

Appendix 1.2 - Update to the Swansea Bay City Region Economic Strategy Economic Context Chapter

Swansea Bay City Region Economic Context

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08 January 2016

Introduction

1. This paper provides an *updated* summary analysis of the economy of the Swansea Bay City Region (SBCR). It is based on the Economic Context chapter of the City Region's Economic Regeneration Strategy, produced in 2013 by SQW Ltd. The paper re-investigates headline economic performance and prospects, reprises the challenges facing the City Region, and looks forward to consider how the economy might develop over the next 15 years.

Headline economic performance and prospects

The City Region is underperforming economically. . .

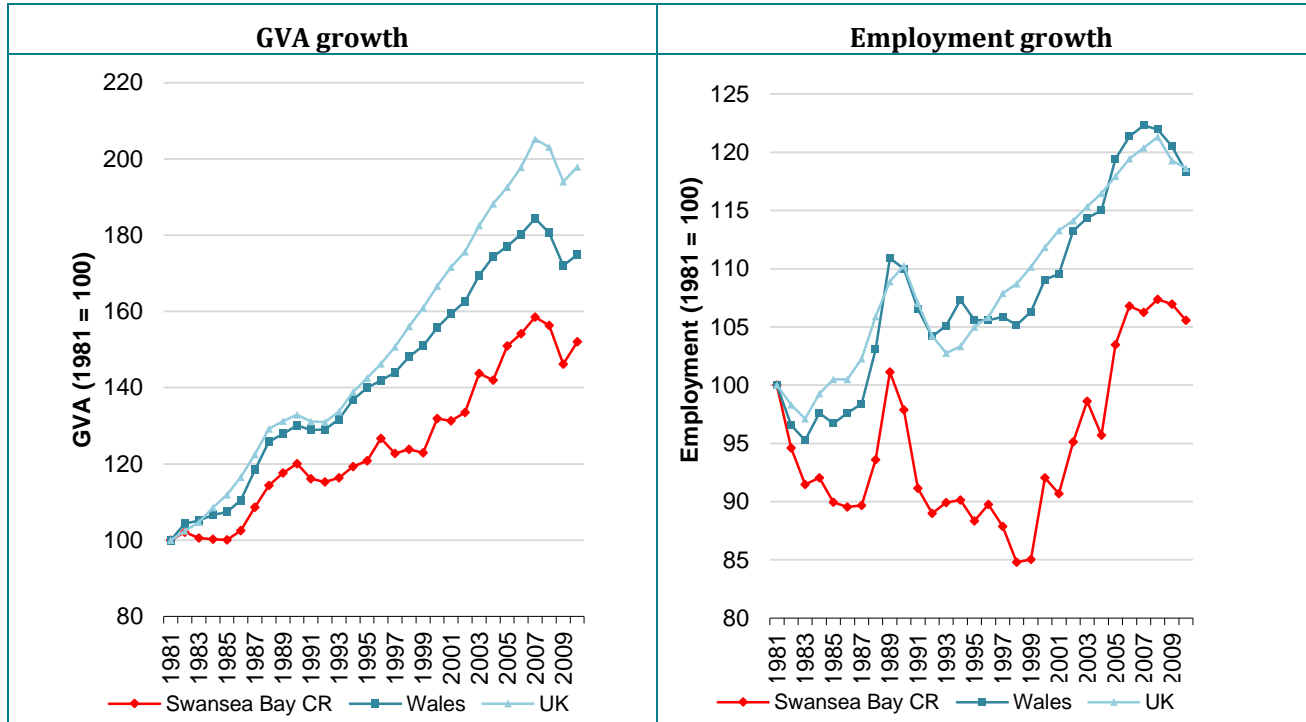
2. **With a resident population of 688,000, and supporting some 302,000 jobs in about 22,000 businesses, the SBCR is a major driver of the Welsh economy.** Beyond the headline numbers, it contains globally significant firms - e.g. Tata Steel in Neath Port Talbot and Valero in Pembrokeshire – and private sector centres of expertise such as the DVLA. The City Region benefits from its leading universities, providing a vital mix of research, development and teaching capabilities. The area also benefits from an excellent quality of life offer, with mature and well regard tourism and leisure assets.

