



# COVID-19

## UK Political Analysis

By Tim Hames, Senior Adviser | 22<sup>nd</sup> May 2020



**Making it Happen. The coronavirus crisis will trigger a rethink about the manufacturing sector.**

This is a somewhat strange moment in the coronavirus crisis and its consequences. There has been a partial liberalisation of the lockdown, but focused on easing social rather than economic restrictions. Behind the scenes, ministers and officials are working intensely to ensure that there will be another step-change at the beginning of June, as proposed but never firmly promised. The lag in assessing the R-number – and the reality that it can only ever be a range, not an absolutely precise figure – is complicating that ambition. So is the fact that the trial of the proposed NHS App on the Isle of Wight has revealed a tranche of teething troubles. These need to be resolved before any serious attempt to restore more of the mothballed economy will be witnessed. It may pass, but frustration is evident.

There is also an acceptance that in the aftermath of the crisis some profound consideration will have to occur about the structure of UK society, the nature of public spending on health and the shape of the economy. One area that will be under the microscope with extra scrutiny is UK manufacturing.

## EXECUTIVE SUMMARY

- Many of the most challenging aspects of combating coronavirus have been the result of the absence of relevant readily-available resources domestically. These include the chemicals that are needed for a comprehensive testing exercise, the facilities in which to conduct such tests at speed and provision for the production of personal protective equipment (PPE).
- This reflects the fact that in terms of overall output, size in relation to gross domestic product and number of people employed, the UK has a quite small manufacturing sector.
- Not only has manufacturing declined, it has changed very dramatically in terms of its sub-sectors, the regional profile of employment and its internal occupational structure.
- Although the shrinkage has occurred over many decades, it has been most pronounced in the past thirty years and until recently official policy here has been close to “benign neglect”, as few saw any credible alternative to being a “high value, low employment” manufacturer.
- Yet, despite this, much of UK manufacturing is highly rated in global assessments and there is a plausible base from which to envisage its revival if the State actively intervenes to do so.
- The combination of the weaknesses exposed by the coronavirus crisis, the core role that this sector may play in the wider “levelling up” agenda to which this Government (unlike some of its recent predecessors) committed itself before the present pandemic and the flexibility in policy which flows from leaving the EU makes a strategic shift about manufacturing likely.
- This in turn may influence and increase its attractiveness to investors such as private equity.

## INTRODUCTION

The challenges of responding to the coronavirus crisis in the UK have been compounded by three significant factors. They are its social and economic demographics (see FTI UK Political Analysis of April 17), the character of health care provision and spending (see FTI UK Political Analysis of May 15) and the scarcity of key resources due to the nature of the manufacturing industry as of today.

That manufacturing industry will thus be the subject of this edition of the FTI UK Political Analysis. It will examine it by a set of international comparisons, its internal features and the historical pattern of its evolution, especially in the past thirty years. The role of official thinking in this is also set out.

### **In terms of overall output, proportion of GDP and employment, UK manufacturing is quite small.**

An effective means of illustrating this is through a landmark study by the Brookings Institute in 2018, written by Darrell M. West and Christian Lansang, entitled Global Manufacturing Scorecard: How the US compares with 18 other countries. The volume has the slight curiosity in that it really refers to nineteen other entities but, presumably for diplomatic reasons, Taiwan is not counted as a country in a data set which also includes China. There is also a technical and terminological issue in that “manufacturing” is equated with “production”. This does not distort the findings, but it should be noted that it slightly exaggerates employment levels (including in the UK) by involving those who are only indirectly engaged in manufacturing. A survey based on “pure” manufacturing would yield some different numbers but have essentially minimal impact on any of the “league tables” included here.

The following three tables neatly summarise the relative position of the United Kingdom.

**Table 1: Leading countries on total manufacturing output, 2015.**

China	\$2,010 billion
USA	\$1,867 billion
Japan	\$1,063 billion
Germany	\$ 700 billion
S Korea	\$ 372 billion
India	\$ 298 billion
France	\$ 274 billion
Italy	\$ 264 billion
UK	\$ 244 billion
Taiwan	\$ 185 billion

The UK thus ranks ninth on the list overall for total output and is responsible for 2% of global output.

