UK POWERHOUSE

A report for Irwin Mitchell

Cebr

Economic Report

Supporting businesses across the UK

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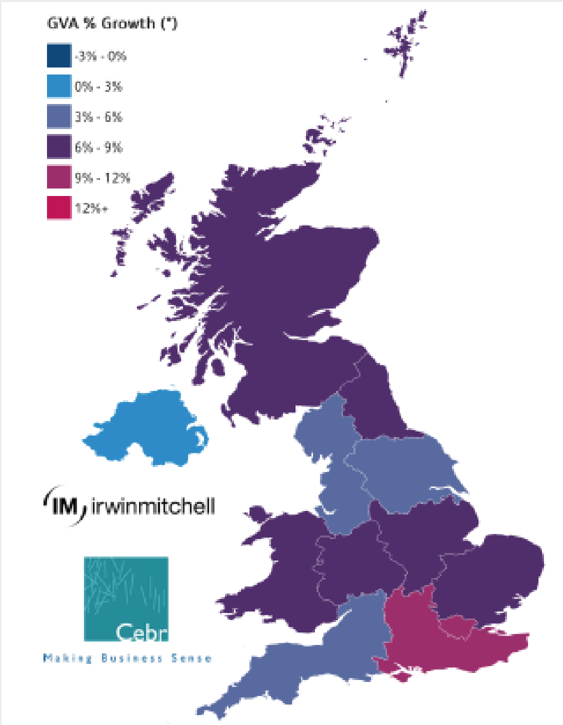
Powerhouse Tracker



UK Powerhouse is an extensive business study produced by Irwin Mitchell and leading economic thinktank Cebr.

This initial report analyses the causes of the economic disparities that exist within the UK and examines whether the Government's current wealth-spreading agenda will work.

The research incorporates a quarterly Powerhouse Tracker - a unique city-by-city 'nowcast' and 10 year forecast of economic strength based on detailed modelling of a range of timely indicators by Cebr, including local labour market data to provide statistics of output and employment.

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The results of the latest interactive Powerhouse Tracker can be viewed at www.irwinmitchell.com/ukpowerhouse

Authorship and acknowledgements
This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. The views expressed herein are those of the authors only and are based upon independent research by them.

London, November 2015

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Foreword

Since 2014, the UK Government has set out its plans to accelerate economic growth outside of London and the South East – particularly in the north of England.

This wealth-spreading agenda should of course be welcomed but it's fair to say that announcements such as the flagship 'Northern Powerhouse' initiative have led to a wide range of opinions and a certain amount of scepticism as to whether it can really make a difference.

At Irwin Mitchell, we've been following the debate closely and believe it's vital that the entire United Kingdom has the opportunity to flex its economic muscle. Not only do we want to see London continue to flourish, we also believe it's absolutely vital that the rest of the UK doesn't get left behind.

In order to assess whether the Government's aim of spreading wealth, jobs and economic growth can be achieved and what the likely impact will be, Irwin Mitchell has teamed up with leading economic consultancy, the Centre for Economics and Business Research (Cebr).

This comprehensive analysis includes predictions for how strong our major city and regional economies will be in the next 10 years, and in particular it provides a forecast as to whether the gap between London and the rest of the UK will shrink or get bigger.

As you will see, this unique tracker of UK economic power is already showing some fascinating results and it is something that we will be returning to on a quarterly basis.

In addition to this analysis from Cebr, the report incorporates the findings from an Irwin Mitchell-commissioned YouGov survey of 1,000 organisations. This research investigates the opinion of business and what senior decision-makers would most like to see to improve economic growth in their region.

We hope that you find our 'UK Powerhouse' report valuable and I look forward to receiving your feedback in the near future.

Niall Baker
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Supporting economic strength and bridging the prosperity gap

Executive Summary

This report examines the economic performance of the UK's regions and cities and considers what policymakers need to do to prevent a widening gap in prosperity across the country. The research is informed by a wide range of datasets, Cebr's forecasts and models, and a YouGov survey of 1,000 UK businesses commissioned by Irwin Mitchell.

The key findings of the report are:

- **Economic activity per person is considerably higher in London compared with the rest of the UK.** In fact, of the 12 regions of the UK, seven have less than half the Gross Value Added (GVA) per head of the capital. These seven are made up primarily of Northern regions, which on the whole lag behind their Southern counterparts.

- **Cebr forecasts that between 2014 and 2025, GVA in London may grow by 31%.** This compares with growth of just 12%, 14% and 16% in Northern Ireland, Wales and the North East of England respectively.

- **London's economy is currently around six times the size of Greater Manchester,** while Inner London alone is just under 10 times the size of Birmingham.

- **In the second quarter of 2015, Cambridge was the fastest growing city economy in the UK, closely followed by Milton Keynes and London.** Middlesbrough and Hull were among the five slowest growing, implying that the gap between these cities and wealthier cities will widen.

- **The differences in economic performance across the regions have a number of causes,** ranging from differences in the industries that operate in the regions, to variations in skills and the level of government investment in infrastructure.

- **London has not only attracted higher levels of infrastructure investment over the past decade but also has a considerable amount more planned in the pipeline compared with other regions.** Analysis by IPPR shows London's per capita publicly supported infrastructure spending projected at £5,426 per resident. Investment in the North West region is estimated to be £1,248 per person, while Yorkshire and the Humber sees £581 per person and the North East only £223 per person.

- **Despite all the rhetoric around building a Northern Powerhouse, a net balance of businesses surveyed in the North disagreed that the government was doing enough to support regional economic growth.** In contrast, a net balance of businesses in London and the Midlands agreed that they were doing enough.

- **Close to half (48%) of businesses surveyed agreed that further devolution of powers would boost regional economic growth, while just over a fifth (22%) disagreed.** The remainder of businesses neither agreed nor disagreed, or "did not know". Belief in devolution was strongest in the North of England, with close to three fifths (59%) of businesses agreeing that it could boost economic growth in the region.

- **Over half of businesses surveyed felt that local determination of business rates could boost economic growth in their region.**

- **Improving road and telecommunications infrastructure were the most frequently cited policies for boosting economic growth among the businesses we surveyed.** Improving local rail services and more home building programmes were also relatively popular answers.

- **Over a fifth (22%) of the London businesses we surveyed thought that more homebuilding was the number one policy for boosting economic growth in the capital –** more popular than any other policy.

The report recommends a number of policy measures to narrow the regional divides in economic performance, and to ensure continued growth in existing powerhouses such as London:

1. **Further devolution of policies to cities, regions and local authorities** – including the ability to set business taxation at a local level.
2. **Rethinking transport policy with a greater emphasis on local rail and roads** – these infrastructure projects would yield significant economic benefits far in excess of their costs.
3. **Introducing a regional Living Wage** – replacing the proposed National Living Wage with a regional Living Wage would protect jobs and ensure a consistent standard of living for lower earners across the UK. The current National Living Wage proposals are set to lead to a loss of 60,000 jobs due to the increased wage bills businesses will face.
4. **Take further steps to reform business rates and also consider a land value tax** – More regular revaluations might help struggling areas to better attract and retain businesses. A land value tax – an annual charge on the rental value of land rather than property – could be explored as an alternative to business rates and other property taxes in the future. Unlike business rates, it would encourage entrepreneurial activity on land, as well as housebuilding. It would discourage unproductive use of land.
5. **Tackling housing shortages** – building on some greenbelt land, densifying existing urban areas and eliminating planning restrictions further should all be explored to help solve the UK's housing crisis.
6. **The introduction of tax competition across regions** – allowing regions to compete on various taxes would allow regions to better attract business investment and top talent.
7. **Greater involvement of businesses in local education policy** – this would better align skills provision with local job vacancies.
8. **The establishment of more industry clusters/ enterprise zones around UK universities** – this would generate concentrations of fast-growing industries around universities and prevent a brain drain of graduate talent to London and the South East.
9. **The devolution of Air Passenger Duty (APD) in England** – Regional airports in England have expressed concern about the impacts of APD devolution to Scotland and Wales on their business. Specifically, they are concerned that a decision to lower APD rates in Scotland or Wales could draw passengers and airlines away from their airports. Devolution of APD would allow councils in England to compete on APD. By offering lower APD, demand for use of regional airports would increase and this would support aviation activity in these parts of the UK.

Introduction

After being severely hit by the financial crisis and the limp recovery which initially followed, the UK economy has turned a corner. Last year and 2015 have seen the country among the fastest growing major advanced economies in the world, with consumer spending and business investment supporting GDP.

However, this growth is not evenly distributed. Too much economic activity is driven by London and the South East. This is creating huge distortions and negative consequences – a brain drain to the South of England, congestion in economically successful areas and soaring house prices, to name a few.

London is an economic powerhouse and policymakers should continue to support the capital's crucial contribution to the UK's prosperity. But more should be done to spread wealth and job opportunities across the country. As data in this report show, the UK is unique among European countries in terms of its overdependence on its capital city. Our forecasts suggest that the economic gap between London and the rest of the UK is set to widen over the next 10 years.

There are success stories outside the South of England. Manchester, Birmingham, Leeds and Glasgow all make sizeable contributions to UK GDP, for example.

But more needs to be done to support these economic powerhouses and spread prosperity across the UK. The government's Northern Powerhouse agenda is a start, but it does not go far enough and at times has seemed like little more than empty rhetoric.

This report for Irwin Mitchell examines the economic performance of the UK's regions and cities, the reasons for these differences in performance and considers what policymakers need to do to prevent a widening gap in prosperity across the country.

The structure of this report is as follows:

- Section 1 considers the size of the gap in economic performance across the UK.
- Section 2 considers some of the reasons for the gaps in economic performance.
- Section 3 considers the appropriate policy response to regional economic inequality.
- Section 4 draws conclusions from the preceding analysis.

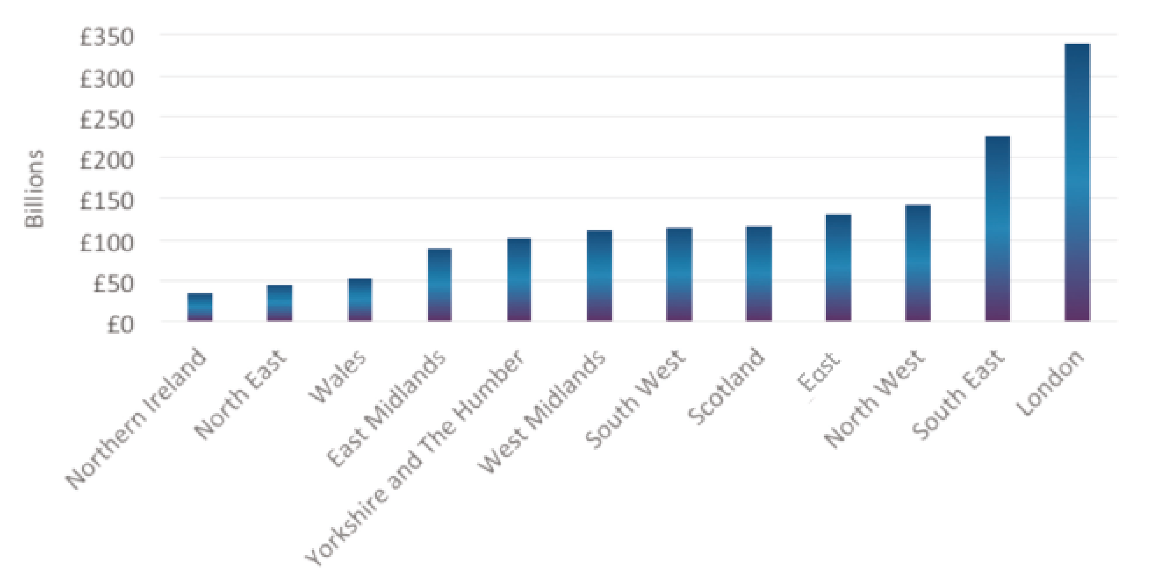
1 Regional divisions across the UK

There are considerable economic disparities across the UK and differences in the economic performance of the various regions have been in the spotlight for some time. This section will explore the sizeable gaps in prosperity that exist and considers whether regional disparities are set to narrow or widen over the coming years.

1.1 Gross Value Added

Gross Value Added (GVA) is a measure of the value of goods and services produced across a given area and is a key measure of the contribution that a region or city provides to overall UK Gross Domestic Product (GDP).

Figure 1 – Total GVA by region in 2013, current prices



Source: Office for National Statistics

As shown in Figure 1, London and the South East comfortably provide the largest contribution to the UK economy of all the regions. Despite accounting for less than 1% of the UK's land mass, nominal GVA in London in 2013[1] was over £338 billion, nearly a fifth (17%) greater than the value of goods and services produced in the entire North of England (North West, North East and Yorkshire and Humber). Combined, London and the South East account for more than a third (37.7%) of the total GVA across the UK.

[1] This is the latest year for which official data are available.

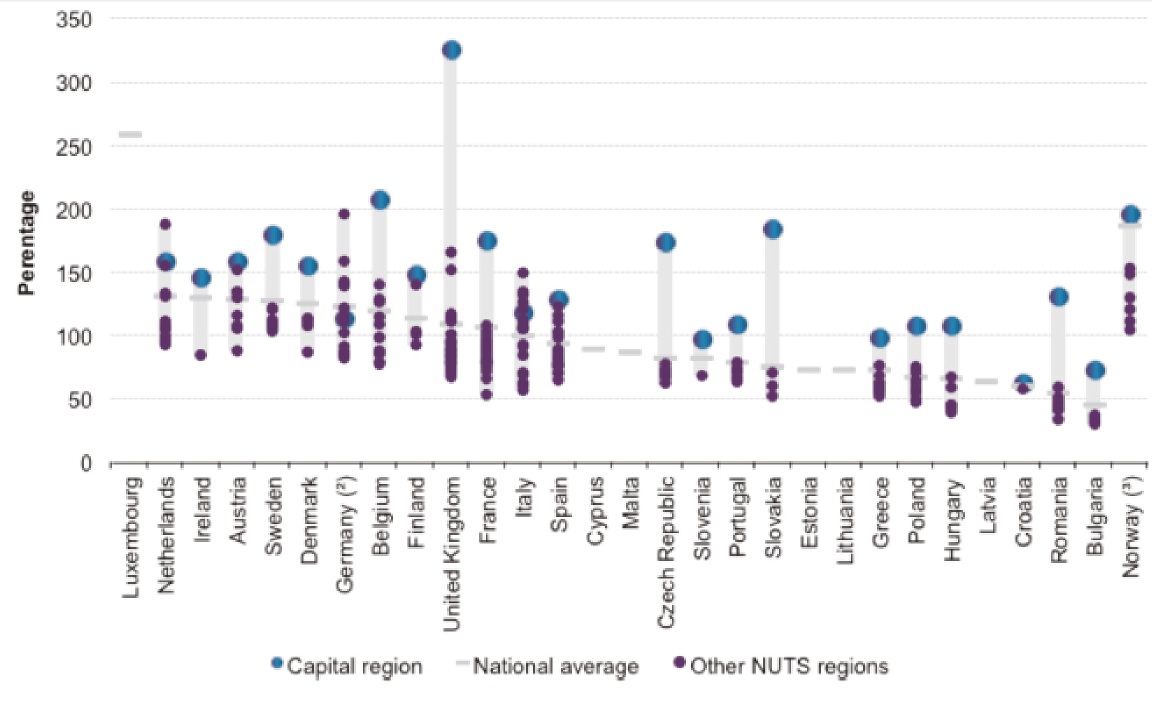
While differences in total GVA can reflect differences in the size of the workforce in each region, it is clear from Figure 2 that economic activity per person is considerably higher in London compared with the rest of the UK. In fact, of the 12 regions of the UK, seven have less than half the GVA per head of the capital. Further, outside of Scotland, these seven are made up primarily of Northern regions, which on the whole lag behind their Southern counterparts. The North West's £19,937 per head remains some way below the lowest ranked region in the South of England, the South West at £21,163.

Figure 2 – GVA per head by region in 2013, current prices

Source: Office for National Statistics

The disparities between the countries and regions of the UK are concerning when contrasted with the regional picture seen across Europe. The disparity between the regions of the UK is far greater than that seen in any other country in Europe, as shown in Figure 3.

