

The Welsh Economy the Labour Market and Challenges

By

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Morgan Academy/WISERD Conference

20 March 2019

How City Deals could make a difference

Swansea University

Economics at Swansea University established in 1937.

It has a strong background in research on regional and labour economics and Welsh Economy going back to Nevin in the 1960s who published the first ever attempt to create a set of economic accounts for Wales and the first for any region of the UK.

Since then important research has been undertaken in these areas helped by the establishment of multi million pound research centres including WELMERC in 2002, SECR in 2008 and WISERD in 2008.

The RAE 2008 feedback on Economics to Swansea University stated, “The major strength of the Department is in Labour Economics...high quality research and policy advice on the Welsh economy for the Welsh Government is noteworthy.”

In REF2014 a number of Impact Case studies received the highest grade and were judged to be “outstanding in terms of reach and significance”, placing Swansea in the top 10 for Impact out of over 100 institutions judged by the Business Panel.



Economics at Swansea University established in 1937. Research over many years, includes work for the WDA, Equally Opportunities Commission, BP and the Welsh Government. Rhodri Morgan when First Minister for Wales noted, research from Swansea

“has contributed to new proposals to help raise economic activity”.



In response to the 2007/08 economic downturn the coalition government implemented a policy of fiscal consolidation, as the 2009-10 budget deficit reached a post-war peak of 11 per cent of GDP.

Fiscal consolidation has had, and will have, a significant impact on:

- **regions particularly dependant on welfare expenditure**
- **the size of the public sector workforce, with regional and highly local implications**

The Budget 2012 OBR forecast projected an estimated fall in government headcount of:

- **630,000 by 2015-16**
- **around 730,000 by 2016-17**

The Centre for Cities, for example, in their annual reports highlighted concerns for two major cities in Wales, *Cities Output* 2011 and 2012 - both Swansea and Newport as among the top 5 cities most vulnerable to government spending cuts.

Top 10 cities for estimated job losses in the public sector			
	Job losses	% of all job	Predicted public sector job losses by 2016 (% of total output)
1 Newport	2,200*	2.94%*	-6.2%†
2 Swansea	3,000*	2.91%*	-5.6%†

*Source Centre for Cities, 2011

†Source Centre for Cities, 2012

The size of the public sector deficit and public sector pay were central issues in the run-up to the 2010 Election, with all parties stating they would limit public sector pay rises.

The emergency budget in 2010 set out the plans for reducing the deficit with detailed spending plans for individual government departments published in the Spending Review.

- **In the Budget a two-year pay freeze was announced for public sector workers except for those earning £21,000 or less who would receive an increase of at least £250 per year.**
- **It was estimated that the pay freeze would save £3.3 billion a year by 2014/15 leading to a reduction in 320,000 public sector jobs by 2013-2014.**

In 2011 the Government considered taking a more regional/local approach to public sector pay and in the Autumn Statement asked the Pay Review Bodies to consider how public sector pay could be made more responsive to local labour market

In their evidence to the Pay Review Bodies the Treasury cited evidence from:

- Institute of Fiscal Studies (IFS) of a 8.3% public sector premium (2009 to 2011)
- Office of National Statistics 7.8% public sector pay premium April 2010

However, they note the pay premium is not uniform in some areas (Wales), it can be up to 18%.

Their Table 1 presents the IFS.

Table 1: IFS estimate of the public sector pay premium by region, 2009-2011

Estimated Public Pay Premium	Men (%)	Women (%)	All (%)
Wales	18.0	18.5	18.0
Yorkshire and the Humber	10.5	16.1	13.4
Scotland	5.6	19.9	13.4
East	12.2	14.0	13.0
Northern Ireland	15.5	10.0	12.3
North East	4.6	18.3	11.7
West Midlands	7.1	15.2	11.5
East Midlands	7.1	15.7	11.3
South West	7.5	13.3	10.4
All UK	5.5	11.3	8.3
North West	4.1	10.2	7.4
London	4.7	4.7	4.6
South East	-1.4	2.3	0.5

Source: Government Evidence to the Pay Review Bodies

Estimated public sector pay premium

Estimated average public–private hourly wage differentials
(2009 Q2–2011 Q1)

	Male	Female	All
Raw differential	+20.2	+27.5	+24.3

Notes and sources: see Table 5.4 of *The IFS Green Budget: February 2012*.

