The Productivity Commission

First evidence session, 'Sizing the productivity problem: international, national, regional and sectoral aspects'

Written evidence submitted by The Heseltine Institute for Public Policy, Practice & Place, University of Liverpool

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Introduction: The Productivity Problem in Liverpool City Region

The UK's productivity problem is complex and multidimensional. Its form, features, and foundations can vary significantly across geographies. In this evidence submission we consider the case of Liverpool City Region (LCR), what this can reveal about the regional dynamics of the UK's productivity problem, and the particular barriers that must first be overcome if places such as LCR are to make a larger contribution to national prosperity.

Comprising Halton, Knowsley, Liverpool, Sefton, St Helens and Wirral, Liverpool City Region is a significant economy in the North West of England. After decades of deindustrialisation and decline, LCR has recently enjoyed something of an economic renaissance, with over £1 billion added to its economy in real terms in the decade prior to the COVID-19 pandemic (LCRCA 2020:15). In this time LCR has built a more diverse economy, developing new strengths, assets, and competencies across a range of sectors (ibid. 10). Globally important firms including Unilever, IBM and Jaguar Land Rover continue to invest in LCR, whilst well-established SME clusters such as Liverpool's Baltic Triangle have supported a growing business base (ibid. 20). Meanwhile, areas of LCR, most notably Liverpool City Centre, have been substantially regenerated, symbolising the City Region's physical and economic transformation in recent years.

Yet this transformation remains incomplete. Long-standing productivity gaps, relative to the national average, have endured and, indeed, widened in the years since the 2008 financial crisis (see Figure 1). Disparities in GVA per hour worked and GVA per job filled hint towards a post-industrial, post-crisis skewing of the City Region's economy towards less productive sectors and job types. Data from 2017 suggests that, of the sectors most concentrated in Liverpool City Region, only two of these (manufacturing and public administration) are more productive than average (LCRCA 2020: 16). Simultaneously, Liverpool City Region has a higher than average proportion of part-time jobs. 34.5% of all jobs in LCR were part-time in 2019, compared to 31.9% in the North West and 32.2% nationally (Nomis n.d.).

