REC Recruitment & Employment Confederation

July 2022

Overcoming shortages

How to create a sustainable labour market

CBI Economics

Contents

Foreword

Over the past two years, labour shortages have become front page news. HGV driver shortages resulting in long queues at petrol station forecourts; a lack of fruit pickers and butchers leaving produce and livestock in the fields; NHS workers overburdened and burning out during a global pandemic and air travel disrupted.

In the recruitment sector, these are issues that many of us saw coming.

At the REC, we have been talking about the issues the British labour market faces for many years. And as we have seen over recent months, they have the potential to significantly damage the UK economy, our ability to invest and grow in the future.

The critical thing here is that while the pandemic has thrown the situation into sharp relief by causing a moment of crisis – the underlying issue has been with us for years. A smaller labour force as "baby boomers" retire, the inefficiencies in our skills system, years of sub-optimal performance in business investment, deployment of technology and productivity, were always going to make the 2020s a challenging decade.

Much of this challenge lies with us in business to address – but we also need an environment that helps us make the changes we need, working with partners in colleges, local areas and government. In an environment where only growth can ensure we are able to both fund public services and maintain competitive tax rates, this is an area for urgent action.

In this report, we show exactly how much damage could be done if we don't step up. With a 10% surge in demand for staff across the economy, and the labour market restricted by shortages, we could see a 1.2% fall in expected GDP and productivity by 2027 – costing the economy anywhere between £30 billion and £39 billion every year. This figure is just short of the entire current defence budget, or two whole Elizabeth Lines.

This report is about finding solutions, not complaining. We turned to businesses across the UK for their views, as well as looking to Canada and Germany for things we could learn. In truth though, the biggest step is the most obvious one – both

We need to put the "people stuff" first

businesses and governments need to change behaviour and put people planning at the top of their list, not dealing with it as a cost to be minimised.

Many businesses talk about staff as their most important asset and the thing that drives their success. That means raising workforce planning up the agenda at C-suite level, ensuring your skills pipeline is getting you the people you need, participating in local and sector planning, and hiring people with a long-term view, rather than dealing with hiring as a procurement function. In 2022, REC members across the country have been advising firms on this.

For government, a proper labour market strategy is vital. Skills is part of that, but not the only part – immigration, devolution and labour market activation all matter. From buses and childcare infrastructure to apprenticeships – the entire business environment influences the investment decisions that firms make. It's vital some unity of thinking is brought to this across the government.

To create a sustainable labour market and stoke economic growth we need to put the "people stuff" first.

Neil Carberry
Chief Executive, REC

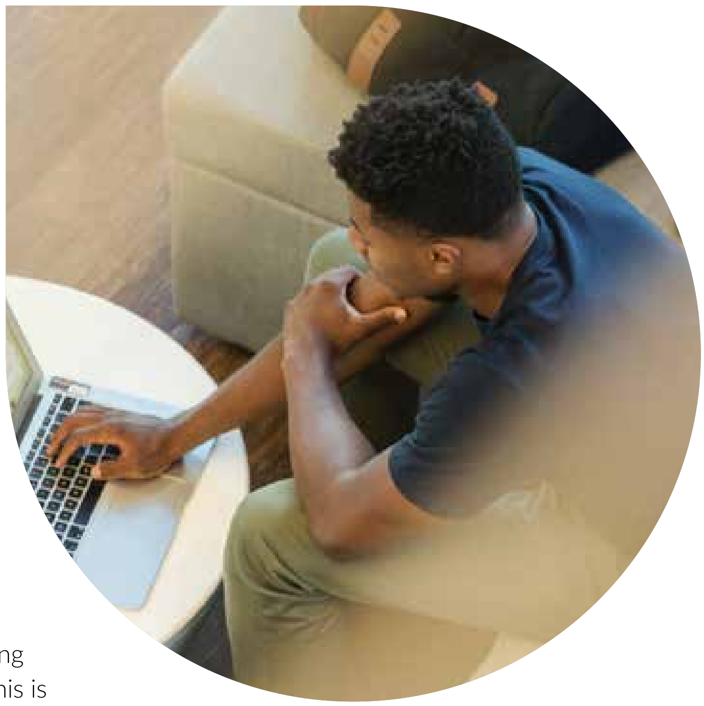
Executive summary

There is structural change in the labour market like we haven't seen in generations. This report examines what is happening and the challenges that need grasping. Growth is the only way to achieve low taxes and good levels of public spending but for that you need a fully enabled jobs market. We do not have that yet.

The UK's labour market is under pressure from worker shortages like never before. There is huge demand for workers and people are making choices about when and how they engage in work with a power they haven't had until now. For example there is growing inactivity with older workers leaving the workplace sooner and younger people staying in education. It is more important than ever that inefficiencies and shortages in the labour market are addressed, to provide a strong platform for growth and prosperity.

The research in this report was carried out by CBI Economics, to demonstrate:

- The economic impact of labour and skills shortages in the UK;
- How the UK labour market and government labour market policies compare to other G7 countries who also face labour market shortages;
- The difficulties UK businesses face when hiring, and what businesses, government and other stakeholders can do to build a longer-term view for skills.



Labour and skills shortages have been a concern in particular sectors for a number of years. However, the situation in the UK has never been this bad. Data from the REC and the Office for National Statistics (ONS) documents record-breaking shortages of workers across all sectors. This is not sustainable if the UK economy is to grow at the rate government and businesses aim for. This report provides further evidence of the need to take radical action to address labour and skills shortages. Otherwise, we risk losing the battle for long-term sustainable economic growth powered by a healthy and well-equipped labour market. The policy solutions outlined by the REC have been shaped by the evidence collected in this report. They will ensure a robust and futureproof supply of skilled people from the UK and abroad.

As part of the analysis, a literature review, economic modelling analysis, international benchmarking and interviews with businesses were carried out, highlighting the following key takeaways:

The economic impact of labour and skills shortages

- Existing theoretical and empirical literature highlights the **negative effect shortages have on productivity, inflation and investment.** These are all real-time issues affecting the UK. There is also a clear link between the need to address labour and skills shortages and addressing **regional inequalities.**
- Modelling analysis demonstrates that **any attempts to boost demand as a means to speed up recovery whilst there are labour shortages that cannot be filled will likely impact the economy negatively in the medium term.** For example, a temporary and hypothetical 10% increase in demand in the economy would need to be accommodated by 1.7 million new jobs. Without this employment increase, real UK GDP would fall by between £30 billion and £39 billion every year from 2024 through to the end of 2027, equivalent to 1.2% to 1.6% of GDP, or the size of the UK recruitment sector in 2019. [1]
- Modelling also shows that a demand boost in the face of shortages leads to higher earnings and inflation, and an overall **fall in real disposable income,** which in turn means **restricted growth in public sector receipts.**

10%
increase in demand in the economy would require
1.7 million
new jobs

What can be done by businesses, government and other stakeholders

- International benchmarking analysis highlights that, in Canada, businesses are **proactively working with educational institutes** as well as **investing heavily in technology and automation** to alleviate the impacts. The Canadian government meanwhile has identified the key sectors afflicted by skills shortages, and is **actively seeking to attract migrants** to these areas, as well as committing to these sectors **funding for training and apprenticeships.**
- In Germany, there has been **extensive collaboration across a large number of public sector agencies** in implementing labour market policies to alleviate the most pressing issues: boosting the low participation rate (the number of people working or actively seeking work), and shortages in skilled and vocational workers.

Without these new jobs, UK GDP would fall by between
£30 & £39 billion
a year

- Interviews with UK businesses highlighted the **importance of collaboration between various stakeholders to ensure a longer-term and more proactive view for skills planning,** including between industry, government, the education sector, and recruiters.
- The interviews also raised the **importance of government policy as a lever to address issues**, and in particular the need for **reform of the apprenticeship levy** and **changes to immigration policy**, to help fill shortages responsibly.

Taken together, these findings show the significant economic impact of labour and skills shortages in the UK and highlight the need for government to act urgently through various policy levers to deal with the current staffing crisis. The policy recommendations outlined by the REC are designed to ensure a longer-term and proactive approach to skills planning and should serve as a guide to creating a sustainable labour market.

In light of this analysis, the REC recommends the creation of a **future workforce strategy,** outlining the skills that the UK economy will need over the coming years. This means putting in place policies for skills, immigration, regional investment and labour market activation. Businesses must also play their part by **pushing workforce planning up the agenda at leadership and board level.** Engaging in workforce planning in partnership with various stakeholders including educational institutions, government and recruiters can ensure businesses have the workers they need to grow and deal with changes in technology and commitments to reach net zero.