Figure 3 – Regional disparities in GDP per head by NUTS 2[2] region, 2013 (% of EU-28 average, purchasing power standard)

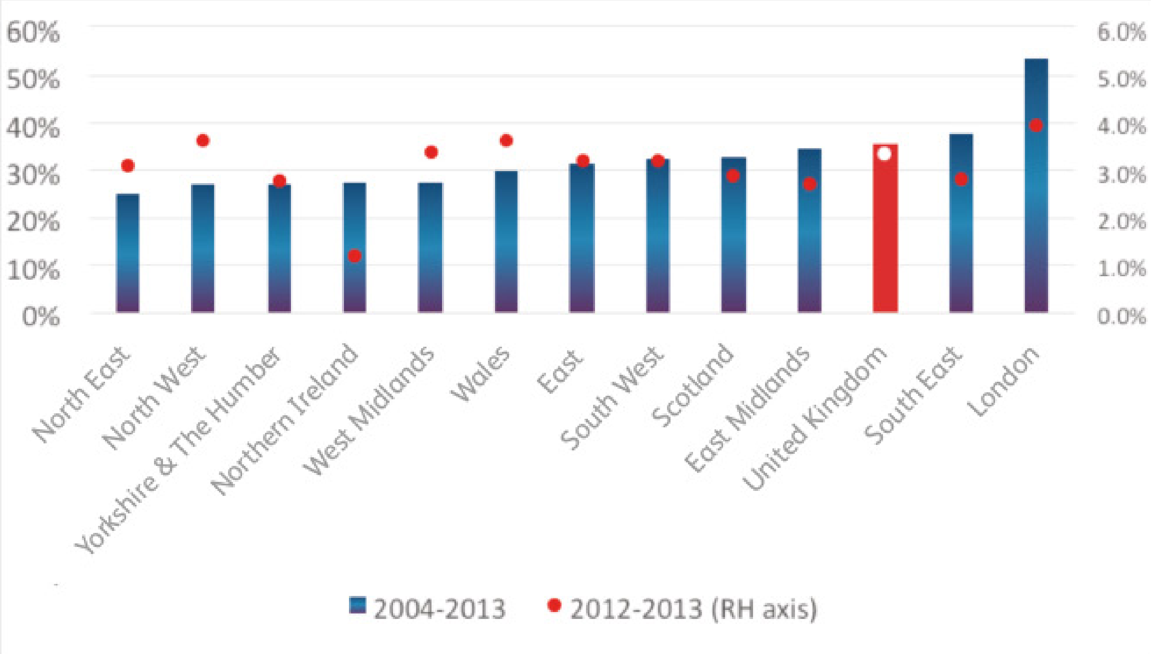


Source: Eurostat

While the great divide between economic activity across the UK's regions is concerning in itself, the issue is compounded by the fact that growth in the most prosperous areas has outstripped that of other regions over the past 10 years – leading to a widening in the gap in prosperity. For instance, London has grown nearly twice as fast as regions such as the West Midlands and the North of England as a whole.

[2] *Broadly speaking data at county level.*

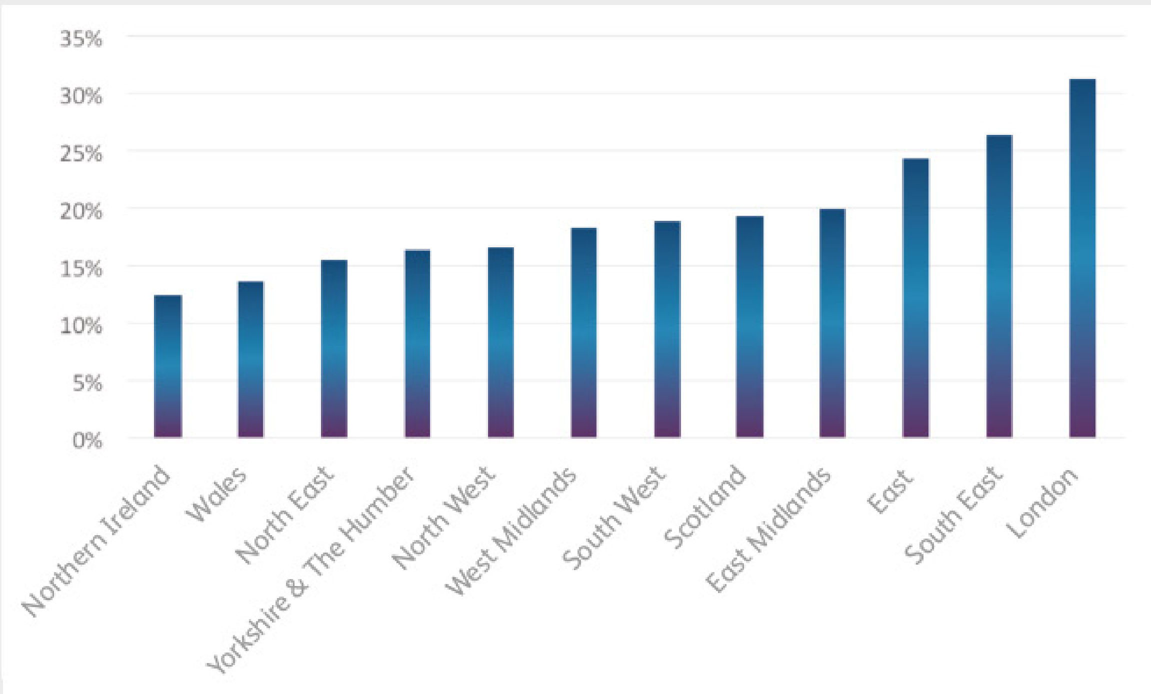
Figure 4 – Total GVA growth



Source: Office for National Statistics

Cebr forecasts a continuation of these trends, as shown in Figure 5. Between 2014 and 2025, GVA in London is forecast to grow by 31 %. This compares with growth of just 12 %, 14 % and 16 % in Northern Ireland, Wales and the North East of England respectively.

Figure 5 – Cebr forecast for GVA growth by region, 2014-2025



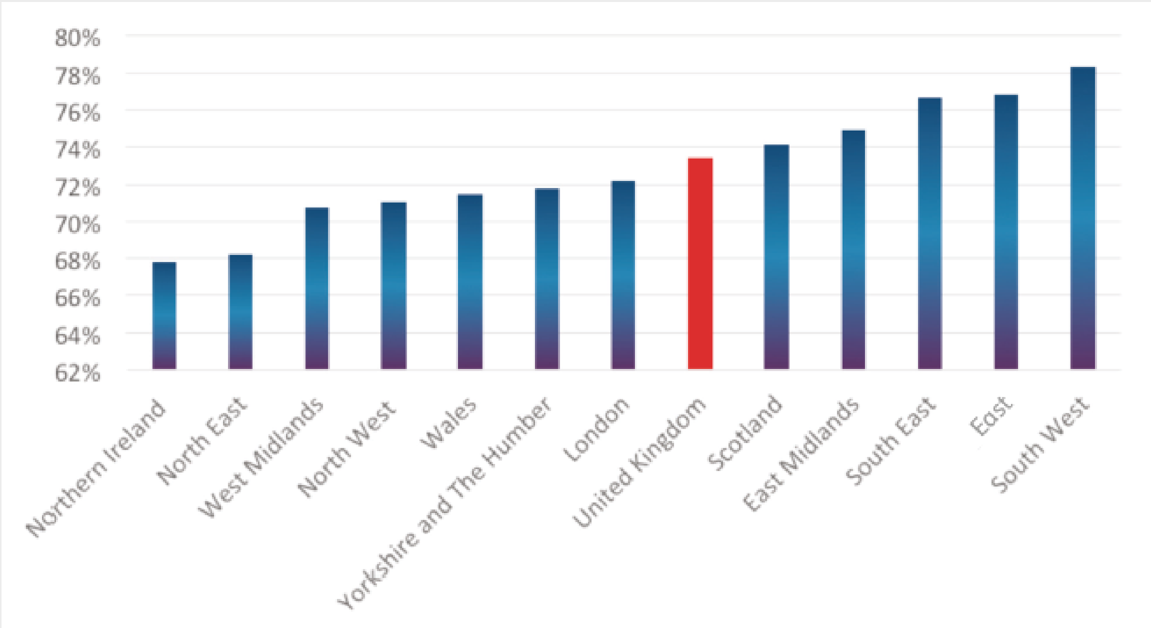
Source: Office for National Statistics, Cebr analysis

1.2 Job creation and earnings

Vast differences in economic performance lead to wide variation in employment prospects and household incomes.

As Figure 6 shows, in Q2 2015 the South East, East of England and South West had employment rates of over 76 % compared with rates of around 68 % in Northern Ireland and the North East.

Figure 6 – Employment rate by region (April – June 2015, working age population)



Source: Office for National Statistics

Differences in both the strength and composition of regional labour markets across the UK have notable impacts on the earnings of the workforce in each area. While London doesn't have the highest employment rate, the typical worker in the capital is paid considerably more than workers in other regions of the UK. The typical employee in London earned £30,338 in 2014, over 30 % higher compared to the next highest region, the South East, where the average worker earned £23,191.

Outside of London, the South East, East of England and Scotland, earnings were fairly even across the regions of Great Britain, with median pay around the £20,000 mark. However, pay levels were more subdued in Northern Ireland, where the typical worker earned £18,764 – just over 60 % of the median level in London.

Differences in earnings between regions are partly reflective of higher living costs in some areas and, as such, the financial impact of these changes on household budgets and spending power may not be that notable. For instance, in the three months to July 2015, average monthly residential rental values in London (£1,538) were more than double that for the rest of the UK (£761[3]) . However, even accounting for the differences in the costs of essential items in each of the regions, it is clear that households in London have significantly higher levels of purchasing power compared with other parts of the country.

The Asda Income Tracker, which measures the 'discretionary income[4]' of households across the UK, shows that the spending power of the average household in London, the South East and East of England is considerably higher compared with other regions of the UK. As shown in Figure 8, average household discretionary income tops £200 per week only in the aforementioned regions. Most other regions ranged between £160 - £170 per week while households in the North East and Northern Ireland had just £125 and £95 a week respectively. Between 2014 and 2015, discretionary incomes rose across all regions, supported by a pick-up in wage growth and a prolonged period of low inflation. However, in absolute terms, London has moved further ahead of the rest of the UK, with spending power rising by £22 a week between Q2 2014 and Q2 2015 compared with £18 a week for the UK as a whole.

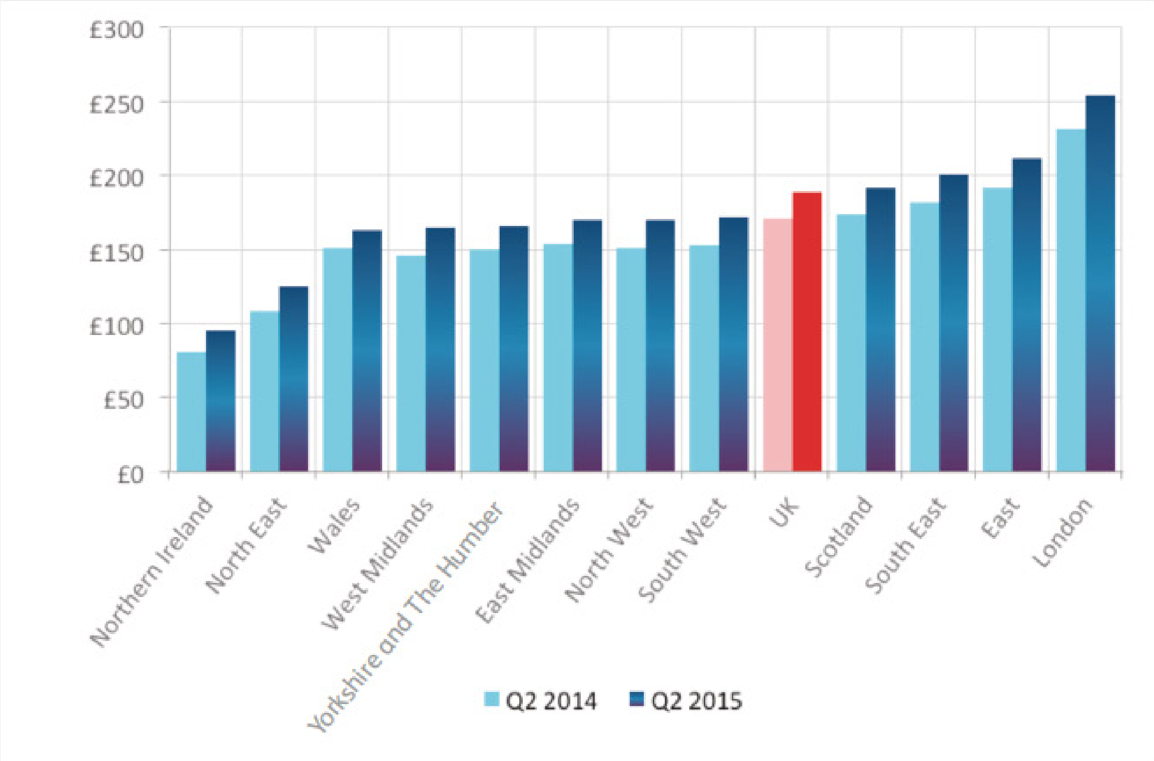
[3] HomeLet Rental Index – July 2015

[4] Reflects the amount remaining after the average household has had taxes subtracted from their income and bought essential items such as: groceries, electricity, gas, transport costs and mortgage interest payments or rent.

Figure 7 – Median annual earnings by region, 2014 (current prices)

Source: Office for National Statistics

Figure 8 – Average household discretionary income by region, £ per week



Source: Asda Income Tracker

1.3

City Regions

The prospects for key cities have long played an important role in the economic performance of the various regions of the UK and with economic activity becoming increasingly concentrated in these hubs, cities are ever more important as a source of growth for the UK's regions. As a result, it's important to consider these city economies when examining differences between the regions. However, official economic data sources for the UK's cities are often dated – the last set of regional economic accounts corresponds to the economy in 2013.

To more accurately estimate current economic activity, Cebr has utilised a range of more timely indicators to create a 'nowcast' of GVA and employment for a range of key cities across the UK. The latest outputs give us a picture of how the regional economies of the UK are performing in 2015.

Table 1 (pages 16-17) highlights the sheer scale of London in contrast to other cities across the UK. London's economy is currently around six times the size of Greater Manchester, while Inner London alone is just under 10 times the size of Birmingham. While employment in the capital is considerably higher when compared with other large cities such as Birmingham, Leeds and Manchester, this does not solely account for the divide between the sizes of these economies, with each worker in Inner London producing about 83 % more than their counterparts in Birmingham (in terms of GVA per worker).

The regional divide highlighted earlier is further underlined by the differences in current estimates for economic growth in each city. As shown in Figure 9 (page 17), Cambridge, Milton Keynes and London are growing faster than cities elsewhere in the country. These economies have been supported by strong growth in sectors such as business services over the past year and, to varying extents, knowledge-based industries such as website/application developers and biotech research. On the flip side, growth in Belfast has been weighed down by the laggard economic recovery in Northern Ireland, which has struggled in the face of public sector austerity and against a more competitive corporate tax regime in the neighbouring Republic of Ireland.

Hull has similarly been weighed down by cuts to the public sector and relatively weak growth in its chemical and manufacturing industries. The presence of Middlesbrough, Hull and Swansea in the bottom five is concerning and implies that the gap between these cities and wealthier cities is continuing to widen. Over the past 10-years each of these economies has fallen in terms of its relative position compared with other cities. Alongside Coventry, which has fallen five places on the back of the continued decline of its automotive and machine tool manufacturing base, Sunderland, Hull and Swansea are some of the largest fallers, dropping 4, 3 and 3 places respectively. Similarly, Middlesbrough stands as the smallest of the city economies tracked and has fallen further behind Bournemouth over the last 10 years. However, it is clear that a number of cities outside of London and the South East have performed relatively strongly over the past year and while they have failed to move higher relative to other cities over the past 10-years, they have the potential to make up some ground under the right economic conditions alongside a supportive policy environment.

