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The Future of Manufacturing in Scotland

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The Future of Manufacturing Industry in Scotland

Introduction

An interesting thing started to happen after the financial crisis swept the globe in autumn 2008... politicians at Scottish and UK level started to talk seriously about manufacturing again. Indeed, a genuine commitment to examine how Government at all levels might more effectively support and nurture manufacturing has since been apparent in election manifestos and a blizzard of related policy papers has emanated from Whitehall and Brusselsⁱ.

This fundamental rethink of economic and industrial policy is long overdue. The 'financialised'ⁱⁱ economic model, pursued with particular vigour in the US and UK, failed on both economic and social grounds: the narrow focus on finance and the primacy given to financial market participants in the development and implementation of policy led to a lop-sided economy; one prone to systemic crisis. Also, the model didn't as was often claimed, lead to greater prosperity for all: it generated moderate GDP and productivity growth, an exponential rise in income and wealth inequality and a decline in social mobility.

And yet, the opportunity for genuine and substantial change already appears to be ebbing away. A full four years have now passed since problems first emerged in the US housing market but there has been no structural reform or effective re-regulation of the financial sector and the banks' business models remain largely untouched. Incredibly, the influence exerted by financial insiders on economic debate and public policy appears undiminished.

The STUC believes that a reinvigorated manufacturing sector is a necessary component of a new, fairer and more sustainable economic and social model. Contrary to prevailing economic orthodoxy, there is no reason whatsoever that this cannot be achieved through a mix of clever and focused Government intervention together with reform of the financial sector to ensure that it supports rather than undermines the productive economy. Other advanced economies have managed to maintain far higher levels of manufacturing employment than the UK.

Scotland benefits from a skilled, productive and committed manufacturing workforce and many outstanding manufacturing businesses across a range of sub-sectors. Scottish manufacturing has experienced a stronger and quicker recovery than services. The STUC believes with the correct policy framework in place, manufacturing can continue to grow; both nominally and as a share of the Scottish economy.

The purpose of this paper is to provoke debate and discussion about the nature and shape of potential levers to support the growth of manufacturing in the years ahead.

The current state of manufacturing in Scotland

The sudden collapse in demand which resulted from the global financial crisis of autumn 2008 hit manufacturing industry hard with the world's great exporting nations such as Germany and Japan suffering the biggest falls in output (if not employment – a point we'll return to later).

Scotland did not escape.

Output

- Over the course of the recession manufacturing GVA in Scotland fell by 11.44% during the recession, which is less than the fall of 14.58% in UK manufacturingⁱⁱⁱ.
- Against a background of a fall in Scottish GDP of 6% during the recession it is evident that some sectors suffered disproportionately. One must be careful of a direct comparison with the aggregate Scottish performance because the downturn began earlier or later in several sectors. Nevertheless, two sectors, chemicals and 'other manufacturing' lost 25% and 21% of their GVA respectively. And the loss of output in chemicals occurred in just 3 quarters. Of the six sectors experiencing contraction between 10% and 20%, three are export orientated manufacturing sectors: electronics, transport equipment and mechanical engineering^{iv}.

Employment

- In September 2010, 176,000^v people were employed in manufacturing industries in Scotland – 9% of the total Scottish workforce. This represents a fall of 37,000^{vi} since the start of the recession and is especially disappointing given that the rate of job losses had slowed significantly since the fallout from the Asian financial crisis led to a sharp decline around the turn of the century.

Exports



The above graph^{vii} confirms that, prior to the credit crunch in 2007, there had been encouraging growth in Scottish manufactured exports. The stabilization since^{viii}, whilst welcome, still leaves exports well below pre-recession levels.

What is manufacturing?

It is worth pausing to reflect on what is meant by the term 'manufacturing'.

"If you take a liberal view of the often seamless range of production and service activities which constitute modern manufacturing, the sector is probably significantly bigger than official statistics suggest – maybe twice the size measured by employment. And if a quarter of the workforce – instead of half that on the official count – depends largely or wholly on manufacturing, the sector's importance is considerably greater". What is Manufacturing? Michael Prest, Prospect, October 2008^{ix}

So comprehensive has been the industrial change over the last three decades that even the definition of a manufacturing business is disputed. The boundary between making things and selling services has undoubtedly become blurred.

National Statistics defines a manufacturing business by the value of the goods it produces. Essentially, a company is classified under 'manufacturing' if more than half its revenue comes from making things. NS's classification system covers manufacturing in 13 categories broken down into 258 sub classes.

As Prest notes, a '*major problem is that these definitions of manufacturing and employment – however frequently and accurately they are updated - do not capture jobs and activities which depend on, or are closely allied to, manufacturing; for example, design work undertaken by a specialist non-manufacturing firm*'^x.

Nor do they clearly capture the balance between ‘manufacturing’ and ‘services’ within a company. It is possible for a company to have more than half its revenues generated by manufacturing but a minority of employees directly engaged in making the product. This is common in science based industries such as pharmaceuticals.

Recommendation

Classification by principal economic activity is the fundamental building block for the industrial classification system at UK national and international level. This is unlikely to change but the STUC agrees with the Work Foundation that:

- Wider measures of activity by manufacturing firms in the UK and Scotland require to be developed in order that manufacturing’s economic contribution is sufficiently recognized and to provide an evidence base which adequately supports public policy interventions.

High value/low value manufacturing

“Manufacturing has a strong future. That future is based on generating high value – to the company, to shareholders and to the country. High value manufacturers have strong financial performance, are strategically important and have positive social impact” IfM, University of Cambridge

“The UK along with other OECD countries has successfully retained large ‘low tech’ manufacturing sectors and we should build on the comparative advantage that implies...in knowledge based manufacturing we also need a ‘low tech’ strategy to complement the traditional ‘high tech’ one” Work Foundation, Manufacturing and the Knowledge Economy

Policy development has understandably focused on ‘hi-tech’ manufacturing given the positive spillovers it generates for the wider economy. Unfortunately, too often policy has also been informed by the lazy assumption that low-tech manufacturing will necessarily migrate from Scottish shores as a result of low wage competition. As the Work Foundation quote above illustrates, ‘low tech’ sectors in Scotland such as food and drink and textiles continue to provide significant levels of employment. This implies strong comparative advantage; often derived from a ‘Made in Scotland’ premium.

In 2006, the low tech manufacturing sector in the UK accounted for over 4 times the employment of high tech and over twice the value added.

In any case, current classifications of ‘high-tech’ and ‘low-tech’ manufacturing are unhelpful in clarifying the nature of the production process because they are based on investment in only one type of knowledge asset: R&D. The STUC would question to what meaningful extent an industry such as whisky can be defined as ‘low-tech’?

Why is manufacturing important?

“A broadly based economy with high-value manufacturing as a component is likely to be more resilient than a narrowly based one. It provides the environment most likely to support innovative, new businesses and retain valued, existing ones. It also ensures that academic innovations have some chance of reaching the market and therefore creating value in the nation that provided the funding”. Sir John Rose, CEO, Rolls-Royce^{xi}

“With 3m jobs spread around the country – a good number in the middle income category – manufacturing is a force for social cohesion in a way that financial services are not”. Richard Lambert, Director, CBI^{xii}

One of the cruelest aspects of the 2008/09 recession is that while the banking industry staged a spectacular comeback on the back of Government support and guarantees, reduced competition and cheap money, manufacturing suffered real and potentially lasting damage. As mentioned above, Scotland has lost 37,000 manufacturing jobs since the start of the recession and is still trying to recover pre-recession levels of output and exports.

The STUC has been consistent in promoting the continuing importance of manufacturing to the Scottish economy in terms of exports, direct and indirect employment and research and development^{xiii}. We believe that significant economic and societal benefits are created through manufacturing:

- **creating genuine wealth** – the STUC believes that far too high a proportion of the economy’s limited resources have been targeted at the shifting and extracting of wealth;
- **driving innovation** - Oxford Economics has calculated that the external return – the return not captured by the company making the investment – from the £149bn R&D spending by British manufacturing is almost 30%^{xiv}. The external return from aerospace R&D is almost 60%. The benefit to the wider economy is significant thereby justifying interventions such as R&D tax breaks. The spillovers from one company alone, Rolls Royce, are estimated to be worth £3.4bn to the UK economy^{xv};
- **enlarging the pool of skills and good jobs** – manufacturing firms have been at the cutting edge of productivity enhancement through fair employment and effective skills utilization. A number of Scotland’s leading manufacturing firms run successful apprenticeship programmes. Such investments ensure these industries have the skills they need to sustain themselves into the future;
- **spreading its benefits throughout the country** (financial services is very much concentrated in the major conurbations) and cementing communities with many middle income/middle status jobs; and,
- **encouraging and sustaining the growth of local supply chain industries and services** – see for instance work undertaken by Fraser of Allander on the economic impact of BAE’s Clyde Shipyards^{xvi};

At a time when Government is implementing massive cuts in public spending in response to the deficit which soared in the aftermath of the banking crisis, the *benefits of a diverse economy and the broad taxation base it provides, should be clear to everyone.*

Scotland's under-performance in Business Enterprise Research and Development is well recognised; less so is the huge proportion of BERD spend accounted for by manufacturing^{xvii}:

	2008 (£1000s)
Manufacturing: total	407,018
Chemicals	159,898
Electrical machinery	109,108
Other manufacturing	113,237
Services	91,703
Other: Total	48,165
Grand total	546,886

Similarly, despite the challenges manufacturing has faced, its share of Scottish exports has consistently remained around 70%.