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Estimated average public–private hourly wage differentials
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	Male	Female	All
Raw differential	+20.2	+27.5	+24.3
Controlling for education, age and qualifications and region	+5.5	+11.3	+8.3

Notes and sources: see Table 5.4 of *The IFS Green Budget: February 2012*.

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In our research we subjected the IFS public/private sector pay estimates to a number of checks and that the economists have found to be included. which the research has found to be flawed. public policy.

We found their results pay gap fell when other important in determining the pay gap. The Welsh Government has stated, “HM Treasury has provided evidence which the Welsh Government regards as flawed”.

In its evidence to the Public Accounts Committee, the Welsh Government has stated, “HM Treasury has provided evidence which the Welsh Government regards as flawed”.

Their report cited our research.

Estimated public-private hourly wage differential (2009 Q2 – 2011 Q1)

	Males	Females
IFS controlling for education, age, qualifications and region (base specification)	5.5	11.3
Swansea controlling for education, age, qualifications and region	5.1	11.5
Swansea controlling for education, age, qualifications and regions – different definition of hourly wages	2.9	10.6
Swansea controlling for education, age, qualifications and regions – including additional controls* and different definition of hourly wage (full specification)	-4.1	5.3

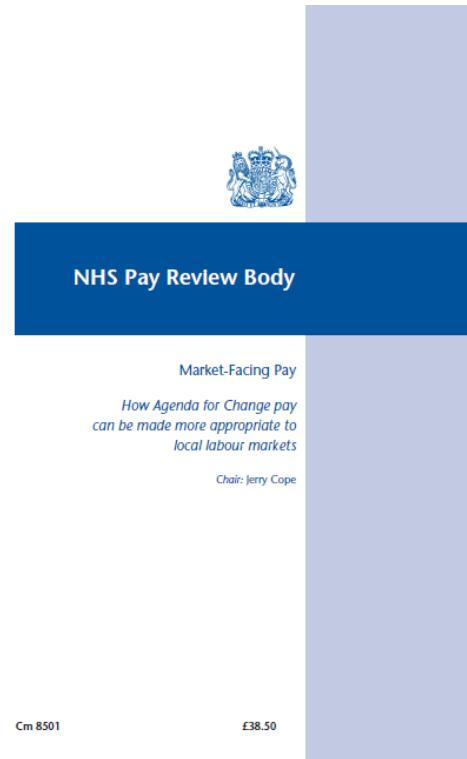
* Notes additional controls include, additional education controls, establishment size, occupational controls, managerial responsibilities, job tenure.

In the Autumn Statement 2012 the Chancellor announced he would not be pursuing market-facing p

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Subsequent research by the ONS (2012) found when introducing organisational size into wage equations the public/private sector differential fell from 7.3% to 2.2%. The Deputy Director, Public Policy Analysis Division ONS stated 2013, when working to improve their estimates of the public/private sector pay differential stated,

“As part of this work we looked at and evaluated external work across a wide range of organisations. One piece of work that was particularly useful was the analysis carried out by Swansea University which offered new insights into some of the variables that influence the pay gap. A particular area of interest was the use of firm size within our model which we had not considered in our earlier work. Having studied the work of Swansea on this variable we then explored using this within our model which improved our analysis and offered new insights.”

Contribution of the research

Economics at Swansea has therefore had an important input into the debate initiated by the Chancellor of the Exchequer in 2011 for millions of public sector employees in the UK which was subsequently abandoned in 2012.

This would have resulted in millions of public sector workers in relatively less prosperous areas of the UK seeing a reduction in their real wage rate and consequently living standards.

The Welsh Labour Market

Wales faced a major challenge of restructuring its economy following the decline of staple industries in the 1970s.

During the 1980s and 1990s it was claimed (mainly by politicians) that the Welsh economy had been successfully transformed.

Coal and steel industries, the backbone of the economy, were being replaced by lighter and more buoyant manufacturing industries helped by large amounts of FDI.