Table 1 - City economic league table, Q2 2015

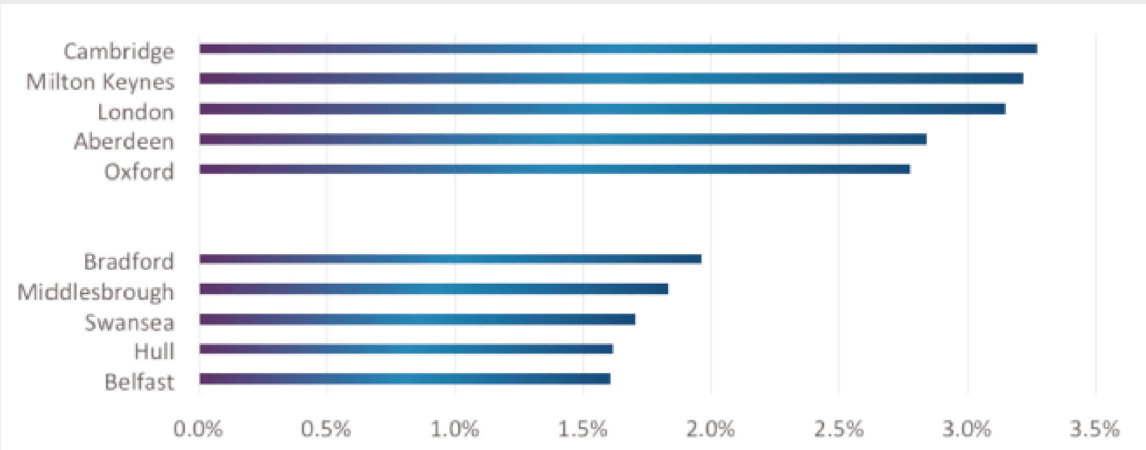
City name	Region	GVA, £millions (Q2 2015, annualised)[5]	Employment (Workplace measure, (Q2 2015)	GVA per employee (Q2 2015)	Change in position since Q2 2005
London	London	£349,668	4,836,525	£72,297	-
Inner London		£244,438	3,138,777	£77,877	-
Outer London		£105,231	1,697,748	£61,983	-
Greater Manchester	North West	£57,649	1,244,319	£46,329	-
Birmingham	West Midlands	£24,552	578,399	£42,449	-
Leeds	Yorkshire & The Humber	£20,899	398,866	£52,397	-
Manchester	North West	£20,647	430,040	£48,011	↑ x1
Glasgow	Scotland	£19,629	420,739	£46,654	↓ x1
Edinburgh	Scotland	£18,945	338,311	£55,999	-
Bristol	South West	£12,942	328,893	£39,350	-
Aberdeen	Scotland	£12,042	191,060	£63,029	↑ x6
Sheffield	Yorkshire & The Humber	£11,422	290,782	£39,282	↓ x1
Liverpool	North West	£10,834	266,286	£40,684	↓ x1
Belfast	Northern Ireland	£10,434	128,937 [6]	N/A	↓ x1
Milton Keynes	South East	£10,056	163,910	£61,353	↑ x4
Cardiff	Wales	£9,682	209,718	£46,167	↓ x2
Newcastle	North East	£9,029	225,096	£40,110	↓ x2
Nottingham	East Midlands	£8,947	228,415	£39,172	↓ x2
Bradford	Yorkshire & The Humber	£8,877	213,178	£41,639	↓ x1
Cambridge	East of England	£8,495	134,674	£63,082	-
Oxford	South East	£7,729	124,372	£62,140	↑ x2

[5] Constant 2012 prices
[6] Employment data for Belfast not comparable with other cities as not based on workplace analysis of labour market statistics

Derby	East Midlands	£7,152	146,489	£48,821	↑ x3
Leicester	East Midlands	£6,985	190,006	£36,760	↓ x1
Coventry	West Midlands	£6,897	164,368	£41,962	↓ x3
Norwich	East of England	£6,876	117,940	£58,300	↓ x1
Brighton	South East	£6,537	141,732	£46,122	↑ x2
Southampton	South East	£5,752	153,074	£37,579	-
Portsmouth	South East	£5,292	115,878	£45,666	↑ x3
Plymouth	South West	£5,249	141,973	£36,969	-
Sunderland	North East	£5,233	115,290	£45,387	↓ x4
Peterborough	East of England	£5,094	110,071	£46,282	↑ x2
Wolverhampton	West Midlands	£4,985	112,522	£44,304	-
Hull	Yorkshire & The Humber	£4,925	133,809	£36,807	↓ x3
Stoke-on-Trent	West Midlands	£4,709	107,091	£43,971	↑ x1
Bournemouth	South West	£4,513	94,716	£47,652	↑ x1
Ipswich	East of England	£4,261	75,990	£56,068	↑ x1
Swansea	Wales	£4,239	120,732	£35,109	↓ x3
Middlesbrough	North East	£3,301	68,264	£48,355	-

Source: Office for National Statistics, Cebr analysis

Figure 9 – Five fastest and slowest cities by annual GVA growth, Q2 2015



Source: Office for National Statistics, Cebr analysis

While each city economy appears to have been firmly in recovery over the past year, not all the cities have yet managed to recover to their pre-crisis levels. In contrast with the UK as a whole, output in real terms in nine cities in the 12 months to Q1 2015 remained below the level recorded in the same period to Q1 2008.

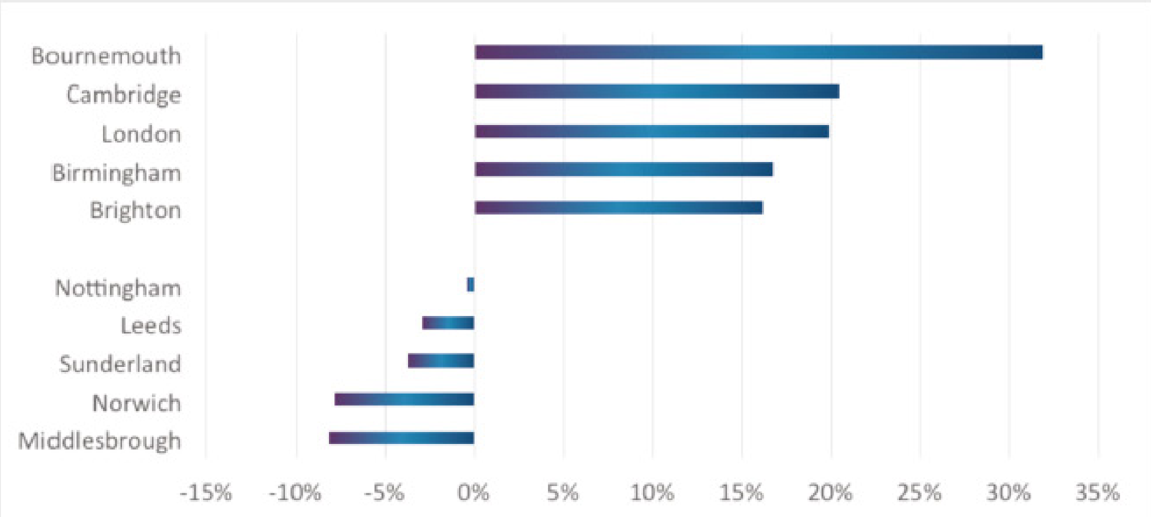
Table 2 – City GVA compared with pre-crisis levels

City Name	Percentage change in GVA between 12-months to Q1 2008 and 12-months to Q1 2015
Sunderland	-8.3 %
Hull	-5.9 %
Southampton	-5.4 %
Leeds	-5.3 %
Middlesbrough	-4.6 %
Bradford	-4.0 %
Cardiff	-2.7 %
Peterborough	-1.7 %
Belfast	-0.3 %

Source: Office for National Statistics, Cebr analysis

As shown in Table 2, excluding a couple of exceptions, the underperforming economies are concentrated in the North of England and devolved nations of Wales and Northern Ireland. Over the same period, a number of cities have seen the level of economic output increase by over 10 % . Despite the prevalence of financial services, Inner London has seen an increase of around 14.6 % between Q1 2008 and Q1 2015 supported by both the recovery of its key service industries and the emergence of its 'Flat-White Economy' of media, internet and creative businesses.

Figure 10 – Percentage change in employment (Q1 2008 – Q1 2015)



Source: Office for National Statistics, Cebr analysis

Although the labour market has seen some quite considerable changes since the beginning of the financial crisis, changes in employment from pre-crisis levels give some indication of activity across the cities following the financial crisis. The presence of economies such as Sunderland and Middlesbrough in the bottom five for both GVA and employment growth over the past decade is concerning, particularly given the increasing focus on improving prospects in these regions.

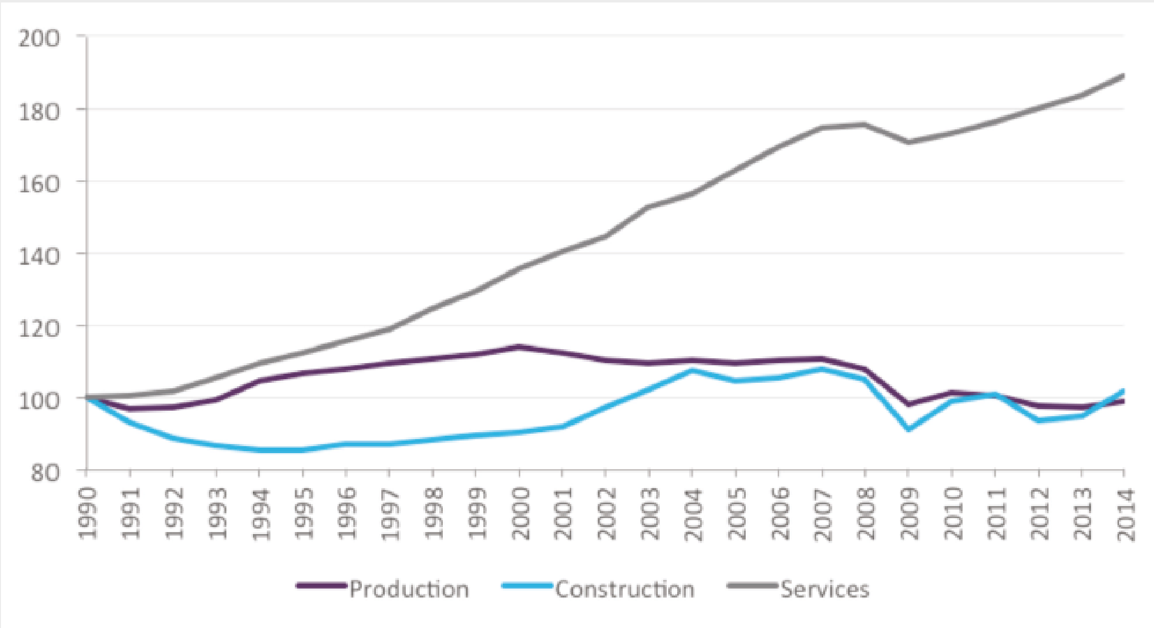
2 Causes of regional disparities

The differences in economic performance across the regions have a number of causes, ranging from differences in the industries that operate in the regions, to variations in skills and the level of government investment in infrastructure.

2.1 Differences in the sector mix

At the UK level there have been substantial differences in the performance of the different sectors of the economy both since the financial crisis and over a greater period of over four decades. Manufacturing, which accounted more than 30 % of the UK's economic output in the early 1970s, now accounts for less than 10 % of output. Instead, UK economic growth has been centred on the rise of the service sector. Between 1990 and 2014, output in the service sector increased by over 88 % and the sector now accounts for around 80 % of total UK economic output. Over the same period, output in the other two key sectors of the economy, production (which includes manufacturing, energy and mining) and construction, is relatively unchanged in real terms.

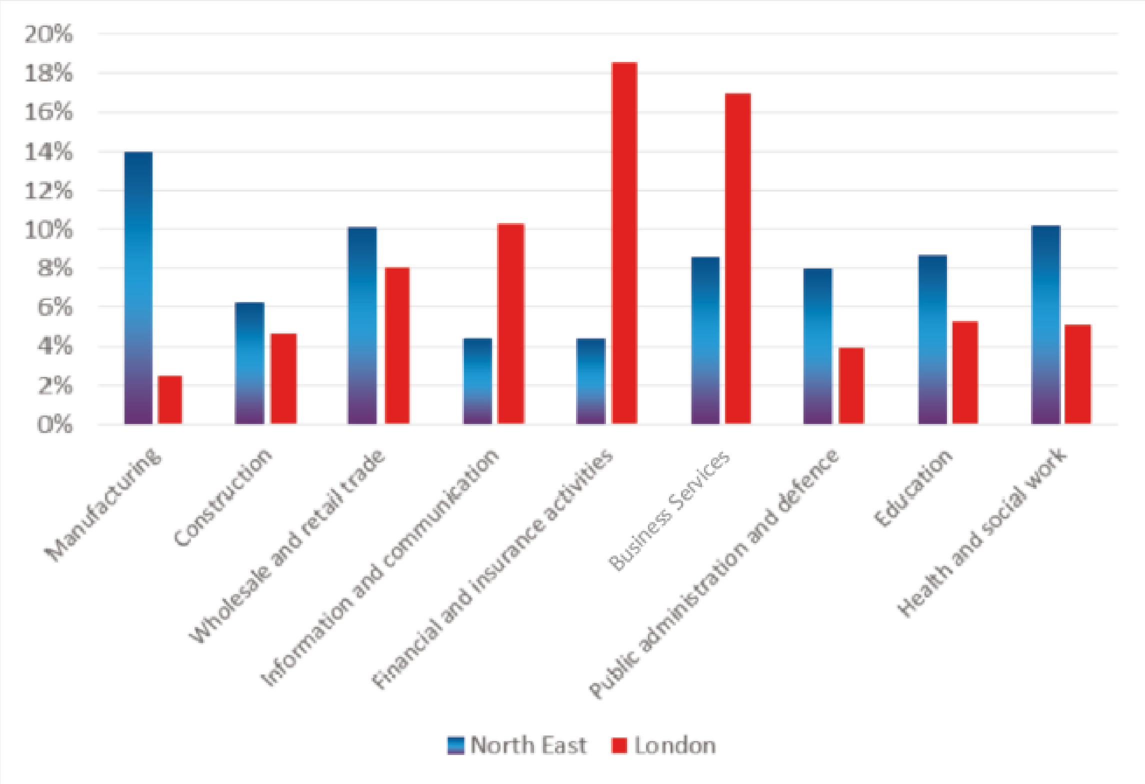
Figure 11 – UK economic output by sector (100 = 1990)



Source: Office for National Statistics, Cebr analysis

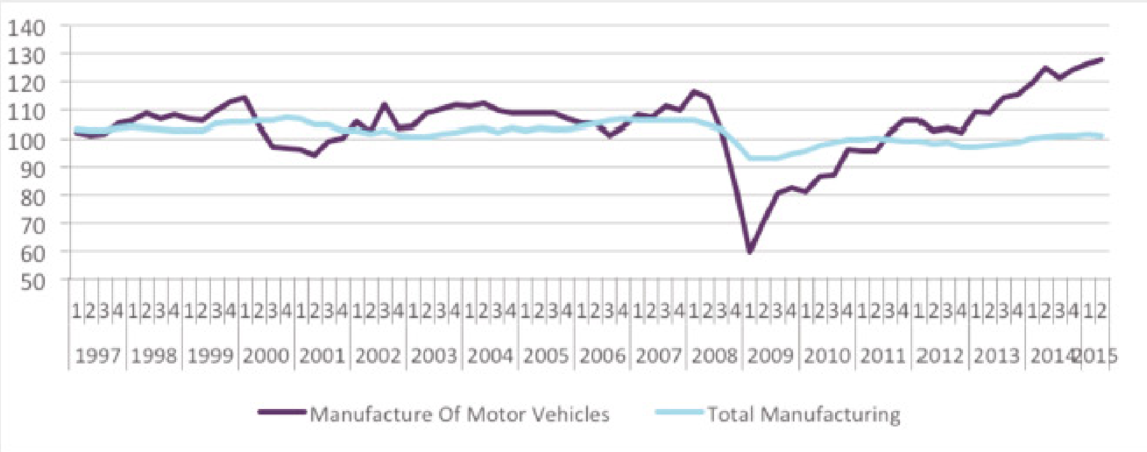
The slimming of the UK's industrial base and continued sluggish performance of sectors such as manufacturing has no doubt played some role in the growing divide that has developed across the regions. Areas such as London and the South East have heavily benefitted from the boom in service sector activity while regions such as the North and the Midlands have been considerably more exposed to weakness in the production industries. Manufacturing accounts for 14 % of economic output in the North East compared with less than 3 % in London.

Figure 12 – Sector contributions to regional GVA, 2012 (share of total)



Of course, not all components of manufacturing have performed poorly over the last couple of decades. For example, the motor vehicle manufacturing industry has been an important source of growth and employment in several regions. Especially in the post-financial crisis period, automotive manufacturing has performed far more strongly than the overall sector, as shown in **Figure 13**.

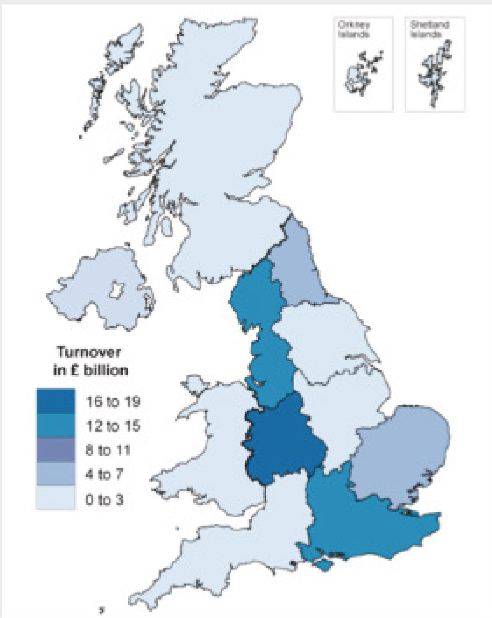
Figure 13 - Manufacturing output, indexed so that 2011=100



Source: Office for National Statistics

On a turnover basis, the regions that have seen the most automotive manufacturing activity are the West Midlands, London, the South East, and the North West.