**Table 2: Manufacturing as a percentage of national output, 2015.**

Taiwan	31%	Poland	20%	India	16%	France	11%
S Korea	29%	Japan	19%	Italy	16%	Canada	11%
China	27%	Mexico	19%	Spain	14%	Brazil	11%
Germany	23%	Switzerland	18%	Holland	12%	Russia	11%
Indonesia	22%	Turkey	18%	USA	12%	UK	10%

This list is clearly dominated by Asia (Germany is the only “western” nation in the top tier). The United Kingdom has the smallest percentage of the twenty (sorry, nineteen) countries put here.

**Table 3: Proportion of total workforce employed in manufacturing, 2015.**

Taiwan	27.1%	South Korea	16.9%	Indonesia	13.5%	India	11.4%
Poland	20.2%	China	16.9%	Switzerland	13.0%	USA	10.5%
Germany	19.0%	Japan	16.9%	France	12.4%	Holland	10.4%
Italy	18.5%	Mexico	16.3%	Spain	12.3%	Canada	10.4%
Turkey	18.1%	Russia	14.4%	Brazil	11.4%	UK	9.5%

These numbers, if anything, probably overstate the extent of employment in manufacturing in the UK. As observed earlier, they are based on manufacturing/production. The UK has a comparatively high number of people captured in these numbers who might be considered to be indirectly part of the manufacturing sector. A “pure” figure for the proportion of those employed in manufacturing directly in the UK would (in 2019) have been 7.6%. That is the lowest tally for any developed nation bar Australia (and Australia has far more people engaged in the extractive industry space). The UK’s rank in terms of manufacturing globally is now 26th and for manufacturing as a % of GDP it is 118th.

## Not only is the UK manufacturing sector small it is also highly distinctive.

Size is not everything. Understanding the nature of UK manufacturing and why this has proved of such importance to the coronavirus crisis also requires an appreciation of its features as well. The most meaningful of these are its sub-sectors, its regional composition and its occupational structure.

**Table 4: Sub-sector output of UK manufacturing as a percentage of total manufacturing, 2018.**

Food, beverages and tobacco	16%	Plastics, glass and cement	7%
Transport (automobile/aerospace)	15%	Chemicals and allied products	7%
Metals and metal products	11%	Pharmaceuticals	7%
Machinery	8%	Wood, paper and printing	6%
Furniture and furniture repairs	8%	Clothes and textiles	3%
Computer, allied products, optical	8%	Electrical equipment	2%

A comparison with Germany in light of the coronavirus crisis is instructive. The crucial resources required in recent weeks have been chemicals and pharmaceuticals (for testing) and clothes and textiles (for PPE). Put together these constitute 17% of the UK's (small) manufacturing output. In Germany, these three sub-sectors (at 11%, 10% and 4.5%) reach 25.5% of a far larger total output. A really critical sub-sub-sector has been that of "technical textiles", clothing for a functional purpose. Not only is Germany the world's largest producer of such items, it has 45% of the global market.

All of which explains why a contest between the UK and the likes of Germany and South Korea for the components demanded to run a testing programme swiftly and at scale, and for PPE to deploy in hospitals and care homes was predetermined from the outset. Germany (and South Korea) had most of what they needed in their own back yard. The

UK had to buy it from wherever it could, as fast as it could, and in a frenzied process in which the risk of being overcharged for inferior materials was real.

The politics of manufacturing in the UK has also been shaped by the extreme regional bias of it.

**Table 5: Proportion of workforce employed in manufacturing by UK region, 2019.**

East Midlands	12%	Wales	10%	North West	10%	Scotland	7%
West Midlands	11%	N Ireland	10%	South West	9%	South East	6%
Yorkshire/Humber	11%	North East	10%	East England	7%	London	2%

This is probably the biggest disparity between regions of any major European nation and could well be the widest globally. In a country dominated by its capital city to an unusual extent, manufacturing manifestly must be disadvantaged by the brutal truth that it is marginal to the pre-eminent region.

Furthermore, what those (comparatively few) people who are employed in manufacturing do when at their work has also changed notably over the past three decades as the table below illustrates.

**Table Six: Occupational Structure of UK manufacturing, 1991 compared with 2012.**

	% of all jobs 1991	% of all jobs 2012
Managers/Directors	14%	11%
Professional, allied and technical	10%	25%
Administrative and clerical	11%	9%
TOTAL "WHITE COLLAR"	35%	45%
Skilled trades	31%	23%

Service trades	4%	3%
Process/plant/machine operatives	26%	21%
Elementary occupations	4%	8%
TOTAL "BLUE COLLAR"	65%	55%

These trends have continued over the past decade, the best estimate is that the 7.6% of the workforce now employed in manufacturing are split evenly between white collar and blue collar. To that extent, manufacturing in the UK can no longer be described as a working-class occupation.

