

# 1 The UK regional–national economic problem

## 1.1 Introduction to the UK regional–national economic problem

The UK is a deeply uneven country on two broad dimensions, namely the geographic dimension and the governance dimension. The effects of modern globalisation, and in particular the links between automation, out-sourcing, off-shoring and the ‘hollowing out’ of many middle-skills jobs, mean that while globally we have observed a broad international convergence between countries’ incomes, within advanced economies we increasingly observe a greater polarisation and divergence of incomes (Bourguignon 2015; Atkinson 2015a, 2015b; Galbraith 2012). In other words falling inequalities internationally are widely associated with increasing intra-national inequalities (McCann 2008; Goos *et al.* 2009; Iammarino and McCann 2013). However, intra-national inequalities also challenge good governance (Galbraith 2012; Berg 2015). Yet, the extent to which these inequalities are also both geographical and regional in nature is almost unique in the case of the UK. In most other advanced economies these changing employment, skills and income distributions are dispersed much more evenly across the country, whereas in the UK they appear to be more heavily biased towards certain regions than in almost any other advanced economy. Moreover, although they pre-dated the 2008 global financial crisis by several decades, these divergence trends have accelerated in the years immediately before and after (Williams 2011) the crisis. Being characterised by these long-standing interregional divergence processes the economic geography of the UK nowadays increasingly reflects the patterns typically observed in developing or former-transition economies rather than in other advanced economies. As we will see in this book, these interregional inequalities also challenge good governance.

As well as interregional inequalities part of the reason is that the UK also simultaneously exhibits one of the most highly centralised governance systems in the industrialised world (Cheshire *et al.* 2014; Coy 2014; RSA 2014; HoC 2014; Adonis 2014; RSA 2015; Diamond and Carr-West 2015). After more than 70 years of increasing centralisation (Diamond and Carr-West 2015)<sup>1</sup> central government in London rather than sub-national government dominates almost all arenas of policy-design, policy-making and

## 2 *The UK regional–national economic problem*

policy interventions to a scale that is almost unknown elsewhere amongst the advanced economies. According to the UK Prime Minister David Cameron “This country has been too London-centric for far too long”<sup>2</sup> and

Over the last century Britain has become one of the most centralised countries in the developed world ... I am convinced that if we have more local discretion – more decisions made and money spent at the local level – we’ll get better outcomes.<sup>3</sup>

and largely the same point is made by the previous UK Prime Minister Gordon Brown throughout his recent book (Brown 2014) and by the Chancellor of the Exchequer George Osborne.<sup>4</sup> At the same time, however, the UK has an also varied and increasingly unequal regional governance system which in many ways is completely out of step with the economic geography realities of today’s UK economy and which works well neither in theory nor in practice. A governance system which in the past appeared to be reasonably well-suited to responding to both national and regional challenges now appears to be increasingly incapable of such responses, in some sense reflecting the regional divergences and in other senses exaggerating them (Bogdanor 2015a).

It is this stark mismatch between the UK’s interregional economic geography and the UK’s regional governance system that is at the heart of the UK’s regional economic problem. Moreover, the scale of this misalignment between the economic geography and the governance system is now so great that most simple policy, academic and constitutional ‘solutions’ offered as remedies for resolving the “over-centralised state and the south-centric economy that are two of Britain’s biggest problems”<sup>5</sup> wholly fail to address the fundamental nature of the problem, which is the *combination* of these two problems.

In order to understand why this mismatch is such a fundamental problem there are two major features that we need to be aware of, namely the role of interregional inequality, and the role of appropriate governance systems, in the functioning and performance of a modern economy. These complex issues are discussed in great detail in the various chapters of this book, but at this stage we can highlight the broad outlines of some key themes central to the overall arguments in the book.

