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Terms of Reference

Great British Growth: how do we take the UK’s economy forward in a period of geopolitical competition?

A Ditchley Foundation conference

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Introduction

The new Labour government has made growth of the British economy a primary objective to provide a basis for national renewal. The November budget raised taxes by £40 billion to cover gaps in existing spending (a claimed £22 billion) and changed debt criteria to create headroom for capital investment for growth. But at present, even with this added investment, forecasts for growth after two years from the Office for Budget Responsibility remain stubbornly low. Low growth seems embedded as a long-term trend for the British economy, spanning changes in political leadership, rather than a cyclical downturn. Business as usual for the UK does not seem likely to lead to a major shift. Recognising this, the government has issued a green paper on modern industrial strategy, is about to announce an ambitious AI strategy, and is exploring how to reset trade relations with the EU.

But how to deliver these ambitions remains a challenge, particularly in a context of geopolitical competition and the election of President Trump. This Ditchley conference will explore the UK's options. What can we do to grow the economy in a period of not only geopolitical competition between the US and China but also likely stark divergence between the US and the European Union on many economic issues? What can we do to take advantage of the still accelerating technological revolution? How can we combine ambitions for growth with an effective green transition with one powering the other? We will be looking for insights on what can get the UK moving in the short term and transformative ideas with a longer time scale.

Detail

There are many diagnoses of the UK's economic challenges: the effects of Brexit; a failure to realise a counter vision of Global Britain; poor levels of investment in infrastructure; skills and technology from both the public and private sectors; demographic challenges; high energy costs; a high percentage of working age people not working; and aversion to risk both in terms of investment and regulation. GDP growth has been anaemic since the Great Financial Crisis of 2008 and forecast to be around 1 percent for 2024. Nonetheless, the UK remains one of the world's leading economies and still has significant advantages including language, the rule of law, geographical position and time zone, London as a global financial centre, science and education and significant soft power. How can we capitalise on our strengths and address our weaknesses?

What will be the impact of the budget on public and private sector productivity? How can we get more people back into work with the right skills for the opportunities that are emerging? How do we boost business investment in skills and technologies? What can be done to increase public sector efficiency and productivity?

The second Trump Administration is likely to pursue further deregulation of the economy; to boost energy production; and to prioritise economic growth and geopolitical competition over action on climate change. There will be significant continuity with some aspects of President Biden's policies – for example intense competition with China – but President Trump will use the threat of tariffs as a bargaining tool against adversaries and allies alike. The EU will be seen as part of the multilateral problem and EU rebels like Hungary as part of the nationalist solution. American pressure, expressed through both economic and defence policies, will increase on countries looking for growth and a margin beyond the US to preserve Chinese investment and trade. For its part, China will be looking for opportunities to ease European countries away from the US' line, offering inducements and flattery but also threatening trade retaliation if countries follow American demands for alignment.

Sitting between the EU and the US, the UK will naturally want to keep its options open but could face some stark choices. If President Trump imposes tariffs on imports from the EU, might the UK be able to negotiate a separate trading relationship? What would that mean for the UK's relationship in turn with the EU? As the US eases regulation on aspects of the banking and financial world, then should the UK follow suit or remain closer to Europe? Similar dilemmas may emerge on AI and other aspects of technology. Will the UK be able to maintain a mid-Atlantic position, or will pressures force convergence with one major economic power or another? Are there economic opportunities that could accrue to the UK as a result of unfolding trading relationships and areas of specific competitive advantage?

For the middle part of the discussion, we will split into three working groups to explore these questions in more detail. Each group will look at the opportunities for growth and the trade-offs implied by taking a different geo-economic course. These trade-offs would also shape the options for innovation, industrial strategy, energy policy and infrastructure which are essential for all paths to greater growth. Rising national debt would also be a factor across all paths. Increasing skills and preparing the workforce for the impact of AI and other forms of automation will be a constant too.