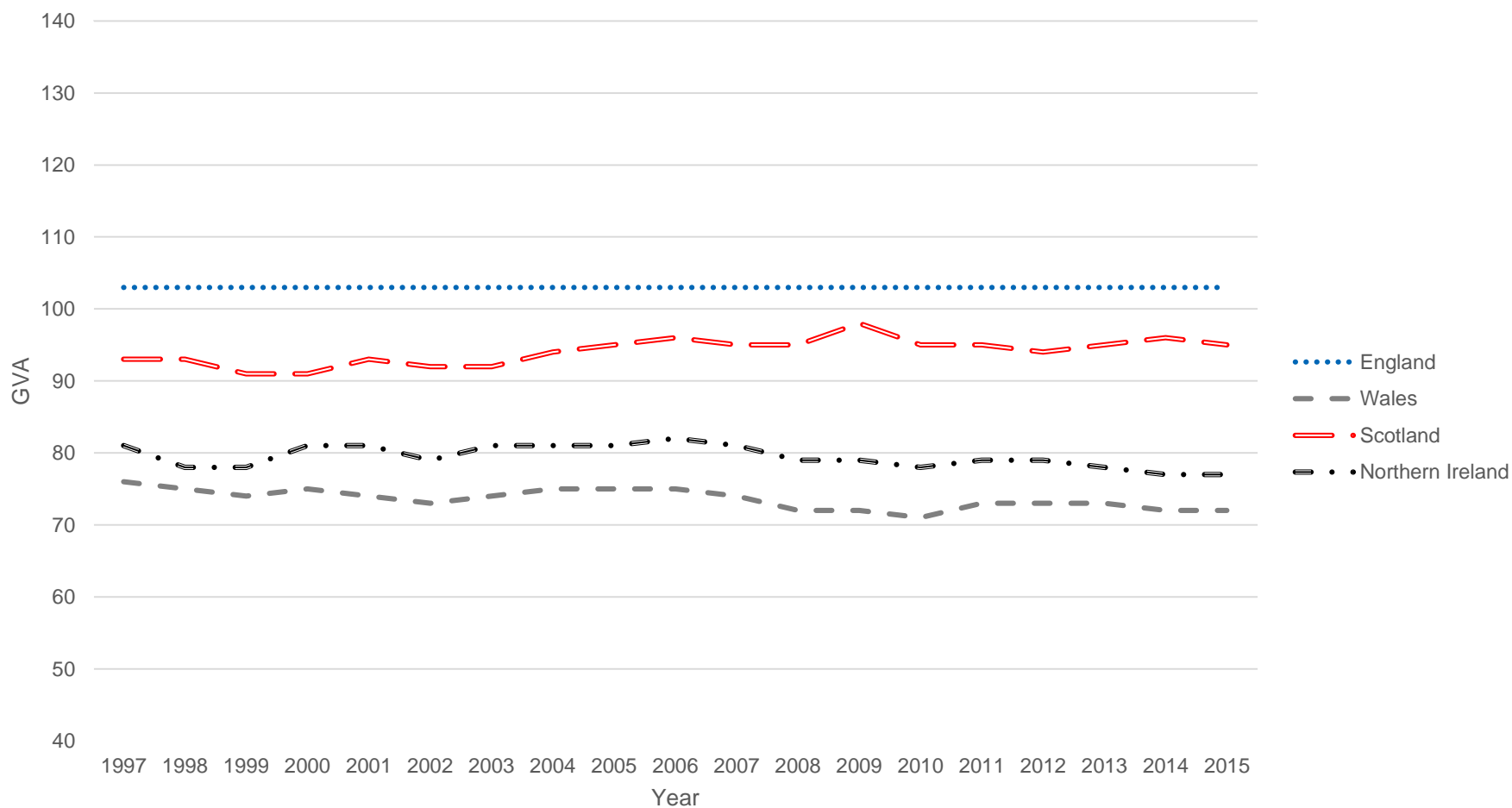
This view didn't go unchallenged and it was noted Wales was near or at the bottom of regional economic league tables measuring economic prosperity.

For example, in 1970 GDP in Wales was 92 per cent of UK average

- **1983 88 per cent**
- **2008 70 per cent**
- **2016 73 per cent**

Measures of GDP as a measure of economic welfare has been challenged.

Figure 1
Gross Value Added by area and component



Within Wales a substantial gap in levels of GDP per head exists between East and West.

Proximity to Offa's Dyke and its major lines of communications to neighbouring English centres of population are major determinants of the more successful areas. However, the notion of an East-West divide is too simplistic since great economic inequalities exist between communities within regions.