In terms of income inequality, there is now a growing body of evidence emerging from very high-level sources such as the IMF and OECD which demonstrates that growth in internal income inequality is not beneficial for long-run national economic growth (Berg and Ostry 2011; OECD 2014a, 2015a; *The Economist* 2014a) and neither is inequality beneficial for urban (Royuela *et al.* 2014) or regional (de Dominicis 2014) economic growth.<sup>6</sup> In particular, in the case of the UK the adverse effects of growing income inequality since the 1980s on the economy’s long-run performance since 1990 have been the third worst in the OECD (OECD 2014a). Whereas previous growth models tended to focus almost entirely on aggregate productivity growth with

little concern for distributional issues, nowadays environmental sustainability and social cohesion are increasingly understood as being essential elements for ensuring strong growth in the long term. In particular, greater income inequality limits the opportunities and thereby inhibits the ability of the lower middle classes to engage and participate in growth-enhancing activities such as education and entrepreneurship, and this subsequently reduces social mobility (OECD 2014a). While higher social class households are largely unaffected by rising income inequality its adverse impacts are felt almost entirely by the lower 40 per cent of the income spectrum, and these adverse impacts on such a broad group reduce the long-run lost potential of the economy (OECD 2014a). At the same time, there is no evidence that redistributive measures promoting access to skills-training, education and welfare via taxes and transfers hamper long-run growth, as these provide social investments for enhancing and widening opportunities.

The awareness that growth is a more multi-dimensional phenomenon than was appreciated in the past has been emerging over the last decade (Stiglitz *et al.* 2009). Indeed, this shift in thinking towards a more multi-dimensional understanding of growth and development reflects something of a worldwide shift away from the more narrow and largely sectoral approaches popular in previous decades which tended to focus almost entirely on investments in human, physical and research capital with little regard for social or environmental sustainability. These new and broader lines of international<sup>7</sup> thinking which pre-dated the 2008 global financial crisis (Stiglitz 2002; Krugman 2003, Porrit 2005) have of course also been bolstered by the painful experience of the 2008 global economic crisis (Roubini and Mihm 2010) and subsequently have underpinned a range of very high-level international reports and commissions examining the nature of growth and development (Stiglitz *et al.* 2009; OECD 2009a; World Bank 2008, 2010a, 2010b). As with previous research, these shifts in thinking have not produced a simple and complete analysis of growth. Rather, what these shifts in thinking all share is a growing consensus that successful long-term development needs to be environmentally aware,<sup>8</sup> broad-based and socially inclusive (World Bank 2008, 2010a, 2010b; NIC 2012; OECD-Ford Foundation 2014) in order to be long-lasting (OECD 2014a, 2015a; Berg and Ostry 2011; Ezcurra 2007; *The Economist* 2014a; Florida 2010; Sachs 2011; Stiglitz 2012, 2015; Piketty 2014), and rising income inequality (Stiglitz 2012; Piketty 2014) is evidence that the current growth trajectory is moving against these desired societal trends (Dorling 2011).

From a policy perspective, these shifts in thinking also imply that in order to be effective policies must be built on a broadly based political consensus. In other words, as well as enhancing economic drivers modern policy approaches to growth and development must also connect with the broader dimensions of social and environmental sustainability, because each of these features plays an important role in fostering the economic, social and civic engagement aspects underpinning the different dimensions of wellbeing (OECD 2011a).<sup>9</sup> As a result, recent policy frameworks such as the 2009 OECD “Global Standard”

#### 4 The UK regional–national economic problem

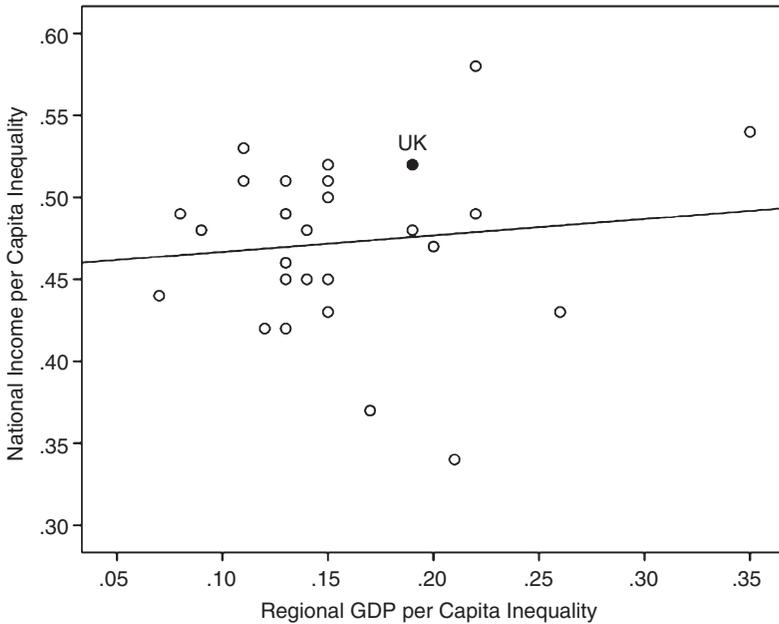


Figure 1.1 National income inequality (pre taxes and transfers) and interregional inequality in GDP per capita across OECD and BRIICS countries