	EU27	Non-EU	Total exports
Agriculture, Forestry and Fishing	155	90	300
Production and Construction	6,995	7,160	14,115
Of which manufacturing	6,695	6,525	13,225
Services	2,480	3,405	5,725
Total	9,590	10,655	21,140

Global Connections Survey 2009^{xviii}

Manufacturing and Services

“Not only is its manufacturing sector 'defying the laws of economic gravity', as one analyst put it, Germany also has high hopes for its unregarded services sector. It has twigged that manufacturing and services aren't alternatives; they travel together. So where German exporters boldly go, Deutsche Bank and SAP follow close after.”
Simon Caulkin, Observer^{xix}

One benefit provided by a strong manufacturing sector that is often overlooked is its importance in supporting the export of business services. It has been suggested that as much as half of British services exports could stem from manufacturing – a finding that significantly increases manufacturing's contribution to the balance of payments^{xx}.

A recent report^{xxi} by the Work Foundation found that:

Exports from the financial sector (primarily the City) provided for just over a third of knowledge service exports (estimated at over £75bn and generating a surplus worth over 3.5% of GDP). However, in the remaining two-thirds manufacturing itself is a significant generator of knowledge service exports such as business services, royalties and license fees and technical and trade related services. According to recent research^{xxii} about 25% of all exports of business services and between 40-45% of trade and technical related service exports were generated by manufacturing firms. The study concluded:

“the propensity to import and export services appears to be higher in manufacturing than services. Trade in producer services may therefore be even more important for manufacturing than services.”

The Future of Manufacturing in Scotland

To maintain current levels of employment and output through the current period of uncertainty represents a significant challenge; growing manufacturing in the future a bigger challenge still. However, the STUC strongly believes that it can be done which is why we are publishing this Discussion Paper examining actions that might be undertaken by Scottish and UK Governments to support Scottish manufacturing industry now and in the years ahead.

The STUC's primary concern is that, at a time when austerity and globalisation are placing manufacturing in all developed countries under increasing pressure, some competitor nations are proving far more adept at retaining manufacturing jobs. ***This is the case even in countries where the regulatory regime is more robust and business taxation higher.*** Of course, what these countries tend to have in common is a superior record of investing in people, plant, infrastructure and research and a higher rate of productivity per hour worked.

	Pop (millions)	Persons employed (1000s)	Labour costs (euro 1000 per employee)	Value added (euro million)
UK	62	3,246	39.5	210,720
Germany	82	7,171	55.0	429,471
France	65	3,737	42.8	214,014
Italy	60	4,610	33.1	208,907
Sweden	9	797	46.2	49,948
Finland	5	407	43.0	30,078
Czech Rep	10	1,354	11.1	26,490
Poland	38	2,473	7.6	48,298

Eurostat^{xxiii}

This suggests that those who propose a future for Scottish manufacturing based on cost minimisation rather than patient investment and productivity augmentation have got it wrong. We will not safeguard Scottish manufacturing by privatising the water industry^{xxiv} or slashing protection for workers, consumers

and the environment. Pre-crisis, business conditions were generally good – stability, low inflation, low interest rates - for over a decade. The disappointment is that too few companies took advantage (were able to take advantage?) of the stable conditions to invest for the future.

A recent Centre for Public Policy in the Regions (CPPR) report examined the comparative position on employment and growth in a range of Western Europe's Old Industrial Regions (OIRs). It found that:

“...the poorer performance of UK OIRs compared to the German OIRs, in terms of creating manufacturing jobs in particular, arguably raises the most interesting set of issues. Given the German economy's widely publicised problems of high unemployment, the difficulties in handling the unification process and its greater proximity to Eastern European accession states, we might have expected a much greater decline in employment in its OIRs. Yet, ^{xxv}with the exception of low-tech manufacturing – where performance is still better than that of the UK – the picture appears to be one of relatively successful adjustment during this period”^{xxvi}.

It is surely incumbent on policy makers to study the ways in which competitor countries support and enhance their manufacturing sectors with a view to learning from their successes.

Germany

For a long-period following reunification, Germany was regarded as the embodiment of 'sclerotic Europe'; its labour laws and relatively restrictive product market regulation were widely judged to be responsible for high unemployment. The success of its manufacturers was overlooked while the dominant voices in the economic commentariat lauded the success of the Anglo-Saxon financialised service-led economies.

How times change. post-crisis the focus is on how other countries might replicate the success of Germany's world beating manufacturing exporters; particularly the *Mittelstand*; family owned companies with highly developed stakeholder relationships, a long-term outlook and a strong commitment to excellence and innovation.

Despite the 'reform agenda' implemented by Gerhard Schroeder and his successor, unit labour costs (see above) and the level of labour market regulation (see below) remain much higher in Germany than the UK. So how to explain the success of Germany's manufacturing sector? The following factors are surely pivotal:

- The *unique corporate culture of the German Mittelstand*: family ownership, focus on long-term sustainability with key stakeholders (customers, employees, suppliers, community at large), high degree of mutual trust between these groups, flat hierarchies, professional practices (best managed companies are family owned but with outside professional management), relentless drive for innovation, continuous improvement in products and services, concentration of resources to achieve leadership in (niche) markets;
- *Skills*: German firms feel an obligation to train in a way that is simply not replicated by its UK counterparts. The German system of vocational education is generally regarded as the best in the world;
- *Corporate Governance*: co-determination system – voices of stakeholders specifically employees are heard and listened to;
- *Industrial relations*: sector level bargaining, restrictive labour laws, plant-level works councils,
- *Financial system*: supports long-term patient investment, bank-centred system including regional development banks, important role for savings banks and credit unions;
- *Global trends*: the rise of China hasn't threatened German manufacturers who have set about providing '*China's factory to the world with its machine tools*'. The trade statistics bear this out – China imports more goods and services from Germany than any other nation. *Mittelstand* companies have worked relentlessly to turn domestic dominance of niche markets into global dominance. Energy is not wasted trying to break into markets dominated by large multinationals. German firms 'don't play where the elephants dance';
- *Wider business cultural values*: manufacturing is respected and valued; financial system is designed to support rather than undermine the productive economy; and,

- ***Euro membership:*** while the Eurozone’s peripheral nations such as Ireland and Greece have been hamstrung by membership during the current crisis, Germany has massively benefitted from a currency trading far below the levels which could be anticipated for a floating Deutschmark. Also, the benefits to German manufacturers in terms of reduced transaction costs are considerable.

The German model has developed in a specific cultural, economic and institutional context. It cannot be exported wholesale to other jurisdictions. However, the STUC believes that there is much that can be learnt from the success of German manufacturing particularly around corporate governance, industrial relations and the financial system.

Recommendation

- **The Scottish Government should convene a study group of all key stakeholders to identify practical policy lessons from German manufacturing.**

The STUC believes Government has a pivotal role to play in ensuring that Scotland’s manufacturing base is stabilised and nurtured. Government support and intervention can include passive measures such as tax credits for research and development and skills support and, in certain circumstances, direct assistance where companies with demonstrable long-term futures are facing short-term difficulty.

It is time for a mature discussion about the future of Scottish manufacturing. This must involve an informed and balanced appraisal of the challenges of globalisation and the level, nature and effectiveness of Government support required to meet these challenges effectively.

