1 Key Policy Insights

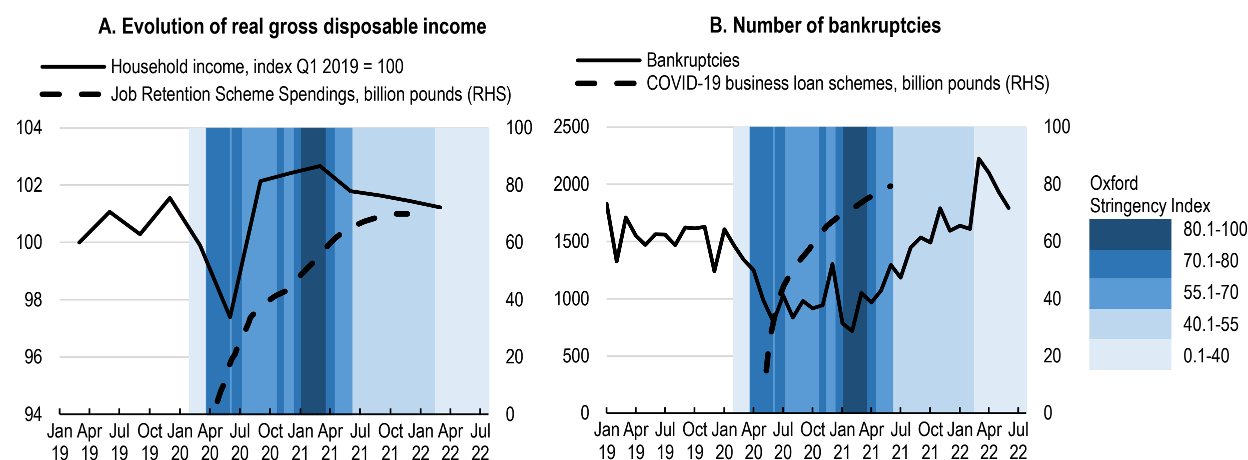
The United Kingdom recovered from the economic shock from the COVID-19 pandemic owing to emergency support packages put in place and a rapid vaccine rollout. However, growth is slowing amid persisting supply shortages and rising inflation. Fiscal policy has to balance gradual tightening with providing well-targeted and temporary support to vulnerable households from rising costs of living, supporting growth and addressing significant spending and investment needs. Accelerating progress towards net zero is fundamental to enhance energy security and reduce dependence on fossil fuels. Policy reforms to support economic reallocation and investments in the green and digital transition can stimulate productivity growth and contribute to reducing disparities across UK regions.

The pandemic and Brexit have magnified structural challenges

The United Kingdom is recovering following the heights of the COVID-19 pandemic. After being severely hit by the pandemic, a quick vaccine rollout in 2021 improved the public health situation and allowed the easing of containment measures. As the economy started to recover in 2021 at a rapid pace, labour shortages intensified on the back of rising global demand and global supply constraints. Price pressures rose significantly, aggravated in early 2022 by surging global energy prices following Russia's invasion of Ukraine. Increased barriers to trade and migration resulting from leaving the European Single Market and Customs Union on 1 January 2021 likely added to supply constraints. Amid persisting supply shortages and rising inflation, growth has started to slow down.

As the immediate impact of the pandemic subsides, the policy focus should shift to addressing long-standing structural challenges that have been magnified by the pandemic and Brexit. The United Kingdom entered the pandemic with weak productivity growth, large regional disparities and an ageing population. Years of underinvestment in public infrastructure resulted in large investment needs. The decade of strong fiscal consolidation ended with the provision of extensive fiscal support during the COVID-19 crisis, which helped to attenuate the loss of household income and allowed businesses to survive (Figure 1.1). However, public debt has increased considerably, calling for a gradual fiscal tightening while also bringing the need to raise productivity and growth to the fore.

Figure 1.1. Fiscal support during the pandemic supported households and businesses



Note: The colour scale of the background reflects confinement stringency based on the Oxford Stringency Index. The Oxford Stringency Index is a composite measure based on 9 response indicators including school closures, workplace closures, and travel bans, rescaled to a value from 0 to 100 (100 = strictest response). Panel A: Cumulative job retention scheme spending. Panel B: Registered company bankruptcies. COVID-19 business loan schemes are the cumulative sum of the total value of loans of the Coronavirus Business Interruption Loan Scheme (CBILS), Coronavirus Large Business Interruption Loan Scheme (CLBILS) and Bounce Back Loan Scheme (BBLS). Figures for CBILS, CLBILS and BBLS are based on management information supplied to HM Treasury by accredited lenders and represent their best estimates of the published totals. The value of BBLS loans approved includes extra value from BBLS loans that have subsequently been 'topped-up'. As of 31 May 2021, 106,660 BBLS top-ups had been approved worth GBP 0.95 billion. Data on the recovery loan scheme are missing as they are not available yet with the time dimension.
Source: OECD (2022), Economic Projections and Statistics database; UK government, Coronavirus job retention scheme Statistics: December 2021; UK Government, Monthly Insolvency Statistics December 2021; UK Government, HM Treasury coronavirus business loan scheme statistics; and Oxford COVID-19 Government Response Tracker, Blavatnik School of Government.

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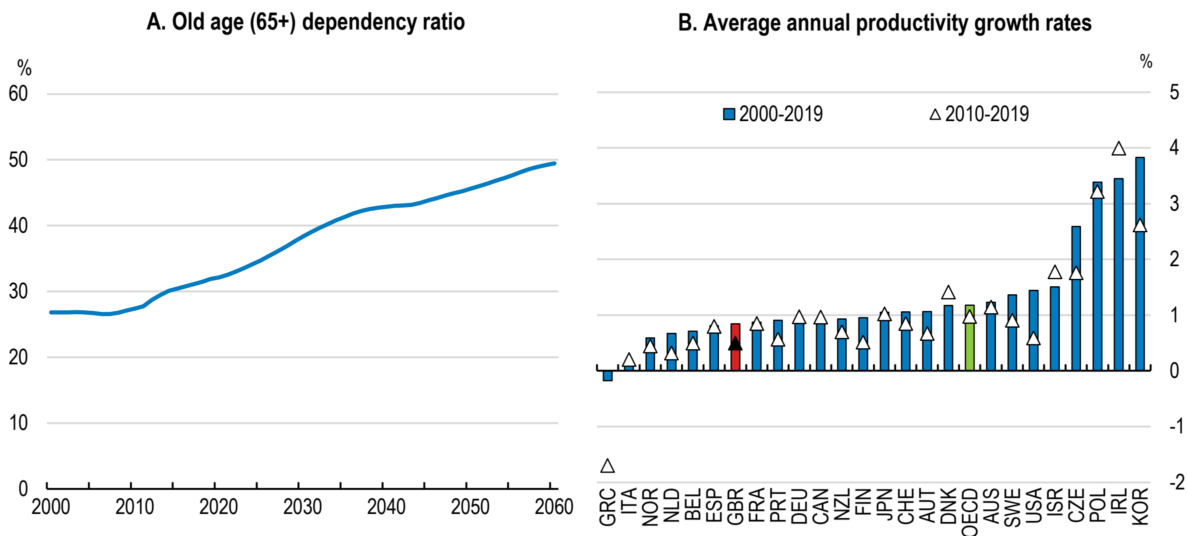
Population ageing, aggravated by potentially lower net migration following Brexit, requires the efficient use of resources to maintain economic growth (Figure 1.2, Panel A). Productivity growth has been almost stagnant over the last decade and is lower than in many other advanced OECD economies (Figure 1.2, Panel B). COVID-19 and leaving the European Union Single Market continue to cast their shadows on the economy. Estimates by the UK Office for Budgetary Responsibility (OBR) suggest that, due to the pandemic, potential output by 2025 will be 2% lower than pre-pandemic trends on the back of higher inactivity rates among older workers, lower net migration, foregone investment, and lower total factor productivity. In addition, the OBR estimates that Brexit will lead to 4% lower productivity after a 15-year period, relative to remaining in the European Union, due to a fall in trade intensity.

Figure 1.2. An ageing population meets low productivity growth



Note: Panel A: Old age dependency ratio is the number of individuals aged 65 and over in relation to the working aged population (25-65 years). Panel B: Labour productivity is measured as GDP per hour worked at constant prices, USD purchasing power parities.
Source: ONS; and OECD (2022), productivity database.

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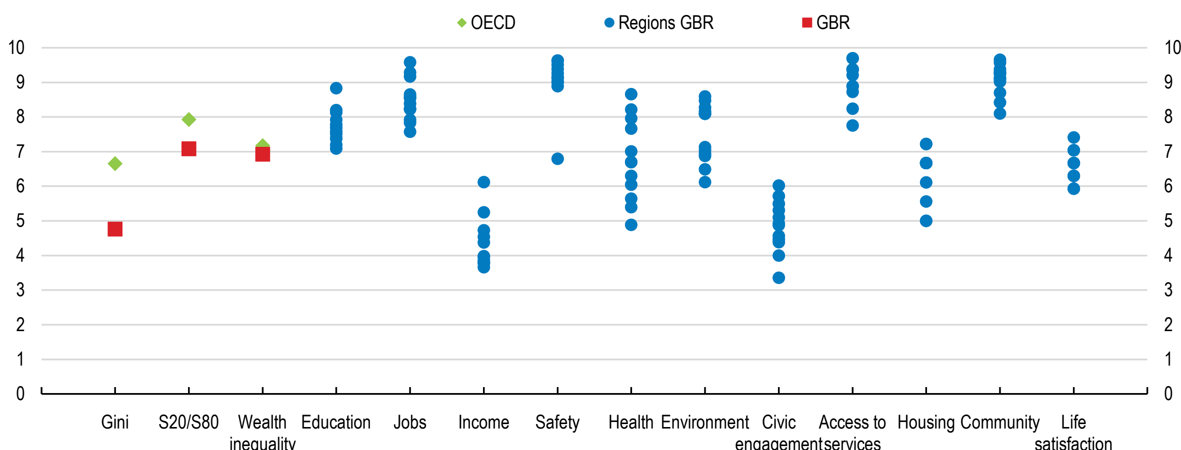
Inequalities in income and wealth were already higher than in most OECD countries before the COVID 19 crisis (Figure 1.3), but have increased further since. In addition, disparities in income, work, education and health are high across UK regions (Figure 1.3). The COVID-19 pandemic also opened up new gaps among people and businesses along dimensions that were previously less significant, such as the ability to work from home and digital access. A highly unequal distribution of skills and qualifications is not only hampering social mobility but has also been contributing to regional disparities, with a concentration of low skills in the least productive regions. Raising productivity and living standards in lagging regions is at the heart of the government’s “Levelling Up” agenda and will require significant public and private investment.

Figure 1.3. Income inequality and regional disparities are high

Regional-Wellbeing, 0-10, 10 indicating higher performance relative to other regions (including inequality measures)



Note: The following indicators are used to construct the different indices by topic as appearing in the figure starting from Education: Labour force with at least secondary education (2017), Employment rate and unemployment rate (2017), Household disposable income per capita (2016), Homicide rate (2016), Life expectancy at birth (2016) and mortality rate (2016), Air quality: PM2.5 (2015), Voter turnout (2015), Share of households with broadband access (2017), Rooms per person (2011), Perceived social network support (2014), Self-assessment of life satisfaction (2014). National data is used for Gini after taxes (2019 or latest), S20/s80 ratio (2019 or latest), share of top 5% of wealth (2019 or latest) rescaled using the min-max formula. OECD aggregate refers to a simple average over countries for which data was available. Latest data available are used for more info see source.
Source: OECD Regional Well-Being database.

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The United Kingdom needs to address its long-standing structural challenges to better weather the deep transformations that it is rapidly undergoing. COVID-19 has sped up digitalisation and people are more likely to work and shop from home. Faster digitalisation and the adoption of new technologies imply an ever-growing need for workers to update their skills to meet new skill requirements. Leaving the EU Single Market and Customs Union resulted in restricted access to the United Kingdom's largest trade and investment partners, calling for a new trade strategy. The United Kingdom is committed to become a net zero greenhouse gas emission economy by 2050. CO_2 emissions per unit of GDP have fallen more rapidly in the United Kingdom than elsewhere in the OECD, but continuing the path to net zero will be considerably more challenging in the years to come. Significant investment needs to decarbonise the economy will reduce fiscal space and will require considerable policy changes affecting businesses and people's daily lives. Changes will affect sectors, regions and population groups to varying degree and at different times, but the required labour and capital reallocations across sectors will be challenging.

Against this background, this Survey discusses policies to consolidate a sustainable and inclusive recovery from the COVID-19 pandemic and to adapt to the economic transformations that Brexit and the transition towards net zero by 2050 require. The main policy messages of the Survey are:

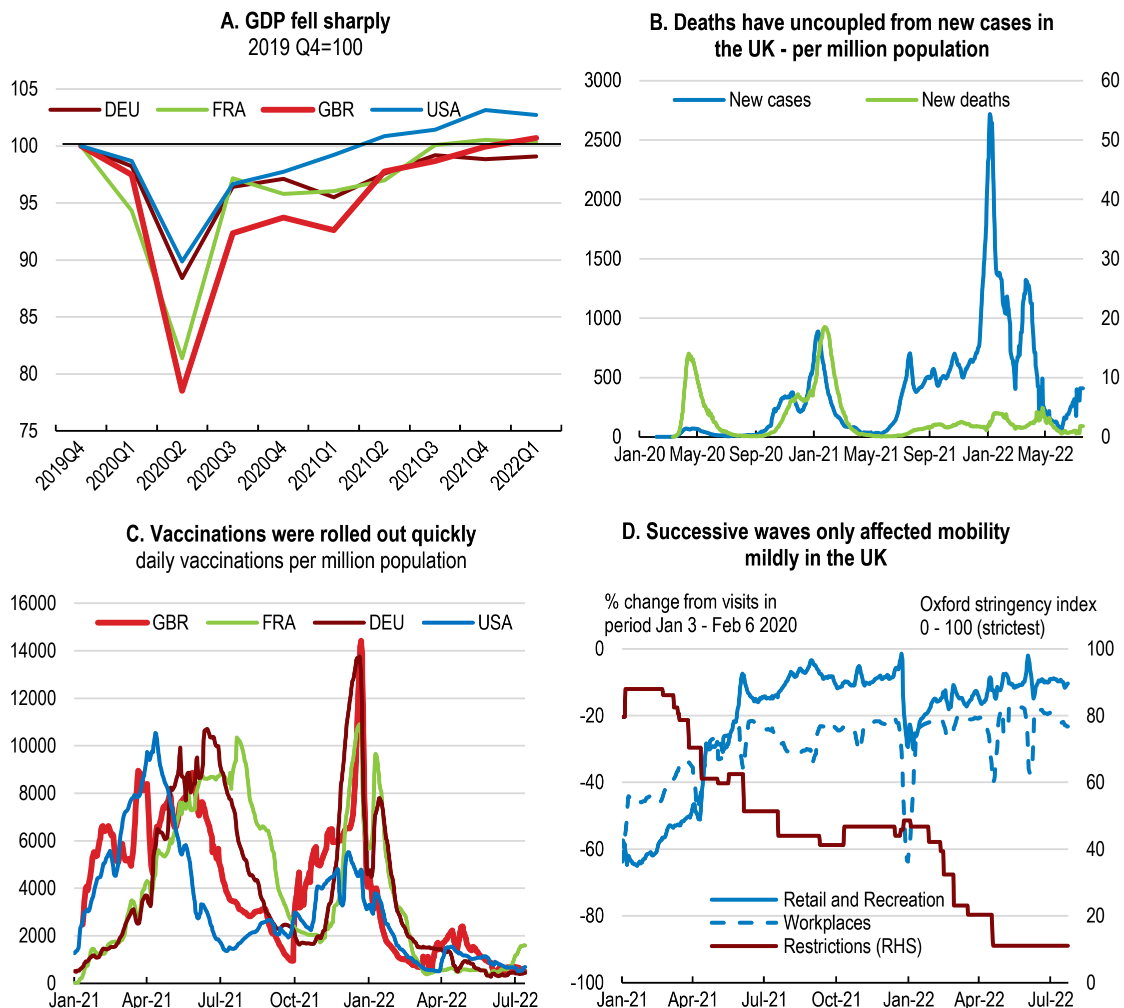
- Following the government's strategy, fiscal policy has to balance gradual fiscal tightening with supporting growth, providing well-targeted and temporary support to protect vulnerable households from high costs of living and addressing significant spending and investment needs to support on-going economic transformations.
- Raising productivity will be key to enhance growth and reduce inequalities across regions. This will require sustained increases in public investment as planned and a substantial rise in private investment. Significant re- and up-skilling are needed to support workers' reallocation and address current and future skill-shortages.
- Achieving net zero greenhouse gas emissions by 2050 calls for timely, coherent and efficient policies across all sectors of the economy, addressing sector-specific market failures, competitiveness and distributional concerns heads-on.

The economy is recovering from the COVID-19 crisis, bringing challenges from leaving the EU to the forefront

Economic growth has slowed after a strong recovery

The economy has rebounded following an unprecedented contraction during the COVID-19 pandemic (Figure 1.4, Panel A), aided by timely government support measures as described in the last Economic Survey (OECD, 2020[1]). As in other OECD countries, the United Kingdom experienced several waves of COVID-19 infections, but a fast initial roll-out of vaccines over the first half of 2021 weakened the link between new COVID-19 cases, hospitalisations and deaths since summer 2021 (Figure 1.4, Panels B and C). With an improved public health situation, COVID-19 related restrictions were gradually eased from April 2021 and economic activities started recovering (Figure 1.4, Panel D). To keep the recovery on track, the government should ensure that the public health situation remains under control by continuing its vaccination efforts in line with international guidance.

Figure 1.4. GDP has recovered on the back of an improved health situation



Note: COVID-19 figures were last updated on 27 July 2022. Panel A: The UK Office for National Statistics is one of the few major National Statistical Institutes to follow the volume indicator approach for most health and education outputs, which is recommended by the European System of National Accounts. This different statistical method may have led to some divergence in reported output declines during the pandemic, but the return to normal should reverse such divergence (see OECD Economic Outlook, Volume 2021 Issue 1, box 1.1 for more details); Panel B: New cases are new confirmed cases of COVID-19 (7-day smoothed) per one million people. New deaths are newly confirmed deaths of COVID-19 (7-day smoothed) per one million people.
Source: OECD (2022), Economic Outlook: Statistics and Projections database; Hale et al., (2022). Oxford COVID-19 Government Response Tracker, Blavatnik School of Government; Google LLC, Google COVID19 Community Mobility Reports; and Roser et al (2022), "Coronavirus Pandemic (COVID-19)". Published online at OurWorldInData.org.

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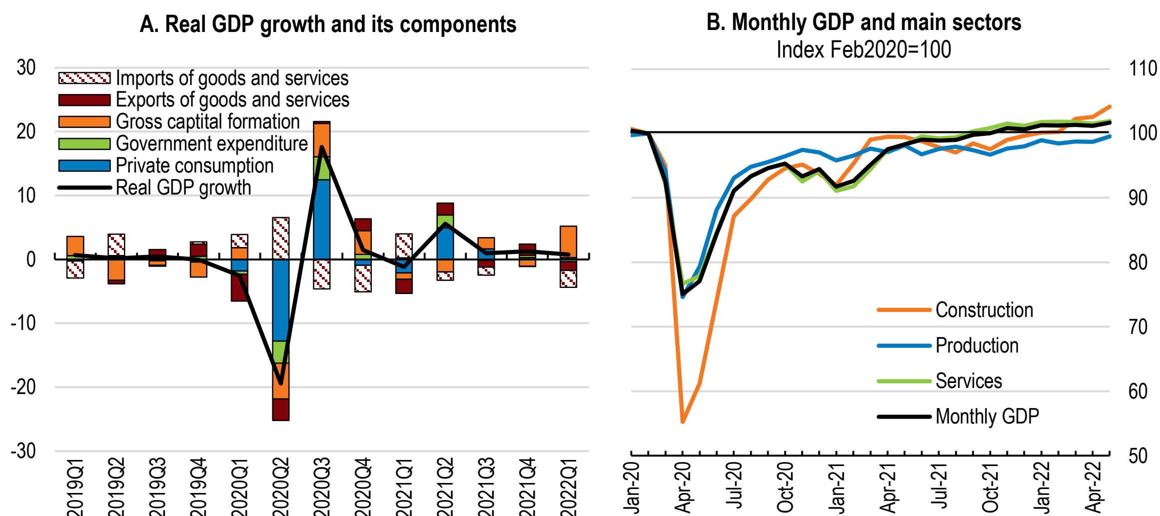
Output recovered to pre-pandemic levels by November 2021, but growth slowed from 1.3% in the last quarter of 2021 to 0.8% in the first quarter of 2022 (Figure 1.5, Panel A). Important sectoral differences remain. The construction sector, heavily affected by the pandemic, was the quickest to recover, reaching pre-pandemic levels by the end of April 2021 (Figure 1.5, Panel B). By beginning 2022, the service sector exceeded pre-pandemic levels, but consumer-facing services, most affected by containment restrictions, still remained 5% below pre-pandemic levels by May 2022. Production output has not recovered to pre-pandemic levels, as early improvements from mid-2020 have slowed due to labour shortages and global supply issues.

