

# *The productivity puzzle*

Business Jury asks what can be done to improve productivity in a rapidly automating world

November 2017





## ***Foreword***

Official figures show that UK productivity has stagnated since the financial crisis and lags behind many other developed nations. But why? And what can be done about it?

People are at the heart of this issue: Is something preventing workers from reaching their full potential? Are businesses failing to get the most out of their people? Or do we have a wider, society-wide education and skills problem? We were keen to hear views from the front line, and so brought together a diverse range of businesses to discuss the productivity from a workforce perspective.

Our so-called Business Jury aimed to get a better handle of the problem, provide a forum for sharing best practice, and come up with new ideas and approaches, including where Government intervention might help. With this in mind, we invited a representative from the Department of Business, Energy and Industrial Strategy (BEIS) to hear and discuss the Jury's conclusions.

The discussion, facilitated by Katie Derham, was wide-ranging, raising many consistent concerns but also examples of innovative approaches that businesses are undertaking themselves. It's clear that everyone has a role to play in driving productivity improvements: The Jury identified a number areas where Government support or intervention would help, but also were very clear that improving productivity was a priority within their own organisation.

As the UK plans for its future outside the EU, there's never been a more important time to see how our businesses and workers can reach their full potential. But as our discussion showed, a perspective is also needed. The productivity puzzle is not unique to the UK, and there are some good reasons – including high employment – why ironically we fare worse than some other developed nations.

We'd like to thank all our participants for taking the time to join us and contribute to the debate.

***Phillippa O'Connor***

Partner, People & Organisation, PwC



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## Methodology

*Our Business Jury event brought together HR and People specialists from businesses, both established and entrepreneurial, in a wide range of sectors. After some scene setting on the productivity puzzle from PwC's senior economic adviser, Andrew Sentance, the jury discussed their own experiences of productivity in the workplace: the barriers, opportunities for improvement, and where Government intervention could help.*

The discussion was broken into two key parts:

1. productivity and skills and
2. productivity, flexibility and well-being.

The discussion also brought in the role of automation, changing work practices and the steps that we may need to take to nurture productivity in the future. Under the guidance of facilitator Katie Derham, the Business Jury then discussed its conclusions with a representative from the Department for Business, Energy and Industrial Strategy (BEIS): Tony Thomas, Head of Strategic Projects, Labour Market Directive.

***“The UK has the most flexible working structure on the plant. We need to maintain that post Brexit.”***



## The main messages

- While productivity growth has stagnated in the UK since the financial crisis, the UK's performance is broadly in line with other nations. There's a risk that too much negativity around this issue could become a self-fulfilling prophecy.
- The skills of new recruits are a particular issue for businesses. It's not just about so-called STEM skills. Many people joining the workforce lack the softer skills crucial for today's working world, including collaboration, resilience, and most importantly, adaptability.
- A closer partnership between business and schools could help to address the deficit between what businesses need and the skills that school leavers and graduates learn.
- Businesses are keen to help. Government support for mentoring, and a structured policy for work experience for all schoolchildren could also make a big difference in developing workplace skills at an earlier stage.
- The Apprenticeship Levy is too restrictive and arguably counterproductive. Broadening it to support different types of training would make a real difference.
- A more flexible workforce is often a more productive one, but infrastructure – particularly slow broadband speeds is a big problem. More Government investment is vital. It would also help to have more communal workspace options for younger people.
- Clarity on worker/employee status is essential – businesses would also like to see a roadmap for the Government's future direction on workplace legislation and industrial strategy, rather than disruptive incremental changes.
- While many businesses are working hard to introduce wellbeing programmes and raise awareness of mental health issues at work, they worry about the lack of medical support for those who need help.

## The jurors

<b>Chris Moore</b>	<b>Adecco</b>
<b>John Whelan</b>	<b>BAE Systems</b>
<b>Annie Gascoyne</b>	<b>CBI</b>
<b>Rebekah Etherington</b>	<b>Close Brothers</b>
<b>Alistair Milnes</b>	<b>Gazprom</b>
<b>Peter Reynolds</b>	<b>Non-Standard Finance</b>
<b>Lynne Highway</b>	<b>RBS</b>
<b>Cristina Tomas</b>	<b>Situs</b>
<b>Helen Hopkin</b>	<b>PwC</b>

## What is productivity?

There's so much written about productivity, but it can mean different things to different people. In macroeconomic terms, productivity generally means a country's GDP relative to employment. But as PwC's senior economic adviser, Andrew Sentence, explained, this raises measurement challenges as there are many compositional issues involved – the GDP of the UK, for example, is made up of different elements than the GDP of Germany.