Sources: OECD (2013, 2014c); OECD Database.

growth strategy (OECD 2009a) of ‘stronger, cleaner and fairer growth’,<sup>10</sup> the Europe 2020 Strategy of ‘smart, sustainable and inclusive’ growth (European Commission 2010), and the US growth strategy of ‘sustainable communities, innovation clusters, revitalizing neighborhoods’<sup>11</sup> all aim to better translate these dimensions into a broader agenda and framework for policy-makers. Yet, changing policy frameworks are themselves unlikely to solve these problems in the near future, and in reality reflect a changing set of emphases and priorities for current and future decision-making. In contrast, today’s internal domestic income inequality is a result of complex social, economic and historical forces as well as political decisions taken over many previous years regarding the role, the scale and the use of the state’s fiscal resources. As has also been mentioned above, over recent years the forces of modern globalisation are also increasingly influencing internal income disparities in many different countries. For our purposes here, however, an important observation is that internal national income inequality is also associated with interregional inequality.

Figures 1.1 and 1.2 show the scatterplots across the OECD and BRIICS<sup>12</sup> countries in 2010 of the relationships between the Gini index of interregional GDP per capita – calculated at the OECD-TL3 level – and the Gini index of domestic income inequality, prior to and post taxes and transfers,

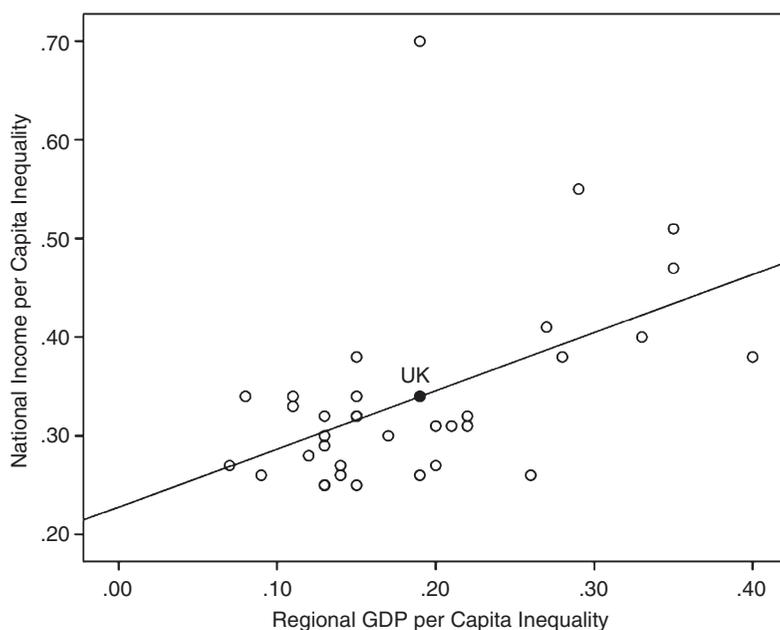
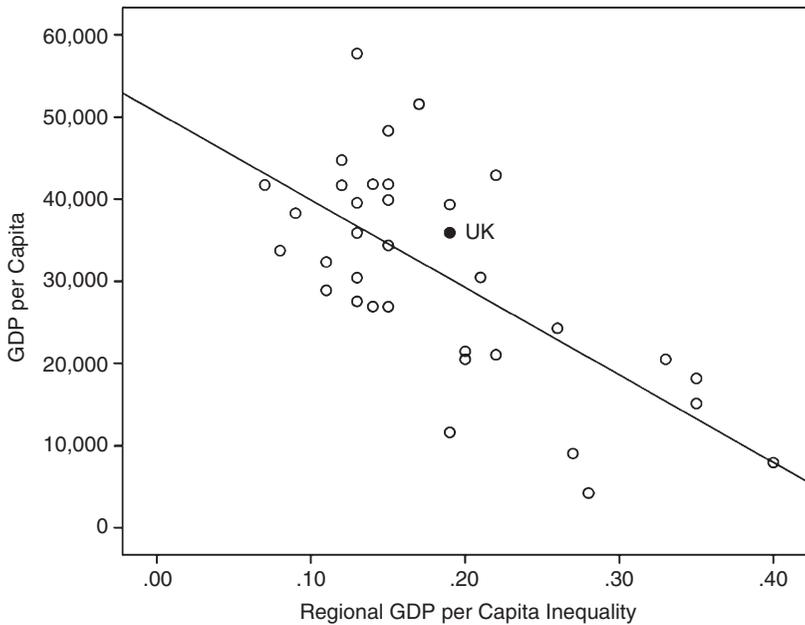