1. Introduction

Background and context

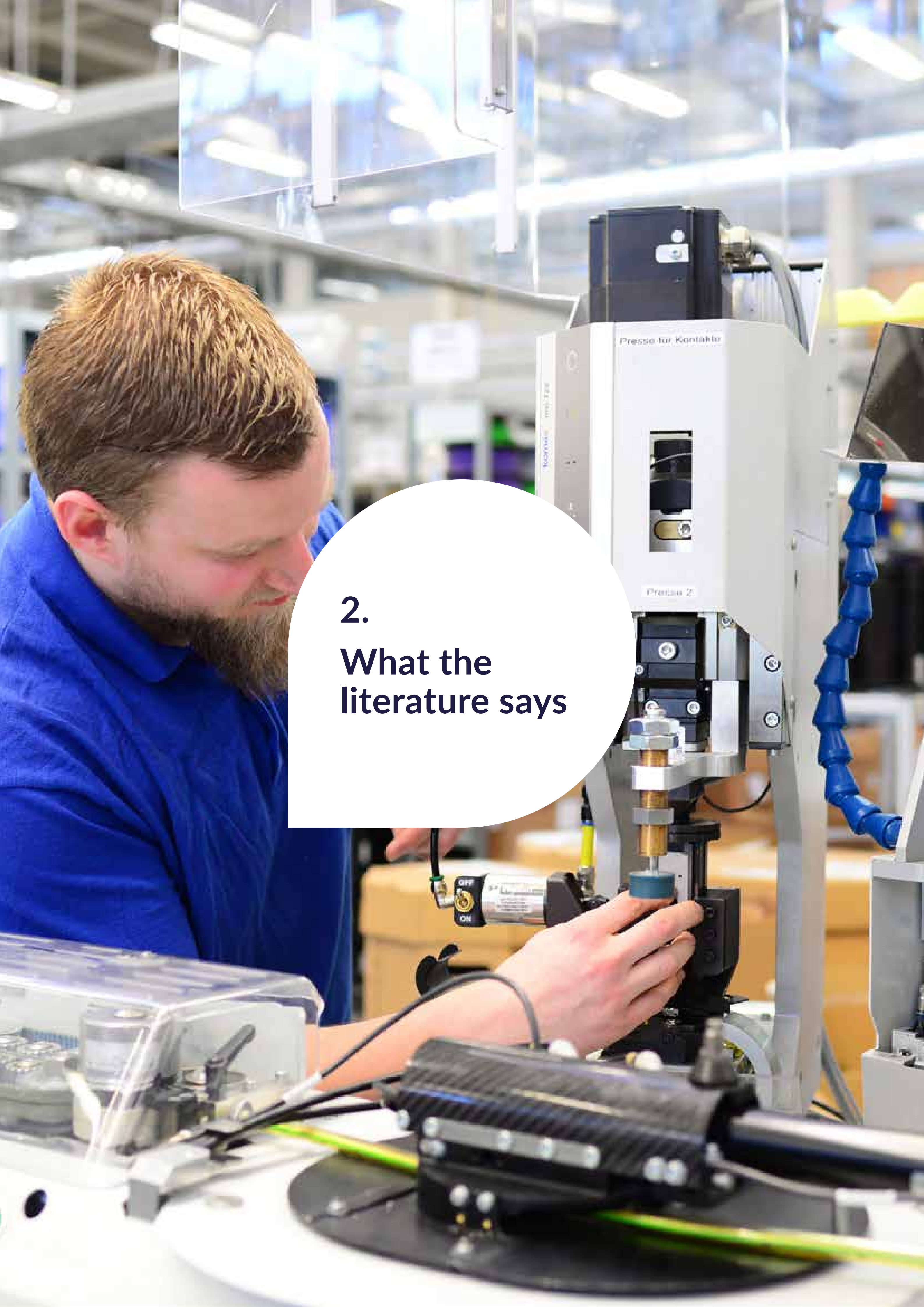
The Recruitment & Employment Confederation (REC) is at the centre of formulating effective labour market policy. This research in the report was carried out by CBI Economics, to demonstrate:

- The economic impact of labour and skills shortages in the UK;
- How the UK labour market and government policies compare to other G7 countries who also face labour market shortages, and what we can learn from the approaches taken by other nations;
- The difficulties UK businesses face when hiring, and;
- What businesses, government and other stakeholders can do to ensure a longer term view for skills.

Methodology

This research presents:

1. A literature review of the economic impact of labour and skills shortages, including evidence from both theoretical and empirical research. This review highlights the key channels through which labour and skills shortages affect the economy.
2. Economic modelling analysis to understand the economic and fiscal impacts of labour market constraints in the context of a not inconceivable temporary 10% increase in demand in the economy.
3. International benchmarking analysis to demonstrate how the UK performs relative to comparable countries in terms of labour market problems and government policies to address labour and skills shortages.
4. Interviews with UK businesses explaining their experience of labour market challenges and what more can be done by businesses, government and other stakeholders to ensure a longer-term view for skills.



2.

What the literature says

The literature review considered a variety of resources including research reports, policy papers, articles, and survey-based reports. Academic and empirical literature into the impact channels of labour and skills shortages identifies reduced productivity, increased costs to businesses, and fewer investment incentives as key channels of impact.

Shortages can have a negative impact on productivity

Labour and skills shortages can have a negative impact on productivity through multiple channels. This includes the fact that vacancies remain open longer which increases the hiring cost per skilled worker[2].

One study found that the increase in skilled labour shortages in the UK over the 1980s reduced productivity growth by around 0.7% per year[3]. Similarly, surveys of high-tech firms in Northern Ireland found a negative effect from unfilled vacancies on the output per worker, reducing productivity levels to 65%-75% in affected firms[4].

Growing skilled labour shortages in the 1980s reduced productivity growth by

0.7%

per year

Further research showed that small and medium-sized manufacturing businesses in Canada felt that shortages have affected their ability to compete and be productive[5].

In addition, businesses have cited a tight labour market as affecting employee turnover, highlighting poor productivity after workers leave a business and the higher levels of training required to hire new workers[6].

Shortages can cause wage pressures and increased inflation

Labour and skills shortages can put workers in a stronger bargaining position, which can have a number of impacts including allowing employees to negotiate higher wages. To some extent, the increase in wages depends on the willingness of employers to concede, but this is significantly affected by the presence of labour and skills shortages[7]. As a result, these impacts can flow into the macroeconomy as increased wages lead to rising inflationary pressures – a phenomenon known as "wage-push inflation"[8]. Higher costs of production can also lead to firms passing costs onto consumers through higher prices[9].

Empirical evidence has been consistent with economic theory that labour and skills shortages increase pressures on wages and inflation. For example, one study on the UK labour market found that labour and skills shortages increased the growth of real wages and decreased unemployment[10]. Both of which suggest inflationary pressures.

Anecdotes and surveys from the CBI's membership body over the past year highlight increased labour costs on account of labour and skills shortages that often have to be passed onto consumers.
The REC's Report on Jobs highlights this further as in late 2021, permanent starters' salaries within the survey rose at the quickest pace since the survey began in 1997[11].

Labour and skills shortages dampen investment demand

In addition to inflation, another macroeconomic impact from labour and skills shortages is lower investment. Shortages may inhibit investment and the implementation of new technologies[12].

The European Investment Bank Investment Survey (EIBIS) found that, on average, 77% of firms report the limited availability of skills as a barrier to investment[13]. It was also the most frequently-named barrier to investment in a list of nine obstacles[14]. This was an extensive survey of approximately 12,000 firms across the EU, 600 in the UK, and 800 in the USA, designed to provide information on skills and investment-related aspects. The survey highlighted that, in order to boost business investment in the UK, labour and skills shortages must be addressed.

77%

of firms say skills shortages are a barrier to investment

The mismatch in labour supply and demand needs to be addressed to level up.

Empirical research has also investigated regional inequalities due to labour and skills shortages. Data from 13,000 firms across 40 regions in the UK found negative spillover effects of skill gaps in related industries and nearby regions. Interestingly, these negative effects were stronger in knowledge-intensive industries such as financial and insurance activities, as skills gaps also link to a loss of learning effects[15]. As a result, the government's levelling up agenda, its Plan for Growth, and also the transition to net zero – which will redistribute economic activity across the UK – will all require skills development in order to be effective[16 17].

Previous research into the North of Tyne Combined Authority (NTCA) uncovered long-term labour market challenges in the NTCA[18]. The research included business interviews and uncovered a range of labour market challenges facing businesses in the NTCA region, some cross-sectoral, and others sector-specific. These labour market challenges include a high churn of employees (particularly amongst more junior employees); a need to offer increased wages to attract and retain workers; more older workers retiring; and a lack of essential skills in younger workers (especially softer and vocational skills).

Impacts of the lack of digital training

Research shows that five million workers could become acutely under-skilled in basic digital skills by 2030, with up to two-thirds of the workforce facing some level of under-skilling[19]. This has wider implications, including undermining the transition to net zero. A survey found that only 15% of IT professionals believe the UK workforce has the digital skills to achieve net zero[20].

Other evidence shows that within the UK, data-driven skills shortages alone are already costing £2bn a year to the economy[21]. Additionally, wider digital skills shortages amongst SMEs are creating an £85bn productivity gap in the UK[22].

Other areas of skills shortages show that over two million workers are likely to be acutely under-skilled in at least one core management skill, including leadership, decision-making or advanced communication[23]. These findings are corroborated by evidence from the CBI's 2021 Education and Skills Survey as well as the Department for Education (DfE) 2019 Education and Skills Survey[24 25].