Figure 14: Automotive manufacturing turnover, 2013, by region



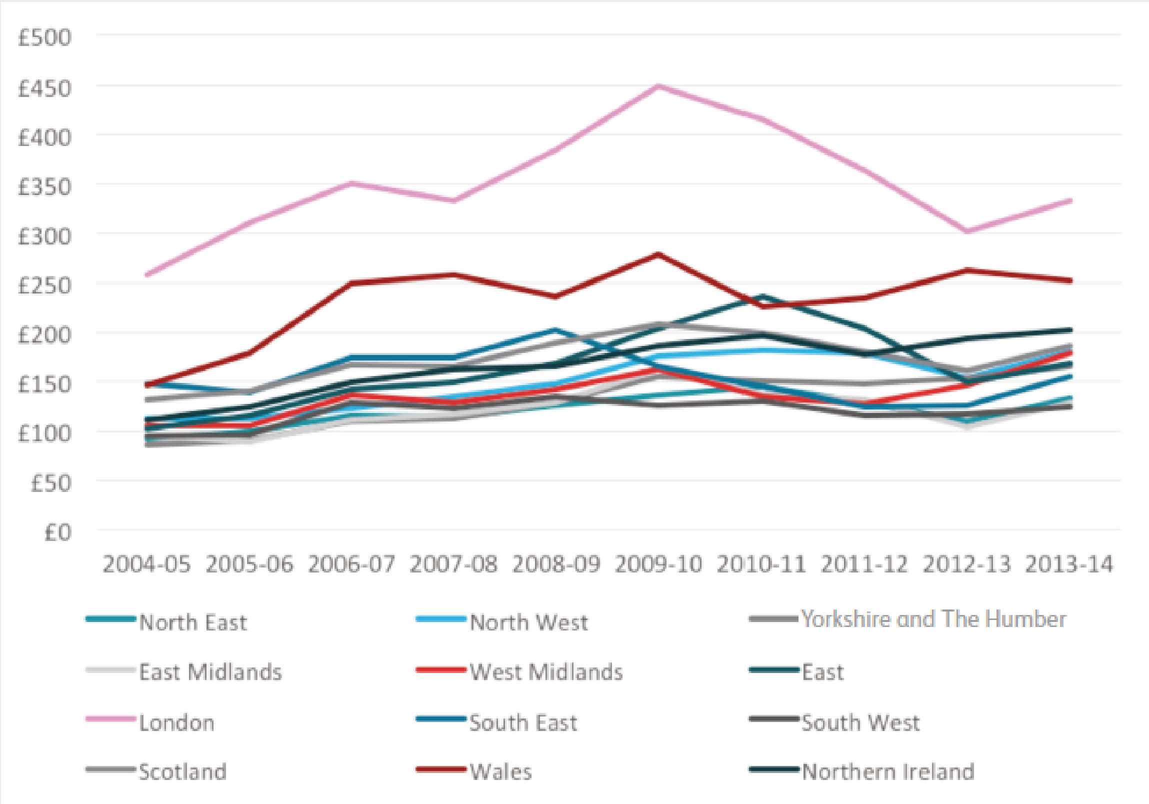
Source: Office for National Statistics

2.2 Infrastructure and investment

One factor contributing to the regional imbalance in economic performance across the UK is distinct variations in the quality and level of investment in infrastructure. Spending on transport dominates public investment on infrastructure and plays a vital role in economic prospects, linking together various factors of the production process and widening access to other markets.

Public sector investment in infrastructure is an important driver of overall infrastructure investment, helping to leverage investment from the private-sector. As such, regions that see higher levels of public infrastructure investment are likely to see higher levels of total spending on infrastructure. Looking at public capital spending on transport projects per head, the differentials between most regions are relatively small. However, it is clear in Figure 15 that public investment into transport in London far outweighs that seen in other regions.

Figure 15 – Public sector capital spending per head on transport projects (current prices)



Source: HM Treasury, Cebr analysis

London has not only attracted higher levels of infrastructure investment over the past decade but also has a considerable amount more planned in the pipeline compared with other regions. While not all the financing in the government's infrastructure plan is from the public purse, the £14.5 billion of capital expenditure planned for London's Crossrail scheme far outweighs the £1.1 billion outlined for the North of England rail programme.

Analysis by IPPR shows London's per capita publicly supported infrastructure spending projected at £5,426 per resident[7]. Investment in the North West region is estimated to be £1,248 per person, with much of that being channelled into the Sellafield decommissioning, while Yorkshire and the Humber sees £581 per person and the North East only £223 per person[8]. The disparities within the current infrastructure plans only act to boost the attractiveness of London and the South East to businesses, attracting further private investment and jobs in these regions at the expense of other parts of the UK.

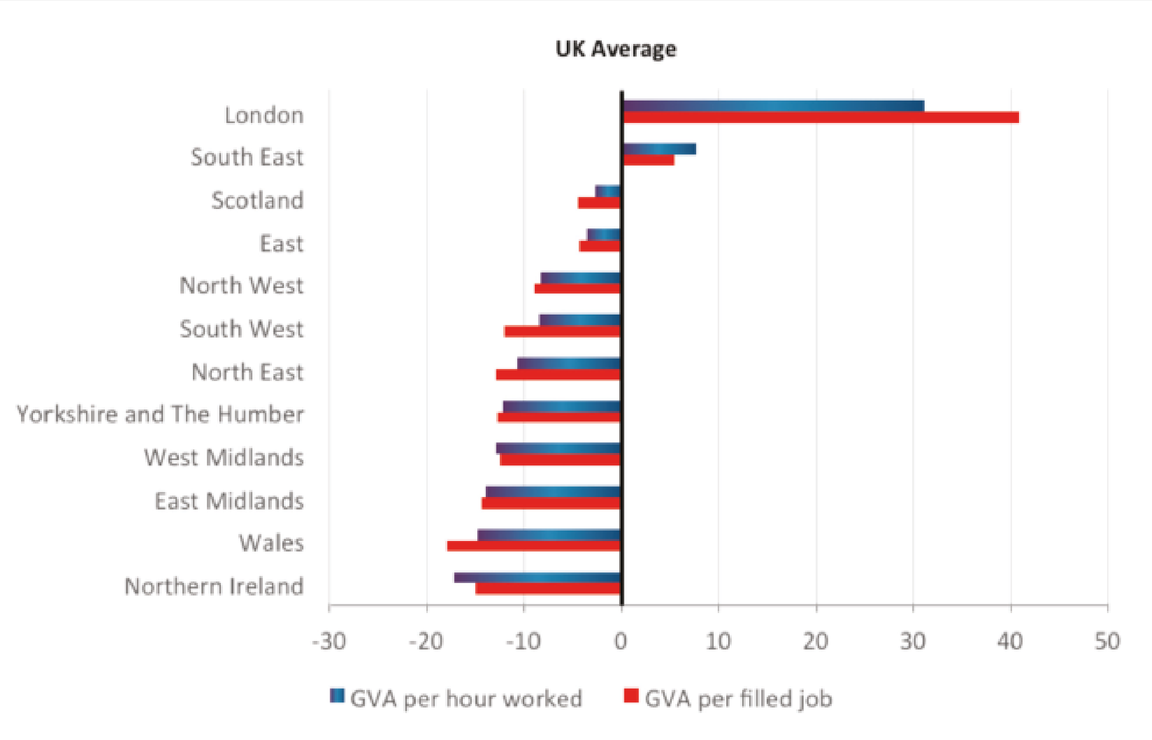
[7] Relates to regionally allocated pipeline projects, using HM Treasury data from 2014

[8] Figures correspond to projects whose benefits have been applied to one specific region. Projects designed to benefit the whole country (e.g. HS2) have been excluded from the calculations.

2.3 Productivity and skills

Looking at productivity across the various countries and regions of the UK, it is clear that there is a considerable divide in productivity levels. As shown in **Figure 16**, only the South East and London sit above the UK average productivity. On the ONS' preferred metric, GVA per hour worked, workers in London are more than 30% more productive than the national average and more than 40% more productive than the regions outside of the South East, Scotland and East of England.

Figure 16 – Productivity by region, 2012 (% difference from UK average)



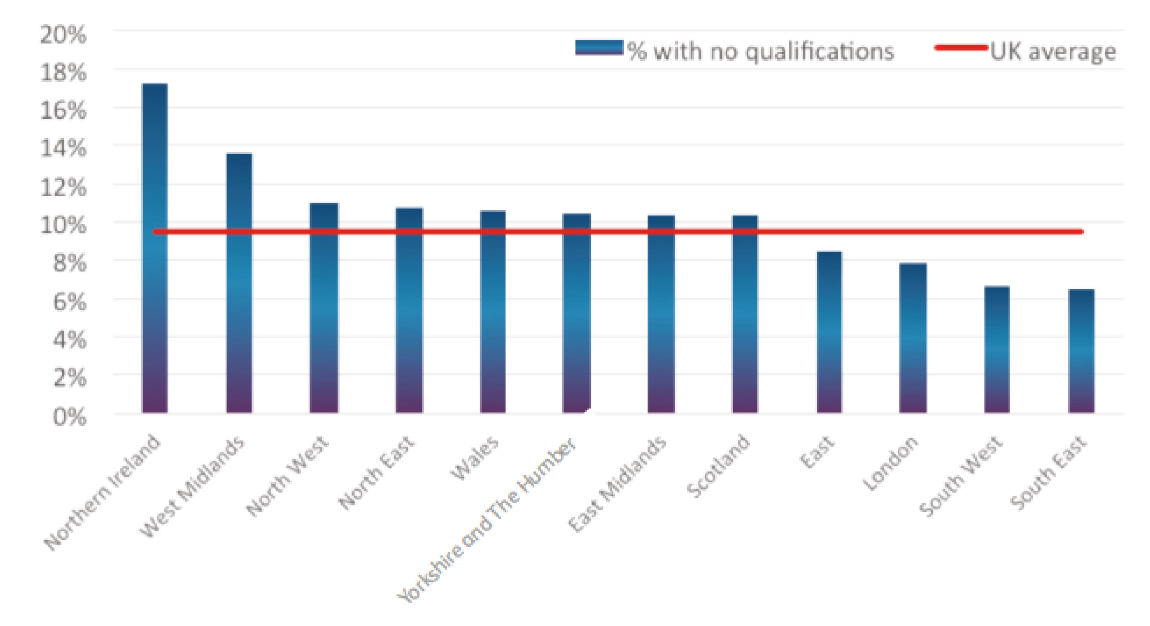
Source: Office for National Statistics, Cebr analysis

In 2009, an academic paper[9] examined the determinants of these regional productivity differentials across regions in England and found that a substantial share of the variation can be explained by a fairly limited set of variables. These include industry mix, capital stock, ownership and skills.

The skills issue is multifaceted. In one sense, regions that have experienced considerable declines in their key industries may have a labour force with quite advanced skills but skills that do not match up with those required by the region's economy in the 21st century. Additionally, the prosperous regions such as London and the South East are highly attractive to more skilled and educated sections of the workforce, which makes it difficult for other regions of the UK to attract and retain talent.

[9] Webber, D. J., Hudson, J., Boddy, M. and Plumridge, A. (2009), Regional productivity differentials in England: Explaining the gap. Papers in Regional Science, 88: 609–621. doi: 10.1111/j.1435-5957.2008.00209.x

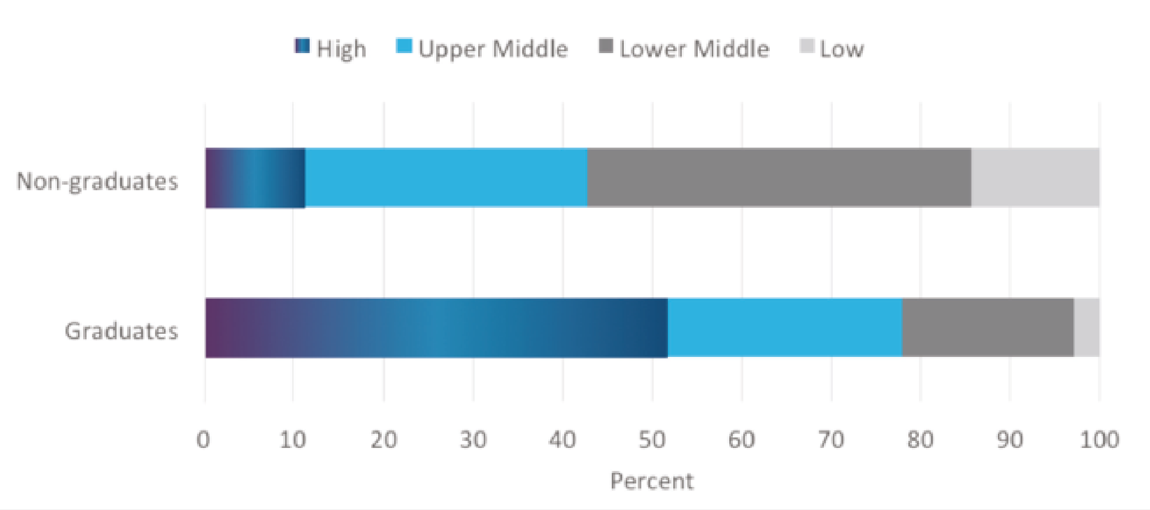
Figure 17 – Share of 16-64 year olds with no qualifications, 2013



Source: Office for National Statistics

Figure 17 highlights a clear disparity between the skills of the labour force in each region. However, while these data provide an insight into the shares of the lowest skilled in each regional economy, the more important driver of regional differences is likely to come from observing the higher end of the qualification spectrum and in turn analysing the share of the workforce that has the capacity to work in more knowledge-intensive, higher value-added roles.

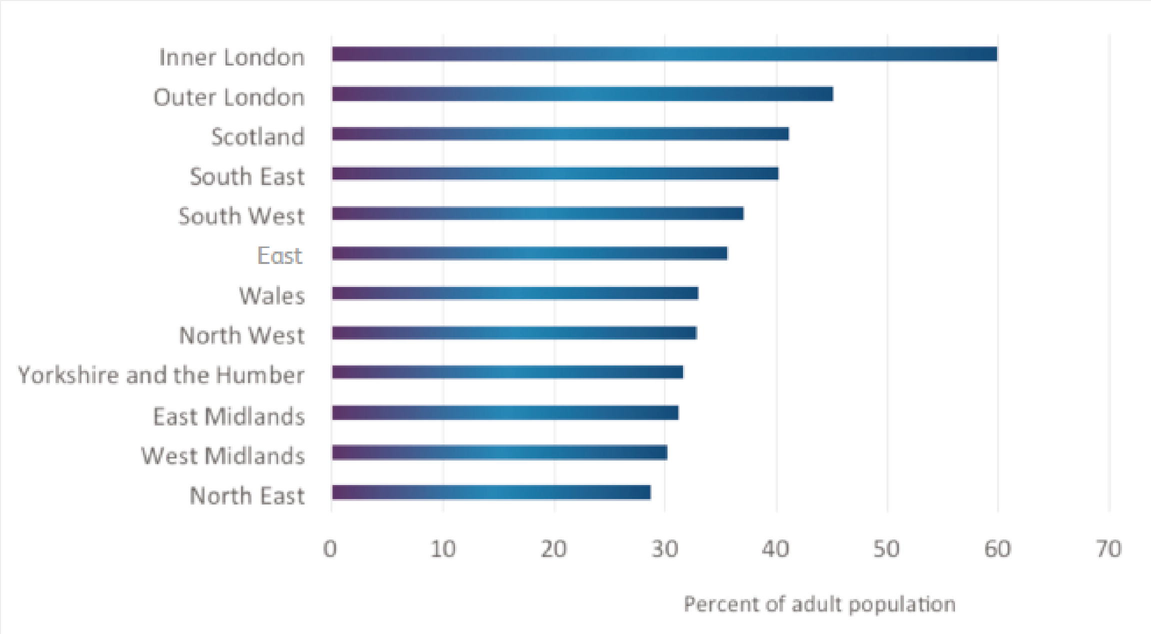
Figure 18 – Graduates and non-graduates by skill level of job, April to June 2013



Source: Office for National Statistics

As shown in ***Figure 18,*** graduates are much more likely to work in high skill jobs than non-graduates and while the percentage of each group in upper-middle skill jobs is fairly similar, there are significant differences in the types of jobs graduates and non-graduates were doing within this category. Graduates in upper-middle skilled employment tended to have roles in marketing, finance and human resources while non-graduates were mainly working in manual roles, for example as carpenters and joiners, plumbers and electricians.