Figure 1.2 National income inequality (post taxes and transfers) and interregional inequality in GDP per capita across OECD and BRIICS countries  
Sources: OECD (2013, 2014c); OECD Database.

respectively. In general countries in the lower left part of the scatterplots exhibit low income inequality and low interregional inequality in GDP per capita while those in the upper right hand part of the scatterplots exhibit high income inequality and high interregional inequality in GDP per capita. Countries in the lower right hand part of the scatterplots exhibit high interregional inequality in GDP per capita but low income inequality while those in the upper left part of the scatterplots exhibit high national income inequality but low interregional inequality in GDP per capita.

As we see from Figure 1.1 and 1.2 there is a correlation between the level of national interregional inequalities in GDP per capita and also the national levels of income inequality, measured either before or after taxes and transfers. We know that the differences between the pre and post transfers and taxes inequalities are a result of the extent to which the national tax systems are redistributive, and across the OECD these systems differ significantly. Yet, even allowing for these differences, the general pattern remains clear that interregional inequality in GDP per capita is associated with higher national income inequality. As such, some levels of income inequality appear to be largely independent of spatial or regional issues, while higher levels of inequality do appear to be related to spatial, geographical and regional issues.



*Figure 1.3* National GDP per capita and interregional inequality in GDP per capita across OECD and BRIICS countries

Sources: OECD (2013, 2014c); OECD Database.

In both cases the position of the UK in the scatterplots is significant. In each of the two scatterplots the UK is at the upper right extreme of the scatterplot of the rich OECD countries with only one of the countries to the right of the UK exhibiting a higher GDP per capita than the UK. All of the other countries to the right of the UK are poorer countries than the UK, comprising the BRIICS countries plus Latin American countries, along with the former transition economies in Europe. In contrast, the countries to the left of the UK in the scatterplots are primarily the group of richer OECD economies, with 12 of the countries to the left of the UK exhibiting higher GDP per capita than the UK.

One often used response to these types of observations is that the national and interregional inequality scores of the UK are primarily due to the great success of the London economy, a genuine ‘global city’ which provides an enormous boon to the overall UK economy and which must not be jeopardised. As we will see in Chapters 2, 3 and 4, the evidence for this position is very much weaker than is typically understood. Yet, doubt about the veracity of this argument immediately emerges from Figure 1.3.

Figure 1.3 displays the scatterplot of the relationship between national GDP per capita and interregional inequality in GDP per capita. This relationship is downward sloping such that scatterplot points in the upper left

hand side of the figure are countries with high GDP and low interregional variations in GDP per capita while those in the bottom right of the figure represent countries with low GDP per capita and high interregional inequalities in GDP per capita. As we see in Figure 1.3, the scatterplot point of only one of the 14 OECD countries with equal or higher GDP per capita than the UK and for which interregional data are available, is located to the right of the UK. All of the other countries to the right of the UK exhibit lower GDP per capita than the UK.

At this stage we make no claims here regarding the mechanisms or directions of causality regarding the relationships between interregional inequalities, national inequalities or national levels of GDP per capita, nor the reasons for the particular position of the UK in these OECD-BRIICS scatterplots. It is simply sufficient at this stage to point out that as a general cross-country pattern there is a positive relationship between interregional inequality in GDP per capita and national income inequality and also a negative relationship between interregional inequality in GDP per capita and national GDP per capita. Yet, one of the issues which emerges immediately from both the observation that interregional inequality, national inequality and national productivity are correlated with each other in differing ways and also that our understanding of growth and development is shifting to a broader and multi-dimensional appreciation, is that the role of place and geography is not neutral. Greater interregional differences imply greater national differences and clues as to much of what is happening nationally are therefore also to be found in what is happening locally. Moreover, this is not simply an aggregation or scaling issue, but rather an essential point about the economic role played by cities and regions in driving national growth. As such, nowadays local and regional elements quickly enter into national growth and policy discussions (OECD 2011b, 2014b) and one of the most obvious policy challenges to be faced is the fact that the trade-offs and complementarities between the different stronger (smart), cleaner (sustainable) and fairer (inclusive) growth dimensions differ between regions and localities (OECD 2009a, 2009b, 2011b, 2014b; Moretti 2012; Hughes 2012). Moreover, while trade-offs tend to arise naturally in contrast complementarities often have to be constructed (Braga de Macedo and Oliviera-Martins 2008, 2010; Braga de Macedo *et al.* 2013), and as such these differences pose major challenges for local, regional and urban policy, aiming to foster stronger and more resilient growth (Zolli and Healy 2012). In particular, the institutional and policy-setting frameworks need to be adaptable to these differing circumstances, and emerging evidence from numerous sources suggests that appropriate and well-functioning governance systems are essential for fostering growth both locally and nationally (OECD 2011a, 2012, 2014b).