The case for industrial strategy

Let’s start with the case against:

“Governments do not have the necessary information and experience to make informed business decisions and ‘pick winners’ through industrial policy. If anything, government decision-makers are likely to pick some spectacular losers, given that they are motivated by power rather than profit and that they do not have to bear the financial consequences of their decisions. Especially if government tries to go against market logic and promote industries that go beyond a country’s given resources and competences, the results are disastrous, as proven by the ‘white elephant’ projects that litter developing countries”. Ha-Joon Chang, 23 Things They Don’t Tell You About Capitalism^{xxvii}

Chang is being deliberately ironic and, having set out the case against, he provides a careful and compelling rebuttal:

- Having better information doesn't guarantee better decisions – if proximity to the situation guaranteed a better decision, no business would ever make a wrong decision. Sometimes being too close to a situation can actually make it more, rather than less, difficult to see the situation objectively;
- There are numerous ways in which Government can acquire better information and improve the quality of its decisions such as legal requirements on firms in industries that receive state support to regularly report on key aspects of their business; informal networks between officials of Government and business (the French policy network built around graduates of the Ecole Nationale d'Administration is probably the best example although there are obvious dangers in such these networks leading to excessive clubbiness if not downright corruption); more formal networks such as Japanese 'deliberation councils'; and,
- Decisions that are good for individual firms may not be good for the national economy as a whole.

Chang concludes, on the basis of a number of specific examples, that Government picking winners against market signals can improve national economic performance, especially if it's done in close (but not too close) collaboration with the private sector. In the same way that the success stories do not allow us to support Governments picking winners under all circumstances, the failures, however many there are, do not invalidate all Government attempts to pick winners.

This shouldn't be a revelation. The reality is that winners are being picked all the time both by the Government and by the private sector, but the most successful ones tend to be done in joint efforts between the two. Consider the US as an example. Often portrayed as the paragon of unfettered market capitalism, the successes of US industrial policy are many and varied. Even while it pretends that it does not, the US Government has picked most of the country's industrial winners since the Second World War through massive support for R&D. Investments channeled through NASA and the Pentagon ensured the US's lead in, for instance, the commercial airline sector and the internet. The computer, semi-conductors, and biotechnology industries were also developed thanks to subsidised R&D from the US Government.

'Freed from the threat of free-riders and the imperatives of short-term profit maximisation, scientists and companies working for the US military have created many of the technologies on which the country's prosperity is now based' John Cassidy, *How Markets Fail – the Logic of Economic Calamities*^{xxviii}

Cassidy goes on to provide some specific examples of commercial products originating in research financed by public authorities: satellite television, titanium golf clubs, GPS navigation systems, water filters, cordless power tools, smoke detectors, car thermometers and scratch resistant spectacles.

Closer to home, other European nations have been investing much more directly in the industries of the future in order to maximise employment: through the 1990s and 2000s the level of state aid provided by the Danish Government to its manufacturers was proportionately 10 times that of the UK^{xxix}. This investment

was used strategically to build the world leading wind turbine sector. In Germany, the feed-in tariff for domestic renewables along with grant assistance help build the solar industry.

An industrial strategy for Scotland

Given that the devolution settlement devolves some important levers to the Scottish Parliament but retains some at Westminster, what might a modern industrial strategy for Scotland look like?

The STUC does accept the argument set out in the UK Coalition Government's recent 'growth review' paper, *The Path to Strong, Sustainable and Balanced Growth*

"...there are actions Government can take for specific sectors that will provide the right conditions for British business to grow. This is not about picking winners – only the interplay of consumers, markets and companies can determine which industries will be the most successful in the future. It is about understanding the landscape that business operates in and making sure that whenever Government is able to remove a barrier to their success, it does so^{xxx}.

If UK policy is to remain entirely passive, we risk being overtaken by competitor nations who are specialising and providing more and better quality support to nascent industries and existing sectors with comparative advantage.

Consider also the approach taken to manufacturing during the recent recession. In the UK there was little effective direct intervention^{xxxi} offered to manufacturing firms to address specific problems emerging from the financial crisis such as access to finance and export credit insurance. Other European nations intervened directly to provide assistance. Also, the active labour market interventions routinely pursued in these nations helped keep workers in jobs and provided support for retraining and upskilling; factors that will help drive competitiveness in the upturn.

Learning lessons from practice elsewhere, the STUC believes that the Scottish Government should develop a modern industrial strategy for Scotland in partnership with stakeholders. This would supplement rather than replace existing economic strategy and would of course have to acknowledge that key levers are reserved. Inevitably, this will have to adjust to UK policy but, at the very least, the co-ordinated voice of Scottish manufacturing should be heard at Westminster level.

The paper now considers the key areas where Government can make a difference:

1 Image

There is little doubt that manufacturing industry currently suffers from a poor public image although this may be changing in the aftermath of the banking crisis. A poor public image matters because manufacturing must attract new recruits

with the necessary skills in order to sustain itself. New entrants to industry must be convinced that manufacturing offers a positive career path.

Trade unions are often accused of talking the prospects of manufacturing down. We resent this charge which reflects the media's tendency to report union views only when redundancies have been announced or are in the offing. The STUC believes that much more detrimental to the image of manufacturing industry is the way in which redundancies and closures are often handled and the low pay and outdated command and control management approaches that persist in some Scottish manufacturing enterprises. ***Employers need to accept that improving the image of industry is largely within their own hands.***

There are currently a number of real success stories in Scottish manufacturing: world class companies fully consulting with their workforces to produce step-changes in productivity allowing them to succeed in competitive global markets. The success of these companies must be promoted both domestically and globally.

Recommendations

- Experience from other countries tell us that political leadership is vital: ***ministerial support for manufacturing must be visible and unrelenting***; Politicians and the media must do more to celebrate Scottish manufacturing success stories;
- ***employers*** must recognise the damage done to manufacturing when outsourcing is poorly handled. Redundancies must be handled more sensitively with earlier involvement of PACE – all alternatives to outsourcing/redundancies must be fully explored; and,
- employers must work with trade unions to address poor employment practices and low pay that persists in some manufacturing sub-sectors.

2 People, skills and management

In the STUC's last discussion paper on manufacturing published in April 2007, we argued for:

- A Scottish skills strategy;
- Greater recognition for the importance of the effective use of skills within the workplace; and,
- Greater resources for the Scottish Manufacturing Advisory Service

The pace of progress on these issues has been encouraging. However, it is clear that challenges remain: too many employers are failing to provide training, the stock of key skills in the labour market is low and too many people – particularly women – who are trained in Science, Technology, Engineering and Maths (STEM) subjects choose to pursue careers beyond manufacturing.

There is a growing and welcome focus on the quality of leadership and management and employee engagement within Scotland's workplaces. A number of prominent commentators, Crawford Gillies, Chair of Scottish Enterprise for one, have noted the existing deficits in these areas and identified progress in both as a key challenge for the Scottish economy.

The STUC welcomes the Scottish Government's initiatives in these areas such as the Skills Utilisation Leadership Group and Cross-Sectoral network.

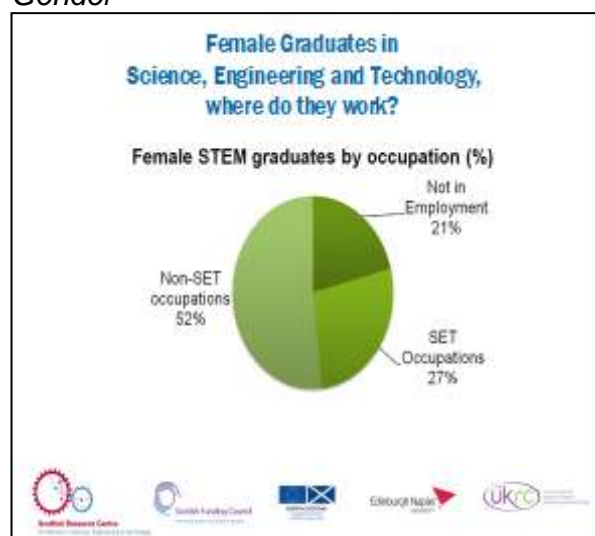
- Recommendation - Grant support to be limited to companies able to demonstrate effective employee engagement, leadership and management and skills utilisation.

The Scottish Government's economic strategy identifies 'key sectors' (financial services, energy, tourism, food and drink, life sciences, creative industries and universities) and 'growth sectors' (textiles, construction, aerospace, defence and marine, forest industries and chemical sciences). The STUC recognises that co-ordinated activity by Government, employers and the key agencies involved has produced/is in the process of producing effective skills strategies for key and growth sectors. However, we are also aware that there has been no worker involvement in some of this work (e.g. food and drink) and that there is a disparity apparent in the resources devoted to developing and funding skills work around 'key' and 'growth' sectors. A sectoral approach is required that genuinely meets the needs of the industry: employers *and* workers.

Recommendations

- ***It is vital that manufacturing growth sectors are resourced to develop coherent, effective skills strategies.*** This work must involve the participation of workers and their representatives. It must also be supplemented by sufficient investment in the generic skills valued by manufacturing industry; and,
- Modern apprenticeships are integral to meeting the skills needs of both industry and young workers and therefore funding at least at current levels must be maintained. ***Growing the penetration of MAs into manufacturing should be a priority.*** There is a clear link between MAs and quality of work and image issues: if young people are to be persuaded that there is a future in manufacturing, they must be able to access (and see others accessing) quality employed status training opportunities.

