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INCENTIVISING AN ETHICAL ECONOMICS

A RADICAL PLAN TO FORCE A STEP CHANGE IN THE QUALITY AND QUANTITY OF THE UK'S ECONOMIC GROWTH

Simon Szreter,
Hilary Cooper
and **Ben Szreter**

July 2019

ABOUT THE IPPR ECONOMICS PRIZE

The inaugural IPPR Economics Prize invited entries in response to the question: **"What would be your radical plan to force a step change in the quality and quantity of the UK's economic growth?"**

We wanted to know whether the downward trend in the rate of economic growth can be reversed, and if so, how this can be done. Is it realistic, desirable and achievable for the UK economy to grow at 3 or 4 per cent in the 2020s? We wanted to capture the best new thinking out there.

Crucially, we wanted to understand not just what policies could raise the growth rate, but also how growth could translate into higher pay for ordinary households and reduced inequalities across regions and generations. We wanted to know whether such proposals could be environmentally sustainable, accelerate decarbonisation, and ensure that the UK meets its international commitments and its responsibilities to present and future generations.

We offered a main prize-pot of £100,000, with a dedicated under-25s prize of £25,000 and a runners-up prize also of £25,000. IPPR and the judging panel, chaired by Stephanie Flanders, with John Eatwell, John Mills and Helena Morrissey, examined over 200 ideas and ultimately awarded prizes to four entries: two winners of the main prize, an under-25 and a runner-up.

The IPPR Economics Prize was generously supported by John Mills, The de Laszlo Foundation, the Nigel Vinson Charitable Trust and Christopher Nieper.

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The progressive policy think tank

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SUMMARY

KEY HIGHLIGHTS

- **Unlocking the productivity secrets of our history**
- **A reinvigorated ethical economics strengthening our democracy**
- **A new social contract to nurture human capital**
- **New ways to incentivise reductions in inequality**
- **A National Care Service to deliver intergenerational equity**
- **Targets and rewards for sustainable growth**

UNLOCKING HISTORY

Our analysis looks at previous periods of British economic history to identify the enabling conditions for our most successful episodes of economic growth, noting the crucial importance of large-scale improvements in welfare and human capital to their success, and the negative impacts when these policies were reversed.

We first examine the importance of the universal parish Poor Law established by Elizabeth I in 1601 in laying the foundations for the Industrial Revolution. Historians have shown that this system of collective responsibility directly stimulated England's successful industrialisation, liberating labour to be mobile and, uniquely in Western Europe, making famine a thing of the past. Combined with the 1601 Charitable Uses Act the wealthy were incentivised to invest in schools, apprenticeships, hospitals and housing for the wider population.

Following this we look at the 'Golden Age' of economic growth from 1945 to 1973. This was the most successful sustained era of productivity growth in our history, averaging 2.4 per cent per annum, with rising public investment in health, education and housing vital to its success. High marginal tax rates on income, capital and inheritance in this period were also instrumental in incentivising business leaders to promote the long-term growth of the corporations they led, rather than focus on their personal short-term gains.

In its own prescription for kick-starting growth, IPPR (2018) calls for a rebalancing of power to move the economy out of its current low wage/low productivity equilibrium. This, IPPR's Commission on Economic Justice argues, requires a shift in power from: corporate management to employees/trade unions; short-term financial interests to long-term investors; dominant companies to entrepreneurs; Westminster to the nations and regions; and households with great wealth to those with little.

We agree wholeheartedly that such structural and institutional change, including a greater emphasis on localities, allied to significant revenue-raising tax and wealth redistribution, is essential to deliver a step change in the quantity and quality of economic growth. We argue that this must be achieved through reconceptualising the welfare system as a growth promoter. Our radical proposal provides a general, motivating mechanism to achieve this.

OUR RADICAL PLAN

Our original contribution starts with a radical new approach based on two new quasi-altruistic contracts, combined with incentivising mechanisms:

- a new, equitable **social contract** to invest in sustainable growth through tax increases – but combined with rewards when targets are met
- a new **intergenerational contract** offering free universal care in old age – conditional on wealth transfers into a citizens' fund.

These two contracts seek to re-establish the ethical principles on which the economic success of the Golden Age was built. However, the special ingredients of the postwar era, when society came together in a collective and – in the main – mutually supportive spirit of regeneration, will be harder to reproduce in our currently more divided society. A different type of motivator will be required in the 2020s.

We therefore propose building on the Elizabethan era's insight that altruistic behaviour can be incentivised by the right policy architecture. We will do this by **offering businesses and higher rate taxpayers the chance to win bi-annually agreed reductions in corporation and income tax**. For businesses this will be after an initial restoration of corporation tax to 2008 levels. Subsequent reductions will be entirely conditional on meeting a set of economy-wide targets for growth, productivity, skills, inequality and investment for decarbonisation. Businesses will develop these targets with government and other stakeholders and will oversee an investment programme directing the tax receipts and their own resources to renewed sustainable growth.

A new top rate of income tax will be introduced and pegged to levels of earnings inequality. **As actions by businesses or government reduce the pay gap between higher and median earnings, fewer taxpayers will pay the highest rates**. The revenue this measure raises will be invested in measures to reduce poverty.

We propose a similar system of mutual gain in crafting a new intergenerational contract, urgently needed as the burgeoning health and care requirements of an ageing population threaten to swamp public spending, diverting resources from public investment. If we fail to solve the emerging care crisis, our productive capacity and growth potential will be affected as support for the older population becomes increasingly provided by family carers.

We therefore argue for significant changes in the taxation of property and inheritance, alongside collective risk pooling of social care costs, through a levy on retired taxpayers. The direct payback offered for this is a promise of **a ring-fenced social care citizens' wealth fund** capturing this revenue. This **will be used to provide a new National Care Service enshrining a guarantee in old age of free care based on need**, on the same popular principle as the NHS and, indeed, fully integrated over time with health provision.

AN ETHICAL ECONOMICS

We contest the conventional assumption that societies can only afford the luxury of welfare on the back of economic growth – and so can be cut during times of difficulty – because it is a burden on the 'productive' economy. The historical truth is that commitment to universal welfare provision, including health, education and training, has been vital for achieving this country's highest rates of productivity growth. As endogenous growth theory implies, investment in the entire population's human capital is critical to long-term economic success.

As we prepare for the challenges of climate change and artificial intelligence, ethical economics must replace models based on the notion of homo economicus – an amoral self-interested agent – so that all parts of society come together to invest in the population's collective human capital. It will require political leadership that guides the economy towards long-term sustainable growth, with a clear democratic commitment to ensuring that short-term gains for some are not prioritised over long-term wellbeing for all.

1.
THE ARGUMENT FROM HISTORY

> *"The longer you can look back, the farther you can look forward."*
> Winston Churchill, 1944

We make no apology for devoting a significant proportion of this proposal to a historical exposition. We should not assume that because the past was different there can be no worthwhile lessons to take from history. Proposals to engender productivity change today will only be successful if they are based on a thorough understanding of productivity change in the past. Such historical understanding is vital to inform proposals that are both genuinely radical and which also exploit the full potential of our culture.

We begin this analysis, then, by looking at the two separate periods in Britain's history of sustained economic success, in the form of rising productivity. Both were intimately associated with the state taking a leading role, innovating a universal and equity-promoting social security and welfare system. The first of these two periods, c.1600–1834, lasting almost one-quarter of a millennium, was widely significant for world history because it culminated in the world's first industrial revolution, c.1800–1870. The second period, 1945–1973, though lasting only one-quarter of a century, is also highly relevant because it is the only substantial period since the Industrial Revolution when universalist principles once again prevailed – and much-increased investment in health and education for the mass of the population again delivered exceptional productivity growth.

1.1 PRODUCTIVITY, LABOUR MOBILITY AND URBANISATION: 1600–1800

From a position of backwardness at the edge of Europe in 1600, over the next two centuries the English economy consistently outperformed the Netherlands, the most advanced, urbanised society in the world in 1600. The proportion of England's population living in towns and cities increased dramatically – by three-and-a-half times – while in the rest of Europe, including even the Netherlands and France, the equivalent rate of increase was only in the range of 10–25 per cent across these two centuries (Wrigley 2004). London became the world's largest city while England's population was fed effectively despite the shrinking proportion of the labour force working on the land because of a long, sustained increase in agricultural productivity.

As a result, well before the first steam-driven factories appeared, England's urbanising economy had been outgrowing the rest of Europe for two centuries, as each generation's young adults stopped working exclusively in the fields. All-important labour power was released for the economy's proliferating cottage industries, its commercial and maritime trading activities and eventually, in the 19th century, its expanding steam-driven mechanised factories. England's population doubled from about 4 million at the start of this period to over 8.5 million in 1801, reaching 15 million by 1841.

While her great imperial rival during the 18th century, France – lacking a universal poor law – saw social breakdown and revolution, England successfully became a

United Kingdom with Scotland in 1707 and with Ireland in 1800. This was followed by a turbulent industrial transition but no 1848 revolution, despite the stresses of economic transformation and a rising population.

The key to achieving such remarkable rates of economic growth in the period 1600–1800 lay in two features. First, raising productivity per acre and per labourer on the land; and second, maximising the mobility of labour power to go to wherever the most valuable forms of new cottage industry and manufacturing were offering higher-waged opportunities.

Taxation, social security and the role of the Elizabethan Poor Law

The Elizabethan or 'Old' Poor Law was a crucial institutional innovation which facilitated precisely the two growth-promoting processes of rising agricultural productivity and labour mobility. It was something which no other economy – not even the Netherlands – had. So, what was it? A universal social security and welfare system: an absolute entitlement to life-preserving 'relief' for every subject of the Crown, primarily in the form of payments in kind or cash.

The Poor Laws were mandated by statute in 1601 with their funding, administration and legal oversight radically devolved. Each of England's approximately 10,000 Anglican parishes (average population 500 people in 1601) had to establish a fund which would support orphans, widows, the old and disabled, the ill and the unemployed all year round in response to demand. It was funded by a thoroughly progressive principle of taxation (Slack 1990). In theory all who were not currently in need were liable to pay in, but payment was strictly proportional to the value of land (the principal source of wealth and income in 1601) which householders occupied in the parish.

Importantly, payment of the tax was neither avoidable nor evadable and was a matter of local public knowledge. Justices of the Peace could punish any member of the community for defaulting on their collective obligation. To avoid problems of unlimited liability, each subject's right to relief was fixed to one parish only, termed their 'settlement'. They inherited their settlement entitlement from their fathers, just like a piece of property. On marriage, a female's settlement became that of her husband's settlement, again mimicking property law. On moving to a new parish for work, individuals could apply to have their settlement entitlement (and that of their children) moved to their new place of residence after a period of one or two years.

So why should this particular system of universal social security have been so beneficial for economic growth when it might be thought that such a 'tax' would be a burden on the 'productive' economy? It is true that by the end of the 18th century approximately 2 per cent of national income was being transferred from the rich to the poor, a far greater outlay on the poor than, for instance, in France (Smith 2011). However, historians have also shown that the Poor Law simultaneously created exactly the right set of incentives both to facilitate rising land and labour productivity in agriculture and also to maximise labour mobility in response to economic opportunities – the two key features identified above for promoting growth.

First, as Peter Solar (1995) has shown, landlords and farmers could reap the economic gains to be had from increased farm sizes – by buying up smaller farms, through parliamentary enclosure of common land and from laying off workers or changing their labour contracts to more efficient weekly or day labour – without this provoking the same fears and strength of protests from those adversely affected, as such attempts, by contrast, elicited on mainland Europe. But equally, they had a strong incentive only to do this if it really made long-term economic sense, because, as ratepayers into the parish Poor Law fund, they would also have

to reckon with their liability for supporting the families of the laid-off workers until they found new work.

Furthermore, from the point of view of the smallholder or tenant, working for wages – whether in the countryside or in the town – was, with the existence of a genuine social security net, not necessarily any less secure than access to a small plot of land. There was no need for the poor to fetishise land ownership as their cherished symbol of family security, as happened among the peasantry on the continent, notoriously in France, whose agriculture was afflicted with the practice of 'morcellement' – ruinous subdividing of family plots (ibid).