Earnings

In 2017 Wales at the foot of the regional earnings league table with a weekly average earnings of £579 per week.

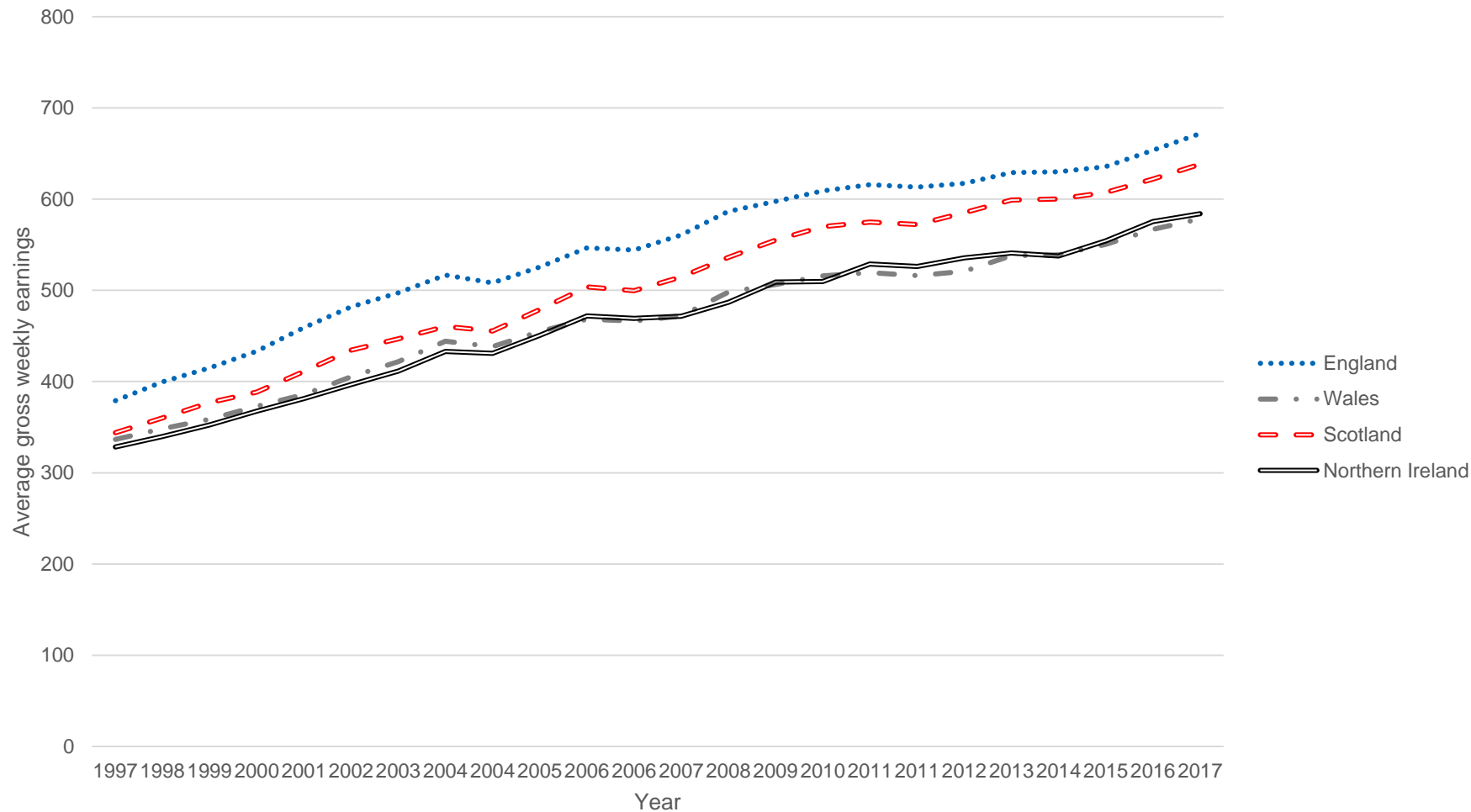
- **£672 in England**
- **£638 in Scotland**
- **£584 in NI**

Wales wasn't always at the bottom of the league tables,, in 1971 earnings were above those of Scotland and many English regions.

Substantial regional variation in earnings exists within Wales, with clear evidence of a rural/urban and East/West divide.

