GROWING A MORE PRODUCTIVE AND COMPETITIVE ECONOMY

A SUBMISSION TO THE CHANCELLOR

OCTOBER 2016

BRC

SUMMARY OF RECOMMENDATIONS

1. WORK WITH THE INDUSTRY TO DELIVER A RETAIL INDUSTRY STRATEGY WHICH PROMOTES POLICIES THAT HELP RETAIL INVEST FOR PRODUCTIVE GROWTH

2. DELIVERING ON BETTER PAY, PROGRESSION AND PRODUCTIVITY

- Take a moderate approach on increasing the National Living Wage
- Strengthen the role of the LPC to enable it to make fully independent recommendations, based on full consideration of economic conditions and free from political intervention
- Ensure an employer-led, industry specific solution to the Apprenticeship Levy, giving businesses more time to prepare by postponing the introduction of the levy and allowing more than 18 months to spend the Levy funds
- Measure outcomes not processes/inputs and ensure funds can be directed to the most valuable types of training and the seamless integration in the devolved nations

3. A SUSTAINABLE BUSINESS RATES SYSTEM

- Revisit the Business Tax Roadmap to deliver meaningful, fundamental reform which moves the UK away from having the highest commercial property taxation in Europe and across the OECD
- Bring forward the switch to CPI and over time introduce a lower flat rate so that rates rise and fall in relation to property values aided by more frequent revaluations every three years
- Introduce a more robust method of determining any infrastructure levy using a business ballot and ensure a fair appeals system, taking account a property's Rateable Value, removing the proposed 'outside the bounds of reasonable professional judgement' clause
- A more collaborative working relationship between the VOA and ratepayers where information and evidence can be shared and appeals avoided should be sought

4. A FAIR BREXIT FOR CONSUMERS

- If consumer prices are to be kept down it is essential that 'Brexit' imposes no new customs duties upon trade with the EU
- MFN rates adopted by the UK once it leaves should be broadly the same as those it applies as part of the EU
- Government should start early on recreating the benefits of EU preference schemes such as GSP in relation to trade with developing countries
- A clear, unambiguous statement from Government that colleagues legally living and working in the UK shall continue to be able to do so following the UK's departure from the EU

FOR ITS PART, UK RETAIL WILL WORK HARD TO IMPROVE PRODUCTIVITY, HARNESS AND DEVELOP NEW AND DIFFERENT SKILLS FOR THE DIGITAL AGE, WHILE CONTINUING TO OFFER HIGH QUALITY, LOW PRICED GOODS TO UK HOUSEHOLDS.

DEAR CHANCELLOR,

Our submission sets out how changes in the retail industry are increasingly impacting our three million employees and the tens of millions of customers they serve each week. It describes why a successful approach to partnership with government is integral to our vision of better retail jobs and crucially, a more productive industry.

Retailers are the most directly customer-facing of all businesses. As their customers' expectations change, empowered by ubiquitous technology in a digital world, so too must they. Because of this, the very nature of retail jobs is changing dramatically with a growing demand for new and diverse skills in the workforce. The UK industry today employs 100,000 people in roles that didn't even exist five years ago.

We know from our Retail 2020 research that the rate of change in the industry is accelerating. This has major consequences for skills requirements, employee pay and progression as well as productivity levels. Change is being driven by a technological revolution that is fundamentally altering how we shop and the way in which retailers do business. It is happening against a challenging backdrop of shop price deflation, subdued sales growth, fierce competition and declining profitability.

Policy decisions by the previous government, in particular changes to the employment landscape and lack of meaningful reform to businesses rates, are increasing the pace of some of these changes, with the impact falling unevenly across the country. Areas that are already economically fragile are likely to see the greatest impact of store closures and some of the people affected by changing roles will be those who may find it hardest to transition into new jobs that are created.

There will be fewer jobs in retail in the future and as a consequence the industry will become more productive. Yet, we do not view future productivity improvements that stem solely from a shrinking workforce as the most desirable objective. As an industry, we are determined that the retail jobs of the future, while fewer, will not only look very different to those of today, they will be higher skilled and better paid - and more productive.

A more holistic measure of productivity is now required. One that gives greater importance to the need for higher level skills and more creativity and judgement from employees than it does to a single headcount figure. This should be at the centre of a retail industry strategy for the next decade.

