KING'S College LONDON

Towards a culture of exporting

How to help UK exporters do more and do better

BARCLAYS

The Policy Institute at King's

Towards a culture of exporting

How to help UK exporters do more and do better

The decision to leave the European Union (EU) has renewed scrutiny and interest in the UK's export performance. While the nature of the UK's post-Brexit trading arrangements with the EU are yet to be decided, it is likely that the shape of the UK's exporting footprint will evolve as the nature of our relationship with our closest neighbours changes.

The percentage of UK exports that go to the EU has been declining in recent years, a trend that may be accelerated by reduced access to the EU member states. However, Brexit may also be an opportunity to take a more strategic view of how we can maximise the longer-term trend towards exporting to the rest of the world, particularly to fast-growing economies like China, Indonesia and Brazil.

The belief that the UK underperforms in global markets predates current debates. On the face of it, the UK is not at crisis point: the UK is the 10th largest exporter of goods in the world and the second largest exporter of services. However, the underlying trends are less positive. The UK's share of global exports is contracting, and most indicators show that this is happening at a faster rate than in other advanced economies.

Clearly, the UK needs to reinvigorate its exporting strategy. But how can the UK Government foster a trade and wider industrial environment that can significantly increase UK exports and deliver sustained wider economic benefits? As part of our programme of work on the UK's economic performance, the Policy Institute at King's partnered with Barclays to run an interactive, day-long intensive 'policy lab' focusing on this issue. Our policy lab brought together stakeholders from policy, industry, government and academia to develop creative thinking and novel policy solutions from the best available evidence.

The lab, in combination with our own research, generated seven broad recommendations for policymakers and industry on developing an effective export strategy in support of UK businesses. These recommendations cover the short, medium and long term with the intention of delivering meaningful and lasting impact and change.

These recommendations are focused mainly on what government can do, but it is also important to look at ways in which businesses themselves can take action independently of government. We will look more closely at this in the next phase of the research. Our recommendations do however highlight where businesses, and the bodies representing them, can better engage with government to shape the support and resources available to exporters and would-be exporters.

The short term

Value over volume

Recommendation 1: The value of exports is more important than the volume of exports. The Government needs to work with large firms that already export to enable and incentivise them to diversify their export activities, which is likely to also benefit smaller firms via their supply chains

Few firms in the UK sell overseas. An important assumption of policy making in this area has been that the key to improving export performance is to increase the proportion of UK firms which participate in trade. The difficulty is that the number of non-exporting businesses that might be suitable candidates for exporting is highly uncertain. In

the short term, therefore, it is important to consider how to maximise export performance amongst existing exporters.

Rather than just encouraging current exporters to sell more of their existing products in their existing export markets, though, an emphasis on diversification seems to be important to manage the risks of export intensification. In short, the UK needs more 'superstar exporters' – firms selling 10 or more products in 10 or more markets. These firms are likely to prove more efficient and sustainable contributors to the UK trade balance. Crucially, they can also provide routes to market for smaller businesses through deep supply chains.

Businesses need to work with government to communicate what support they might need to achieve this. Tax incentives, for example, may be one way of encouraging export intensification by large firms. Enhanced research and development tax credits are permissible under World Trade Organization rules and could help to encourage innovation activity necessary for large firms to diversify their range of products for export. Actions to protect the supply chains of big exporters, both in the Brexit transition phase and beyond, are also vital in ensuring their capacity to export.

Recommendation 2: The Government needs not only to protect but to strengthen trade relations with the US and EU

Countries trade more when the costs of trade are lower (widely termed the 'gravity model'). This means that more trade is more likely with partners who are geographically closer and economically larger. There is emergent evidence that social, cultural, legal and regulatory similarities are also associated with lower trade costs and therefore greater trade, and it is possible that these factors could be more important for trade in services than in goods. This could have potentially important implications for the UK given its reliance on services exports. The gravity model appears to hold strongly in the case of the UK; the EU and US represent by far our largest trading partners.

There is a need to look more at the influence of cultural proximity on trade patterns. The US, for example, is by some margin the single largest market for UK services exports, despite its geographical distance and the absence of a trade deal covering this area. This may be due to similarities in legal and regulatory structures and in consumer preferences relating to financial and professional services.

Additionally, the UK's position as an entry point into the European Single Market accounts for some of our attractiveness as a trade partner with non-EU countries, including the US. If economic performance is to be sustained, and ultimately improved, the Government must maintain and strengthen access to these markets, most obviously through the Brexit negotiations.