Second, as Richard Smith (1986) has emphasised, attachment to landholding at all costs was also attenuated because the aged poor, disabled and widowed had an alternative, collectively provided source of support in this recognised right to call on the parish fund, obviating the absolute necessity to retain close contact between the family's generations. This removed a significant obstacle to labour mobility, as did the younger generation's relative certainty of being provided for, within the rules governing Poor Law settlement rights, wherever they moved to work in the economy (Taylor 1989, Solar and Smith 2003).

For all these reasons, research has found English society to have been hyper-mobile in the era of the 'Old' Poor Laws, with very high proportions of both sexes marrying outside the parish in which they were born (Macfarlane 1986). One in six of the entire population migrated to London, alone, in the course of their lives (Wrigley 1987). The majority of young adults left home early in their teens, worked and saved independently for a decade or more before getting married and setting up their own independent household for child-raising, with as much as 10–20 per cent of each generation never marrying (Kussmaul 1981).

This degree of independent living and the avoidance of multigenerational households for mutual support is unusual (in world history) and it has sometimes been one-sidedly portrayed as 'English individualism' although, more accurately, it was a collectivist-individualist regime. It did encourage individual mobility and income earning and saving by young adults, but this was only feasible because of the parish-based collectivist solution to the problem of old-age insecurity, permitting the younger generation to act in an independent fashion, to the great benefit of a growth-oriented economy (Schofield 1989; Smith 1986, 1996).

Third, another major, long-term economic benefit deriving from the Poor Laws is that, since the 1620s, there has been no significant famine in England (Galloway 1988, Walter and Schofield 1989, Kelly and O'Grada 2011). Poor Law relief sustained a buoyant level of effective demand for the economy's produce, even in times of dearth, by maintaining the purchasing power of the poorer section of society when food prices rose. The English nation was the first in Europe by well over a century to be free from the age-old, devastating insecurity of famine, demonstrating the importance of effective social policy in achieving this fundamental freedom (Solar 1995). Only in a society free from regular acute food insecurity can the practice of personal saving and lifetime-planning become a rational practice for the vast majority of people, not merely the elite.

Finally, by a brilliant piece of statecraft, the wealthy in each parish were simultaneously financially incentivised through the Charitable Uses Act of 1601 to engage in civic leadership to create apprenticeships, schools for orphans and poor scholars, bequests and almshouses for the ill and the elderly, cottages for the poor, and eventually to found hospitals (Szreter and Ishkanian 2012). Plaques in almost every parish church in the country attest to the culture of civic philanthropy which ensued. This was only truly effective, however, by virtue of being framed within the obligatory parish tax system, since philanthropy on its own was a weak and unreliable source of support for the poor (De Swaan

1988: 21–36). To the extent that their charitable endeavours did then truly pay off in promoting the poor's independence, the parishes' wealthier families were alleviating their own compulsory tax-burden through the poor rates.

Overall, Elizabeth I's Poor Law facilitated the most sustained period of rising economic prosperity in the nation's history so that by the beginning of the 19th century England had become the most dynamic economy in the world, underpinned by its social security system.

1.2 THE IMPETUS FOR GROWTH IS LOST: 1834–1945

During the protracted continental wars with revolutionary and Napoleonic France, 1793–1815, not only the national debt but also the costs of the Poor Law had risen for a nation with so much of its manpower mobilised and injured. The governing class now began to question the validity and expense of the Poor Law's principle of collective provision, influenced by new ideas stressing individual responsibility and agency.

The free market economic ideas of Adam Smith, Malthus and Ricardo are well known. But equally important ingredients were the utilitarians' pleasure–pain principle for designing policy (a kind of proto-nudge theory) along with a brand of moralising evangelical Protestant Christianity (Hilton 1988, Mandler 1987). The governing elite was now persuaded to dramatically cut the costs of universal relief in what had become the world's first rapidly urbanising, industrial nation. They thought charity could fill the gaps, though it soon proved inadequate, as Hennock (1973) has shown. Consequently, in 1834 the principles of poor relief were transformed into the harshly deterrent system of the workhouse test, the New Poor Law, which virtually criminalised the poor as work-shy moral delinquents (Brundage 2001).

While the costs of poor relief were, indeed, held down for the rest of the century, the UK's manufacturing industry had by 1914 lost its world-leading place to the US and Germany, and only further lost ground to the US in the interwar decades. These countries had taken a different approach when their economies subsequently industrialised: 50 years after the Old Poor Law had been abandoned in Britain, Germany adopted a generous universal social insurance system for its workers during the 1880s; while the US led the UK by over 30 years in its commitment to universal secondary education from 1910.

This failure in Britain to take a lead in driving forward investments in human capital held back industrial productivity growth, squandering the enormous advantage that had been built up by the 1830s. The UK's overall productivity growth averaged only 0.8 per cent per annum between 1871 and 1911 and 0.9 per cent per annum between 1911 and 1937, well behind the rates achieved by the US and Germany (Crafts 2014)

Nor was empire an unproblematic economic success story. Trade and overseas investment expanded, yet in the decades following Queen Victoria's assumption of the title 'Empress of India' millions died in famines in the subcontinent. Even within the United Kingdom itself the new governing ideology and its poor law workhouses presided over the worst famine in Ireland's history, 1845–49 (Gray 1999).

Seebohm Rowntree's famous investigation into poverty found that, by the end of Victoria's reign and despite 300 years of economic growth, 30 per cent of the future workforce was growing up in households in poverty. Rowntree's research showed that poverty was mainly due to situations out of the control of the poor: most were poor because of low wages (52 per cent), some because they had many

children (22.2 per cent), and others because of the death or incapacity of the chief wage earner (20.7 per cent) (Rowntree 1901).

The period culminated in recurrent mass unemployment, the General Strike of 1926 and the many hunger marches, of which the famous Jarrow Crusade of October 1936 was only one. Meanwhile, British society had become a divisively class-ridden one, in which those with a little property increasingly turned their backs on those without – sometimes literally.[1]

1.3 THE GOLDEN AGE: 1945–73

Finally endowed with universal suffrage from 1928, 90 years after the Chartists first campaigned for it, and following the fight against fascism, 1939–45, the electorate voted for values of solidarity over individualism and the postwar welfare state was born. After a 110-year absence, the collective responsibility principles of the Elizabethan Poor Law were reinstated with steeply progressive taxation once again funding universal provision of welfare, healthcare, training and education. Occupational and social mobility blossomed, and the economy's productivity growth fired upwards for the first time in a century.

From 1950–73 UK productivity growth achieved a historic peak, averaging 2.4 per cent per annum – almost three times higher than throughout the entire period 1871–1937 – and once again matching the US (Crafts 2014). These productivity gains were all the more impressive as they were achieved under conditions of full employment. GDP grew at similar steady rates up until 1973, with Keynesian demand management ensuring there were none of the deep plunges into recession that came subsequently.

In his ground-breaking work *Capital in the 21st Century*, Piketty argues that the decades of the Golden Age were unique in recent economic history in curtailing wealth concentrations. His analysis shows that, whereas in the years around 1910 the top decile of wealth owners in France and the UK were in command of around 90 per cent of all capital (80 per cent in the US), by the early 1970s this had reduced in all three countries to around 60–65 per cent (Piketty 2014). This, Piketty argues, is an exception to the general tendency in a capitalist economy, where the returns to capital will, if left unchecked and untaxed, always exceed economic growth – a principle captured in his now famous inequality expression, $r > g$.

Piketty's point is that whenever the return to wealth exceeds the return to labour then, as a matter of definition, societies will experience ever-increasing inequality as wealth becomes more and more concentrated. Ultimately this becomes a threat to democracy as an effective oligarchy of wealth concentrate not only economic power but also political influence to shore up their position, seeking to block policies that might reverse their ability to capture these high returns – as aptly demonstrated by the amounts wealthy individuals and corporations are prepared to spend on political lobbying (Page, Bartels and Seawright 2013, Page and Gillens 2014, Skocpol and Hertel-Fernandez 2016).

Piketty's analysis shows that for several decades leading up to the 1970s there was a temporary, anomalous period both in Europe and the US, as a set of historically unusual circumstances coalesced. This was due to the severe depletion in the value of the stock of capital held by the elites as a result of two world wars combined with the 1929 financial crash and the subsequent business failures of the Great Depression. In addition, the enormous demands that these events placed on national finances necessitated unprecedented levels of taxation to which the elite found they had no option but to acquiesce. The thoroughly progressive

1 A particularly graphic example was the building of the Cutteslowe walls in North Oxford in 1934 by a private developer to keep out neighbouring council house tenants (Collison 1963).

taxation of inheritance, capital and income adopted during the second world war was then successfully extended by a postwar generation, now fully enfranchised, and collectively endorsing the equitable rebuilding of their societies through a redistributionist state.

Although hard to believe in today's neoliberal world, for four decades from 1942–82, the US had widely supported tax rates of between 70 per cent and 90 per cent on top incomes and in the UK the top rate of income tax was set at 90 per cent or above for almost the entire 40-year period (Piketty 2014). Support for this form of taxation of excessive incomes was, as Piketty shows, an American invention. Irving Fisher, the respected president of the American Economic Association, proposed in his address of 1919 that the concentrations of wealth accumulated by robber barons like Carnegie and Rockefeller posed an undemocratic threat that should be remedied by a 100 per cent tax on estates passed on to the third generation, to prevent, as he argued, the US coming to resemble neo-aristocratic Old Europe.

The US economy grew at least as strongly during the postwar period of high taxes on the wealthy as it has since, while the UK economy, as demonstrated above, experienced its highest historic rates of productivity growth during the three postwar decades of high progressive taxation. As Piketty (2014) argues, in eras of higher marginal tax rates such as this, business leaders are likely to switch from actions directed towards personal gain, in which they are no longer so invested, to decisions that deliver wider, inclusive economic benefit.

In his review of Piketty, Szreter (2015) writes that as a result of "the introduction of progressive death duties and taxes on the unearned incomes from ownership of capital … 'inheritance collapsed' and in its place something more like meritocracy and upward social mobility arose". This saw the elite 10 per cent of capital owners joined by another 40 per cent of the population who were able to convert their earnings into home ownership.

Complementary to this taxation regime, its revenue supported increased redistributive spending on health and education, with the flagship policy of this era being the establishment of the NHS in 1948, for the first time offering free universal healthcare. At the same time the UK finally followed the US in introducing free secondary education for all from 1944; and then mandatory grants for university maintenance and fees from 1962. UK state investment in education massively expanded, more than doubling in proportionate terms from 2.7 per cent of GDP in 1939 to peak at 6.4 per cent in 1975/6 (HM Treasury 2006; IFS 2011).

This powerful interaction between progressive taxation, especially of wealth and inheritance, breaking for a few decades the cycle of ever-increasing wealth concentrations and, critically, supporting investment in the health and education of the workforce, constituted an oasis of equitable human capital investment in our modern history. This has since evaporated – paradoxically, partly because of its own success. A mass electorate of increasingly home-owning taxpayers (more workers were being drawn into the tax net by the 'fiscal drag' of the 1960s and 1970s) was successfully enlisted by Conservative governments in the 1980s to support the capital-owning elite as they sought lower taxation of income and wealth. This led, as Piketty's analysis would predict, to a resurgence of inequality and a significant rise in poverty, as neoliberalism took hold.

1.4 NEOLIBERALISM TO THE FINANCIAL CRASH

The 1970s ushered in the end of Bretton Woods and witnessed two oil price crises. In the UK the electoral consequence was a turn to the New Right of Thatcherism. Competition and consumer choice would supposedly ensure efficiency. Inequality was to be embraced, as a natural reward for the economy's winners, from whom

prosperity would ‘trickle down’. Thatcher extolled Victorian values, repudiating collective social responsibility, and the Conservative secretary of state for social security, Peter Lilley, announced in 1992 his plan to "close down 'the something for nothing' society". Such an approach contrasts starkly with the universalism and ‘pre-distribution’ of the Golden Age, in which access to opportunities based on merit was opened up via inclusive social provision.

Economic growth under neoliberalism was aided by labour market and supply side reforms – though now punctuated by recurring recessions – while productivity growth continued at a steady but slower pace up to the watershed of the financial crisis. But the momentum of rising education spending was lost, as the percentage of GDP devoted to education was cut for the first time in modern history – by a whopping one-third between 1975/6 and 1988/9 with teachers in state schools reduced by 50,000 – 10 per cent of the workforce (IFS 2006, 2011; HM Treasury 2006).