3. **SBCR has benefited from significant investments in its infrastructure over the past decade.** These range from the regeneration of Llanelli town centre in Carmarthenshire, to the portfolio of incubation centres created across the City Region, and on to the 'Harbour Way Project', linking Port Talbot and the Docks to the M4 is creating a vital link east to Cardiff, the wider UK motorway network and mainland Europe (the largest transport project in Wales since the construction of the M4). Major improvements have been made to the A40 in Pembrokeshire, and the development of Swansea University's new Bay Campus (SA1), an applied R&D campus led by Swansea University, offers the prospect of a radical uplift in the City Region's innovation, technology, and engineering capacity.

4. **This recognised, SWCR is underperforming economically, and failing to reach its full potential.** The primary indicator used to measure an economy's overall performance is Gross Value Added (GVA). The City Region generated GVA of £10.5bn in 2015, which accounted for 20% of the Welsh total. The city of Swansea accounted for £4.1bn, Carmarthenshire £2.6bn, Neath Port Talbot £1.9bn, and Pembrokeshire £2.0bn. Therefore, while Swansea is clearly vital to the City Region's overall economic prospects, all four of the area's Unitary Authority Areas matter economically, notwithstanding their different economic roles.

5. Long-run both GVA and employment growth rates in the City Region were below consistently those of the UK and Wales between 1981 and 2010, as shown in Figure 1.

Figure 1: GVA and employment growth 1981-2010 in the Swansea Bay City Region, Wales and the UK



Source: SQW analysis of Cambridge Econometrics data, 2016

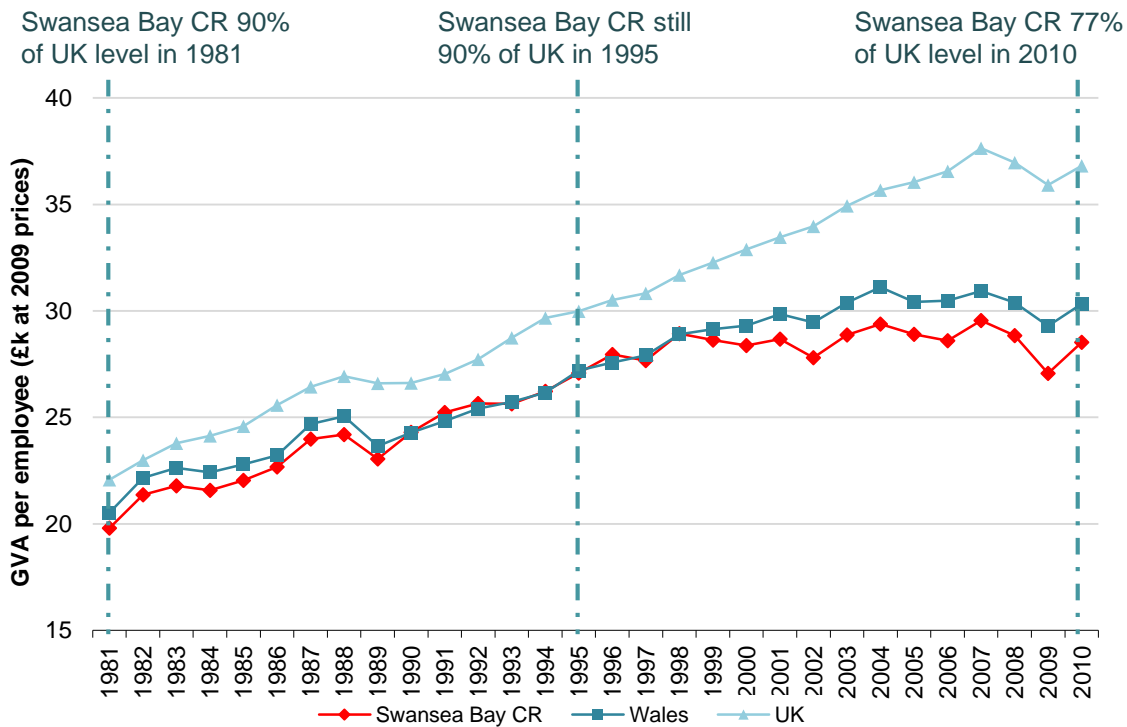
6. The City Region's underperformance in GVA growth became most pronounced in the aftermath of, and longer-term recovery from, the 1990/91 recession. Over the following decade, as firms closed down or left the area and were not replaced, employment volumes also fell. This trend was the polar opposite to what was happening nationally, where employment levels increased.