Gender



Slides from NEF December 2010^{xxxii}

Manufacturing has a very high gender pay gap, at ~40%. It is very similar to that in the financial services sector. This is likely to be explained by the fact that women are concentrated in the relatively low-paid sub-sectors of manufacturing (horizontal segregation), like food and textiles, and in more junior roles within all sub-sectors (vertical segregation), but no modelling of the pay gap within manufacturing has been carried out.

Organisations working around the pay gap, and occupational segregation (including Close the Gap, Winnet8 partnership, Scottish Resource Centre for Women in SET, Engender, and Scottish Women's Convention) have focused principally on the key sectors identified in the Government Economic Strategy, and on construction, as well as undervaluation of women's work (cleaning, catering, clerical, caring, and retail) and women's associated poverty. Manufacturing, which is perceived to offer low wages and fewer opportunities for women's progression, has not been a target for activity, although the traditional frameworks in the Modern Apprenticeship programme have.

Barriers to women's progression across all economic sectors are: a lack of flexible or part-time working at supervisory or management levels; presenteeist cultures, leading to reduced aspirations to managerial work with attendant long hours; biased recruitment practices (advertising in gendered publications, recruiting on grounds that the job doesn't require e.g. physical strength, ability to run as fast as men); taste-based preferences of employers, rooted in assumptions about women's skills, temperaments, and interests; and direct unlawful discrimination. Close the Gap has identified contributing factors to the glass ceiling in specific sectors (e.g. financial services, various sections of the public sector) and others have done recent work in Scotland around forestry. Although the general themes are the same, the way barriers play out in specific sectors, and even individual companies, must be understood before strategies to remove them can be operationalised.

Health and safety has been a driver of equality in some areas of manufacturing, as operator experience of production line conditions has been fed back to supervisors and managers and incremental changes to practices made. Some employers, like Blackwool, talk about the business case for equality, and how they have expanded their pool of labour by changing the way their production line operates, and their advertising and recruitment practices^{xxxiii}. This reflects mainstream diversity management thinking, whereby employers benefit from employing the most effective employees by widening their potential employee group from men, to men and women. There is obviously more salience to business case arguments for diversity programmes in tight labour markets, and especially those with high skills and training costs. Manufacturing has not historically been seen as one of these labour markets, although this may be predicated on outdated assumptions about manufacturing job roles. It's possible that the geographic implications of gender and manufacturing are being overlooked, particularly in areas where manufacturers are monopsony employers of semi-skilled labour.

Recommendations

- Too little is known about gender and manufacturing. The Scottish Government should resource an investigation into the gendered issues restricting growth and/or jeopardizing the sustainability of Scottish manufacturing.

3 Finance

“The indicators show that the UK has experienced a period of relative macroeconomic stability, compared to its competitors, as measured by the volatility of GDP growth and short-term interest rates, since 1998. However, this has not yet translated into a superior investment performance, as assessed by other investment indicators. UK business investment has averaged a lower proportion of GDP than France, Germany and the USA since 2000. ...the UK’s relatively low investment over the last few decades means that the capital stock has a long way to go to catch up with the US, France and Germany”.^{xxxiv}

“We need to create a network of public/private banks to support industrial and infrastructure investment and we need a wholesale transformation in the short-term, risk-averse way in which British banks have treated manufacturing companies for more than a century”. Will Hutton, Work Foundation^{xxxv}

“Private capital markets are prey to short-termism and other market failures and tend to provide less finance than is optimal to projects that generate economic benefits to the wider economy in excess of their private returns. A public development bank can circumvent these shortcomings by taking a longer-term view and by including these external benefits in its project appraisals”.^{xxxvi}

The inability of the financial sector to support Scottish manufacturing industry with the type of committed capital available to manufacturers elsewhere^{xxxvii} is a longstanding source of frustration to trade unions and, we suspect, many employers. As argued by Will Hutton and others for at least a couple of decades, it is this lack of supportive capital that explains the UK and Scotland’s poor record on investing in capital stock, R&D and human capital.

The share of domestic lending going to (UK) manufacturing fell from 5.2% in 1999 to 2.3% in 2007 while the share going to other financial intermediaries rose from 25% to 31%^{xxxviii}. Today patient investment in the companies of the future is an increasingly fringe activity compared with speculating on share prices, interest rates and currency movements. The Anglo-Saxon model continues to favour merger and acquisition over organic growth.

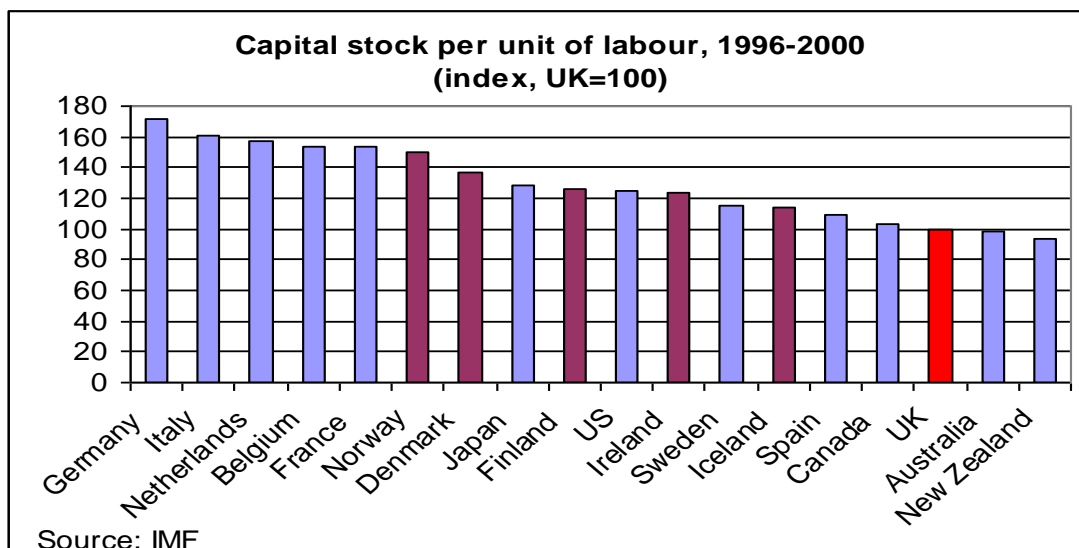
This structural problem is reflected in an interview with a City Analyst in a study by Manchester Business School: *“When I talk to the corporate managers of large German and Japanese companies, they speak of products, quality, customers and costs. They assume that if they produce innovative, high quality products at a competitive cost, they will do well and be profitable. With UK and US managers the opposite applies...many of them seem to be a million miles away from the real business”*^{xxxix}.

Academic studies identify skills deficiencies as accounting for only between a fifth and an eighth of the UK's relative productivity gap with France and Germany. Skills do not appear to account for the skills gap with the USA at all^{xi}.

The main explanation for the gap with Germany, France and the USA remains the UK's persistently poor record on investing in physical capital, R&D and infrastructure. Despite over a decade of macroeconomic stability, the Government's own evidence suggests that UK companies fail to invest to the levels of our competitors.

This problem was highlighted in a 2007 Scottish Enterprise report 'Investment and Economic Growth'^{xli} which found that:

- Investment, defined as the physical capital available to workers, is an important driver of productivity growth.
- The UK has one of the lowest levels of capital stock (measured per worker or as a proportion of GDP) among OECD countries, although latest data is for 2001. No capital stock data is available for Scotland.
- Scotland's rate of annual investment (gross fixed capital formation) is estimated to be slightly below the UK average. The UK's rate, however, lags most other OECD economies – and has done so for a number of years.
- Business investment accounts for the majority of overall investment. The UK's rate business of business investment lags all other OECD countries, although it is unclear why this is. No robust data exists for Scotland, although performance is likely to be similar to the UK's.
- There is a lack of robust data on capital stock and annual investment (total and business investment) for Scotland. This is a significant evidence gap in the understanding of Scotland's relative productivity performance.



The report also highlighted some of the factors which have been suggested as explaining the UK's poor performance on investment: economic instability, unattractive rates of return, funding of pension deficits, planning regulations, poor management practices and skills. At best these were considered to have a marginal impact. More compelling as an explanation was the UK's capital market - compared to many European countries, a higher proportion of UK businesses have their shares listed and actively traded on the stock market, and a higher proportion of these shares are likely to be owned by financial institutions. It is suggested that management decisions may be more influenced by actions that maximise short term shareholder value, rather than looking to longer term investment strategies

A 2009 BIS report, *the Provision of Growth Capital to UK Small and Medium Sized Enterprises*^{xlii} found that 'a gap exists for companies looking for between £2m and £10m in growth capital. Neither bank lending nor equity investors are likely to fill this gap in the foreseeable future'.