## Explaining the historical evolution of UK manufacturing.

The history of the decline in manufacturing in the UK is a long one. It started in absolute terms from 1950 (when it was about 45% of both total output and in employment) to 1970 but in relative terms this was far less evident. In 1970, the proportion of the workforce employed in manufacturing in the UK was, at 27%, entirely typical of other developed countries. Although the recessions of the 1970s and 1980s hit relatively low value manufacturing in the UK very hard, with customers moving to far cheaper competitors overseas, as late as 1990 the UK was the fifth largest manufacturer globally.

**Table 7: Decline in UK manufacturing as a share of UK economic output, 1990 to 2018.**

1990: 17.3% 1995: 17.1% 2000: 15.0% 2005: 11.8% 2010: 10.6% 2015: 10.4% 2018: 9.9%

This is mirrored in a fall in "pure" manufacturing employment in the UK over the same period.

**Table 8: Decline in UK manufacturing employment as a share of all work, 1991 to 2019.**

1991: 15.7%                      2002: 11.7%                      2010: 8.1%                      2019: 7.6%



The end result of this is that the service sector in 2019 was 80% of all national output (up from 69% in 1990) and that services are responsible for 85.1% of all employment (up from 76.9% in 1998).

This is very nearly (but, strictly speaking, not) a story of outright absolute as well as relative decline. Total manufacturing output was 7% higher in 2018 than in 1990. Service sector output was up 106%.

Although the global financial crisis might have been thought to have the greatest impact on services (particularly financial services) this is not actually accurate. Between Q1 2008 and Q3 2009, UK manufacturing output fell by 13 per cent in real terms compared to 6 per cent for the economy as a whole. Added to which, manufacturing output a decade later than this (Q3 2019) was still 2% below its pre-recession peak. Output for the whole economy was 18% above the pre-recession standard.

The response in terms of public policy may be described as “benign neglect”. The reconfiguration of UK manufacturing towards the high value but low employment end of the spectrum was viewed as inevitable, unavoidable and not entirely unwelcome. An official report commissioned in 2013 more or less concluded that there was no point in seeking to drive employment numbers any higher. The approach taken by the Conservative/Liberal Democrat coalition between 2010 and 2015 was more subtle than that, but still preferred to place more emphasis on the niches in manufacturing where the UK was strong, rather than seek to recapture lost territory. Yet in many ways this is paradoxical.

## **UK manufacturing punches well above its weight.**

For a seemingly unloved element of the economy, manufacturing has proved extremely resilient. This is perhaps better appreciated by outsiders than those in the UK. The aforementioned seminal research into comparative manufacturing performance undertaken by the Brookings Institute in 2018 sought, as its highlight, to come to a verdict as to which nation had the most appealing overall manufacturing environment. It did this via marks out of twenty on five dimensions, namely (1) the overall policy and regulatory framework, (2) tax policy, (3) energy, transportation and health costs, (4)

workforce quality and (5) infrastructure and innovation. This is the final score out of 100 points.

**Table 9: Brookings Institute rankings on manufacturing appeal by country, 2018.**

United Kingdom	78	Holland	74	France	70	India	57
Switzerland	78	S Korea	73	Poland	69	Russia	56
USA	77	Germany	73	Italy	62	Mexico	56
Japan	74	Taiwan	72	China	61	Indonesia	53
Canada	74	Spain	72	Turkey	58	Brazil	51

There is quite a lot of bunching here in that only nine points separate the top twelve cited. It is still, though, very hard to write off UK manufacturing on the basis of this independent assessment. The UK owed its exalted status to its pro-business environment, risk index, lack of corruption and its corporate taxation framework. It fared less well on infrastructure, patent filings and skills spending.

Nor does this appear an irrational analysis. Allowing for its low overall total manufacturing output, small proportion of GDP and very low percentage of total employment, the UK sector does well.

**Table 10: Key statistics on the UK manufacturing sector, 2019.**

Manufacturing in the UK is responsible for:

44% of all exports (or 42% for “pure” manufacturing).

69% of all business research and development.

66% of all UK research and development.

15% of total business investment.

Manufacturing productivity in the UK in 2019 was also 12% higher than the national economic norm.