... and must respond quickly to the productivity imperative

7. Employment growth in the City Region returned by the end of the 1990s, and continued to rise until the downturn/recession hit, nationally, in 2008. However, too much of the employment created across the City Region over this period was in lower value sectors and occupations, often in parts of Education, Health and the wider Public Sector. And as traditional employment in the City Region was lost, with, for example, over 30,000 fewer jobs in manufacturing in 2010 than was the case in 1990, **a major productivity gap emerged between SBCR and the UK. The productivity gap is now the key factor underpinning the City Region's sub-optimal economic performance** and is the unambiguous priority of the City Region's *Economic Regeneration Strategy*.

8. GVA per employee in the City Region was £34,300 in 2015 (at 2011 prices), against a comparable figure of £46,200 in the UK, or 74% of the UK average. By contrast, in 1990, GVA per worker in the City Region was 90% of the UK level, as had been the case in 1981. Clearly, external factors are at play here, with UK growth driven by the performance of London as a leading global city and the wider South East of England in particular. However, **productivity in the City Region has also fallen below the Welsh level for the past 15 years**. In 2015, productivity in the City Region was equivalent to only 93% of the Welsh level. The decline in our productivity relative to the rest of Wales and the wider UK can be seen in Figure 2, looking at the 1981 to 2010 period.

Figure 2: Productivity in the Swansea Bay City Region, Wales and the UK, 1981-2010



Source: SQW analysis of Cambridge Econometrics data, 2016

9. This productivity deficit is *not* because workers in the City Region work less hard than those elsewhere. Indeed, the average hours worked in our City Region are essentially the same as in the rest of the UK. Rather, two key factors drive this under-performance. First, the sectoral mix of the economy as a whole is geared towards lower value sectors compared to the UK. Second is the nature of occupations on offer within these sectors, which are generally of a lower value than elsewhere. Only in 'Electricity, Gas and Water' and 'Accommodation and Food Services' is productivity higher in the City Region than the UK. Table 1 refers.

10. This productivity deficit matters: if GVA per employee in the City Region in 2015 was at the UK level, the economy would generate an extra £3.6bn pa. SBCR is significantly less wealthy than it could be.

Table 1: Sectoral employment and productivity (2011 prices) in the Swansea Bay City Region and the UK (2015)

	Swansea Bay City Region		UK	
	% employees	GVA per worker	% employees	GVA per worker
Manufacturing	9%	£52,554	8%	£58,653
Electricity, gas & water	1%	£102,341	1%	£98,469
Construction	8%	£30,629	6%	£44,363
Distribution	15%	£27,315	14%	£37,579
Transport & storage	3%	£29,321	5%	£41,371
Accommodation & food services	6%	£21,065	7%	£19,770
Information & communication	2%	£44,813	4%	£72,160
Financial & business services	14%	£36,669	22%	£50,614
Government services	32%	£29,407	26%	£33,113
Other services	6%	£22,425	6%	£32,413

Source: SQW analysis of Cambridge Econometrics data Note: excludes Agriculture and Mining, 2016