Productivity is, of course, notoriously difficult to measure. The UK was once an economy dominated by manufacturing – in the 1960s, 35% of the UK's employment came from manufacturing but today that proportion is just 8%. Measuring productivity is relatively simple when it involves counting the output of factories – measuring the output of the UK's now-dominant service sector is much more of a challenge.

### ***Does the UK really have a productivity growth problem?***

When we look at the growth of GDP across the G7 nations since the recovery began after the financial crisis, the UK stands firmly in the centre of the pack – Japan, France and Italy are all less productive by this measure. The UK shows GDP growth of around 2% – considerably less than the 6.5% recorded by China, but still respectable for a mature economy. The financial services sector in the UK, has been the most productive in terms of GDP for over 20 years. But while productivity in the sector grew strongly between 1995 and 2007, there has been no increase in productivity in the sector since the financial crisis.

GDP per person employed, though, shows that much of the UK's growth has come from an increase in employment. But while the UK is less productive than the US by this measure, again it's not significantly less productive than other large European nations. This suggests that, while there is work to do, the UK is beating itself up a little too much about its productivity challenge and should instead be seizing the opportunities to reaccelerate growth from a relatively strong base.

That is because the real problem is that productivity rates have remained stubbornly low in all developed nations since the financial crisis. In other words, this is an international productivity puzzle and not unique to the UK. The consensus among economists is that this is caused by a combination of:

- historically low interest rates, which dampens the incentive for capital to move around
- a lack of investment in skills, innovation and capital
- structural shifts to sectors with lower productivity, and
- drag from underperforming sectors.

If you accept these conclusions the key activity for business becomes what actions are required to counteract these factors.

***“Productivity, and the reasons why it stagnates, is an issue that economists have struggled with for decades. The reasons behind the slowdown in productivity in the 1970s, for example, have never been clearly identified. Theories and ideas abound, but not many answers.”***

***“It's clear that the US has a productivity edge but it's less clear that the UK is lagging behind the rest of Europe.”***

## Productivity and skills

The Jury began by discussing the relationship between productivity and skills. What skills do businesses really need? It's a pertinent question in the digital age, as an increasing number of tasks and roles are being automated and no-one can predict with confidence what skills businesses will need 20 years from now.

For our jurors, one of the biggest concerns was the skills gap among new joiners to organisations. There's a big focus on STEM skills, but equally important are softer skills – and these are often sorely lacking.

### **The essential soft skills**

Two characteristics in particular were seen as essential but often lacking in new recruits: adaptability and resilience. Many jurors felt that the strong focus on rote learning at many schools means that pupils don't develop the problem-solving, organisational and collaborative skills that are so important in the workplace.

The Jury agreed that there were steps the Government could take to encourage the development of soft skills, adaptability and practical problem-solving. 'The school curriculum is very tight and doesn't leave a lot of room for innovation,' said one. 'Personally I would like to see children learn to apply their technical skills in a different environment.' Businesses too would be very willing to help.

Some of the businesses represented were taking their own steps to try to address this. For example, concerted efforts to recruit school-leavers from socially deprived backgrounds, sometimes lowering their qualification requirements in order to do so. 'The level of engagement and enthusiasm they have brought to the business is fantastic,' said one juror. 'It's infectious in the organisation.'

***“Some of the young people we see have had very little experience of failure. They have been quite protected. If they fail, they learn to get over it and organise themselves better. They learn resilience – and that's something that we have often found lacking.”***

***“Recruits who've faced more challenges often have a different attitude: let me show you what I can do for you rather than you show me what you can do for me.”***

## **Getting new recruits business-ready**

This discussion raised the question of whether business should be more involved in education. The jurors said they would like to see businesses establish better relationships with schools and the education system, engaging children on their future options and being vocal on the skills that organisations need. ‘It’s telling that so many kids don’t know what they want to do when they leave school,’ said one. ‘To my mind that’s a real marketing failure on the part of business and industry.’

