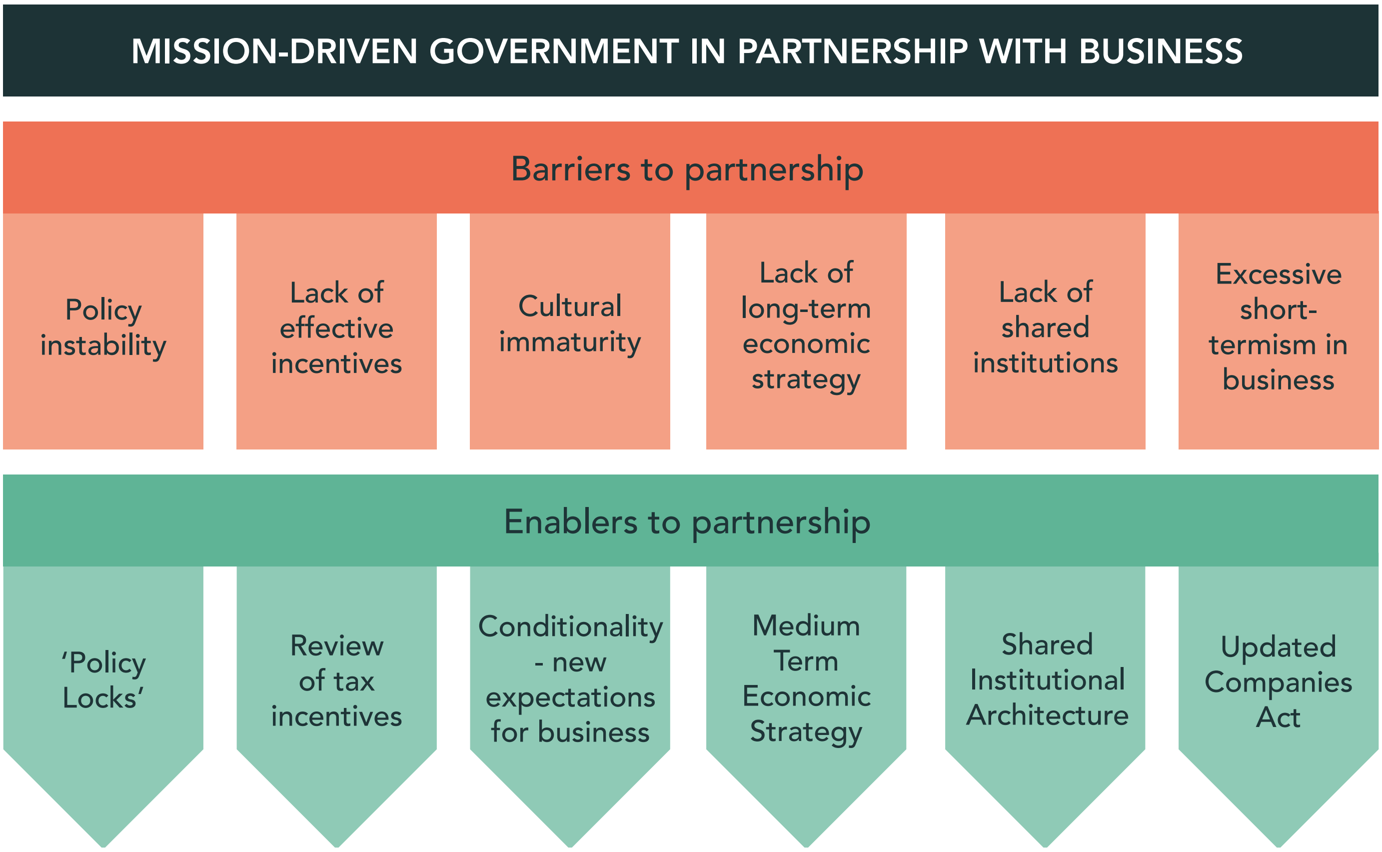
In designing the right policies to build stronger partnership between business and government, we need to identify the barriers that need to be overcome.

1 Labour Party, Change: General Election Manifesto 2024, June 2024

In this paper, we outline six barriers and six potential policy options that the new government will need to address to create a supportive policy environment for collaboration between the public and private sectors.

We also outline some potential policy options to tackle these challenges. However, to grow the economy and achieve the government's missions, we will need to deep dive into key sectors. This will be the next stage of the Business Partnership Council's work.