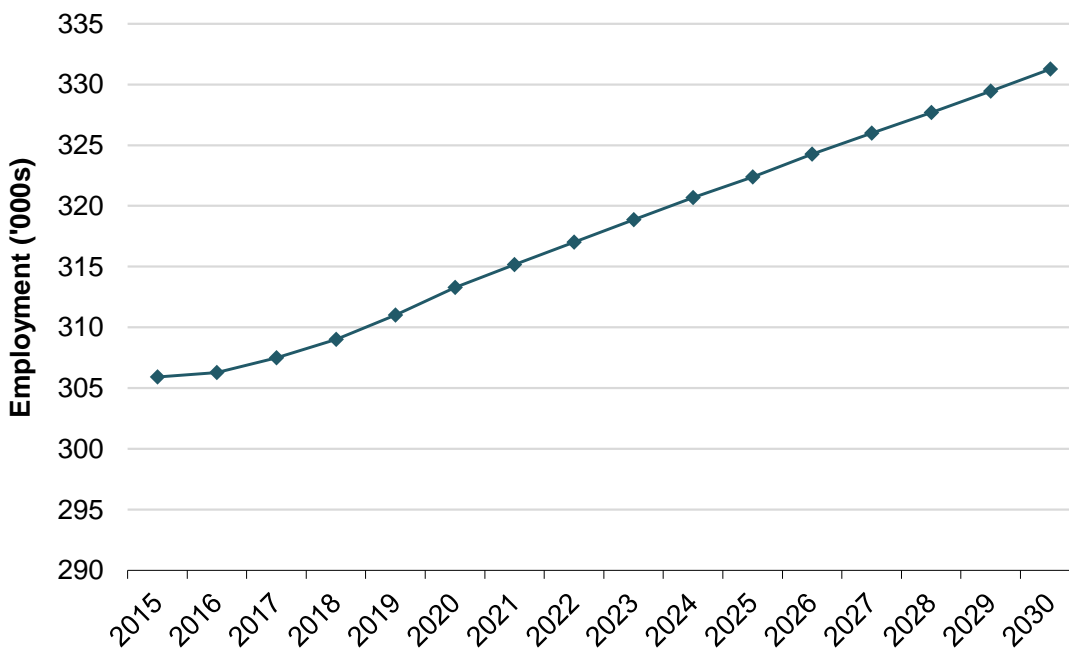
11. Looking forward, **the productivity gap between the Swansea Bay City Region and the rest of the UK is forecast to remain in place unless action is not taken.** Unaltered, by 2030, GVA per worker in the City Region is forecast to be £43,200 (2011 prices), compared with £59,100 in the UK, i.e. just 73% of the UK total. **If the area does not act to drive productivity improvements, it will continue to perform at about three-quarters of its true economic potential.**

... and ensure that the area's positive employment prospects are realised

12. There is no doubt that tackling the productivity imperative is fundamental to raising the prosperity (and thereby quality of life) of the City Region. But there is a second, related challenge, namely that of creating new, and sustaining existing, employment for the City Region and its workers. As the data show, following the 1990/91 recession it took the Swansea Bay City Region over a decade to recover in employment terms.

13. However, forecast data suggest that the City Region has been much more resilient in the face of the 2008/09 recession, and will grow strongly in the coming years. Although employment in the SBCR had slipped to 288,000 in 2012, by 2015 it had risen to 306,000, well-above the pre-recession peak of 297,000 (2008). By 2030, employment is expected to build to 331,000, an increase of 8% on 2015, as depicted in Figure 3. These projections suggest stronger growth in the City Region than across both Wales and the UK, and represent a marked improvement in expected fortunes from the projections available in 2013.

Figure 3: Employment forecast for the Swansea Bay City Region, 2015 to 2030



Source: SQW analysis of Cambridge Econometrics data, 2016

Other economic challenges and opportunities . . .

14. Other issues facing the City Region are as follows:

- **On Enterprise, the area has too few businesses and is not growing its business base quickly enough.** The latest data indicate that the City Region had fewer businesses per head of the population than the UK as a whole (518 per 10k of the Working Age population, compared to 602 across the UK) meaning that there are fewer businesses to generate the wealth and employment opportunities for local people than elsewhere. That said, the *rate* of new business formation in the City Region (53 per

10k of the Working Age population in 2015) is higher than in Wales (44), although lower than the UK as a whole (58), so there is prospect of the gap with the UK closing.