Problems with the availability and cost of finance during the downturn are likely to add an extra constraint to investment expenditure, particularly among SMEs. This could mean that business investment as a proportion of GDP declines more rapidly than output, and should therefore be closely monitored. Increased capital scrapping over the downturn is likely to fuel investment during the recovery.

Recent analysis suggests that the lack of R&D investment is attributable to the lower levels of retained profits in UK based firms caused primarily by higher dividend payments. The pressure for UK firms to deliver high returns within a very short timescale continues to seriously undermine prospects for long-term growth. It is widely recognised that the pressure on UK companies to deliver high returns over a very short timescale inhibits the kind of nurturing investment necessary to develop successful high-value manufacturing businesses in the longer-term.

Many innovative Scottish owned and/or based companies also continue to struggle to find the investment needed to grow. In his keynote speech to the third annual Business in the Parliament Conference on 3 November 2006, Nicol Stephen MSP, Deputy First Minister and Enterprise Minister, discussed Scotland's long-standing deficit on R&D spending before mentioning three examples of Scottish companies having to find investment elsewhere despite Scotland's highly developed financial sector:

"The first is Pelamis – Ocean Power Delivery, our wave-power generating company and the first in the world at a commercial level. Its latest funding round, announced in the middle of the year, was £13m of new investment. How much of that came from the Scottish financial community? Out of £13m of new investment, £0.5m came from Scotland, and half of that was from the Scottish public sector. The second is Cyclacel in Dundee – a fantastic company with huge potential for the future. Its latest fundraising was through a flotation in the United States, achieved through a merger with a NASDAQ listed company. The third is Wavegen in Inverness, one of the great companies that has huge potential for the future. It is now owned by Voit Siemens".^{xliii}

Both the Scottish Government and UK Coalition Government recognise this problem. The question is whether the support currently available and that proposed is sufficient in aggregate, provided at an affordable cost and targeted appropriately.

Fonds Strategique D'Investissement^{xliiv}

A major initiative of President Sarkozy's 'new industrial policy' is the Fonds Strategique D'Investissement (Strategic Investment Fund, FSI). Gilles Michel, Chief Executive, FSI describes the initiative thus:

"It is a public body to support French companies in growth and competitiveness, to reinforce the French nature of their capital structures (i.e. to provide for a stronger proportion of their capital structure that is French) and to support SME's."

Governance

The FSI is incorporated as a company. It has two shareholders – the Caisse des Depots, which has a 51% stake and the Government has a 49% stake. The Caisse des Depots was established in 1816 to restore economic confidence following the financial crisis after the Napoleonic wars. Using private investment funds, notably pension funds, it is, itself, a long term investor, able to commit the time needed for sustainable growth. It also invests in projects in which it is deemed that the market itself cannot satisfy. However, the FSI was established to meet a unique objective, i.e. to strengthen French competitiveness. The FSI does not invest in areas that are traditionally covered by the Caisse des Depots, such as infrastructure or financial services, but invests only in equity.

FSI funds are managed through a board of seven people, four from government and three from the private sector. A governance body, composed of 20 people from unions (all three French trade union federations have a seat), MPs and business associations, is asked to advise on investment strategies. The staff of the FSI is composed of corporate/investment professionals. Gilles Michel worked in the private sector for 20 years before taking the post of CEO. The FSI invests in large, listed companies; in mid-sized, often not listed companies; and in SMEs. Some SME interventions are private investments, of which the FSI is one part, but not the only part. This allows investment in technical areas, start-ups etc.

Investment Strategy

The FSI's money is utilised exclusively through investment in the capital structure of private companies, with the FSI taking a role as a minority shareholder. The FSI seeks to be a long-term investor, investing for up to 8-10 years, possibly longer. It invests an amount of money that gives it presence and allows a say in governance (through seats on boards). It also

makes a commitment to exit in a way that supports the company in question. Rather than offering subsidies, it associates itself with entrepreneurial risk. It is emphatically not nationalising companies.

The FSI has 20bn euros at its disposal: 6bn euros in cash and 14bn in equity stakes in companies. This money and equity comes directly from its two principle shareholders, the government and the Caisse des Depots. It is permanently established and has a permanent investment capacity of 2.5bn euros a year, by virtue of a rotating portfolio and dividends from companies in which it has invested.

So far, 750m euros have been invested in 18 companies, 600m of which have been invested in funds established in partnership with private companies, especially in the biotech sector and in the motor industry.

Recommendations

The STUC believes that action is required at UK and Scottish level to overcome the serious structural failure described above. It must be emphasised that growing SME's struggled to find patient committed investment prior to the banking crisis which only served to exacerbate a very longstanding problem.

When announcing the establishment of a Scottish Investment Bank at STUC Congress 2009, Alex Salmond MSP, First Minister, described it as '*an acorn from which a tree would grow*'. The STUC welcomes the progress since which culminated in the recent announcement of a Scottish Loan Fund which will supplement the existing funds administered by the Scottish Investment Bank (SIB): the Scottish Seed Fund, the Scottish Co-Investment Fund and the Scottish Venture Fund.

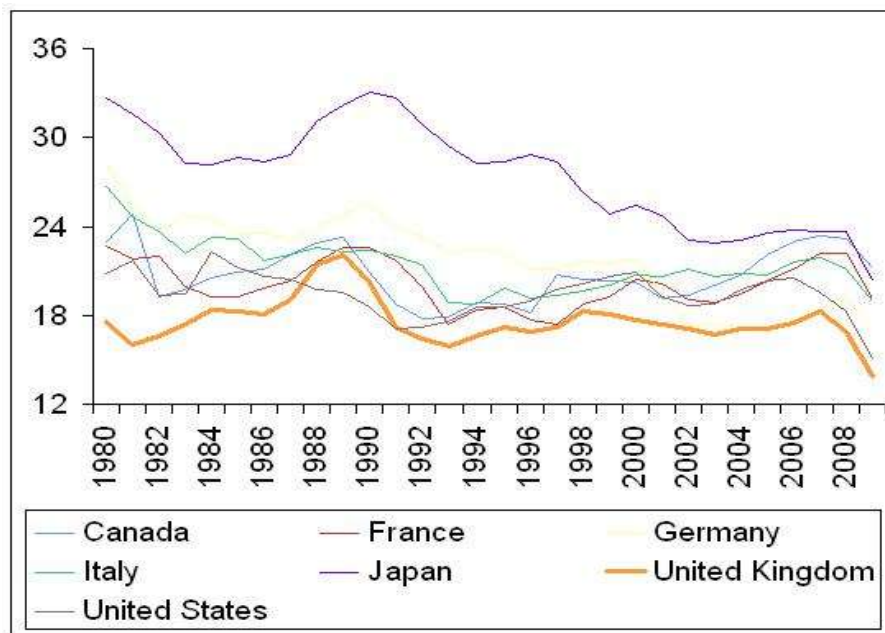
Significant progress has been made at Scottish level through the SIB but further action is required if the market failure described above is to be fully addressed. Bringing existing support under a unified structure is welcome but it is far removed from the fully fledged industrial development and reconstruction bank envisaged by the STUC. The STUC is already aware, anecdotally, that support provided through the Scottish Loan Fund may be too expensive for some SME's in Scottish growth sectors. These companies, whether they fit 'growth' criteria or not, are anxious to invest and support employment in Scotland.

- The Scottish Investment Bank must continue to develop to a stage where it can provide patient, committed capital to Scottish companies across the economy. It is essential that the SIB does not simply replicate failed private sector structures; there is a clear social dimension here – the SIB has an opportunity to help the economy expand in a way that helps meet all the Scottish Government's economic targets (including those on solidarity, cohesion and sustainability). Policy guidelines for the Bank should be set by a management board that reflects the diversity of the Scottish economy and recognises that sustainable economic development should aim to make Scotland a better place in which to live and work as

well as a better place in which to do business. The board should therefore comprise the Scottish Government, the enterprise networks, local authorities, trade unions and employers from both the financial community and manufacturing industry; and,

- The STUC proposes that the Small Business Bonus scheme is ended and funding transferred to the Scottish Investment Bank where it will have a much more efficient impact on growth and employment.

Action is also necessary at UK level to address the UK's longstanding investment gap:



It is essential that the current BIS consultation **A Long Term Focus for Corporate Britain** results in genuine and sustainable change to the UK's 'financialised', short-termist business culture. But new institutions will be necessary to fill the investment gap. Far more valuable than the various incentives proposed by the coalition to boost employment in the regions (National Insurance holidays, regional growth funds etc) will be a comprehensive network of regional industrial and infrastructure development banks.