FIGURE 1



REALISING THE FULL POTENTIAL OF BUSINESS

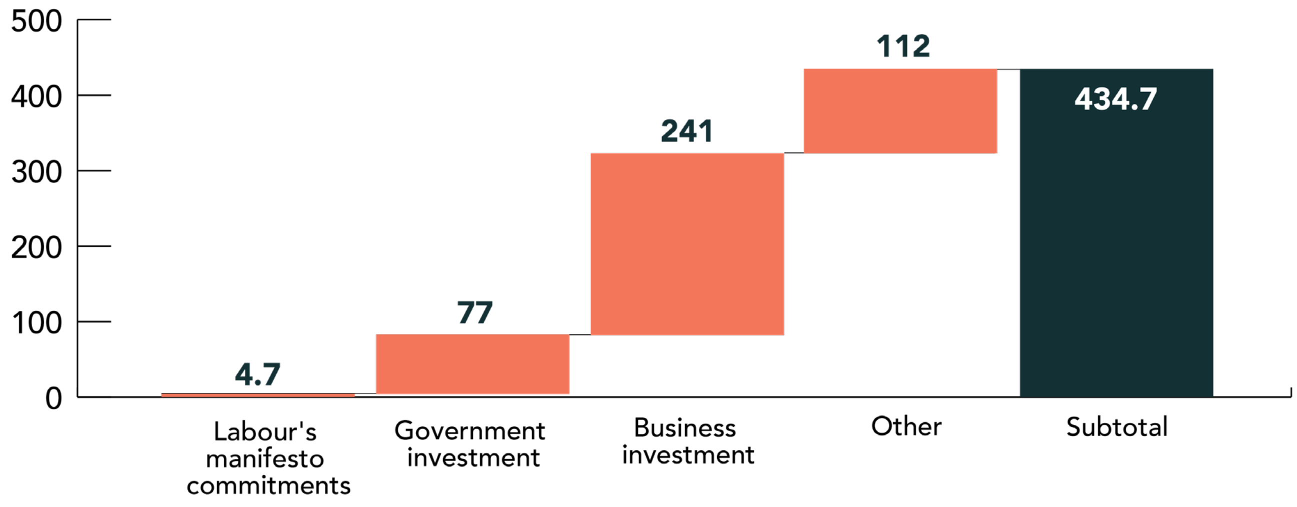
The government's five missions are ambitious goals to transform major parts of the UK economy and public sector.

As outlined in Labour's manifesto, "[s]ustained economic growth is the only route to improving the prosperity of our country and the living standards of working people. That is why it is Labour's first mission for government." Central to achieving mission-driven government is a new approach to business, "an enduring partnership…to deliver the economic growth we need."[2] Although partnership with business is required for all the missions laid out by the government, we focus primarily on the first mission: growth.

Figure 2 shows why missions require a new partnership with business. Labour's own investment plans are equivalent to just 1% of the UK's current annual investment. In crude terms, Labour's own plans are simply a rounding error in accounting terms and will not make a significant difference to the UK's growth rate alone. To make an impact, Labour needs to get businesses to co-invest alongside the government.

2 Ibid.

FIGURE 2
GROSS FIXED CAPITAL FORMATION BY SECTOR AND TYPE OF ASSET, 2023 (£BN)

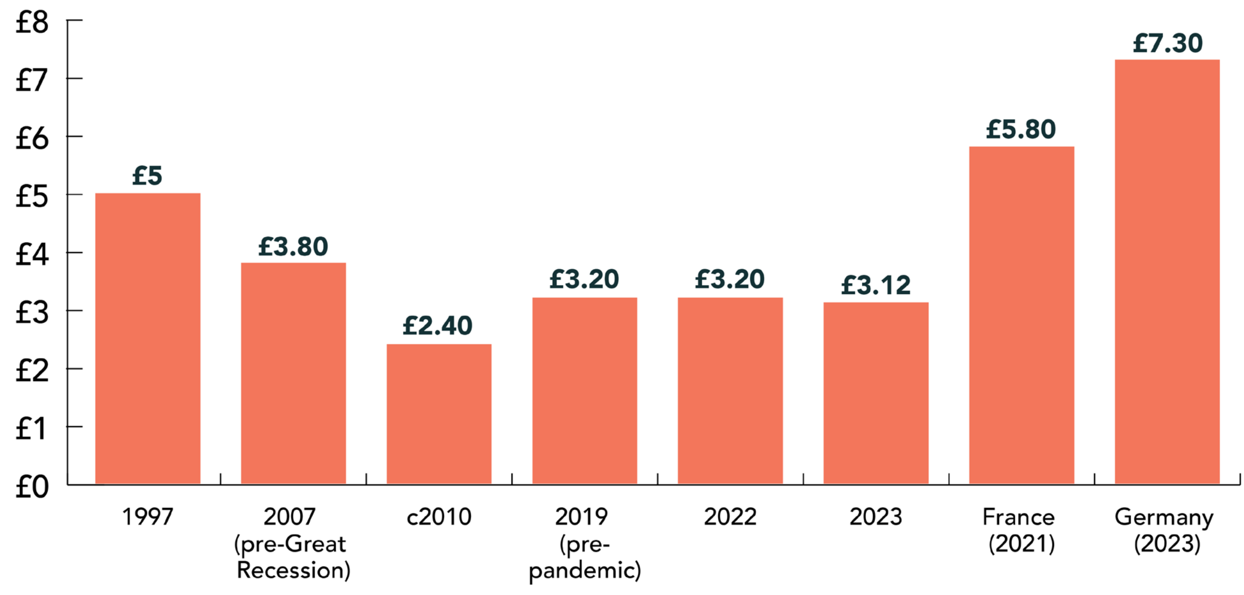


Source: Office for National Statistics & Labour General Election Manifesto 2024

However, this has been something that UK Governments have struggled to achieve for several decades. The ratio of investment between government and business investment has fallen by 38% since 1997, as highlighted in Figure 3.

The good news is that the data also shows that there is *huge potential* to boost the UK economy with the right relationship in place. Germany and France both achieve levels of business investment per pound of government investment at almost ***double*** the levels achieved by the UK. If the UK could achieve a ratio of business to government investment equal to those achieved in France then based on current levels of investment, **the UK would leap from the worst performing country to the second best performing country in terms of investment**, just behind Japan.