Gwynedd had the lowest level of earnings in 2017 (as it did in 1997) at £412 per week, compared to £536 in Flintshire and £529 in Cardiff.

Figure 2
Average gross weekly earnings



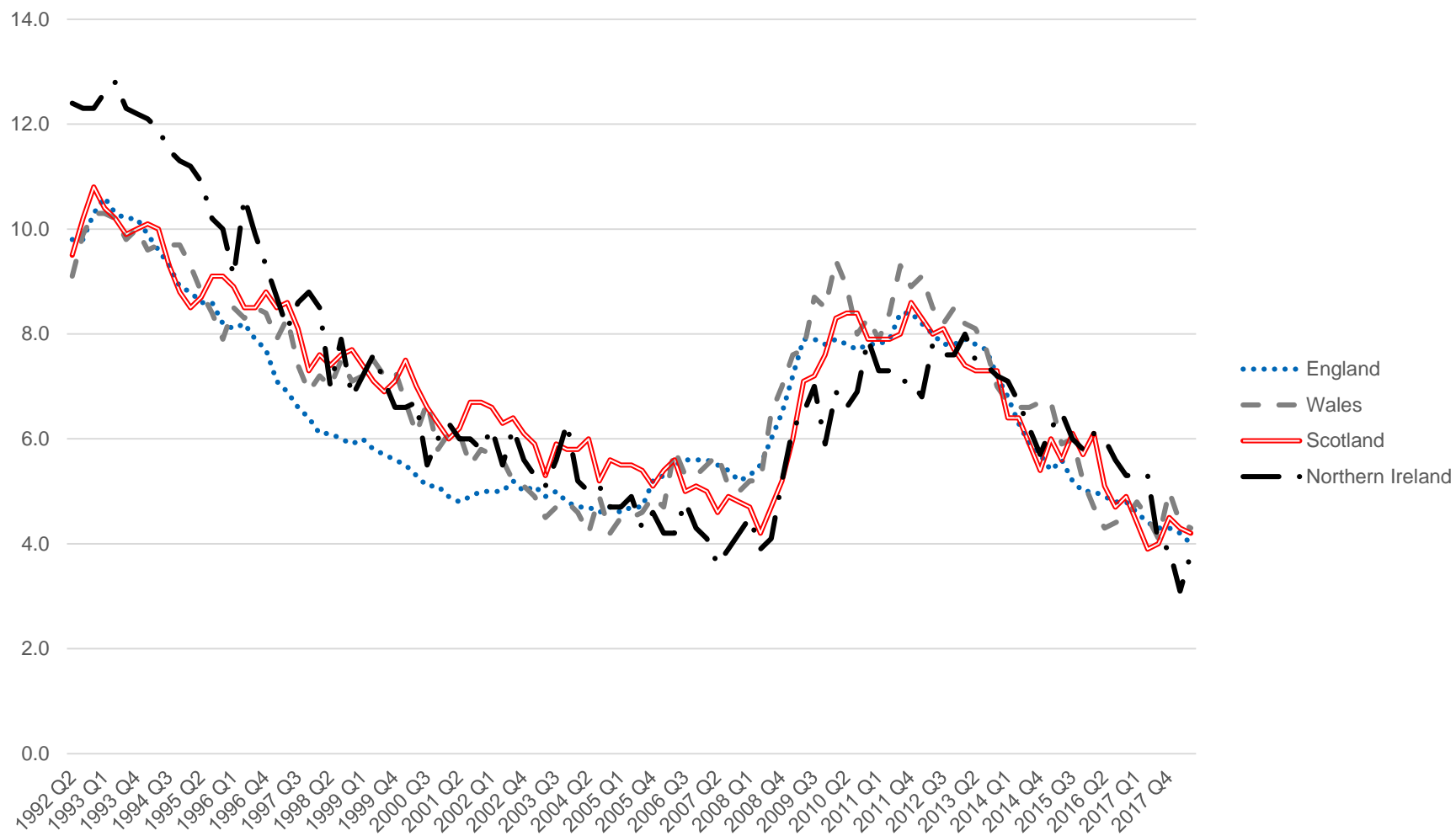
Unemployment

Restructuring of the Welsh economy has been accompanied by relatively high levels of unemployment, with large local variations.

The ease and speed with which individuals found work depended on the characteristics of the unemployed and the health of the local labour market. Those labour markets heavily dependant on a small number of firms and in sectors in relative decline faced considerable problems.