Over the past thirty years, the UK has developed a manufacturing sector that is different from many of its European neighbours, particularly other relatively large European countries (by population). It has become a specialist in high-end manufacturing research and development. Collaboration in this between business and the university sector is arguably among the best in the world. It has two fairly sizeable spheres (automobiles and aerospace) that are undeniably at the top of any Premier League. About 50 per cent of all automobiles built in the UK are exported. There are in excess of 2,000 other companies involved in providing components and services for that sector and eighteen of the largest twenty automotive suppliers are located in this country. An astonishing 90 per cent of all aerospace products made in the UK are exported, with an extremely strong foothold in intricate parts such as wings, engines, avionics and complex systems for civil aircraft. Defence manufacturing is also strong.

Yet this decision to be so specialist comes with costs. We buy low- and medium-value manufactured goods from elsewhere. This means that despite manufacturing being responsible for 44% of all UK exports (worth £275 billion in 2018), it is also the case that manufactured goods from elsewhere are the source of 53% of all UK imports (£367 billion in 2018). That leaves a numbing trade imbalance in manufactured goods (£92 billion) that the service sector, including financial services, does not make up for. It is the single largest challenge in UK trade policy. It is central to the EU Brexit negotiations.

It also has a side effect that ministers and officials are aware the coronavirus crisis has revealed. A somewhat boutique manufacturing industry that relies heavily on automobiles and aerospace is not one that can be recast at speed to meet demand for chemicals, pharmaceuticals and textiles. In PPE, spectacularly, what little increase in domestic production has been achieved has been largely the result of a handful of companies with factories in the UK (such as Burberry in West Yorkshire, the two Mulberry plants in Somerset and Barbour in Tyne and Wear) rising to the occasion. As splendid as those efforts have been, they have been dwarfed by the need to acquire PPE from outside the UK.

## CONCLUSION

Much of what has been written here might seem to be downbeat, even damning, about the country. It should not be. There are many spheres in which the UK has been and will be a leader of the first rank in the struggle against the virus. These flow from being so adept at high end research and development. The UK has been the dominant actor when it has come to modelling outcomes for coronavirus, it has been a massive player in understanding the nature of the disease and how it may mutate and is in the forefront of research into a vaccine, the one silver bullet in this entire situation.

All of this is the result of a focus at the very top of the scale. The same is true in manufacturing. The UK should want to be a high value country, even if that means lower employment than elsewhere. It should not wish to trade this for a more substantial presence in the lower value realms of this sector. It is unlikely, even if it were to want to do so, that it could execute such a swap successfully. The real questions for debate are different. The first is whether there is a wider range of high value areas of manufacturing where the UK could be a significant economic force if it pivoted towards them. The second is whether there is a bare minimum level of other sub-sectors of manufacturing where there is an unacceptable degree of strategic risk in falling below it. The third is whether in future shorter and safer if comparatively expensive supply chains may be preferred to longer but less secure if relatively cheap ones. While there is a danger of “fighting the last war” in boosting manufacturing simply to avert a repetition of the coronavirus outbreak (the next form of a mega-threat might be in the form of a vast cybersecurity attack, not public health via a virus), deep reflection will occur.

This crisis will trigger a serious rethink about manufacturing in official circles. There had been the first stirrings of this under Theresa May with the creation and the rebranding of a Department for Business, Energy and Industrial Strategy in 2016, followed by the formal launch of a new Industrial Strategy in 2017. It will be accelerated hereafter by three factors: the legacy of the pandemic and the very difficult position the UK found itself in to respond to the sudden challenges that it created: a wider political desire to level up the UK economy through targeted support for the regions (where manufacturing is at its strongest, albeit at far lower levels than was true in 1990, never mind in 1970) and that the UK’s departure from the European Union (once the end of the transition

period allows that process to be complete) means that it will have autonomy for innovation via State Aid.

What can be anticipated, therefore, over the course of this Parliament is a switch away from “benign neglect” to active interventionism with regards to the manufacturing sector. Tax, business rates and regulatory policy are likely to be looked at afresh with the view as to what could be done to provide incentives for onshoring and for the expansion of sub-sectors beyond automobiles and aerospace. It is hard to change a long held official mindset, but not impossible. Now it is about making it happen.

**Tim Hames**

Senior Adviser

Strategic Communications

Tim.Hames@FTIConsulting.com



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