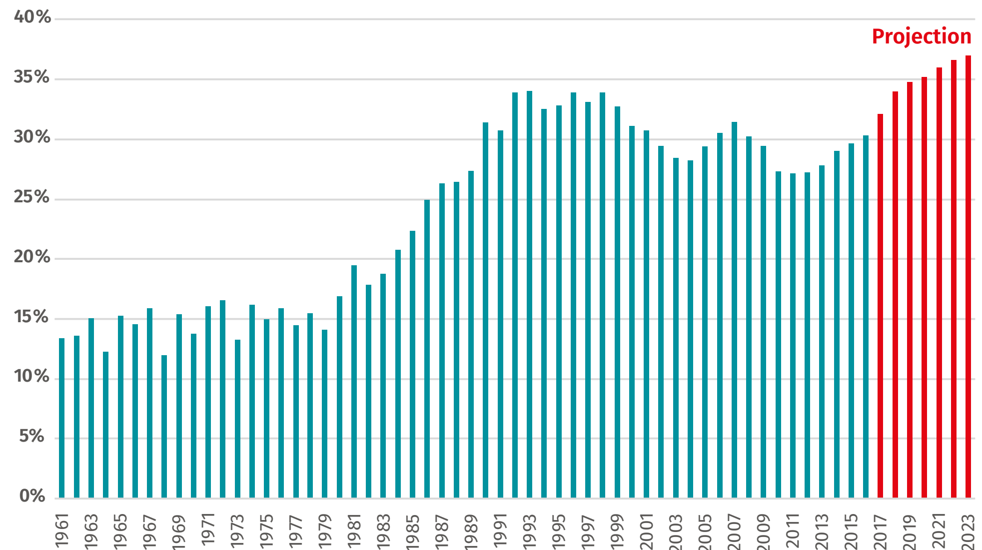
The period was accompanied by widening inequality, escalating house prices, reduced social mobility and over nearly two decades a new norm of permanent mass unemployment, never below 2 million in the period 1981–97 (ONS 2019). Trade union powers were curtailed, union membership plummeted and the share of output going to labour fell. Meanwhile reduced taxation for businesses and business leaders and shareholder short-termism created incentives for risk-taking behaviour for anticipated personal gain. When allied to financial deregulation and failures of oversight, the stage was set for the 2008 financial crash.

The post-2010 ‘austerity’ regime of spending cuts which was introduced to redress the deficit created by the financial crisis, has lowered GDP (Stirling 2019), seen the lowest growth in real earnings since the end of the Napoleonic wars – albeit alongside significantly expanding employment – and, as a result of deliberate policy, led to significant real reductions in welfare provision and rapidly growing food bank use. Since 2008 the average annual rate of productivity growth in the UK has been just 0.4 per cent, opening up a substantial productivity gap with other Western economies (Giles 2018). This ‘productivity puzzle’ is now a key focus of attention for political and economic commentators.

Figure 1.1, from Corlett (2019), graphically illustrates the steep rise in relative child poverty during the era of neoliberalism, with a temporary but small alleviation during the years of New Labour in response to measures such as the minimum wage and targeted tax credits. There has been a clear acceleration since the years of austerity, such that child poverty (measured on contemporary definitions) is now 30 per cent – the same as that found by Rowntree using his measures at the end of the Victorian era. Child poverty is projected to rise further, potentially reaching 37 per cent by 2023–24, meaning more than 5 million children would be living in households with income below 60 per cent of the median – this would be a level unprecedented in recent history.

FIGURE 1.1: CHILD POVERTY IS PROJECTED TO RISE TO A LEVEL UNPRECEDENTED IN RECENT HISTORY

Proportion of children living in relative poverty (after housing costs)



Notes: Financial years after 1993. GB only before 2002–03. Bars in red are projections.
Source: Resolution Foundation analysis of Department for Work and Pensions 2018; Resolution Foundation projections; and IFS 2019.

This outcome is the culmination of four decades of neoliberal policies, where 'greed is good' became an accepted value, and which have succeeded only in promoting rampant inequality. It is depressingly obvious from an historical perspective that such misguidedly myopic 'individualist' policies could only return the UK to all the social and economic ills of the Victorian and interwar period along with its flagging productivity. Is there a 'productivity puzzle' or are we simply overlooking 'the bleeding obvious'?

1.5 WHY INEQUALITY MATTERS

Income inequality in the UK has risen substantially since 1979. Data published by the Institute for Fiscal Studies (Cribb et al 2018) shows that for 20 years from 1961 to 1980 income inequality was broadly stable, but then rose suddenly and rapidly during the following decade.[2] Despite some small variations up and down since then, it has not fallen back below the peak levels reached at the end of the 1980s.

This was the direct result of policies pursued by the Conservative government 1979-97, was tacitly condoned by the New Labour government 1997–2010, and once again allowed to continue by the Coalition and Conservative governments of 2010–19. In each of these three eras the precise reason why the varying policy priorities produced or sustained this steep rise in inequality was different (a focus on increasing incentives for 'wealth creators' and breaking the bargaining power of trade unions until 1997; a primary focus on the reduction of poverty rather than inequality from 1997–2010; and austerity policies that have increasingly reduced public services and income-supporting transfers to the vulnerable since 2010).

2 The IFS analysis uses the Gini coefficient, the conventional headline measure of inequality

Evidence emerged soon after 1979 that a government pursuing a policy of raising economic inequality and permitting unemployment to rise would run the risk of worsening health inequalities and could even reduce absolute levels of health among the poor (Moser, Fox and Jones 1986; Moser, Goldblatt and Fox 1990). Those promoting the policy seemingly believed that in the medium and longer term their recipe for increased economic growth would 'raise all boats' so that temporary health problems for the poor and unemployed would in due course disappear; and that, in any case, nobody in the UK suffered the kind of absolute poverty that was life-threatening.

Politicians and economists entirely discounted a problem which, initially, only certain public health experts were warning against (Wilkinson 1996). This was that inequality itself and also substantial rises in inequality, could themselves be harmful to the health and wellbeing, including the psychological wellbeing, of a large proportion of the population. This is more fully expounded in subsequent research by Wilkinson and Pickett which has been critical in showing that those who, for whatever reason, find themselves living in circumstances of relative poverty, are not only afflicted by a range of material deprivations relative to their more fortunate fellow citizens. They may also be additionally emotionally burdened with a sense of the social injustice of their situation, in particular perhaps in relation to the predicament of their children (Wilkinson and Pickett 2009, 2018).

Given the ups and downs of any particular industry or town in a global free market economy, many people will be exposed to these feelings of injustice as a result of insecure work and income. There is robust research which shows that in circumstances of multiple and compounded socioeconomic risks, only the most resilient of parents can avoid a range of behaviours which, unfortunately, are harmful in terms of Bowlby's (1969) seminal attachment theory of child development. These include dissociative behaviour (being too distracted to give attention); frightened or frightening behaviour due to moments of extreme anxiety (note this is not physically or sexually abusive behaviour but does include violence of language, despairing language, interacting with children as though the child was in control); or withdrawing/distant behaviour (Cyr et al 2010). They result in insecure attachments: 'anxious-resistant', 'anxious-avoidant', or 'disorganised/disoriented' (Ainsworth 1978).

Deficiencies of this sort in the fundamental quality of child–parent attachment can have deeply damaging intergenerational consequences that imperil the nation's long-term economic productivity. Children with disorganised attachment are likely to be less able to learn effectively or behave 'normally' in schools, degrading their own future capacities to acquire human capital, to remain healthy and socially connected and to integrate into their society (Geddes 2018). As teenagers and adults there is a higher chance that these attachment-compromised children will go on to require a range of expensive resources and rehabilitation services, particularly in relation to mental health and behavioural issues, including potential involvement in crime or substance abuse.[3]

All of this is profoundly and thoroughly correlated with social patterns of both inequality and poverty; and is manifesting now in complex and long-term problems. In other words, far from fostering healthy competition and improved growth via the incentives to join the ranks of the rich and successful, inequality – and especially the rising inequality associated with poverty and economic insecurity – in fact has the opposite effect. Alongside the human cost, we are threatening future growth as inequality saps the ability of current and future generations to make a productive economic contribution. We have repeated the productivity-degrading policy mistakes of failing to nurture human capital that were made after 1834 when the New Poor Law replaced the Old.

3 In the UK we now have a minister for suicide prevention, while Wacquant 2010 argues that the US is now simply incarcerating the children of the poor, as a (very expensive) alternative to rehabilitation efforts.

2.
THE POLICY LESSONS FROM HISTORY

The lessons of the two distinct periods of impressive productivity growth in the British economy are very clear. They indicate to us something important about how the long-established characteristics of British society and culture can be best harnessed for a form of economic productivity that is in fact inclusive and sustainable. There are six lessons in common in both periods which could now be adapted into policy for the immediate future.

LESSON 1: EMBRACING COLLECTIVE RESPONSIBILITY

Of critical importance is **a positive value of collective responsibility that is expressed in a universal social security policy and a welfare system** aimed at enhancing the capabilities of those needing its support. Such support is understood to be a positive entitlement of all UK subjects because it contributes positively to the welfare of all and builds human capital to support economic productivity; and it is therefore specifically not seen as a burden or unproductive cost on the economy or as something which should be begrudged to the unfortunate fellow citizens who need it. The provision of collective support and security is essential for independent individualism to flourish at all levels of society.

LESSON 2: GUARANTEEING FREEDOM FROM INSECURITY

Absolute **guaranteed security for all citizens from the primary wants of food and shelter must be a matter of national pride** not shame; not only because they are humanitarian rights which a civilised society should uphold, but also because history shows they are crucial forms of freedom for all citizens to be able to begin to act as independent economic agents. The true and long-term cost to the economy is not in the transfer payments which should ensure that all have food and housing security, but in the inability of those who would be denied these functional basics to act independently; and because they are sentient humans who understand this degradation to their dignity, sources of psychic escape might be sought which are further costly to themselves and society. The 2,000 food banks and the nearly 600 deaths on the streets in 2017,[4] many linked to alcohol and drug addiction, each demonstrate – as the repeated hunger marches of the interwar decades did in their different way – the current policy failure here.

LESSON 3: MAXIMISING LABOUR MOBILITY

Institutional and economic conditions that maximise labour mobility and access to new sources of desirable employment for the rising younger generation are crucial. This was true both in the era before 1834 and in the Golden Age when free educational opportunities at secondary and tertiary levels were repeatedly upgraded starting in 1944. At the same time, both geographical and social mobility was supported by a reasonably generous social security system for the mobile young and the immobile elderly, respectively; while housing opportunities for the independent young to build families were affordable across the economy.

4 Deaths of homeless people in England and Wales have increased 24 per cent in five years (ONS 2018a).

LESSON 4: ENDORSING PROGRESSIVE TAXATION

Both due to the 1601 Charitable Uses Act and the **acceptance of steeply progressive taxation rates** for several decades after 1945, in effect the wealthier minority of society found it acceptable **to invest in all of their society's human capital**, not just in that of their own offspring. They were accepting the responsibility in particular to engage in funding health, education and training for the poorer sections of society. This ethos needs to be endorsed once again.

LESSON 5: INCENTIVISING LONG-TERM BEHAVIOURS

The **leaders of enterprise were in both periods incentivised to consider the long-term productivity and prosperity of the productive assets under their management**. In the era of the Old Poor Law, as discussed, landowners and farmers in England engaged in major and often quite risky undertakings, redrawing the fields of their parishes, draining lands and innovating rotation crops, building turnpike roads and later canals and excavating mines. Little of this was a route to rapid returns and much of it required them to pay attention to the co-prosperity of the working families, for whom they could not abdicate responsibility. As Piketty (2014) and others have carefully pointed out, in the Golden Age era, the equivalent class, the captains of industry and corporate executives, were also constrained by the institutional and incentive structure system within which they found themselves. This meant focusing on the long-term prosperity of the businesses they ran, drawing their source of personal esteem and sense of achievement from the whole company's long-term performance and that of its workers, and not so much from their own salary levels because the very high rates of marginal tax rates reduced their interest in such purely personal rewards.