Figure 1.5. The economy recovered to pre-pandemic levels



Source: OECD (2022), Economic outlook: statistics and projections database; and ONS.

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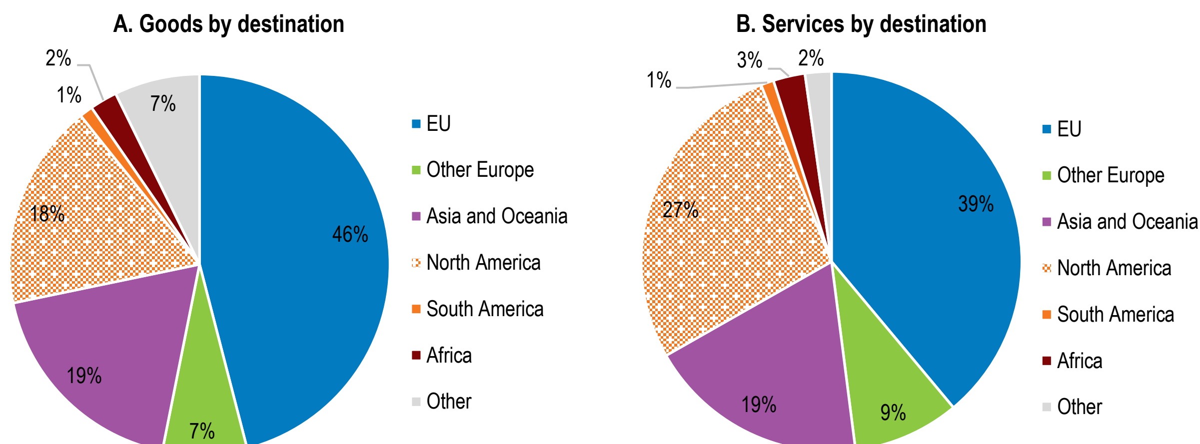
The United Kingdom's departure from the European Union Single Market and the pandemic weigh on trade

Trade has not only suffered from supply bottlenecks and suppressed demand during the pandemic, but also from increased trade frictions with the European Union owing to Brexit (Box 1.1). The European Union was the destination of 46% of UK's goods exports and 39% of services exports and the origin of 49% of both goods and services imports in 2019 (Figure 1.6). Trade in goods with the European Union dropped sharply in January 2021, when the transition period ended, and the United Kingdom effectively left the EU Single Market and Customs Union (Figure 1.7). Since then, trade flows have recovered somewhat, especially UK exports to the European Union. However, recent analysis suggests that the number of trade relationships dropped by one third after January 2021, as trade costs due to administrative burden increased (Box 1.2). While large firms that drive aggregate exports have not yet been severely affected, increased fixed cost have curbed the ability of smaller firms to export (Freeman et al., 2022[2]). Recent interventions to provide SMEs with export support are welcome and should be sustained. Imports from the European Union remain depressed as increased trade costs lead to both UK import activity shifting away from the European Union and EU firms for which the UK market accounts only for a small share of sales reducing exports to the United Kingdom. Services exports and imports declined during the pandemic, with imports from the European Union decreasing the most.

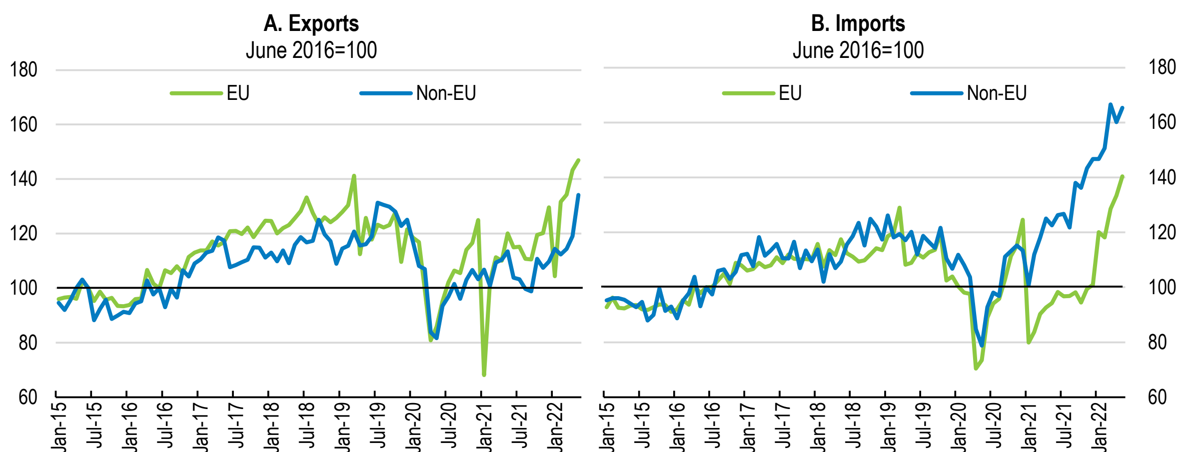
Figure 1.6. The European Union is a major trading partner

Share of exports by sector and destination, 2019



Source: OECD (2022), International Trade Statistics.

Figure 1.7. Leaving the EU Single Market has affected imports more than exports



Note: Goods imports and exports exclude precious metals. In January 2022 there have been changes to the way HM Revenues and Customs (HMRC) collect data for both imports from and exports to the EU; because of these changes caution should be taken when interpreting these data.
Source: ONS, UK trade: goods and services publication tables.

The TCA has clarified the post-Brexit trading relationship between the United Kingdom and the EU. Some uncertainties around the Withdrawal Agreement (WA) remain, in particular about implementing the Northern Ireland Protocol (Box 1.1). To support exports to the EU market, the United Kingdom and the European Union should discuss to reduce non-tariff barriers for EU-UK goods trade and improve market access for services. The further phase-in of checks on goods imported from the European Union will continue from next year (2023), including additional sanitary and phytosanitary (SPS) checks, and its impact on trade flows should be monitored closely. Access to comprehensive export support services, especially for SMEs, should continue to be provided (Table 1.1) while targeted support to firms and workers that may suffer from trade frictions could be considered.

Box 1.1. The Withdrawal Agreement, Trade and Cooperation Agreement and the special trade status of Northern Ireland

The Trade and Cooperation Agreement

The United Kingdom and European Union agreed on a comprehensive Trade and Cooperation Agreement (TCA) in 2020 that entered into force on 1st January 2021. The TCA allows for zero-tariff, zero-quota trade in goods between the United Kingdom and the European Union. Although comprehensive in scope as a free trade agreement, it entails significant trade frictions for UK based goods and services exporters. While it guarantees tariff-free access for goods trade, non-tariff technical barriers such as sanitary and phytosanitary requirements and rules of origin are not addressed. The agreement is more limited with regards to services, introducing non-tariff barriers and reduced access to the Single Market and very limited provisions on financial services. The level-playing field provisions in the TCA imply that trade restrictions could be introduced by either side in case of significant divergence in areas such as labour, climate or subsidy policy.

The special trade status of Northern Ireland

The Northern Ireland Protocol is part of the Withdrawal Agreement between the United Kingdom and the European Union. Agreed on 17 October 2019, with provisions applying from 1 January 2021, it arranges the rules for cross-border flows of goods, services and migration between the European Union (i.e., the Republic of Ireland) and Northern Ireland. In light of protecting the peace process and the 1998 Belfast agreements, the intent has been to prevent a hard or soft border between the European Union and Northern Ireland. The Northern Ireland Protocol in the Withdrawal Agreement effectively leaves Northern Ireland as part of the Single Market, avoiding the need for a border between Northern Ireland and the Irish Republic. Northern Ireland hence needs to align itself with Single Market rules with regard to trade in goods. To preserve the integrity of the Single Market, it was agreed that some checks will be required at the sea border between Northern Ireland and Great Britain. Although the agreement benefits Northern Ireland as it gives full access to the EU Single Market, trade with Great Britain has experienced frictions.

On 13 June, the UK government introduced a new bill in parliament that would enable it to unilaterally disapply elements of the Northern Ireland Protocol in the United Kingdom. The bill would empower ministers to introduce changes in four areas of the protocol, covering customs and food safety checks, the application of EU regulations, VAT changes and the role of the European Court of Justice (ECJ). The government's stated aim is to facilitate trade destined for Northern Ireland from Great Britain by reducing custom checks on goods crossing between the two. Before coming into effect, the bill has to be debated and voted on in parliament. The UK government has stated that its preference remains finding a negotiated solution with the EU. The publication of the new bill adds to uncertainty for businesses in Northern Ireland, potentially affecting trade and investment.

Source: UK-EU Withdrawal Agreement, October 2019; UK government, Northern Ireland Protocol Bill 2022.

The UK government is developing a new trade strategy. Having left the European Union and its trade framework, the United Kingdom has replaced the EU external tariff with a new "UK global tariff" under which the number of goods with zero tariffs increased. The openness to services trade has further improved as evidenced by an improved score on the OECD Services Trade Restrictiveness Index, bringing the UK in fifth position out of 38 OECD countries. The UK has also concluded continuity agreements with almost all countries that had trade agreements with the European Union at the time of exit, as well as new agreements with Japan, the EFTA countries (Iceland, Liechtenstein, Norway and Switzerland), Australia and New Zealand. The United Kingdom maintains an interest in a trade agreement with the United States, but has recently shifted attention toward the Indo-Pacific region to benefit from its growth potential

(Department for International Trade, 2021[3]). The United Kingdom is also in the accession process to become a member of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and is negotiating an agreement with India, aiming to reduce barriers for goods and services trade.

The new trade agreements the United Kingdom has finalised so far are unlikely to make up for the loss of EU export market shares. Reduced trade frictions between the United Kingdom and the CPTPP countries and India may boost UK exports in the longer run, but will have a modest impact in the short term as they respectively accounted for just over 8% and 1.5% of UK exports in 2017-2019 (Hale, 2022[4]). Furthermore, the United Kingdom will be competing for these export markets against existing members such as Canada and Japan. A deep trade agreement with the United States could give the United Kingdom exports a bigger boost in the near term, as exports to the United States accounted for 20% of total exports in 2019. In addition to facilitating UK exports to the EU, the government should continue to negotiate new trade deals with other partners. The long-term economic impact of Brexit remains uncertain and will depend on multiple factors including the streamlining of global supply chains in response to Brexit (and the pandemic), access to the EU Single Market, regulatory divergence to the European Union, the relative attractiveness of the United Kingdom driven by policy choices in the United Kingdom and abroad and the number and nature of the UK's new trade agreements.

Box 1.2. The administrative costs of EU-Great Britain goods trade post Brexit

Trade between Great Britain and the European Union faces a range of customs requirements since the UK departure from the EU.

All goods will require:

- Customs declarations;
- Customs duties for goods that do not comply with preferential rules of origin;
- Import VAT;
- Safety and security declarations.

Some goods need additional checks:

- Checks required by international conventions such as endangered species;
- Sanitary and phytosanitary checks including documentary, identity and physical checks;
- Excise duties.

Source: Institute for Government (2022[5]).

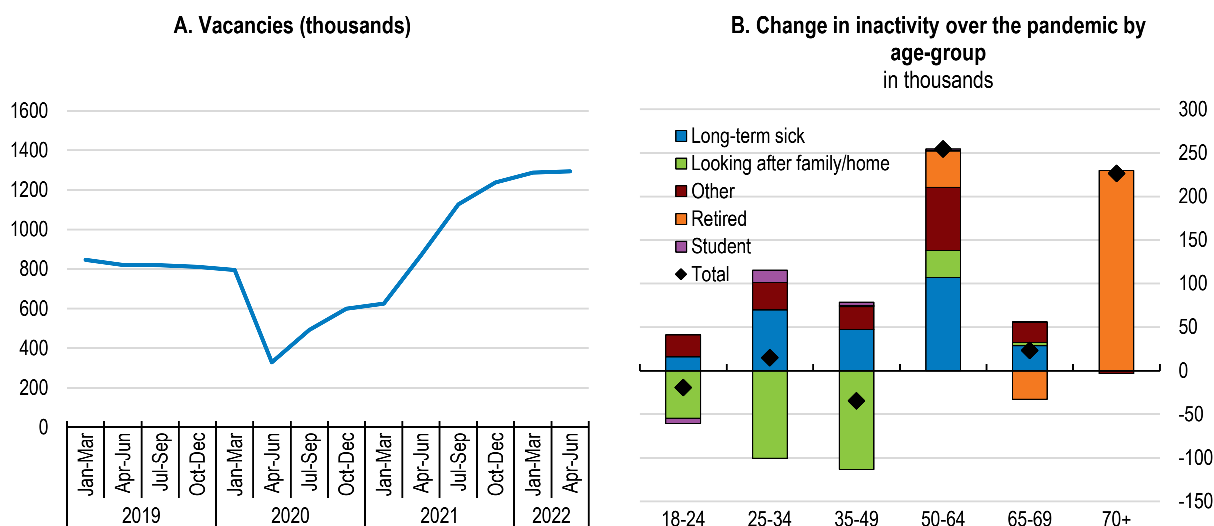
Table 1.1. Past recommendations on international trade

Recommendation in previous *Surveys*	Actions taken since last *Survey*
Keep low barriers to trade and investment with the European Union and others, particularly market access for the service sectors including financial services	The UK-EU Trade and Cooperation Agreement entered into force on 1 January 2021. It allows quota and tariff free trade for goods but introduces a range of technical barriers, whilst there is a more limited number of provisions regarding services within the TCA.
Enhance communication on a no-deal exit from the European Union	A no-deal exit was avoided with the conclusion of the Trade and Cooperation Agreement.
Prepare targeted support to firms and workers that may suffer the most.	SME Brexit support fund launched in February 2021 offering up to GBP 2 000 for smaller businesses to pay for practical support for importing and exporting, such as dealing with new customs, rules of origin, and VAT rules.
Put in place trade facilitation measures to smooth disruptions at the border.	The introduction of further border checks on EU imports is being phased in gradually from 2023.

The labour market is tight

The labour market bounced back quickly from the pandemic shock, with the number of vacancies reaching a record high of almost 1.3 million in the first quarter of 2022 (Figure 1.8, Panel A). Government support through the job furlough scheme helped to keep the rise in unemployment contained during the pandemic (OECD, 2020[1]). After peaking at 5.2% in the fourth quarter of 2020, unemployment fell to a pre-pandemic low of 3.7% in the first quarter of 2022. The gradual phasing out of the furlough scheme ensured a smooth transition and did not lead to a pick-up in unemployment once the scheme ended in October 2021. The COVID-19 crisis disproportionally affected the 16 to 25 years olds, with the employment rate declining, and their economic inactivity and unemployment rates rising by more than those aged 25 and over (Office for National Statistics, 2021[6]). However, individuals aged under 25 were also quicker in finding a job once restrictions eased. By contrast, inactivity rates increased for people aged 55 and older as the pandemic continued, with many of them dropping out of the labour force and entering early retirement. The overall inactivity rate remains above pre-pandemic levels mainly due to people studying and due to long-term sickness (Figure 1.8, Panel B), a development that is not unique to the United Kingdom (Box 1.3).

Figure 1.8. The labour market has rebounded



Note: Panel A: Vacancies exclude agriculture, forestry and fishing. Latest data refers to Mar-May 2022. Panel B: Shows changes between the fourth quarter of 2019 and the fourth quarter of 2021.
Source: ONS, labour market statistics.

Labour shortages have been partially exacerbated by reduced net migration. Towards the end of 2021, labour shortages predominantly emerged in low-skilled sectors that were particularly affected by the pandemic and those in which a high share of EU-born migrants were working, such as the hospitality sector (13% of workers) and the transport and storage sector (11% of workers) (Office for Budget Responsibility, 2021[7]; Fernández-Reino and Rienzo, 2021[8]). Surveys suggest that half of all firms are having difficulty recruiting new workers, while around one in five firms are having issues retaining existing staff. Although most of the shortages can be explained by economic restructuring due to the pandemic, one in ten firms report that the UK's point-based immigration regime is causing labour shortages (De Lyon and Dhingra, 2021[9]). From 2019 to 2020, immigration is estimated to have fallen between 50% and 60% (Office for National Statistics, 2021[10]), although these numbers should be taken cautiously because of difficulties in data collection during the pandemic and a change in methodology (Box 1.4). Immigration of EU-born nationals decreased slightly more than that of non-EU nationals (around 67% compared to 50%), a trend

that is likely to have continued following the end of free movement of labour between the United Kingdom and the European Union since January 2021. In the context of a tight labour market, the government should ensure that the migration system is sufficiently flexible to quickly address rising labour shortages.

Box 1.3. Labour market participation in the US after the heights of the pandemic

In the US, the employment-to-working age population ratio fell by 10 percentage points between January and April 2020. While the employment fall was more gradual in the UK, reaching a maximum of 2 p.p. in the fourth quarter of 2020 relative to 2019Q4, both countries found themselves in similar situations regarding labour market tightness. Employment in the US gradually recovered, but the aggregate labour force participation rate remains below the pre-pandemic level and about 0.4 percentage points below where the Congressional Budget Office expected it to be in their pre-pandemic forecast. This mostly reflects the significant decline in the participation rate of older workers. In particular, there has been a fall in the share of existing retirees transitioning back into the labour force. In addition, a continued decline in immigration, from a combination of the pandemic along with pre-pandemic policies, has also weighed on labour supply and the participation rate. While concerns about contracting COVID-19 may have kept some from returning to work, especially those previously in face-to-face industries with heightened transmission risk, recent numbers suggest that it is unlikely that there will be a large increase in the number of older workers who have moved into retirement re-entering the labour force.

Source: OECD Economic Survey of the USA 2022, forthcoming.

Box 1.4. EU migration post-Brexit

Before Brexit, free movement rules gave EU citizens the right to live and work in the United Kingdom without requiring permission. As of 1 January 2021, EU citizens (except Irish citizens) who wish to move to the United Kingdom are subject to the same new Points Based Immigration System that also applies to non-EU citizens. The Point Based Immigration System is aimed at the most highly skilled workers, skilled workers, students and a range of other specialist work routes including those for global leaders in their field and innovators. For the skilled worker route, points are awarded for a job offer at the appropriate skill level, knowledge of English and being paid a minimum salary. People will normally need to be paid at least GBP 25 600 per year, have enough money to pay the application fee, the health care surcharge and be able to support themselves. The visa lasts for up to five years before it needs to be extended. Alongside the skilled worker route, several other new routes have opened over 2019 and 2020 including Global Talent, Innovator, Start-up, Graduate, Student and Child Student, Further routes are opened in 2022 for entrepreneurs and highly skilled people, including the Global Business Mobility route (April 2022), the High Potential Individual route (May 2022) and the Scale-Up route (August 2022).

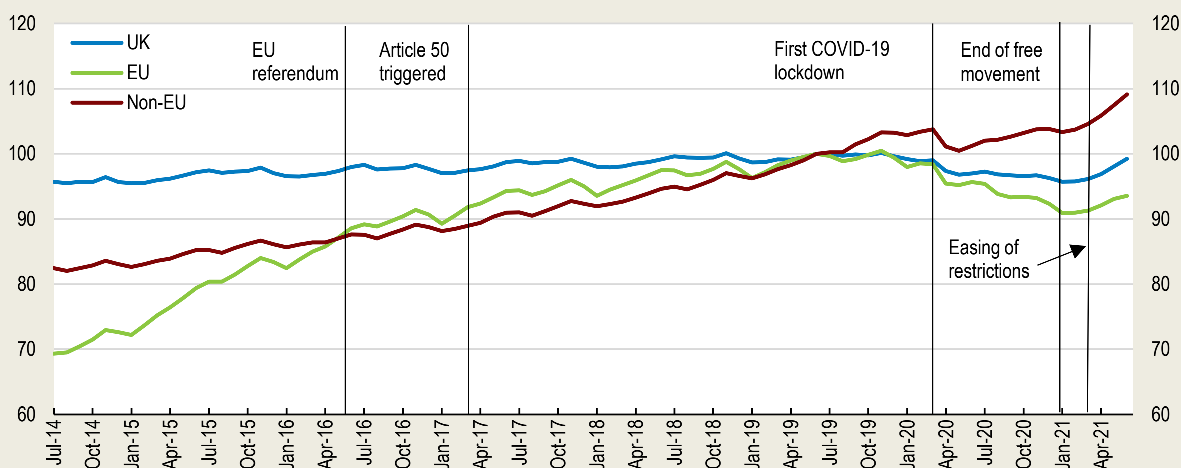
Effect of new rules on EU migration

The end of free movement for EU citizens coincided with the COVID-19 pandemic. It can be expected that both the pandemic and Brexit have fundamentally changed migration patterns in and out of the United Kingdom. The effect is still unclear due to data collection issues and changes in methodology. The usual source for measuring migration in the UK, the International Passenger Survey (IPS), was suspended at the start of the pandemic. Instead, the ONS developed experimental statistical models which indicate that EU net migration was negative in 2020, with an estimated 94 000 more EU nationals leaving the UK than arriving. EU immigration dropped considerably in 2020 compared with previous years, while numbers of EU people emigrating held steady (Office for National Statistics, 2021[10]). In

addition, the ONS estimated the number of migrants in the United Kingdom using payroll information (Figure 1.9), which show a decline in pay-rolled employment held by EU nationals since the onset of the pandemic, and although there is a slight improvement from 2021 onwards, it is not as pronounced as for non-EU nationals.