3. Economic and fiscal impacts

A challenging context for the UK economy – baseline projections to 2027

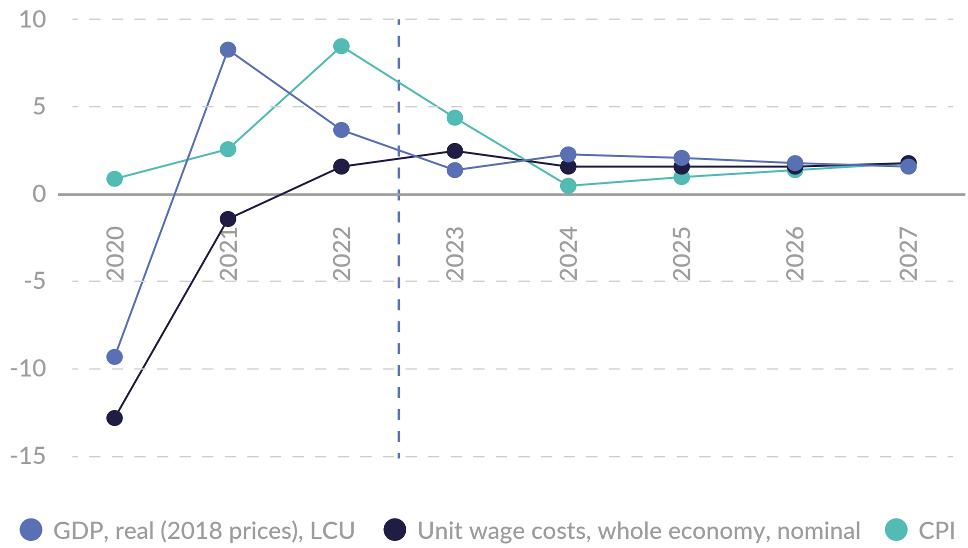
CBI Economics' modelling is set against a real-time challenging economic backdrop. Post-pandemic declines in labour market activity have exacerbated pre-existing labour supply challenges, and, alongside a global energy crisis, are fuelling cost and wage pressures, short-circuiting the UK's recovery from the COVID-19 pandemic. Sustainable wage growth is only achieved through stable and low increases to the cost of living over time. However in the current climate, despite earnings growth picking up, households are seeing a historic squeeze in their real incomes, which is weighing on consumer spending and leading to plummeting consumer confidence. With business confidence also falling, a fall in private investment as well as historically low export demand will contribute further to a weakening in GDP growth.

CBI Economics forecasts are for the next five years to be characterised by anaemic growth and stagnant productivity. The UK economy is expected to grow by 8% in real terms between 2023 and 2027, a similar pace of growth to that experienced over the four-year period before the pandemic. The unemployment rate is expected to stabilise at new lows of below 4%, and employment growth is set to be weak over the forecast period, alongside weak growth in the working age population.

The CBI also expects inflation to remain high this year, rising to a peak of 11% in the last quarter of 2022 before falling back to historic levels below the Bank of England's 2% target at the end of 2023[26 27].

Figure 1 below summarises the trends expected over the period to 2027.

FIGURE 1 **Baseline economic growth to 2027**



Source: Oxford Economics Global Forecasting Model, June 2022 update

Against this baseline, two counterfactual scenarios have been tested (see Appendix for details on the methodology). The impacts under each scenario are set out below.

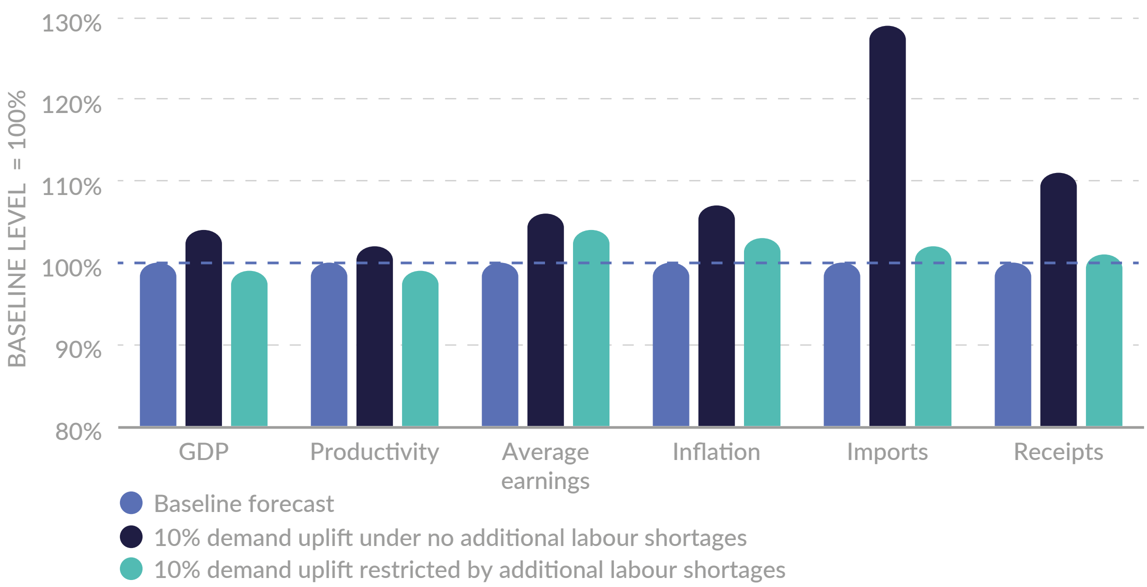
Labour constraints act to lower productivity and hinder economic growth

Based on the findings from the literature review on the key impacts of labour and skills shortages, economic modelling analysis was carried out to understand the economic and fiscal impacts of labour constraints in the context of a temporary increase in demand in the economy. The impacts of labour and skills shortages are typically felt acutely by hiring businesses, but their response also contributes to economy-wide changes, as previously discussed.[28] This is also backed by economic modelling done for this report.

The main adjustments to higher demand in the short term are seen in temporary productivity increases, but with persisting labour market constraints, additional adjustments take place through higher earnings and imports, with an effect also seen on inflation. In the medium term, labour and skills shortages can indeed act to lower productivity and GDP.

Figure 2 below summarises the potential impacts of a temporary 10% uplift in demand in 2023 with and without additional labour shortages compared to the baseline[29].

FIGURE 2 **Scenario comparison on key variables, 2027**



Source: CBI Economics modelling, June 2022

The modelling has shown that a temporary shock to demand under labour supply constraints lowers real GDP levels and productivity within two years of the shock[30]. Relative to current baseline forecasts for the UK economy, applying this shock in 2023 would require 1.7 million new jobs to accommodate it alongside productivity improvements. Without this employment increase, real UK GDP would fall by between £30 billion and £39 billion every year from 2024 over a four-year period through to the end of 2027. This is equivalent to 1.2% to 1.6% of GDP per year, around the size of the UK recruitment sector in 2019, or almost the entire current defence budget[31 32].

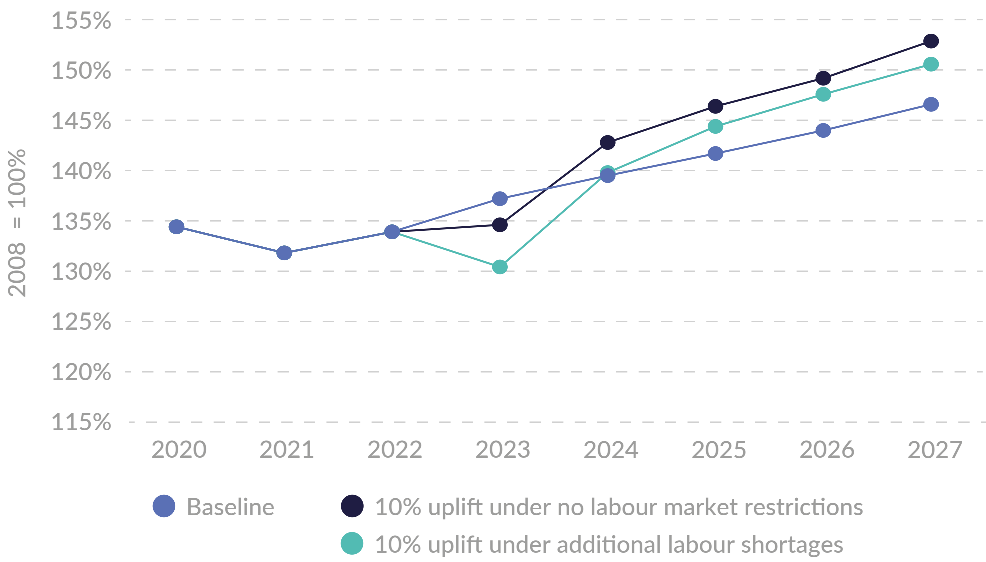
real UK GDP would fall by between

£30 & £39 billion

every year

The same demand shock acts to gradually increase subsequent average earnings every year, by an average of 2.7% over the forecast period. By 2027, average wage costs are 4% higher than the baseline. However, given an overall decline in productivity, earnings rise at a slower pace under additional labour shortages than they would without any labour market constraints – under no labour market restrictions, the same 10% demand uplift would push wage costs 6.2% above the baseline by 2027, compared to 4% under additional labour shortages.