LESSON 6: LOCKING IN REWARDS AND SANCTIONS

A **credible system of rewards, monitoring and sanctions must underpin participation in the collective endeavour**. In the era of the Elizabethan Poor Law, small, close communities meant that contributions to relief were transparent and Justices of the Peace secured compliance. Those making philanthropic contributions were publicly acknowledged in the many civic statues, plaques and other tributes still visible today. After the second world war, the extremely high marginal tax rates for the rich were continued even by several successive Conservative governments (1951–64), as the elite accepted the case for building a welfare state in the new democracy. Electoral support for the educational and health improvements secured by the postwar settlement was judged too strong to row back on. As the economy prospered, a society-wide consensus was maintained until the oil crises ushered in the rise of Thatcherite neoliberalism.

We now turn to a review of the UK's current and emerging economic challenges before presenting a radical new proposal to steer us to a paradigm shift in our approach to growth.

3.
THE CURRENT UK CONTEXT

3.1 OVERVIEW

The challenges we face as we move towards a potential historic decoupling from Europe are many and varied. Indifferent growth coexists with flat-lining productivity among a long tail of businesses; and, despite recent increases, real earnings have barely returned to pre-financial crisis levels.

We now appear to be stuck in a low wage/low productivity equilibrium as we grapple with low levels of skills and what seems to be inadequate diffusion of knowledge, innovation and technology from more productive companies. Where wages are low, incentives to invest in productivity-enhancing technology are weak. It is also possible that employers are now increasing employment as the cheapest and most flexible response to Brexit uncertainty, eschewing potentially riskier but much-needed capital investment.

A hard Brexit could deliver both a sharp initial shock and a reduction in growth against baseline expectations for many years. Unless recent falls in net in-migration of EU workers are reversed or offset by migration from elsewhere then we can expect labour and skill shortages at every level of the labour market, with implications for future growth unless productivity can be kick-started. The impact of potential disruption to our key trading relationships on our trade and balance of payments, already a significant concern, is also extremely uncertain, albeit one that may be mitigated by exchange rate falls that might occur. All of this takes place amid signs of a global slowdown and increased trade tensions among many of our important trading partners.

Persistently high wealth and income inequality sit alongside marked regional inequalities in both per capita income and other key wellbeing measures such as health and life expectancy. Despite record levels of employment, many former industrial areas and declining coastal towns struggle to provide good-quality jobs, while the insecure, low-wage and gig economies thrive. For towns and cities outside London, low productivity is the norm while many individual localities also conceal shockingly high inequalities. For instance, the World Health Organization (WHO) (2008) cites the case of two Glasgow districts eight miles apart whose male life expectancies are, respectively, 82 years (Lenzie North) and 54 years (Calton).

Austerity policies have borne down on welfare provision, reducing entitlements and, since April 2016, removing the annual uprating of working-age benefits in line with inflation. As discussed earlier, poverty, including significant in-work poverty, affects the life chances of nearly one-third of our nation's children; Corlett (2019) predicts that more than half the children of single parents or who live in private or social rented housing will be in poverty by 2023–24.

Long periods of house price inflation running well in excess of earnings growth mean that, increasingly, younger people cannot afford to buy their own home, yet face the exorbitant costs of inadequately controlled rents.[5] This hampers labour

5 While some will inherit from their parents, for most this inheritance comes in the approach to their own retirement, not at an age when it can assist with getting established in work and family life. Before this point, the Bank of Mum and Dad may step in to help those from well-off backgrounds, further increasing intra-generational inequalities.

mobility, especially if it pushes them to remain in or return to their parental home. It may also have less obvious social and ultimately economic impacts if young people then delay or decide against having children.[6]

Meanwhile the economic consequences of globalisation for those communities whose sense of alienation was articulated during the Brexit referendum will potentially be amplified by what is being dubbed the fourth industrial revolution. Artificial intelligence and machine learning may affect both less-skilled work and mid- or even high-level jobs in advice, diagnostics and similar automatable functions. Climate change adaptation will produce further disruption to existing jobs and skills. A wholescale reconfiguration of education and training will be required to meet future needs alongside, potentially, a reassessment of the future of work itself. Handled in the right way, these developments could be turned to benefits, but equally presage untold risks if we fail to secure positive outcomes for all, taking on board the lessons of previous economic transformations.

3.2 HOW DID WE GET TO THIS POINT?

Land, housing and debt-driven consumption

Rent-seeking through housing wealth – 'residential capitalism' – has increasingly led to investment being diverted into non-productive forms of capital and profit, dampening economic growth, producing inefficient capital allocation and driving higher inequality (Ryan-Collins, Lloyd and Macfarlane 2017). Banks are creating credit, money and purchasing power that did not previously exist, which is directed towards increased consumption and asset purchase, primarily land and housing. The resulting inequalities fuel increasing debt as the rich spend less of their income than those on middle or lower incomes. The increased savings of the rich must be offset by increased borrowing by everyone else to sustain overall demand. Hence "rising credit ... become[s] necessary to maintain economic growth" – a destabilising situation that inevitably leads to crisis (Turner 2016).

The UK's debt-fuelled growth and misallocation of investment into these unproductive ends accelerated in the 1980s when the relaxation of regulations governing mortgage lending supercharged house price inflation and rent-seeking behaviour in the ensuing decades.[7] Reversing it will require new approaches to property, land and inheritance tax, allied to tighter regulation of mortgage lending and property acquisition.

Shareholder capitalism

Corporations in the UK are so enthralled to the mantra of shareholder value that someone who has been a shareholder for a matter of days has as many rights as a long-term investor. This has produced institutions dominated by people incentivised almost entirely in the direction of short-term returns (Mayer 2013). This both inhibits long-term investment horizons and opens up vulnerability to hostile takeovers that can destroy jobs, markets and ethics, even in long-established companies – see for instance the fates of Cadbury and GKN Aerospace.

Moreover, the UK is almost unique as an advanced nation in currently lacking a state investment or infrastructure bank (Ryan-Collins, Lloyd and Macfarlane 2017). Yet as Turner (2016) argues, "free financial markets alone ... are not sufficient to ensure adequate support for the investment and innovation that drive forward economic progress: governments have often played important roles." This view is

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6 ONS data (ONS 2017, ONS 2018b) show births per woman have fallen from 1.94 in 2012 to 1.76 in 2017, while the percentage of 20–34-year-olds living with their parents rose from 21 per cent in 1996 to 26 per cent in 2017, increasing from 2.7 million to 3.4 million. Due to long-standing British cultural norms, it is unusual for the younger generation to start a family until they can access their own independent household.

7 The subsequent introduction of Help to Buy, presented as supporting first-time buyers, in fact mostly benefits property developers.

also powerfully argued in Offer 2018 and Mazzucato 2013, which discusses the role of government in shaping a long-term vision through innovation and risk-taking in which the state can, and should, create markets because some markets would not otherwise be created.

Lack of investment

Sitting alongside this destructive short-termism and overdependence on consumption, our economy suffers from woefully inadequate investment by both the public and private sector in productive and exporting capacity. This applies to skills where we lag behind our competitors but also extends to technology and innovation, research and development (R&D), physical infrastructure and support for business start-up and development. Illustrations of the likely impact of this on our productivity can be found in a recent study of Birmingham, which suggests that transport congestion in the city lowers productivity by preventing it capitalising fully on the agglomeration effect of being a large city (Forth 2019), and in work for the Greater Manchester Independent Prosperity Review (2019) showing that agglomeration effects are also stronger where there are higher skill levels.

3.3 UPCOMING CHALLENGES

Climate change adaptation

The environmental challenge we face is profound, encompassing climate change and most natural systems, with the UN secretary general now warning that 'we face a direct existential threat' (Guterres 2018). The risks we face include not just the threat to ourselves and other species but also very immediate large-scale disruption as environmental disasters, including loss of food security, lead to potential conflict or mass migration, with the poorest parts of the world likely to be affected most.

The UK's Climate Change Act of 2008 was an important milestone in signalling government intention to act. However, the UK's climate advisor is now warning that, after some good progress on emission levels, a lack of policies and funding mean that the UK is no longer expected to meet its legally binding decarbonisation targets for the 2020s and 2030s (Laybourn-Langton, Rankin and Baxter 2019).

From a theoretical standpoint, addressing climate change presents both a collective action problem – requiring solutions that incentivise joint behaviour and prevent free-riding – and a deferred benefit problem – in which those taking action may not be the ones who directly benefit (Zenghelis 2016), a point coming into sharper relief as anxious and exasperated young people take to the national and international stage to put the case for their generation's future.

One of the biggest barriers in responding to climate change is that previous technologies have taken economic development on what can be now seen to be a sub-optimal path-dependent route in using fossil fuel-based energy for production and consumption. The (short-term) market incentives remain strongly in favour of carbon-based development as much of our physical energy infrastructure is reliant on it. Indeed, 30 per cent of the market value of the FTSE 100 stock is from oil, gas and mining companies (New Economics Foundation 2017). Undoing these past decisions will be costly, disruptive and potentially destabilising – the Bank of England governor Mark Carney has referred to possible systemic risks (a climate 'Minsky moment') if, for instance, there were to be a too rapid downward repricing of carbon assets in response to action to meet carbon budgets (Carney 2015).

All of this points to the conclusion that responding to climate change must go well beyond market solutions or market-based approaches, with strong government action to break path-dependent inertia (Zenghelis 2016). Long-term financial commitments on uncertain technological development are required, not suited to

market-based investment (although a clear commitment to green technology will crowd-in private investment via the long-term market-creation it signals). With time, new technologies and engineering solutions are likely to deliver energy at lower cost than the fossil fuel-driven economy. For the present, however, investment must include long-term patient capital directed at both research and development and early-stage green technology companies.

As we plan for this, we must mitigate the sorts of transition risks highlighted by the Bank of England governor. Equally we must work with trade unions and others to support workers in the carbon economy who are displaced by technological change so that they can retrain and move into the green economy. This must be explicit from the outset to avoid public backlash.

Ultimately, none of this will be successful unless we also start to change behaviours and incentivise reduced consumption of carbon-intensive goods and services, encourage sustainable travel, reduce domestic carbon consumption and increase sustainable food production. Reduction in carbon emissions requires action to innovate a green economy, but also requires a fundamental change in the drivers of unsustainable behaviour.

Artificial intelligence

Artificial intelligence (AI) and machine learning are set to impact every aspect of work and society, offering huge potential benefits for both business and public services, not least in health and social care. But AI also has the potential to significantly disrupt our economic landscape. Moore's law – that computing power approximately doubles every two years – does not seem to be slowing down so that computers continue to become both cheaper and more powerful. In combination with growing AI sophistication this is eroding human advantage in many production processes, including tasks in the knowledge economy, since human productivity cannot continuously increase at a comparable rate.

We have, of course adapted, albeit often painfully, to previous periods of rapid technological change. It is impossible to predict with any certainty what the future structure of employment might be in a world dominated by ever more-powerful machine learning. What we can do is to think now about the numerous social and economic challenges that the transition to this new economy will present.

A high priority will be to support displaced workers to adapt and retrain, preparing them to develop and deliver the tools needed for AI-enhanced industries or to provide personalised products or personal service roles that will not be ceded to robots. We may also need to debate the extent to which income should continue to be contingent on work, and, not unconnected to this, consider how to ensure that the wealth created by AI does not exclusively flow to its owners. An active state must ensure that technological change occurs for the benefit of society so that everyone is supported to participate productively in the new economy or to undertake other roles that continue to maintain their sense of purpose and self-esteem.

As we think forward to the world of AI, we need also to address the challenges of current monopolistic IT platforms. This includes the specific threat of 'surveillance capitalism' so effectively articulated in Zuboff (2018), in which private experience is translated into behavioural data to be used in computational processes and ultimately monetised. Regulation has not even begun to catch up with the sorts of infringements of privacy and evading of democratic accountability that this entails, nor have we yet thought about how to leverage big data effectively for public benefit.

Population ageing

The forecast rise in the number of people aged over 65, as increased longevity combines with the ageing of the baby boomers, will create huge challenges as people live longer with more extended periods of dependency, with dementia alone now affecting one in five people aged 85 to 89 (Alzheimer's Research UK 2019). Although the increase in life expectancies has recently stalled, projections are still for significant population ageing, with the over-85s the fastest increasing group (likely to have doubled to more than 3 million by 2041). When combined with potential falls in immigration and a below replacement birth rate, dependency ratios will worsen (despite later retirement), meaning more tax must be secured from a declining base. The pressure on public finances will be enormous: reviewing the March 2019 spring statement, IFS director Paul Johnson noted that "we are now perhaps only 20 years from the moment when half of all state spending goes on just health, pensions and social care. It was 30 per cent at the turn of the century" (Johnson 2019).