In more recent recessions regional unemployment disparities have declined.

Figure 3
Unemployment rate



Employment

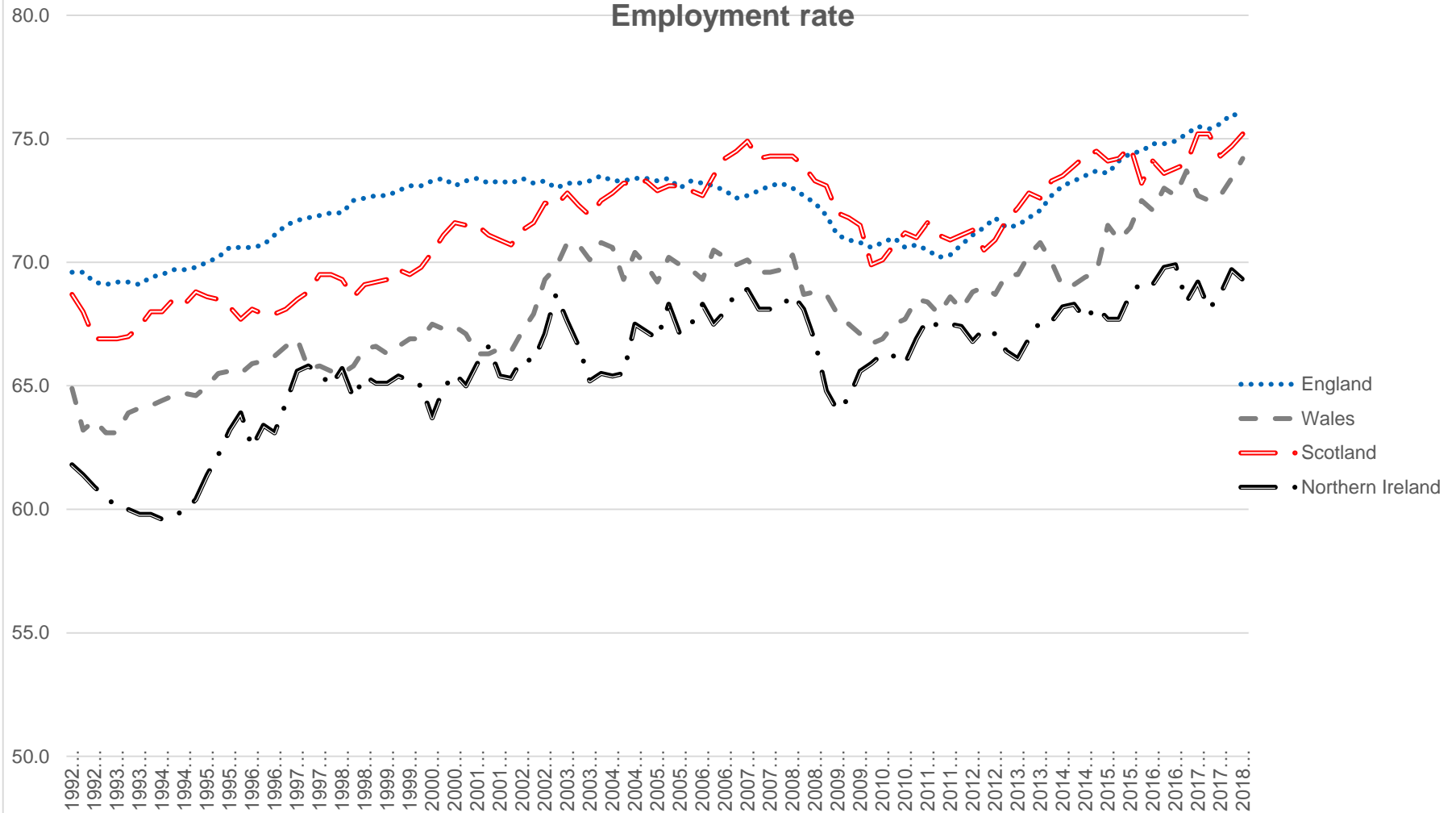
Wales also had relatively low employment rates and high levels of economic inactivity.

In the 1990s the difference between employment rates in Wales and England was over 5 percentage points.