FIGURE 3 The impact of a 10% increase in demand on earnings with and without additional labour shortages



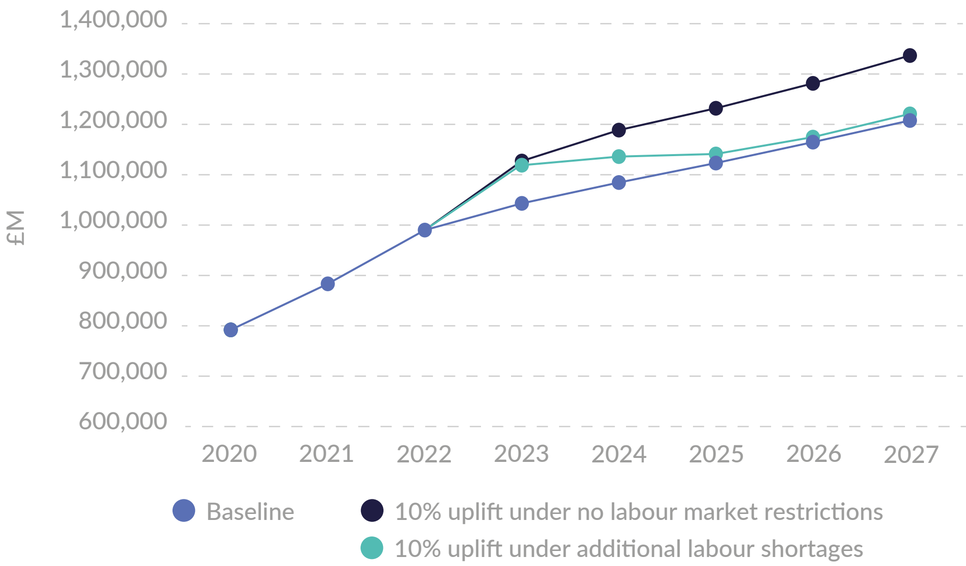
Source: CBI Economics modelling, June 2022

In line with the theoretical evidence and what is being seen in the economy at the moment, labour constraints fuel inflationary rises which exceed the growth in earnings. This causes a 1% fall in real incomes as productivity falls. Inflation under this scenario increases to 3% above the baseline level by the end of the forecast period.

Finally, the same 10% rise in demand would push public sector receipts 1.1% above the baseline by 2027. However, this is 10.6% lower than under a scenario of unrestricted growth due to falling productivity and output, and therefore falling receipts from production and income taxes.

FIGURE 4

The impact of a 10% increase in demand on public sector receipts with and without additional labour shortages



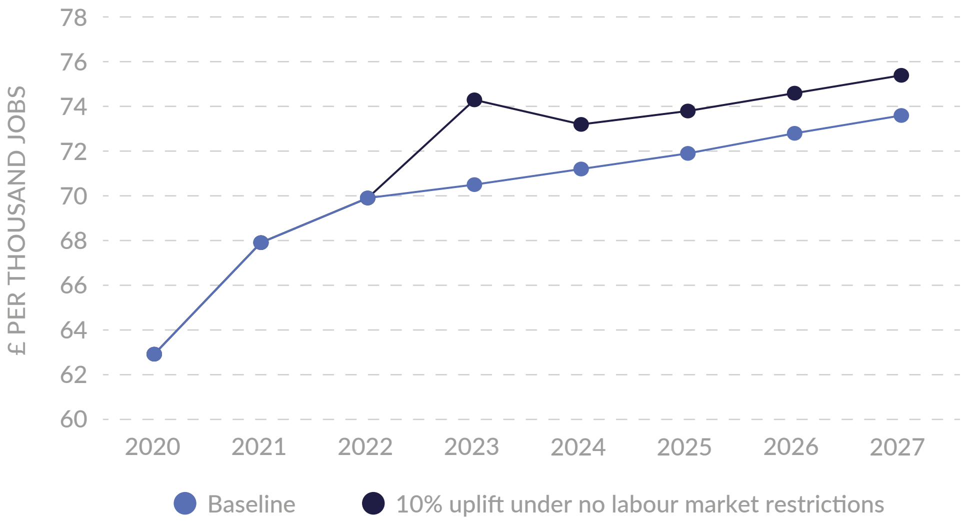
Source: CBI Economics modelling, June 2022

The impact of a demand shock under no labour market restrictions

To illustrate the difference in how the economy responds to a temporary demand shock under labour supply constraints, the same shock is first tested allowing adjustments through all channels available, including employment. Under this scenario, productivity rises in 2023 with the 10% uplift in demand and remains 2.4% above the baseline level at the end of the forecast period, in 2027. This is shown in **Figure 5**.

FIGURE 5

Productivity relative to baseline – 10% demand uplift in 2023 under no additional labour shortages



Source: CBI Economics modelling, June 2022

Without additional labour shortages, the 10% uplift in demand brings additional revenues to the Exchequer. The modelling shows public sector receipts rising 10.7% above the baseline by 2027 under this scenario.

The 10% uplift in demand also acts to increase earnings, with labour costs rising 6.2% above the baseline. With this, inflation also rises, exceeding the baseline by 7.3% at the end of the forecast period.

The impact of a demand shock with additional labour shortages

A 10% demand shock in 2023 acts to lower GDP levels by the end of the forecast period under a scenario in which the labour supply is restricted. Absent the demand shock, real GDP is 1.2% lower in 2027 than it otherwise would have been, in itself demonstrating the negative impact of labour constraints. It is important to note that the scale of the UK's existing labour and skills shortages is implicit within the baseline forecasts, and this scenario demonstrates the impacts of additional labour constraints. Against the current backdrop, an increase in demand would exacerbate existing impacts already seen in the economy.

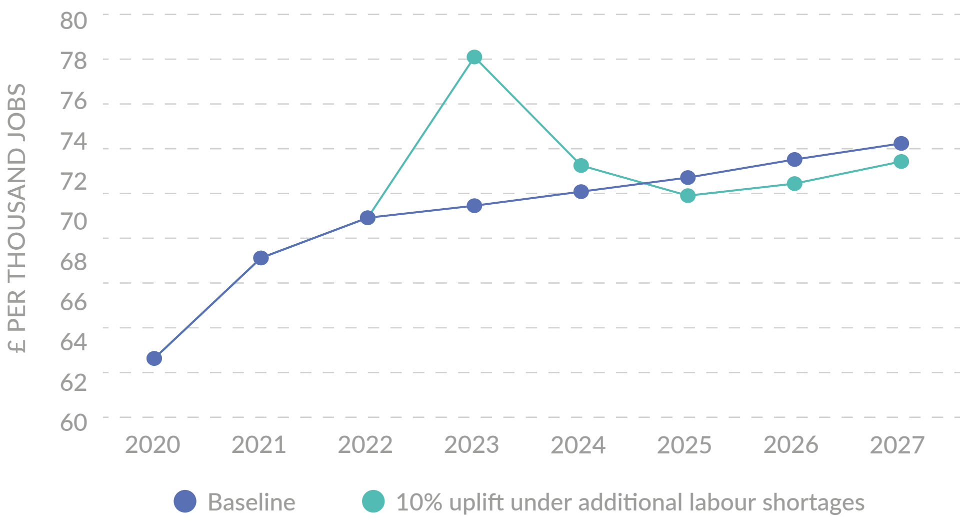
Accommodating a 10% demand increase in 2023 would require an additional 1.7 million jobs in the same year. The cost of a 1.7 million jobs shortage in 2023 would amount to a 1.2% decline in GDP and productivity by 2027.

This could potentially cost the UK economy £30.5 billion to £39.3 billion, which is equivalent to the contribution of the entire recruitment industry, annually from 2024 onwards[33]. Reduction in productivity, together with increase in inflation and imports, is what impacts the GDP. This implies a lower cost per job relative to studies in Germany and Canada, which estimate the impact of existing labour and skills shortages, although some of the cost of labour constraints is already accounted for in the baseline[34 35].

Figure 6 below shows the changes in productivity expected over the forecast period, relative to the baseline.

FIGURE 6

Productivity relative to baseline – 10% demand uplift in 2023 restricted by labour supply



Source: CBI Economics modelling, June 2022

In line with the broader evidence presented earlier in this report, labour shortages can result in higher earnings and inflation. Modelling shows earnings rise at a faster pace under additional labour shortages relative to baseline projections. Average wage costs are expected to grow by 12.7% between 2022 and 2027 under baseline conditions, taking into account existing labour shortages. With a 10% demand uplift under restricted labour supply, however, they are expected to grow by 16.7% over the same period. At the same time, inflation is 14% higher by 2027 compared to 2022, or 2.2% above the baseline projection for the Consumer Price Index (CPI).