There was a strong feeling that teaching could be more closely aligned to what business needs, but less agreement on how this could be achieved. One juror suggested that schools should be assessed not on academic results, but on what their pupils achieve 10 years after leaving. Success is too often measured on where students go to university or college, not on what happens next.

Everyone agreed that better access to work experience for all school children would bring benefits. Far too few people have access to these opportunities.

One juror commented that, understandably, many teachers haven’t worked in business so the links between schools and business often don’t exist.

There was consensus that both Business and Government need to do more to forge greater partnerships with schools.

## **Training, retraining and automation**

The Jury agreed unanimously that training and retraining are essential in improving productivity. The need to retrain more and more workers as tasks and roles evolve with the digital revolution was an issue on everyone’s mind. Some jobs would be lost to automation, but a whole host of new ones are likely to emerge. This is already happened one juror spoke of the rise of the data scientist, from ‘zero to hero’ in their organisation.

While some of the largest employers have publicly committed to re-training everyone displaced by automation, the Jury acknowledged that this wouldn’t be possible for every business. And while businesses can make training available, that’s only half the battle. ‘Re-training is a motivational issue as well as a skills issue,’ said one juror. ‘Not everyone wants to retrain.’

So, this becomes about encouraging a culture shift among employees, one where lifelong learning and retraining become the norm. The businesses represented had taken a variety of steps to encourage their employees to consider extra training. PwC is currently trialling a ‘skills audit’ system which gathers data not only on the skills that employees hold, but also on what they aspire to do. Another business represented on the Jury was making use of social media to reach its workers and encourage them to learn new skills.

More Government support for training in the workplace is seen as essential – in the form of a training levy made available when a job becomes obsolete, for example. This point led to a discussion of the Apprenticeship Levy, which came into effect on 6 April 2017 and which was felt to be far too inflexible. One juror described it as a tax on employment at a time of challenging productivity. Several members of the Jury said they would rather use the funds to train a wider selection of employees, particularly those affected by automation.

Government could also play a role in the culture shift required for workers to embrace changing jobs and roles. Younger people are arguably less likely to be scared of change, while other workers could be left behind.

It was also felt that larger businesses could share best practice and possibly partner with smaller ones on reskilling and retraining initiatives.

## **Skills and leaving the EU**

The jury had mixed views on the potential impact of leaving the EU on the availability of skills. It would be vital though for Government to promote the UK as much as possible. Key to this is a strong roadmap for the future. More clarity on the industrial strategy and what it means for technology, innovation and infrastructure would help.

**“Business needs to get more involved in schools. We shouldn’t just wait for something to be delivered and then complain about the final product.”**



## Flexibility and wellbeing

The Jury moved on to discuss flexible working and contingent workers and their role in productivity, as well as the impact of wellbeing.

### **The status of workers**

The need for contingent workers, agreed the Jury, will only increase with automation. Some of the organisations represented already rely heavily on freelance or contract workers, and felt being able to flex their workforce size to their business needs/conditions improved productivity.

Everyone felt the flexibility of employment is one of the UK's strengths. Great care would be needed to prevent any changes to working models jeopardising this position.

It is not just about businesses' needs, but how people wanted to work. According to the Resolution Foundation, four-fifths of self-employed people say they wouldn't choose to be employed<sup>1</sup>. Similarly, when McDonalds conducted a trial to see if their staff wanted to move off zero-hour contracts, 80% chose to remain on flexible contracts<sup>2</sup>.

The Jury called for greater clarity and guidance from the Government on the status of workers. At the moment, said one juror, the typical workforce consists of three broad groups – the employed, the self-employed, and 'something in the middle'. The biggest issue for many large employers is working out which category people fall into. Uncertainty around the future of contingent workers, zero hour contracts and IR 35 contractors is casting a constant shadow over business.