The 51st state: a closer economic relationship with the United States (Group A)

If not an FTA, are there other transformational options with the US that would make the inevitable complication of interests with the EU worthwhile for the UK, for example a special relationship on AI development and deployment?

President Trump's newly nominated Treasury Secretary has talked about a "3-3-3" strategy. This would mean a slashing of the budget to bring the federal deficit down to 3% of GDP; deregulation to drive growth of 3%; and support for affordable energy through an added 3 million barrels of oil daily. Linking the UK to such a dynamic economy would have advantages and tie in with technological and defence ties.

However, from other perspectives - trade, attitudes to multilateral institutions, employees' rights, and climate action - the positions of the US and the UK would be diverging. There is also the tough economic fact that the EU, still the UK's largest trading partner, would view a separate and closer relationship between the UK and the US as exactly the kind of competitive threat it feared from Brexit. How would these factors play out?

The US would likely expect the UK to align policies on China. What would be the economic impact for the UK of a tougher line on China, particularly if that provoked disproportionate retaliation against the UK in return?

In partnership with the US, how could we create the infrastructure and the environment for the UK to be a good home for the industries of the future? What would this mean for energy supply and distribution? Could partnership with the US be made consistent with hitting our green goals and with EU carbon border adjustment tariffs?

What can we do to increase not only the rate of scientific discovery in the UK but also the commercialisation and scaling of those discoveries and innovations into companies? How do we increase investment in groundbreaking technologies? Are there particular opportunities for the UK in bringing together AI and biology in concert with the US? Building on other traditional strengths, how do we grow our cyber security and fintech industries? Could defence industries in partnership with the US be a major source of growth for the UK?

What would closer partnership with the US mean for the UK's national debt? Would we be able to match US moves (even scaled down to the UK's GDP), given that we do not have the protection of the dollar as the global reserve currency and have no plans to slash central government spending?

Edging towards the Single Market: a closer economic relationship with the EU (Group B)

Many companies, politicians and pressure groups are calling for the UK to align as closely as possible with European standards and regulations to reduce the friction that Brexit introduced into trade with the EU, still our largest trading partner by far. The Government has ruled out a return to the single market but what can be done to digitise and modernise processes? How far can we align on phytosanitary regulations? Is there anything that can be achieved from our position outside the EU on movement of people to ease controlled and agreed migration of talent? What would such moves do for growth both now and for the long term? Can an improved deal with the EU be achieved? What would be the trade-offs in terms of restriction of freedom of manoeuvre?

Increased integration with the EU would be likely to make any separate accommodation and integration with the US economy more difficult. If forced to choose between the EU and the US, would current trade and economic interests (clearly in favour with a closer relationship with the EU) align with long term future prospects? Is the EU the right bet for the future?

Could we align with the EU on goods but keep more freedom of manoeuvre on services and the technological industries of the future? What would closer alignment with the EU mean for energy policy and AI strategy and other forms of innovation, especially in coordination with the US?

How would we manage climate policy as part of alignment with the EU? Would the UK need to introduce Carbon Border Adjustment Measures (CBAMs)?

Would the UK also need to align with the EU on trade and other economic policies towards China? How would the US respond? Could UK companies be hit by secondary sanctions for example? Would the UK want to align policy towards the rest of the Indo-Pacific with the EU or to define a separate path?

Are there prospects for greater integration of European defence and defence industries? Could the UK's financial industry regain an expanded role in Europe as part of reform of capital markets?

The UK would be aligning without access to EU subsidies or other funding mechanisms. What would that mean for rising national debt and the competitiveness of the UK economy?

What impact, positive and negative, would aligning with the EU have on investment on infrastructure? Would investment from the US go down? Would we want increased investment from China? What about other sources of funding?

Sensible pragmatism or a doomed attempt to have cake and eat it? (Group C)

The dilemmas addressed by Group A and Group B are likely to mean an attempt to steer a course between the Trump Administration (which may or may not mark a lasting change in the US policy) and closer engagement with the EU. Would this be British pragmatism in action or just wishful thinking: an attempt to have cake and to eat it? Are our long-term economic interests served by the UK charting a separate independent course economically, or is that no longer workable in the new context of geopolitical competition?