FIGURE 3
GROSS FIXED CAPITAL FORMATION (BUSINESS) PER POUND OF GOVERNMENT INVESTMENT



Source: Author's analysis - Office for National Statistics, Federal Statistics Office of Germany, Institute for Fiscal Studies

The UK is simply not maximising the true potential of the private sector and this hampers every policy objective the UK government is trying to achieve. We need to create a supportive policy environment for collaboration between government and business. To do this, we need a clear-eyed assessment of the barriers to building effective partnership working.

BARRIER 1
LACK OF COHERENT LONG TERM PLAN FOR THE ECONOMY

A major feature of the new government's approach to business engagement is the development of missions. However, 'mission-driven government' is just one of a succession of economic strategies that the UK has sought to implement since 1997. Below outlines, in broad terms, recent approaches deployed to generate economic growth and partnership model with business.

FIVE UK NATIONAL ECONOMIC GROWTH STRATEGIES SINCE 1997[3]

1. **New Labour - Macroeconomic stability, financial services and public investment (1997-2010):** economic growth was to be driven through significant increases in public spending, particularly in education and health, alongside 'fiscal prudence' (e.g. keeping public borrowing affordable). Unfortunately, this was disrupted by the global financial crisis. In this approach, economic strategy was primarily market-led.

2. **Coalition Government - 'expansionary fiscal contraction' and tax cuts (2010-2015):** sought to maintain macroeconomic stability but believed that excessive government spending had 'crowded out' the private sector and also made borrowing more expensive which in turn reduced investment and long term productivity. The solution was to hold down public spending to free up space for private investment and cut taxes for business to create incentives, so-called 'expansionary fiscal contraction'. In this approach, economic strategy was primarily market-led.

3 Adapted from A O'Brien, The Purpose Dividend, October 2023

3. **May & Johnson Ministries - active state and infrastructure spending (2016-2020):** a shift towards an active industrial strategy (e.g. creating new institutions such as Advanced Research and Invention Agency, ARIA) to back particular sectors combined with even higher levels of public investment. Net public sector investment was proposed to increase by 78% from 2019- 20 to 2024-25, returning back to levels seen under New Labour. Business tax cuts were halted and the tax burden on business increased. In this approach, economic strategy was more state-led.

4. **Sunak Ministry - technology and tax cuts (2022-2024):** sought to achieve higher levels of growth through embracing new technologies (like AI) and investing in key skills such as maths. A renewed focus on lowering business and personal taxation in order to drive growth and encourage investment. In this approach, economic strategy returned to being more market-led.

5. **Mission-driven government and macroeconomic stability (2024-?):** Labour's five missions, including a mission to achieve the fastest growth rate in the G7, will now be the primary goal, with greater coordination of government and business activities through policies such as the National Wealth Fund and Green Prosperity Plan. Missions are also expected to give greater levels of stability. In this approach, economic strategy is returning to being more state-led.

The chop and change in strategies since 2016 has made it hard for businesses to know what the government's overall economic approach is and this has made designing effective policies difficult.

POLICY OPTION 1: PUBLISHING A MEDIUM TERM ECONOMIC STRATEGY

The new government has started well through a clear articulation of its missions, but more needs to be done to clarify its economic model and this will determine *what kind of partnership* it wishes to create with business and its theory for growth. The Chancellor's recent Mais Lecture provides some hints about how she thinks economic growth can be achieved, but there are also tensions within it.[4]

Understanding how the government understands the pathway to economic growth is essential information for business, in order to enable effective communication between both sides. Governments have done this in the past (e.g. Wilson's 1964 National Plan). This guided overall policy making. However, in recent decades, economic strategy has been something articulated more in unofficial settings, such as the Mais Lecture, rather than in public documents. This creates uncertainty about the status of these policy statements.

The new government should consider developing an official Medium Term Economic Strategy to cover the next seven years. This should outline how the government assesses the strengths and weaknesses of the UK economy, how it intends to achieve growth and its overall economic strategy. This would give business confidence in the overall direction of travel and understand how it can best engage with the government in policy development as well as highlighting any potential misunderstandings.

4 A O'Brien, There are three speeches in Reeves' Mais Lecture - which will she govern with?, 21 March 2024

BARRIER 2
POLICY INSTABILITY

A key barrier to partnership working between business and government has been high levels of policy instability. In her Mais Lecture, the Chancellor said that "political and policy instability" had become the "new 'British disease".[5] Housing is a classic example. There have been 16 Ministers for Housing since 2010, which previous ministers have highlighted is a barrier to policy stability.[6] In the King's Speech, Labour has promised a new Planning and Infrastructure Bill to "unlock more housing" as an "enabler of growth".[7]

The National Planning Policy Framework (NPPF) was created in 2012 to bring together over 1,000 pages of planning guidance which was considered to be too burdensome. The NPPF at the time was considered to be a "pro-growth" document, which would stimulate more house building.[8] Policy instability emerged in 2018, where the NPPF has been revised five times in the space of five years, twice in 2023 alone. These changes have led to a significant reduction in planning approvals for new homes, with the number of housing units approved for building falling by 37% between Q4 2018 and Q1 2024 according to the Home Builders Federation.[9]

Moreover, as Demos found in our report, *The Triple Dividend*, the UK has not had a consistent policy to improve our existing housing stock. 81% of our housing stock was built before 1990 and the majority of the homes that will be living in over the coming decades have already been built.[10] Consequently, UK homes are poorer quality than many of their peers in the most developed economies.[11]