These issues would appear to be particularly pertinent in the case of the UK. In Figs 1.1 and 1.2 we see that the UK is at the upper end of each of the dimensions of the OECD inequality scatterplot distributions. As we will see in Chapter 2, in the UK the interregional inequalities have increased

markedly since the early 1990s, as have national income inequalities. Indeed, across the whole of the OECD's 34 countries as well as the EU28 (Armstrong and Ebell 2015), the UK is now one of the most unequal countries according to interregional inequalities, as well as both forms of income inequality. Furthermore, as Chapter 3 argues, the performance of the UK's large cities also largely depends on which region they are located in. As such, in terms of economic geography, the UK's regional and urban challenges are largely synonymous with each other. Moreover, to the extent that UK long-run growth performance has been significantly and adversely affected by rising internal income inequality, the UK's rising interregional inequality is likely to be a fundamental part of this story. Indeed, understanding the interregional inequality story is the major objective of the first five chapters of this book.

The second major issue to be discussed concerns the questions of institutions and governance. While market mechanisms are central to our understanding of the processing re-shaping economic geography (World Bank 2009), at the same time contemporary thinking about economic development (Rodrik 2007) also emphasises that well-functioning and appropriate governance systems are essential for fostering economic growth. Indeed, modern regional economic development approaches (Pike *et al.* 2010; OECD 2011b; Barca *et al.* 2012; Storper 2013; McCann and Ortega-Argilés 2013) follow exactly the same logic. However, in the particular case of the UK there are growing intellectual grounds for arguing that the current UK governance system may not be particularly appropriate, well-suited or well-functioning for responding to the realities and challenges thrown up by today's UK economic geography, characterised as it is by significant and growing interregional inequalities (Armstrong and Ebell 2015). Moreover, and in some ways even more important than the growing intellectual arguments are the recently shifting public perceptions. A broadly based alignment of public perceptions is essential for underpinning the salience, credibility and legitimacy (Cash *et al.* 2003) requirements of national governance and institutional systems and when these perceptions begin to shift or fracture the salience and legitimacy of the current workings of government begin to weaken. The various devolution and independence debates being played out within the UK suggest that there is now also a growing groundswell of public opinion in the popular press and the world of politics that national, regional and local governance and the links between these three governance levels (*The Economist* 2014b) may not be ideally suited to the UK's interregional and economic geography realities. Understanding the causes of the UK's interregional inequalities and also the links between these inequalities and the UK's different types of regional and national governance systems is therefore imperative if we are to improve the future functioning and performance of the UK economy. Therefore, the major theme examined by the second part of the book comprising three chapters concerns the question of how UK governance can be better shaped to respond to the UK's current economic geography

realities and the intellectual ideas and insights driving these debates. These arguments depend partly on internal discussions and experiences and also on insights from other countries. However, this is not so straightforward, because of the pattern of internal UK political discourses.