Could the UK manage to act as a bridge between the US and the EU, helping to find some common ground? Is that what the Trump Administration, or the EU, will want?

What other economic options could the UK pursue unilaterally? For example, what can we do to build on our membership of the Comprehensive and Progressive Agreement Trans-Pacific Partnership (CPTPP)? Could we take the relationship with India forward in parallel? Is there more the UK could do with Japan?

To what extent could the UK chart a separate course with China, whilst remaining close to the US on the one hand and the EU on the other?

Could the UK benefit from an influx of American talent and capital in the context of a Trump Administration? How could the government balance engagement with a Trump Administration with the nurturing of links to more like-minded groups amongst more traditional Republicans and Democrats and at the state and city level in the US?

How might the UK look unilaterally to build industries of the future? Could we build a platform for innovation through visa policy, education and light regulation compared to the EU, that would be attractive to international talent and investment?

How could we drive international investment in the UK to help build infrastructure and energy supply? What would be the likely sources of that investment?

What would this independent course mean for rising national debt and the stability of the pound and other market vulnerabilities? What would an independent course mean for the UK's role in the world?

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Annex

Further background – where we start from after four years of the Biden Administration and the Draghi report

The new Labour Government has made investment a priority. It is core to a plethora of new commissions and government conferences. For example, it is the focus for the first Council of the Nations and Regions and the subject of an International Summit held in autumn 2024. Investment in basic physical infrastructure is essential to underpin all and any economic growth. This includes the hard infrastructure of electricity, water, energy, transport, housing, schools and hospitals. *Crucially, investment is more than patching up and making good the decades of under or no funding, there must be a critical pathway for investment that potentially leapfrogs some parts of our current infrastructure to prepare the ground for a future economy.* Transport, food production, housing, health care facilities, the creation of skills, new ways of working and future cities will evolve over time. Can investment both patch up and plan for future innovation? Is there a proper distinction to be made between investment that feeds continued consumption and that which makes a future return?

The expectation is that the new commissions and policy generating fora will allow innovation across the policy board from breaking cycles of low productivity, supporting innovation in training and skills, creating regulatory and planning systems that allow a much faster rate of infrastructure building, greater regional control and responsive adaptation to climate change planning. Can these go further to support the rebuilding of social and democratic resilience in a demographically changing population to reduce child poverty, increase equality, address looming heath challenges and find a way to manage immigration? The government's first stab at industrial strategy was set out in autumn 2024; what signals is it already sending?

Dealing with these deep structural challenges will also change the UK's relationships in the world, with Europe, the US, the Indo-Pacific and the emerging economies across Africa, Asia and Central America. Where does the UK sit, for example, in relation both to an evolving mesh of industrial policy elsewhere and the economic and security policies of both the US and the EU? Outside the EU, does the UK have less sway than it once had to shape and influence US policy? What does it mean for the UK to re-set trading relationships around the world? Can the UK contribute to a bigger 'western' industrial policy as envisioned by the US for a common approach to China and the development of friendlier supply chains? Can the UK define its own path and work through its own interests before following the one set for it by the US?

This conference will build on the last five years of intense discussion. As well as many conferences on innovation, tech, AI and education, Ditchley has reviewed many of the UK's structural challenges with conferences on:

- Renewing democratic societies to face the future. April 2019
- Defining the modern UK. March 2020.
- Take back control part two. June 2021
- Ditchley Regional Devolution Briefing. April 2022
- A hungry world on the move: the impact of the food crisis on migration and how we must respond. October 2022
- A profound economic crisis. January 2023

- Does older mean poorer. What will demographic change mean for economic prosperity and social cohesion in developed economies? June 2024
- Allies of the US, October 2024
- Climate and Security Trade-Offs: transatlantic industrial and trade policy in the green transition. November 2024.