Figure 1.9. The number of pay-rolled employment held by EU nationals has declined

Change in pay-rolled employments by nationality, June 2019 = 100 (non-seasonally adjusted)

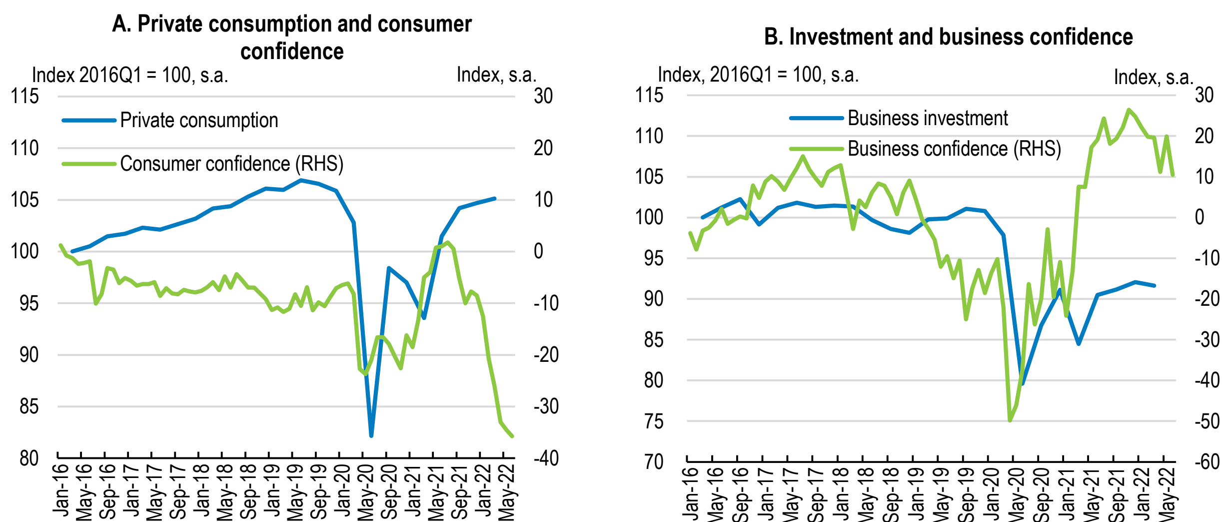


Source: OECD (2021[11]); Office for National Statistics (2021[12]); Figure: Office for National Statistics (2022[13]).

Consumption has supported growth but confidence is deteriorating

Private consumption fuelled the recovery as containment restrictions were eased (Figure 1.10, Panel A). However, consumption remains volatile, in particular as the cost of living is rising as reflected by developments in consumer confidence. While consumer confidence has plummeted amid rising goods and energy prices (see below), further aggravated by spill over effects from the Ukraine war, business confidence so far remains well above pre-pandemic levels. Business investment gradually improved following the COVID-19 crisis aided by tax incentives (Figure 1.10, Panel B), but remains subdued and below pre-pandemic level. To support business investment, the government announced a two-year tax "super-deduction" in the March 2021 budget. Companies investing in new assets between 1 April 2021 and 31 March 2023 can claim a 130% capital allowance on qualifying plant and machinery investments and a 50% first-year allowance for qualifying special rate assets.

Figure 1.10. Investment is recovering but confidence is volatile



Note: Panel B: Business confidence refers to the manufacturing sector. Business investment refers to private non-residential gross fixed capital formation.

Source: OECD (2022), OECD Economic Outlook: Statistics and Projections (database); and OECD (2022), OECD Main Economic Indicators (database).

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Low income households are pressured by rising cost of living

Quickly rising cost of living have resulted in increasing pressure on people's incomes. As a response, the government introduced several measures to aid households with rising energy costs in February and March 2022. In May 2022, the government introduced new measures totalling GBP 15 billion (about 0.7% of GDP), which provide temporary support to households with rising energy costs mainly targeted to those most in need. About 8 million households on means-tested tested benefits will receive a one-off payment of GBP 650 this year paid in two instalments, and one-off payments of GBP 300 will go to pensioner households and GBP 150 to individuals receiving disability benefits. The previously announced energy discount for 2022 is doubled to GBP 400 per household and becomes non-repayable. This targeted and temporary support is welcome as it helps to temporarily ease the financial distress of the most vulnerable households.

The May measures came on top of previously announced measures bringing total support in 2022 to a sizable GBP 37 billion (1.5% of GDP). Previous measures announced include, in March, a GBP 5p per litre cut in fuel duty, an increase in the national insurance threshold, zero-VAT on energy efficiency home improvements and an extra GBP 500 million for the household support fund managed by local councils, and in February a GBP 200 discount on energy bills and a targeted GBP 150 rebate on council tax. These measures are welcome. The May package in particular is better targeted at low-income households and those out of work.

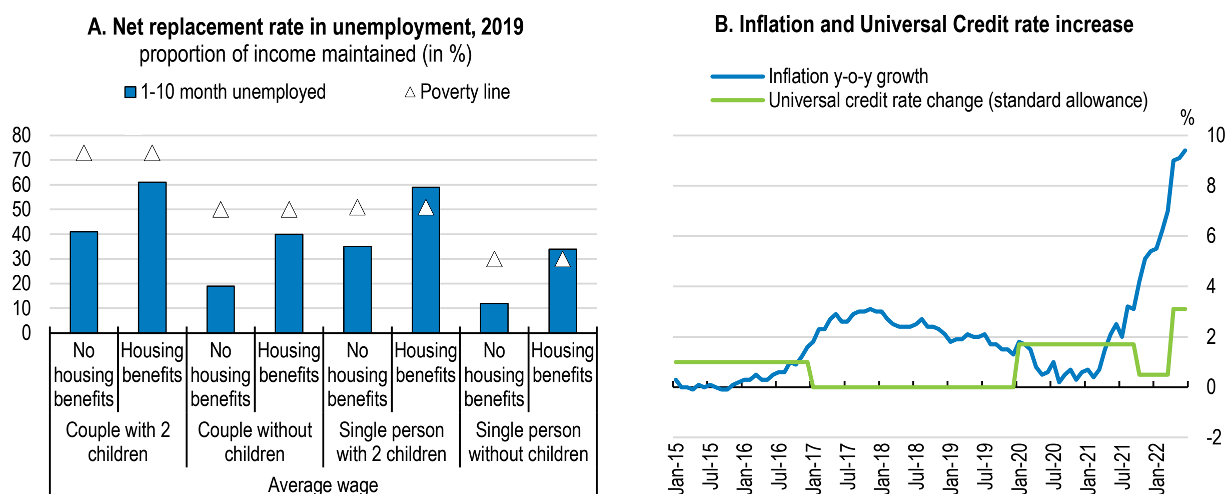
Part of the May support package will be financed by higher borrowing, and GBP 5 billion will be funded by a new Energy Profits Levy. However, to ensure that investment continues to take place in UK oil and gas extraction, the government introduced within the Energy Profits Levy a new 80% investment allowance. While higher UK extraction reduces dependence of imports of fossil fuels, the government should also consider expanding the investment allowance to include renewables to aid the transition to net zero.

Apart from temporarily introduced measures, people with low income, who are out of work or who are unable to work can receive benefits of the Universal Credit, the main support to cover living costs. The Universal Credit integrates a number of the legacy system's benefits and aims at simplifying access and

extending the existing activation efforts across all benefits (OECD, 2020[1]). During the height of the COVID-19 crisis, the government swiftly adapted the claim process and temporarily lifted payments by GBP 20 per week. Although this timely government response successfully avoided an increase in income inequalities during the pandemic, non-working households were worse off in real terms as this temporary support was withdrawn in October 2021 (Brewer and Tasseva, 2021[14]; Bronka, Collado and Richiardi, 2020[15]; HM Treasury, 2020[16]; Waters et al., 2020[17]). Rising inflation since mid-2021 has contributed to a significant decline in real terms of Universal Credit. In the Autumn Budget 2021, the government announced to increase earnings for working universal credit recipients by raising work allowances by GBP 500 a year and reducing the taper rate from 63% to 55%, which reduces the impact of the withdrawal of the GBP 20 per week raise and increases work incentives. This is welcome. However, at the beginning of 2022, the basic level of Universal Credit in real terms had fallen 11.5% below its value when introduced in 2013.

At present, the targeted support to deal with cost of living is sizable and well targeted and will provide support to vulnerable households. However, in the longer term, the government should follow its annual uprating of universal credit as planned and ensure that it is adequate to cover the minimum living standard. Economic restructuring linked to the digital and green transition is likely to accelerate in coming years leading to rising unemployment among workers, especially low skilled workers, and such strengthened safety net could help address persistently high income inequality in the United Kingdom (OECD, 2018[18]). And, already before the pandemic, Universal Credit did not provide a sufficient safety net (Figure 1.11, Panel A). The government froze Universal Credit benefit levels as part of the post-financial crisis fiscal consolidation between 2017 and 2020 (Figure 1.11, Panel B). Moreover, unemployment benefits for many households remain below the levels of many other OECD countries and poverty rates are highest among households out of work (OECD, 2020[1]).

Figure 1.11. Unemployment benefits are low and uprating of Universal Credit has fallen behind inflation growth



Note: The indicator is the ratio of net household income during a selected month of the unemployment spell to the net household income before the job loss. Calculations refer to a jobseeker aged 40 with an uninterrupted employment record since age of 19 until the job loss. For a detailed description of the assumptions underlying the OECD Tax-Benefit model and the related policy indicators, please see the source.
Source: OECD (2022), Social protection and well-being database; UK Government, department for Work and Pensions; and ONS.

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Economic growth will continue to slow

Growth is slowing amid persisting supply shortages and rising inflation. Output is projected to grow by 3.6% in 2022 before stagnating in 2023 due to depressed demand (Table 1.2). Inflation will continue to rise, peaking at just over 10% in the fourth quarter of 2022, driven by increasing global prices of tradable goods and services due to continuous supply bottlenecks and higher global energy prices. Continued tightness of the labour market is expected to feed through to higher wage growth in 2022 and 2023, but with wage growth remaining below inflation. Tighter monetary policy and easing supply constraints over 2023 are expected to help inflation decline to 4.7% by the end of 2023.

Private consumption is expected to slow as rising prices erode households' income. However, spending will be supported by further declines in the households saving rate to below pre-pandemic levels, with some households taking on more debt to keep up with the rising cost of living. Unemployment is set to remain low but gradually increase to 4.5% by the end of 2023 due to weaker demand. Business investment will be supported by the super deduction for some types of investments available until April 2023, although the positive effect will be damped by rising interest rates, high energy prices and lingering uncertainties. Trade intensity with trading partners in Europe will decline, as growth in Europe is expected to slow amid the EU embargo on Russian oil. Public investment will be affected by supply shortages in 2022, hindering planned investment, but is expected to pick up in 2023 with planned spending increases on infrastructure and climate. The general government deficit is projected to decline gradually to 5.3% of GDP in 2022 and 4.1% of GDP in 2023.

Table 1.2. Macroeconomic indicators and projections

Annual percentage change, volume (2019 prices)

	2018	2019	2020	2021	2022	2023
	Current prices (EUR billion)					
Gross domestic product (GDP)	**2,174.4**	**1.7**	**-9.3**	**7.4**	**3.6**	**0.0**
Private consumption	1,412.3	1.3	-10.6	6.2	4.5	0.7
Government consumption	399.0	4.2	-5.9	14.3	1.4	0.8
Gross fixed capital formation	386.5	0.5	-9.5	5.9	8.0	2.1
Housing	112.0	-2.5	-12.2	13.8	7.7	0.0
Business	217.3	0.9	-11.5	0.8	4.3	1.9
Government	57.2	5.0	2.6	9.6	19.2	5.7
Final domestic demand	2,197.8	1.7	-9.5	7.9	4.5	1.0
Stockbuilding[1]	4.9	-0.1	-0.6	0.6	3.5	0.0
Total domestic demand	2,202.7	1.6	-10.2	8.3	8.0	0.9
Exports of goods and services	663.3	3.4	-13.0	-1.3	0.9	1.5
Imports of goods and services	691.6	2.9	-15.8	3.8	15.7	3.6
Net exports[1]	-28.3	0.1	1.0	-1.4	-4.2	-0.7
Other indicators (growth rates, unless specified)						
Potential GDP	. .	1.8	1.5	-1.2	1.1	1.1
Output gap[2]	. .	-0.6	-11.1	-3.3	-0.9	-2.0
Employment	. .	1.1	-0.8	-0.5	0.9	0.5
Unemployment rate	. .	3.8	4.5	4.5	3.8	4.3
GDP deflator	. .	2.0	5.1	0.3	5.7	4.9
Consumer price index (harmonised)	. .	1.8	0.9	2.6	8.8	7.4
Core consumer prices (harmonised)	. .	1.7	1.4	2.4	6.4	5.9
Household saving ratio, net[3]	. .	-1.6	8.2	4.4	-1.5	-5.3
Current account balance[4]	. .	-2.7	-2.5	-2.6	-7.2	-7.6
General government fiscal balance[4]	. .	-2.3	-12.8	-8.3	-5.3	-4.1
Underlying general government fiscal balance[2]	. .	-2.0	-5.1	-6.2	-4.8	-3.0

Underlying government primary fiscal balance[2]	. .	-0.1	-3.6	-3.9	-2.0	-0.2
General government gross debt[4]		118.5	149.1	143.1	139.2	138.6
General government net debt[4]	. .	84.7	109.3	105.0	101.1	100.5
Three-month money market rate, average	. .	0.8	0.3	0.1	1.4	2.4
Ten-year government bond yield, average	. .	0.9	0.4	0.8	1.8	2.5

1. Contribution to changes in real GDP.
2. As a percentage of potential GDP.
3. As a percentage of household disposable income.
4. As a percentage of GDP.
Source: OECD Economic Outlook 111 database.

Risks to the outlook are considerable. Spill-overs from economic sanctions, higher than expected energy prices as the Ukraine war drags on, and a deterioration in the public health situation due to new COVID strains are significant downside risks (Table 1.3). The United Kingdom has limited direct trade and financial linkages with Russia and Ukraine, but higher global energy prices and further economic slowdowns in major European trading partners could add to higher than expected goods and energy prices weighing on consumption and further lower growth. A prolonged period of acute supply and labour shortages could force firms into a more permanent reduction in their operating capacity. Progress in trade deals could support trade and improve the medium- to long-term outlook.

Table 1.3. Events that could lead to major changes in the outlook

Uncertainty	Possible outcomes
Pandemic outbreaks	Reduction of activities where distancing is a concern could lead to firm failures and increased unemployment. Highly contagious forms of the virus could affect the provision of labour due to isolation and quarantine requirements.
Intensified and prolonged geopolitical conflicts in Europe	Spill-overs from Russia's invasion could drive up energy prices, as the Ukraine war drags on, squeezing household incomes and slowing down economic growth on the back of lower consumption.

Monetary policy should continue to tighten to curb the risk of a de-anchoring of inflation expectations

Inflationary pressures started to mount in the second half of 2021 on the back of supply and labour shortages and rising energy prices. CPI inflation rose from 2% in summer 2021 to 9.4% in June 2022 (Figure 1.12, Panel A). The surge reflects elevated energy and goods prices, largely determined by global markets, global supply shortages and strong (pent-up) demand for goods exacerbated by higher energy prices following Russia's invasion of Ukraine. Administrative trade costs have increased due to Brexit. Core inflation has significantly picked up as well (Figure 1.12, Panel A) and inflation expectations have increased. Tight labour markets, with high turnover and record vacancies have led to solid wage growth since 2021, reaching 4.8% year-on-year in January 2022 and surveys point at continued strong pay growth in 2022; the government also implemented a 6.6% increase in the minimum wage in April 2022.

Monetary policy, highly accommodative during the pandemic, started tightening from end-2021. In March 2020, the Bank of England (BoE) cut the bank rate from 0.75% to 0.1% and increased its bond purchasing programme over the course of the crisis to a total of GBP 895 billion (about 44% of GDP in 2020) (Figure 1.12, Panel B). Since December 2021, the BoE gradually has increased the policy rate from 0.1% to 1.25% in June, on the back of the recovery and rising inflation pressures (Figure 1.12, Panel C). The BoE ended its quantitative easing program in December 2021. In February 2022, the BoE decided not to reinvest any future maturities and announced to gradually sell its stocks of sterling corporate bonds and end the program towards the end of 2023. A strategy for selling the stock of government bonds will be discussed at the August 2022 monetary policy meeting.

In the context of high inflation and rising wages, further tightening of monetary policy is welcome to support the return of inflation to target and to anchor inflation expectations, which remain elevated at around 6% for the next 12 month as measured by the YouGov/Citigroup survey in June 2022. Clear and carefully communicated forward guidance will be important to limit second-round effects and avoid uncertainty. The decline in asset holdings should continue to follow a predictable and well-communicated strategy to guide markets and reduce financial stability risks. As planned, the Bank should outline a clear quantitative tightening strategy to manage market expectations.

Figure 1.12. Monetary policy, supportive during the crisis, has started to tighten

A. Headline and core inflation

B. Quantity of assets purchased by the creation of central bank reserves on a settled basis
in sterling billions

C. Bank rate

Source: ONS; and BoE.

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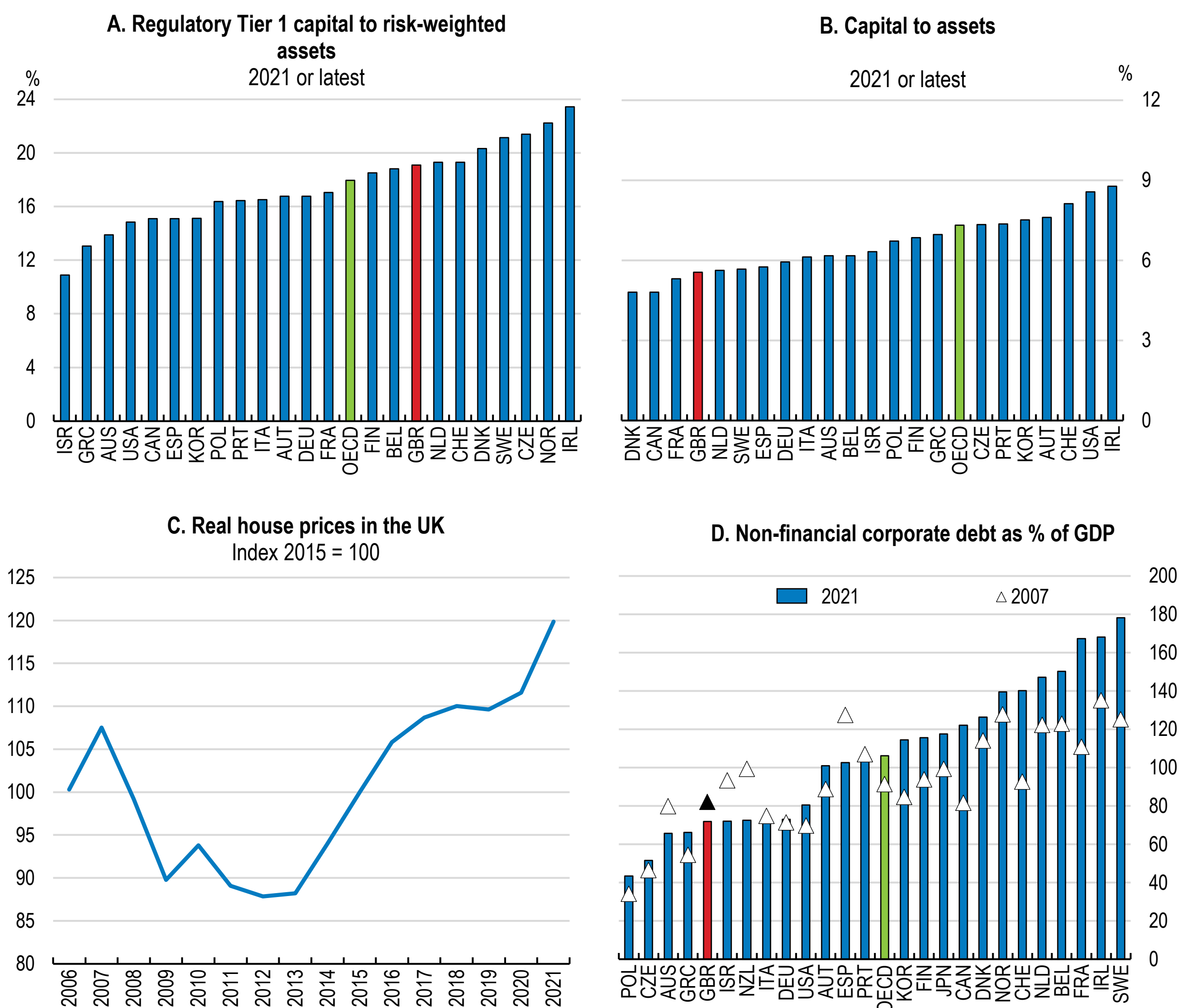
The financial system withstood the shock from the COVID-19 crisis and the withdrawal from the EU Single Market

The banking sector entered the pandemic well capitalised, allowing it to absorb the effects of the pandemic and continue to provide services to households and businesses. While banks are still highly leveraged in gross terms, average risk-weighted capital is around the OECD average (Figure 1.13, Panels A and B).