It is already the case that social care needs are nowhere near being met. One in five working women over the age of 40 now provides informal care (Petrie and Kirkup 2018), and increasing numbers are leaving work because of adult caring responsibilities (Carers UK 2019a). Many mature workers at the peak of their careers may be prevented, as their parents age, from being fully mobile or from continuing in work at all; or less effective when working due to the distraction of unpredictable care needs. This has consequences for productivity if employers are not able to retain these workers and for equity and the gender pay gap since women are most affected by this, as by childcare.

For all these reasons – the impact on our fiscal base and our productive potential – population ageing is leading us to the point where "caring is … rapidly becoming one of the biggest political challenges of the 21st century" (Carers UK 2019b). We need to find a way to provide high-quality and compassionate care, but without diverting vital public spending away from other urgent needs.

4.
IS A HIGH GROWTH TARGET FOR GDP EITHER FEASIBLE OR DESIRABLE?

IPPR has suggested that a trend growth rate of 3.5 per cent might be an aspirational target within a radical new plan, albeit seeking views on its feasibility. In response we would argue that a long-term trend economic and productivity growth rate of 2.5–3.0 per cent would be a more realistic aspiration, and a stretching target to aim for. Since this would match or surpass rates achieved during the postwar Golden Age, we consider it unlikely that this could be bettered in the foreseeable future.

In developing future growth targets, we need also to consider the sort of economy that will help deliver decarbonisation, sustainable growth and social equity. We are concerned that a target that focuses primarily on GDP as currently measured fails to take these crucial issues into account. As a measure of economic success, GDP is a recent invention and its construction has itself been radically revised several times since 1945.[8] We therefore join calls for it to be re-examined, either significantly changing the concept of GDP or at the very least radically changing the way it is measured.

Even on its own terms GDP is not measuring economic and real value and has not done so since its inception – not least in its failure (known from the outset) to reflect non-market and other unpaid activity, much of it performed by women.[9] GDP's inappropriateness as a measure is again resurfacing as the pace of technological change raises questions about the notion of value, which it is supposed to measure. As rapidly upgraded contemporary technological products, such as phones or televisions, see their market utility swiftly devalued, GDP's ability to capture value becomes increasingly time-inconsistent. More pertinent still is the fact that digital technology now means that many things can be reproduced and distributed at almost zero marginal cost, raising the question of how value can be captured at all through standard GDP measures.

At this point, however, rather than trying to fix GDP, we believe that we should be seeking to reconceptualise GDP and growth. It will be impossible to change economic behaviour if we do not have an output measure to reflect what we want to achieve. If the way things are measured dictates behaviour – the "performativity of measures" (Mazzucato 2018) – then we must now seek a measure of 'GDP' that reflects our desired environmental and inclusivity goals, which will be crucial to gaining the political will for sustainable growth. This could, for example, include full cost accounting that deducts environmental damage and resource depletion from GDP.[10] Similarly, we support proposals for a GDP measure that takes account of income distribution.

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8 Alternative measures now include the UN's HDI, and the rankings produced by the United Nations' Sustainable Development Solutions Network (UNSDSN) World Happiness Report. See also Mazzucato (2018) for a fuller discussion.

9 The economic historian Phyllis Deane petitioned Stone, the architect of the measure, to include a valorisation of women's work following her fieldwork in Africa observing both monetised and non-monetised economic activity; arguments that, as we know, fell on deaf ears (Messac 2018).

10 According to Komlos (2015) this would leave current and recent GDP growth close to zero.

We raise the question here of how current concepts and measures of GDP should be revised, but do not answer it in any detail. What we would propose as a matter of urgency is the establishment of a publicly accountable stakeholder-led working group to examine the most appropriate future measures by which to judge sustainable economic growth and productivity and make recommendations as appropriate, with the agreed measures fed into future targets.

5.
OUR RADICAL PLAN TO TRANSFORM UK ECONOMIC PERFORMANCE

5.1 TWO NEW INCENTIVISED SOCIAL CONTRACTS

Our review of Britain's long and successful earlier history as the world's first nation to industrialise argues that we must reconceptualise welfare provision – including both its safety net and its directed investment in human capital – as a growth-promoter.

Relatively high levels of tax and wealth redistribution acted as a direct source of productivity-enhancing growth, both in the period 1600–1834 and again during the three decades after 1945. In both periods the more prosperous were proactive participants and contributors to this while the brake on individual wealth acquisition also helped to avoid the politically destabilising consequences of ever-increasing inequality.

Our vision for transforming UK economic performance seeks, therefore, to reprise the original Elizabethan insight: that altruistic behaviour contributing to wider economic and social goals can be incentivised by the right policy architecture.

We propose two innovative society-wide contracts to achieve this.

1. **A new social contract that raises taxes to invest for sustainable growth, rewarding businesses and higher-rate taxpayers with bi-annually agreed reductions in tax if mutually agreed targets are met.**

Contributions required:

- corporation tax to be restored to 2008 levels (28 per cent)
- new income tax rate of 60 per cent for earnings exceeding 10 times the median.

Payback offered:

- corporation tax reduced by up to 2 percentage points every two years if agreed targets are met
- reductions in pay gaps reduce exposure to the higher rate tax.

Funds used for:

- an intensive programme of investment in decarbonisation, human capital and regional renewal to meet collectively agreed targets
- reversal of cuts to working-age benefits and investment in poverty reduction.

2. **A new intergenerational contract to meet the pressures created by an ageing population by offering universal, unconditional free care provision in old age, funded by large-scale reform of property and inheritance taxation.**

Contributions required:

- new taxes on very high-value properties (and/or total wealth holdings)
- inheritance tax reformed and limited to personal lifetime bequests
- social care levy for better-off retirees
- revaluation of domestic property values to update council tax charges.

Payback offered:

- fully funded National Care Service with a guarantee that care in old age will be free at the point of delivery based on need – the same principles as the NHS; and with an aspiration for the two services to be integrated.

Funds used for:

- a ring-fenced and dedicated social care citizens' wealth fund to secure long-term funding for the new National Care Service.

5.2 TARGETS FOR SUSTAINABLE GROWTH

In the first of these two contracts taxes will rise initially with a promise of conditional tax reductions subsequently. Our aim is to encourage business leaders and others to see themselves as direct stakeholders in the success of the project, proactively investing alongside government, rather than passive contributors to an amorphous tax hike levied on unspecific promises of future improvement.

A very early task, therefore, will be to agree a dashboard of overarching targets with key stakeholders, including government, business, employee representatives and locality-specific bodies. This would clearly need further consultation and discussion through an appropriate institutional structure, but should, we think, include:

- sustainable economic and productivity growth (on new agreed measures) achieving a trend rate of 2.5–3.0 per cent per annum
- targets for reducing overall wealth and income inequality (and potentially supplementary targets by decile, age and gender) along with social mobility as a measure of the effective use of the nation's resources
- reintroduction of urgent targets on child (and overall) poverty reduction, based on both relative income measures and measures of absolute deprivation
- annually rising percentage of the working-age population qualified to at least level 3 and/or retraining to at least level 2 in a current or future high-demand skill
- commitment to achievement of internationally agreed targets for reduction in carbon emissions
- targets for percentage of investment directed to the green economy and targets on renewable energy, sustainable infrastructure and training for 'green collar' jobs
- targets to reduce regional (and potentially subregional) inequalities in GDP, per capita income, skills, employment and unemployment rates and health outcomes.

These targets would then inform the proposed performance-based rewards.

For businesses there will be the potential to earn reductions in corporation tax of up to two percentage points every two years. Any such reductions will apply to all businesses and will be based on independent statistical measures of achievement

against aggregate economy-wide targets, measured on a long-term trend basis. The exact reduction at each point will be calculated by a formula based on rules agreed with all parties about the mix of pro rata achievement of the targets. It also follows that if subsequent regression occurs in the targets then corporation tax rates will have to once again rise, as in any properly incentivised system.

The reward system for top-rate taxpayers is simpler, since their tax liability is pegged to reductions in income inequality. As the gap between median and higher pre-tax earnings reduces, the liability of the latter to higher rates reduces. As with corporation tax, this will build in increases should income inequality rise.

Alongside formal targets and rewards it would be possible to introduce forms of conditionality to encourage action in support of agreed economic priorities. For instance, public procurement might be linked to a business's use of clean technologies and/or commitment to decarbonisation. Or employment taxes such as employers' national insurance contributions might be lowered in relation to specific objectives, such as investment in deprived areas or specific skills upgrading programmes.

In all of this the aim would be to encourage a new 'sustainable stakeholder economics' to flourish in place of environmentally blind 'shareholder value', so that businesses balance the interests of shareholders with employees, customers, suppliers and the natural environment: investing from profits, alongside government investment programmes, to return the economy to high productivity growth.

Ultimately, if businesses believe we are entering a new period of transformational, low-carbon growth, then this should in itself create an impetus to invest to secure the benefits; just as earlier generations of landowners saw that investing in draining lands, building turnpike roads and canals, would be the pathway to future prosperity – both theirs and that of the population for which they took responsibility.

5.3 INTERGENERATIONAL FAIRNESS – A CITIZENS' WEALTH FUND

Our second proposed contract is for a citizens' wealth fund. These funds are state investment vehicles owned by and run in the interests of citizens. A portion of the nation's wealth becomes commonly owned and invested for a return, with the income used to meet a defined goal.[11] This can be conceptualised as a counterweight to the otherwise inexorable forces identified in Piketty (2014), leading to increased private wealth concentrations. Citizens' wealth funds can, by contrast, support greater equality of wealth ownership.

Our specific proposal is for a social care citizens' wealth fund that is supported by an intergenerational transfer of wealth into public ownership. As outlined by Lansley, McCann and Shifferes (2018) in their discussion of the principles of citizens' wealth funds, an initial endowment in the region of £100 billion is necessary to establish any such fund, which they recommend should come from issuing a long-term government bond plus the transfer of some public assets. Again, building on Lansley, McCann and Shifferes (2018), we propose that after its initial endowment, an annual revenue stream of around £50 billion should be paid into the fund from a social care levy on better-off retirees and from radical changes to the taxation of wealth and inheritances.[12]

11 Norway and Alaska have successful oil-financed wealth funds, with the Alaskan fund paying an annual citizens' dividend, while the Australian Futures Fund uses the proceeds from the sale of Telstra to fund disability care and medical research.

12 Lansley, McCann and Shifferes (2018) consider the theoretical case of a social care trust fund as one of three possible models for a citizens' wealth fund. They calculate that, after 10 years, the funding we propose in this essay would deliver an annual revenue of £25–30 billion, potentially rising to around £45 billion after 20 years, and sufficient to cover the bulk of age-related social care costs.

The aim, once the social care citizens' wealth fund is generating sufficient returns (after around 10 years), would be to deliver a guarantee of free, universal care in old age through the proposed new National Care Service. As well as delivering benefits to the older population a key objective will be to reduce the future burden of taxation and unpaid family care support on the younger working-age population.

Obviously while the fund is building to maturity, there will need to be transitional arrangements to address current social care needs, perhaps at least in part making use of the extra funding going to local authorities from the reform of council tax valuations. This will be important to ensure that those contributing to the fund through increased taxation are not disadvantaged at the start of the process, but the transitional arrangements should not be seen as a substitute for the long-term solution.

6.
TAXATION REFORM TO SUPPORT ECONOMIC TRANSFORMATION

Delivering our vision through these new social contracts requires significant new taxation, as we now outline.

6.1 ECONOMIC GROWTH AND PRODUCTIVITY

Once the dashboard of targets has been agreed, a significant tranche of the revenue needed for future investment will be raised, as indicated, by an initial temporary rise in corporation tax, restoring it to the pre-financial crash 2008 level of 28 per cent (which, when introduced, in fact represented a reduction on the previous rate of 30 per cent). As the agreed targets are met, future reductions in corporation tax will be calculated and awarded bi-annually, as outlined above.

To put this in the context of other G20 economies, a corporation tax rate of 28 per cent is below current rates in France (33.3 per cent), Japan (30.86 per cent), Germany (29.79 per cent), marginally above rates in Canada (26.5 per cent) and the Netherlands (25 per cent) and more substantially above rates in two very contrasting economies – the free market US (21 per cent) and Singapore (17 per cent) (Trading Economics 2019), where 90 per cent of land is state-controlled despite its free market reputation (Ryan-Collins, Lloyd and Macfarlane 2017).