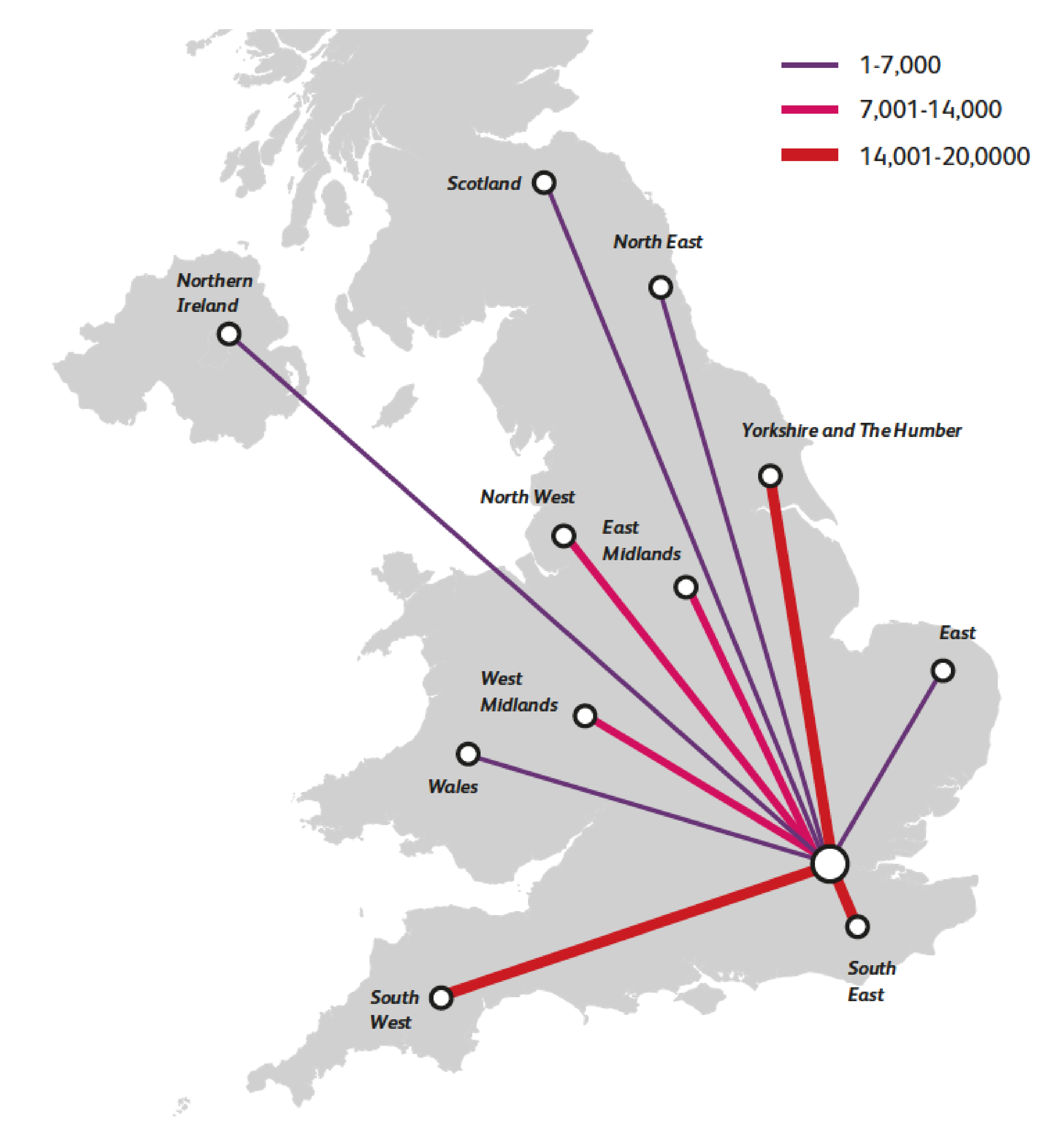
Figure 19 – Concentration of graduates across Great Britain, January to December 2012



Source: Office for National Statistics

Looking at the concentration of graduates across regions, a clear divide between London and other regions once again emerges. For every ten adults living in Inner London, six have graduate degrees. In contrast, less than three in ten adults living in the North East of England are degree educated. Looking at the spread of students across the country, it is clear that a significant share of the graduates in London have migrated there following graduation, either from abroad or from other regions of the UK. In its 2014 Cities Outlook report, the Centre for Cities found that one in three 22 to 30-year-olds who have changed their city of residence have headed to London and 80,000 people within the age group moved to the capital between 2009 and 2013, with a net inflow of over 48,000.

Figure 20 - Migration of 33 – 39 year olds to London, July 2011 – June 2014



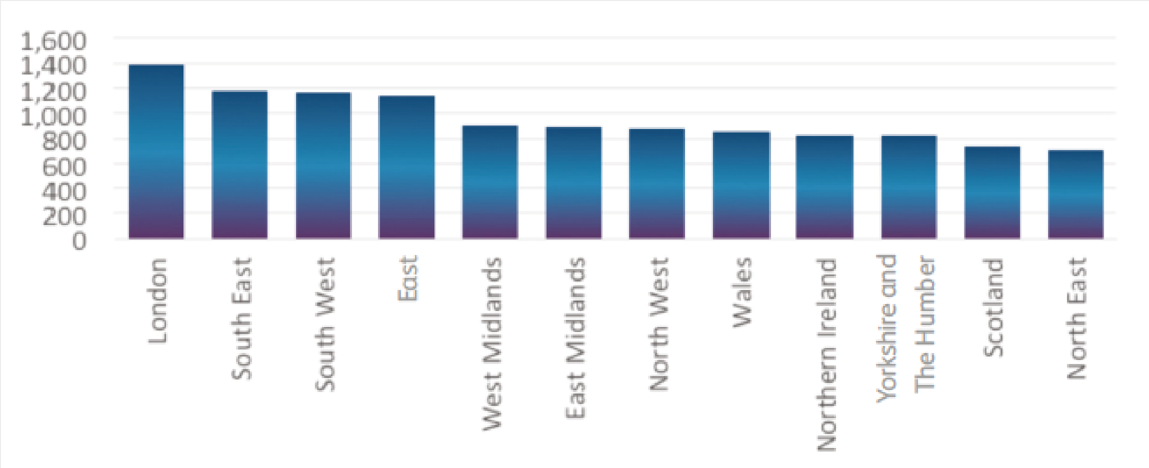
Source: Office for National Statistics, Cebr analysis

2.4

Entrepreneurship

Another potential cause of interregional disparities is the variation in the level of entrepreneurial activity taking place in each part of the country. One measure of 'business dynamism' or the level of business opportunity generated is the number of businesses in a particular region. **Figure 21** looks at this metric.

Figure 21 - Number of businesses per 10,000 adults, 2014

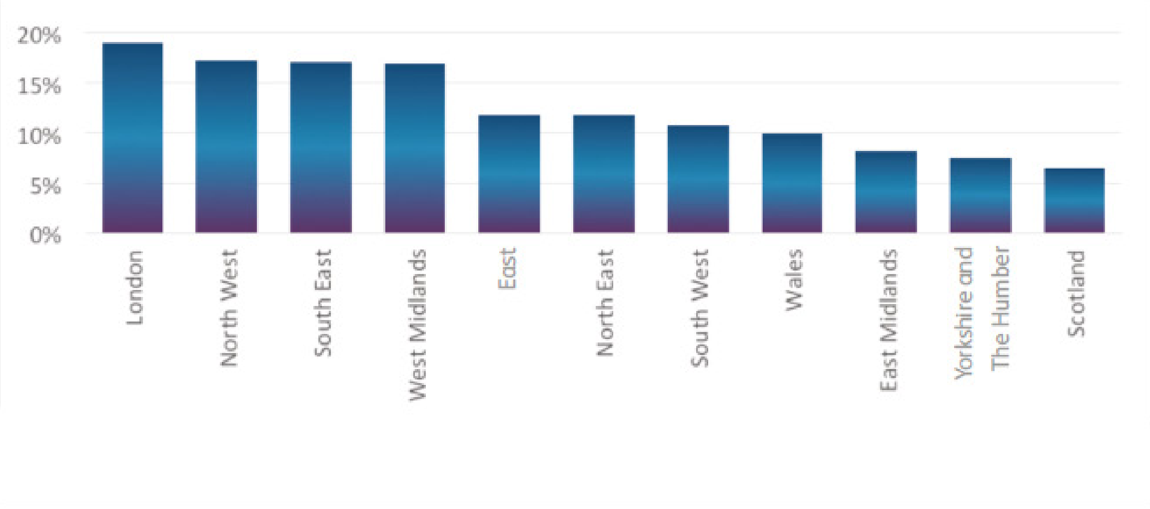


Source: BIS, Business Population Estimates

In 2014, London had 1,391 businesses per 10,000 adult residents. This is nearly twice the 701 figure for the North East. Fewer businesses may mean that there are less employment opportunities available for residents. Furthermore, differences in entrepreneurial activity can be self-perpetuating as businesses often want to position themselves in an area where a strong business community already exists. This is because an interconnected hub of knowledge and business services can improve company performance.

The fact that many self-employed entrepreneurs prefer setting up a business near an existing interconnected business hub may also explain the strong growth in the number of self-employed persons in London.

Figure 22 - Change in the number of self-employed persons in the 2008-2013 period



Source: Annual Population Survey

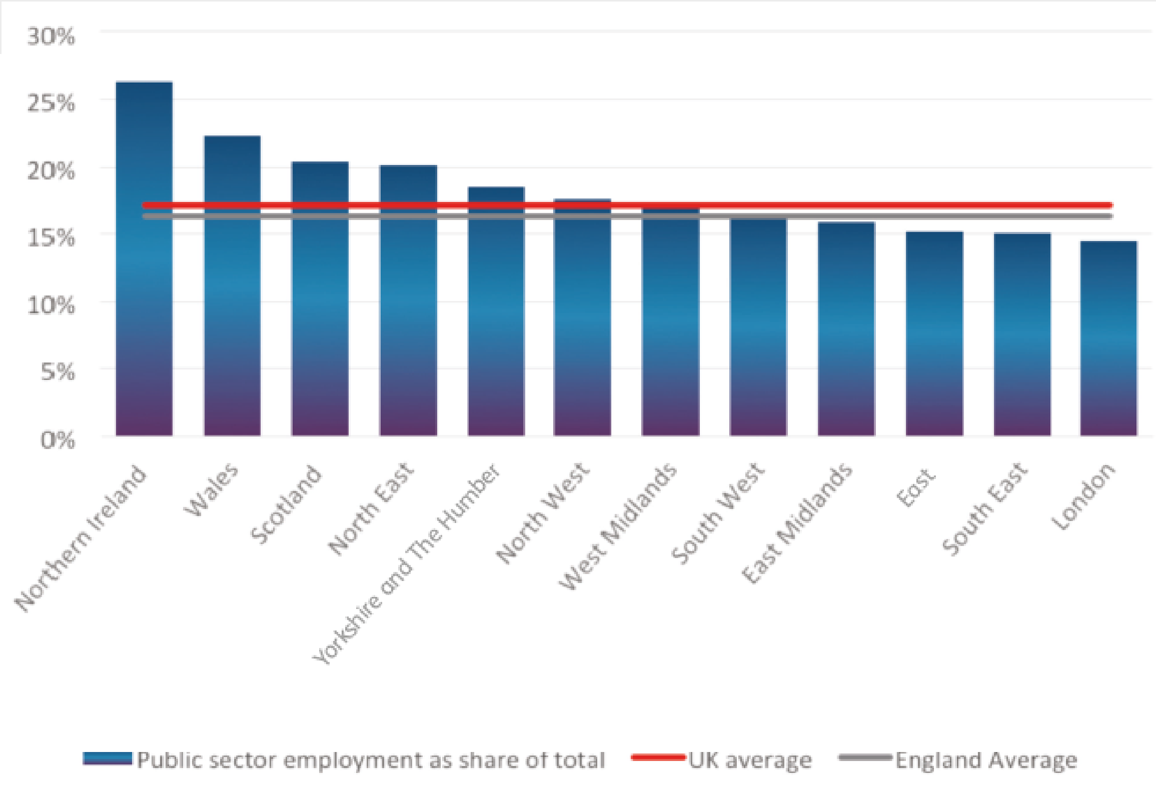
Between 2008 and 2013, the number of self-employed persons in London grew 19 % from 571,000 to 679,000. This was a higher rate of growth than any other British region. London is also the region with the highest number of self-employed persons in absolute terms with 679,000 people working independently in 2013.

2.5 Public sector dependence

Austerity measures over the new parliament will impact the British regions to a varying extent. Those regions that are more dependent on public sector employment and that enjoy a higher level of public spending are more vulnerable to austerity measures.

In the first quarter of 2015, Northern Ireland was most dependant on the State as a source of employment with 26.3 % of its workforce in the public sector. Out of the English regions, the North East had the highest and London the lowest share of its workforce in the public sector with values of 20.2 % and 14.5 % respectively.

Figure 23 - Public sector employment as share of total[10]

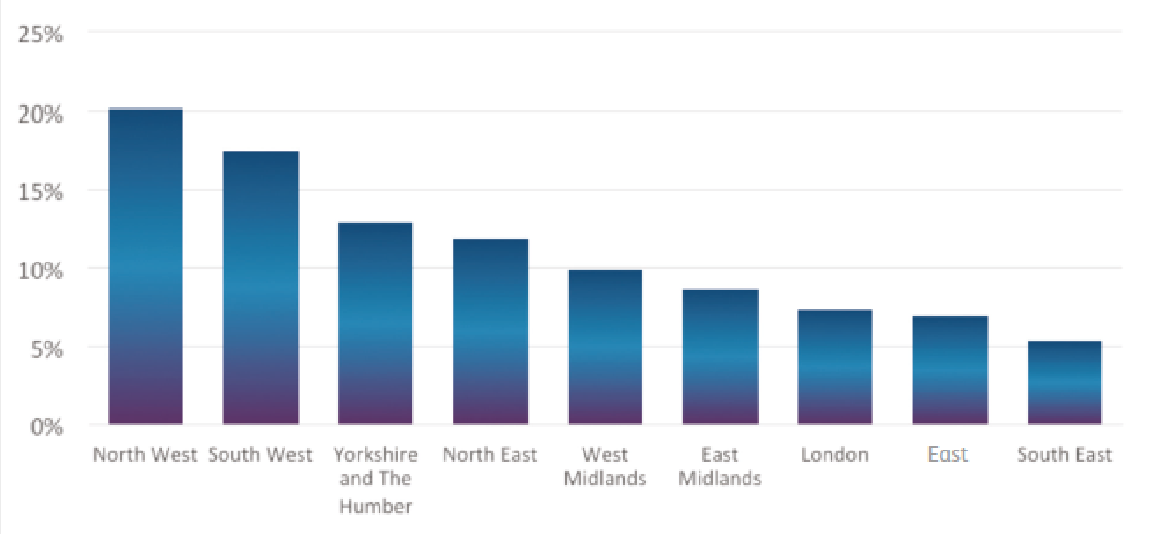


Source: Office for National Statistics

Since public sector job shedding began in 2010, the number of job cuts has been unevenly distributed among the regions. Comparing the number of people in public employment in 2008 with Q1 2015 reveals a decrease of 381,000. Of this, 303,000 jobs were cut in England. **Figure 24** shows the share of the public sector job cuts by region.

[10]The figure excludes the distorting effects of major public/private reclassifications over recent years.

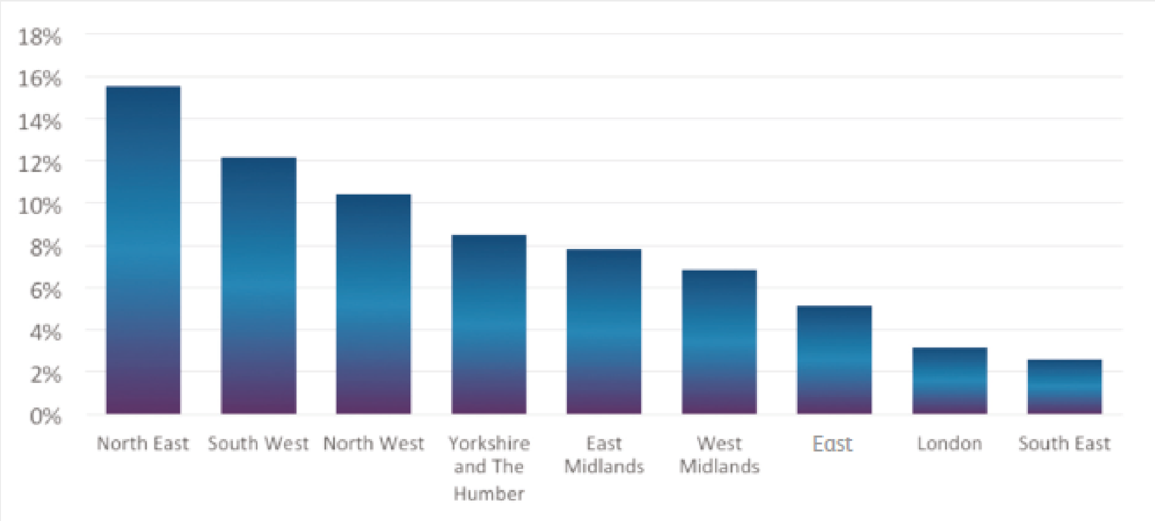
Figure 24 - Share of public sector job cuts 2010-Q1 2015 in England, by region



Source: Office for National Statistics

In terms of the number of public sector job cuts, the greatest losses in the 2010-Q1 2015 period were seen in the North East with 61,000 fewer jobs followed by the South West (53,000) and Yorkshire and the Humber (39,000). To put these figures into perspective **figure 25** looks at these job cuts as a share of the current public sector workforce.

Figure 25 - 2010-Q1 2015 public sector job cuts as share of the region's Q1 2015 public sector workforce



Source: Office for National Statistics

Based on this metric the North East, South West and North West's labour markets have been most severely impacted by public sector job cuts thus far. Given that roughly 500,000 more jobs are expected to be cut up to 2020, these regions may begin to face rising unemployment.