To prevent financial tightening that could exacerbate the crisis, the Bank of England lowered the countercyclical capital buffer during the pandemic. Multiple government support schemes also softened the pandemic's impact and contained insolvencies. Government loan schemes supported SMEs who bore the brunt of COVID-19. Income support through the furlough scheme and payment deferrals supported households. The share of non-performing loans increased somewhat at the start of the pandemic, but remained relatively low and is gradually declining (Bank of England, 2021[19]).

Figure 1.13. The banking system is well capitalised



Source: IMF (2021), IMF Financial Soundness Indicators Database; OECD (2021) National accounts at a glance; and BIS.

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The economic consequences of the pandemic will take time to resolve and some of the impact is only now becoming visible as support measures are withdrawn. A recent stress test by the Bank of England (2020[20]) suggests that the financial sector could withstand a very severe downturn in addition to the COVID-19 pandemic shock of 2020.

Risks arising from rapidly rising house prices remain contained, but vigilance remains warranted. House prices increased by 11.8% over the year to September 2021 fuelled by increased demand as a result of the pandemic, supply pressures and tax incentives (Figure 1.13, Panel C). But compared to before the

pandemic, high loan-to-value mortgages remain a smaller share of new mortgages (Bank of England, 2021[21]). Most households that benefited from mortgage payment deferrals at the start of the pandemic have restarted full or partial repayments (Bank of England, 2021[22]). In June 2022, the Bank of England's Financial Policy Committee announced the removal of the affordability test, which assesses whether the borrower could afford payments if the policy rate increases by three percentage points above their reversion rate specified in the mortgage contract. Removing this test simplifies the framework and reduces constraints for some borrowers. The Loan to Income (LTI) flow limit, which is seen as more effective, remains in place in addition to the affordability measures of the Financial Conduct Authority (Bank of England, 2021[19]). Because the FCA affordability test is less stringent on average over interest rate cycles, it is important that the effect of simplification is monitored to ensure macroprudential tools contain risks from the mortgage market for the UK banking system and remain effective.

Corporate debt has increased during the pandemic, including borrowing from government support packages, but corporate debt levels remained well below the OECD average as a percentage of GDP in 2020 (Figure 1.13, Panel D). Simulations show that it would take a large shock to impair business ability to service their debt on aggregate (Bank of England, 2021[19]). However, some pockets of risk exist due to the uneven distribution of debt (Bank of England, 2021). For instance, debt held by SMEs has increased. Risks to lenders are limited as the majority of lending through the pandemic occurred with government guarantees, at low and fixed interest rates (Bank of England, 2021[19]). Insolvencies have been rising to pre-pandemic levels (see above), but already before the pandemic, UK's insolvency regime was fairly efficient and greater flexibility was provided through the 2020 Corporate Insolvency and Governance Act. The insolvency regime should therefore be able to deal with a rise in cases (Adalet McGowan and Andrews, 2018[23]; OECD, 2020[1]). In addition, UK banks hold around GBP 31 billion in provisions to deal with future credit losses (Bank of England, 2021[19]).

As the immediate effects of the pandemic fade, macrofinancial vulnerabilities may emerge as the consequences of leaving the European Union and the transition to net zero come to the forefront. With the departure from the European Union, some segments of the financial sector based in the United Kingdom can no longer directly service EU clients through the EU passporting regime as they could previously. Access to EU labour has become more cumbersome due to new visa regulations. However, the transition so far has occurred smoothly (see Box 1.5). The long-term impact of leaving the EU Single Market on the UK financial sector remains uncertain. The government is using its new powers to replace the EU financial services framework and will introduce a financial services and markets bill this year. This will include updating the objectives of the financial regulators and revising capital markets regulation. The government is consulting to better understand how reforms to insurance regulation (Solvency II) would enable insurance firms to invest more in long-term infrastructure products and hold less capital (Glen, 2022[24]). Although some adjustments to insurance regulation are warranted - the European Union is going through a similar process - and incentivising private sector investment in longer term and more illiquid assets is positive, the development of new regulation should be approached carefully and financial stability implications, and costs to policyholders, should continue to feature prominently.

Adjusting to the pandemic, Brexit and net zero will require some reallocation of labour and capital. UK SMEs are largely dependent on bank funding, but larger firms rely heavily on market funding. The resilience of the banking system and a return to risk appetite mean lending conditions to firms remain supportive while large firms maintained access to market-based funding (Bank of England, 2021[19]).

Transitioning to net zero provides investment opportunities, but may also put additional pressures on financial institutions, particularly in the transition phase. Climate change increases the scale and frequency of natural disasters such as floods and storms, raising the claims burden for insurers and re-insurers, even though this will be reflected in premiums over time. In 2021, the Bank has launched the Climate Biennial Exploratory Scenario (CBES) exercise to assess the resilience of major UK banks, insurers, and the wider financial system to different climate scenarios, which is a timely innovation.

Box 1.5. The effect of leaving the European Union on the financial services sector

In financial services, an important source of the UK's comparative advantage, market access between the UK and the EU is to a significant extent managed through equivalence, where either side can grant the other equivalent status in relation to a number of legislated areas. In November 2020, the UK published a guidance document setting out its approach to operating its equivalence framework and granted a package of equivalence decisions in respect of the EEA states. The UK has replicated most of the equivalence determinations in respect of overseas jurisdictions made by the European Commission pre-Brexit. As of November 2021, 32 jurisdictions plus the EEA benefit from UK equivalence decisions The European Union granted equivalence for UK regulatory standards only temporarily and in specific areas, such as derivatives clearing.

Following its departure from the European Union, the United Kingdom needs to establish an independent regulatory framework. At the point of EU exit, directly applicable EU legislation (including that relating to financial services) was brought into the UK law so that it would continue to have effect in the UK after withdrawal. This "retained EU law" was amended as necessary to ensure that it would continue to operate effectively in the UK after exit (a process known as "onshoring"). This provided continuity and stability at the point of exit, but it was not intended to be a permanent approach to financial services regulation. This retained EU law will now be repealed so that regulation in these areas can be brought into line with the UK's domestic model of regulation where the design and implementation of firm-facing rules is the responsibility of the UK regulators (Bank of England (BoE), Prudential Regulation Authority (PRA), and Financial Conduct Authority (FCA)). The goal of the UK government is to create a financial services sector, built around four themes of Openness; Green Finance; Technology; and Competitiveness. The government intends to tailor its approach to financial services regulation to reflect the UK's new position outside the EU, while ensuring it supports and promotes the interests of UK markets and maintains high regulatory standards in the face of new and evolving risks. As announced in the Queen's Speech on 11 May 2022, the government will be bringing forward a Financial Services and Markets Bill, which will deliver on these commitments by implementing the outcomes of the Future Regulatory Framework (FRF) Review as well as a series of important initiatives underpinning the government's vision.

The transition to the new regime on January 1, 2021, went smoothly thanks to joint efforts by financial firms and UK authorities. There are no formal statistics on the number of UK-based financial services jobs that have moved from the United Kingdom to the European Union, but estimates suggest around 7 000 jobs have been relocated by March 2022 (EY, 2022[25]), which remains well below most estimates before EU exit. The long-term impact of EU exit on the UK financial sector remains unclear.

Some aspects of EU exit were phased in gradually, including:

- A **Temporary Transition Power (TTP)** given by HMT to the FCA, PRA and BoE allowed them to temporarily waive or amend rules post-Brexit until end-March 2022 or December 2022. In the areas where TTP relief ended in March 2022, there has been no material disruption as a consequence.
- The **Temporary Permissions Regime** (TPR) allows temporary continued access to the UK market for EEA-based firms that were passporting into the United Kingdom at the end of the transition period (31 December 2020). During the temporary period of access, the firms must seek full authorisation by the Prudential Regulatory Authority (PRA) or the FCA as required in the UK to continue to access the UK market (FCA, 2018). This will happen in a staggered process. Around 1500 EEA-based firms entered the FCA Temporary Permissions Regime at the beginning of 2021. The Temporary Permissions Regimes will expire at the end-2023.

- **Derivative Clearing**: The European Union has granted the United Kingdom temporary equivalence status with regard to clearing, allowing EU derivatives to be cleared in the United Kingdom. This permission expires in 2025.

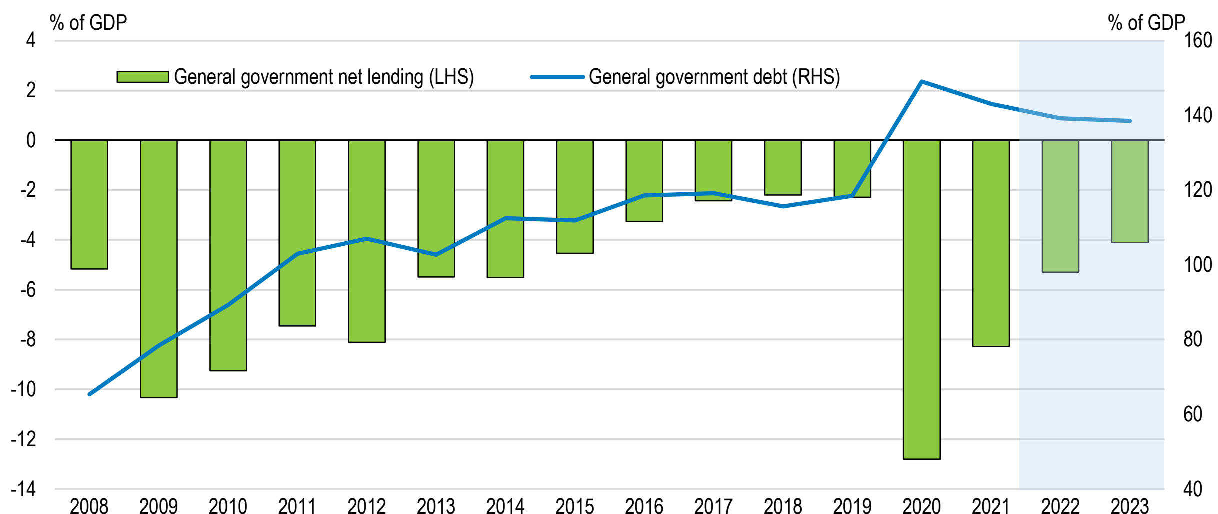
Source: FCA (2021), "Seizing opportunity – challenges and priorities for the FCA". https://www.fca.org.uk/news/speeches/seizing-opportunity-challenges-priorities-fca; FCA (2020), "Onshoring and the Temporary Transitional Power", https://www.fca.org.uk/brexit/onshoring-temporary-transitional-power-ttp; FCA (2018), "Temporary permissions regime", https://www.fca.org.uk/brexit/temporary-permissions-regime-tpr.

Fiscal policy has to balance consolidation with supporting growth and addressing investment needs

Tax increases will contribute to a declining fiscal deficit

The pandemic triggered a strong fiscal response of around 19% of 2020 GDP by September 2021 supporting household incomes and attenuating the rise in unemployment and business insolvencies (IMF, 2021[26]). The budget deficit rose to a record -12.8% in 2020 and gross public debt increased by 36 percentage points (Figure 1.14). As the main support measures were phased out in October 2021, the fiscal balance improved and gross public debt declined to 143.1% of GDP in 2021.

Figure 1.14. The pandemic led to a record high budget deficit that pushed up public debt



Source: OECD (2022), OECD Economic Outlook: Statistics and Projections (database), June.

The government has committed to a gradual medium-term fiscal consolidation plan and to increased tax revenues. National-insurance contributions rose by 1.25% from April 2022 to fund health and social care spending while tax free allowances and higher rate thresholds for income tax are frozen until 2025-26, a policy that now has a bigger positive impact on revenues than anticipated when introduced in early 2021 due to high inflation. The corporate income tax rate will increase from 19% to 25% in April 2023. These tax changes will result in an increased overall tax intake from 33% of GDP in 2019-20 to almost 37% of GDP in 2026-27 as forecasted by the OBR, despite a hike in the national insurance threshold and a cut to income tax in 2024 (Institute for Fiscal Studies, 2022[27]; Office for Budget Responsibility, 2022[28]). Overall, tax changes will put a higher share of the burden on richer households and will be progressive (Institute for

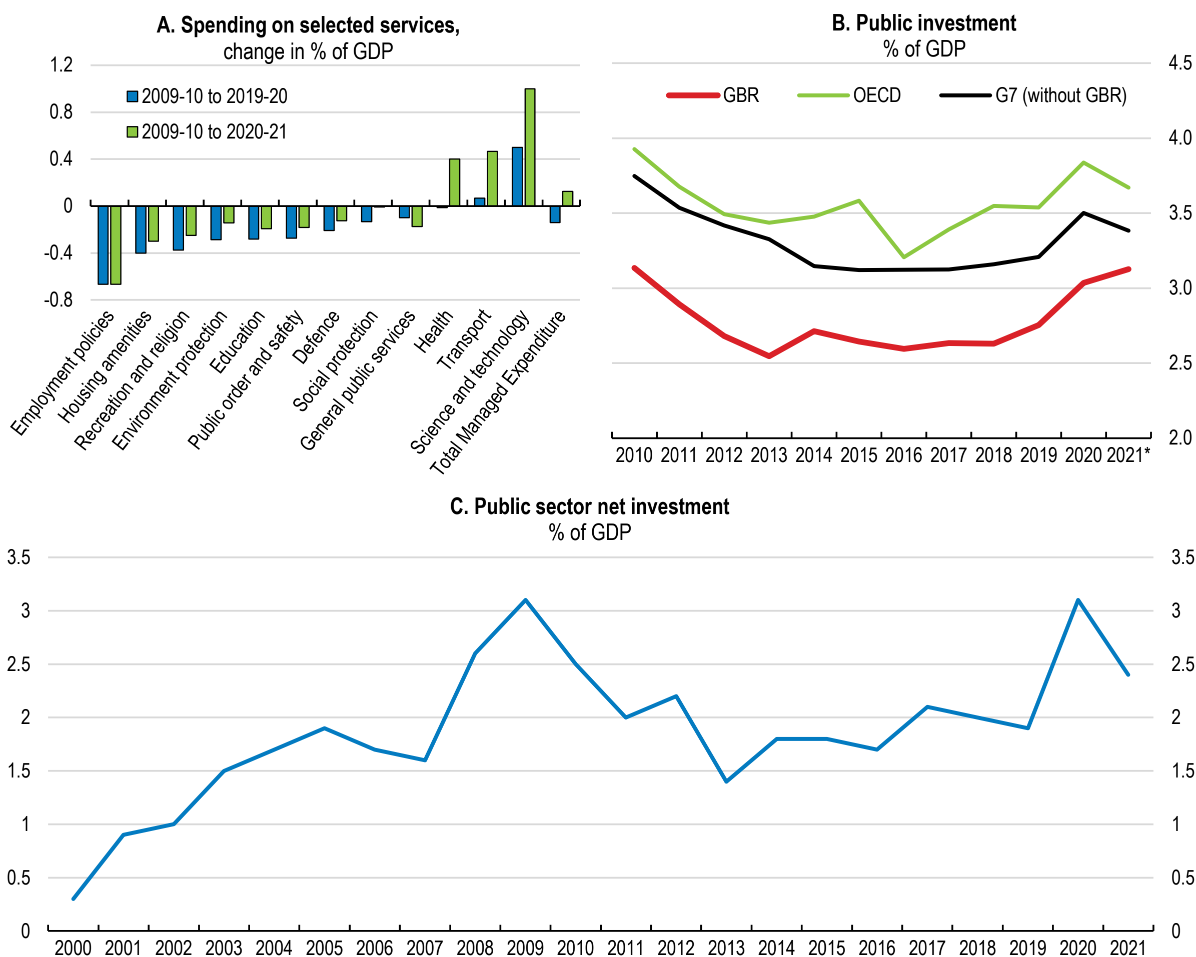
Fiscal Studies, 2022[27]), but still imply a higher individual tax liability for almost all workers in the coming years. Based on government medium term plans, the deficit will fall from about 15% in 2020-21 to around 1% of GDP in fiscal year 2024-25, with the largest fiscal withdrawal happening in 2023-24. Public net debt will fall from 96.5% of GDP in 2021 to 88% of GDP by 2025-26.

Fiscal consolidation will need to accommodate significant investment and spending needs

Fiscal policy will need to balance consolidation with public investment and spending needs. Planned higher spending and investment over the coming years is welcome after a decade of fiscal restraint and low public investment. But current plans still leave some areas (including employment policy and education) with more limited funding than before the global financial crisis (Figure 1.15, Panel A) and substantial investment is needed to address the green transition and levelling up agenda to reduce regional inequality. In 2020 and 2021, the government announced departmental spending increases of over 2% of GDP (Office for Budget Responsibility, 2021[7]). By 2024-25, public spending will be 41.6% of GDP - a historic high - of which 8.4% is allocated to health, 5.4% to pensions, 5% to education and 4.8% to welfare (Office for Budget Responsibility, 2021[7]). Rising inflation and interest rates will lead to a spike in debt interest rate payments in 2022-23 before declining as inflation is forecasted to gradually fall (Office for Budget Responsibility, 2022[28]). The health and social care levy is expected to raise around GBP 18 billion by 2026-27 (Office for Budget Responsibility, 2021[7]). This should be sufficient to cover short-term health funding needs, although other constraints such as staffing shortages might remain and indicators point at intense pressures on the NHS. More funding might be required for social care and to deal with long-term health cost pressures (Paul Johnson et al., 2021[29]). In line with the 2017 Industrial Strategy and the 2021 Plan for Growth (Box 1.7), public sector net investment is projected to be 2.5% of GDP on average per year up to 2026-27 (Office for Budget Responsibility, 2022[28]; 2021[7]). This is above levels observed in the United Kingdom in the previous decades but remains below the OECD average (Figure 1.15, Panels B and C).

Spending and investment needs will remain high over the coming years, limiting the scope for tax cuts and requiring a focus on making the tax system more efficient and fairer. Tax revenues at 33% of GDP are lower than in peer European countries (Figure 1.16, Panel A), but are projected to reach about 37% of GDP the coming years (Office for Budget Responsibility, 2022[28]). A tax review into reliefs and allowances has been announced in the Spring Statement 2022 and is planned to go ahead before 2024 (HM Treasury, 2022[30]), which is welcome. It will be particularly important to review the existing tax and spending mix with a focus on ending reliefs and exemptions that do not serve an economic, social or environmental purpose. Tax breaks that tend to benefit higher-income households can be gradually reduced to improve the effectiveness of the tax system and its redistributive effects. The VAT base is eroded by various (partial) exemptions that exist for a wide range of goods including some financial service activities, some vehicles or gambling and that contribute to significant VAT revenue shortfalls (Figure 1.16, Panel C). Broadening the VAT tax base while compensating poorer households, would reduce distortions and make the tax system more efficient and effective, as discussed in previous Economic Surveys (OECD, 2020[1]; 2017[31]). Council tax could be made fairer and less distortive by adjusting thresholds for higher property values or even a proportional rate and by updating outdated property values that determine the amount due, as recommended in previous Surveys (OECD, 2020[1]; OECD, 2015[32]; Institute for Fiscal Studies, 2020[33]). To improve efficiency, the government should also consider reducing further the gap between national insurance rates for the self-employed and employed, which has increased in 2021 (Johnson, 2021[34]), as recommended in the last Economic Survey.

