National Institute of Economic and Social Research

Productivity and Investment

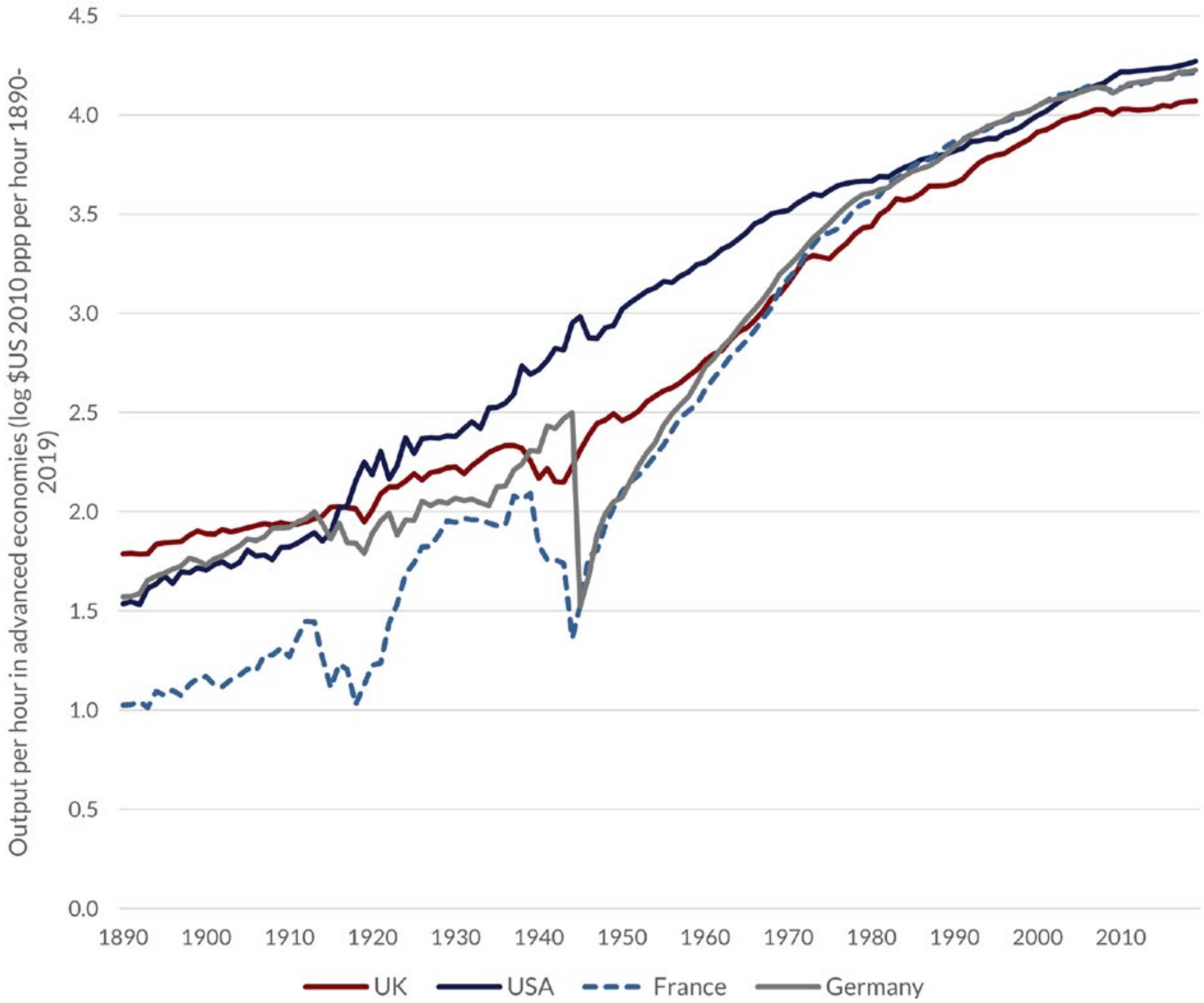
Time to Manage the Project of Renewal

Paul Fisher – March 2024

Re-Framing the Productivity Debate

- The slowdown in productivity is affecting all industrialised countries. When did it start? Taking the US as the best dating evidence, probably in the 1970s (see figure 2).

Figure 2 Comparison of productivity in logs



Source: Bergeaud et al., (2016).
Figure 2 transforms the data using a log scale.

THE PRODUCTIVITY INSTITUTE
PRODUCTIVITY COMMISSION

- Constant exponential GDP growth was never going to be sustainable.
- Concepts of productivity growth in manufacturing – such as quantity per labour hour – are simply not appropriate for services, where quality is a much more important component.
- Investment in the regions and nations of the UK should be supported where it is socially desirable and economically beneficial. But regional discrepancies are not the cause of the UK productivity slowdown, and addressing them will have little impact on that.
- GDP is becoming less and less appropriate as a measure of welfare and well-being as the economy matures and continues to de-industrialise.
- The productivity slowdown does create problems for the fiscal position, but reactions to that have been counter-productive. Attempts to reduce taxes, squeeze public sector spending and reduce national debt – sometimes in the name of promoting growth - have been producing the exact opposite (everywhere, not just in the UK).
- To make the public sector more productive requires more investment spending, not less. Simply squeezing budgets nearly always generates worse productivity outcomes – and that helps produce the perverse outcomes.
- Health and education provision could and should be slowly expanded as a share of GDP, through higher investment to ensure that both quality and quantity rise. This could happen by either public or private sector provision – that is a political choice. The UK is not trying to do either.
- Investing to improve economic outcomes, whether public or private, requires us to recognise the structure of the economy today and its direction of travel, not hark back to the ‘glory days’ of British manufacturing, which are long behind us.
- In services, and the digital economy, most of the investment needed is in people and in items such as intangibles, digital networks, cloud computing and AI - not in plant, machinery and IT spending which is the focus of current investment policy.
- In addition, the UK urgently needs to invest actively in the transition to net zero and beyond. This investment should not be portrayed as a net cost or a trade-off against growth. Failure to reverse greenhouse gas emissions globally risks bringing eventual economic disaster for everybody. The UK – as the original home of the industrial revolution - must be seen to be a global leader.
- We need to promote forward, rational, long-term thinking and be more activist in our investment strategy. That would require changes to many areas of policy from the fiscal framework to national and local planning.