As an indication of the impact that this measure could have, HMRC's ready-reckoner for the effects of illustrative tax changes shows that each one-percentage-point increase in corporation tax would raise £3.1 billion if implemented from 2021–22 (HMRC 2019). Increasing corporation tax to 28 per cent from its current level of 19 per cent could therefore raise just under £28 billion a year (£34 billion if current Conservative plans to reduce UK corporation tax to 17 per cent are implemented).

This is not a one-off stimulus – our plan is that this would provide a continuous annual stream of new investment funding with corporation tax gradually reduced as national targets are met and revenue from increased growth secured.

It would also be possible to further bolster the tax take available for national investment funding by ending tax breaks that have little remaining justification, such as higher-rate relief on pension contributions, entrepreneurs' relief and, potentially, national insurance tapering at higher incomes.

6.2 INCOME INEQUALITY

A new income tax band of 60 per cent will be introduced at the point at which earnings exceed 10 times median earnings (with the potential for higher rates at higher multiples such as 20, 30 and 40 times the median). Median full-time weekly earnings of employees were £569 (£29,667 per annum) in April 2018, implying an annual earnings threshold of around £297,000 before this higher rate would apply (ONS 2018c).

Higher earners will therefore be rewarded with lower tax to the extent that measures are taken to increase the earnings of those lower down the income distribution, or to reduce them at the top. Some may seek to characterise this as forcing down the pay of the 'successful', but the scheme can be defended as raising the pay of all employees who contribute to the success of a business or enterprise and therefore more equitably sharing the fruits of such success. The resulting symbolic pressure to move towards a flatter earnings distribution for the very highest earners may also act to compress gender and other pay gaps at this level.

The money raised from this will go towards restoring the cuts to working-age benefits introduced under austerity and to wider poverty reduction and early intervention measures. This will both embed fairness while contributing to reductions in future inequality.

6.3 WEALTH REDISTRIBUTION

To reduce wealth concentrations, notably those stemming from past windfall gains in housing values, significant reforms to property and inheritance tax will be introduced. Approximately £3 trillion of the nation's £4.6 trillion of housing wealth is held by those aged 55 or over and inter- and intragenerational wealth inequalities are becoming increasingly problematic.[13]

The proceeds from these measures (apart from the council tax changes)[14] will, as outlined, be placed in a social care citizens' wealth fund to support care needs in old age. This purpose of and payback from these tax changes will of course need to be clearly articulated and reassurances given over transitional arrangements.

In brief, the new taxes, some of which have also been proposed by other commentators (for instance, Resolution Foundation 2018) will include some, or all, of the following:

- a tax on very high-value properties (such as a mansion or land tax) and/or a tax on total wealth holdings of the super-rich
- at death (or second death where assets were transferred to a spouse) a new variable rate tax on property within the estate similar to current progressive stamp duty thresholds and rates, applied to main properties and second homes
- inheritance tax to become a tax on individuals receiving gifts/bequests above an agreed lifetime threshold, levied at their marginal income tax rate – moving from taxation of the estate to taxation of the recipient should encourage a wider dispersal of inheritance and bring bequests into a fully progressive tax structure
- a revaluation of domestic property values so that wealth changes are reflected in updated council tax bands/charges or, alternatively, a simple percentage tax on actual property value.

6.4 RISK POOLING TO FUND SOCIAL CARE

Evidence from the annual British Social Attitudes Survey (Morgan and Harding 2018) shows that support for raising tax to invest in improved public services is high and increasing. In 2017, 60 per cent agreed with the proposition that government should "increase taxes and spend more on health, education and social benefits", the highest level of support for tax rises since 2002. Among those

13 Calculated from ONS 2018d.

14 The increased revenue from the reform of council tax will be required to support the transitional arrangements as the wealth fund builds up, and to maintain general adult social care before old age.

aged 55–64 support was even higher – 67 per cent – with this age group no doubt mindful of their increasing calls on health and welfare provision as they age.

Building on this we will require people over state pension age with incomes above the basic income tax threshold (£12,500 from April 2019) to pay a 'social care premium'. The amount levied will be aligned to national insurance contribution rates (not currently paid beyond retirement age).[15] This in effect embodies the principle of risk pooling already adopted in many other countries as a rational form of social insurance against open-ended care costs, and, indeed, might be one of the issues that the much-anticipated green paper on the funding of social care could address or propose.

The money raised will be combined with the revenue from increased property and inheritance tax and ring-fenced inside the proposed social care citizens' wealth fund that will support the new National Care Service, with a target annual tax take of £50 billion.

The payback for individuals will be an end, via the care guarantee, to the spectre of the lottery of crippling care costs – the 'dementia taxes' of recent discourse – with their random impact on individuals and families alike, and the intra-familial pressures this may create, including older people spending their final years worrying that their longevity is simply a burden on their family. Moreover, the greatly reduced need to save for uncertain care costs and the knowledge that wealth and inheritance will be more heavily taxed may lead to increased spending and less fetishisation of property ownership as the best form of investment, with potentially quite significant economic and social benefits.

6.5 MORE EQUITABLE HOUSING

To further incentivise progress towards a more equitable distribution of housing wealth, buy-to-let landlords and second home owners will be given a capital gains tax holiday (time-limited to three years) if they sell to either their tenant, a first-time buyer (non-family) or a local council – with councils fully enabled to borrow to fund house purchases.[16] In addition, consideration should be given at the end of this period to taxing all capital gains, including from housing, as ordinary income.

These measures should facilitate a transfer of housing to those seeking a home to live in, rather than those using it as an asset, at the same time supporting councils to rent out properties at a fair rate to those in housing need.[17] It would also counteract the current mass transfer of housing benefit to private landlords, yielding a continuous stream of future savings on one of the key – and rising – components of the welfare bill.

15 This exemption from national insurance is often rationalised by the argument that, once retired, people are receiving the pension benefits for which these contributions were levied. However, social care funding presents a wholly new challenge, requiring a new tax to perform a function not envisaged in the original design of the national insurance system. Our proposal is in any case highly progressive (the basic state pension is below the threshold for paying income tax) so only better-off pensioners – generally those with the highest life expectancies – will pay this levy.

16 The idea of a capital gains tax holiday was proposed by the Resolution Foundation (2018), although only in relation to first-time buyers.

17 To stop this money simply being recycled, future purchases of buy-to-let or second homes will be much more significantly taxed.

7. BUILDING A CONSENSUS IN SUPPORT OF THE PLAN

Radical proposals such as these will have detractors who argue that they cannot be delivered because those affected will work out ways to 'game' the system or will simply take a back seat, acting as 'free riders' on the efforts of others. We tackle these arguments below, in order to show that they are not insuperable objections, prior to the more positive task of discussing how to win hearts and minds to build a constructive consensus in support of the plan.

7.1 GAMING THE TAXES

A principal objection to proposals for significant increases in taxes is that they may be self-defeating by disincentivising people/businesses so that they work less or because they make greater efforts to avoid the taxes. In the case of the UK this may mean that businesses and individuals seek to reduce their exposure to the taxes by, for instance: moving business headquarters elsewhere; secreting money into tax havens; setting up protected trusts; or by simply themselves moving tax jurisdiction to avoid taxes on their personal income and wealth, including future legacies. This is obviously not a new issue, but it may come into sharper focus as a result of the changes that we are proposing.

A body of literature has grown up around the construct known as the Laffer Curve, which shows the theoretical relationship between rates of taxation and resulting levels of government revenue. At the peak of the curve revenues are maximised. This therefore represents the maximum efficient tax rate – the argument being that a tax rate above this level is self-defeating because it leads to an overall reduction in revenue. In practice, however, the revenue maximising rate is contingent on the circumstances of any given economy at any given time, with estimates of its level both greatly contested and varying wildly, even up to rates in the region of 70 per cent. The Mirrlees review of possible UK income tax rises stated that "we do not know with confidence what the revenue-maximising top tax rate is", acknowledging that the positive evidence about the likelihood of disincentive effects occurring if the top income tax rate in the UK were increased is pretty weak and quoting 1980s evidence showing only "a two-thirds chance that the revenue maximising rate was somewhere between 33 per cent and 57 per cent" (Mirrlees et al 2011).[18]

A more recent look at the behavioural responses to potential income tax increases in the UK concluded that "it is unlikely that top taxpayers will work less hard, but it is likely they will try harder to avoid paying tax. This means tougher enforcement will be needed if taxes rise" (Manning 2015). This reinforces earlier arguments that "widening the income tax base – removing reliefs and clamping down on avoidance – not only raises money directly but also reduces the scope for shifting income into tax-free forms and thereby makes tax rate increases more effective revenue-raisers" (IFS 2011). If then, as this suggests, it is the strength of the measures to

18 After the top rate of tax was cut from 50 per cent to 45 per cent in April 2013 in the UK there were claims that it had, perversely, increased the tax take. However, this was later shown to have resulted from distortions as people deferred tax from the earlier to the later year.

prevent avoidance and non-payment of tax that has the most impact on the revenue maximising tax rate, and not some theoretical constant (which would be extremely implausible when one considers the success of countries such as Sweden in raising revenue through high rates) then the task ahead becomes clearer.

A first and obvious response would be to increase HMRC resources to ensure compliance, prevent money being moved offshore and to more actively police 'tax aggressive' avoidance including via general anti-avoidance rules. Compliance measures should also include blocking businesses and individuals taking action in the lead up to the changes being implemented, recognising that increasing HMRC staffing would be more than self-funding in terms of tax revenues protected.

The need to prevent non-compliance applies equally to income tax, corporation tax and the wealth and inheritance tax changes that we propose. In the latter case, this would also need to include action to ensure lifetime transfers of wealth and property were adequately recorded and that avoidance vehicles for inheritance transfers were minimised.

Of course, an even more robust solution would be to introduce mechanisms to frustrate tax avoidance at its core.

- For multinational companies this could include a presumption that companies pay a minimum percentage of UK turnover in corporation tax, rather than the tiny fraction that some, such as Google and Amazon, have been able to pay up until now.[19]
- For individuals we could aspire to follow the US example of taxation of citizens in the same way wherever they and their assets reside, which has been an extremely effective policy in reducing opportunities to game or legally avoid tax.

There is no reason why, in seeking to gain wider support for our proposals, that these sorts of measures, which are already part of public discourse, could not be added to the mix. This might be presented as part of a debate to move opinion in the direction of collective responsibility alongside the pursuit of compliance.

Indeed, many of those businesses and individuals who would be paying higher taxes might well support policies that levelled the playing field in this way. It should not be assumed that everyone would simply seek to avoid being part of a collective effort which in the long run would also benefit them and future generations. What people would expect, however, is that everyone takes part equally with nobody allowed to disengage by not contributing fairly.

7.2 GAMING THE TARGETS

The scope for gaming the targets is likely to be a lot less than that for gaming taxes. Targets will be set and monitored at national level and the tax reductions that can be earned will be determined in relation to those targets and applied uniformly to all businesses and taxpayers. Provided there is effective, independent auditing and rigorous data collection underpinning the measurement of the targets it will be difficult to game this national system.

One area of risk might be in relation to earnings data if, for instance, all businesses were collectively to find ways to understate bonuses or move remuneration into other areas, creating the impression that income inequality had been reduced. Employers or their representative bodies might also be less inclined to offer salary-sacrifice schemes (for instance, in relation to childcare) which passport earnings into benefits, but which may as a consequence reduce

19 This would significantly increase tax take even without an increase in corporation tax and would send a strong signal to those who might otherwise seek to subvert future planned increases.

median pay. Issues of this type have already been identified in relation to gender pay gap reporting and no doubt data collection processes and auditing could be strengthened to mitigate their impact.

Collective targets also present a possible free-rider problem in that individual businesses may decide that they can gain from the efforts of others without themselves making any changes to deliver targets for skills, decarbonisation, and so on. A variant of this problem might be recidivism where earlier improvements are no longer pursued once rewards have been secured. However, as all businesses will be contributing to government investment programmes via increased corporation taxes, any free riding would be on only additional business investment beyond that.

It is also the intention that the establishment of new institutional structures to bring all parties together in a shared sense of collective endeavour to which they have publicly committed would mitigate free-rider problems as a new sense of civic responsibility for investing to improve collective welfare develops. This will be supported by measures to reward such civic behaviour, to which we now turn.