Figure 1.15. Public investment and spending on services is improving



Note: Panel A: Enterprise and economic development and Agriculture, fisheries and forestry are excluded. Panel B: Public investment refers to gross investment to allow for international comparability; as 2021 data was not yet available for all OECD countries, for the OECD estimate of 2021, data available for 2021 or latest were used. Panel C: Excludes public sector banks.
Source: ONS; and OECD (2022), OECD Economic Outlook: Statistics and Projections (database).

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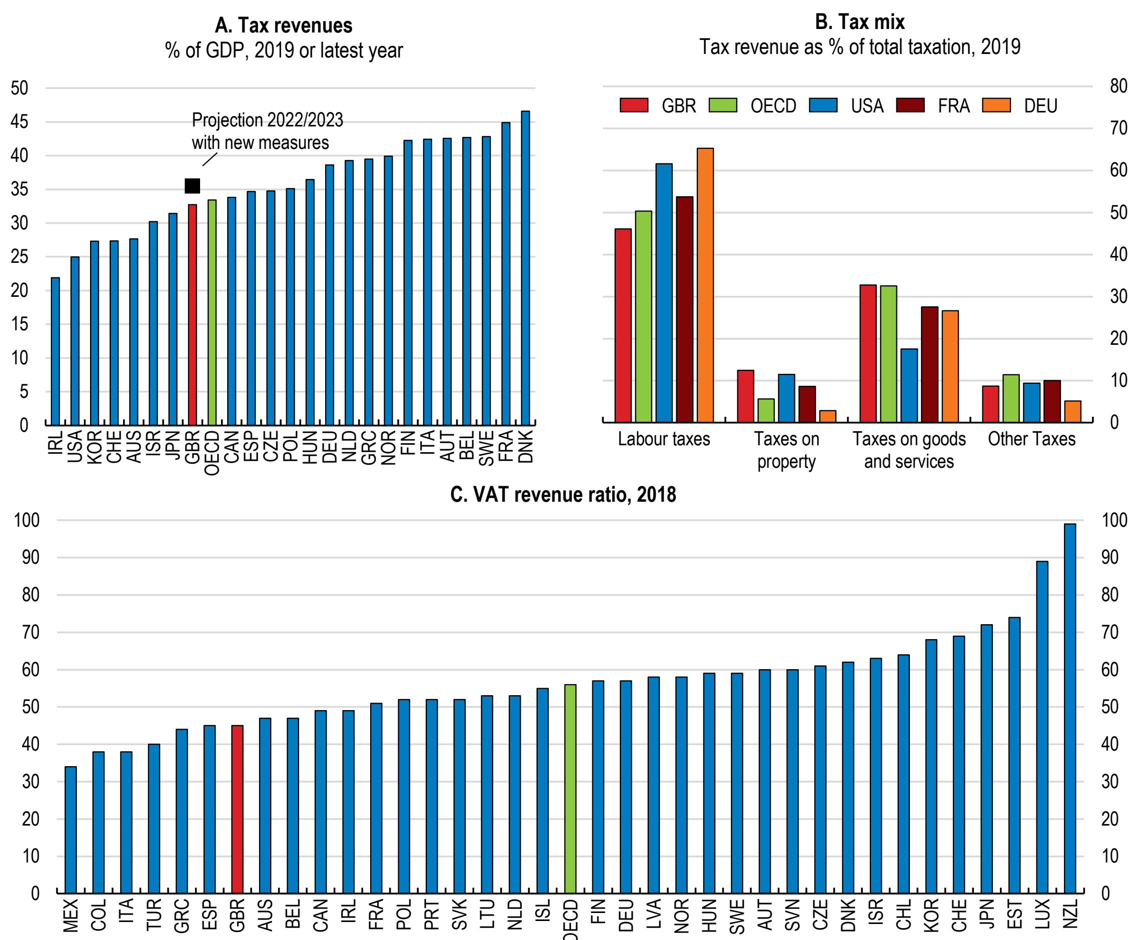
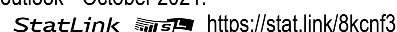
The government proposed new fiscal rules in the October 2021 Budget. A new core target is set as a declining net sector debt ratio (excluding the Bank of England balance sheet), by the third year of the rolling forecast period. Three supplementary targets aim at balancing the budget (excluding public investment) by the third year, ensuring public sector investment remains below 3% of GDP on average across the 5-year rolling forecast period and welfare spending remains below a cap set by the UK Treasury. The framework allows a suspension of the targets in case of a significant negative shock. The independent fiscal advisory council, the Office for Budget Responsibility, forecasts that the fiscal targets will be reached, including a declining net sector debt ratio. Hence, the framework provides guidance about the medium-term plan for returning to debt sustainability. Fiscal rules were introduced in the late 1990s and were revised in 2010. Since 2010, they have been revised three times amid large economic shocks. It should be ensured that changes to fiscal targets are both credible and relevant. Sweden for example reviews its fiscal target regularly under a disciplined process, thus revisions to the target are carried out in a predictable and credible way. The government has announced that its fiscal rules will guide its policy for at least this Parliament and will be reviewed at the start of each subsequent Parliament to support credibility and confidence in the UK's long-term fiscal trajectory.

Figure 1.16. Tax revenues are lower than in peer countries



Note: Tax revenues for GBR in 2022/2023 are projections from the last Economic Outlook report of the OBR.
Source: OECD (2022), OECD Tax Revenue Statistics (database); and OBR Economic and fiscal outlook - October 2021.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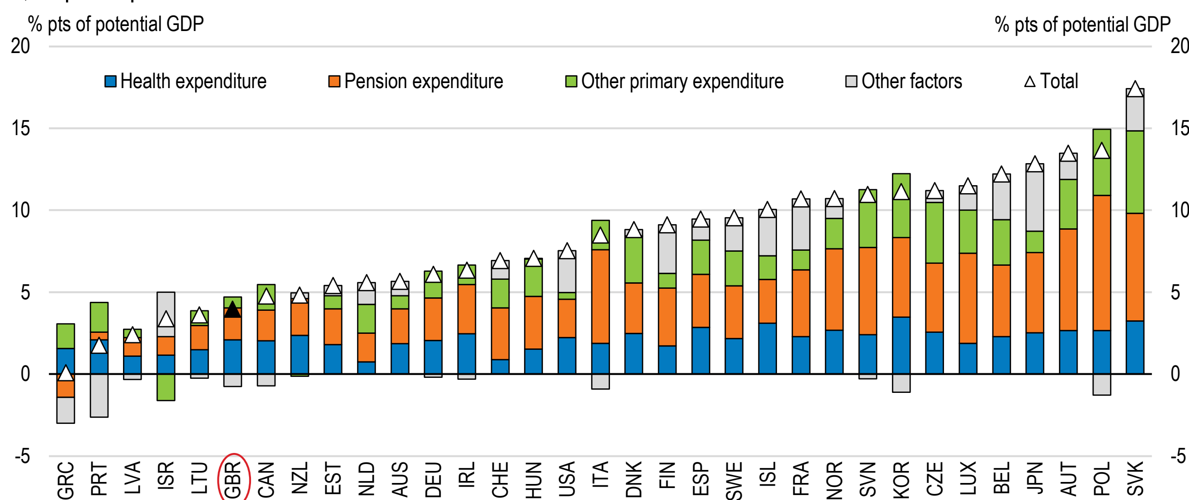
Ageing related expenses will put pressure on public finances

In the coming decades, the United Kingdom faces significant fiscal pressures mostly driven by ageing related increases in health, long-term care and pension expenditures. In a cross-country comparison these pressures appear mild as the structural primary revenue, or corresponding savings, would have to increase close to 5 percentage points of GDP to keep the current debt-to-GDP ratio constant (Figure 1.17). However, this does not take into account the effects of the green transition, which will require investment and lead to reduced revenue in the case of unchanged policy (Chapter 2). Under a baseline scenario of fiscal consolidation of about 1.5 percentage points of GDP over the next 10 years and no further reforms, ageing related costs would push up the public debt-to-GDP ratio close to 250% by 2060 (Figure 1.18, blue line). Transitioning to net zero will create some shortfalls in revenues, most importantly in fuel excise duty, which provides annual revenues of about 1.6% of GDP. Shifting to electric vehicles and phasing out all new petrol and diesel cars and vans by 2030 according to government plans will result in a gradual loss and increase in the public debt-to-GDP ratio beyond 250% by 2060 (Figure 1.18, orange line). As discussed in Chapter 2, the fuel excise duty targets a number of externalities from road use and is an important revenue source. It should therefore be replaced by a new system to tax road use. Greenhouse gas related revenues from an expanded UK ETS or carbon tax can help finance necessary green investments, offset negative distributional effects of carbon pricing and help secure public acceptance (Box 1.6).

In the absence of improved productivity to sustain economic growth, long-term fiscal sustainability will depend on prudent policies and the implementation of reforms. Spending on state pensions and pensioner benefits is expected to increase from 6% of GDP in 2021-22 to 8.2% in 2067-68 (Office for Budget Responsibility, 2021[35]). To contain the rise, the retirement age is set to gradually increase to 67 years by 2028 and has to be reviewed regularly as per the Pension Act 2014. Under triple lock rules state pensions are increased by the highest of inflation, average earnings growth or a flat 2.5% rise, which is expensive. The triple lock is suspended for one year over 2022-2023 and should be eliminated, as recommended in the previous Survey (OECD, 2020[1]). Replacing the lock with the indexation of pensions to an average of CPI and wage inflation would help to contain public debt substantially (Figure 1.18, green line; Box 1.6). Already replacing the triple lock with a more flexible system that allows deviations in case of unusual high earnings or inflation would give the government more control over long-term pension liabilities. In the United Kingdom, voluntary private occupational pension plans contribute more to gross pension replacement rates than state pensions (OECD, 2021[36]). The replacement rate for state pensions is lower than in many OECD countries putting pensioners without access to a private pension at risk of poverty. The reform of the triple lock should therefore be complemented by targeted direct transfers to limit the impact on poorer pensioners and limit poverty risks.

Figure 1.17. Ageing and health related expenditures add to future fiscal pressure

Change in structural primary revenue to GDP between 2021 and 2060 needed to stabilise the gross debt-to-GDP ratio, % pts of potential GDP



Note: The chart shows how the ratio of structural primary revenue to GDP must evolve between 2021 and 2060 to keep the gross debt-to-GDP ratio stable near its current value over the projection period (which also implies a stable net debt-to-GDP ratio given the assumption that government financial assets remain stable as a share of GDP). The necessary change in structural primary revenue is decomposed into specific spending categories and 'other factors'. This latter component captures anything that affects debt dynamics other than the explicit expenditure components (it mostly reflects the correction of any disequilibrium between the initial structural primary balance and the one that would stabilise the debt ratio).
Source: Simulations using the OECD Economics Department Long-term Model.

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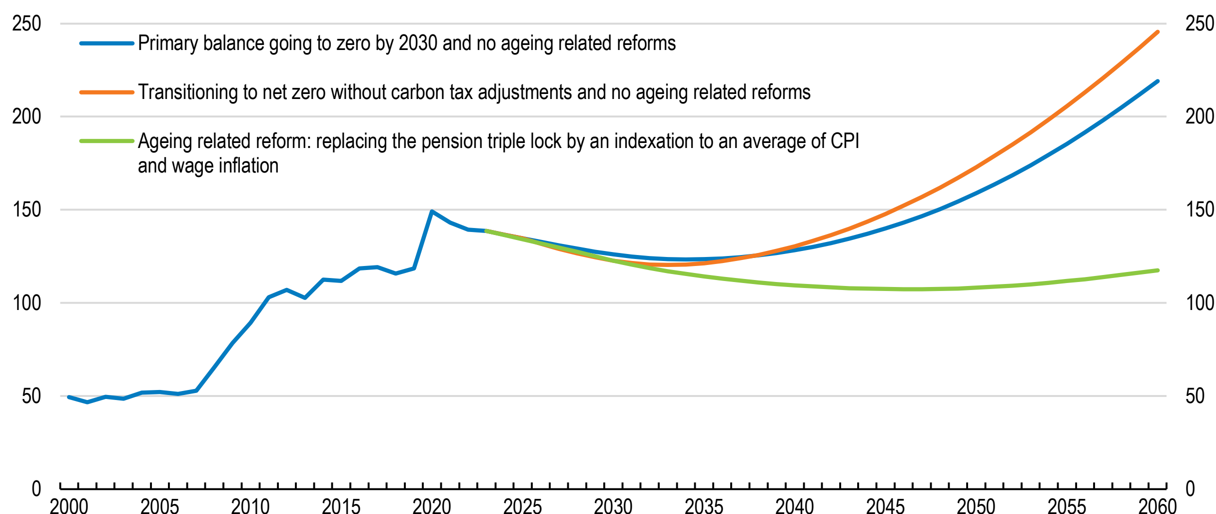
Figure 1.18. Reforms are needed to stabilise public debt

Gross government debt, % of GDP



Note: The baseline scenario assumes a fiscal consolidation allowing to reach a zero primary balance (which for simplification of the model includes interest receipts) by 2030 followed by a deterioration because of ageing costs. The baseline scenario assumes that the trip-lock pension is maintained. The pension reform scenario shows the impact of moving from trip-lock pension to CPI indexation. The fuel levy scenario shows the impact of early action on fuel levy in line with the OBR fiscal risk report which assumes a significant decline in the fuel levy from 2030 as new petrol and diesel cars will be banned from sales. Further general assumptions of the model are outlined in Guillemette (2021).
Source: OBR Fiscal risks report July 2021; and simulations based on the OECD Economics Department Long-term Model.

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Table 1.4. Past recommendations on fiscal policy

Recommendations from past Surveys	Action taken
Replace the pensions “triple lock” by indexing pensions to average earnings and ensure adequate income is provided to poorer pensioners.	For the 2022-2023 financial year the earnings element of the triple lock was temporarily suspended given extremely high 2021 earnings
Set a stable medium-term framework to improve guidance to policy and markets	In 2021, the government has introduced a new fiscal framework including a core target of a declining net sector debt ratio, excluding the Bank of England balance sheet, by the third year of the rolling forecast and three supplementary targets.
Align social security contributions between self-employed and employed, by increasing contributions paid by the self-employed.	Reform to off-payroll working rules (IR35), designed to ensure individuals working like employees but through an intermediary, usually a personal service company (PSC), pay broadly the same Income Tax and National Insurance contributions (NICs) as those who are directly employed, were introduced for the private and voluntary sectors in April 2021 (public sector already in 2017).

Box 1.6. Quantifying the impact of selected recommendations

This box summarises potential long-term impacts of selected structural reforms included in this Survey on GDP (Table 1.5) and the fiscal balance (Table 1.6). The quantified impacts are merely illustrative. The estimated fiscal effects include only the direct impact and exclude behavioural responses that may occur due to policy change.

Table 1.5. Illustrative GDP impact of selected recommendations

Policy	Scenario	Impact
Policies to reduce income inequality	Increased labour efficiency through 10% reduction of income inequality	+0.3% of potential GDP on average over next 10 years
Reduce the cost of childcare for parents	Increase family benefits in kind by 10%	+0.5% of GDP per capita after 10 years

Source: OECD calculations using the OECD Economics Department's long-term model; OECD calculations based on the framework in Égert and Gal (2017), "The Quantification of Structural Reforms in OECD Countries: A New Framework", OECD Economics Department Working Papers, No. 1354.

Table 1.6. Illustrative fiscal impact of recommended reforms

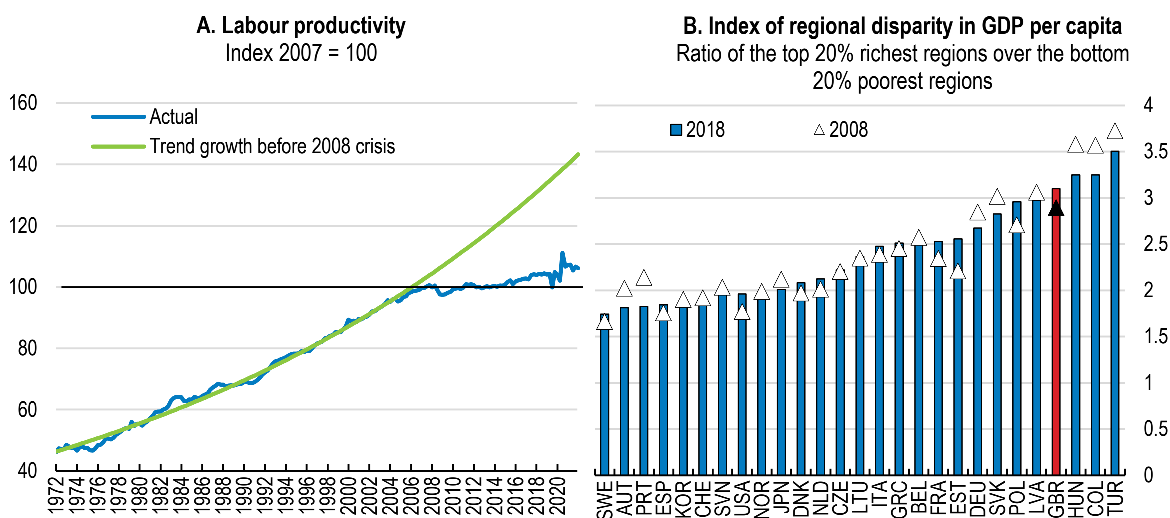
Measure	Description	Net fiscal impact; percentage of GDP
Reduce the cost of childcare for parents	Increase family benefits in kind by 10%	-0.2% on average over next 10 years
Increase the cap on paternity pay and relate it to father's income		↓
Shifting to an average of CPI and wage indexation of pensions		1.9% on average over next 10 years
Broadening VAT tax base	Broadening the VAT tax base to the level of the OECD average keeping the standard rate	1.5%
Increase property taxes through the council tax	Doubling the rates for bands E, F, G, and H, and E (last survey)	0.4%
Expanding the emissions trading scheme and/or implementing well-designed carbon taxes.		↑

Source: OECD calculations based on the OECD Economics Department's long-term model.

Raising productivity

Productivity growth in the United Kingdom has been sluggish since the global financial crisis (Figure 1.19, Panel A). Previous OECD Surveys identified a range of issues, such as skill mismatches, low innovation and knowledge diffusion, low digital adoption in particular by SME's, as well as low private and public investment (Kierzenkowski, Machlica and Fulop, 2018[37]; OECD, 2020[1]; OECD, 2017[31]). Low aggregate productivity in the United Kingdom is also a product of large regional disparities, which have further increased over the last decade (Figure 1.19, Panel B). Structural reforms to raise productivity across regions will be crucial for managing shocks and the transition to net zero over the coming years as it will to help sustain employment and wages and thereby living standards and well-being.

Figure 1.19. Productivity performance has been poor since the financial crisis



Note: Panel A: Labour productivity refers to real GDP divided per total hours worked. Pre-crisis labour productivity trend growth is calculated between 1972 Q1 and 2007 Q4, and is projected from 2008 onwards. Panel B: The GDP per capita of the top and bottom 20% regions (TL3) are defined as those with the highest/lowest GDP per capita until the equivalent of 20% of national population is reached.
Source: OECD (2022), OECD Economic Outlook: Statistics and Projections (database); and OECD Regions and Cities at a glance 2020.

After a decade of low public investment and low productivity growth, the government recognises the need to deliver higher productivity through the private and public sector with three priorities: capital, people and ideas (HM Treasury, 2022[38]). It therefore developed an ambitious plan to support productivity in the United Kingdom and aid the digital and green transition. The government's Plan for Growth outlines an agenda to facilitate structural transformation towards greener and more inclusive growth, centred on investments in infrastructure, skills and innovation, as well as leveraging the new opportunities from leaving the European Union (Box 1.7). The Plan for Growth replaces the 2017 Industrial Strategy continuing with a tendency to change policy frameworks as new governments come in. Some long-term stability was maintained by keeping the National Infrastructure Commission and continuing the Industrial Strategy's sector deals, but the Industrial Strategy Council that oversaw the progress on the Industrial Strategy has been disbanded. An overarching independent body overseeing progress and implementation of all individual elements of the Plan for Growth is missing, but could help to increase transparency and accountability and ultimately stimulate private investment.