Lack of policy stability has created a growing gap between the investment we have generated and the investment we need. Investment levels have remained relatively flat. Between 1997 and 2009, private investment in dwellings averaged £73.5bn per year. Between 2010 and 2023, private investment in dwellings was £77bn per year.[12] Building 1.5m homes over the next Parliament will

5 R. Reeves, Mais Lecture 2024, 19 March 2024
6 Sky News, 16 housing ministers in 13 years - has it stopped the job getting done?, 14 November 2023
7 HM Government, The King's Speech 2024 - Background Briefing, July 2024
8 Holmes & Hills Solicitors, The National Planning Policy Framework: still pro-growth?, 23 July 2012
9 Home Builders Federation, New Housing Pipeline - Q1 2024, accessed July 2024
10 Centre for Ageing Better, Good Home Inquiry, 2021
11 A. Corlett & L. Judge, Housing Outlook Q1 2024, Resolution Foundation, Mar
12 Office for National Statistics, Gross Fixed Capital Formation by sector and type of asset, chained volume measure, seasonally adjusted, 28 June 2024

require an enormous increase in private sector investment. Based on current investment levels[13] and data on dwellings started,[14] **to achieve Labour's target, overall investment in housing may need to increase by up to 70% per year over the next five years.** A significant period of policy stability is likely needed to achieve this. This is true for a range of policy challenges, including infrastructure, skills and boosting exports.

POLICY OPTION 2: 'POLICY LOCKS' TO TACKLE POLICY INSTABILITY

One way that stability could be created is through the development of 'policy locks', which provide protections for key policy areas from being changed over a set period of time and if certain conditions are met.

The UK has experimented with locks in fiscal policy for some time, the most famous being the 'Triple Lock' for pensions which guarantees that they will rise by inflation, earnings or 2.5% whichever is highest. This lock has been remarkably resilient to change, despite economic instability, partly because it has been clearly communicated to the public but also the principle of a 'lock' is to make a commitment thats value is in the fact that it is not subject to change.

Planning reforms are one area where a policy lock process could be beneficial. Labour has promised planning reform, but as important as the reforms is the stability of the system. Once the reforms have been completed, a 'policy lock' mechanism would help to give businesses the confidence that they need to invest in the future. In the case of planning, given how long projects take to get off the ground and build, this lock should be as long as possible (e.g. seven to eight years) so that stability is baked into the system.

A 'policy lock' in this scenario would be similar to the triple lock for pensions, with ministers at the outset of the policy development publicly outlining how long the change will be 'locked in' for (e.g. five years) and building in an independent review of the policy for the end of that period to inform further changes.

A policy which has been 'locked' would only be open to change if certain conditions were met which are outlined at the beginning of its announcement (e.g. a severe economic downturn, a failure to achieve certain targets). Apart from these conditions, the policy would not be open to further announcements or changes for that period.

Policy locks would be overseen by the Public Administration Committee in Parliament, which would monitor and report on whether any locks have been breached by the government.

Government could go even further and create a legislative framework for policy locks, whereby once a policy has been designated as 'locked', further changes are only possible through parliamentary approval. This may be particularly useful for major reforms, such as planning or the government's New Deal for Workers, which require long term patient private sector investment.

To make partnership between the public and private sector work effectively, it is important that the government gives up some of its power in order to change, in order to create certainty for businesses and a stable platform for partnership. The power imbalance between government and business will always exist, but the government can take steps to give businesses confidence that the policies which have been outlined will last more than a few years.

13 Ibid
14 Office for National Statistics, UK House building: permanent dwellings started and completed, 24 April 2024

BARRIER 3
INEFFECTIVE INCENTIVES

One way to encourage businesses to collaborate with the government is to put in place the right incentives. These can be tax reliefs, grant programmes or other forms of matched investment. Just as with the policy environment overall, there has been considerable instability in the government's approach to designing incentives for the private sector to invest in the UK.

The Annual Investment Allowance (AIA) provides a textbook example. The AIA enabled a business to deduct a qualifying item from a business' tax bill up to a certain amount. Table 1 shows how the AIA has changed since 2008.

TABLE 1

ANNUAL INVESTMENT ALLOWANCE LEVEL	TIME PERIOD	INCREASE/DECREASE ON PREVIOUS TIME PERIOD
£50,000	1 April 2008 - 31 March 2010	**N/A**
£100,000	1 April 2010 - 31 March 2012	**Increase**
£25,000	1 April 2012 - 31 December 2012	**Decrease**
£250,000	1 January 2013 - 31 March 2014	**Increase**
£500,000	1 April 2014 - 31 December 2015	**Increase**
£200,000	1 January 2016 - 31 December 2018	**Decrease**
£1,000,000	1 January 2019 - Present	**Increase**

Consistency alone does not, however, mean that the right partnership will be put in place. For example, corporation tax was consistently cut between 2010 and 2018, with the headline rate falling by 9 percentage points during that period. However, during that period in only one year (2015) did the increase in business investment offset the cost of the tax cut.[15] This frustrated policy makers because one of the reasons why this tax cut was introduced was to create an incentive for businesses to invest in the UK following several decades of underinvestment.