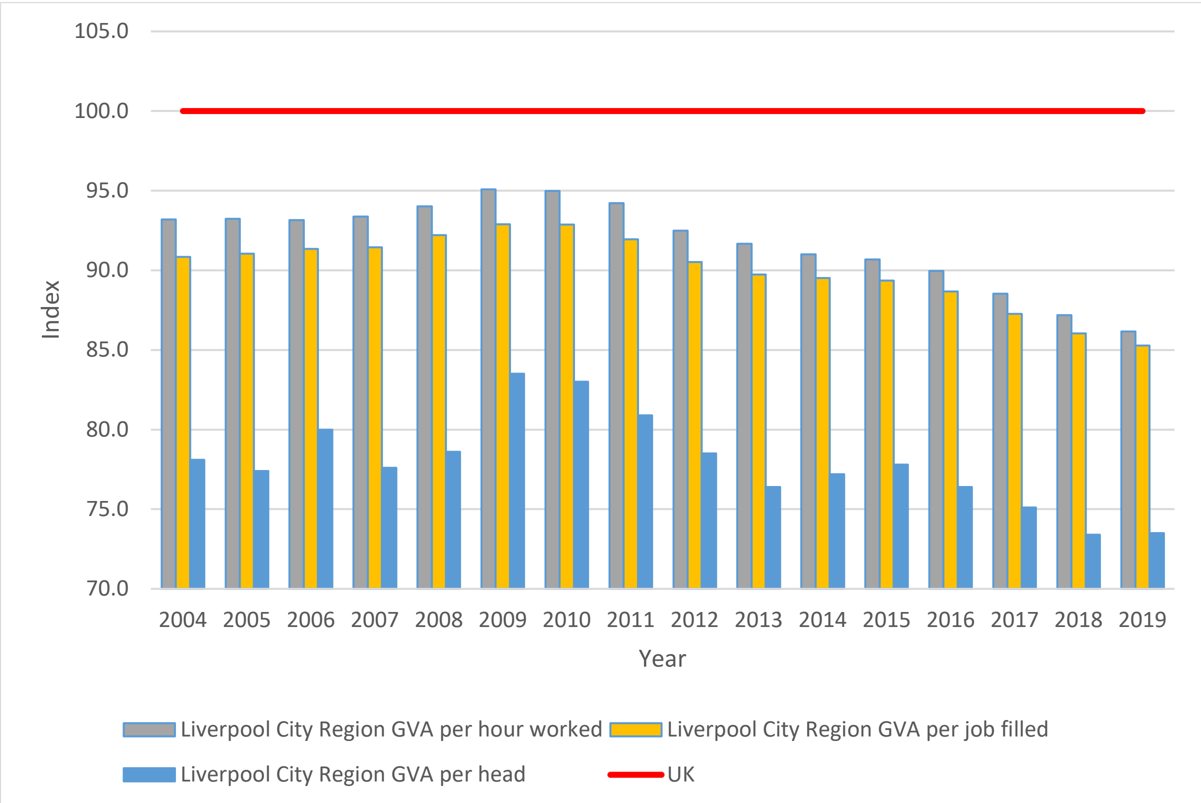

Figure 1: Productivity gaps between LCR and UK average, 2004-2019 (ONS 2021a; 2021b)

However, Liverpool City Region's productivity problem cannot simply be solved by promoting the growth of higher productivity sectors and employment opportunities. Instead performance must be improved across the whole economy. This is evident given LCR's significant gap in relation to GVA per head, which was more than 25% below UK average in 2019. This sizeable gap is a function of multiple complex socio-economic challenges that impact LCR's labour market composition, impede economic performance, and undermine quality of life.

For all of LCR's recent economic growth and success, too many people and places remain excluded from economic opportunity, with significant areas of poverty and inequality remaining. Although improving in recent years, economic inactivity remains too high in Liverpool City Region at 24%, whilst 18.6% of households in LCR are workless (compared to 21.6% and 13.9% nationally) (Nomis, n.d.). Meanwhile, almost one-third of the City Region's neighbourhoods rank amongst the most deprived in the UK (see Figure 2), with many areas of the City Region growing more deprived relative to other parts of England in recent years (MHCLG 2019: 16). These challenges are exacerbated by a very low business density (LCRCA 2020: 21), with too few businesses creating the high quality, stable employment opportunities that people and communities need to thrive. Therefore, to understand Liverpool City Region's productivity gaps, we must first understand the multiple complex factors that are preventing all people and places from effectively contributing to, and benefiting from, the local economy.