A problem here is that UK internal political and popular debates tend to pay very little heed to the possible lessons derived from other countries, and where they do so, they tend to overly emphasise insights from the USA or other rich Commonwealth countries such as Australia, Canada or New Zealand which have similar legal and land market systems to the UK. This is particularly the case when discussing issues heavily shaped by modern globalisation such as inequality and governance. As much as anything this myopia is likely to be related to our poor foreign-language skills which limit our exposure and awareness of developments taking place in other more appropriate comparator countries. In addition, UK academic debates also tend to be heavily dominated and in some cases over-dominated by US-oriented debates. The UK interregional inequalities are so large and over such short distances that these ‘Anglo-Saxon’ comparisons offer rather little in terms of useful insights. Moreover, these other ‘Anglo-Saxon’ countries all tend to be very different to the UK in terms of governance systems, most notably having separate political and economic capitals, and in all but one case functioning as a federal state with a written constitution. In contrast, the UK is in many ways both a very strange as well as a unique polity and more fruitful insights can be gained by observations from a broader range of comparator cases than the usual set of other English-speaking countries which are typically alluded to. Most of these alternative comparator cases are in Europe or East Asia but there is often a reluctance in the UK media to engage seriously with the lessons and insights from these countries. In part, this is due to a lack of awareness of the potential for learning that the UK can enjoy by considering these cases, and to some extent this is also driven by a lack of appreciation of the lead that some of these countries have over the UK in various specific matters. The reasons for this lack of awareness and appreciation are likely to be found in a mix of linguistic limitations and cultural perceptions, but whatever the reasons, the point is that they inhibit UK learning from other more appropriate cases. We will return to these issues shortly at the end of this chapter.

In terms of governance, the United Kingdom nation-state is comprised of four nations: England, Scotland, Wales and Northern Ireland, each with different governance systems, and all of which are embodied in different ways within the overall UK governance system. Each of the four member nations of the unified UK state displays different levels and forms of autonomy relating in each case to different issues. While on cultural grounds, and to differing extents also political grounds, these four operate as countries or partially autonomous regions, in purely economic grounds they each operate as open regions within the unitary national state. Yet, to some extent this situation is already beginning to change in a rather ad hoc manner into something of a quasi-federal state (Bogdanor 2015b).

The recent debates and the 2014 vote on Scottish independence, plus the ensuing Smith Commission<sup>13</sup> recommendations regarding the devolving of income tax powers to Scotland have subsequently spurred a wider debate regarding devolution and decentralisation amongst not only the four constituent nations of the UK, but also amongst the cities and regions of England (*The Economist* 2014c, 2014d, 2014e; Brown 2014; Mount 2014; Gallagher 2014; *The Guardian* 2014a; *The Spectator* 2014). As we will see in Chapter 6, these debates and various policy actions and governance reforms long pre-date the Scottish independence referendum,<sup>14</sup> but the Scottish vote has given a major impetus to these debates. These debates are particularly pertinent in the case of the UK because UK local government has a very limited role by international standards (OECD 2013), with the vast majority of its funding and policy priorities and implementation frameworks being decided centrally. At the same time, the three devolved regions of Scotland, Wales and Northern Ireland display differing degrees of autonomy from the Westminster government. However, within England in particular, the highly centralised and largely top-down and ‘one-size-fits-all’ governance system is wholly at odds with the economic geography of the UK. In terms of economic geography the current reality of the UK economy is one of almost unprecedented inequality and these inequalities are most marked in the case of England. Moreover, the UK as a whole, and within the UK England in particular, is not only a largely unitary state, but one which is more centralised than almost any other large state anywhere else in the world (Cheshire *et al.* 2014; Coy 2014; RSA 2014). The business cycles and patterns of economic shocks across UK regions are today less correlated than those between countries across the European Union with the London economy in particular becoming increasingly disconnected from the rest of the UK (Deutsche Bank 2013). In other words, the internal workings of the UK interregional economic system are in many ways actually less cohesive and integrated than the wider EU economy. Indeed, at the level of the 12 UK OECD-TL2/EU-NUTS1 large statistical regions the scale of UK interregional differences in GDP per capita is comparable to the international GDP per capita differences across 17 European countries and across 22 OECD countries. At the lower level of the OECD-TL3/EU-NUTS3 regions of the UK, the interregional GDP per capita differences within the UK are comparable to those across 22 European countries and 27 OECD countries.

One outcome of these inequalities is that the UK does not resemble anything like an optimal currency area and as we will see in detail in Chapter 6 these increasing UK interregional inequalities pose fundamental questions regarding the economic governance of the unified UK state. While on the one hand the various parts of the English economy increasingly appear to co-exist without any real economic interactions taking place with other parts of the same country, at the same time on the other hand, the English governance system in particular, is based on the assumption that England is economically a cohesive whole, which it is clearly not. Given the economic governance difficulties faced by the Eurozone since the 2008 global economic crisis, the fact

that the UK nowadays is actually less of an optimal currency area than the EU itself challenges the notion that the UK's highly centralised government system is indeed the most appropriate governance structure for managing the UK economy for the benefit of all parts of the UK.