2.6 Industrial clusters

Another factor that may contribute to regional disparities is the concentration of successful industries in a particular area. Various methods exist for assessing if an industry is heavily concentrated in a particular geographical area or a small number of areas or if employment is spread out more evenly across the country. In 2012, the Office for National Statistics carried out a study using three measures of geographical concentration (the Herfindahl-Hirschman index, the Locational Gini and the Maurel and Sedillot index) to assess which industries in the UK are heavily concentrated in small geographical areas. The 19 analysed industries are listed in the table below in the order from most to least concentrated.

Table 3 - List of UK industries from most to least geographically concentrated

Industry	Concentration
Mining and quarrying	High
Financial and insurance activities	High
Professional, scientific and technical activities	High
Information and communication	High
Real estate activities	High
Agriculture, forestry and fishing	Relatively low
Electricity, gas, steam and air conditioning supply	Relatively low
Transportation and storage	Relatively low
Accommodation and food service activities	Relatively low
Public administration and defence; compulsory social security	Relatively low
Administrative and support service activities	Low
Other service activities	Low
Arts, entertainment and recreation	Low
Education	Low
Human health and social work activities	Low
Manufacturing	Low
Wholesale and retail trade; repair of motor vehicles and motorcycles	Low
Construction	Low
Water supply; sewerage, waste management and remediation activities	Low

Source: Office for National Statistics

Industries at the top of the chart are highly concentrated geographically not beause a small number of large firms dominate. Rather, a large number of independent firms have settled in proximity to one another.

In order to understand how industry clustering impacts various local authorities and therefore regions, we now examine specific industry clusters and where they are located. Clustering in certain sectors, for example mining and quarrying, is explained by geographical limitations i.e. oil extraction is heavily concentrated around Aberdeen because of North Sea oil.

However, for other services such as scientific activities, firms had no pre-existing reason to establish themselves in the same area. Rather, the benefit comes from the very fact that other industry players are located in the area. Specifically, the benefits for companies within industry clusters include:

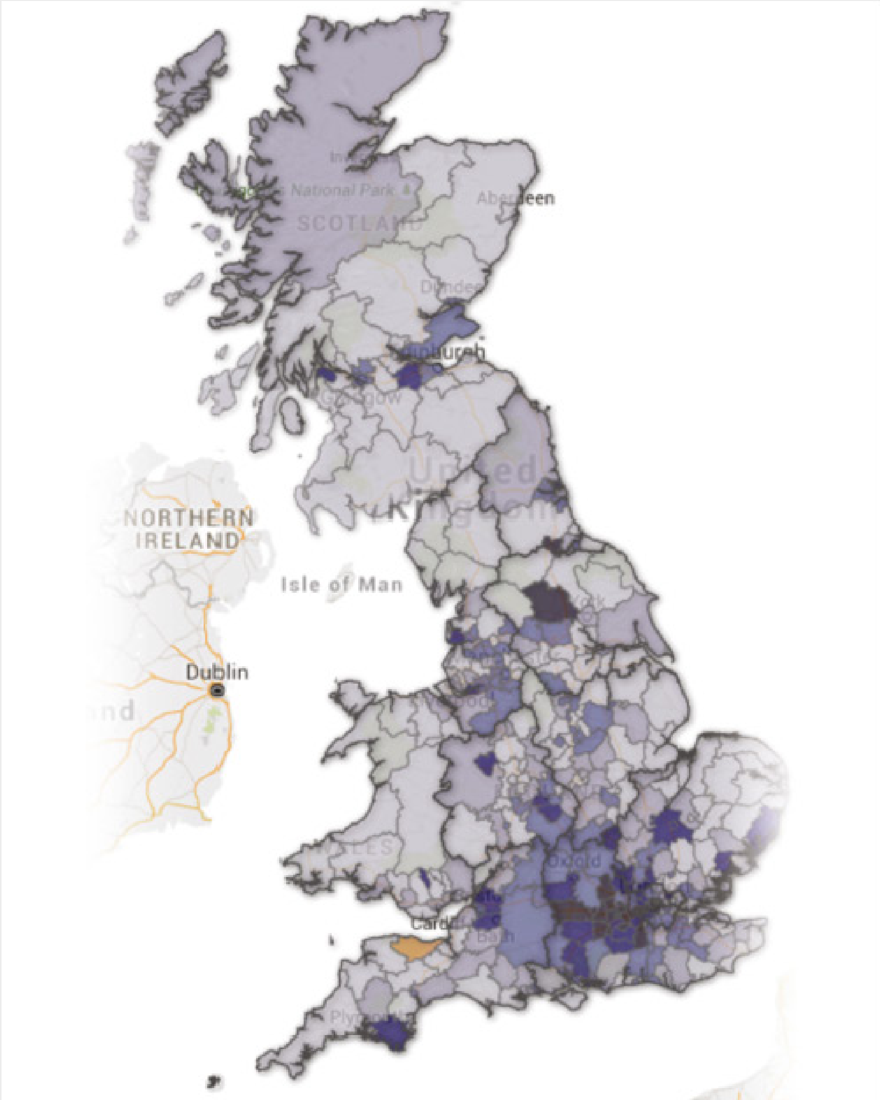
- Proximity to industry input providers
- Access to a rich labour market with a specific skill set
- Existence of informal spillovers e.g. knowledge sharing[11]

Through these channels, firms located within an industrial cluster experience various productivity benefits. Regions that have drawn specific industry clusters have also benefited from the boost to economic activity. London is a hub for certain types of firms including financial services providers and science activities. Science activities also cluster around Cambridge. Both location choices can be partially explained by proximity to universities which benefits science-focused firms e.g. pharmaceutical labs in all three of the ways described above. Universities not only produce graduates with the necessary skills for the science industry, but also serve as knowledge centres for advancements in the sectors.

[11] Based on the work of Alfred Marshall in 1890

Figure 26 - Concentration of finance and insurance services firms by geographic area

London is by no means the only region that has witnessed and benefited from the formation of industry clusters. Although manufacturing is a relatively non-concentrated sector, the East Midlands and the West Midlands are the regions with the highest share of manufacturing employee jobs relative to their overall share of jobs. Specifically, the success of the automotive industry has been a driving force behind regional growth.

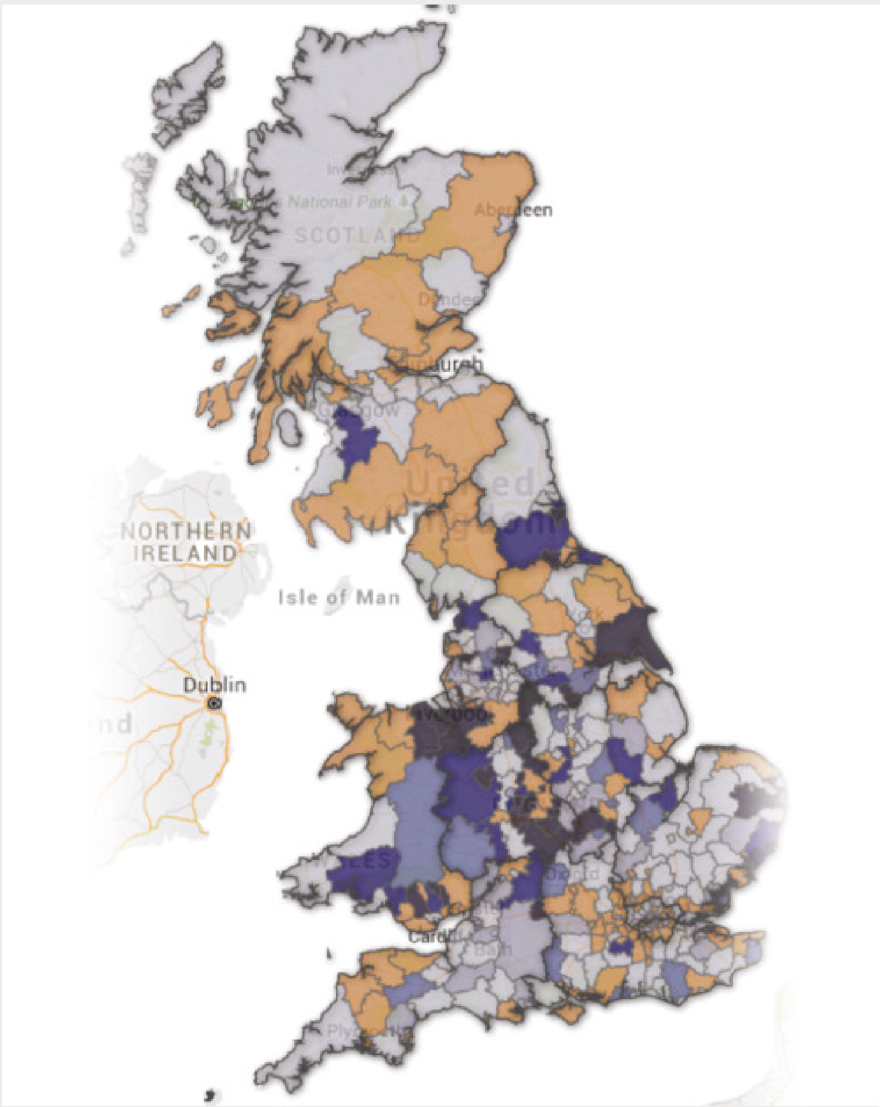


Note: A darker colour signifies a higher industry concentration

Source: Office for National Statistics

Figure 27 - Concentration of firms that operate in the manufacturing of motor vehicles industry

However, although exceptions do exist industry clustering remains a mostly South-specific phenomenon. Examining the top five most concentrated industries identified in Table 3 reveals that other than some heavy mining activity around Hull and services firms in the proximity of Leeds, most of the significant industry clustering occurs around London and in the southern regions. Hence, areas in the North are not benefiting as much from this type of economic dynamism.



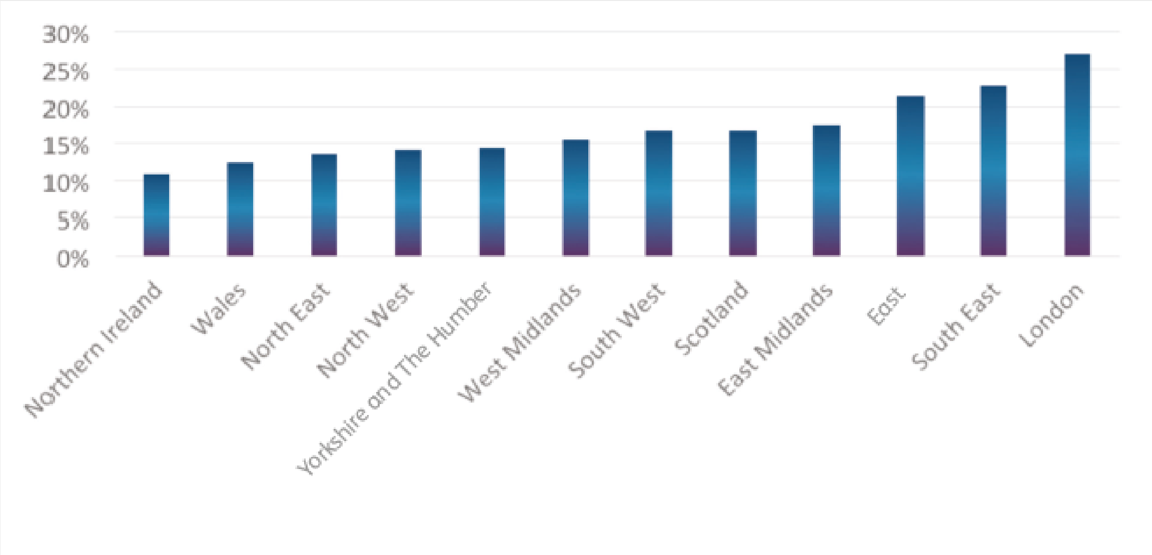
Note: A darker colour signifies a higher industry concentration

Source: Office for National Statistics

3 Regional policy solutions

On current trends, the divide between the regions and counties of the UK is likely to grow ever larger. We expect output across London to grow to be just shy of £450 billion (2012-prices) by 2025, an increase of 27% from 2015. At the same time, we expect the combined growth across the North West, North East and Yorkshire & Humber to total a little over 14% over the period, leaving output in these regions more than £110 billion lower than that of London in 2025.

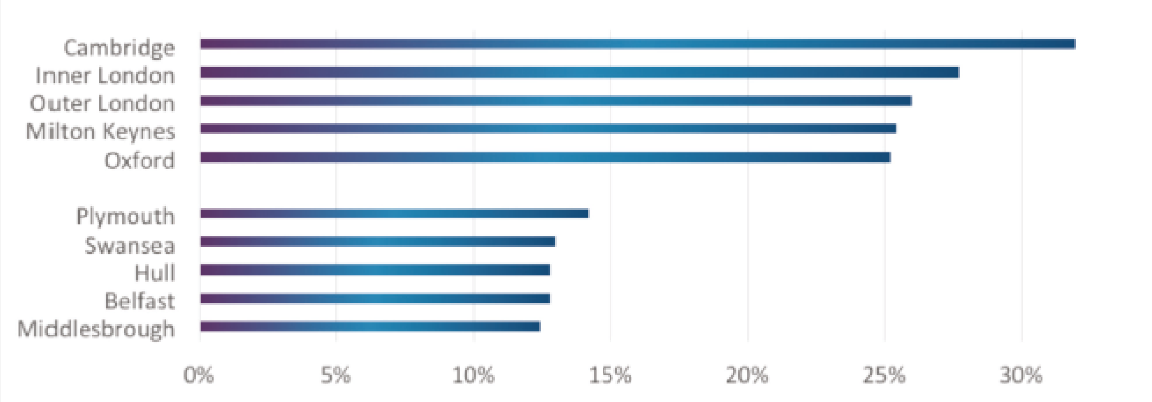
Figure 28 – Projected real GVA growth by region, 2015 – 2025



Source: Office for National Statistics, Cebr analysis

Similarly, at a city level, the pace of growth in London and cities including Cambridge, Milton Keynes and Oxford is expected to far outweigh that of cities such as Middlesbrough, Belfast and Hull as a result of the continued success of these areas in attracting skilled labour into sectors ranging from the already well established business services, finance and law industries to growing technical and knowledge-based sectors such as computing and research and development in a variety of fields.

Figure 29 – Projected real GVA growth by city, Q2 2015 – Q2 2025



Source: Office for National Statistics, Cebr analysis

Resolving the vast differences in economic performance across the UK's regions will be challenging, given the fact that there are several causes for these differences. No one policy solution will suit each region, and the priority of growth policies differs across the UK. To build a series of regional powerhouses a number of policies need to be implemented. This section of the report considers the measures which policymakers should implement to narrow the regional divide in economic performance, as well as to ensure the continued success of existing regional powerhouses such as London (which faces its own unique challenges). The conclusions are informed by Cebr's economic analysis, existing research and a new survey of 1,000 businesses which was undertaken by YouGov as part of this research.

3.1 The voice of businesses

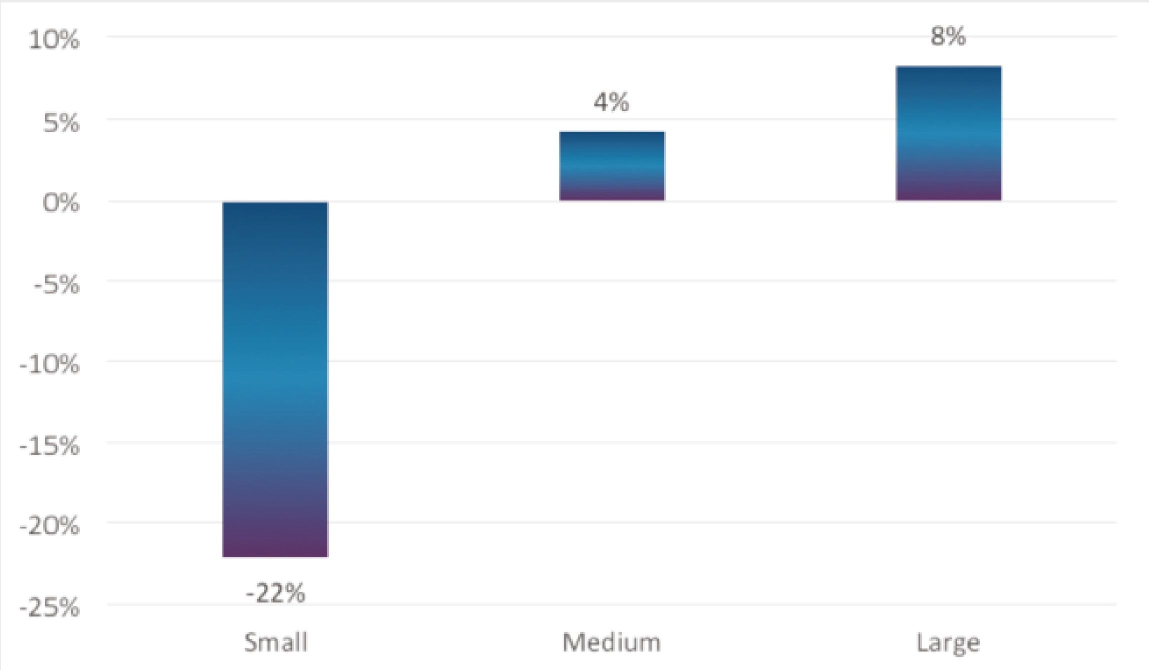
As part of this research Irwin Mitchell commissioned a YouGov survey of 1,000 UK businesses to examine the issues affecting companies in different parts of the country and to understand the policy measures which the business community themselves think are the best way of boosting regional economic growth.