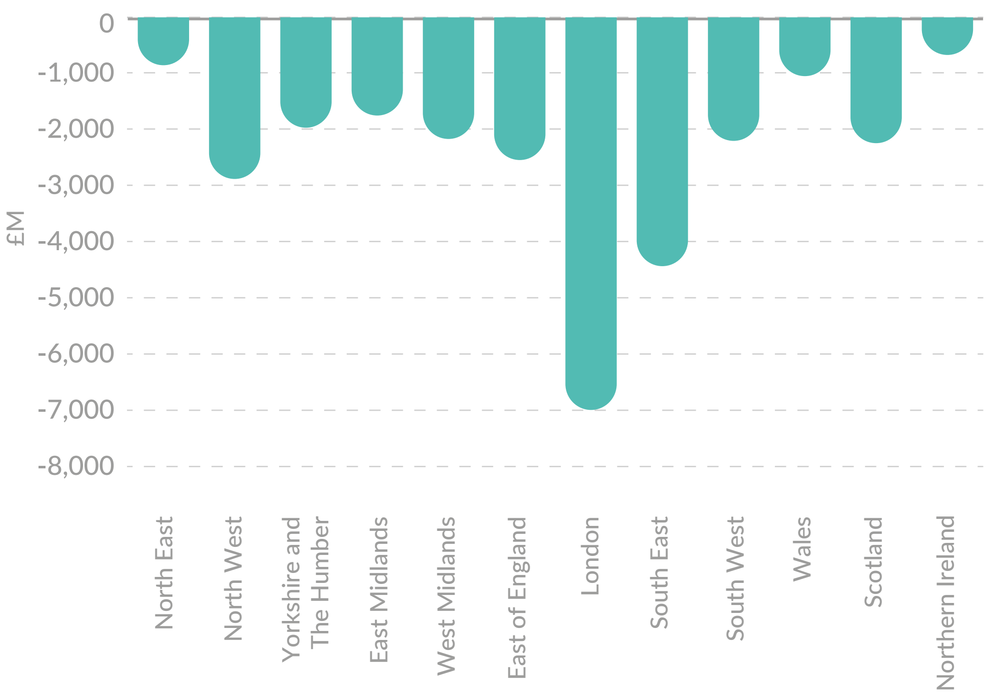
Despite higher earnings and inflation feeding into higher income tax receipts, the decline in productivity and real GDP act to limit growth in overall public sector revenues. Compared to growth under a scenario with no additional labour shortages, public sector receipts under this scenario are 10% lower.

Regional implications for falling productivity and GDP

While the extent to which labour and skills shortages affect regional economies is likely to vary, assuming the same scenarios have a consistent impact on GDP across the UK regions provides a broad illustration of how regions could be impacted.

Figure 7 summarises the regional distribution of the UK economy impacts on real GDP, apportioning the total cost associated with a 1.7 million jobs shortfall to regional economies by regional size. London and the South-East would be worst affected.

FIGURE 7 **Regional distribution of the real GDP impacts by 2027**



Source: CBI Economics modelling, June 2022

The regional impacts on real GDP associated with a 10% demand uplift under supply chain restrictions range from -£7 billion in the London region in 2027 to -£670 million in Northern Ireland[36]. The regional impacts are likely to be higher or lower than these estimates depending on the scale of the labour and skills shortages in each region. Depending on the metrics used to measure and compare labour and skills shortages, the regions that stand out with the most significant challenges vary.

More recent insight on unemployment rates across the UK regions shows the North East (6.1% of the working age population), London (5.8%) and the West Midlands (5.2%) stand out with the highest unemployment rates, while the South West (3.4%), Northern Ireland (3.8%), the East of England (3.9%), and the South East (3.9%) recorded the lowest rates[37]. A low unemployment rate may be a sign of a tight labour market, particularly if matched by a high number of vacancies and high growth in earnings. The latest ONS vacancies data, published in June 2022, shows the highest growth in the weekly average number of online job adverts between February 2020 and June 2022 was recorded in Northern Ireland (69% growth) and the North East (+41%), while the South East and the East of England recorded the lowest growth (+6%) over the same period[38]. The REC's latest Labour Market Tracker, updated in June 2022, also shows the North East (+74%) and London (+60%) standing out with the sharpest growth in active job postings at the start of June 2022 relative to the last week of December 2021[39].

While the likely scale of labour and skills shortages at regional levels and their impact on regional GDP is inconclusive, it is clear that labour constraints would act to hinder growth for most UK regions.

4. Comparisons with other countries

Having illustrated the scale of impact associated with labour and skills shortages, the following international benchmarking analysis demonstrates how the UK performs relative to comparable countries in terms of actions taken to address labour market shortages.

In the CBI's recent surveys, the most cited policy issue was labour shortages (by 36% of businesses), highlighting the importance of improving government policy in this area[40].

Benchmark selection and international literature review

Canada and Germany were selected as comparable countries for the international benchmarking against the UK. They were chosen from the G7 countries because data is comparable to the UK across two themes: the economy and the labour market.

The economy side covers key indicators such as GDP per capita, inflation, unemployment and investment. The labour market side includes digital skills training, immigration, labour productivity, and youth unemployment (which has a high cost to economy and society).

Key comparison areas within Canada and Germany for the benchmarking included:

- Costs of labour and skills shortages
- Evidence of labour and skills shortages
- Sectors most acutely affected
- Skills most in-demand
- Training and other labour market policies

Labour and skills shortages in Canada

Key learning:

Labour and skills shortages are also impacting the Canadian economy, particularly in accommodation and food services, construction, and manufacturing. Businesses are proactively working with educational institutes as well as investing heavily in technology and automation to alleviate the impacts.

The government has identified the key sectors for the skills shortages, and is actively seeking to attract immigration to these areas. Furthermore, extensive funding has been committed by the government for training and apprenticeships – again targeted to the sectors where demand is highest.

Context

Labour and skills shortages are evident in Canada. A survey found that 55% of Canadian entrepreneurs are struggling to hire the workers they need[41]. Furthermore, compared to 2013, more executives consider a shortage of skilled workers an issue (75% up from 68%) as well as finding young workers (66% up from 51%).

In order to close this skills gap, 47% of executives are offering more training for new employees, compared to only 36% of executives who expect prospective employees to be better prepared for the labour market[42].

When looking into sector-specific disparities, in a recent 2022 survey by Statistics Canada, the sector most impacted by labour challenges was accommodation and food services – with two-thirds of businesses in the sector facing labour shortages[43]. Construction and manufacturing are also expecting heavy recruiting challenges[44]. On the other hand, agriculture, forestry and fishing, professional services and real estate are the least likely to expect workforce-related challenges[45].

47%

of Canadian executives are offering more training for new employees to close skills gaps

How are businesses combatting this?

In a 2022 survey by the Business Council of Canada, the most effective action taken by businesses to alleviate the labour shortage was reported to be work-integrated learning. This is being increasingly adopted as part of recruitment strategies and businesses are collaborating with post-secondary education institutions to do so[46].

Furthermore, in a study looking at the biggest strategies employed by Canadian businesses to deal with labour and skills shortages, investing in technology and automation was amongst the most popular strategies[47].

Labour market policies

In 2021, the government of Canada announced $298 million over three years in a Skills for Success programme[48]. The programme will fund skills development in both numeracy and soft skills, and approximately 90,000 Canadians will benefit. Furthermore, $470 million over three years was committed to the Apprenticeship Service to help 55,000 first-year apprentices in eligible trades connect with opportunities at small and medium-sized employers.

Canada's Sectoral Workforce Solutions Program committed

$960 million

to training in skilled sectors like health, clean energy and construction

To target the labour and skills shortages, the Sectoral Workforce Solutions Program committed $960 million over three years to connect up to 90,000 Canadians with training for these skilled sectors, such as health, clean energy, and construction[49]. Through the Canada Digital Adoption Program, $1.4 billion was committed over four years to support 160,000 businesses to go digital[50].

Immigration is amongst the top priority policy areas being used in Canada to alleviate labour and skills shortages. In fact, about two-thirds of Canada's population growth is due to immigrants – which is projected to increase as well[51].

As part of this, Immigration and Citizenship Canada implemented the Global Skills Strategy to support businesses in attracting foreign talent in a simpler way[52]. This includes shorter application processing times and exemptions from having to acquire work permits targeted by the government to the skilled workers who are most in demand.

Labour and skills shortages in Germany

Key learning:

In Germany, labour market policies have been targeted to alleviate the most pressing issues: boosting the low participation rate, and shortages in skilled and vocational workers, particularly in healthcare, engineering, and skilled crafts. In implementing these targeted labour market policies, there has been extensive collaboration across a large number of public sector agencies, as well as an emphasis on immigration.

Context

It has been reported that between 2011-2018, vacancies in occupations with labour and skills shortages rose from 43% to 79% in Germany[53]. In addition, more than 50% of businesses view labour and skills shortages as the greatest threat to the development of their business[54]. As recently as the second quarter of 2022, labour and skills shortages were reported to disrupt the operations of 44% of businesses[55].

More specifically, key shortages have been identified for workers with a vocational qualification, and skilled workers in STEM (science, technology, engineering, and mathematics), healthcare and geriatric nursing, engineering, and skilled crafts such as electricians[56].

Furthermore, according to current forecasts, the working-age population is estimated to drop by 3.9 million, to 45.9 million, by 2030, and to fall by 10.2 million by 2060. This is not estimated to be offset by immigration, resulting in an expected fall in the total labour force[57].

This is on top of pressures to the labour force caused by Germany facing a below-average participation rate (the number of people working or actively seeking work as a percentage of the working population) of 61%, which compares to 79% in the UK[58].

In order to tackle this array of challenges, targeted policies have been implemented by the German government.

The German Federal and state governments, business and trade unions have formed an alliance to boost vocational qualifications

Labour market policies

In Germany, the government and federal agencies have proactively identified where support in the labour market is most required. For example, to boost vocational qualifications, a key shortage, the Federal Government, the Federal Employment Agency, commerce, trade unions and the Länder (the 16 federal subdivisions of Germany) formed the Alliance for Initial and Further Training. A main aim of the Alliance is to promote the 300 professions for which vocational training is available to young people. Furthermore,to increase the participation rate,a campaign was established to involve more women and older people in working life, as well as providing support to companies to promote a diverse workforce[59]. This kind of joined up work is a model the UK should be following to deal with shortages.