7.3 ETHICAL BUSINESS

The advice from behavioural science is that: "If a policy has a public purpose that would be endorsed by citizens, make sure that the moral message is clear. In advocating a policy, do not assume that self-interest is the only basis of citizen's support." Policymakers need to frame incentives as a collective outcome that all are contributing to, rather than a direct form of self-interest. Otherwise, "the extensive use of incentives may adversely affect the evolution of civic preferences in the long run" (Bowles 2016).

This principle dovetails with our proposal that future earned reductions in either corporation tax or higher-rate income tax would be consequent on the outcome of a collective endeavour directed towards nationally agreed targets and outcomes and that the rewards would also accrue to everyone. To make this even more explicit, we propose that the additional tranche of corporation tax levied above the baseline level at the time of introduction be given a distinct name marking out its purpose such as 'transformation tax'.

In support of this notion of collective endeavour, we propose that the honours system be reformed to give public recognition to those doing most towards meeting national priorities and targets. This would be adjudicated via an ethical register in which all companies report on what specific actions they have taken to help support national targets, what their pay disparities are, and why, and what action has been taken to address them. It would also include information on whether they have employee representatives on their boards and remuneration committees, how they are paying out share options and bonuses to senior executives and other staff, what their tax compliance strategy is, and what their actual tax paid relative to turnover is in the UK.

All those who meet a certain threshold will be accorded ethical business status and will as a result be eligible to be considered for honours, while executives whose business interests do not meet the threshold would not be considered, sending a clear signal on the high valuation attached to collectively beneficial behaviour.

7.4 WINNING HEARTS AND MINDS

Securing much wider public support for our proposal will be critical. This can in the first instance build on evidence from the British Social Attitudes Survey that has consistently shown over many decades that more than 90 per cent of people do not want tax cuts that would reduce spending on education, health and social benefits (an impressive statistic curiously ignored by mainstream media and

politicians). Moreover, the proportion who actually support higher taxation to increase spending on public services (as opposed to just keeping tax constant) has increased from 30 per cent to 60 per cent since 2010 (driven mainly by an increase in support from Conservative voters) and replicating the public level of support for such higher taxation seen throughout the 1990s (Morgan and Harding 2018).

A well-thought-out media strategy will therefore be required to counteract the view – contradicted by the survey evidence – that people resist tax increases and seek only personal gain via tax reductions. This should also challenge the argument that businesses need ever-reducing rates of corporation tax to incentivise their activities – such that the next cut scheduled would place us joint bottom (with Singapore) of the G20 countries for business tax. This is despite other highly successful G20 economies having corporation tax rates nearer the top of the G20 league, and little evidence that there is widespread public pressure for further cuts in the UK.

Given the crucial importance of the older generation to our plan there will also need to be a public debate around intergenerational justice and inequality, building on older people's expressed concerns about the economic pressures that younger people are facing and the increasing demands that they themselves are making on health, welfare and, indeed, family budgets. It will be important to give a clear undertaking that these issues can be addressed through the proposed intergenerational pact, presenting this as a policy that works because it both benefits people in their later years – by removing the risk of being exposed to unlimited future care costs – and because it alleviates future tax pressures and frees up public funds for much-needed investment.

Finally, there needs to be a wider public campaign to develop a narrative of mutual support that fosters inclusive language in place of negative or misleading rhetoric ('scrounger', 'undeserving', 'waster', and so on). This would seek to win over hearts and minds to the value of working together as a society, promoting a vision in which economic transformation and reduced inequality delivers benefits for all citizens and all regions of the country.

8.
ESTABLISHING NEW INSTITUTIONAL STRUCTURES

Essential to the delivery of our plan will be new institutional structures that include:

- a national economic council that brings together government, employer representatives, trade unions and others to agree targets that all parties commit to and which will form the basis for judging and rewarding future performance
- mechanisms such as an investment or infrastructure bank or other vehicles to deliver the investment priorities that have been identified
- new regional, subregional and local governance bodies to direct investment and local delivery and take action to address inequalities
- a new government department or agency to oversee the establishment of the social care citizens' wealth fund under the governance of independent trustees; and to set up the new National Care Service, including future integration with healthcare.

Establishing an effective national economic council or similar that commands respect and authority is fundamental. It will be the driving force behind setting and agreeing targets and securing collective and public commitment to their delivery, including through the ethical register of businesses. It will also have a wider role in working with government and potentially citizens' assemblies to design the investment and poverty reduction programmes that will be funded by the agreed increases in corporation and income inequality taxes.

There is of course a history of mutual cooperation of the sort we propose from earlier periods in our postwar history which will no doubt furnish some insights into the best way to proceed, and there are also various models to draw on from other successful economies such as Germany, France, Japan and elsewhere.

There is already much discussion about potential new regional and local governance models to oversee local economic development and investment priorities and bring a greater sense of local empowerment. For instance, it has been proposed that England should have four 'mezzanine tier' regional economic authorities alongside the devolved administrations, underpinned by combined local authorities in both city and county regions (CEJ 2018). Thinking and practice around models of governance, including the recent moves to establish elected mayors, now also includes a strong emphasis on democratic accountability.[20]

While this debate has some way to go, we support the view that new subnational governance bodies are needed that align with local identities and loyalties. We also concur that they should have a strong democratic underpinning and some genuinely independent and significant revenue-raising and borrowing powers.

As new locality-based bodies develop, it may be possible to use friendly rivalry, perhaps in the form of city or regional league tables, to spur on local investment and performance against the dashboard by government and businesses. This

20 This contrasts with the nine administratively based regional government offices in existence from 1994 to 2011, staffed by civil servants operating as central government in the regions.

has an interesting historical pedigree in the rivalry between provincial industrial cities of the late 19th century, who were often more innovative than the national government at this time, and competed to attract business and investment by initiating public health measures to secure a healthier workforce and more congenial living conditions (Szreter 2005).

Clearly there will need to be consultation about the form that each of the institutions we propose should take along with a detailed articulation of their remits. While crucial to the success of our proposal, the precise nature of the institutions that will be required is a matter for future debate.

9.
ETHICAL ECONOMICS: INVESTING FOR FUTURE WELLBEING

We have outlined a proposal to reform taxation to provide the revenue for large-scale investment in productivity-enhancing and decarbonising growth. By aligning this with financial and civic reward for achieving mutually agreed targets we aim to fundamentally change the behaviour of those holding the levers of economic power.

Governments will also need to take active steps to facilitate changes that support and stimulate renewed growth. The IPPR Commission on Economic Justice (2018) identified many key areas for such intervention, with which we agree. This includes reforms to corporate governance such as the introduction of a duty to promote the long-term success of the company to replace short-term shareholder gratification with investment-led growth; a national investment bank that helps build successful start-up companies into major exporting businesses; and measures to raise wages and strengthen trade unions and workers' bargaining power.

Our vision for taking the economy to the next step is for the proposed new national economic council to agree a comprehensive investment programme which would have three overriding priorities: decarbonisation, workforce transformation and regional renewal.

9.1 INVESTING FOR DECARBONISATION

With economy-wide targets on carbon emissions and environmentally sustainable investment already agreed in our plan, resources for decarbonisation and innovating a green economy would be targeted at whole-scale market creation. Intervention on this scale, taking on the role of the 'entrepreneurial state' (Mazzucato 2013), is necessary to move the economy away from its historic dependence on fossil fuel technology.

It would include:

- public investment in research and development to develop green technologies and support zero-carbon manufacturing, backed up with incentives to support technology adoption
- creation of a zero-emission vehicle infrastructure, rapid adoption of electric car manufacturing, a national charging network, and incentives to aid switching
- significantly increased investment in renewable energy including incentives to scale emerging green energy technologies combined with effective electricity storage
- development of green construction technology for all buildings, both domestic and commercial, including geothermal technology
- large-scale targeted training for the 'green collar' jobs of the future to ensure the right skills are in place and that workers whose jobs are likely to disappear can be redeployed.

Directed taxation can be used to discourage undesirable activity and encourage the adaptation required, using measures such as:

- well-targeted carbon taxes
- windfall taxes on oil and gas company profits
- road congestion taxes
- home subsidies for solar panel installation, home insulation and geothermal heating and support for widespread retrofitting of premises to move towards zero emissions
- green savings accounts offered to the public for investment in greening the economy.

Social media and other campaigns to change behaviour would also have a role, 'nudging' people towards:

- changing eating habits, for instance switching away from red meat, reducing food waste and encouraging locally sourced food purchase
- changing travel habits to reduce single car use, increase vehicle sharing and use of public transport, and encourage more frequent homeworking and staycations
- changing attitudes to clothing and fashion to encourage recycling, rewearing, mending and exchanging, and similar 'circular economy' measures.

Behavioural nudges could also be introduced to encourage changes in business behaviour – for instance a requirement for energy companies to provide an annual statement for investors and customers stating their fuel sources with comparisons to the industry average would be a significant motivator to switch to environmentally friendly energy sources.

As technologies such as virtual reality (VR) interfaces continue to develop there could be scope to leverage them more proactively for environmental benefit. If it were possible to visit an art exhibition, climb the Eiffel tower or play a tennis match with a friend without using physical resources, especially transport resources, then people could participate in leisure activities without increasing their carbon footprint. It might also be very enriching for people with limited resources of time or money or who are older or less physically able.

9.2 INVESTING FOR WORKFORCE TRANSFORMATION

Tackling poverty will be the first requirement for reinvesting in a population that is capable of contributing productively to economic progress, rather than one where people are simply fighting to keep their heads above water, unable to achieve their full potential.

In the light of the shocking findings of the recent report from the UN rapporteur on the impacts of austerity (Alston 2018), which he characterises as overturning key elements of the postwar Beveridge social contract, locking the disabled and millions of children into a cycle of poverty, we must take action to:

- restore adequate welfare payments, remedy past benefit freezes, end the universal credit waiting period and review the way in which benefit sanctions are being used
- address low and insecure pay and hours, a significant contributor to in-work poverty
- tackle housing affordability, poor housing conditions, insecurity of tenancy and rent poverty.

As history has shown, an empowering welfare system is the trigger that supports growth and adaptation to new industry and technology. In a period of significant

economic change, we should again create a climate conducive to innovation where people feel supported and willing to take risks, as was the case during our successful centuries of urbanisation.

The second requirement will be to **address past deficits in education and training** to secure the supply of skills required for transformational growth. A large-scale upskilling programme is needed, supported by both government, business, trade unions and local partners, which must be focused on the industries of the future in order to:

- retrain those displaced by advances in artificial intelligence and other technology
- provide the higher-level skills required for the technologies and industries of the future
- prepare for a shift from carbon intensive industry to the 'green' economy
- raise overall levels of education and skills to a level at least comparable to our competitors.

In order to support this, we propose a policy of 'tertiary education for all': that everyone regardless of age should be entitled to receive full funding to gain qualifications at either level 2 or 3 in a suite of designated skills for the future.[21] This should be introduced as part of a single, lifelong entitlement to up to three years tertiary education or training to be taken up when required, and actively promoted with suitable career and job counselling to those most likely to be affected by upcoming economic changes.[22]

Third, a proactive programme to **invest in the health of the workforce** will be needed to bring as many people as possible into productive work and to ensure that the whole workforce enjoys high levels of both physical and mental wellbeing. Over 70 years after the NHS delivered a transformation in healthcare for ordinary people we are seeing widespread health inequalities linked to poverty and deprivation. This includes the mental health and addiction issues that coexist with high levels of anxiety and insecurity and which are no longer being ameliorated by preventative services such as early years or youth services.

Given the significant social determinants of health inequalities, as demonstrated globally by Sir Michael Marmot (2015), strategies to improve mental and physical health will need to focus on addressing social drivers such as housing, diet and nutrition, education and access to good jobs, as well as preventative health measures around smoking, drinking, and so on. This may be most effectively delivered at local level – the recent establishment of 'Marmot cities' that engage local agencies in holistic programmes to tackle the social causes of health inequalities is a potentially helpful model.[23]

9.3 INVESTING FOR REGIONAL RENEWAL

As Diane Coyle remarks in the Greater Manchester Independent Prosperity Review (2019), 'to increase the UK's national level of productivity will require everywhere to improve. If productivity rises only in London that is no more sustainable than a plane flying on just one engine.'