4 Taxation, Regulation and Business Support

Are UK businesses over-regulated and over-taxed?

Too often a mature discussion about Government support for manufacturing, or indeed business in general, is crowded out by claims that all Government needs to do is get out the way; Scotland is we are told, an over-taxed, over-regulated business dystopia. This skews the debate and does nothing to help the image of Scotland an inward investment location. It is also demonstrably false.

The World Bank currently rates the UK (Scotland is not rated separately) 4th out of 183 countries in its Ease of Doing Business Rankings^{xlv}; an index averaging

each country's percentile rankings on 9 topics, made up of a variety of indicators, giving equal weight to each topic. The UK scores as follows:

- On 'starting a business' the UK ranks 17th out of 183 countries; Denmark ranks 27th, Norway 33rd and Germany 88th; and,
- On 'paying taxes' – which considers both the level of business taxation and the administration required to comply – the UK ranks 16th; Denmark 13th, Norway 18th and Germany 88th. The United States ranks 62nd on this measure.

The '*paying taxes*' ranking assesses performance on a number of indicators including the '*total tax rate*' which is designed to provide a comprehensive measure of the cost of all the taxes a business bears. It differs from the statutory tax rate, which merely provides the factor to be applied to the tax base. In computing the total tax rate, the actual tax payable is divided by commercial profit.

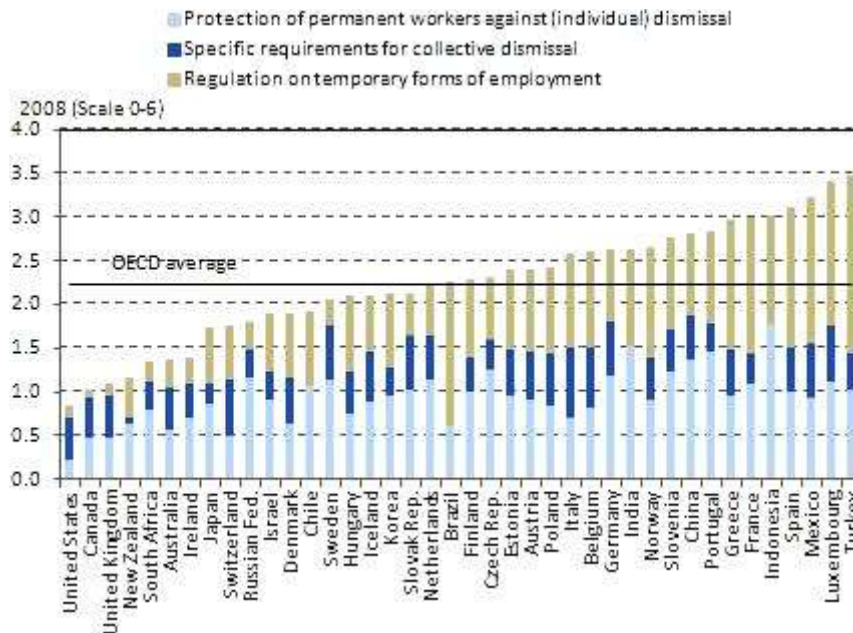
On this measure, the UK's rate of 37.3% is less than the OECD average of 43%. Only New Zealand, Canada, Switzerland, Iceland and Ireland have lower rates. The great exporting nations of Germany (48.2%), Japan (48.6%) and Sweden (54.6%) all have substantially higher rates.

On headline rates of corporation and small business tax rates, the UK rate is slightly higher than the OECD^{xvii} average. However, the average is reduced by the very low rates in Ireland, Iceland and the EU accession states. The UK's combined corporate income tax rate of 28% is lower than that of the US (39.21%), Spain (30%), France (34.43%), Germany (30.18%), Australia (30%), Japan (39.54%), Belgium (33.99%) and New Zealand (30%). The coalition Government's commitment to reducing the headline rate to 24% over the course of this Parliament will take the UK rate below that of Austria, Sweden, Denmark, Finland and Norway.

The OECD index of employment protection measures the procedures and costs involved in dismissing individuals or groups of workers and the procedures involved in hiring workers on fixed-term or temporary work agency contracts. The latest index (2008), shown below, confirms that the UK is currently the third least stringently regulated labour market in the developed world.

Employment Protection in 2008 in OECD and selected non-OECD countries^{xlvii}

Scale from 0 (least stringent) to 6 (most restrictive)



The OECD also publishes Indicators of Product Market Regulation; a comprehensive and internationally-comparable set of indicators that measure the degree to which policies promote or inhibit competition in areas of the product market where competition is viable. The indicators cover formal regulations in the following areas: state control of business enterprises; legal and administrative barriers to entrepreneurship; barriers to international trade and investment.

The OECD's analysis^{xlviii} of product market regulation 2008 found that, out of the 37 countries studied, **only the United States regulated its product markets less stringently than the UK.**

The STUC is aware of no credible international comparative work that contradicts the evidence cited above. **The UK is, on any measure, a lightly regulated economy.** The story is not quite so clear cut on taxation where there are layers of complexity around the effective as compared to the nominal rate of corporation tax as well as the ability of corporations to avoid and evade substantial proportions of their taxation responsibilities. However, **the credible international comparative data does not support the proposition that UK companies are rendered 'uncompetitive' due to high levels of taxation.** More than that, it is manifestly the case that the nations where manufacturing continues to account for a higher proportion of GDP supporting a balance of trade surplus, pay higher rates of taxation than the UK.

A number of other crucial points must be borne in mind:

- The international evidence on regulation and taxation provides no support for the contention, ubiquitous in the Scottish policy debate, that economic success in the globalised economy is dependent on low regulation and

low business taxation. Some of the poorest nations in the world have the least regulation. Countries which are recovering strongly from the financial crisis induced recession have levels of regulation and business taxation far in excess of the UK. Resisting, not joining the race to the bottom, appears to be the way forward for manufacturing;

- The evidence strongly suggests that the coalition government has its priorities very wrong if it believes further undermining of employment legislation is the path to economic dynamism. The UK labour market is already very lightly regulated in comparison to our international competitors. Again, those countries where manufacturing remains strong often have comparatively high levels of employment protection. Of course, these countries often invest more in capital stock, R&D, skills, employee engagement (Germany's system of co-determination for example) and leadership and management thereby facilitating 'high-road' approaches to productivity growth;
- Although a longer consideration of the causes and effects of growing income and wealth inequality is not appropriate in this paper, there is a strong correlation between labour market deregulation and the decline of wages as a proportion of GDP and the higher proportion of GDP accounted for by profits. It will be impossible to realise the coalition government's ambition of building an economy with strong demand but less reliant on debt if wages continue to fall; and,
- Deregulating product markets may appease those with a strong theoretical and/or ideological approach to economic development but it does not guarantee economic success. It is no accident that the UK and US, the most lightly regulated product markets in the developed world were at the epicentre of the global financial crisis.

What should the government do to support business?

The STUC believes that Government's approach to manufacturing should not seek to pander to discredited economic theory. Rather the focus should be on support that is practical and effective. For instance,

Economic development: the STUC has been concerned by the growing body of opinion arguing that Scotland's economic development institutions (Scottish Enterprise and Highlands and Islands Enterprise) should be abolished and business support left to the market. This debate has been stimulated by the coalition government's decision to abolish the Regional Development Agencies in England. The STUC believes that the evidence is clear: all successful economies (national and regional) have robust economic development agencies.

SE and HIE are currently providing significant support to manufacturing through their sectoral teams (i.e. Scottish Textiles) and, importantly, the **Scottish Manufacturing Advisory Service (SMAS)** which is providing tailored assistance to improve the productivity of Scottish manufacturing companies. It is encouraging that the success of SMAS has been widely recognized and that funding has been safeguarded. It is essential that SMAS continues to be properly resourced.

The abolition of the RDA's provides SE and HIE with a major advantage over the rest of the UK market. The STUC is already aware of jobs being created and

saved in Scotland because firms were able to draw on the support provided by these agencies while competitors in England could not. Reasonable people will continue to disagree over the role and remit of SE and HIE but their abolition, or gradual wind down through persistent funding cuts, will be hugely detrimental to Scottish manufacturing and the economy as a whole.

Export support – the latest figures published on 9 February 2011 showed a record trade deficit of £9.2bn in December 2009. The goods deficit was up by £700m, from £8.5bn in November, underlining the extent of the challenge facing coalition Ministers as they battle to rebalance the economy towards exports and manufacturing.