Immigration has also been a key policy for Germany, with latest data showing approximately 2.7 million net migrants in 2021, more than double that of the UK. The Federal Ministry of Labour and Social Affairs has focused on legislation to attract skilled workers with vocational training qualifications from third countries. This includes learning German, as one of the most important factors determining integration into society and work, and the federal government establishing language programmes in order to do so[60].

The Federal Ministry for Economic Affairs and Climate Action has supported 170 refugee recruitment advisors to help companies in filling their vacancies and vocational training positions with refugees since spring 2016[61]. These advisors organise work placements, job shadowing opportunities, support in acquiring basic skills, and find jobs and vocational training positions. As of 2018, they helped 9,700 refugees find work and 2,585 took up dual vocational training. The Integration through Qualification programme – implemented in cooperation with the Federal Ministry of Education and Research and the Federal Employment Agency – provided assistance with equivalence recognition from abroad and improved employment opportunities for migrants[62]. The Skilled Immigration Act introduced on 1 March 2020 expands the framework for qualified professionals from non-EU countries to work in Germany. This is tailored particularly to professionals with a vocational training qualification[63].

5.

The business view

UK businesses were asked about the labour market challenges they face and what more can be done by businesses, government and other stakeholders to ensure a longer-term view for skills and to overcome shortages. In total, 15 businesses were interviewed in June 2022.

The businesses ranged in size, were distributed throughout the UK, and represented a range of sectors including retail, professional, scientific and technical activities, real estate, manufacturing, health and social work, education, and wholesale and retail trade.

Six key themes emerged from the business interviews:

1. The importance of collaboration between industry and government
2. The need for apprenticeship levy reform
3. The importance of business collaboration with the educational sector
4. The need for changes to immigration policy
5. Regional businesses struggle to compete on salary
6. The importance of collaboration between recruiters and business

More collaboration between industry and government is important

It was noted by multiple businesses that closer collaboration between government and industry would be helpful, for example, by enabling government to better understand problems and to broker useful connections for businesses.

Businesses noted some examples of how existing collaboration with government works well. A food service wholesaler raised the Regional Learning and Skills Partnership as a good attempt to bring together schools, universities, local authorities and Welsh government to help resolve skills gaps now and in the future.

An engineering company highlighted their work with trade bodies to understand what the total labour pool looks like. They also mentioned that the government's broad visibility across many different areas allows them to broker useful connections for industry, for example notifying businesses of a trade fair which they found very useful to spur engagement with academic institutions.

A number of businesses mentioned that an even more joined-up approach with government would be beneficial. An education training provider said that there are often different conversations happening on the same issue and that a unified voice is required. A housing association mentioned that despite the government's talk about future skills gaps, they believe there is a lack of a joined-up strategic approach in place to deal with this.

A few businesses held the view that government needs to engage with businesses more to understand the issues they face. A concrete manufacturer mentioned that local politicians don't engage enough to understand issues and that they want to work more closely with them on how policies affect industry.

An executive search and selection company based in Scotland mentioned that whilst they have engagement with senior politicians in Scotland, it tends to be government telling them about issues rather than listening to understand the key issues businesses are facing. A few interviewees mentioned that they have been caught off guard when it comes to skills requirements. An NHS Trust mentioned when interviewed that the NHS was unaware just five years ago of how important technologies such as AI and robotics would be in surgeries today (see case study). A manufacturer raised the frequency of advances in engines and that they find it difficult to predict the next disruption in this area. These stories suggest a greater role for horizon-scanning in workforce planning, ensuring that relevant experts are involved.

NHS Trust

New technologies took public healthcare by surprise

An NHS Trust mentioned that just five years ago the healthcare sector was not fully aware of the importance that technologies such as artificial intelligence and robotics would play in healthcare, for instance in spinal surgeries.

They raised the importance of ensuring that the right people are involved in workforce planning conversations, to ensure a more proactive approach to future skills gaps. Having those at the forefront of scientific research, whether they be in the education sector or in industry, working with individuals in government would increase the ability of healthcare providers to pre-empt and prepare for such disruptive change.

The importance of healthcare providers working closely with educational institutions to ensure an adequate future workforce was also mentioned. The trust mentioned that technological transformation in healthcare necessitates that surgeons receive both medical and digital training. Greater foresight about such disruption would allow meaningful collaboration between healthcare and educational institutions to happen in a timely manner.

More flexibility in the use of apprenticeship levy funds

Several of the businesses interviewed mentioned that more flexibility in the use of apprenticeship levy funds would go some way to helping fill skills gaps.

First Intuition, a professional education training provider, mentioned that it would be useful to be able to use apprenticeship levy funds for more short-term modular training (see case study). An engineering firm had the view that it was very difficult to spend apprenticeship levy funds due to the inflexibility on how they can be spent, whilst a housing association mentioned that this inflexibility means that they rarely use all of the levy funds, which then end up going back to the government.

First Intuition

A professional education training provider stressed the importance of being able to use apprenticeship levy funds more flexibly

First Intuition is a professional education training provider. They stressed the importance of more flexible use of apprenticeship levy funds to enable more dynamic, short-term, modular training.

They mentioned the growing importance of upskilling in areas which are going to be crucial to the future of the UK economy, such as digital and decarbonisation. However, it was their view that upskilling in these areas often does not require a year-long course or building towards a full qualification, and therefore that levy funds often don't enable access to such training.

First Intuition believes in the usefulness of incentives to bring young adults into their industry and invest in training, but feel that more flexibility in the types of training that are incentivised could go a long way.

Business should collaborate more with the education sector

Several of the businesses interviewed mentioned that greater collaboration between industry, government and educational institutions would help enable a more proactive and longer-term view for skills.

A benefit of collaboration that was consistently raised was the opportunity for businesses to help ensure students learn the right things to help fill important skills gaps, and ensure students are more aware of various career paths, especially those that currently or will face future shortages. LiveWest Homes, a housing association, expressed a desire to partner with educational institutions to develop important retrofit skills training, an area they saw as a current gap and one that is likely to get more severe over the next decade (see case study).

LiveWest Homes

A housing association wants to partner with educational establishments to fill an important skill gap

LiveWest Homes is a housing association with homes across the South West of England. They mentioned that retrofit skills are an important skill gap within the UK. Retrofitting is the process of making changes to existing buildings so that energy consumption and emissions are reduced and is an important priority in the push to net zero carbon emissions.

LiveWest would like to work closely with local educational establishments to develop training courses that would enable businesses to either train up their existing workforce or increase the pool of workers that can be drawn upon with these skills. Their view is that rather than wait for these skills to be available, they would prefer to take a more proactive approach. By partnering with educational establishments, LiveWest hopes to help shape courses that will deliver the essential retrofit skills they need now and over the next decade.

A global commercial real estate services firm suggested that real estate courses could be altered to better target the skills that employers in the sector need, and that businesses need to be involved in this process to ensure the right content is included. It was the view of a food manufacturing business that some educational institutes are not very effective at promoting lower-profile sectors as potential career paths, such as agriculture, where innovative technologies may not have been well-marketed by the sector. It was mentioned that more involvement from industry could help advertise these career paths.

Similarly, an engineering firm facing shortages in a variety of blue-collar roles, including welders and pipe-riggers, felt that industry working more closely with educational institutions could ensure more people move into these STEM-based careers, which may not traditionally be seen as desirable career choices.

Finally, a healthcare provider mentioned that working more closely with schools could make young students more aware of various healthcare roles and help ensure the healthcare system has the right talent over the next decade, as well as potentially enabling alternative routes into the healthcare sector to reduce gaps.

A similar point made in interviews was that businesses could do more to help educational institutions prepare students for the world of work. It was the view of a discount store chain that technology is moving faster than the pace of education, and that a more joined up approach between industry and education could ensure students enter the world of work with vital technology skills. A number of businesses mentioned that government could facilitate more employability and careers advice early on, involving local industry.

To build on reform to the apprenticeship levy, a number of businesses interviewed mentioned that greater collaboration with educational institutions could enable a greater number of apprenticeships. Adi Group, an engineering firm, is developing their talent pool through apprenticeships and pre-apprenticeships (see case study). The global real estate firm expressed a desire to offer more apprenticeships, but felt that the expansion would require more joined up work with schools, local education authorities and colleges.

adi Group

An engineering firm is tackling a 40+ year industry skills gap through apprenticeships and pre-apprenticeships

adi Group is a multi-discplinary engineering firm providing services across the UK and Ireland. They mentioned that in order to tackle a long-standing skills gap of engineers, particularly mechanical and electrical, adi Group have instigated programmes to inspire the next generation of engineers, which includes a pre-apprenticeship, as well as their core apprenticeship academy, thus developing the wider pool of engineers.

adi Group works with local educational institutes, particularly schools, to put in place apprenticeships and pre-apprenticeships with an aim to have in excess of 5% of their total workforce to be full-time apprentices. Their pre-apprenticeship programme provides GCSE students the opportunity to spend up to 10% of their time working with adi.

adi Group hopes this will also encourage other businesses to be proactive in the school system to inspire and develop the skills of students, and expand the talent pool of engineers.

A UK law firm felt that students are generally not well-educated on apprenticeship opportunities, limiting the total number of apprenticeships, and that there could be a role for government to be more involved in advertising such opportunities. Similarly, a retail bank felt that apprenticeships were not being adequately promoted in schools.