Box 1.7. Plan for Growth – Build back better

In March 2021, the government published its Plan for Growth for the post-COVID-19 world replacing the 2017 Industrial Strategy. The plan focuses on infrastructure, skills and innovation as pillars to deliver three strategies: the levelling up agenda to deliver equal opportunities and quality of life through the UK; the Net-Zero Strategy to deliver a decarbonised economy by 2050; and a Global Britain vision, including trade policy and regulatory reforms in the financial sector, to deliver domestic prosperity through deeper integration into the global economic and financial system.

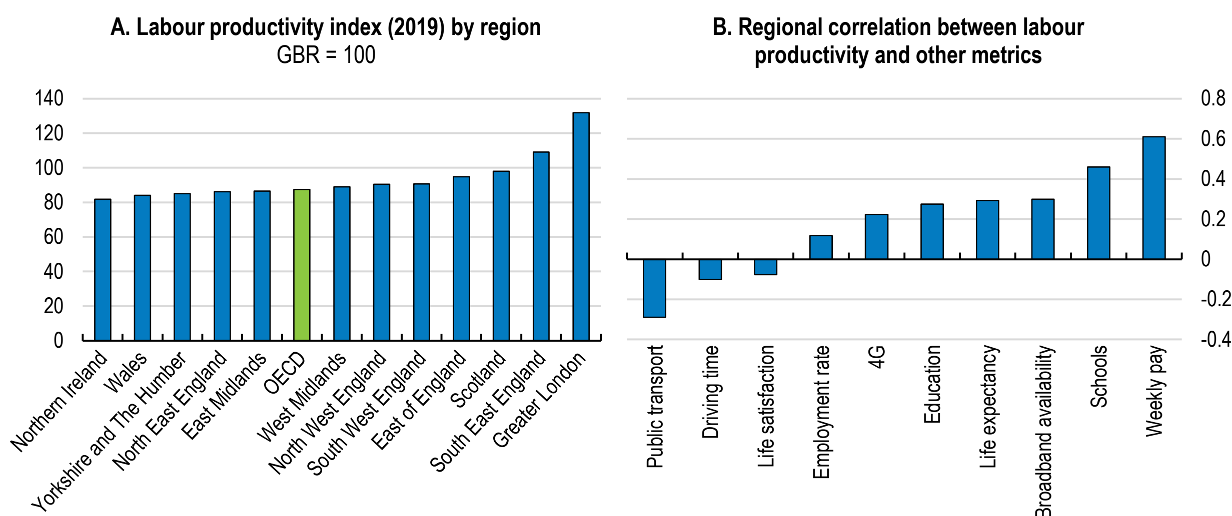
Pillar \ Key Policy	Levelling Up the Whole of the UK	Supporting the Transition to Net Zero	Support the Vision for Global Britain
Infrastructure	Connect people to opportunity via the UK-wide Levelling Up Fund and UK Shared Prosperity Fund, as well as the Towns Fund and High Street Fund, to invest in broadband, roads, rails, cities and in local areas (Levelling Up Fund). Gross public investments allocated amounts to around GBP 600 billion by 2026-27, taking public sector net public investment to 2.5% on average per year up to 2026-27.	GBP 30 billion in funding for climate change priorities between 2021 and 2025, set out in the Net Zero Strategy and Spending Review 2021. This includes GBP 500 million for grants to install new home heating systems and replace boilers	Open new trade and investment hubs.
	Crowd in private investment through the new UK Infrastructure Bank		
Skills	Use the UK Shared Prosperity Fund to improve public services in education and skills in struggling regions, including a strong focus on improving adult numeracy.		Various targeted high skilled visa reforms, alongside a global outreach strategy.
	• Introduce the Lifetime Skills Guarantee to enable lifelong learning through free fully funded Level 3 courses, rolling out employer-led skills bootcamps, and introducing the Lifelong Loan Entitlement. • Take steps to improve the apprenticeship system for employers, through enabling the transfer of unspent levy funds and allowing employers to front load apprenticeship training. • reforming technical education to align the post-16 technical education system with employer demand • Provide technical qualifications by opening 9 additional Institutes of Technology (IoTs), bringing the total number to 21. Funding for additional hours in the classroom for 16–19 years old		
Innovation	Develop innovative hubs of high-value activity in core cities.		Pursue regulatory reforms to unlock cutting-edge technologies and boost competition
	• Increase public investment in R&D to GBP 20 billion a year by FY24/25, part of the government's objectives to increase R&D spending to GBP 22 billion by 2026/27 and economy-wide R&D investment to 2.4% of GDP in 2027. • Review of R&D tax reliefs. • Consult on measures to address barriers posed to pension funds when looking to invest in high growth innovative companies. • Introduced GBP 375 million "Future Fund: Breakthrough" to address the scale up gap for innovative businesses and other equity products. • Launch the Help to Grow program to support over 100 000 SMEs improve their productivity through management training and digital adoption		

Source: HM Treasury (2021[39]).

Reducing the regional productivity gap is at the core of the Plan for Growth

Weak average productivity outside of London holds back aggregate productivity, reinforcing regional disparities along several quality of life dimensions (Figure 1.20, Panel A). Strong regional concentration of certain economic sectors, agglomeration benefits, and regional skill mismatches explain most of the productivity differentials. For example, the higher concentration of knowledge intensive services in the densely populated and highly productive South facilitates access to skills and knowledge diffusion (OECD, 2017[31]; OECD, 2020[40]). Regions that are more productive also have better infrastructure facilitating agglomeration benefits, such as good broadband availability, 4G coverage and transport infrastructure (Figure 1.20, Panel B).

Figure 1.20. Inequalities across regions are high



Note: Panel A: Productivity index for regions in the UK is based on gross value added per hour. Productivity of OECD relative to the UK is based on GDP per hour. Panel B: Correlation between productivity (Gross value added per hour worked) and different metrics displayed on the horizontal axis by local authority districts.
Source: ONS; OECD (2022) Regional well-being database; OECD (2022), Regions and cities database.

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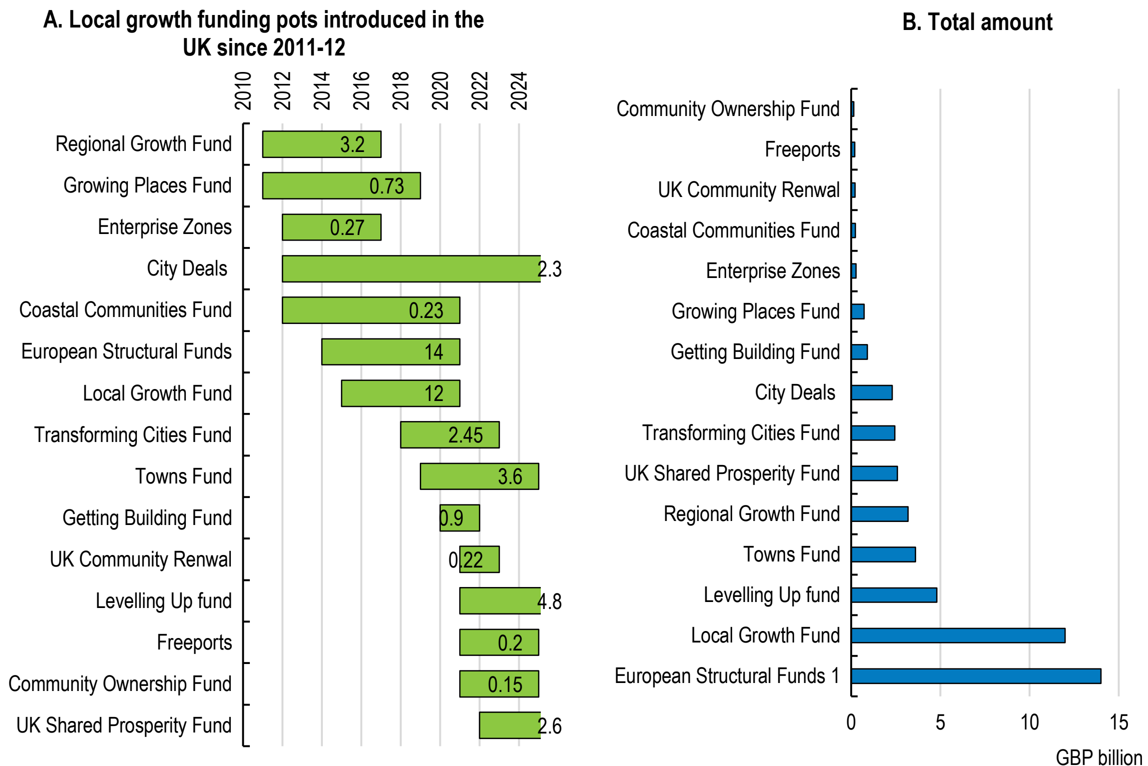
"Levelling up the Whole of the United Kingdom" is a priority of the government to reduce regional disparities (HM Government, 2022[41]). Apart from infrastructure investments and targeted spending in poorer areas outside London and the South East, the levelling up strategy envisions greater empowerment for local governments through a new framework for devolution in England and set up 12 medium-term "missions" or objectives, to be reached by 2030. The UK governments has the statutory duty to produce an annual report assessing progress against the missions, and a new Levelling Up Advisory Council will support Ministers by advising on the design, delivery and impact of levelling up policy. A new body that will be tasked with local government data, transparency and outcomes is under discussion. Improving subnational data collection and strengthening the monitoring framework would be a welcome development, as is the medium term perspective of the policy framework. Still, the missions are ambitious and a longer term perspective beyond 2030 is warranted. The 2021 Spending Review set out the funding for the Levelling Up strategy until 2024, but funding needs should be evaluated and set out beyond the current budget and in line with the timeline of the missions.

England is very centralised and local councils have less power than devolved authorities in Scotland, Wales and Northern Ireland (OECD, 2017[31]). Until now, only metropolitan areas were able to strike devolution deals, but the new devolution framework for England extends to every area of England that wants one. Depending on the agreed setup, local authorities will get greater powers and functions ranging

from a strategic role in service delivery to the ability to adjust property taxes through the council tax and supplement on business rates. Greater devolution of power creates more incentives for local leadership to raise productivity and improve service delivery, while transfers from the central government provide some degree of risk sharing. In particular, redistribution of income and resources may be an important aspect for reducing spatial disparities in the early phase, but going forward further decentralisation of power and tax revenue could be considered, as is for example the case in Finland or Sweden (OECD, 2020[42]). It should be ensured that devolution is designed in such a way that the integrity of the tax system is maintained and that government fragmentation is reduced by providing clarity on local responsibilities. Platforms for dialogue could further stimulate exchange and co-operation within and between different layers of government.

Figure 1.21. Local authorities need to deal with numerous growth funding funds



Note: The amount of European Structural Fund converted using an exchange rate of GBP 1 = EUR 1.18. The amount of Levelling Up funds includes GBP 0.3bn from Towns Fund. GBP 1.5bn of UK Shared Prosperity fund in 2024/25
Source: UK Levelling Up White Paper (2022).

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Several funds are available for local governments to support levelling up their area, but the funding landscape is fragmented and challenging to navigate for local authorities with limited administrative capacity (Figure 1.21). Most recently, the government allocated a total of GBP 4.8 billion by 2026 to the Levelling Up Fund, a competitive fund, which provides funds for local infrastructure that improves everyday life. For round one, about 77% of the GBP 1.6 billion allocation in Great Britain will go to the places defined as being in the highest need according to the index created for the Levelling Up Fund (HM Treasury, 2021[43]; Department for Levelling Up, Housing and Communities, 2021[44]). However, analysis using the index of Multiple Deprivation shows that some of England's most deprived areas received no or far less funding from the Levelling Up Fund, than some of the richer ones (Centre for Inequality and Levelling Up,

2022[45]). Thus, 60 of the 100 most deprived places according to the index of Multiple Deprivation missed out on the Levelling Up fund in the first round. Although those local authorities may bid and receive funds in the upcoming rounds, it should be ensured that more deprived areas are not constrained in their capacity to access those funds. Identifying and eliminating barriers to local funds early on will be crucial to ensure that areas in most need receive needed funds. Creating a single information source and streamlining administrative requirements for funding available to the local level would increase transparency and ease administrative procedures.

Table 1.7. Past recommendations on regional productivity

Recommendation in previous *Surveys*	Actions taken since the last *Survey*
Invest in improving inter- and intra-city transport links where such investments can foster agglomeration effects and unlock related productivity benefits	The government is committed to investing GBP 4.2 billion in intra-city transport settlements from 2022-23 for city regions. The 2021 Integrated Rail Plan commits GBP 96 billion to improve rail capacity in the Midlands and North but cancelling the eastern leg of HighSpeed2.

Addressing infrastructure needs will be key for unlocking faster productivity growth

Public investment has increased and should be sustained to support the Levelling Up Agenda and the Net Zero transition. Years of under-investment in public infrastructure have resulted in a significant infrastructure deficit weighing on productivity. Although infrastructure quality in the United Kingdom ranked 11th in the world in 2019 according to the World Economic Forum (2019[46]), it lags behind comparable European economies such as France, Germany and the Netherlands. The country underperforms for example with respect to the quality of its road and utility infrastructure (Figure 1.22, Panels A and B). Only recently public investment as a share of GDP has increased as the UK government started to address infrastructure investment needs (Figure 1.22, Panel C). Within the 2021 Plan for Growth, GBR 600 billion of gross public capital investment by 2026-27 will be devoted to broadband, roads, rail and cities (Box 1.7), areas that have been previously identified as needing upgrades and further investment (Jones and Llewellyn, 2019[47]; HM Treasury, 2022[48]). These plans translate into higher public capital investment of 2.5% of GDP over the coming fiscal years (Office for Budget Responsibility, 2022[28]). This is a substantial increase compared to pre-2017 levels, remaining within the 3% cap set in the fiscal rules.

Substantial private infrastructure investment is also needed. The government's strategy aims for a mix of public and private investment with private investment dominating in the regulated industries (energy, utilities and digital) (Figure 1.23). While the regulatory system has generated investment and improved performance (National Infrastructure Commission, 2019[49]), it increasingly faces challenges it was not designed to address. Managing increasing risks of floods and drought, transitioning to full fibre digital networks and achieving net zero emissions by 2050 calls for significant private investment. The government should therefore consider to follow the advice of the National Infrastructure Commission and broaden the network sector regulators' duties to include resilience to the impacts of climate change, net zero and increasing transparency through providing long-term strategic guidance (National Infrastructure Commission, 2020[50]). In the case of broadband provisioning, the government is working with private telecoms operators to rollout gigabit-capable connectivity to the hardest to reach areas of the UK. The government's GBP 5 billion investment is subsidising gigabit rollout to uncommercial premises, which will help the government realise its target of providing gigabit connectivity to 85% of the UK by 2025 and 99% of the country by 2030.

Figure 1.22. Total investment in infrastructure has been low until recently

A. Quality of road infrastructure
1-100(best), 2019

B. Quality of utility infrastructure
1-100(best), 2019

C. Infrastructure investment and maintenance
% of GDP

Note: Panel C: Infrastructure investment and maintenance in rail, road, air, inland waterways and sea. OECD and G7 (without UK) unweighted averages. Only public investment on infrastructure and maintenance is taken into account. Total investment on infrastructure and maintenance could be higher due to complementary spending through PPP, limiting international comparability.
Source: World Economic Forum, The Global Competitiveness Index dataset, Geneva; and OECD (2022), ITF Transport Statistics database.

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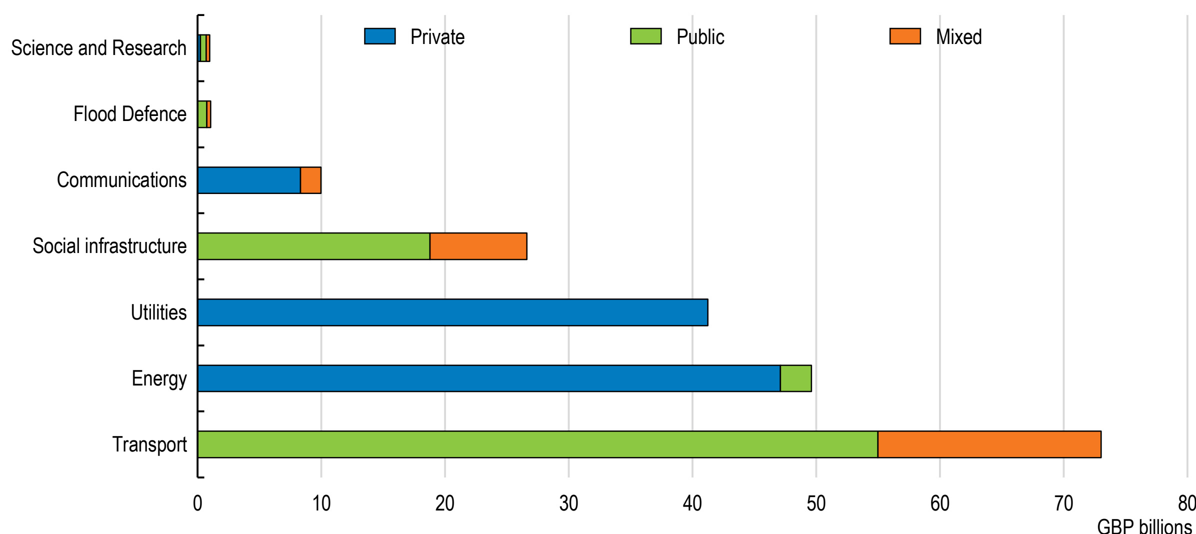
To unlock private capital for the funding of large investment needs, the government launched the UK Infrastructure Bank (UKIB) in the summer of 2021. This is a welcome development but will only partially offset the loss of the European Investment Bank (EIB) funding. The UKIB will lend and provide equity financing and guarantees for projects that support regional economic growth and tackle climate change across sectors. It is focused on clean energy, transport, water and waste projects and it is foreseen it will disburse around GBP 1.5 billion per year (Office of Budget Responsibility, 2021[51]), about a third of previous EIB financing prior to the referendum. The UKIB will also take over the UK Guarantee Scheme, which can currently issue up to GBP 40 billion in guarantees, though the bank will initially be able issuing only GBP 10 billion initially (Office for Budget Responsibility, 2021[7]). To guide markets, existing investment strategies should be fleshed out and medium term objectives should be created, in particular with respect to the green transition.

Figure 1.23. Planned national infrastructure projects need substantial private investment

Funding mix of planned investment in the government national infrastructure pipeline from 2021/22 to 2024/25 by sector, GBP billions



Source: UK Government, National Infrastructure and Construction Pipeline 2021 paper.

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The government is currently consulting on reforms to the prudential regulation of the insurance sector. One of the objectives of the review is to incentivise insurance companies to invest more in long-term infrastructure assets and enable the insurance sector to play a significant role in supporting the government's objectives in relation to the provision of long-term capital to support growth, including investment in infrastructure (see financial stability section). The pension sector has also been asked by the government to voluntarily invest more in UK infrastructure projects and local government pensions schemes face a 5% target of investment in projects that support local areas (HM Government, 2022[41]). Removing barriers to private sector investment, such as adjustments to financial regulation, could unlock capital, but the resulting higher risk taking and hence financial stability implications should be explicitly taken into account.

Public investment management is sound, but could improve in some areas to increase the return to public investment. A dedicated task force, the Infrastructure and Project Authority, reporting to the Cabinet Office and HM Treasury, has developed a Transforming Infrastructure Performance roadmap to 2030 that includes an action plan and the list of infrastructure projects in the pipeline, an overview of planned procurement and investment necessary to implement the National Infrastructure Strategy (Infrastructure and Ports Authority, 2021[52]; Infrastructure Projects Authority, 2021[53]). As recommended in the last Survey, further improvements in the public investment management framework, including better coordination between national and subnational government levels, would be welcome (OECD, 2020[1]) (Demmou and Franco, 2020[54]). Better project selection procedures and ex-post evaluation of large investment projects was advised by the Resolution Foundation (Bailey et al., 2021[55]). A recent National Audit Office report also recommends further improvements in the spending evaluation framework, such as further clarification of responsibilities, oversight and publishing evaluation analysis (National Audit Office, 2021[56]).