Your forthcoming Autumn Statement is an opportunity to work with the industry to shape the implications of the industry's transformation for the benefit of its customers, the workforce and the Government's productivity agenda.

HELEN DICKINSON OBE
Chief Executive
BRC

A RETAIL INDUSTRY STRATEGY

A new retail landscape is being created. Consumers are demanding more service, a more technologically-driven offer and more engagement and personalisation. New competitors are emerging from both within and outside the industry. And in a world where shopping is no longer synonymous with physical shops, what is the role of and the future for store networks? What are the skills needed in a "digital first" world? The future is uncertain, but we know that it will be different. There are four fundamental reasons why significant change in the industry is inevitable.

The effect of change could have profound impacts on communities, opportunities for people to progress and the availability of geographically diverse entry level jobs. At the same time, this presents an opportunity for the industry and government to come together and redefine the rules of the game. >>

SOCIAL

- As the largest and most geographically diverse private sector employer, the industry sustains local economies, spreads wealth and brings jobs to communities across the country
- Labour costs are set to rise more quickly while greater technological capability is available at lower cost, and we anticipate that the rate of store closures is likely to increase
- Our analysis suggests there could be up to 900,000 fewer jobs in retail by 2025 [1]
- This will impact unevenly across the country and on different groups of people
- The impact will be higher where economic growth is weakest, and the National Living Wage is highest relative to local median wages
- This in turn will impact on those more vulnerable in the workforce. As locality and flexibility are the most important reasons to work in retail, some people may be less inclined or able to take jobs with more travel or hours that don't work for them

FINANCIAL

- Costs are rising faster than the market is growing
- Competition is intense. Shop prices have been falling for over 3 years [2]
- Industry profitability has declined from net margins of 6-8% of sales pre-2007 to 3-5% today
- The annual cost of implementation of the National Living Wage is expected to be between £1.5bn and £3bn and Apprenticeship Levy between £140m and £160m from 2017
- Business rates continue to rise and by 2020 the retail industry burden will be £550m higher than in 2017
- The impact of these alone equates to 20 per cent of industry profitability and it is unlikely that additional costs will pass through into prices due to high levels of competition
- While the decline in retail productivity was less severe than in the rest of the economy and is now 15% above its pre-crisis peak, it is still 12% below where it would have been if it had continued to grow at its pre-crisis trend rate [3]

1 BRC - Retail 2020: Fewer but better jobs
2 BRC - Shop Price Index
3 Capital Economics and ONS

The strategy should be more ambitious than structured and effective dialogue. It ought to become a benchmark against which each proposal for policy and regulation can be tested. The strategy must have the industry's and Government's shared focus on enhanced productivity and the industry vision of better jobs[1].

The BRC is ready to work with the Government to develop a joint industry/ Government retail strategy.

1 As defined in BRC's Report, Retail 2020 Report 3: Solutions – the journey to better jobs, and committed to by over 40 companies employing over 1.2m people.

PEOPLE RELATED

- Throughout the 1990s about 15% of all employees and about a third of retail employees were on low pay. In the last few years the incidence of low pay in retail has risen faster than across the economy as a whole
- Around 1.5m people currently work in low paid roles in retail, of which 70% are female and one in five are recipients of means-tested working age tax credits[4]
- Retail now employs 100,000 people in types of roles that did not exist in 2011
- Many progress but others are 'stuck' on low pay or do not want to take more responsibility for the pay that is offered
- Retail employees are not a homogeneous group. Groups differ significantly in their needs, motivations and attitudes - a one size fits all approach by employers or policy makers will be ineffective
- Maximising the engagement, contribution and productivity of people will become even more crucial to future success as new and varied skills are needed

TECHNOLOGICAL AND STRUCTURAL

- The way people shop is changing. There are 40,000 fewer shops than there were in 2006 and approximately 15% of retail sales are online (and growing at 10-15% per year)
- Investment in digital is rising and investment in physical space is falling
- The rate of store closures will increase as more leases come up for renewal
- 60% of retail jobs are at a high risk of automation in the next 20 years, higher than any other industry[5]
- Physical retailing is changing and the role of the store is being re-imagined
- The ways shoppers might engage, even in the near team, cannot be anticipated with total certainty - not least because the technologies which could come to the fore may not even have been invented yet
- Growth in digital and the ubiquity of technology may adversely affect the number of jobs, but it also will make better jobs possible – requiring higher level of skills and more creativity and judgement