- **On Skills, there are major deficits across the City Region. The area has insufficient people with higher level qualifications, and too many people with no qualifications at all.** Increasingly, as the UK competes on the basis of quality, and as economies globally develop their own capacity, the skills of the labour market will be a key determinant of economic success. Currently, the Swansea Bay City Region underperforms against the UK, with only 31% of residents having NVQ4+ qualifications (degree level or equivalent), compared to 36% across the UK. Further, 12% of Working Age residents have no qualifications, compared with 9% in the UK.
- **On Employment, unemployment and economic inactivity remains too high across the City Region.** All places across the UK suffered as a result of the late 2008/09 recession in terms of rising unemployment and economic inactivity. However, over the long-term, engagement in the labour market has been lower in the City Region than elsewhere, and economic activity in particular is now well below national levels – at 74% in the Swansea Bay City Region compared to 77% in the UK (and 75% in Wales). Further, jobs are all too often in those occupations which tend to pay relatively low wages; the average weekly salary in the City Region was around £369, compared to £426 in the UK.
- **On Land, Property & Infrastructure, despite the significant investment that has gone into the physical fabric of the Swansea Bay City Region over the past decade, major challenges still remain.** In terms of the physical offer, much of its commercial and retail property is of a low quality, and there is limited speculative commercial development activity as demand is low and potential rents and take-up rates are poor; gap funding is often necessary to bring schemes forward. Further, the connecting infrastructure requires investment; rural communities across the City Region face limited broadband availability, and strategic transport links to the West of the City Region in particular are under-developed, limiting the potential for internal City Region commuting and business-to-business linkages. Air connectivity to major international business centres from South Wales also needs to be improved.
- **On Inclusion and Communities, although many of the area's places are prosperous, too many of its communities continue to suffer from high levels of multiple deprivation and poverty.** There are pockets of very severe deprivation in all of the area's Unitary Authority Areas, and across both urban and rural places. In many of these areas, inter-generational worklessness remains a stubborn issue to address, often exacerbated by physical isolation, through poor local transport links.

15. These are important challenges to be sighted on. But there are also major opportunities to build on:

- **SBCR has many important innovation and knowledge economy assets.** Its Universities provide both pure and applied R&D offers, as well as expertise in Cultural/Creative industries. The new £200m Bay Campus of Swansea University is one of the UK's major transformational innovation projects, with the potential for creating thousands of new high quality jobs - directly and indirectly – now starting to be realised. It will deliver a step change in the City Region's innovation offer and will put Swansea on an international platform; much of the site opened in 2015, with completion expected by 2020. It is essential that the economic and wider impacts of this strategic development are maximised.
- **The area has existing strengths in key sectors with potential to drive productivity gains and boost economic competitiveness,** both through existing firms and through new in-movers and

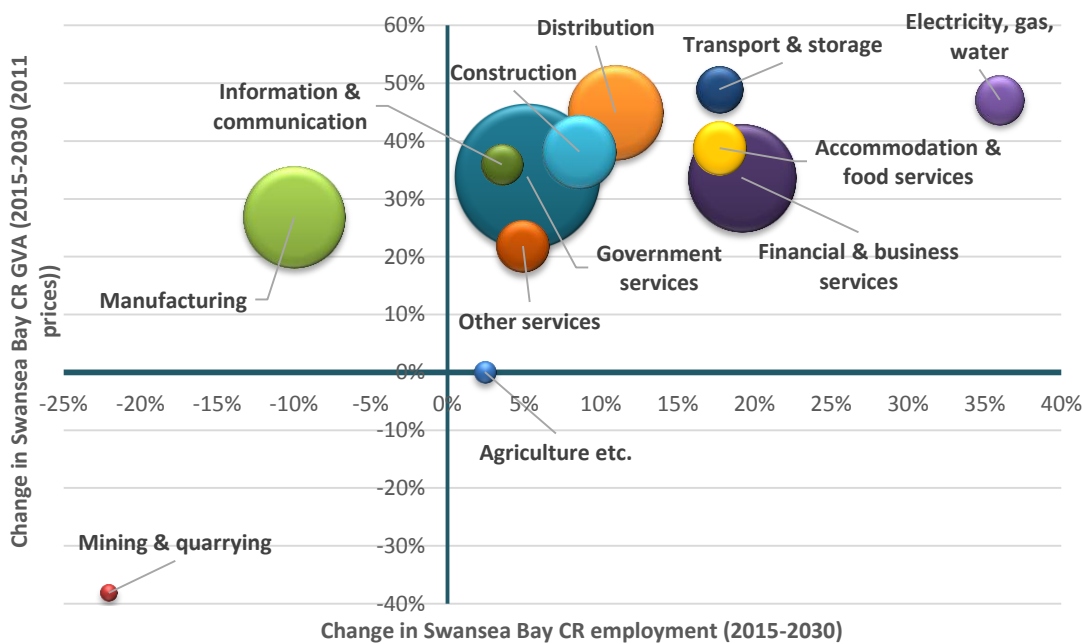
further enterprise development. These sectors include: Energy, Advanced Engineering/High Value Manufacturing, Financial and Business Services, ICT, and Tourism.