Today the employment rate in Wales is higher than the UK average. Reductions in economic inactivity rates followed introduction of policies by UK government (both Labour and Conservative) to make work pay.

In the most recent recession the Welsh Government introduced ProAct and ReAct programmes (estimates suggest around 10,000 jobs were safeguarded).

Figure 4
Employment rate



Public Sector Pay

Gender Pay Gap

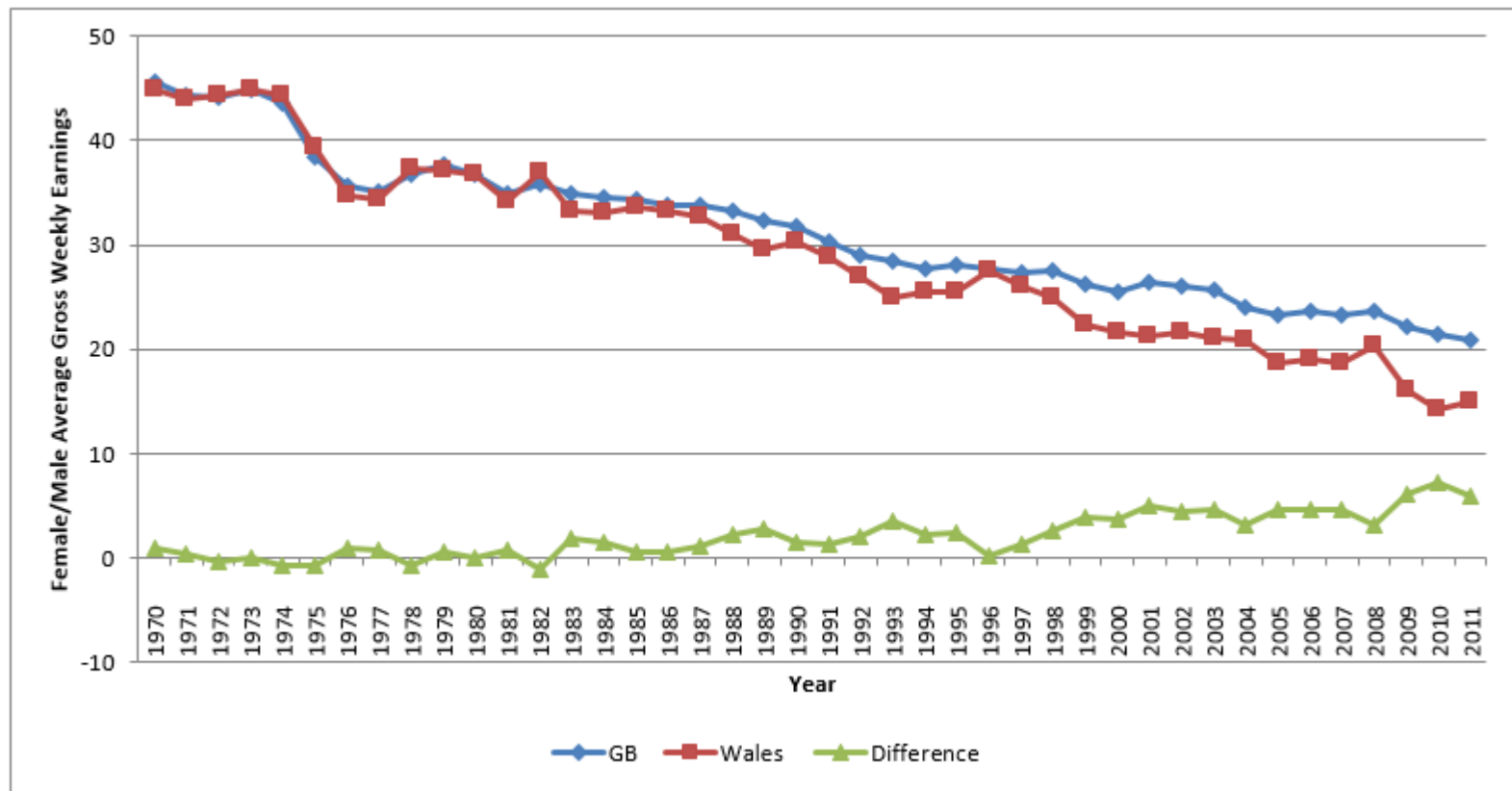
After 1996 in particular Wales generally does better than the UK in closing the gender pay gap.