The UK also continues to have distortions in the tax system. For example, the differential tax rate between debt and equity investment means that companies are incentivised to take on debt rather than to raise equity capital for their business. According to the OECD, Britain and other developed countries tax debt-based finance 3.8-6% lower than equity investments.[16] The former carries greater risk for businesses than the latter. According to the OECD, UK non-financial businesses have debts totaling 4.8 times greater than their operating profits.[17] Research by academics has shown that excessive levels of debt can lead to a reduction in investment, particularly in the wake of financial shocks such as the financial crisis or the pandemic.[18] The Mireless Review, a review of the tax system in 2010, recommended an Allowance for Corporate Equity (ACE) to create incentives for equity investment, but despite research finding that this allowance would boost investment, it has never been implemented.[19]

POLICY OPTION 3: A COMPREHENSIVE REVIEW OF TAX INCENTIVES

The new government should use the development of its Business Tax Roadmap to have an open conversation with business and redesign the tax system to ensure that all our taxes, reliefs and expensing rules encourage long term investment.

Significantly increasing the Annual Investment Allowance and maintaining a high level of allowance for a long period (at least seven years) would give business the incentive to invest. The government should also explore an Allowance for Corporate Equity, as outlined above, to rebalance the way that investment is undertaken.

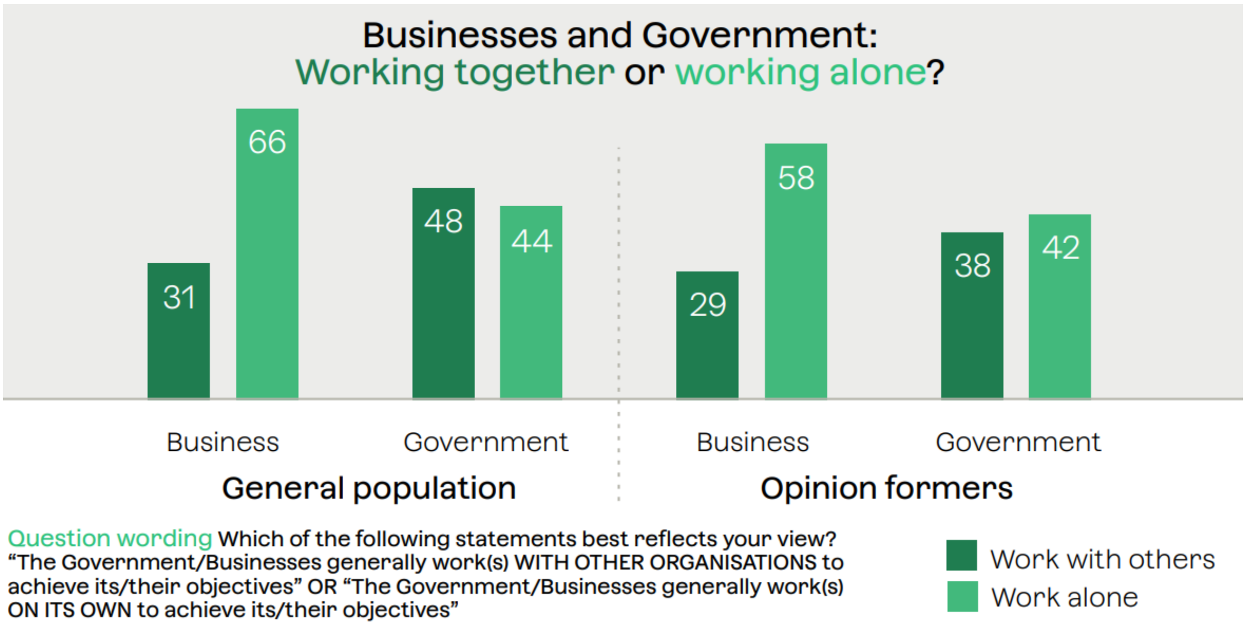
The UK should also consider expensing to include digital technologies, which are the key to growth. The UK is underperforming on the adoption and use of digital technologies compared to our international competitors. Untapped technology adoption could add £232bn to the UK economy.[20] The UK should adopt a similar approach to Australia by extending the full expensing of capital to digital technology investments, not just plant and machinery.[21] This would enable every business that invests in digital technology to cut their tax bill by 25p for every £1 that they invest. This would help the government to achieve its ambition to make the UK a global centre for science and technology.

15 A O'Brien, Bounce Back Britain, June 2020
16 The Economist, Why the bias for debt over equity is hard to dislodge, 22 January 2022
17 OECD, Non-financial corporations debt to surplus ratio, accessed July 2024
18 S. Kalemli et al, Debt overhang, rollover risk, and corporate investment: evidence from the European crisis, February 2019
19 A. Klemm, Allowances for Corporate Equity in Practice, International Monetary Fund, November 2016
20 Sage, Digital Britain Report, June 2022
21 Australian Government, Small business technology investment boost, 19 June 2024

BARRIER 4
CULTURAL IMMATURITY

The public, politicians and business know that the UK lacks a culture of collaboration that is the basis of successful partnership. Figure 4 shows polling from Headland's paper ***The Collaborative Corporate.*** This found that 66% of the general public and 58% of opinion formers believed that business generally works alone rather than with others.[22] As the Chancellor has outlined "As our world has changed, so must the relationship between business and government."[23]

FIGURE 4



Source: Headland

22 Headland, The Collaborative Corporate, November 2023
23 R. Reeves, Speech at Labour's Business Conference, 1 February 2024

There is clear evidence that collaboration is essential to achieving economic success. *The Collaborative Corporate* identified that businesses benefit from a 'collaborative advantage' if they are able to strengthen their relationships with government, consumers and competitors through shared, transformational goals.[24]

Labour has sought to develop national missions in collaboration with the private sector before, in particular the *National Plan* developed by Harold Wilson's government in 1964. We know that this is an example that Labour has explored in developing its own missions.

