What should the next UK prime minister do?

Britain faces crises in energy and productivity, both of which have been crushing people's living standards. However, neither is being addressed by the two leadership candidates, Rishi Sunak and Liz Truss. ***Anna Valero*** *and* ***John Van Reenen*** *write that the endemic short-termism of the public and private sectors needs to be reversed, so that barriers to investment can be addressed. For them, the UK is in urgent need of a new economic strategy for stronger, fairer, and sustainable growth.*

Very soon we will know who the next UK prime minister will be. Only the members of the Conservative Party – about four in every thousand voters – will get a say. They are not only few in number, but are far from representative – more male, older, paler.

But even if the vast majority of us have no say in who will be our ruler, we can at least assess what is on offer.

And from the perspective of the big challenges facing the country, the answer is: "not much".

Britain faces a fast-burning energy crisis and a slow-burning productivity crisis. Both have the effect of crushing people's living standards, and neither is being addressed by the two leadership candidates. They have been living in a parallel universe where cutting taxes is the obsession.

The house is on fire….

The most pressing crisis is the extraordinary increase in living costs. This is primarily due to Russia's invasion of Ukraine but is also mixed up with the supply chain disruption from the twin shocks of COVID and Brexit.

Typical energy bills are heading for £3,600 in October and over £5,000 in January. The result will be average winter bills of nearly £500 a month, three times those of last year.

Liz Truss plans to remove green levies from energy bills, and Rishi Sunak wants to scrap VAT on domestic energy. Analysis from the Resolution Foundation shows that each of these proposals – universally applied – would be worth only around £100 for the typical household. Scrapping the recent rise in national insurance, advocated by Liz Truss, would do little to help low-income households, and while Sunak's payments via the benefits system are targeted, these would exclude 40% of households in the bottom fifth. Deeper and more targeted support is needed.

The opposition parties propose freezing everyone's bills, which does get to the core problem of surging prices. But because it's not targeted to those most in need of support, it comes with a whopping price tag of around £36bn this winter and £64bn next year. We do need to keep the price cap lower than planned, but we need to combine this with massive support for the most vulnerable.

And it's not just households. Many otherwise viable businesses will not be able to absorb rising energy costs, battered as they are by supply chain disruptions and volatility over the past two years. So far, no additional support for firms has been announced, though those in the most energy intensive sectors could see further relief. Similarly, no support has been announced for key public sector institutions such as schools and hospitals, already stretched and anticipating a bleak winter ahead.

… and its foundations have been slowly crumbling

The long-burning crisis is the stagnation of productivity and pay. Britain's productivity growth was about five times faster in the three decades before the 2008 global financial crisis than it has been since then. So, it should be no surprise that wages after inflation are lower than they were when Tony Blair left office – the worst pay performance this century. The low growth of the past 15 years and high inequality of the past four decades make the UK a stagnation nation.

So, what is the Liz Truss solution to this? First, cancelling Sunak's planned increase in the main rate of corporation tax from 19% to 25%, despite the evidence that such handouts to big business do little to rekindle investment and growth. Second, reversing the national insurance rise – a giveaway that would see twice the benefit going to the top 5% as the entire bottom half. This would cost over £30bn.

The reality is that taxes will need to rise on those who can best bear to pay them. This means higher "solidarity" income taxes for the better off and higher windfall taxes on energy producers and generators.

More fundamentally, the UK is in urgent need of a new economic strategy for stronger, fairer and sustainable growth. Our long-run productivity problem is pervasive across sectors, and lies in a systemic failure to make adequate investments in productive assets – particularly in skills and innovation. As we highlighted in the LSE Growth Commission, the endemic short-termism of the public and private sectors needs to be reversed, such that barriers to investment can be addressed.

But there are reasons to be optimistic about what is *possible*

Innovation is at the heart of productivity growth and the good news is that we actually know a lot about what policies work. Moreover, there are many underlying strengths that can be built upon. The UK specialises in a number of high value (and knowledge intensive) tradeable sectors. Yes, we are a services exporting superpower, but our enduring strengths in services extend beyond finance, and include business services and the creative industries. Some parts of manufacturing such as pharmaceuticals, beverages and aerospace are also world leading.

Experiences during the pandemic have shown what is possible in a crisis, when the incentives of the key players in policy, industry and society are aligned. The rapid development and deployment of COVID-19 vaccines highlighted the UK's strengths in the bio-medical sector and the key role of research taking place in our world-class universities and broader research system. Many organisations responded quickly to disruption caused by the pandemic by accelerating the adoption of digital technologies and better managerial practices. And government responded quickly to the economic crisis by developing the furlough scheme and other support mechanisms to protect viable businesses and jobs.

The energy crisis only heightens the urgency of decarbonising the economy. Over and above the imperative to meet net zero commitments in response to the climate crisis (where, despite strong UK ambition, there are concerns about delivery), high energy prices show how important increased investment in ever cheaper zero carbon energy and energy efficiency is in terms of national security and ensuring affordability beyond this current time. While other countries have doubled down on improving energy efficiency over the summer months, the British government has been missing in action (and this follows significant policy failure in this area over the past decade). Other countries have also provided advice on energy saving measures which alone cannot solve the crisis but can certainly help reduce costs and waste.

Moreover, harnessing our comparative advantages in "clean" technologies, such as offshore wind, tidal energy and carbon capture usage and storage will generate growth opportunities and good jobs across the country. Strong and coordinated policies are required to make a successful transition and capture associated opportunities, but there are such doubts on the green credentials of both candidates that even the outgoing PM is urging his successor not to "give up on green energy".

Conversations about "doomsters" and "boosters" miss the point. We need to be realistic about the UK's strengths and weaknesses, and how evidence-based policies can help seize and spread opportunities in face of significant change this decade and beyond. We must reject the policy attention deficit disorder that has led to chronic institutional instability, harming investment. Liz Truss's comments risk undermining independent institutions such as the Bank of England, Office of Budget Responsibility and sectoral regulators. This generates policy uncertainty and is as counterproductive as the abolition of our nascent industrial strategy and council in 2021.

Britain needs a robust growth (and broader economic) strategy and a home-grown Marshall Plan to re-build the economic foundations of our shared home. As optimists, we can see that such a strategy is *possible*. Sadly, observing the state of this leadership contest, the prospects of a realistic growth strategy appear dim, for now.

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