Zero-hour Contracts

In 2015, 48,000 individuals in Wales were on zero-hour contracts. The third highest of any devolved nation or English region, after the North West and South West. Research finds advantages tended to accrue to employers and the disadvantages to employees.

Figure 5

Female Average Gross Weekly Earnings (including overtime) as a Percentage of their Male Counterparts, 1970--2011



Education

An important determinant of an individual's earnings is the level of qualifications obtained and the amount of job training undertaken.

Much has been written on the education system in Wales since devolution and not all of it favourable.

- Burgess *et al.* (2013) fall in GCSE results (equivalent to 1.92 GCSE grades per student per year) compared to England when school league tables were abolished in 2002.
- Rees and Taylor (2014) given higher levels of poverty found in Wales, one would expect lower levels of achievement, however “there is at least a *prima facie* case that attainment levels in Wales lag behind those in comparable countries.

The emphasis following devolution appears to have been on nation building with an emphasis on bilingual education.

The concern that the education system may not be delivering the necessary skills required by the labour market is longstanding.

Back as far as 1776 Adam Smith in the Wealth of nations wrote, “the greater part of what is taught in schools and universities...does not seem to be proper preparation for that of business”.

It matters what is taught, economic returns to university degrees varies widely across degree subjects.

Average annual salary, 11 years after graduation, 2006 values

Clinical dentistry	£61,718
Economics	£51,768
Law	£49,450
Engineering	£46,992
Computer Science	£45,363
Mathematics	£45,037
Accountancy	£44,071
Business and management	£41,796
Politics	£37,407
Languages	£37,393
History	£36,143
Geography	£34,558
Sociology	£31,047

Source: *Mapping the Careers of Highly Qualified Workers*, HERCE Research Series, July 1997. Data are based on a sample of 1,410 male graduates.

Most lucrative degrees, 10 years on

Degree	Women's salaries	Men's salaries
Medicine	£45,400	£55,300
Economics	£38,200	£42,000
Engineering and technology	£23,200	£31,200
Law	£26,200	£30,100
Physical Sciences	£24,800	£29,800
Education	£24,400	£29,600
Maths and Computer Science	£22,000	£26,800
Business	£22,000	£26,500
History and philosophy	£23,200	£26,500
Social sciences	£20,500	£26,200
Biological sciences	£23,800	£25,200
European languages and literature	£26,400	£25,000
Linguistics and classics	£23,200	£24,100
Veterinary and agriculture	£18,900	£21,400
Creative arts	£14,500	£17,900

Base: Median annual salary

Source: IFS. *How domiciled graduate earnings vary with gender attended, subject and socioeconomic background*

Britton, Dearden, Shepherd and Vianoles (2016)

Brexit

Brexit could have dramatic implications for the Welsh economy although the trading arrangements after Brexit are still to be agreed so costs and benefits are unknown.

- relatively large agricultural and manufacturing sectors
- could reduce FDI inflows to UK and Wales
- uncertainty in the area of regional aid. Since 2000 Wales has received approximately £5bn in Structural Funding.

Regional Policy

Wales was the only area in the UK receiving the highest rates of EU support, new policy might spread support more evenly across the UK.

It follows current Industrial Strategy thinking it may be based on identifying places that have, “the potential to contribute towards economic growth”, so based on impact rather than current need, which could be detrimental to Wales.

To date regional policy in the UK recognised the importance of attempting to reduce regional inequalities:

- in 1970s special needs of Wales was recognised in the Barnett Formula.
- also many public sector jobs moved out of London.
- perhaps Wales needs its own internal type Barnett Formula more active strategy of moving public sector jobs out of Cardiff.

Exchanging some of the Barnett funding for tax raising powers, is risky and takes away part of our safety net.

Moving away from a needs based approach to regional policy to one based on potential and performance could result in some of Wales poorest areas falling further behind.

City deals are already changing the shape of regional policy.

Concerns have been raised around the transparency of City Deals, and governance arrangement and lack of deal for Mid Wales region.

Such deals add to the structure of bureaucracy surrounding economic policy in Wales given we already have devolution which does not exist in England.

These deals, initiated from London, lack a coherent wall Wales approach, with certain parts of Wales, especially rural areas, are already economically disadvantaged being left out.