The National Plan is a *practical* example of trying to put partnership with business into practice. This shift was developed to replace the "stop-go economic policy" of the previous Conservative Government that saw significant policy instability.[25] Labour's view was that there was a lack of coordination between government, business and trade unions to ensure that investment was directed into the right industries and sustain growth. Wilson's attempt to correct this was through the use of 'indicative planning'. Essentially, this involved carrying out market research to understand potential growth opportunities, identify bottlenecks and then disseminate these findings throughout the economy to encourage investment. As noted by economic historian Jim Tomlinson, the "prime purpose was educational".[26] It was not conducted in a vacuum, the National Plan was based on "elaborate negotiations between government, trade union leaders, and employers."[27] Academic analysis in the wake of the plan found that the reason the plan failed was not excessive interference but a lack of government action, hamstrung by an immature culture that saw all government action as unwanted interference.[28] The same barrier could hold back missions today.

Is our culture better today? The evidence suggests that we have still not found the right balance.

The example of corporation tax reform is enlightening. In 2008, business leaders called for the headline corporation tax rate to fall from 28% to 18% within eight years in order to boost investment and growth.[29] The Coalition and Conservative Governments then put in place reforms to achieve this overall reduction in corporation tax rates, and go even further, reducing the overall rate to 17% by 2020.[30] However, despite the significant cost of this measure (over £80bn), the policy never achieved the aspirations outlined for it.[31] Even excluding the instability of Brexit, net investment between 2011 and 2016 increased by only £47bn, £27bn less than the overall cost of the tax cut.[32] Despite its failure to raise business investment, at no point did business groups call for the government to review this change or recommend alternative measures.

We need a grown up conversation where the government is not encouraged to just do whatever business demands and where businesses are honest about their strengths and weaknesses. Government also needs to engage more deeply with decision makers to truly understand the challenges and motivations of shareholders, business leaders and investors to create the right policy environment.

POLICY OPTION 4: CONDITIONALITY - CREATING NEW EXPECTATIONS OF BUSINESS

A challenge which the new government faces and that has dogged previous governments is that policy changes are often a one-sided gamble, with the government taking considerable risks (often financial) with no firm commitment from business. This is partly because of the fragmented nature of business. Ultimately, the government can speak with a single voice if necessary, but coordinating tens of thousands of firms is very challenging. However, it is also because of the approach that has been taken to policy development in the past which has placed limited expectations on business.

24 Headland, The Collaborative Corporate, November 2023
25 Labour Party, The New Britain, 1964
26 J. Tomlinson, Managing the Economy, Managing the People, Oxford University Press, 2017 p. 173
27 Ibid
28 J. Hayward, National Aptitudes for Planning in Britain, France and Italy, Government and Opposition, Vol. 9, No. 4, 1974, p. 406-407
29 Independent, CBI calls for major overhaul of business tax system, 10 March 2008
30 HM Revenue and Customs, Policy Paper: Corporation Tax to 17% in 2020, 16 March 2016
31 A O'Brien, Bounce Back Britain, June 2020
32 Ibid.

The UK can learn from the experience of COVID and other countries about embedding 'conditionality' into policy changes, something recently outlined by world renowned economists Dani Rodrik and Mariana Mazzucato.[33] During COVID, for example, in return for government backed loans, firms were restricted from undertaking certain activities such as share buybacks and dividend payments.[34] The United States' CHIPS Act, to stimulate advanced manufacturing, has put conditions on businesses to work in the United States, develop training for the workforce and not undertake any share buybacks or dividends for five years.[35]

Conditionality is something that can be more easily implemented in areas such as procurement and grant programmes where the government has direct control over spending. The new government has made a move in this direction through the British Jobs Bonus, for example.[36] We can call this *hard conditionality*, where contracts or grant agreements can be used to directly influence business behaviour in return for commercial success. The new government should make clear from the outset that conditionality of this kind will become a core feature of government spending, utilising legislation such as the Public Services (Social Value) Act.[37] The new government could also use hard conditionality to tackle issues such as late payments for small businesses to reduce cash flow concerns.

However, we can also create *soft conditionality* through other government levers, such as tax changes or regulatory reforms, where changes that are likely to benefit businesses or individual sectors financially are linked to wider goals (e.g. missions).

As outlined by Mazzucato and Rodrik, soft conditionality can be achieved through clear metrics and evaluation procedures. The government's proposed Business Tax Roadmap, for example, should be aligned to a clear set of targets for increased investment and workforce training spend and progress towards Net Zero. These targets should be updated alongside updates to progress on the Roadmap, using OBR forecasts and outlining whether the Tax Roadmap is on track to achieve the targets that have been set. If the UK is not on track to significantly boost investment, workforce training, Net Zero or other mission-related targets, then the government is within its rights to reverse the changes made and redeploy the spend elsewhere. Tax cuts and reliefs should be provided on a 'use it or lose it' basis rather than unconditionally. This can only succeed if there are clear, transparent policy objectives.