Finance, investment and growth

Since Russia's invasion of Ukraine there has been much concern about economic dependencies particularly over energy and now overlaid by China's evident lead in some areas of renewable energy technologies, including those that will define future economic strength and the geopolitical balance of power.

Investment requires the financial architecture to encourage capital flows and to face head on the relationship between debt and growth. The US has begun to invest $trillions in clean domestic energy production. Mario Draghi in his report 'Future of European Competitiveness', (published autumn 2024) has set out a comprehensive programme for the EU to rebuild competitiveness in relation to the US and China. He argues that the EU should make annual investment at over EUR 800 billion, or about 5% of EU GDP for defence, innovation, decarbonisation and economic security (aligning these goals). How much of the diagnosis and Draghi's prescription is also relevant for the UK?

In his analysis of economic competitiveness, Draghi highlights the fact that *"there is no EU company with a market capitalisation over EUR 100 billion that has been set up from scratch in the last fifty years. All six US companies with valuations above EUR 1 trillion have been created in that period of time."*[1] Draghi draws attention to a divergence between the manner in which US corporations have been able to reinvest in innovation in ways that EU companies have not. Does the EU architecture which attempts to protect consumers (anti-trust, compliance with WTO trade rules) work against global competitiveness, while US practice supports innovation and global competitiveness but ultimately benefits the corporations over consumers? The US break with neoliberalism has worked to reinforce the power of capital. How should the UK respond to these inherent economic trajectories? Will adoption of industrial strategies change global capitalism?

Attempts to be more proactive have led to adoption of industrial strategies in many countries, Australia, Germany, France and notably in the US. Industrial strategies, including local industrial strategies have become acceptable. The admission of China into the WTO and the US response has weakened the post 1945 governance of trade.

[1] Address by Mr. Draghi – Presentation of the report on the Future of European competitiveness – European Parliament – Strasbourg – 17 September 2024

Social and democratic resilience in the UK

After 100 years of the welfare state how will the UK reimagine its future to balance changing needs, the drawn-out impacts of a 'cost of living crisis' and a re-balancing of rights and responsibilities? How best will the UK population cope with the further costs of climate impacts (currently 1.1% of GDP and projected to increase to 3.3% by 2050) which fall most heavily on those who suffer them, how is the country to properly adapt? Is it right that consumers must bear the cost of essential investment in utilities such as the water and sewage system? Are there new models to take the place of failed privatisation that can also provide forms of collective protection?

Innovation

If the UK's competitive advantage rests on innovation, R&D and investment, how can the current innovation system best be characterised? Where are the strengths both geographically and by sector? How are the current clusters working? What is the picture of universities' and research institutions' spin outs? What's the role for public expenditure? Should there be a smaller number of agreed UK priorities?

Mario Draghi's report is about how to close the innovation gap between the EU and US economies which he sees as at the root of the EU's lower productivity. In 2021, EU companies spent around EUR 270 billion less on R&D than those in the US. Draghi argues that the EU industrial structure is static and dominated by the same companies and technologies as it was decades ago. New companies and newer technologies are not coming through EU economies strongly enough. The problem as he describes is not a lack of R&D or entrepreneurship but a failure to translate innovation into commercial success.

Further considerations for innovation are to do with innovation in policy making and in skills creation.

Britain's role in the world

The adoption of industrial policy in the US, and China as well as several other countries has, in the analysis of the Draghi report, left the European Union's model of working exposed, reliant on the post 1945 model of an open and competitive market of free trade governed by a rules-based international system. What does the solution as set out by Draghi mean for the UK's own industrial policy, competitiveness, innovation and for its role in relation to the EU, the US, other partners in the G7 and to a range of emerging markets? Are there sectors in which the UK could operate as key suppliers to both the EU and the US (as part of a 'western industrial strategy') for example in some aspects of the pharma industry, space, defence, data services, financial services and insurance and some areas of technological innovation? Are there opportunities for complementary uses of state subsidy that benefit a coalition of countries? Can allied economies work together to bring forward those of the global south?
