UK: spending to address COVID-19 and Brexit should fit with productivity, social and environmental goals

14/10/2020 – The United Kingdom faces major challenges from the COVID-19 crisis and leaving the EU Single Market. Ramping up investment in the digital economy, the service sector, green infrastructure and adult skills would strengthen the recovery and help to boost productivity and environmental sustainability for the long term, according to a new OECD report.

The latest OECD Economic Survey of the United Kingdom underlines the importance of the emergency support measures put in place to address the coronavirus crisis, but also stresses the need to address longer-term challenges. Active labour market spending for displaced and low-skilled workers should be increased to help workers in sectors with uncertain futures move into quality jobs, and infrastructure spending should focus on the most deprived regions. Low interest rates mean there is room for more stimulus, if needed. Public investment should build on existing efforts to revive productivity growth and transition to a low-carbon economy.

"The combination of COVID-19 and the exit from the EU Single Market makes the UK outlook exceptionally uncertain. Actions taken to address the pandemic and decisions made on future trading relationships will have a lasting impact on the UK's economic trajectory for years to come, so they should be in line with long-term objectives," said **OECD Chief Economist Laurence Boone**. "Productivity growth in service sectors will have to accelerate significantly for the recovery to be long-lasting and sustainable."

The coronavirus crisis erupted against a background of subdued growth, stagnant productivity and flat investment in the United Kingdom and triggered one of the most severe falls in output of OECD countries, reflecting the economy's deep integration in the world economy and the fact that the hard-hit service sector makes up around 80% of UK output and employment.

While a rapid and massive emergency response has helped to steady the economy, the United Kingdom still faces a prolonged period of disruption to economic activity, which risks exacerbating pre-existing inequalities and regional disparities. Most households have reported a drop in income since the crisis. Economic activity will only recover gradually, with several years of high unemployment likely due to business closures and delayed investment. The Survey, assuming a smooth transition to an EU Free Trade Agreement, projects an unprecedented fall in GDP in 2020 of 10.1%, with activity still below its pre-crisis level by the end of 2021. The unemployment rate is projected to be 7.1% in 2021, up from 3.8% in 2019.

Leaving the EU Single Market at the end of year will require firms to adapt.

Avoiding a “no deal” outcome would benefit both the United Kingdom and the European Union. Were there to be an EU exit with no free trade deal, the government should be ready to provide targeted support for affected firms and workers and put in place trade facilitation measures to smooth disruptions at the border.

While the increase in barriers to trade resulting from any form of exit from the EU Single Market will lower growth over the medium term, a disorderly exit would be more costly and disruptive. Managing a disorderly exit would be complicated by the fact that firms have diverted their attention to dealing with COVID-19, and those with reduced earnings will be less able to invest in new systems, staff and training.

The UK’s Industrial Strategy should help to revive productivity growth – which is key to sustaining jobs and wage growth – yet more could still be done to encourage innovation and reduce gaps in adopting new technology between leading firms and laggards. Overall public investment has been lower than in other leading economies in recent years, and investment in digital infrastructure still lags investment in transport, energy and utilities. These are all areas where the UK lags the best-performing OECD countries and which are likely to bring high productivity gains. Planned spending to improve digital skills could also be more ambitious, as the COVID-19 crisis makes the low level of adult training in the United Kingdom a more urgent concern.

See an Overview of the UK Survey with key findings and charts (this link can be included in media articles).

For further information, journalists are invited to contact Catherine Bremer in the OECD Media Office (+33 1 45 24 97 00).