A partnership is only a partnership if both sides are prepared to make changes and commit to shared goals. If the government is prepared to reduce its flexibility to change policy to provide greater certainty for business, then businesses need to also be prepared for policy changes to be linked to specific goals. Both sides need to have 'skin in the game' if mission-driven government is to deliver a true basis for partnership, conditionality will help to ensure that both businesses and government have a shared interest in working together to deliver missions.

33 M. Mazzucato & D. Rodrik, Industrial Policy with Conditionalities, September 2023
34 Clifford Chance, COVID-19 UK Government Aid: Impact on Dividend Payments and Executive Pay, November 2020
35 M. Mazzucato & D. Rodrik, Industrial Policy with Conditionalities, September 2023
36 Labour Party, Starmer's Energy Ambition: How Labour's British Jobs Bonus will create jobs and boost investment into Scottish and UK energy heartlands, November 2023
37 See upcoming Demos report, Taming the Wild West - due to be published July 2023

BARRIER 5
EXCESSIVE SHORT-TERMISM IN BUSINESS

Government cannot ignore the structure and intent of business itself, a point recently made in Demos ***The Purpose Dividend.***

Professor Colin Mayer, Chair of the British Academy's *Future of the Corporation*, programme said that the UK has an "extreme form of capitalism" that focuses purely on financial return for shareholders rather than wider goals.[38] The Kay Review of UK Equity Markets and Long Term Decision Making found that businesses were excessively focused on short-term fluctuations on their share price and returns rather than long term value creation.[39] IPPR's Commission on Economic Justice came to a similar conclusion.[40] All this has led to lower levels of investment in the UK economy and made developing shared goals between government and business harder to achieve.

As the new Chancellor Rachel Reeves noted in her paper *A New Business Model for Britain* "there has long been a recognition that our corporate governance structures are an obstacle to investment and long-term planning."[41] The Prime Minister in his 2021 Labour Party Conference pledged to "change the priority duty of directors to make long-term success of the company the main priority… with the blessing of British business."[42] This commitment was also featured in Labour's Industrial Policy document.[43] Creating ambitious goals without reforming the structure of businesses to align it with them is likely to create challenges.

POLICY OPTION 5: AN UPDATED COMPANIES ACT

The UK's Companies Act will be twenty years old in 2026, in the middle of this new Parliament and the Act itself is historically subject to revisions every 15-20 years. It is highly likely, therefore, that Labour will have to update the Companies Act to ensure that the UK remains at the forefront of good corporate governance.

38 BBC News, UK 'has particularly extreme of capitalism', 27 November 2021
39 Department for Business, Innovation and Skills, The Kay Review of UK Equity Markets and Long Term Decision Making, July 2012
40 IPPR, Prosperity and Justice: A Plan for the New Economy - Final Report of The IPPR Commission on Economic Justice, September 2018
41 R. Reeves, A New Business Model for Britain - Building Economic Strength in An Age of Insecurity, May 2023
42 Labour List, "We can win the next election" - Keir Starmer's Labour conference speech, 29 September 2021
43 Labour Party, Prosperity through Partnership: Labour's Industrial Strategy, September 2022

One small change that the new government can make to better align business and government to create a strong partnership is through changing directors duties so that they align with the wider interests of society and the environment, alongside financial considerations. This change has been endorsed by over 2,500 businesses, academics and business groups such as Institute for Directors.[44] Updating corporate governance rules could make the UK more attractive to ESG investment, with assets under management by ESG funds predicted to rise to $40 trillion by 2030.[45] This would help boost investment in the UK.

Demos' report *The Purpose Dividend* estimated the economic impact that could be achieved if UK firms acted like 'purpose-led' businesses that sought to achieve a positive social and environmental impact alongside financial return. It found that if every business acted like a 'purpose-led' business, the economy could be up to £149bn a year larger than it is today.[46]

Businesses need to be given the *freedom* to collaborate with the government, without being driven in a particular direction by one of their stakeholders. Corporate governance reform is not simply about aligning business and government together but also creating the conditions by which businesses can effectively engage with the government.

Reform to the structure of business is an essential if partnership is to succeed over the long term.

44 https://betterbusinessact.org/
45 Bloomberg, Global ESG assets predicted to hit $40 trillion by 2030, despite challenging environment, forecasts Bloomberg Intelligence, 8 February 2024
46 A O'Brien, The Purpose Dividend, November 2023

BARRIER 6
LACK OF SHARED INSTITUTIONS

In recent years, governments have sought to create forums to bring business and the state together to work in partnership, However, these institutions have often had short life spans because they have been under the complete control of government. Getting the policy environment right requires, as the Chancellor has outlined, "getting the institutional framework right, and enshrining that core growth mission within our economic architecture."[47]

Institutions that include both government and business representation have rarely lasted. The Industrial Strategy Council, created in 2017, included the voice of business but was then abolished in 2021. The Inclusive Economy Partnership, a bringing together of 80 businesses and civil society representatives and convened by government, was set up in 2017 to tackle a number of shared challenges from mental health to financial inclusion.[48] However, despite initial success in bringing together business, civil society and government together to invest in these long term goals, the Partnership was sidelined by 2021 and its webpage has now been archived by the government, with its current status unclear.[49]

Labour has promised to put the Industrial Strategy Council on a statutory footing and create legislative protections for one of the new government's key institutions is one way to ensure their longevity and encourage business engagement. However, the legislative status of the organisation is not the only factor in determining partnership, partnership needs co-production of solutions where those affected by challenges actively help to build the solutions.