- **SBCR’s natural environment, and its local places, offer residents, visitors and investors a very attractive quality of life.** The area’s jewels include the Pembrokeshire Coast National Park, the Gower Peninsula, rural Carmarthenshire, and the Brecon Beacons National Park. Swansea Bay City Region ‘the place’ is a strong brand on which to build and market, not least as an affordable choice for families, with an average housing cost of under £128k, compared to more than £217k across England and Wales.

Insights in to the changing economy of the future

16. SBCR’s economy will experience significant change over the next two decades. Although the area has experienced large-scale industrial re-structuring already, the economic projections from Cambridge Econometrics suggest that changes in the sectoral mix of the economy will continue to impact on SBCR’s future economic performance and wider prospects. The overall sectoral shape of the economy over the next 15 years is summarised below:

Figure 4: Sectoral shapes over the next two decades (size of the bubble = GVA in 2015)



Source: SQW analysis of Cambridge Econometrics data, 2016

17. From the Figure above, three types of broad sector are evident:

- *Expanding Sectors*, which will witness growth in GVA and employment
- *Adjusting Sectors*, where GVA will increase, but employment is likely to decrease¹
- *Shrinking Sectors*, which will see both GVA and employment decrease over the next decade.

18. Drawing on this typology, and the more fine-grained data in Table 2 below, the following points are made:

¹ Note that one sector (Air Transport) is expected to see a decrease in GVA and an increase in employment, but these are both from an exceptionally low base

- **Expanding sectors** include a broad range of knowledge orientated services, Transport and Logistics activities, the Public Sector, as well as several smaller sectors. Key expanding sectors include: **Retail; Business Support Services; Financial and Insurance; Health; Construction; Public Administration and Defence; and Accommodation**. The highest absolute growth in both GVA and employment is forecast in **Retail**. The highest growth rate for GVA is expected in **Water Transport**, while the highest growth rate for employment is expected in **Water, Sewerage and Waste**, although both sectors are small absolutely.
- **Adjusting sectors** are those that are becoming more productive as a result of continued improvements in ICT, productive processes and other economic developments, often at the expense of employment. Sectors involved are **Coke and Petroleum; Motor Vehicles Trade; and 'Other' Manufacturing & Repair**. The most divergent sector, i.e. that with the biggest disparity between jobs growth and GVA growth, is forecast to be **Food, Drink and Tobacco**, which will more than double in GVA contribution terms, but will largely stand-still in employment terms, though in both respects the sector is small to begin with.
- **Shrinking sectors** are, encouragingly, very few in number and represent only about 2% of the City Region's current GVA and 1% of current employment. The sectors are **Mining and Quarrying, Wood and Paper** and **Electronics**. Of these three, **Electronics** is expected to see the largest loss in employees (58%), but **Wood and Paper** is expected to see the largest loss in GVA (41%). Despite their modest scales, the decline of these sectors still needs to be managed carefully, with effort made to ensure that those leaving employment in these traditional industries are able to re-engage fully with the labour market, by re-skilling so that they can make the transition to higher-value sectors with sustainable growth potential.

19. Sectors such as Health, Education and Public Administration are forecast to grow over the long-term in relation to employment levels. However, over the short-term and largely as a result of austerity, significant employment loss is forecast in the public sector at large, with around 4,000 fewer employees projected in by 2017 than 2014. Given the dependence of the City Region on public sector employment – accounting for currently around 28% of workers - this represents a considerable risk to the economy. It is essential that the SBCR develops a more balanced and economic base, capable of mitigating this potential over- exposure.

Table 2: Growth in employment and GVA (2011 prices) by sector, from 2015 to 2030

Sector	Employment			GVA		
	2015 (000s)	2030 (000s)	% change	2015 (£m)	2030 (£m)	% change
1 Agriculture	9.4	9.6	2	63.4	63.4	0.1
2 Mining & Quarrying	0.7	0.6	-22	37.6	23.3	-38.1
3 Food, Drink & Tobacco	2.8	2.8	0	122.3	229.5	87.7
4 Textiles	0.7	0.5	-23	16.3	20.3	24.2
5 Wood & Paper	1.4	1.3	-7	71.7	42.3	-41.0
6 Printing & Recording	0.8	0.8	3	5.1	5.6	11.6
7 Coke & Petroleum	0.8	0.7	-21	189.6	278.3	46.8
8 Chemicals	0.6	0.5	-21	49.9	62.8	25.9
9 Pharmaceuticals	0.2	0.2	-2	28.0	36.7	31.2
10 Non-Metallic Mineral Production	2.7	2.4	-12	116.7	187.0	60.2