A more flexible immigration system would help with shortages

Difficulties with hiring workers from abroad, and therefore the ability to fill labour gaps, was noted by a number of businesses. It was mentioned that changes to the immigration system to ensure more flexible immigration would be beneficial for businesses, alongside homegrown skills development.

Princess Yachts, a luxury yacht manufacturer, mentioned that they have particular struggles recruiting carpenters (see case study). A global commercial real estate firm noted a shortage of high calibre individuals and called for an immigration system that recognises talent.

Princess Yachts

A luxury motor yacht manufacturer is struggling to recruit overseas workers for important roles

Princess Yachts is a luxury motor yacht manufacturer based in Plymouth, England. They noted that the government's policy on migrant workers has contributed to difficulties filling certain roles.

In particular, Princess Yachts highlighted that they are facing a significant shortage of skilled carpenters, in part due to high demand for such skills in a burgeoning housing market. There are not enough homegrown carpenters to fill the roles they have available right now. They recounted that hiring one skilled carpenter from Poland took months and was a painful process. They would welcome more flexible, easy immigration from around the world to help fill important labour gaps.

A food service wholesaler raised that inflexible immigration policy has had an impact on their suppliers, resulting in a knock-on effect on their business. An education training provider raised that a declining working population spurs the need to increase the number of people entering the country through a flexible immigration system.

An executive search firm called on government to take more leadership in engaging with people who are not in this country, but who may be willing to relocate. A concrete manufacturer and supplier mentioned that the skill level they are recruiting for is not on the shortage occupation list.

As well as being a prominent point that came out of the business interviews, the importance of more flexible immigration is a point that has consistently been raised by the CBI's membership body more widely, with businesses calling for a push for more immigration to deal with current shortages, including seasonal workers in sectors such as food production.

A number of businesses expressed difficulties stemming from the visa system. A chain of discount stores felt that the visa and work sponsorship systems were overly bureaucratic and expensive, and that reform could help increase the number of workers to fill entry-level jobs, an area they feel is a current gap.

A concrete manufacturer felt that English requirements for tier 2 visas were too high, inhibiting useful immigration. A retail bank commented that they have had to hire workers on fixed term contracts due to uncertainties over their future visa status, which ultimately makes it more difficult to fully invest in these individuals.

Finally, a food manufacturing business noted that skilled worker visas have increased their costs, as they have had to increase salaries across the business to match what skilled workers are paid abroad. Overall, they view that skilled worker visas have made hiring workers from abroad less attractive in comparison to the previous tier 2 general work visa.

Regional businesses often struggle to compete on salary

It was mentioned by businesses in certain regions that they struggle to pay the same salaries as businesses in other regions, which contributes to attrition and workforce gaps that can be difficult to fill.

A law firm based in the South West of England, highlighted that the majority of lawyers are based in London and that it can be difficult to access the talent needed in their area, in part due to the higher salaries that can be earned. They mentioned that businesses outside of London need to compete on other factors, for example working hours and work-life balance.

A food service wholesaler based in Wales mentioned that there is phenomenon of workers moving in search of higher pay, with Welsh workers moving to England and English workers moving to higher wage areas within England, particularly London.

This is also a point that the CBI has heard from its membership, with businesses telling the CBI that workers outside of London, particularly those in the digital sector, can easily take London jobs whilst resident in their region, due to the nature of such roles facilitating remote working. Businesses have raised the need to pay higher salaries in response, to try and retain workers.

Businesses could benefit from closer collaboration with recruiters

Several of the businesses interviewed noted that they are becoming more reliant on recruiters to fill vacancies. Avison Young, a global real estate services firm, noted that the time and cost associated with recruiting have increased and therefore that they have had to rely on the expertise of recruiters (see case study).

A law firm mentioned that they are supported by recruitment agencies on a daily basis, with virtually all of their experienced hiring going through an agency. A chain of discount stores also highlighted their work with external recruiters, despite also having an in-house recruitment team.

A recruitment agency interviewed also sees a greater role for them to collaborate with various stakeholders. They mentioned that recruiters can work with educational providers and students to help with CV preparation and interview advice. Whilst this will not increase the size of the overall talent pool, it will help prepare students for the world of work and improve the allocation of students to vacancies.

Avison Young

A global commercial real estate services firm found that the time and cost to recruit have increased

Avison Young, a global commercial real estate services firm, mentioned that labour shortages have significantly increased the time associated with hiring, and have therefore necessitated the use of recruiters.

In particular, Avison Young finds recruiters' expertise valuable when they are looking for a particular type of person to fill a vacancy. They mentioned that, as a real estate firm which requires qualifications, the talent pool is ring-fenced and mid-market candidates are the most difficult to source. They mentioned that recruiters generally understand their markets and the available candidate pool very well and, given that in-house recruitment teams cannot be specialists across multiple markets, it is often necessary and beneficial to use recruiters to hire specific types of people that may sit outside the specialty of in-house teams.

Avison Young also mentioned that, without recruiters, shortlists of candidates would have to be smaller, with negative impacts on diversity and inclusion.

6.

Overcoming shortages

Policy and business recommendations

This report has highlighted why the current staffing crisis needs to be urgently addressed.

If we don't act now, we won't have a claim on the UK leading the charge as a powerhouse for growth, competitiveness, productivity and inclusion. Essentially we have to start putting people first. These interventions should be centred around plans to boost company performance, tackle labour shortages, raise skills levels and create better working environments for all.

Our recommendations are a first step towards achieving those goals[64].

Recommendations for business

Businesses are the key actors in delivering growth. It is their leadership on investment, inclusion and productivity that government intervention should be aiming to drive – with each pound of public money designed to catalyse private sector investment. But we should be clear – as a business community we have tolerated too much short-termism on the "people stuff" for years. Firms must play their part on skills, and finally behave as if people are their greatest asset – not just say it.

- Businesses should have a five-year workforce strategy and investment plan signed off and reviewed by the board annually. Detail should focus on developing management skills and innovation in work design.

Skills are an investment, not a cost

Increasing investment in skills isn't effective unless it is targeted and integrated with the overall commercial growth plan. Any commercial long-term strategy should include a people plan which treats skills spending as investment rather than cost. Businesses should:

- Increase investment in training and development for all staff, giving them opportunities to grow and progress in their careers as this will also boost firms' productivity and revenue.
- Get involved in local and sectoral skills co-ordination – 90% of what you need is also required by other local firms in your sector, so work together to ensure good provision, and view it as time well spent. As this grows, use local and sectoral networks to bring more firms in and expand the network.

Equality, diversity and inclusion should be at the core of your people plan

Most businesses know that achieving an equal, diverse and inclusive workplace is essential for commercial and ethical reasons. And we increasingly have examples in recruitment of candidates refusing job offers for companies that don't demonstrate their EDI credentials. But still not every business is acting to bring this important change about.

Recruiters can be great partners in delivering this, especially in a tight labour market that will leave you behind if you don't act to recruit and retain the best talent from all demographic groups available.

- Implement equality, diversity and inclusion (EDI) policies with your internal workforce, to actively address imbalances in the labour market such as through recruiting from more diverse talent pools and providing tailored support for employees.
- Work closely with recruitment agencies and EDI specialists to regularly review your internal policies and ensure they are up to date and in line with best practice. Things can move fast in this space – don't get caught out and left behind.
- Be a champion for EDI, educate clients and other stakeholders on the benefits of a diverse and inclusive workplace and encourage others to do the same.

Working conditions matter

There has been a huge shift in how people work due to the pandemic, and this has triggered a broader conversation amongst employees and employers around flexibility. Employers need to deploy good employment relations skills. This debate cannot be ignored and instead should be embraced with active listening by deploying a range of engagement tools and negotiation with employees on the needs of businesses as well as employees.

Salaries have increased in this tight labour market, but this isn't the only answer to enticing new staff in a market where shortages are rife. For a sustainable hiring strategy there are many other actions to be considered to attract and retain talented people.

- Improve staff engagement when considering benefits and conditions. This could include introducing flexible working arrangements, mentoring programmes, and regular pay and benefits reviews. Implement an employee wellbeing programme so workers feel comfortable and safe in the workplace. This might include mental health support, wellbeing days or employee assistance programme.

Recommendations for governments

Alongside business, there is a key role for government to play. Develop a proper plan for how to support and develop our labour market, tackling the forest of unlinked interventions coming from at least five different departments. Success should be measured by outcomes, and by the private investment that has been encouraged – not by places filled on a 'flavour of the month' training course. Acknowledge links between employment and other enabling issues – like childcare and transport. And this plan must be given a proper home with clear accountability, regular reporting and assessment.

Here we outline our recommendations including on skills, immigration, regional investment and labour market activation more specifically.

- Commission, with immediate effect, a cohesive, long-term plan for how the UK will put people planning at the heart of its growth strategy, and the unified role government can play. This must go well beyond just skills.
- Give this plan a home in the Cabinet Office or with an independent commission. Work closely with business and others on developing and monitoring progress. Commit to keeping the approach in place over many years – like productivity commissions elsewhere in the world. The most successful UK labour market changes of the past few decades – such as the National Living Wage and pensions auto-enrolment – have been delivered this way, by governments of all parties. It's a proven formula for success.

Skills – ensure policies catalyse private sector investment

While the skills systems of the four nations differ, all four need to improve their responsiveness to local needs, while maintaining high quality. Governments' role should be to ensure that supply is available for business needs locally, and that the quality of that supply is high. Funding arrangements need to ensure that public money catalyses private investment and creates an atmosphere in sectors and local areas where free riding by non-training employers is challenged. The current apprenticeship levy doesn't do that – and this has always been businesses' primary complaint, rather than the cost.