The story of Better Society Capital (BSC), created in 2010, is enlightening. BSC was set up to channel private investment into third sector organisations and to improve social outcomes through blending private and public finance. Unusually, however, it was co-owned by both the state and the private sector through the Merlin Agreement, with the high street banks investing £200m alongside over £400m provided through dormant assets.[50] This co-ownership of the institution meant that it needed to engage with both government and business stakeholders forging closer relationships between the public and private sectors. Since its creation, it has been able to unlock an additional

47 R. Reeves, Mais Lecture 2024, 19 March 2024
48 HM Government, Inclusive Economy Partnership: There's power in partnership, 2019
49 https://webarchive.nationalarchives.gov.uk/ukgwa/20211119162505/https://www.inclusiveeconomypartnership.gov.uk//
50 House of Commons Library, Project Merlin, 14 February 2013

£3bn in private investment to go alongside its initial resources and has longevity through its independence from government.[51] This is a level of matched investment from the private sector which the new government will be seeking to achieve. Where there have been challenges, it has been through the lack of engagement from government, despite it being an institution that was initially created through significant amounts of public money.[52]

Another challenge is the appointment process for business representation in these institutions. Labour, for example, has created a National Wealth Fund Taskforce to advise on the creation of its National Wealth Fund and brought businesses to advise on the British Infrastructure Council.[53] It is good that businesses are being appointed to work with the government, but we need to ensure that this is done in a transparent and inclusive way so that all relevant parties are around the table. Where possible, the government should work with Parliament to ensure that those appointed to advise on these projects are able to present their views and answer questions from MPs. This 'pre-appointment' session is standard for many roles in the public sector. Getting the appointment and engagement process right will not only ensure that we get a good balance of business perspectives around the table but also strengthen the legitimacy and longevity of these organisations.

POLICY OPTION 6: A NEW SHARED INSTITUTIONAL ARCHITECTURE

Stability, conditionality and corporate governance reform would all help to strengthen the partnership between business and government, but they need to be overseen with the right institutions.

The new government has outlined a number of institutional changes such as the creation of a mission boards. However, as noted above, institutions that have been purely sponsored by the government have come and gone regularly. These are unlikely to command business confidence. Learning the lesson from successful long term partnerships such as Better Society Capital, it is important that businesses feel ownership of the institutions that are being created and that they are inclusive of key stakeholders.

A new shared institutional architecture is essential for partnership to take root and be sustained over the long term. This needs to be at both a national and sectoral.

Placing the Industrial Strategy Council and National Wealth Fund on a statutory footing is a step in the right direction. However, the new government should also look at other key economic institutions such as UK Export Finance and ensure that these are genuine public-private partnerships. These institutions should be given independent endowments so that they can control their resources and sustain themselves through any temporary changes in government direction. Appointment processes also need to be open and transparent, giving a full range of business voices and experts to apply and serve and to ensure legitimacy, rather than based on the patronage of ministers.

Crucially, partnership requires institutions that enable a frank and free exchange of views about shared objectives. Government needs to be prepared to hear things that it does not want to hear from the bodies that it creates and enable them to make their views public so that they have legitimacy and credibility. The Industrial Strategy Council, British Infrastructure Council and other sectoral bodies need to have the freedom to raise their recommendations and views in public. This is the key lesson from the success of the Office for Budget Responsibility.

A new shared institutional architecture is critical if we are going to achieve effective partnership working between government and business.

51 Civil Society Media, BIg Society Capital changes name to 'better reflect its mission' 29 April 2024
52 Independent Commission on Social Investment, Reclaiming the Future, July 2022
53 https://www.greenfinanceinstitute.com/national-wealth-fund-taskforce/

NEXT STEPS

We are moving into a new era of partnership between government and business, with both public and private sectors looking to reset the relationship and create a new culture.

Time is of the essence. Putting in place the key changes will take time and will have a knock-on effect on the ability to achieve the missions. The sooner that we can take steps to build the right policy environment to support partnership between business and government, the sooner we can get on with the delivery of the missions and achieving a decade of national renewal.

This is why Demos, in partnership with Headland, is hosting a *Business Partnership Council* to bring government, businesses and other experts together to discuss how we can put partnership into practice.

To be more than words, partnership needs to focus on specific challenges and so over the course of the Autumn 2024, we will be hosting roundtables on the following areas:

- How government can coordinate with business on the missions
- How the UK can rebuild its infrastructure
- Harnessing science and technology to drive growth
- Building the workforce of the future
- Unlocking business investment to drive growth

All of these areas are essential to delivering mission-driven government. Papers from these roundtable discussions will be published providing the voice of business, government and other stakeholders on how we can build specific partnerships to tackle the biggest challenges and realise the biggest opportunities facing the country.

What is clear is that we need a new approach to collaboration between business and government.

The past provides lessons that we can learn from, but we need a fresh start. We need a new energy to build a new culture of collaboration.

Over the coming months, Demos and Headland hope to work with the new government and business leaders to inform the policy debate and provide practical steps for how we can build successful partnerships.

If you would like to participate and learn more about Business Partnership Council, please contact:

Andrew O’Brien
Director of Policy and Impact, Demos
andrew.obrien@demos.co.uk

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15 WHITEHALL, LONDON, SW1A 2DD
T: 020 3878 3955
HELLO@DEMOS.CO.UK
WWW.DEMOS.CO.UK