When asked about the extent to which they agreed with the statement that the government has taken the necessary steps to address economic growth in the region in which they are based, more businesses disagreed (38 %) than agreed (31 %) with the statement.

There are wide variations in agreement by company size, industry and location.

While a net balance of 22 % of small businesses felt the government had not taken the necessary steps to boost economic growth, for medium and large businesses a respective net balance of 4 % and 8 % agreed with the statement.

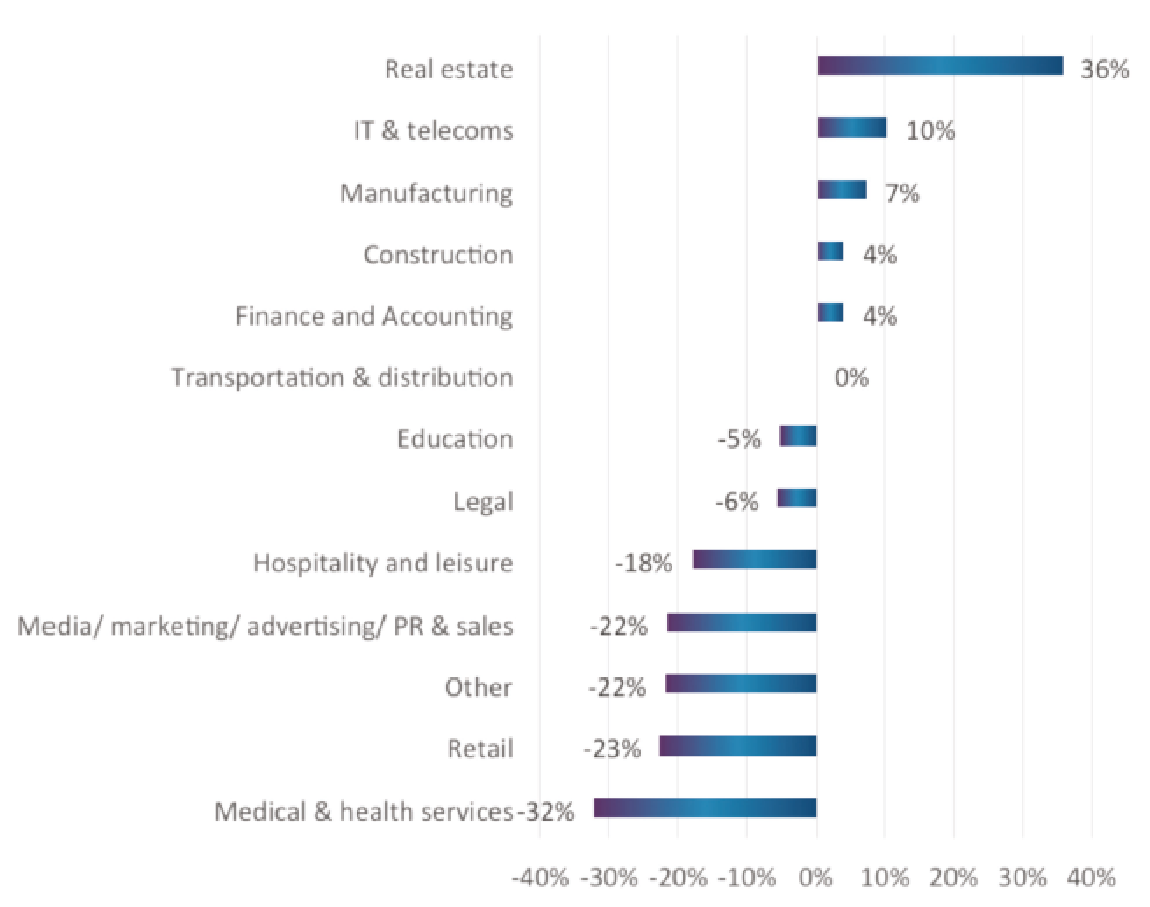
Figure 30 - Net balance of businesses agreeing with the statement "the Government has taken the necessary steps required to boost economic growth in the region where my business is based"



Source: YouGov, Cebr analysis

By industry grouping, the medical, retail, education and hospitality & leisure sectors all saw a net balance of businesses disagreeing with the statement. The real estate sector saw the greatest net balance of businesses agreeing with the statement, probably reflecting the surge in property prices seen over the past two years.

Figure 31 - Net balance of businesses agreeing with the statement "the Government has taken the necessary steps required to boost economic growth in the region where my business is based"



Source: YouGov, Cebr analysis

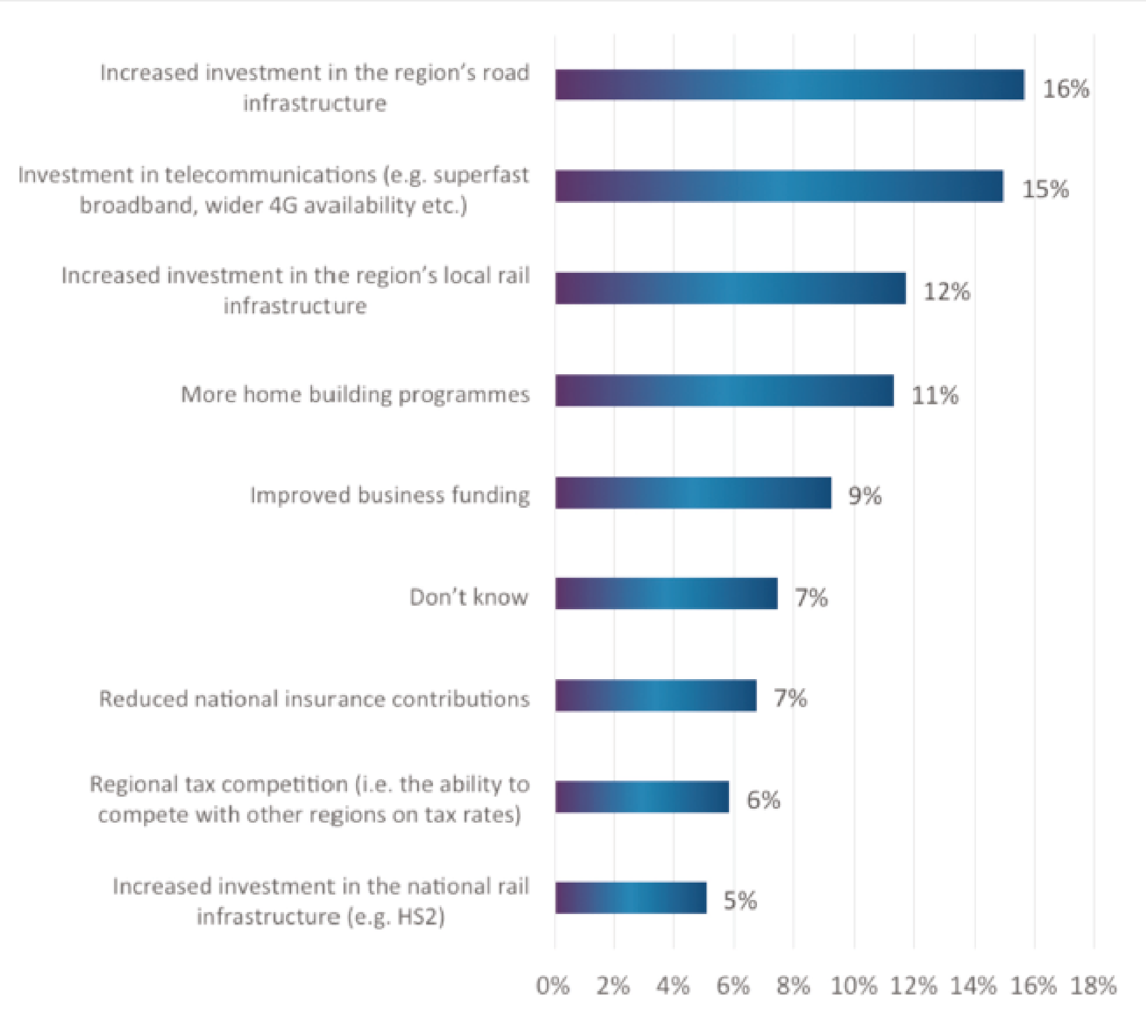
The regional breakdown of the survey results is stark. Despite all the rhetoric around building a Northern Powerhouse, a net balance of businesses in the North disagreed that the government was doing enough to support regional economic growth.

In contrast, a net balance of businesses agreed with the statement in London and the Midlands. The devolved administrations of Scotland and Wales have the greatest net balance of businesses believing that the Government is not doing enough to support regional growth.

Figure 32 - Net balance of businesses agreeing with the statement "the Government has taken the necessary steps required to boost economic growth in the region where my business is based"

Source: YouGov, Cebr analysis

Figure 33 - Which ONE, if any, of the following would you most like to see improve economic growth in the region where your business is based?



Source: YouGov, Cebr analysis

Clearly, then, businesses in general believe that more could be done to support economic growth, particularly outside of London and for smaller businesses. This begs the question of what policies should be implemented.

Asking businesses to choose the one policy they would most like to see to improve economic growth in their region shows a range of responses. Across all the businesses surveyed, improving road infrastructure (16 %) and telecommunications infrastructure (15 %) were the most frequently cited answers. Improving local rail services and more home building programmes were also relatively popular answers.

3.2

Policy consideration 1: Devolve more powers to cities, regions and local authorities

Variations in skill levels, demographics and business activity in different parts of the UK mean that a one-size-fits-all approach to policy is inappropriate. With economic prospects set to diverge over the coming years, there is a strong case for devolving a wide range of policies to the local level – including education, taxation, housing and infrastructure policy.

We asked the 1,000 businesses we surveyed whether they felt that greater devolution of powers would boost economic growth in the region in which they operated. Close to half (48%) of businesses agreed that this would boost economic growth, while just over a fifth (22%) disagreed. The remainder of businesses neither agreed nor disagreed, or did not know.

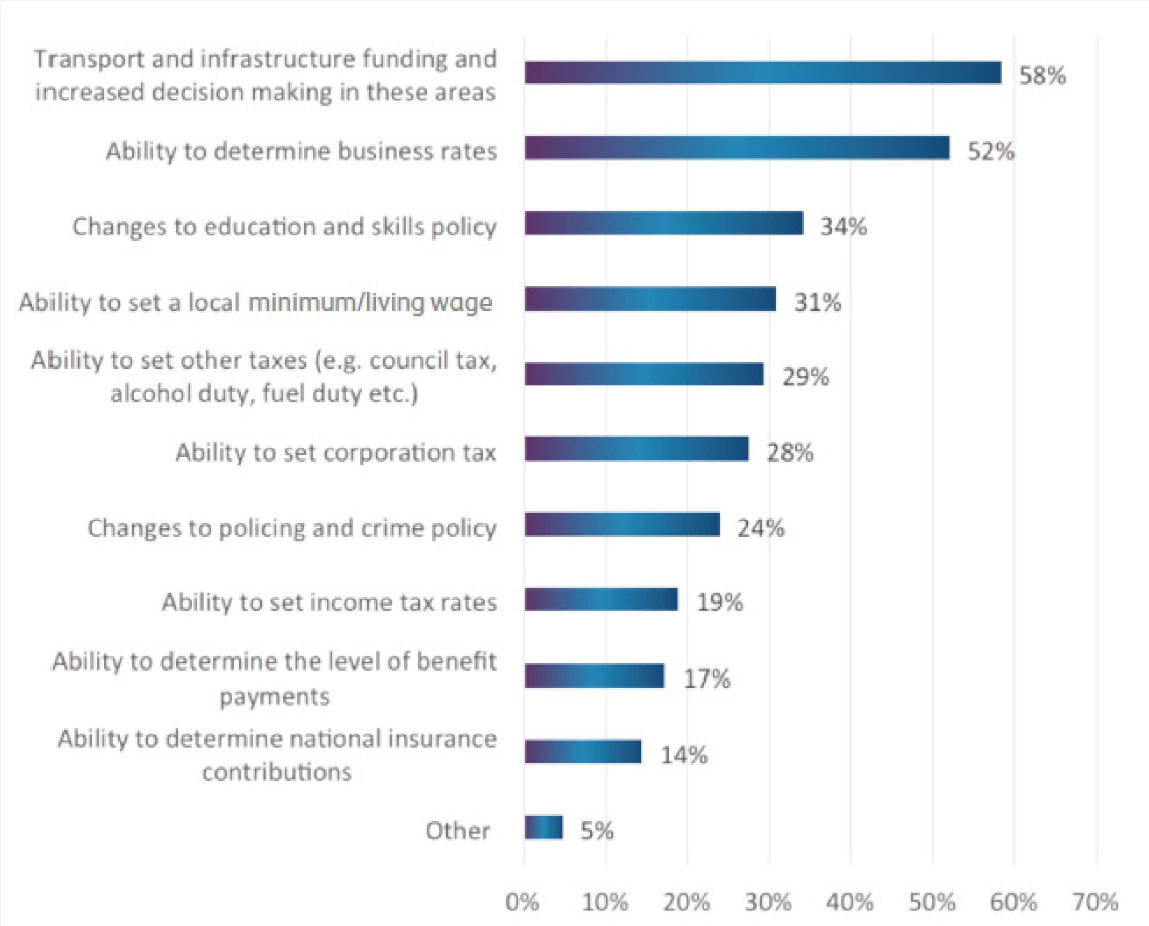
Belief in devolution was strongest in the North of England, with close to three fifths (59%) of businesses agreeing that it could boost economic growth in the region.

Businesses were asked about the policies they thought would help to boost growth in the region in which they operated. Across most regions and industries, two key policies were most frequently cited:

1. Increased infrastructure funding and local decision-making
2. The ability to determine business rates.

Over half of businesses surveyed believed that devolution of these powers has helped or could help boost economic growth in the regions in which they are based. Education/skills policy and the ability to set a local minimum/living wage were also frequently cited. The ability to set income tax rates and national insurance contributions was less frequently cited, as shown in **Figure 34**.

Figure 34 - Which, if any, of the following powers or functions do you think have helped/would help to boost the economic growth in the region where your business is based? % of respondents choosing power/function



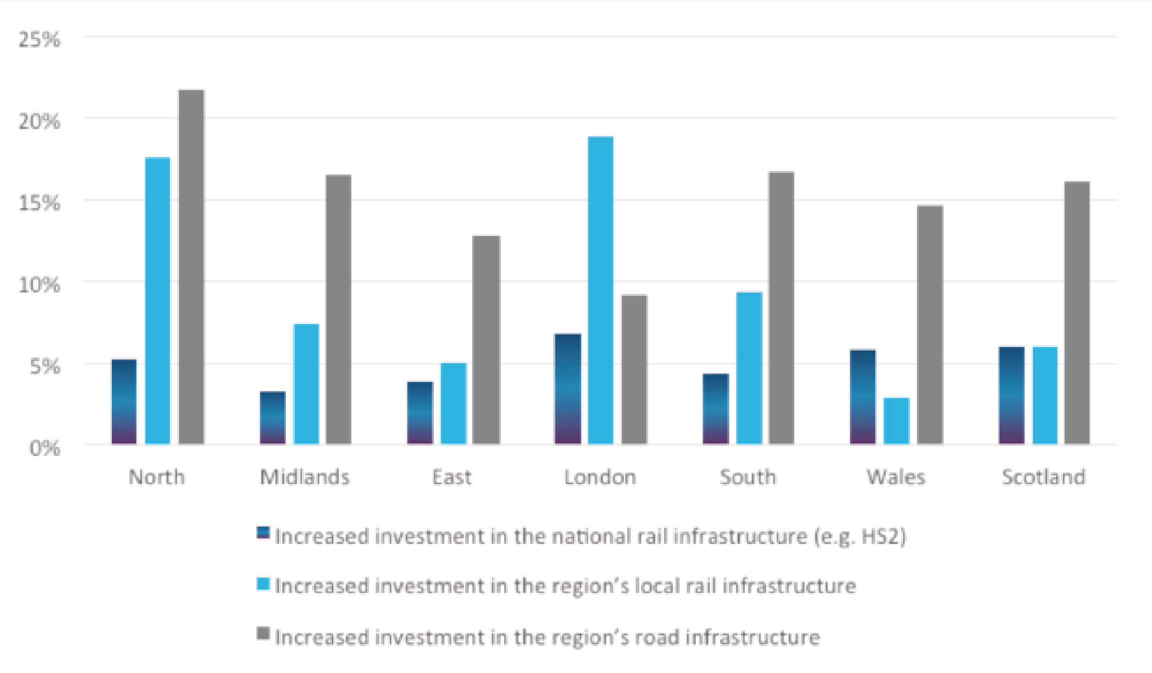
Source: YouGov, Cebr analysis

3.3

Policy consideration 2: Rethink existing transport policy and focus more on local road and rail projects

As our survey of businesses showed, companies have a preference for local transport projects over national transport projects. Furthermore, with the exception of London, businesses in general expressed a preference for road investment over rail investment as a means of improving regional economic growth. This is particularly the case in the North of England.