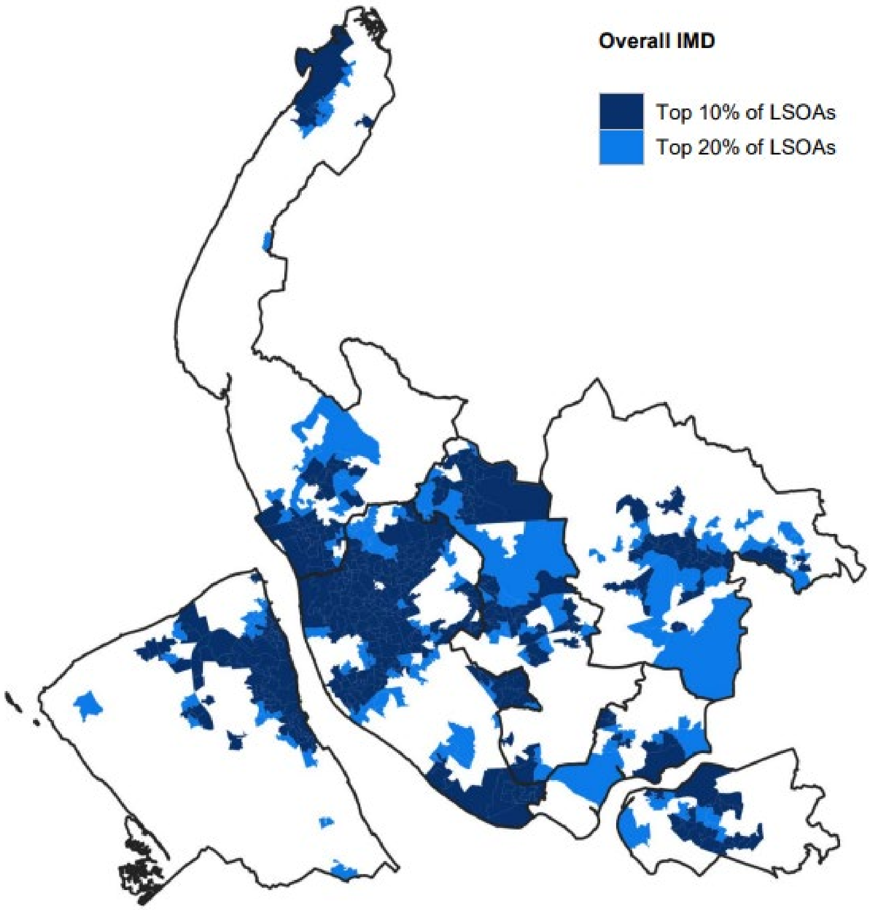

Figure 2: Most deprived Lower Super Output Areas (LSOAs) in Liverpool City Region (MHCLG 2019)

What are the key barriers to productivity in Liverpool City Region?

1. Health and Wellbeing

Average life expectancy in LCR is around two years lower than the rest of England, and there is considerable inequality in life expectancy between the most and least deprived areas of the City Region. Across LCR almost one in four people are reported as having a limiting long-term illness or disability, with poor mental health a particular concern. Around 20% of LCR's population aged 16 and over is estimated to suffer from a common mental health disorder (Public Health England n.d.). These health challenges are likely to have only been exacerbated further by a COVID-19 pandemic which has hit Liverpool City Region disproportionately hard (cf. LCR APPG 2021: 2).

This has consequences for economic opportunity and employment, with 30% of those that are economically inactive in LCR reporting that this is due to ill health (LCRCA 2020:19). A common challenge across the North of England, it is estimated that ill health is responsible for 30% of the gap in productivity between the North and the rest of the country (Bambra et al. 2018: 4). Addressing the causes of ill health must therefore be recognised as a crucial step towards improving labour market participation and productivity in places like LCR.

The socioeconomic drivers of poor health outcomes are well documented. In particular, *the Marmot Review* (2010) identified the social gradient of health inequality in England, with poorer health outcomes arising from the complex interaction of inequalities in housing, income, education, and a host of other wider social and economic determinants of health. This highlights the vicious cycle that needs to be broken in places like LCR, where economic inequality perpetuates poor health; and poor health perpetuates economic inequality.

2. Housing and Neighbourhoods

More than half the private homes in LCR were built before 1940, often to low standards, while 60% of properties have an EPC rating of D or below. Aging, low quality, energy inefficient homes present challenges for environmental sustainability, fuel poverty, and public health. In many of the City Region's most vulnerable neighbourhoods there is a particular prevalence of poor quality, low value private rented stock and some areas also experience higher than average vacancy rates that need to be addressed (LCRCA 2019a).

Improving housing choice, quality and supply is critical to addressing economic underperformance in LCR. Providing the right mix of housing types and tenures to meet demand, will be important to ensuring LCR can attract and retain the talented workforce, and private sector investment, necessary to sustain its long-term economic prosperity. In some areas this will mean improving the supply of good quality one-bedroom homes, in others a greater supply of larger, higher value homes will be required to support growing families to stay and invest in communities. Addressing poor housing quality will also be necessary to address broader socio-economic challenges within vulnerable neighbourhoods. Current concentrations of poor-quality properties often lead to higher than average population churn rates within communities, undermining longer-term neighbourhood sustainability and exacerbating place-based deprivation (LCRCA 2019a: 16). Moreover, poor housing quality risks perpetuating significant health and wellbeing challenges, as well as household poverty, within LCR's most deprived neighbourhoods.

Retrofitting existing housing stock will, along with improving the supply of good new homes, be vital to improving housing quality and choice in LCR. Co-ordinated action and investment will be needed to achieve this, with the Combined Authority calculating that at least £12 billion will be required in total to improve local housing through energy and thermal efficiency retrofit (LCR APPG 2021: 10). However, such necessary investment would not only help to improve the desirability of LCR's housing market, but would also help to support high skill, high quality jobs in the local construction sector.