***“We need to be careful that the government doesn't force people to do something they don't want to do. Some people want to be self-employed. Don't force them into a work status they don't want.”***

***“There is a risk of regulatory creep in this area. Working models tend to develop because there is a commercial opportunity there. If the government curtails that, productivity will fall.”***

<sup>1</sup> Just the job – or a working compromise?: the changing nature of self-employment in the UK, D'Arcy, C. and Gardiner, L., Resolution Foundation, 2014

<sup>2</sup> <https://www.theguardian.com/business/2017/apr/25/mcdonalds-contracts-uk-zero-hours-workers>

## **Flexibility and productivity**

Flexible working practices is seen as a significant driver of productivity by our Business Jury. ‘Broadly, people are more motivated and engaged when they have flexibility, despite the management challenges that come with that,’ said one. Most of the jurors allow flexible working to some extent, although complaints about the quality and speed of broadband and mobile phone connections in some parts of the country – and even in some major cities – were raised. Investment in world-class communications infrastructure should be a Government priority, said the Jury.

But that’s not the only infrastructure problem standing in the way – one juror pointed out that younger employees in big cities tend to live in shared housing, which makes finding a quiet space to work at home difficult. One juror’s organisation had solved that particular problem by suggesting that teams collect at each other’s homes to work, and idea that had proved popular with staff.

## **The role of wellbeing**

Several jurors said their businesses had developed wellbeing programmes for staff and were seeing the benefits. One said that their business was piloting a programme of yoga, meditation and mindfulness, and was hoping that this would address high levels of absenteeism in some parts of the business.

Another had set up a mental health awareness programme – mental health is expected to be the biggest cause of absenteeism by 2030. However, jurors were worried that identifying the problem was only half of the battle. ‘Raising awareness is one thing, but finding help if someone needs it is another. Sometimes we worry that we’re making things worse by raising awareness because the help just isn’t available.’ It was felt that improving the support framework for mental health beyond the business should be a priority for Government.

## **Detoxing from digital life**

The high rate of productivity in the US compared to the UK raises the question of whether the US working model – where 10 days’ annual leave is the norm in some sectors – is the more productive option. Would UK organisations consider moving to the US model? The Jury disagreed wholeheartedly – in fact, many said they sometimes struggled to persuade some of their workers to take enough holiday.

A couple of organisations had experimented with an option to ‘buy’ or ‘sell’ holiday entitlement – but in most cases the option to sell holiday had eventually been withdrawn because of the impact on wellbeing of some staff, who were not resting enough.

‘Switching off’ is clearly a problem for some workers in the digital age. Could the 24-hour ‘always on’ world of electronic communication be contributing to the productivity problem? ‘Email is a big distraction for organisations generally,’ was the view of one juror.

Some of the businesses represented had considered switching off servers over the weekend or banning emails after a certain time of night, but as one juror pointed out, this doesn’t work for everyone – some people have family commitments that mean they want to work after the children have gone to bed. ‘It’s about expectation,’ said one. ‘If you receive an email at midnight no-one should expect you to reply at once.’ When it comes to work/life balance, it should be recognised that people often fall into two camps: integrators and separators, with separators needing to leave work behind.

In many areas technology was seen to improve well-being. One example cited by PwC was the use of algorithms to allocate work more fairly, smoothing disparities between people with high utilisation rates and those who were under utilised. Likewise, technology was helping with ‘post code’ resourcing, fitting people with assignments closer to where they live.

**“Sometimes people are less productive simply because they are bored. More variety in tasks would help that.”**

**“From a wellbeing point of view, four or five weeks leave a year is a good thing.”**

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## *In conclusion*

Tony Thomas from BEIS welcomed the opportunity to hear first-hand the experience of such a broad range of businesses, and he reassured the Jury that many of the issues discussed were already high on the Government's list of priorities.

Even so, education, and making sure that new recruits have the right skills for business, remain a big challenge for the UK. There are good examples in practice of business working closely with universities and the Government is keen to encourage more of that. Similarly, third sector organisations (such as Career Ready) are working hard to improve access to work experience and to give children a better understanding of the work environment before they enter it. Discussions such as this were helpful, he added, and the Jury's conclusions would be fed back to Department for Education.

The UK has a light touch in terms of regulation around working life but the risk with some working models was that flexibility was used as a way of transferring risk from employer to worker. There is a danger in allowing a choice of working models that a minority of organisations push the rules as far as possible. The Government's aim is to retain flexibility but also to protect the most vulnerable.

Overall our BEIS guest stressed that change couldn't happen quickly; any solution must work for workers and businesses, and change would involve detailed and lengthy consultation with both. But events such as this Business Jury will continue to be invaluable in making the views of business heard.



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