Opinion: The UK needs a new industrial strategy or it will lose the global green subsidy race

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UK businesses have criticized the government for the lack of a clear industrial policy. Industry body Make UK has warned the country "risks being squeezed" by US and EU green subsidy packages.

Outside the UK, industrial policy is back—and in a big way. Around the world, there has been a noticeable shift towards greater government intervention in the economy.

Recent shocks such as the COVID pandemic and the energy price spike arising from the Ukrainian war, have led to breakdowns in global supply chains and high inflation. In Europe and the US they also exposed fragility and a lack of resilience—especially in key areas such as energy security and the supply of medical equipment.

These governments seem to recognize the role of industrial policy in supporting domestic manufacturing to safeguard against future crises, reduce reliance upon Chinese imports, and in dealing with the climate emergency. They are also promoting industrial policies to enhance competitiveness, productivity and economic growth.

New industrial policies

The US has been the most prominent flag-bearer for these new industrial policies. President Joe Biden's 2022 Inflation Reduction Act (IRA) allocates almost US$700 billion (£555 billion) of federal funding over the next decade to support US industries, particularly healthcare, renewables and clean-tech sectors.

This includes subsidies and tax breaks to US manufacturers and consumers to encourage investment in, and use of, low carbon technologies (such as electric vehicles, heat pumps and carbon capture), as well as semiconductors. There are also new rules to encourage the use of local supplies to support US manufacturing.

The US has also recently enacted the Bipartisan Infrastructure Deal and the Chips and Science Act to boost transport and communication networks, and promote R&D, especially in regional high-tech hubs. Over the next decade, these three packages are expected to total over US$2 trillion of industrial policy support for US businesses.

Yet, there are concerns that these interventions are protectionist and violate rules set by the World Trade Organization (WTO)—the global body that oversees trade between countries—on procurement and subsidies by unduly favoring US firms. The EU has spoken out about the possible impact of the IRA on its own clean-tech industries, particularly in terms of harming its exports and diverting investment away from Europe.

The EU has also questioned China's industrial subsidies, possible infringements of intellectual property rights by Chinese companies, and the difficulties European businesses face in operating in China.

To combat these issues, the EU announced its own €250 billion (£217 billion) Green Deal Industrial Plan in February. This includes relaxing EU state aid rules to allow member states to fast-track investment in green sectors. The emphasis is on support for skills and supply chains, alongside smarter and simpler regulation.

A European Sovereignty Fund is also expected to offer subsidies for clean-tech innovation and infrastructure, while net-zero industry academies will train European workers for the green transition.

What about the UK?

One argument put forward for Brexit was that EU state aid rules stifle the ability of the UK to support its industries. But, post-Brexit, how has the UK responded? Its industrial strategy was scrapped under the Johnson government. And so far, there has been no policy response to either the US or EU packages.

Indeed, the UK's net zero initiatives to date have generally lacked sufficient funding. The Green Alliance think tank believes there is a £14.1 billion shortfall in low carbon infrastructure investment in the UK.

The UK's haphazard approach to net zero has also sometimes conflicted with other policies. For instance, the windfall tax on North Sea oil and gas firms applies to some wind and solar electricity generators, discouraging investment in renewables.

At the end of March, Jeremy Hunt said he would wait and see what the EU will do on its green industrial policy. It seems the UK position has been to watch as the action unfolds elsewhere—for example on attracting investment to build battery giga-factories. This is in stark contrast to the US and EU.

The Labour Party has promised to invest £28 billion a year through a dedicated green investment fund and transition program. This proposal has been cautiously welcomed by climate experts. But doubts remain about whether the speed and nature of Labour's proposals will be sufficient for a successful UK green transition.

Labour has also discussed a "Buy British" procurement policy. But this approach is also likely to fall foul of existing WTO rules and possibly the EU-UK Trade and Co-operation Agreement.

The green subsidy race

The UK needs to get serious about its own "Green New Deal" if it is to meet its net zero commitments, build low-carbon resilience in its energy supply, and compete with the US, EU and China.

Both the US and EU subsidy schemes should help to accelerate a much needed green transition. They will help to reduce barriers to clean-tech investment and innovation, create new jobs and generate greener growth in those regions. At a global level, this should accelerate decarbonization and the move to net-zero.

They could also create a green subsidy race—with UK not yet even at the starting line. There is a risk these subsidy schemes will stifle competition, raise global trade tensions and reduce opportunities for developing economies to grow their own clean-tech sectors.

They will also challenge the existing WTO framework and its rules to promote fair and free trade. This could lead to a major reset for the WTO. It may need to adopt a wider remit that aligns global co-operation on free and fair trade with that on climate action. Doing so would enhance the prospects of all countries in this race in delivering sustainable, inclusive and green growth.