The medium term

Value and volume: growing the number of UK exporters

Recommendation 3: The huge economic potential of 'exportable' businesses needs to be leveraged. Government, business and business support organisations need to work together to achieve this

There are opportunities to draw new firms into exporting, but doing so at scale is a more challenging proposition than increasing exports from existing exporters. The term 'exportable businesses' describes firms which do not export, but share many of the characteristics of successful exporters (for example in terms of size, productivity and the sector they operate in). As these businesses are hard to identify among the population of non-exporters, local bodies and the private sector, including trade associations, regional chambers of commerce and local enterprise partnerships, may be better placed to reach them than central government.

These organisations can help to encourage exporting by connecting potential exporters with firms that already export, sharing exporting best practice and providing accessible, targeted exporting advice and market information. It is vital that businesses communicate the assistance from central government or business support organisations that would be most useful to them, and how it could most effectively be delivered.

Trusted business advisors such as accountants and bank managers could also help to identify suitable firms and nudge them into exporting if provided with some basic information on what an exportable business looks like. There is also a role here for research organisations to develop more sophisticated and accurate methods for identifying these businesses.

Recommendation 4: Government needs to work with medium-sized firms to leverage their export potential

Medium-sized businesses (typically defined as having between 50 and 249 employees) are more likely to have the characteristics of successful exporters, for example in terms of their sector, size, productivity level and investments in research and development. The success of the German 'Mittelstand', for instance, is an example of a medium-sized business population that is competitive in global markets.

Greater support for these businesses to begin or expand exporting could be achieved via many of the routes outlined under Recommendation 3; a decentralised approach involving support and advice from local and sectoral bodies, fellow businesses and trusted business advisors. Once again, business needs to be closely involved in shaping the support

offered by these bodies to ensure that it is useful and accessible. It also requires more targeted data and analysis on firms of this size, which are frequently grouped with small businesses in the small and medium-sized enterprise (SME) category. Anecdotally, the inflection point in business complexity often seems to occur at around £5-10 million turnover, suggesting that the SME definition is unhelpful in describing the needs of mid-sized businesses, though further research would be helpful here.

Recommendation 5: Greater demand will be driven by a refreshed, reinvigorated campaign to promote UK exports that emphasises quality, innovation and creativity in UK products and services

Goods and services produced in the UK have a reputation for quality, innovation and creativity, particularly in emerging markets. While it is difficult for UK firms to compete on price with emerging market firms given their higher cost bases, they may be able to leverage these product features to build demand for higher margin UK exports.

Interventions that could help to strengthen the UK brand and its global recognition include hosting trade shows, organising trade missions and other showcasing techniques that emphasise these valued product characteristics. There may also be clearer or more accessible ways of articulating the Government's existing support in this area to businesses that already export or are considering it. Better supporting businesses to utilise aspects of the UK brand in promoting their own products could also be feasible and valuable.

The long term

Building a culture of exporting

Recommendation 6: Developing the fundamentals of the UK economy is likely to provide a significant boost to exporting over the longer term

Better firms are more likely to export and export more. The best evidence on the drivers of exporting points to the importance of firm-level characteristics: size, ownership, productivity, research and development and the application of human and physical capital.

In the longer term, policy that develops these fundamentals in the UK economy, specifically helping firms to grow and become more productive, can help to substantially boost exporting and bolster overall economic performance. Manufacturing firms also have a particularly high propensity to export. Supporting the growth of manufacturing industries, especially high-tech manufacturing – where there is some evidence of a comparative advantage for the UK – would therefore also be valuable.

Recommendation 7: Targeted, non-formal trade agreements can be used alongside more formal negotiations to unlock barriers faced by specific sectors

Non-tariff barriers (such as differing regulatory structures and standards) continue to suppress trade. This is particularly true in services like banking, where there is typically a requirement for the firm exporting services to be subject to local supervision, or else meet significantly higher standards than domestic firms. Host nations have greater freedom under global trade rules to set standards unilaterally to protect their economies and society.

While formal trade negotiations to reduce these barriers are essential, they typically take years to complete. In the meantime, there may be opportunities for less formal agreements to increase market access. This might involve regulatory agencies in the UK and the partner country agreeing non-binding mechanisms to increase harmonisation. The US 'TIFAs' (Trade and Investment Framework Agreements) may provide a blueprint for this approach. There are also promising examples from the UK that could be built on – for example, the UK China Economic and Financial Dialogue. This recently addressed aspects of the UK-China financial services relationship and agreed several areas for cooperation. These negotiations should prioritise barriers in sectors in which the UK has a clear comparative advantage, such as business and financial services.

Sector bodies would again be best-placed to identify these barriers and communicate them to government. This necessitates a strong set of well-resourced industry or sector bodies that are representative of UK employers. Some sector organisations may already be well-placed to take on this role, while others may need support to increase their membership and develop their policy functions. Suggestions for how to do this range from making membership of a trade body mandatory to providing stronger incentives for firms to join by improving the way that government engages with these organisations. There is also a clear need for further research here.