Alongside improving the quality of housing, it will also be crucial to improve the quality of neighbourhoods. Although many places across LCR are vibrant and thriving, there are a number of town centres and high streets experiencing long-term decline that require a renewed sense of purpose (LCRCA 2020: 18). In many cases this decline has been exacerbated by national trends in retail and hospitality, and changing patterns of consumption (Longlands et al. 2021:17). Meanwhile other places may have experienced the loss or decline of major local employers, alongside a steady erosion of social infrastructure. Addressing this will be vital to raise living standards, increase desirability of local neighbourhoods, and enhance economic prosperity and investment within communities.

3. Connectivity

Like most English city-regions, transport within LCR remains largely car-based. 68% of journeys to work are made by car, including around half of all journeys less than 5km. High levels of car dependency have resulted in high levels of congestion, particularly at peak commuting times and around schools, and is a contributor to LCR's poor air quality (LCRCA 2021a).

The Merseyrail network is well-used and continues to grow, and is currently being enhanced through a programme of rolling stock renewal. However, other parts of the LCR rail network are of poor quality, particularly links between Liverpool and the Wirral (LCRCA 2019b).

Deregulation of bus services from the 1980s onwards has resulted in a patchwork of different operators across LCR, leaving some areas without sufficient service. Cost is also an issue, particularly for journeys using multiple bus operators.

External connectivity is a major issue for businesses in LCR, particularly given the City Region's important role in the UK's maritime, freight and logistics sectors. Inadequate rail links to the port mean freight is largely road-based, placing additional pressure on congested local networks and contributing further to air pollution.

Issues with transport connectivity in LCR restrict productivity growth in several ways. Due to weaknesses in public transport infrastructure there are fewer jobs available within reasonable commuting time than in much of London and the South East of England. This means workers in LCR have fewer options when searching for jobs, and employers have a smaller labour pool to choose from when hiring. In addition, key sectors (most notably linked to the City Region's port infrastructure) are hindered by congestion and slow journey times on local roads, and poor links to the other parts of the UK. High levels of air pollution, noise pollution and congestion also mean the living environment in LCR is poorer than it otherwise could be.

The mass adoption of working from home (WFH) will undoubtedly have some impact on this picture. There may be opportunities to increase productivity in some sectors by improving WFH conditions, for example by improving the availability and affordability of childcare, and investing in broadband infrastructure. However, Liverpool City Region has a higher proportion of residents than the national average employed in sectors where home-working is not feasible, such as retail, tourism, accommodation, distribution and building services. Tackling weaknesses in intra-city and intercity connectivity will therefore remain crucial, despite potential changes to labour market conditions over coming years.

4. Education and Skills

While there has been progress over recent years, GCSE results in LCR remain below the national average, and there are significant differences in attainment levels within the City Region (LCRCA 2021b). Over 50% of LCR pupils do not achieve the expected education standard at age 16, with low levels of Maths and English attainment creating particular problems as students leave education and enter the jobs market (LCRCA 2021c).

Poor attainment in these two vital subjects means many further education providers in LCR spend a large amount of time on ‘catch up’ courses, bringing students up to the minimum level required to be able to enter the labour market rather than developing the more advanced skills asked for by employers (LCRCA 2018), limiting progression into higher value roles.

The lack of opportunities for workers to retrain and gain new skills has also emerged as a particularly acute issue over recent years, limiting pathways to career progression. Adult participation in learning has fallen to its lowest level in nearly 25 years, with the decline amongst working adults during this period particularly stark (Smith et al 2019). Cuts to adult education funding over the last decade have contributed to this decline. The recent commitments to the National Skills Fund and Lifetime Skills Guarantee represent a welcome reversal of this trend (Sibieta et al. 2021). However, more investment in further education will be crucial over the coming years if skills gaps are to be closed.

Given the multitude of organisations involved in delivering school-age and adult education, any interventions will need to involve close co-operation between national, city-regional and local government. The London Challenge, which helped to improve educational outcomes in the capital during the 00s, demonstrates the results that can be achieved if education interventions are targeted at the right areas and in partnership with local leaders (Ofsted 2010).

Closer to home the North Birkenhead Cradle to Career Team and the Liverpool City Region Combined Authority’s Household into Work Programme (Tyrell 2020) highlights the value of locally tailored programmes which are cognisant of the multiple needs of individuals (going beyond skills alone) to deliver improved educational and employment outcomes.