Regional disparities in the UK persist at very high levels on a whole range of measures including employment, skills, wages, crime, health outcomes and life expectancy, with intra-regional disparities arguably as significant, if not more

21 These are the key intermediate levels below degree level, equivalent to GCSE and A level, respectively, including a range of vocational qualifications mainly delivered through the further education sector.

22 For a fuller exposition see Szreter (2011) and Hutton and Adonis (2018).

23 Marmot cities are inspired by Sir Michael Marmot, a leading expert on the social determinants of health inequalities. They include Stoke, Newcastle, Gateshead, Bristol and Coventry.

so. Since 2010 the central government grant to local government has been cut by almost 60 per cent, leading to reductions in service provision and some poorer households becoming liable for council tax for the first time (Adam, Joyce and Pope 2019). Departure from the EU will, unfortunately, also deprive many areas of access to regeneration funding. Although proposals are now emerging for alternative targeted pots of money, it is questionable whether these will make sufficient difference.

Our proposed dashboard of national targets includes reductions in regional inequalities in growth, per capita income, skills, employment and unemployment rates and health outcomes, as well as other generic inequality targets. We have also proposed strengthened subnational governance bodies with strong democratic leadership. As with late Victorian municipal 'gas and water socialism', we would argue that independent resources and incentives are vital for regional renewal (Hunt 2004).

As well as devolution of funding, we also propose that the large-scale investment funding that our plan generates at the national level should include a presumption that localities of greatest economic need are benefited to the greatest extent possible by new investment and business support.

Investment should therefore be targeted towards geographical areas of need, as follows:

- establishing new green R&D, clean energy and manufacturing facilities (for instance electric cars) that include training academies to enable people in the locality to benefit
- developing new clusters of innovation-based and potentially export-orientated businesses, and funding new science-based universities or other research facilities around them
- identifying areas where improvements in transport and other infrastructure (such as business incubator support) will deliver greatest benefits to the productivity of local economies in order to prioritise investment
- providing hands-on business support for small and medium-sized enterprises to assist the adoption of productivity-raising working practices and if appropriate support with exporting
- promoting and accelerating the take up of new technologies in all businesses, not just those at the technology frontier, in order to raise overall productivity
- identifying where education, skills and health investment will have most impact in reducing inequalities and enhancing workers' productive capacity, targeting resources accordingly.

As this investment begins to raise growth in disadvantaged local areas it should also start to generate beneficial local multiplier effects helping to counteract the effects of cuts in local government spending and employment of recent years.

10. INVESTING FOR FUTURE WELLBEING – EVIDENCE OF IMPACT

In this chapter, we remake the case for investing in our productive capacity, drawing on economic theory, evidence from history and contemporary cross-country analysis.

10.1 REDUCED INEQUALITY BENEFITS GROWTH

Each period in Britain's history in which significant economic progress has been made required a broad consensus across society in favour of productivity-driven growth through resource transfers which were associated with significant reductions in insecurity and inequality. All the historic evidence presented at the start of this essay shows that this directly benefited growth.

There is also contemporary evidence, published by researchers at the International Monetary Fund, that supports the thesis that reducing inequality benefits growth (Ostry, Berg and Tsangarides 2014). Their analysis of cross-country data on growth, inequality and redistribution over a five-year period shows that, "lower ... inequality is robustly correlated with faster and more durable growth" and that efforts to remedy inequality through redistribution do not harm growth except in extreme cases. This, they say, confirms earlier findings showing a "multi-decade cross-country relationship between inequality and the fragility of economic growth". The explanation they offer is that inequality can "undermine progress in health and education, cause investment-reducing ... instability, and undercut the social consensus required to adjust [to] shocks, and thus ... tend to reduce the pace and durability of growth."

Discussing these findings in the *Financial Times*, Martin Wolf (2014) noted that, in Europe, the highly redistributive Scandinavian economies have outperformed their less redistributive peers and that the far more equal east Asian countries, especially Japan and South Korea, vastly outperformed the far less equal countries of Latin America after the second world war. Lower inequality, Wolf argues, increases "the ability of the entire population to participate, on more equal terms", although only so long as "politics is not unduly beholden to wealth". It should be no surprise then that, unlike the US and UK where productivity growth is now falling well behind the OECD average, Denmark, Germany and Sweden, with their long-term focus on investing in their population's productivity and wellbeing, have all maintained or exceeded the average since 2010 (OECD 2019).

10.2 PRODUCTIVITY AND ENDOGENOUS GROWTH

In neoclassical economics, economic growth is driven by external factors, notably (unexplained) technological progress. Endogenous growth theory, by contrast, contends that growth is produced by forces internal to the economy, in particular investment in human capital that leads to innovation and the development of new forms of technology. Within this model, continuous investment in human capital is essential for sustained long-term growth. Periods of high welfare spending – in

its broadest sense of investment in health, education and poverty alleviation – are repaid as enhanced human capital feeds through into higher productivity and moves the economy onto a different, higher-growth path. This is exactly what our analysis has shown was achieved in two significant periods of Britain's history.

But we have also shown that the opposite pertains. When the UK entered its period of most rapid industrial growth after 1830, new welfare policies were imposed that reduced security and saw high mortality and poor physical development in the working classes, as commented on, for example, by Friedrich Engels in the 1840s (Engels 1958). This shift away from material support for the labouring classes conditioned later economic growth such that by 1914 the UK had slipped behind rivals such as the US and Germany. When long-term human capital formation is undermined in this way, the economy is then at risk of moving into negative hysteresis and onto a lower-growth trajectory.

The UK is currently experiencing another such period in which neoliberal policies, which have neglected to foster human capital, may be moving us to a lower-growth path. In particular we are beginning to see in the younger generation what looks like an unwinding of previous skills improvements. A 2012 OECD survey of adult basic skills across 23 major economies concluded that "in most countries, but not in England, younger people have stronger basic skills than the generation of people approaching retirement" (Kuczera, Field and Windisch 2016).

While our oldest workers (aged 55–65) have above-average basic skills according to this study, the opposite is true for those aged 16–24 where we have one of the highest proportions of low-skilled young workers of the advanced economies – well over 25 per cent. The OECD's report puts this down to poor basic education, which, as we saw earlier, suffered dramatic cuts after 1979. Although education spending improved under New Labour, cuts since 2010 have again been severe, particularly in further education. This presents us with a significant challenge in overcoming weak productivity and sustaining our competitiveness into the future.

This is not the only area of concern. We are also witnessing increasing health inequality, a worrying slowdown in improvements in life expectancy and poor health outcomes associated with low pay, poverty and deprivation (Dorling 2018). Poverty affects both mental and physical health as worries over housing, food and insecurity of employment take their toll, adding to the harmful effects on attachment relationships outlined previously, which reproduce over generations. As with skills, the evidence is mounting on the negative impact that poor health and deprivation are currently having on our productivity (RSA 2017).

More insidious problems arise from ever more-constrained housing and the increasing impact of austerity on households, both through direct effects on family welfare but also via its wider impact on family support structures as social care and other support is pared away. Whereas the historic 'Old' Poor Laws originating in the Elizabethan era helped propel labour into the rapidly expanding urban areas, with guarantees of a safety net should it be needed and reassurances that older family members left behind would be supported, a rather different situation prevails in the 21st century. Exorbitant housing costs and the lack of easily available social housing impede mobility as do caring responsibilities for older family members, both potentially impacting long-term growth.

As Kuczera, Field and Windisch (2016) remind us, skills and other human capital deficiencies "reduce productivity and employability, damage citizenship, and are therefore profoundly implicated in challenges of equity and social exclusion". We must now take action to reverse this degradation of our human capital investment and secure the productivity and wellbeing improvements required for renewed, endogenous growth, acknowledging that there will be a time lag before this can be delivered.

The north European nations all seem to have permanently learned the lesson of the policies pioneered in England from 1600 and revived in 1945. To consistently raise the productivity of an entire population requires sustained investment in their intergenerational security, and in their enhanced health, education and training. The whole populace has to buy in to supporting this through a carefully designed institutional structure of incentives to bind in the elites.

11. DELIVERING ON THE LESSONS OF HISTORY

We have offered a proposal to incentivise a new altruistic consensus in favour of increased taxation and investment in long-term sustainable growth. We have also proposed the creation of a social care citizens' wealth fund that draws on our collective wealth to deliver an equitable response to the challenge of population ageing.

Our argument has been that the design of these policies must learn from the lessons of history: identifying, adapting and embedding the features that have been critical to past UK success into a radical contemporary plan. We now return to the six lessons that we set out at the start in order to evaluate our proposals against these historic criteria.

HOW OUR RADICAL PROPOSAL DELIVERS ON THE SIX LESSONS OF HISTORY

A positive value of collective responsibility expressed in a universal social welfare system

The citizens' wealth fund offers universal social care, free at the point of delivery, with collective, pooled responsibility for providing resources to invest in the fund, based on wealth and income.

Guaranteed security for all from primary wants of food and shelter as a matter of national pride

The proposed reform of welfare to reverse previous cuts, alongside action to address low pay and housing poverty, is designed to end the national shame of food banks and homelessness.

Institutional and economic conditions to maximise labour mobility and access to employment

Wealth and housing taxes and measures to disincentivise 'residential capitalism' will improve housing affordability, supporting young people to be mobile. Universal social care in old age will stop care responsibilities impacting on labour supply. Rising investment for all levels of education and guaranteed funding for skills acquisition will promote regionally equitable access to employment.

Acceptance of significantly progressive taxation rates to invest in society's human capital

The threshold for the highest rate of income tax will reflect earnings inequality, with the proceeds directed at reducing poverty, so that fairness is explicit in its design. A public debate will put the case for two new social contracts to promote human capital and long-term sustainable growth.

Leaders of enterprise incentivised to consider long-term productivity and prosperity
New institutional arrangements and an incentivised policy architecture will encourage businesses to work with government and unions to identify targets and agree how best to direct investment towards decarbonisation, investment in human capital and regional renewal in a green economy.

A credible system of rewards and monitoring and sanctions underpinning the collective endeavour
The proposal to raise corporation and higher-rate income tax has at its core a reward system to deliver tax reductions as agreed targets are met. An ethical business register will encourage civic responsibility, tax compliance will be strengthened and opportunities to opt out closed off.

12.
CONCLUDING THOUGHTS

For the sake of both our democracy and our future productivity, we need policies that are founded on an ethical economics, not on 'homo economicus' – the abstract notion of 'rational' economic man operating outside of ethics.[24] The point of our review of history is to demonstrate the practicality of this because there have been two substantial periods in our history when an ethical economics prevailed and in both cases these were the periods when our economy was at its most productive. Each required a broad consensus across society in favour of investment in the population's welfare, which was then able to secure productivity-driven growth.

We have offered a radical proposal to directly incentivise such a consensus to be built once again in our post-crisis, post-austerity, post-Brexit society. The deep investment now required in the welfare and skills of the population, in moving the economy away from dependence on fossil fuel technology, and in reform of housing to avoid the exclusion of a generation from affordable rent or home ownership, cannot be delivered though 'ordinary taxation' with its political cycles and changing priorities. But, if it can be delivered through newly incentivised social and intergenerational contracts built on ethical economics, then our own history tells us the payoff will be transformational.

Crucial to establishing this ethical economics will be political leadership that guides the market towards long-term sustainable growth, ensuring that short-term gains for some are not prioritised over long-term wellbeing for all. Money and financial power must not drive our politics – a polity organised on the basis of 'money votes' will become a plutocracy reflecting the interests of what is in effect an oligarchy of birth. As Piketty (2014) and many others recognise, the unchecked growth and concentration of capital in the hands of the few is an immense threat to democracy. If the unrestrained economic liberalism that permits such wealth concentrations is allowed to undermine political liberalism then it will subvert the possibility of an inclusive prosperity for all, which should be the true prize of democracy.

We are optimistic that we have reached a point in our history where we can make the radical case anew for progressive taxation and redistributive policies which build in paybacks that are clear and fair to all those who contribute. At the opening of the 2012 London Olympics, Danny Boyle gave us a vision of a nation proud of its history, proud of the unique institution of its NHS and of a diverse, inclusive society celebrating and investing in the next generation. We now offer two new altruistic contracts and the incentive architecture to deliver on that positive, optimistic vision.

24 As Sen (1977) argued, the word 'rational' is a value term not a self-evidently ideal behaviour.

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