4 BRC – Retail 2020: What our people think
5 Deloitte: Transformers, 2016

DELIVERING ON BETTER PAY, PROGRESSION AND PRODUCTIVITY

Retail plays a central role in the UK's employment landscape. As the largest private sector employer, it provides jobs for three million people from a very broad range of backgrounds in a wide range of roles. More young people start their working life in retail than in any other industry – one in three employees is aged under 25 – and many go on to pursue long and rewarding careers both within the industry and the wider economy, using the skills and experience they acquired. The geographical reach of retail is also a significant benefit to the UK economy – providing employment opportunities in villages, towns and cities across the country.

Recent government initiatives on pay and apprenticeships have an important bearing on the industry given the transformation the industry is undergoing. We support the National Living Wage and recognise the objectives which have informed the development of the Apprenticeship Levy. At the same time, the significant additional costs associated with both policies are only sustainable if they actively support the industry in adapting to the structural change already in train.

In the case of the National Living Wage, we believe that some simple steps can provide much needed enhanced certainty and sustainability as the new statutory pay level is developed.

RECOMMENDATIONS

- For the coming year, take a moderate approach on increasing the National Living Wage, taking full account of current conditions and the outlook at the time of decision. Over the long term, this should mean a dynamic, rather than an absolute, target.
- The longer term goal should be to achieve the stated 60 per cent share of median earnings rather than a flat cash rate.
- The role of the LPC should be strengthened to enable it to make fully independent recommendations on the rate of increases, informed by all relevant factors based on full consideration of economic conditions and free from political intervention.

At the same time, it is apparent to industry that more changes to the design of the Apprenticeship Levy are necessary if the desired volume and quality of apprenticeships is to be met.

RECOMMENDATIONS

- Ensure an employer-led, industry specific solution to the Apprenticeship Levy.
- Give businesses more time to prepare, postponing the introduction of the levy and allowing more than 18 months to spend the Apprenticeship Levy funds.
- Measure outcomes not processes/inputs – specifically address concerns about Ofsted inspections and Skills Funding Agency registration.
- Ensure funds can be directed to the most valuable types of training – including Level 1 and internal training programmes.
- Ensure seamless integration of the approach in the devolved nations.

A SUSTAINABLE BUSINESS RATES SYSTEM

Retailers regularly review their property portfolios and consider the fixed costs including business rates to review profitability of individual stores to decide whether to open or close them. In a world where shopping is no longer synonymous with physical shops, many retailers are working through what the role of and the future for their store networks looks like.

The previous government published its Business Tax Roadmap before knowing the outcome of the EU referendum. It committed to reform some aspects of business rates which we welcomed. Although aiming to encourage investment, the Roadmap did not go far enough in addressing an unsustainable system that continues to discourage community level investment in local jobs and growth at a time when Government is seeking to ensure wealth and opportunity are spread more evenly across the country.

REDUCING THE BURDEN

The Treasury's signalling that the policy for deficit reduction and a budget surplus by 2019/20 has been modified is therefore welcome and provides an opportunity to undertake more meaningful change.

RECOMMENDATIONS

- Revisit the Business Tax Roadmap to deliver meaningful, fundamental reform which moves the UK away from having the highest commercial property taxation in Europe and across the OECD.
- Bring forward the switch to CPI indexation to 2017 and over time introduce a lower flat rate so that rates rise and fall in relation to property values aided by more frequent revaluations every three years.

INFRASTRUCTURE LEVY

Plans for elected mayors to propose an infrastructure levy up to two per cent of a property's Rateable Value if approved by Local Enterprise Partnerships (LEP) boards should be revised. Many combined authority boundaries take little account of LEP boundaries and LEPs do not effectively represent the diverse range of private sector views. LEP boards determining an additional levy leads to questions of accountability and transparency given they are not required to adhere to Freedom of Information Act or Code of Practice on Consultation.

RECOMMENDATION

- A more robust method of determining any levy would be to use a business ballot, allowing the impacted businesses a vote similar to what is used to successfully fund Business Improvement Districts.

CHECK, CHALLENGE AND APPEAL

It is essential each ratepayer pays their fair share – no more, no less. Plans to allow the Valuation Tribunal for England to only order a change in valuation if it is "outside the bounds of reasonable professional judgement" are counterproductive and create additional uncertainty for local government.