5. Business Environment

Liverpool City Region has a deficit in its business base and ability to stimulate new businesses when compared to national averages. Currently, there are over 37,000 businesses in the City Region, which equates to a shortage of 18,500 businesses when compared to the national average. A business that starts in Liverpool City Region is less likely to survive three years than in other urban regions of the UK economy (a rate of 53% for businesses that started in 2015 compared to 57% nationally) (LCR LEP 2016). As a result, LCR’s business and job densities, relative to its working age population, remain very low. As of 2016, there are 535 business in the Liverpool City Region for every 10,000 working age residents. This is particularly weak when compared to 683 in Greater Manchester, or 900 in Cheshire and Warrington.

An important factor underpinning this weak business environment is the large scale of recent public sector cuts, which since 2010, have affected LCR’s consumer spending and local economy (Parkinson et al 2016). Northern English cities, such as Liverpool, have been hit hardest by austerity over the last decade. LCR has seen on average cuts of 20 percent to their spending, contrasted to only 9 percent for cities in the South West and South East (excluding London). On a per capita basis, Liverpool has seen the largest cut. Its £441 million reduction in spending equates to £816 fall for every resident in the city (Centre for Cities 2019).

Austerity has eroded day to day local government spending on services, including business support. Although the City Region has an established Local Growth Hub business support service, businesses report that there is a lack of measured and long-term incentives in the City Region that are important for capital survival, particularly for SMEs. LCR's local businesses must be supported to flourish, and more businesses must be attracted to invest and locate in the City Region. A reversal of austerity cuts will be critical to increase the number of good quality jobs and the competitiveness and resilience of LCR's business base.

6. Governance and Institutions

Developing strong local institutions is key to improving productivity in English city-regions. By international standards, the UK's system of governance remains highly centralised. Local and regional governments in England have few powers and resources to respond effectively to locally identified challenges. This should be understood as a key factor underpinning the UK's interregional inequalities (McCann 2016).

Despite moves in recent years to devolve certain areas of policy to the city-region scale, sub-national government in England has little freedom to raise revenue itself and is therefore highly reliant on central government grant funding. This situation is in stark contrast to other major European nations. In Germany for example, over 30% of tax revenue is raised at the sub-national level, compared to under 5% in the UK (OECD 2020).

Cleary, England's highly centralised governance system means any transition to greater fiscal independence for city-regions must be implements gradually to ensure a level of stability. However, in the short to medium term, subnational institutions must be given more time and certainty when designing and delivering plans to tackle long-standing economic challenges. The trend in recent years towards subnational government funding based on deals agreed with national government means funding streams are uncertain and often linked to delivery of specific projects, rather than based on delivery of longer-term policy objectives. A 'single pot' approach to local government funding, enabling local leaders to determine priorities based on local needs, is preferable. In the longer term, government should allow local government to raise and spend more of their own money. Geographical differences in economic outcomes will always mean there will need to be some degree of internal fiscal transfers directed by central government. However, allowing local governments more freedom and flexibility in fiscal policy would provide them with more resources to address productivity challenges, bringing English cities more in line with their international counterparts.

Conclusion

In many ways, Liverpool City Region is an exemplar of the UK productivity problem. Rather than realising its potential as an engine for national productivity and prosperity, and despite significant regeneration over the last three decades, the LCR economy continues to underperform, and underdeliver for local communities. Solving this problem, locally and nationally, will require an approach to the economy that seeks to disrupt multiple long-standing challenges and dismantle the vicious cycle that exists between socioeconomic inequality and low productivity.

However, economic productivity should not be seen as an end to be chased in and of itself. In isolation, such an approach would merely address a symptom, rather than the root causes, of economic underperformance in places like LCR, and could lead to a myopic focus on a small number of high productivity sectors rather than improving performance and prosperity across the whole economy. Instead productivity uplift should be viewed as a side effect of maintaining a well-functioning regional and national economy; one that effectively builds the wealth of communities, provides the foundations for good lives and livelihoods, and enables every individual to fulfil their potential. This will require coordinated, strategic interventions across the whole economy to address deeply entrenched, systemic challenges. A renewed national commitment to deeper fiscal and political devolution in places such as Liverpool City Region will be critical to achieving this.

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