Worryingly, ONS data confirmed that the UK's key markets remain the US and the Eurozone with the UK is currently exporting almost 2 and ½ times more goods and services to the Irish Republic than it is to China. The UK is China's 7th top export market but not in its top ten import suppliers^{xlix}.

Therefore, the STUC welcomes the coalition government's trade white paper and in particular its commitment to '*Improve and expand the trade finance and insurance products it offers – boosting support for businesses who want to export, particularly SMEs – and bringing the UK broadly into line with the services provided in other countries*'.

However, we doubt the measures proposed therein will be sufficient to effectively rebalance trade with emerging economies. It is disappointing that the Government appears to have rejected calls to provide a similar level of export assistance to that available to firms in France and Germany^l.

Taxation: the STUC is concerned over the failure of too many UK companies to comply with their taxation responsibilities. We also recognize that the effective rate of taxation for large firms is often lower than the headline rate. The evidence simply does not support the widespread view that UK firms are over-taxed.

However, the STUC does believe that the taxation system should, as far as possible, favour manufacturing companies investing in people, plant and research over financial enterprises whose net impact on the economy is often extractive.

Therefore, the STUC cannot support the coalition government's recent changes to the tax system which compensate for the withdrawal of allowances with a cut in the headline rate. As Martin Wolf has argued in the Financial Times^{li}, the Government, '*should also reverse its policy of cutting headline rates of corporation tax, while limiting the investment allowances. This favours banking over manufacturing. Why do that?*'

Recommendations

On the basis of a large and accumulating body of data, the STUC is convinced that a 'low road' approach to competitiveness prioritizing deregulation and low business taxation is bound to fail. Instead a policy framework which provides practical support to companies and rewards investment should be pursued. Such a strategy must include:

- Government challenging employer representative organizations to raise their game by moving beyond false narratives around tax and regulation;
- Recognising that a reasonable level of labour and product market regulation is essential to protect responsible firms from cowboy operators and ultimately safeguard the economy from systemic crisis (i.e. banking crisis);
- Provide political support and sufficient resourcing for Scottish Enterprise and Highlands and Islands Enterprise including protection of the SMAS budget;
- The UK Government providing an effective level of export guarantees for UK firms; and,
- The reversal of current Government taxation policy which undermines manufacturing investment and favours finance over manufacturing; this runs contrary to the stated aims of the coalition to 'rebalance the UK economy'.

5 Ownership and Control

"A major motivator for takeovers is the rewards they decant into boardrooms, legal firms, investment banks and PR advisers. The incentives in the top ranks of a target company are stacked towards succumbing to a hostile bidder, after racking up the price. In the case of Kraft, Irene Rosenfield had a 40% pay rise to £17m last year but 'loser' Todd Stitzer, the former Cadbury chief executive walked away with £40m in cash, shares and pensions. The hedge funds just want a quick return and even 'long-term' shareholders often prefer to cash out at a profit to boost their quarterly performance figures. It is not an environment conducive to the welfare of employees or pension fund members or to the long-term interests of the UK". Ruth Sutherland, Observer 25 April 2010

The STUC has been arguing for several years that there needs to be a public debate on foreign takeovers – a lonely view until US company Kraft's takeover of British chocolate-maker Cadbury brought the issue centre stage.

With the hostile takeover of Cadburys by Kraft, partially funded by a nationalised bank, the ownership of industry for a short while became a topical but fraught issue. Many commentators express concern when foreign companies buy out UK or Scottish businesses but any action that could possibly curtail this increasingly common process is casually dismissed as protectionism.

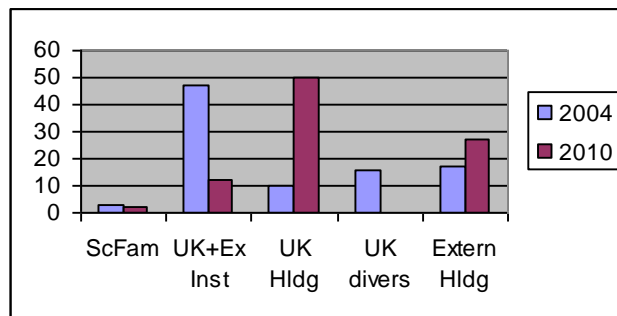
Few dispute that indigenous ownership provides benefits in terms of control and high quality HQ and research jobs. The shift in the Scottish economy towards external ownership has not been match by increased investment. As John Fosterⁱⁱⁱ, Professor of Economics, UWS has argued, *'the current shift in ownership is not principally about bringing in new investment and knowledge. It is primarily about changing the control of what already exists'*.

Scotland needs a mature debate about ownership of industry. The debate has to be informed not just by a full and proper understanding of the constraints on Government's ability to act but also of the un-level playing field that exists

whereby tax breaks are often available to foreign-based companies purchasing UK concerns.

Top 100 biggest Scottish registered companies

Percentage of value added contributed by firms owned by
 Scottish families/Scottish trusts, UK and
 external institutions, UK holding companies, diversified
 UK financial institutions, external holding companies



Politically and psychologically, it is easier for foreign owners to cut jobs here than for British-based firms: if the HQ is elsewhere, jobs here are seen as peripheral. It is also practically easier to shed workers in the UK than in, say, France or Germany, where employment protection is much stronger.

There are benefits in Scotland being a very open economy. But as long as the playing field remains uneven, we are likely to suffer from the loss of ownership. Other nations, including India, persist in erecting barriers to overseas investors. It would be helpful to know whether the UK and Scottish administrations believe any industries remain that would be considered too strategically important to pass out of domestic control?

The 'Wimbledon' theory of ownership states that the takeover of UK firms by foreign owners shouldn't concern us as long as the business takes place in the UK. Wimbledon after all, is a successful British institution even although our players don't win.

The 62 non-financial Scottish registered firms with highest turnover

	1974	2004	2010
Wholly-owned subsidiary	7	26	29 (and 5 of the 26 dissolved)
Exclusive majority: one interest owns over 50%	11	11	7
Shared majority: more than one interest with over 50% combined	2	2	1
Exclusive minority:	19	3	5

one interest owns between 10% and 50%			
Shared minority: more than one interest owning between 10% and 50%	26	18	6
Limited minority: more than one interest owning between 5 and 50%	4	2	9

It can be argued that the theory holds true for the City. The fact that US and European banks have colonised the City with no discernible adverse impact is explicable by the special factors at play: the English language, a convenient time zone and a favourable tax regime. These do not apply to the manufacturing industry.

Meanwhile there is positive action that can be undertaken to promote business models that have a higher chance of sustaining indigenous ownership. This is one of the main reasons the STUC supported the establishment of Co-operative Development Scotland. However, we are less than assured that the organisation is receiving sufficient support or resources as part of the enterprise networks.

Ownership – Recommendations

- Ministers to promote the positive benefits of Scottish ownership of industry and to defend Scottish ownership interests when necessary;
- Ministers to address the lack of a level playing field at EU and WTO level; and,
- CDS to receive more support and resources.

5 Procurement

Public procurement in Scotland each year accounts for some £8bn of spending. The STUC's aspiration for procurement policy is twofold:

- For procurement to play a pivotal role in securing the future of Scottish manufacturing. Trade unions recognise that public authorities must operate within tight EU competition rules but so far other countries have been far better at giving their manufacturers a slice of the public procurement cake; and,
- For procurement to be used to drive up standards across the economy. Contracts drawn up with suppliers and service providers can incorporate clauses on better employment standards, training provision, health and safety and environmental sustainability. There is great potential for procurement to help make Scotland a better place in which to live and work.

It is estimated that the public sector, including central and local government, together with bodies such as the Ministry of Defence and the National Health Service, spends £130 billion per year in the UK procuring goods and services and some £5bn in Scotland. The way in which this money is spent could be crucial to the long-term health of the UK's manufacturing sector.

European rules dictate what can and cannot be done with regard to procurement. In general terms, it is illegal for Member States to discriminate against the goods and services of any other Member State in their purchasing decisions. In theory, providers of goods and services from any country should have the same chance of winning a procurement contract in any other country.

Whether this works in practice is another matter. In November 2004, the Wood Review, *'Investigating UK business experiences of competing for public contracts in other EU countries'*, was presented to the Chancellor.

This review, conducted by Alan Wood, Chief Executive of Siemens plc, reported that:

"Although we were asked to look in particular at the application of Single Market public procurement rules, it became clear from the consultation that 'the rules' in themselves (or their application) are not seen as the key problem. Few examples of discrimination in clear breach of Single Market public procurement law were provided for the Review. Most of these were anecdotal and difficult to substantiate..."

"The problems are seen to be elsewhere, often described as 'grey areas' where Single Market rules are formally respected and yet national firms appear to be favoured."