RECOMMENDATION

- Ensure a fair appeals system taking account of a property's Rateable Value, therefore, removing the proposed 'outside the bounds of reasonable professional judgement' clause.
- A more collaborative working relationship between the VOA and ratepayers where information and evidence can be shared and appeals avoided should be sought.

A FAIR BREXIT FOR CONSUMERS

Leaving the EU will have fundamental implications for regulation and other areas of public policy for years to come. Individual retailers will make their own assessment of what is best for their business, their staff and customers and whether leaving the EU on the final terms of the negotiations will provide better access to competitive retail markets in Europe and elsewhere, and access to the widest range of sustainable products to meet the demands of consumers globally.

Though the UK remains a full member of the EU for the time being, for retail some of these effects are already being felt and will require retailers and the Government to work together from the beginning of the withdrawal process. The following three areas deserve immediate consideration.

KEEPING PRICES LOW FOR CONSUMERS

Much of the discussion about the UK's future trading relationship with the rest of Europe has focused on British exports. However, the UK imports more from Europe than it exports to it, and it is on import trade where some of the most significant economic effects of Brexit could be felt. As one of the UK's largest importers retail is uniquely placed to lay out the consequences of this.

Membership of the EU provides benefits to UK traders including reduced rates of customs duty. In the case of trade within the EU, customs duties have been abolished altogether. Further afield, EU preferential schemes such as the Generalised System of Preferences (GSP) provide valuable trading benefits to developing countries and other bilateral trade agreements offer better trading opportunities with a range of more developed countries.

RECOMMENDATIONS

- If consumer prices are to be kept down, it is essential, then, that 'Brexit' imposes no new customs duties upon trade with the EU.
- MFN rates adopted by the UK once it leaves the EU should be broadly the same as those it applies as part of the EU [1].
- Government should start early on recreating the benefits of EU preference schemes such as GSP in relation to trade with developing countries.

A FAIR DEAL FOR EU COLLEAGUES

An estimated 100,000-200,000 people from other EU countries work in UK retail. These colleagues are concerned about their jobs and their livelihoods in the UK. They make a significant and valued contribution to the success of many retail businesses. The areas already being highlighted as concerns relate to digital talent, employees in distribution centres, in London and in parts of the supply chain, most notably in food. As responsible employers, our members have a duty to seek reassurance for these colleagues about their future.

RECOMMENDATION

- A clear, unambiguous statement from government that colleagues legally living and working in the UK shall continue to be able to do so following the UK's departure from the EU.

2 If MFN rates applied to the UK's trade with the EU it would have serious consequences for UK retail and for its customers. MFN duty rates are highest for essential consumer goods, in particular food and clothing. For example, the average MFN rate for clothing is up to 16% and meat is 27%.

FOCUS ON GROWTH

The transition of retail to higher productivity will require significant investment. Alongside which the challenging operating environment for retail has been exacerbated by the EU referendum result. The sharp devaluation of the pound has put upward pressure on import costs. This will increasingly squeeze margins as retailers seek to enter into new contracts with foreign suppliers over the coming months and fierce competition in the market makes it difficult for retailers to fully pass through any price increases to shoppers.

Against this backdrop and upward pressure on import costs, retailers need domestic policies that encourage and support growth - that benefits employer, employee and the customer - if they are to continue to make the investments needed to deliver productivity growth.

RECOMMENDATIONS

- The creation of new roadmap for beyond 2017 (when the current plan expires) for the roll out of widely accessible ultra-fast broadband, prioritising both business and consumer broadband access and connectivity.
- Local infrastructure initiatives (as well large scale projects) should be prioritised and easier routes for planning and decision making facilitated.
- Initiatives that enhance the competitiveness of UK businesses should be given priority and programmes that are in train that do not achieve this aim to be paused or scrapped altogether.