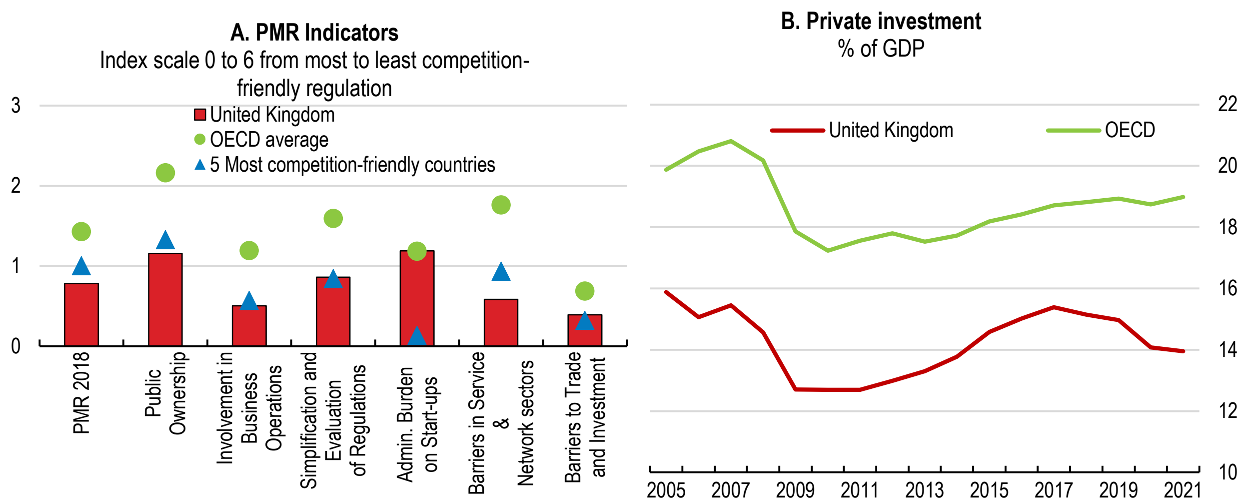
Table 1.8. Past recommendations on infrastructure investment

Recommendations in previous *Surveys*	Actions taken since the last *Survey*
Ensure continuity in government support through the Industrial Strategy, a multidimensional approach to boost investment, innovation and skills intended to foster productivity growth.	The Industrial Strategy was replaced by the Plan for Growth in 2021, which offers a similar multidimensional approach, but the independent Industrial Strategy Council was abolished
Prioritise digital infrastructure, particularly in deprived regions, in the allocation of the planned increase in public investment. Ensure sound governance of infrastructure investments.	The government is subsidising the rollout to 20% of premises for which installing high speed broadband access is considered uncommercial while mobile operators are expected to fund access to high-speed broadband to 80% of premises.
Continue to change existing investment rules to remove barriers for UK pension funds to diversify their portfolios to increase the financing pool available to young firms, in light of the ongoing review.	Local Government Pension schemes face a target of 5% for investment in local infrastructure schemes as per the Levelling up White Paper.
Secure venture capital public funding over the long term and provide clarity to investors in terms of how EU funding will be replaced.	The government set up the Future Fund in 2021, a temporary co-investment scheme to inject funds in start-ups and by the end 2021 265 firms had converted loans into equity shares

Improving productivity through higher private investment in ICT and innovation

Businesses in the United Kingdom have been lagging behind their peers in other OECD countries in investing in physical capital, innovation or new processes that would make labour more productive (OECD, 2020[1]; 2017[31]). While the United Kingdom has competition friendly product market regulations that should support investment (Figure 1.24, Panel A), uncertainties following the 2016 Referendum and more recently the COVID-19 pandemic weighed on aggregate private investment (Bank of England, 2021[57]; OECD, 2020[1]) (Figure 1.24, Panel B). Spending on digitalisation has increased as the COVID-19 crisis and subsequent lockdowns have pushed firms towards teleworking and investing in digital innovation. Business surveys indicate that in particular service sectors, which have been lagging behind in digital adoption as highlighted in the last Economic Survey, seem to have been given the necessary boost (Valero, Riom and Oliveira-Cunha, 2021[58]). Still, further investment in ICT is needed for the United Kingdom to catch up to its peers, in particular investments to support the adoption of productivity enhancing techniques and to create an environment that can utilise benefits from big data processing and Artificial Intelligence (Sorbe et al., 2019[59]).

Figure 1.24. Product market regulations are lean but private investment is low



Note: Panel B: OECD unweighted average of 23 countries for which comparable data on private investment were available.
Source: OECD 2018 PMR database – information refers to laws and regulation in force on 1 January 2018; and OECD (2022), Economic Outlook: Projections and Statistics Database.

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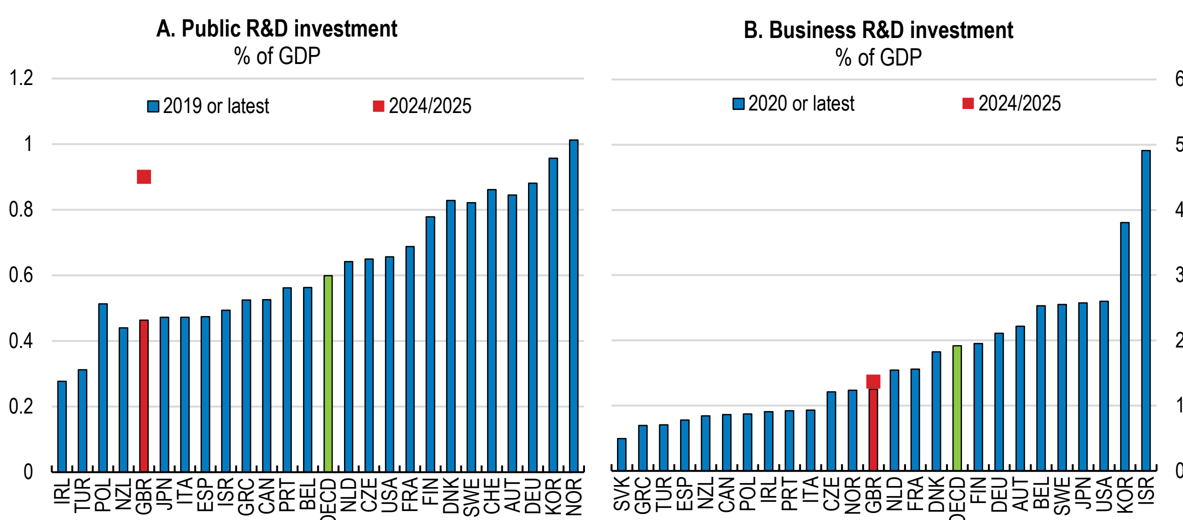
Innovation will be key to stronger productivity growth, but private and public spending on Research and Development (R&D) in the United Kingdom has been relatively low compared to peer countries (Figure 1.25). As public R&D investment induces private investment - every pound the government spends is estimated to stimulate, on average, around GBP 2 of private investment (HM Treasury, 2021[60]) – the government has boosted spending. Aiming to bring public and private R&D investment together to 2.4% of GDP by 2026-27, the government announced to increase public R&D investment to GBP 20 billion by 2024-25 (almost 1% of GDP per year). To support the Levelling Up agenda (see above), regions outside London and South East England are targeted. These developments are welcome and will raise public R&D investment to the level of OECD peers (Figure 1.25, Panel A). To further crowd in private investment, the government announced to broaden the scope of qualifying expenditure for R&D tax credits to include data and cloud computing from April 2023. This expansion is welcome as it will allow the R&D support system to cover data driven research, benefitting improvements in research, product development and productivity in the UK.

Figure 1.25. Planned public R&D investment will be above the OECD average



Note: Panel A: Planned investment as percentage of GDP as projected by OBR in its Autumn forecast. Panel B: The target of the UK government is that investment in R&D increases to 2.4% by 2027. Assuming a constant growth rate over the time period for Business R&D investment and keeping Public R&D investment at 0.9% over the period 2025-2027, business investment is estimated to reach 1.37% in 2024/2025 and 1.5% in 2027.
Source: OECD (2022), Main Science and Technology Indicators database; and ONS.

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Good access to finance is critical for advancing digitalisation and stimulating innovation, particularly among smaller firms. Although equity markets are more developed than in many OECD countries, difficulties to access finance persist especially for investment in intangibles by young and digital firms. In addition, information asymmetries make it harder for some SMEs to navigate financial markets and identify the right type of finance to suit their needs. The government is committed to increasing firms' ability to access primary and secondary markets and is exploring proposals how the regulatory regime can be amended to facilitate this (HM Treasury, 2022[61]). The government could for example explore new digital financing solutions, such as peer-to-peer lending and crowdfunding could be explored.

Table 1.9. Past recommendations on investments supporting digitalisation and R&D

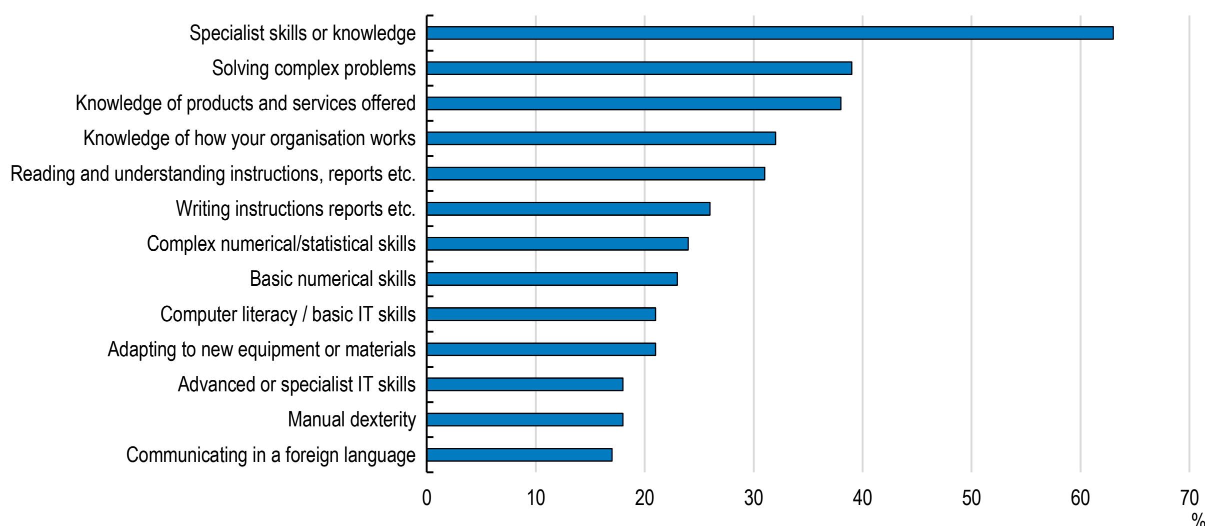
Recommendations in previous *Surveys*	Actions taken since the last *Survey*
Refine the competition framework to adapt it to the digital economy: enable greater personal data mobility and systems with open standards; adopt a broader approach to merger assessment including an evaluation of the overall economic impact of mergers.	A Digital Markets Unit (DMU) was set up within the CMA in April 2021 to monitor and regulate the behaviour of platforms with significant market power. A competition framework for digital markets is in the process.
Prioritise digital infrastructure, particularly in deprived regions, in the allocation of the planned increase in public investment. The government may invest directly in high-speed fixed networks or incentivise private investment, including by competitive tendering, tax exemptions, low interest loans or lower spectrum fees	The government is subsidising the rollout to 20% of premises for which installing high-speed commercial broadband is uncommercial
Continue to boost direct funding to R&D to raise innovation levels	Direct public funding will be increased to GBP 22 billion by 2026/27. The scope of qualifying expenditure for the R&D tax credit was announced to be broadened to include data and cloud computing.

Skills shortages weigh on productivity growth

Over the last two decades, the share of highly skilled workers in employment in the UK increased while the share of low and middle-skilled workers fell (Cominetti et al., 2022[62]). This development has likely been accelerated by COVID-19, and will continue as routine tasks are increasingly automated (OECD, 2019[63]). Already before current acute labour shortages in the hospitality sector and transport and storage in response to the pandemic and the end of free movement for EU nationals following Brexit (see above), vacancies in particular in business services, health and social work could not be filled due to lacking skills. Businesses reported difficulties in filling about one in four vacancies due to skill shortages, mostly in specialist and technical fields (Winterbotham et al., 2020[64]) (Figure 1.26). Keeping up with rapid progress in digital technologies also require transversal skills, such as complex problem solving, analytical skills and creativity, which allow people to adjust to changing skills demands (OECD, 2021[65]). The transition to net zero will add to the need of re- and up-skilling due to sectoral shifts and increasing demand for new skills as highlighted in Chapter 2.

Figure 1.26. Type of technical and practical skills missing in the labour market

Specialist and technical skills found difficult to obtain from applicants, 2019



Note: Employers could cite more than one skill lacking among applicants for each of their skill-shortage vacancies, thus the sum of percentages can be greater than 100%.
Source: UK government, Employer Skills Survey 2019 research report.

The government recognises the need for lifelong learning opportunities to upgrade and reskill the existing workforce to quickly meet rising skill needs. However, adult participation in continuing education and training is low, in particular among low-skilled workers, and decreased by over one million between 2011/12 and 2018/19. To reverse this trend, the government has increased resources for lifelong learning, allocating around GBP 2 billion to the National Skills Fund in the period up to 2024/25. Investment by the National Skills Fund will support free courses in areas where skill shortages are prevalent or emerging, such as healthcare, education, STEM fields, digital technologies and fields related to net zero (Department for Education, 2021[66]). Free courses are available to anyone aged 19 and above without A-Level qualifications and to everyone earning below the annual national living wage. Short, flexible 12-16 week training is offered through employer-led digital boot-camps for anyone aged 19 and above to retrain, top up skills, or gain new specialist skills in order to meet critical skill needs. These measures respond to the strong need for training opportunities for the low-qualified and low income earners emphasised in the last Survey. Uptake and effectiveness should be closely monitored to ensure that targeted groups take up training and education opportunities. Statistical tools could help to improve targeting training to low skilled workers affected by digitalisation and the green transition, while carefully targeted campaigns to raise awareness of learning opportunities can stimulate further uptake, as has been done in the Netherlands, for example (OECD, 2021[67]).

Skill accumulation and on-the-job training suffered during the pandemic as many workers were furloughed. Businesses in the United Kingdom invest less in training than their counterparts in other European countries. While tertiary education attainment is comparatively high, only 18% of 25-64 year olds hold an upper secondary or postsecondary vocational qualification – significantly less than the OECD average of 27% (OECD, 2020[68]). Moreover, 32% of 25-64 year olds only have below upper secondary education, compared to an OECD average of 22% (OECD, 2020[68]). Pursuing vocational routes can be one way to increase educational attainment for people with lower qualifications, in particular for those leaving school early. In the United Kingdom however, apprenticeships are often used by businesses to upskill their workers rather than recruit and train new hires (Kuczera and Field, 2018[69]; Winterbotham et al., 2020[64]). Within the Plan for Jobs, the government introduced a payment to employers in England for each new apprentices hired between August 2020 and March 2022 (HM Treasury, 2020[70]). The government should evaluate the effectiveness of these payments in concert with incentives created by the apprenticeship levy introduced in 2017. Businesses with an annual pay bill of GBP 3 million pay an apprenticeship levy, and to recover some of that tax payment, businesses might be inclined to provide training to their employees through the apprenticeship system rather than other forms of training. Thus, the proportion of businesses only offering apprenticeships to existing employees increased slightly since the introduction of the apprenticeship levy, from 6% in 2016 to 10% in 2019 (Department for Education, 2020[71]). The government should monitor whether this development effectively crowds out low skilled and young people seeking to transition into employment via the apprenticeship system.

Active labour market policy programmes focus on a "Work first" approach over work quality and skill adequacy, which could lead to lower productivity through skill mismatch. With the launch of the Plan for Jobs in July 2020, the government increased spending on active labour market policies, in particular on the number of staff working with job seekers and on programmes facilitating labour reallocation, such as the Sector-Based Work Academy Programme. It also aims to prevent long-term unemployment among younger people through measures like the "Kickstart" and tackle long-term unemployment through its "Restart" programme.

Spending on ALMPs announced during the Autumn 2021 Budget amounts to over GBP 6 billion over the next three years, which comes on top of the GBP 3.6 billion additional funding for 2021- 2022 announced in Spending Review 2020 with the Plan for Jobs (HM Treasury, 2021[60]). Increased spending on ALMPs is welcome, but the outcome of the programmes should be monitored closely and, if necessary, adjusted, for example by increasing guidance and counselling services for medium and low skilled workers (OECD, 2021[72]). A focus should be on matching workers' skills with employers' needs. Since February 2022, the

government requires the unemployed to look for jobs outside their preferred line of work already after one month, down from three months. Non-compliance will lead to payment sanctions in their Universal Credit in order to increase work incentives. It is important that these job search requirements balance faster return to work with risks of increasing skill mismatch from pushing unemployed to the next job available regardless of skill adequacy.

Future skill shortages have to be addressed through the education of today's young people. In the United Kingdom, 15-year-olds perform above the OECD average in reading, mathematics and science, but, as in other systems, their performance is influenced by socio-economic background. Moreover, schools in disadvantaged areas often have larger class sizes and less experienced teachers (OECD, 2019[73]). During the pandemic, school closures further increased inequality as access to digital infrastructure necessary for remote learning varies by socio-economic background and children in poorer areas have been disproportionately affected by disruption in the delivery of school education due to higher COVID-19 incidence rates (Xu et al., 2022[74]). Reading test scores in the United Kingdom in autumn 2020 showed learning loss equivalent to around 2 months of progress, which was even larger for those from more disadvantaged backgrounds (Department for Education, 2021[75]). To reduce the growing learning gaps, the government has made GBP 4.9 billion available since the academic year 2020-21 to support education recovery through additional classes for 16-19 year-olds and tutoring courses for the most disadvantaged pupils (HM Treasury, 2021[60]). This investment is welcome, but does not reverse the drop of spending per pupil of 9% in real terms between 2009–10 and 2019–20 in England and more funding as announced in the 2021 Spending Review is warranted (Waltmann et al., 2021[76]). The Levelling Up Agenda provides a framework to investigate whether allocated spending is sufficient to tackle inequalities in education. Where shortcomings are found, additional funding should be allocated prioritising the most deprived schools.

Table 1.10. Past recommendations on skills development

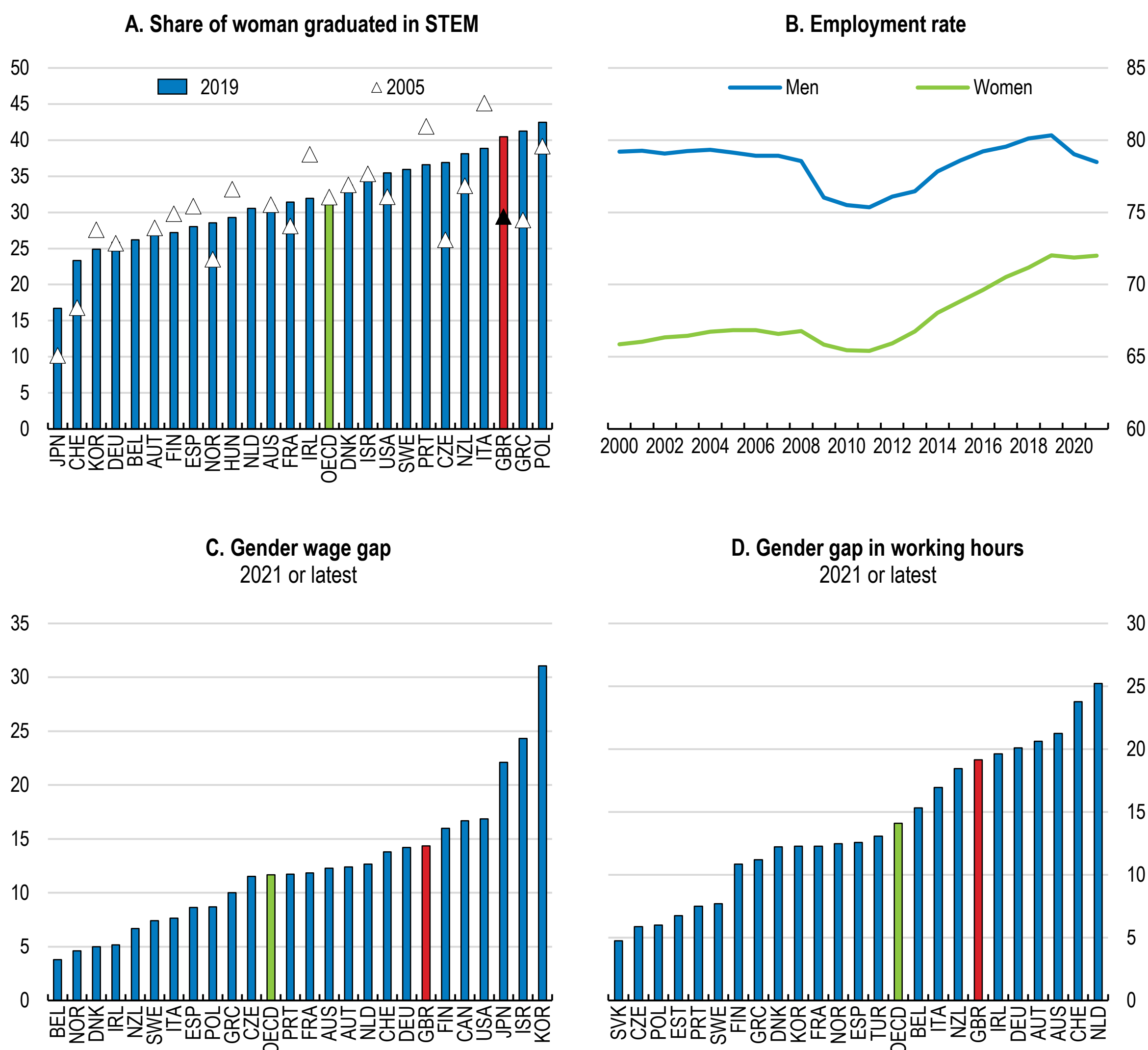
Recommendation in previous *Surveys*	Actions taken since the last *Survey*
Develop digital skills of low-skilled workers, including through further increasing public spending on training. Better target the apprenticeship system to favour the access of low-skilled workers. Introduce individually targeted programmes for low-wage and low-skilled workers to improve their lifelong learning opportunities	The National Retraining Scheme was integrated into the National Skill Fund. A series of free level 3 qualifications for adults aged 19 and over, who do not already have a level 3 qualification or higher, or whose earning is under the National Living Wage annually (GBP 18,525) will also be able to access these qualifications for free, regardless of their prior qualification level.