Sector	Employment			GVA		
	2015 (000s)	2030 (000s)	% change	2015 (£m)	2030 (£m)	% change
11 Metals & Metal Production	9.4	9.5	1	401.6	454.6	13.2
12 Electronics	0.7	0.3	-58	66.4	65.4	-1.6
13 Electrical Equipment	1.0	0.9	-13	44.1	57.1	29.5
14 Machinery	1.2	0.8	-32	53.3	62.6	17.6
15 Motor Vehicles	2.6	2.1	-18	109.0	123.4	13.2
16 Other Transport Equipment	0.6	0.6	-3	40.6	56.8	39.7
17 Other Manufacturing & Repair	2.0	1.4	-30	129.3	149.6	15.7
18 Electricity & Gas	0.8	0.8	-3	96.7	105.1	8.7
19 Water, Sewerage & Waste	2.4	3.6	49	234.6	382.2	62.9
20 Construction	24.7	26.9	9	757.5	1,046.5	38.2
21 Motor Vehicles Trade	5.9	5.8	-1	250.6	297.7	18.8
22 Wholesale Trade	7.9	8.4	6	116.8	159.4	36.5
23 Retail Trade	31.3	35.8	15	863.6	1,326.9	53.6
24 Land Transport	5.8	7.3	28	138.7	210.5	51.8
25 Water Transport	0.4	0.6	45	60.4	107.9	78.8
26 Air Transport	0.02	0.03	22	1.5	1.5	-3.7
27 Warehousing & Postal	4.2	4.3	2	104.6	134.6	28.7
28 Accommodation	5.3	7.3	38	169.8	267.5	57.5
29 Food & Beverage Services	13.4	14.7	10	222.9	277.6	24.5
30 Media	1.5	1.4	-3	89.9	100.9	12.3
31 IT Services	3.8	4.1	6	147.5	221.9	50.4
32 Financial & Insurance	7.0	9.4	34	457.0	613.0	34.1
33 Real Estate	4.7	5.9	25	382.2	552.8	44.7
34 Legal & Accounting	4.1	4.3	5	60.3	63.6	5.5
35 Head offices & management consultancy	2.4	2.5	5	31.9	36.8	15.7
36 Architecture & Engineering Services	3.2	3.0	-4	123.9	140.8	13.7
37 Other Professional Services	3.6	5.1	43	133.5	185.1	38.7
38 Business Support Services	19.3	22.5	17	435.5	579.0	32.9
39 Public Administration & Defence	22.1	24.2	9	935.9	1,241.5	32.7
40 Education	29.9	29.9	0	871.8	1,072.5	23.0
41 Health	26.7	28.9	9	890.2	1,210.7	36.0

Sector	Employment			GVA		
	2015 (000s)	2030 (000s)	% change	2015 (£m)	2030 (£m)	% change
42 Residential & Social	20.7	21.5	4	225.2	387.6	72.1
43 Arts	2.2	2.7	22	37.9	47.7	25.6
44 Recreational Services	6.2	6.2	0	113.4	121.2	6.9
45 Other Services	8.8	9.2	4	234.4	301.2	28.5

Source: SQW analysis of Cambridge Econometrics data, 2016

Understanding the scale of the opportunity

20. The Swansea Bay City Region needs to sustain and create new employment, while at the same time, driving productivity growth. This is neither simple nor easy, but the scale of the opportunity is significant. Indicatively, if the area can grow its employment base as forecast to 2030, and over that time return to 90% of the UK's productivity level, where the economy has sat traditionally, then the area would be an £18bn economy. And if the productivity could match the UK level, it would be a £20bn economy, almost 40% larger than as at present.

Table 3: The indicative scale of the Swansea Bay City Region economy based on productivity forecasts

	2020 (£bn)	2030 (£bn)
Current trajectory	11.6	14.3
At Wales level of productivity	12.5	15.5
At 90% UK level of productivity	14.1	17.6
At UK level of productivity	15.7	19.6

Source: SQW analysis of Cambridge Econometrics forecasts, 2016