BREXIT: THE IMPACT ON RETAIL SPENDING AND SHOP PRICES

THERE HAS BEEN NO DISCERNIBLE IMPACT ON RETAIL SPENDING AND SHOP PRICES SINCE THE VOTE

- We have had three months of slow sales growth
- Retail sales were already slowing pre the vote as a result of a softening of the underlying drivers of spending, such as real wage and employment growth
- We are in the fourth year of falling shop prices as a result of intense competition and transformational change in the industry as consumers have access to more choices and greater ability to compare prices than ever before
- The rate of shop price deflation has not changed markedly since the vote
- At present it is difficult to link any impact on spending or prices to the referendum outcome, despite the best attempts of some

UPWARD PRESSURES ON SHOP PRICES ARE IN THE PIPELINE

- Some retailers face increases in input costs either now or the near future as they negotiate new contracts with foreign suppliers following the devaluation of the pound
- The data on imports show a clear jump in prices faced by UK businesses, particularly for non-food
- As they introduce stock bought post-referendum, retailers will have to decide how much of any increased cost to pass onto their customers
- The decision to pass on costs will not be an easy one. On the one hand, rising property and labour costs are already creating pressure points in many parts of the industry and the exchange rate movement only adds to the growing imperative to pass cost increases on. On the other hand, competition remains strong and many retailers may absorb much of the cost into their already squeezed margins in order to maintain their position in the market
- Overall, we expect some pass through to shop prices, probably focussed in the first half of next year, although those price increases are likely to be less dramatic than implied by the exchange rate movement
- This is the backdrop before considering any implications of any new tariffs that could arise depending on the exit route taken
- Hence the need for a negotiating strategy by government which is based on the need to keep consumer prices down

THE FUTURE IMPLICATIONS FOR RETAIL SPENDING WILL DEPEND ON WHAT HAPPENS IN THE WIDER ECONOMY

- The amount of money that consumers have available to spend is key to the future outlook along with their financial and job security
- Even before the referendum real wage growth had softened and, notwithstanding the outcome of the vote, most economists expected consumer spending and the economy as a whole to see a drop in the pace of growth from earlier expectations
- It is too soon to assess the knock on impacts on jobs and wages from any slowdown in business investment as we have yet to see hard evidence on the extent to which investment levels changed post June 23
- If GDP growth does slow to 0.7 per cent next year as independent forecasters are now on average, predicting, then that will be felt keenly by retailers
- We are in uncharted territory, Brexit was not a "normal" economic event so it's difficult to calibrate any model of the future with any confidence

RETAIL SALES

1% QTR 3

1.2% PREV. 12 MONTHS*

SHOP PRICE INFLATION

-1.8% QTR 3

-1.8% PREV. 12 MONTHS*

*JUNE 2015 - JUNE 2016

FALL IN

11% £: EUR:

12% £: $:

23 JUNE - 29 SEPTEMBER 2016

THE NEXT YEAR WILL BRING CHALLENGES FOR RETAILERS LOOKING TO KEEP PRICES LOW FOR THEIR CUSTOMERS AND THE VERY LAST THING THEY WILL NEED ARE FURTHER COST PRESSURES BOUGHT ON BY NEW REGULATORY BURDENS, SUCH AS NEW TARIFFS AND CUSTOMS RED TAPE. IT IS DIFFICULT FOR THE GOVERNMENT TO DIRECTLY AFFECT THE MACROECONOMIC CONDITIONS, BUT IT CAN AND MUST SEEK TO MINIMISE THE DISRUPTION AND COST DIRECTLY ASSOCIATED WITH THE BREXIT NEGOTIATIONS. WE STAND READY TO HELP THE GOVERNMENT IDENTIFY THESE POTENTIAL COSTS AND TO AVOID THEM.

THE RETAIL INDUSTRY'S CONTRIBUTION

40M

NO. OF CUSTOMERS

350M

TRANSACTIONS PER WEEK

41

MONTHS OF SHOP PRICE DEFLATION

£340BN

RETAIL SALES 2015

£43BN

ONLINE RETAIL SALES 2015

£200BN

GOODS FOR RESALE

£55BN

SERVICES SUPPORTED

3M

RETAIL WORKFORCE

THE BRITISH RETAIL CONSORTIUM

The BRC is the go to trade association for all UK retailers, delighting our members, promoting the story of retail, shaping debates and influencing the issues and opportunities that matter to the industry.

Our mission is to make a positive difference to the retail industry and the customers it serves. We stand for what is important to the industry and work in partnership with our members to shape debates and influence outcomes. We work with government to ensure a competitive market which creates the right conditions for growth and innovation, we champion great careers and we promote responsible retail's vital role in the community.

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