Reducing gender inequality to draw on a wider pool of skilled labour

Increasing female employment would help to reduce gender earnings gaps and address skill shortages. Women in the UK have made major advances in education, but their skills are often not fully utilised in the labour market. In 2008, the share of women holding tertiary education overtook the one of men (OECD, 2022[77]) and the share of women graduating in STEM fields has risen throughout the years reaching about 40% in 2019 (Figure 1.27, Panel A). Female labour market participation has steadily increased (Figure 1.27, Panel B), and is well above the OECD average (OECD, 2022[78]). However, a third of women work part-time, roughly three times more than men. Important gender inequalities persist. The wage gap has only declined moderately in the past 15 years, and in 2020, working women earned 13% less than men, a larger gap than in many European countries (Figure 1.27, Panel C).

Gender norms, parental leave entitlements and access to affordable and high-quality childcare all play a part in penalising motherhood. Estimates suggest that women in the United Kingdom experience a sharp and persistent drop after the birth of the first child, and even 10 years later earnings are 44% lower, whereas father's earnings remain virtually unaffected (Kleven et al., 2019[79]). Women spend more time in unpaid work than men suggesting that they are more likely to reduce work and take over care work (Figure 1.27, Panel D). In 2018, over half of mothers (56.2%) said they had made a change to their employment for childcare reasons, compared with only 22.4% of fathers (Office for National Statistics, 2019[80]).

Figure 1.27. Gender gaps continue to persist



Note: Panel A: OECD average based on countries for which data was available in both years. STEM refers to Natural sciences, mathematics and Statistics; Engineering, manufacturing and construction; and Information and Communication Technologies (ICT's). Panel C: The gender wage gap is defined as the difference between median earnings of men and women relative to the median earnings of men. Data refer to full-time employees. Panel D refers to the gap between women's and men's average usual weekly working hours on the main job as a share of men's working hours, total declared employment. 15-64 year-olds.
Source: OECD (2022), Labour Force Statistics.

StatLink https://stat.link/wo03lr

Improving access to affordable and good quality childcare would help. As highlighted in the last Survey, childcare costs to parents are amongst the highest in the OECD (Figure 1.28, Panel A). In particular, costs for childcare for children under two years are high, which may explain why less than a third of children under the age of two taking up child care in a formal institution compared to 90% of three to four year olds for whom more government support exists (Farquharson and Olorenshaw, 2022[81]; Department for Education, 2019[82]). However, the average hours spent in formal childcare across age groups is 22 hours, well below the OECD average of about 31 hours (OECD, 2016[83]). Expanding access to full-time high-quality child-care would allow mothers to increase working hours and reduce the duration of the career break, as well as support social mobility for children from disadvantaged backgrounds.

Figure 1.28. Childcare costs in the UK are high

Net childcare costs for parents using childcare facilities, percentage of the average wage, 2020 or latest

A. Net childcare costs for parents using childcare facilities, 2021 or latest

% of avg. wage

EST ITA DEU AUT LUX PRT TUR ISL KOR SWE GRC HUN JPN LVA NOR BEL ESP LTU DNK OECD POL FRA ISR SVN NLD SVK CAN FIN CHE USA AUS IRL GBR CZE

B. Total paid leave available to mothers, 2020

Weeks

Length

Full-rate equivalent

USA MEX CHE ISR NLD ESP CRI AUS COL NZL ISL IRL CHL PRT BEL GBR FRA GRC LUX ITA DNK CAN OECD POL SVN SWE DEU JPN TUR AUT LTU KOR CZE EST NOR LVA HUN FIN SVK

Note: Panel A: Net costs paid by parents for full-time centre-based childcare, after any benefits designed to reduce the gross childcare fees. The simulation shown concerns a family with two children. Both adults work full-time at 67% of the average wage. Panel B: Information refers to paid parental leave and subsequent periods of paid home care leave to care for young children. The graph refers to paid leave entitlements in place as of April 2020. The full-rate equivalent is calculated as the average payment rate times the length of the leave. See source for more details.

Source: OECD (2022), Social protection and Well-being database; and OECD Family Database: Public policies for families and children (PF2.1).

https://stat.link/9vez0g

Parental leave policies are favouring entrenched gender roles. Paid maternity leave at 39 weeks is around the OECD average, but replacement rates are amongst the lowest in the OECD (Figure 1.28, Panel B). The statutory maternity pay consists of 6 weeks at 90% of average gross earnings and up to 33 weeks at the lesser of the statutory rate of GBP 151.97 per week or 90% of average gross weekly earnings. Paternity leave is available for two weeks at 90% of earnings up to a maximum of GBP 151.97 per week. Since 2015, parents can share 50 weeks of parental leave and up to 37 weeks of pay among them (Atkinson, O'Brien and Koslowski, 2021[84]). Low replacement rates with leave pay capped at GBP 151.97 per week create disincentives for the uptake of shared parental leave of fathers, especially in those families where the father is the main family income earner. Eliminating or increasing the cap on paternity pay, as is done

for the mothers during the first 6 weeks, should be considered to limit the earnings shortfall for fathers. Data on the uptake of leave is not routinely collected. To understand the full extent of the problem, the government should improve the monitoring framework and evaluate the coverage and uptake of shared parental leave and its appropriateness in addressing gender inequalities.

Table 1.11. Past recommendations on childcare provision

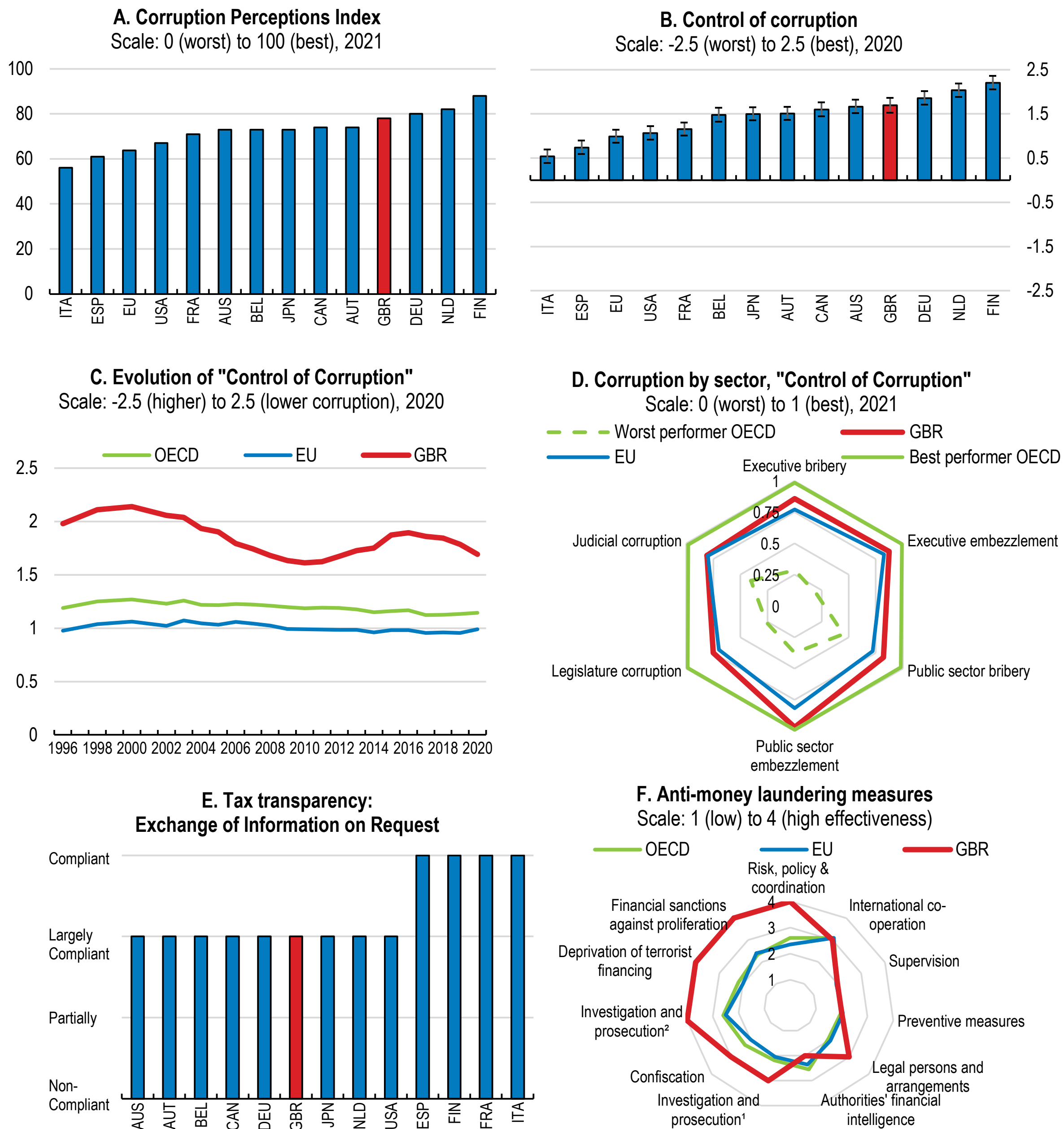
Recommendations in previous *Surveys*	Actions taken since the last *Survey*
Strengthen efforts to make good-quality childcare less costly	No action taken

Maintaining trust in government institutions

Transitioning to net zero will affect people's lives. To get their buy in, trust in the government will be crucial. This has been highlighted by the pandemic, which showed that trust in public institutions was important for people to understand and comply with extraordinary measures (OECD, 2021[85]). In the United Kingdom, indicators of perceived corruption are low by international comparison (Figure 1.29). The October 2021 Additional Follow-Up report by the OECD Working Group on Bribery in International Business Transactions found that the United Kingdom had made further progress in implementing the Working Group's recommendations from its 2017 Phase 4 evaluation of the United Kingdom. However, more progress is still needed to better detect foreign bribery through anti-money laundering reporting, to increase resources for law enforcement, to clarify corporate liability for foreign bribery, and to enhance safeguards ensuring prosecutorial independence.

Public trust in the government could benefit from strengthening oversight of the Ministerial Code. In recent years, the public perception of the extent to which public power is exercised for private gain deteriorated, though the United Kingdom still scores significantly better than the OECD and the EU average (Figure 1.29, Panel C). In its latest report, the Committee for Standards in Public Life recommended placing the Independent Advisor on a statutory basis (The Committee on Standards in Public Life, 2021[86]). This recommendation should be followed as it could increase independence of the Independent Advisor and by allowing initiating investigations and determining findings of breaches of the Ministerial Code, greater compliance could be achieved. Going one step further, greater independence could be achieved if the independent Advisor would also be charged with the sanctioning of rule breaking. While under the current arrangements the Prime Minister may ask the independent Adviser for confidential advice on the appropriate sanction, the decision power lies with the prime minister.

Figure 1.29. Corruption appears to be low



Note: Panel B shows the point estimate and the margin of error. Panel D shows sector-based subcomponents of the "Control of Corruption" indicator by the Varieties of Democracy Project. Panel E summarises the overall assessment on the exchange of information in practice from peer reviews by the Global Forum on Transparency and Exchange of Information for Tax Purposes. Peer reviews assess member jurisdictions' ability to ensure the transparency of their legal entities and arrangements and to co-operate with other tax administrations in accordance with the internationally agreed standard. The figure shows first round results; a second round is ongoing. Panel F shows ratings from the FATF peer reviews of each member to assess levels of implementation of the FATF Recommendations. The ratings reflect the extent to which a country's measures are effective against 11 immediate outcomes. "Investigation and prosecution[1]" refers to money laundering. "Investigation and prosecution[2]" refers to terrorist financing.

Source: Panel A: Transparency International; Panels B and C: World Bank, Worldwide Governance Indicators; Panel D: Varieties of Democracy Project, V-Dem Dataset v11. Panels E and F: OECD Secretariat's own calculation based on the materials from the Global Forum on Transparency and Exchange of Information for Tax Purposes; and OECD, Financial Action Task Force (FATF).

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Table 1.12. Findings and recommendations

FINDINGS (Main findings in bold)	RECOMMENDATIONS (Key recommendations in bold)
Supporting a sustainable recovery	
The economy has recovered to pre-pandemic levels. High energy prices and rising cost of living are slowing growth. **Monetary policy has started to tighten as inflation increased sharply and persistently.** The BoE announced to gradually sell its stocks of sterling corporate bonds and end the program towards the end of 2023. A strategy for government bonds sales will be discussed at the August 2022 monetary policy meeting.	**Continue to progressively raise the Bank Rate to ensure the return of inflation to target, while taking into account any significant changes in economic conditions.** As planned, communicate a clear medium term strategy for reducing asset holdings to manage market expectations.
The pandemic and leaving the EU Single Market and Customs Union have weighed on trade. Non-tariff trade barriers with the EU increases administrative costs. Services account for a large share of trade, but the UK-EU agreement focuses mostly on goods.	**Discuss with the European Union to reduce non-tariff barriers for EU-UK trade in goods and improve mutual market access for services.** Continue to provide access to comprehensive export support services, especially for SMEs. In addition to facilitating UK export to the EU, continue to negotiate new trade deals while ensuring their costs and benefits remain in balance.
The labour market is tightening and labour shortages have been partly exacerbated by reduced net migration.	Ensure that the migration system is sufficiently flexible to address quickly rising labour shortages.
Income inequalities are high and unemployment benefits for many households remain below the levels of many other OECD countries and poverty rates are highest among households out of work.	Continue to uprate universal credit annually to ensure that it is adequate to cover the minimum living standard.
The banking sector is well capitalized on average. House prices have increased but macrofinancial risks remain contained. The Bank of England announced the removal of the affordability test to simplify the framework. The Loan-to-Income flow limit remains in place in addition to the less stringent affordability measures by the Financial Conduct Authority.	Monitor the effect of the removal of the affordability test to ensure macroprudential tools remain effective to contain risks from the mortgage market for the UK banking system.
Addressing fiscal challenges	
Following the phasing out of extensive COVID-19 support measures, fiscal policy has to balance fiscal tightening with supporting growth and meeting significant investment needs.	**Gradually lower the fiscal deficit and the public debt-to-GDP ratio as planned while ensuring temporary support through income transfers targeted at low-income households .**
Fiscal targets are changing frequently. The government has introduced new fiscal rules and targets in 2021, providing clear guidance about the medium-term plan for returning to debt sustainability. The government announced that its fiscal rules will guide its policy for at least this Parliament and will be reviewed at the start of each subsequent Parliament.	Ensure that future changes to fiscal targets follow a regular process to support credibility of fiscal policy
In the longer term, fiscal space is pressured by ageing related spending pressures and decreasing fiscal revenues as the economy is transitioning to net zero carbon emission.	**Replace the state pensions triple lock by indexing pensions to an average of CPI and wage inflation and provide direct transfers to poor pensioners to mitigate poverty risks.**
There is scope to improve the efficiency and fairness of the tax system. A tax review has been announced in the Spring Statement 2022 to go ahead before 2024.	Make council tax fairer by adjusting thresholds for higher property values and by updating property valuation. Broaden the tax base by phasing out inefficient and regressive exemptions, for example by removing partial VAT exemptions. Reduce the gap between the rates of national insurance contributions between employed and self-employed people.
Raising productivity	
Productivity growth has been sluggish since the Global Financial Crisis. Under an ambitious Plan for Growth, large scale investments in infrastructure, skills and innovations are planned, but investment needs are large. **Aggregate productivity is weighed down by regional disparities.**	**Continue ambitious public investment as planned, and implement existing Levelling Up White Paper proposals to ensure it is well targeted, better streamlined, and with a special focus on improving productivity in lagging regions.**
Local authorities face a fragmented funding landscape, which the 2021 Levelling Up White Paper committed to streamline and simplify. Poorer areas have not benefited to the same extent from the allocation of the first round of the new Levelling Up Fund.	**Identify and reduce barriers to access funds for local authorities and provide capacity building measures to ensure lagging regions make use of available funds.** Streamline administrative requirements for funding available to local governments.

The Levelling-Up strategy monitors progress through missions to be achieved by 2030. Funding plans are not set out beyond the current budget.	Evaluate longer-term funding needs in accordance with the missions' timeline. Ensure that devolution deals do not create government fragmentation by defining clear responsibilities within and across levels of government.
The UK Infrastructure Bank (UKIB) was established in the summer of 2021, but will only partially offset the loss of access to the European Investment Bank (EIB).	Expand existing investment strategies and create medium term objectives for the UKIB, in particular with respect to the green transition, to guide markets.
Business investment has been slow on the back of Brexit and pandemic related uncertainty, contributing to low productivity growth	**Ensure long-term policy transparency and continuity of government programmes to reduce uncertainties for businesses.**
The transition to net zero will provide new job opportunities and require new skills. Adding to existing skill-shortages, quickly rising demand for skills requires the need for re- and upskilling of the exiting workforce.	**Use statistical tools to target training to low skilled workers affected by digitalisation and the green transition to strengthen their skills to transit to new jobs.** Ensure that training opportunities for adults are of high quality and respond to identified skills need. Increase guidance and counselling efforts to improve targeting if found necessary. Remain flexible to adjust programme design or curricula of newly introduced programmes, such as Kickstarter programme.
Transversal and strong foundational skills will be essential for the future of work. While UK 15-year-olds perform above the OECD average at age 15, substantial performance differences between schools and between students from different socio-economic backgrounds remain. Businesses often use the apprenticeship system to upskill their employees rather than to recruit and train new workers. This reduces apprenticeship opportunities for young people seeking to transition into employment.	Target additional resources to support the highest quality teaching in schools in the most deprived areas. Monitor the incentives set by the apprenticeship levy and ensure apprenticeships are taken up by low skilled workers and early school leavers.
Women are highly educated but their skills are not fully utilised in the labour market and inequalities in earnings persist. Women adjust working hours to take over care responsibilities. Parental leave pay rates are low, providing little incentives to shift leave to fathers. Data on the uptake of parental leave is not routinely collected.	**Increase funding to reduce the cost of good-quality childcare, in particular for under 2 year olds, giving priority to low income households.** **Increase the cap on paternity pay and relate it to father's income.** Improve data collection of the uptake of parental leave in order to be able to evaluate effectiveness of current policies in reducing gender gaps.
The October 2021 Additional Follow-Up report by the OECD Working Group on Bribery in International Business Transactions found that the United Kingdom had made further progress in implementing the Working Group's recommendations from its 2017 Phase 4 evaluation of the United Kingdom. However, more progress is needed to address foreign bribery.	Ensure adequate resources for law enforcement, clarify aspects of corporate liability for foreign bribery, and strengthen measures to ensure that prosecutions are not influenced by considerations of national economic interests, the potential effect upon relations with another state or the identity of the natural or legal persons involved.
Despite low levels of corruption measured using international indicators, trust in national government has declined.	Give more power to the Independent Advisor, allowing to initiate investigations and determine findings of breaches of the Ministerial Code.

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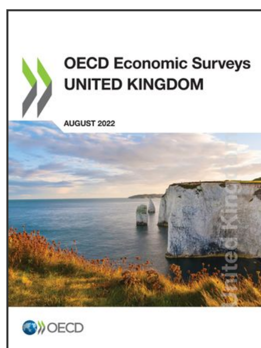

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