- Accept that the apprenticeship levy has failed in its ambitions, and work with business to redesign it in ways that encourage high-quality early-career apprenticeships, good retraining options and modular interventions that help move careers on quickly by addressing shortages and helping to level up through increased salaries for enhanced skills. The issue is not the existence of a levy – it is making sure it funds the right things.
- Give even more power over skills policy to devolved governments and local and regional mayors – along with control over the fiscal measures required to fund this. Consolidate this by ensuring that local businesses and recruiters are consulted on the skills needs in their area.
- Expand Local Skills Improvement Plans (LSIPs) across England with a view to supporting the model across the entire UK, in ways which are appropriate for each devolved system. Improvements should be made to build on the success of the eight current schemes, including offering more short and modular courses, and ensuring that participating colleges have access to current employer data.
- Create a tax credit scheme for employers who invest in training, and specifically, a 'green tax credit' for businesses that invest in green skills, green jobs and reduce their carbon footprint.

Immigration policies that go beyond politics to address critical labour needs

We should have an 'immigration for growth' policy approach. Part of a responsive and responsible labour market has to be an immigration system that meets business needs to facilitate growth, innovation and encourage increased productivity.

- Extend work visas to at least five years – from the current two or three years.
- Update the Shortage Occupations List (SOL) every six months to make the immigration system more responsive.
- Reduce the waiting time for asylum seekers to be eligible to work in the UK from 12 months to six months.
- Establish an immigration route for entry-level skilled workers.

There are several small, practical changes that the Home Office can make to existing routes – such as extending the lengths of the Graduate Visa, Youth Mobility Scheme and High Potential Individual Visa; updating the SOL more frequently; and letting refugees access work earlier. Allowing asylum seekers to work after a shorter period of time would allow businesses to access a small pool of skilled workers, and also help their integration into the UK. For example in Germany, the government provides targeted support for refugees, deploying 170 refugee recruitment advisors and supporting refugees into vocational training and jobs. UK recruiters could also help with such a scheme.

Most importantly, the UK urgently requires an immigration route for workers at skill levels 1 and 2. Critical sectors such as construction, logistics, retail and hospitality are experiencing a severe shortage of staff at these levels and this demand cannot be met by the domestic supply of labour. The immigration system therefore must be flexible to the needs of these key sectors of the UK economy.

Levelling Up – making local labour markets work

- Further invest in local transport, involve local businesses in local transport plans, and reward businesses who operate private transport services for their workers.
- Build on the success of the Gatsby Benchmarks to ensure every young person gets effective, locally-relevant careers advice
- Improve access to childcare for working families by reforming childcare benefits and improving funding for childcare providers.
- Introduce statutory two-week leave for grandparents and require businesses to conduct a review with all staff over the age of 55 on flexible working arrangements.
- Mandate ethnicity and disability pay gap reporting for large businesses to further diversify the labour market and retain talent.
- Create the next iteration of the Kickstart Scheme, learning from past experience.

Local businesses, local authorities and local people are the experts when it comes to their areas. But currently there is a mismatch between the jobs that are available locally and the skills, education, training opportunities and infrastructure available to fill them. Local businesses and governments are keen to address these. With the right powers and incentives, central government can unlock the vast potential of these areas and help the devolved nations, regions and local areas across the UK to level up.

There are a number of opportunities that the government can provide to a wide range of marginalised groups who are currently excluded from the labour market. The government needs to review the current legislative and benefits framework, so they provide the right type of support to accommodate different people such as older workers, ethnic minorities, people with disabilities, young entrants to the jobs market and those with caring responsibilities.

To deliver these policy recommendations, government should first create a future workforce strategy, which will help avoid future recessions, boost productivity and increase investment. Without this collaboration, the government won't achieve its ambitions for a high-wage, high-growth economy.

Key recommendation for governments:

Create a Future Workforce Strategy, outlining the skills that the UK economy will need over the coming years and putting in place the policies that will be needed to make this a reality.

Key recommendation for businesses:

Unless workforce planning is pushed up the agenda at leadership level, businesses will be stifled in their own attempts to grow and innovate. Many companies say their staff are their greatest asset and their top priority – it is time that was followed with action.

Conclusion

Business and government have a duty to overcome shortages if we want to create sustainability in our labour market. Rather than talking about the problems we face, we now need solutions and action.

This report has aimed to provide evidence on **why** we should act: with a 10% surge in demand for workers across the economy, and the labour market restricted by shortages, we could see a 1.2% fall in expected GDP and productivity by 2027 – costing the economy anywhere between £30 billion and £39 billion every year. The UK recruitment industry creates that value in any given year – it's like our industry's hard work would be fighting to keep us standing still, when it could be leveraged to create bigger and more sustainable growth.

We have found examples of **how** we can create change, learning from our international cousins in the G7 – both in terms of what works and what doesn't. While every context is always unique, the issues facing the German and Canadian labour markets share some similar characteristics with the UK. In both countries, governments have deployed active and symbiotic skills and immigration systems to overcome labour shortfalls, crucially supported by business engagement.

And finally, in talking to UK businesses, we have identified key concerns and **what** businesses need to overcome these problems. The consistency in views from a range of businesses that vary by size, location, and sector is striking.

The pandemic and its aftermath showed us what it takes to survive and thrive – businesses need the right people in the right jobs. The onus on creating the right environment for people to fully participate in their jobs is on the businesses employing them – which is why we need more than lip service from business now. People plans and people management need to be at the heart of every business strategy, and the recommendations we make here build on the evidence and good practice identified by this research.

But if businesses are truly to put their people first, they also need the underlying conditions to be working to support growth – and these are levers that government have at their disposal. Real change will not be achieved in a few short months or years. We only have to look at how long we have been bemoaning labour and skills shortages to know the validity of this. So we need consistency and boldness in our approach, that steps away from government funding short-term, opportunistic or quick-fix approaches.

Instead, we need to create a long-term vision based on shared goals of creating a more prosperous, productive and inclusive UK.

As experts in the labour market, we stand ready to work with the policymakers to achieve this bold ambition for our future.

Appendix

Modelling methodology

To illustrate how labour constraints play out in the economy, CBI Economics used the Oxford Economics Global Forecasting Model to test a 10% temporary demand uplift in 2023 against the baseline forecasts for the UK economy between 2022 and 2027. This enabled us to gauge both the immediate response to such a shock and the medium-term impacts on key economic variables such as real GDP, average productivity, average earnings, inflation and imports. CBI Economics also assessed the impact on public sector receipts.

The demand uplift was applied to individual components of GDP: household consumption, government spending, fixed investment, and exports.

The impact of a demand shock under baseline conditions

Our first scenario tests the impacts to 2027 relative to the baseline forecasts under no restrictions on the UK's labour supply or on productivity. This fully utilises the econometric relationships between key economic variables underlying the model, with no interference to override these relationships.

The impact of a demand shock under additional labour supply constraints

This scenario essentially 'fixes' our baseline employment forecasts such that employment is not allowed to change with the uplift in demand. Under this scenario, productivity is free to change, but the model assumes that productivity cannot be increased infinitely, and other channels – such as imports, wage increases, and inflation – will act to dampen down demand in the medium-term.

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28. CBI Industrial Trade Survey, Distributive Trade Survey, Services Sector Survey (June 2022)
29. The 10% uplift in demand is tested under two scenarios: one which allows the economy to respond to higher demand through all impact channels available, including the labour supply; and the second which is fixing the labour supply at baseline levels, therefore not allowing adjustments to increased demand through higher employment. Comparing the two scenarios can therefore illustrate the impact of labour shortages beyond those already present in the economy, implicit within the baseline.
30. This is driven by an increase in household expenditure, investment, government spend, and export demand. Note that the 10% uplift is intended to be used for illustrative purposes. A real GDP increase of this scale is typically only realistic when the economy is bouncing back from a period of decline. By 2023, the UK economy will have mostly recovered from the impact of the COVID-19 pandemic, which saw GDP contract by

31. £31.5bn in Gross Value Added in 2019 according to ONS Regional gross value added (balanced) by industry publication (May 2022)
32. A decline of 1.2% between quarter 4 2020 and quarter 1 2021 according to ONS GDP first quarterly estimate time series (May 2022)
33. £31.5bn in Gross Value Added in 2019 according to ONS Regional gross value added (balanced) by industry publication (May 2022)
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35. Institute of the German Economy (2018). Skilled labour shortages slow down growth.
36. Note that, based on the average regional shares of the UK real GDP over 2018 – 2020, the projected regional impacts reflect regional size rather than regional labour market challenges or the make-up of the regional economies.
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64. These policy recommendations come from the REC.

REC Recruitment & Employment Confederation

The Recruitment & Employment Confederation is the voice of the recruitment industry, speaking up for great recruiters. We drive standards and empower UK recruitment businesses to build better futures for their candidates and themselves. We are champions of an industry which is fundamental to the strength of the UK economy.

Find out more about the REC at **www.rec.uk.com**

Dorset House
First Floor
27-45 Stamford Street
London SE1 9NT

020 7009 2100
info@rec.uk.com
@RECmembers
www.rec.uk.com

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