"Many of the concerns expressed can be related to issues of industrial policy, including different approaches to state aid, market liberalisation and commitment to open competition."^{liii}

This appears to confirm the stereotype that the UK complies with European rules more strictly than our competitors.

Article 19

The use of reserved contracts and supported employment programmes is an important social issue and there is a serious shortage of good quality work going into supported employment factories. Article 19 of the European Public Sector Procurement Directive (2006) states:

“Member states may reserve the right to participate in public contracts awards procedures to sheltered workshops or provide for such contracts to be executed in the context of sheltered employment programmes where most of the employees concerned are handicapped persons, who, by reason of the nature or the seriousness of their disabilities cannot carry out occupations under normal circumstances”.

The STUC welcomed the recognition that this is a very important provision and we argued at the time that the Scottish Executive should provide clear, positive and constructive guidance on how purchasers can make best use of this provision.

The British Association of Supported Employment (BASE) with the support of the Scottish Government, STUC, GMB, Community, Unite and Social Firms Scotland has produced a brochure entitled ‘Supported Businesses in Scotland.’

This brochure provides a list of Scotland based organisations who are supported Businesses along with information, guidance and links on how to use Reserved Contracts.

It is now Scottish Government policy that every public body should aim to have at least one contract with a supported factory or business. The STUC looks forward to working with the Scottish Government to ensure that this policy is realised and built upon.

Recommendations

In our 2007 paper, the STUC outlined a number of examples where strict interpretation of EU law undermined opportunities for Scottish and UK firms relative to their European competitors. Happily, since this paper was published there has been something of a rethink in Government circles which is best reflected in the statement from Peter Mandelson, during his time as Secretary of State for Business,

There is also a need to see the Government’s long-term role as a direct customer and purchaser in the same way. The public sector itself spends or invests around £175 billion annually and is by far the largest customer in the British market. This procurement can have a powerful role in shaping markets, with the potential to drive demand for new technologies, skills, and processes. This in turn represents a huge source of opportunity for UK-based businesses and their employees, where they can compete successfully to meet Government needs.

This requires that we see the 'pre-procurement' phase as just as important as the procurement process itself. The Government needs to think ahead about the shape and nature of its likely requirements for new products and processes. It needs to communicate those requirements, in a structured way, to the right audiences. Particularly where markets are new and significant, it should be willing to take active steps to encourage new supply chains and to ensure UK businesses of all sizes are able to compete. The Government must work actively with UK-based businesses to overcome their potential skills and technology deficits so as to enhance their ability to compete.

During 2009, all Government Departments must publish Innovation Procurement Plans that will embed a clear obligation to procure goods and services in a way that drives innovation, and to identify clearly the areas in which they are seeking to procure innovative solutions to help deliver their objectives^{liv}.

This new approach should be built upon to ensure that opportunities for Scottish firms must be maximised.

- The UK and Scottish administrations must build on the work already underway to ensure that procurement policy supports indigenous manufacturing as far as is practicable under EU law;
- Specifically, both administrations should further develop strategies to support Remploy and sustainable procurement; and,
- The Scottish Government's Procurement Directorate should work proactively with Industry Advisory Groups to identify opportunities, and where appropriate, develop procurement strategies.

Conclusion

If this paper has a guiding argument, it is that there has been far too much complacency over the overall decline in manufacturing as a share of total employment in Scotland; a near 45% decrease in employment over a 12 year period was neither inevitable nor desirable. This reflects complacency over both the importance of manufacturing in the economy and the ability of government to influence the path of development.

As this paper is being finalized, cost pressures (primarily raw materials) are threatening the recovery in manufacturing. These pressures are often exacerbated by the loss of indigenous supply chains; the STUC has warned over such 'critical mass' issues for years.

It should now be apparent that financial services cannot be trusted to be the main source of employment and wealth creation in the UK. As a number of commentators have pointed out, the City is a machine for transferring wealth from outsiders to insiders whilst imperiling the wider economy.

Neglect of manufacturing by Government and finance and loss of ownership and control has left Scotland less well placed to exploit opportunities in emerging low carbon sectors; we risk the benefits from low carbon development flowing out of Scotland and driving up other nations' technology. Government support is

necessary to maximize low carbon employment opportunities and it is questionable whether enough will be forthcoming.

The STUC firmly believes that manufacturing industry in Scotland can have a positive future. As a minimum, the aim of public policy must be to stabilise the manufacturing sector in Scotland in order to safeguard the jobs it currently provides. Growing the manufacturing base in the longer-term is both achievable and desirable. The aspiration driving policy should be the creation of a sustainable, balanced economy benefiting from successful world class service industries and a re-invigorated manufacturing sector.

STUC March 2011

ⁱ The previous UK administration was particularly busy in this regard. See *New Industry, New Jobs* (2009); *Advanced Manufacturing* (2009). Also work around EU2020 has stressed the importance of manufacturing. The new UK coalition has continued to build on the work around *Advanced Manufacturing* ;

ⁱⁱ The US economist Thomas Palley describes the principal impacts of financialisation as (1) elevating the significance of the financial sector relative to the real sector; (2) transferring income from the real sector to the financial sector; (3) contributing to income inequality and wage stagnation. See *Financialisation: what it is and why it matters*, Thomas Palley, Political Economy Research Institute, November 2007

ⁱⁱⁱ Fraser of Allander Economic Commentary Vol 34 No 1

^{iv} Ibid

^v National Statistics Labour market Scotland published 19 January 2011

<http://www.statistics.gov.uk/StatBase/Product.asp?vlnk=15084>

^{vi} Ibid

^{vii} Scottish Government, Index of Manufactured Exports 2010 Q3

<http://www.scotland.gov.uk/Publications/2011/01/IME2010Q3>

^{viii} Manufactured export sales decreased by 0.7% in the 3rd Quarter of 2010 but increased by 0.7% over the year. Ibid.

^{ix} Supplement provided with Prospect magazine, October 2008 issue

^x Ibid

^{xi} 'Britain needs an industrial route map', John Rose, Financial Times 22 April 2008

^{xii} 'British manufacturing is at a critical point', Richard Lambert, Financial Times, 7 September 2008

^{xiii} The STUC published an Economy Discussion Paper, *The Future of Manufacturing Industry in Scotland* in April 2007: <http://www.stuc.org.uk/policy/economic-industrial-policy/discussion-papers-series/the-future-of-manufacturing-industry-in-scotland#introduction>

^{xiv} Pg 8, *the Return of Manufacturing*, Prospect Supplement, October 2008

^{xv} *Engine Maker weights up the value of its ideas*, Financial Times, 1 August 2010

^{xvi} http://www.baesystems.com/Newsroom/NewsReleases/2007/autoGen_107219164722.html

^{xvii} *Business Enterprise Research and Development Scotland 2008*, Scottish Government, February 2010 <http://www.scotland.gov.uk/Resource/Doc/981/0099273.pdf>

^{xviii} Pg 3, *Scotland's Global Connections Survey 2009*, Scottish Government published 21 January 2011 <http://www.scotland.gov.uk/Resource/Doc/933/0111039.pdf> (note – the total exports figure contains £55m worth of exports that could not be allocated to a region)

^{xix} 'There's life beyond the British super Casino', Simon Caulkin, The Observer 3 February 2008

^{xx} Finbarr Livesey of Cambridge University's Institute for Manufacturing as referenced by Michael Prest in 'The Return of Manufacturing' Prospect, October 2008

^{xxi} *Manufacturing and the Knowledge Economy*, Work Foundation, January 2009

^{xxii} Hijzen, Pisu and Upward *A Portrait of Trade in Services*, Report to the DTI, June 2006

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- xxxvi A way out of Britain's growth dilemma, Robert Skidelsky and Felix Martin, Financial Times, 21 March 2011
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- xxxviii Pg 15, Do the Super-Rich Matter, Stewart Lansley, TUC Touchstone Pamphlet 2008
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- xlii <http://www.berr.gov.uk/files/file53698.pdf>
- xliii <http://www.scotland.gov.uk/Topics/Business-Industry/Enterprise/18977/Conference2006/transcript2006>
- xliv For a fuller analysis of the French model including the FSI see TUC policy paper 'Developing UK Industrial Policy – lessons from France' <http://www.tuc.org.uk/extras/strategicinvestmentfund.pdf>
- xlvi <http://www.doingbusiness.org/rankings>
- xlvii <http://www.oecd.org/dataoecd/26/56/33717459.xls>
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- liii In a lecture 'Does Ownership Matter in the Scottish Economy?' delivered at Glasgow Caledonian University on 2 February 2011. See a condensed version of this lecture here <http://stucbetterway.blogspot.com/2011/02/does-it-matter-who-owns-scottish.html>
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