Figure 35 - Which ONE, if any, of the following would you most like to see improve economic growth in the region where your business is based?



Source: YouGov, Cebr analysis

These results align with a bulk of economic evidence which suggests that road projects tend to have greater net economic benefits than rail projects. Examining a range of transport projects in the UK, the RAC foundation estimated an average benefit-cost ratio of over four for Highways agency road and local road schemes[12], this compares with benefit-cost ratios of less than three for rail schemes.

With businesses preferring local over national transport schemes, and with the higher benefit-cost ratios for roads, the efficacy of High Speed 2 (HS2) as a means of distributing growth across the regional powerhouses is debatable. Among the businesses we surveyed, national rail schemes were the least frequently cited option for boosting regional economic growth (see **Figure 33**).

[12]Rates of Return on Public Spending on Transport, RAC Foundation, 2009

As the costs of HS2 have increased, the benefit-costratio has fallen:

Table 4 - Benefit-Cost ratios for HS2

	February 2011	October 2013
Phase 1	2.0	1.7
Full Y network	2.6	2.3

Source: House of Commons Standard Note SN316

HS2 may yield economic benefits, but it would be sensible to research further. The Government needs to compare the cost benefit analysis of having local transport schemes in isolation with that of improving national infrastructure.

At the 2015 Conservative Party conference, the Chancellor George Osborne announced the establishment of a new National Infrastructure Commission headed up by former Labour Cabinet minister Lord Adonis. The Commission will produce a report at the start of each five-year parliament, containing recommendations of projects which governments should be pushing forward. The Chancellor also announced £5 billion of additional infrastructure spending over the course of the current parliament, raised with cash from the sale of land, buildings and other state assets.

The National Infrastructure Commission will start work immediately with an initial focus on:

- Plans to transform the connectivity of the Northern cities, including high speed rail (HS3)
- Priorities for future large-scale investment in London's public transport infrastructure
- Measures to ensure investment in energy infrastructure can meet future demand in the most efficient way

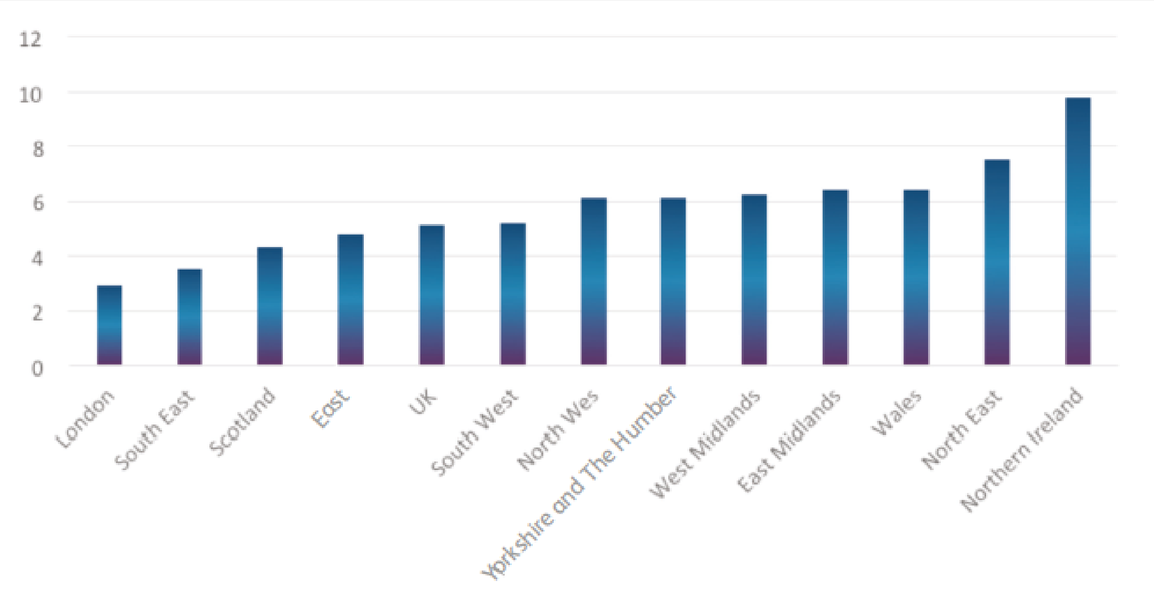
While this additional infrastructure spending is welcome, and there would be clear benefits associated with HS3 and improvements in London's public transport infrastructure, the Government must not overlook the benefits that investment in roads across the country could bring.

3.4 Policy consideration 3: Allow the Living Wage to vary across regions

The National Living Wage, announced in the July Budget, will have a significant impact on businesses – particularly those in sectors where pay rates are currently relatively low, such as hospitality, cleaning and care.

While the Living Wage will bring a number of economic benefits, including higher living standards and consumer spending for some individuals, this does not come without significant economic costs. Official estimates suggest that the measure will lead to the loss of 60,000 jobs in the UK as company wage bills increase. These job losses will be particularly concentrated in low wage sectors. They are also likely to be concentrated in parts of the UK where wages are relatively low. As Figure 36 shows, London is likely to be better-placed to absorb the living wage when it comes into effect next year, as wage rates are already relatively high in the capital and there are fewer employees on the current National Minimum Wage.

Figure 36 - Percentage of jobs that are NMW, by region (2013)



Source: Low Pay Commission

To support existing jobs and encourage further job creation, the Government should rethink its Living Wage policy to allow the living wage to vary across regions. There's no reason to have a single living wage given the huge differentials in living costs across the country, and indeed past references to a living wage have tended to express the need for a different wage in London compared with elsewhere.

One way of setting a regional living wage is to link the wage to the cost of living in different parts of the UK, implying a higher living wage in London and a lower living wage in the North of England for example. This would allow the regions outside of London to remain competitive in terms of labour costs, supporting job creation and encouraging businesses to base themselves in these parts of the country. Linking the living wage to the cost of living in different regions will also help equalise living standards for lower earners across the country. The current proposals will see lower earners in London facing an inferior standard of living compared to lower earners in other parts of the country.

3.5 Policy consideration 4: Take further steps to reform business rates and consider replacing with a local Land Value Tax

Business rates have constantly been an issue for businesses across the UK and there is widespread agreement that the rates system is not fit for purpose. In particular, rates do not sufficiently take account of the individual circumstances of businesses and their ability to pay rates.

Business rates are a property tax paid by occupants of non-domestic properties. The basic rates bill of a property is determined by multiplying its rateable value by a 'multiplier'. A property's rateable value is set by the Valuation Office Agency (in Scotland, the Assessors; and in Northern Ireland, Land and Property Services) at regular intervals. The multiplier is expressed in pence per pound of rateable value.

Various reliefs, both mandatory and discretionary, are available from full business rates liability. Limited powers also exist for local authorities to set supplementary business rates.

Devolution in the setting of business rates across England – something which was announced at the Conservative Party conference in 2015 – should allow local authorities to better attract businesses, or allow authorities to raise the money needed for infrastructure improvements.

The Government should consider reforming business rates in other ways too, for example by reconsidering valuation periods. More frequent revaluations, perhaps every year, may also help businesses in struggling areas as it would ensure that businesses pay rates based on up to date rental values.

The government could go further and consider alternatives to business rates. In particular, there is an extremely strong case for replacing business rates (and other taxes on property) with a land value tax.

Land value taxation is essentially a method of raising public revenue by means of an annual charge on the rental value of land rather than property. The value of every parcel of land in Britain would be assessed regularly and the land value tax levied as a percentage of those assessed values. Because it is a tax on land rather than business property, it does not deter entrepreneurial activity (unlike business rates). Taxing business property inefficiently discourages the development and use of business property. If possible, it would be better to tax the value of the land excluding the value of any buildings on it, which would have no such effects.

Because a land value tax is charged whether or not land is put to commercial use (or indeed residential use) it encourages landowners to make the best use of this land.

Land value tax could not be introduced overnight, and there would be some challenges. In particular, there would initially be difficulties in determining the value of individual land holdings separate from any buildings on them. However, this can be resolved – for example, one could compare rental values for comparable properties in different locations.

We have seen some form of land value taxation in countries such as Denmark and Australia.

3.6 Policy consideration 5: Tackle housing shortages

The UK's housing crisis – a result of a chronic undersupply of housing relative to demand – is undoubtedly a significant economic issue. Rising prices in recent years have priced many out of homeownership.

This has implications for businesses too. High house prices and rents translate into higher staff salaries in order to attract and retain talent. The squeeze on household spending power caused by rising housing costs also negatively impacts consumer-dependent sectors such as retail.

Interestingly, among the companies we surveyed in London, businesses cited "more home building programmes" as the preferred means of boosting economic growth more than any other policy – with 22% choosing this. This is the only region in which this is the case and suggests that the capital's rocketing house prices are now having a tangible and significant impact on the business community.

Tackling London's – and the UK's – housing crisis will be no small feat, especially as many individuals directly benefit from high house prices and the positive impact this has on their wealth. This limits the political will to address the problem despite the impact it is having on consumers and businesses. If these political barriers can be overcome, a series of measures could be introduced to reduce or stabilise the cost of housing:

- Rethinking the concept of greenbelt land around urban powerhouses – allowing urban powerhouses to expand on land which is underutilised and often not particularly beautiful.
- Considering densification of urban areas.
- Taking measures to tackle empty homes – such as further increases in Council Tax charged on empty properties.
- Easing of planning restrictions.
- A greater supply of local authority housing.

One could say that the housing crisis in London is a symptom of relatively weak economic growth in other parts of the UK. The capital's success has led to a significant influx of people from other regions to London. Migrants from outside the UK have also increased demand for London property.

Arguably, if economic growth was spread across the UK, then pressures on housing would be more evenly distributed as the brain drain to London from elsewhere would be less severe. At least a partial solution to London's housing problem is to bolster other economic powerhouses in the UK.

3.7 Policy consideration 6: Facilitate greater tax competition

Across all the businesses we surveyed, regional tax competition was not frequently cited as the number one measure to boost regional economic growth – just 6 % of respondents thought this was the case. There were differences by firm size – 3 % of small businesses thought it was the number one measure, rising to 8 % of medium businesses and 13 % of large businesses. A higher proportion of businesses in the North of England (9 %) than any other region thought it was the number one priority.

In theory, tax competition has huge potential to narrow differences in economic performance. Allowing regions to compete on business rates, income tax and other taxes may help allow regions to attract business investment and top talent. At an international level, we have seen countries such as the Republic of Ireland benefitting from increased business investment due to having a very competitive corporate tax regime.

In practice, the evidence on sub-national tax competition from other countries has been mixed. The Organization for Economic Cooperation and Development (OECD) examined sub-national tax competition in a range of countries such as the US, Spain and Belgium[13]. The study found that tax rates tend to be consistently lower in wealthier regions, than in poorer regions, questioning the notion that poorer regions would choose to cut taxes to stimulate economic activity.

It is sometimes suggested that regions with weak tax raising capacity are forced to set higher tax rates in order to fund a given level of public services and to maintain fiscal sustainability.

Arguably, however, this situation could be avoided. The introduction of tax competition could include an initial grace period during which the regions are still in receipt of central government funding. This would allow their economies time to expand in response to lower tax rates. Once businesses have invested in an area and individuals have relocated, the need for central government funding diminishes.

[13]Tax Competition between Sub-Central Governments, OECD, 2011

3.8 Policy consideration 7: Greater involvement of businesses in education policy

Over a third of the businesses we surveyed stated that changes to skills/education policy would help boost economic growth in the region in which they are based.

At present, there is a significant mismatch between local education and the skills needed by local businesses. Existing surveys such as the ICAEW/Grant Thornton Business Confidence Monitor show that skills shortages are becoming a significant constraint in certain sectors of the economy such as construction. Despite this, the number of apprenticeship starts in Construction, Planning and the Built Environment has fallen back significantly in recent years. In 2013/14, there were 16,000 starts, compared with 22,000 in 2010/11.

There should be greater linkages between Local Enterprise Partnerships and local schools, colleges and training providers. Students should be made aware of the job vacancies available in their local area and the training opportunities available to help them gain employment in these local industries should they wish. In addition, businesses should be able to inform education providers about the skills shortages they face. Local education provision should at least be partially adjusted to help address these skills shortages.

3.9 Policy consideration 8: Create more enterprise hubs/zones around universities

In addition to greater linkages between Local Enterprise Partnerships and the education sector, more could be done to proactively encourage the establishment of local business hubs and clusters around the UK's universities. For example, enterprise zones with tax reliefs could be created around the universities.

The benefits of increasing collaboration between businesses and universities are potentially wide-ranging. The World Economic Forum's Global Competitiveness report ranks the UK 2nd in the world for quality of scientific research and many universities remain an untapped resource to help support business innovation and research. Successful collaborations are already taking place across the country.

For instance, PwC and the Institute for Chartered Accountants in England and Wales have been supporting Newcastle University's business school in offering their 'Flying Start Degree Programme'. However, not only could more collaboration take place on a national level but more could be done to internalise the benefits of the UK's university system to the local city economies.

The establishment of hi-tech industry clusters has been a key part of the recent economic success seen in cities such as Cambridge. Not only do these businesses collaborate with the two universities in the city, they also offer attractive employment opportunities for the well-educated graduates of these institutions and an allure for similarly educated graduates from elsewhere in the country and overseas. Support for similar developments around UK universities, which are well spread across the UK, could help to reduce the impact of the internal brain-drain and support both the diversification and economic prospects for local economies in the future.

3.10 Policy consideration 9: Devolve Air Passenger Duty in England

In July 2012, the government devolved powers over rates of Air Passenger Duty (APD) for direct long haul flights to the Northern Ireland Assembly. In September 2014, the cross-party Smith Commission recommended the devolution of APD to the Scottish Parliament. The government introduced legislation to enable this in May 2015, as part of the Scotland Bill. In February 2015, as part of the St David's Day Agreement on the future of devolution in Wales, the government announced it will consider the case for devolving APD to the Welsh Assembly.

Regional airports in England have expressed concern about the impacts of APD devolution to Scotland and Wales on their business. Specifically, they are concerned that a decision to lower APD rates in Scotland or Wales could draw passengers and airlines away from their airports.

Devolution of APD would allow councils in England to compete on APD. By offering lower APD, demand for use of regional airports would increase and this would support aviation activity in these parts of the UK. Alternatively, central government could vary APD rates in England without full devolution of the setting of these rates.

4 Conclusions

This report shows huge gaps in economic performance across the UK. Undoubtedly the economic powerhouse of London is leaps and bounds ahead of every other part of the country when it comes to economic output, productivity and employee earnings. Our "nowcast" of city activity shows that London's economy is currently around six times the size of Greater Manchester, while Inner London alone is just under 10 times the size of Birmingham.

Our forecasts suggest that, despite the Government's Northern Powerhouse agenda, the gap in economic performance across the regions will widen over the next ten years.

Building regional powerhouses outside the capital is crucial, especially as London is in many ways becoming a victim of its massive success. The high demand to live and work in London has pushed up house prices to such an extent that it is harming business performance by squeezing consumer spending and making it harder to attract and retain talent. Over a fifth of the London businesses we surveyed thought that more homebuilding was the number one policy for boosting economic growth in the capital – more popular than any other policy.

Across the UK, of all the businesses we surveyed, addressing infrastructure spending was the most commonly cited number one measure for boosting regional economic growth – with a strong preference for road and local rail over national projects such as HS2. This suggests the Government ought to rethink its current transport strategy and refocus on local road schemes to support regional powerhouses outside of London.

After winning the May general election, David Cameron vowed to lead a "One Nation" Conservative government. Yet significant announcements to spread growth across the UK have been surprisingly lacking to date. The findings of this report suggest that more radical measures are needed to generate a series of regional powerhouses, including:

- Further reform of business rates and possibly replacing rates with a land value tax.
- A rethink of transport strategy to focus on local projects (particularly road projects).
- Drastic measures to resolve housing shortages, particularly in London.
- Tax competition.
- A regional Living Wage.

Without these, David Cameron risks breaking his "One Nation" vow, particularly as further austerity holds back the economies of some of the UK's poorest regions. It is vital that private enterprise is allowed to thrive in these regions as a way of offsetting austerity.

Appendix – survey information

As part of this research, a YouGov survey of 1,007 British businesses was undertaken.

The survey took place between 24th August 2015 and 1st September 2015.

Notes

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