In order to describe the current interregional realities of the UK's economic geography *The Economist* (2013f) uses the distinction between the two codes of the sport of rugby, namely rugby union and rugby league, as a useful metaphor for this type of co-existence and separation. These two codes of rugby and all of their associated fan-bases and commercial support largely co-exist with little or no interactions between them. In England Rugby League is played almost entirely in towns scattered along what is known as the 'M62 Corridor', and this broadly describes an area which is oriented east-west and which links the northern cities of Liverpool, Manchester, Leeds and Hull. Traditionally from the late nineteenth century, throughout the twentieth century and into the early twenty-first century, this was perceived of primarily as being a game for miners, steelworkers and factory workers, and indeed the towns which excel in these sports largely reflected this economic history. In England, Rugby Union in contrast was largely a game associated with private and grammar schools and elite universities and almost all of the major rugby union clubs are located south of an imaginary line linking the River Severn in the south west of England with The Wash on the northern edge of East Anglia. To an external observer with little detailed knowledge of these games both codes of rugby appear to be very similar to each other and to substantiate this point there are many high-profile players and coaches who have successfully switched between the two codes at various points in their careers. More recently, however, such switches have tended to be uni-directional and away from Rugby League and towards Rugby Union as increasing moneys pour into Rugby Union. To the vast majority of people deeply embedded within each individual code of rugby, including supporters and club members, however, the two codes of rugby largely co-exist, with little interaction, mutual awareness, or other forms of linkages between them at the same time as one of the codes is becoming increasingly wealthy relative to the other.<sup>15</sup> As much as anything, the reason is that the societal context within which the two sports are played reflect very different social, cultural, geographical and industrial histories (Collins 1998), and these different contexts remain deeply entrenched on many levels. Indeed, this rugby metaphor provides a surprisingly good analogy of the current economic geography realities within England, which as we will see in Chapters 2–5, reflect a deeply and increasingly divided nation. Similar metaphors can increasingly be provided nowadays also by professional football.<sup>16</sup> If we add to these English economic geography realities also the diverse economic experiences of the three devolved regions of Wales, Scotland and Northern Ireland (Cambridge Econometrics 2013) plus the high levels of international openness displayed by the UK economy as a whole, then the overall picture becomes both extremely complex and interesting. On a regional level people's experiences of the economic

and social realities are simply so different in the UK that nowadays regional as well as local communities perceive also their needs in totally different ways.<sup>17</sup> This will have profound long-run implications for the governance of the UK as many of the social and cultural national institutions underpinning the national polity increasingly give way to diverging regional interests. In terms of the public consciousness, the most obvious case, of course, is that of Scotland. Yet, as we will see in the coming chapters, the issues raised in this book do not fundamentally change if at some point in the future Scotland chooses to become independent from the rest of the UK. Many of the important issues arising out of the Scottish case are also at least as applicable in the case of other UK regions, if not more so. Indeed, on many levels many of these issues would become even more starkly delineated in the event of Scotland becoming fully independent.

The fact that in economic terms at least many UK regions appear to co-exist while displaying little or no economic cohesion between the different parts of the country therefore raises three fundamental governance questions. First, how are public resources to be allocated? Should they be targeted at the more prosperous parts of the UK or at the weaker parts of the UK and why? Overman (2013) refers to these challenges in his ‘jam-spreading’ analogy which argues that resources – i.e. ‘jam’ – should not be spread too thinly on political grounds and instead focused on potentially successful cities in order to generate scale effects. This analogy has also since been picked up by front-line political circles with Boris Johnson’s ‘jam and Ryvita’ argument that by concentrating resources – i.e. jam – in London eventually much greater economic benefits will spread out across the country – i.e. across the Ryvita – according to some sort of spatial ‘trickle down’ or interregional ‘spread’ (Richardson 1978) effect.<sup>18</sup> The Overman (2013) use of the analogy raises important issues regarding resource concentration and policy prioritisation which we begin to discuss in detail from Chapter 6 onwards whereas the Johnson version of the analogy is incorrect. While ‘trickle down’ ideas at the national level have been firmly refuted by the OECD (2014a) and IMF (Berg and Ostry 2011) on the basis of all of the available international evidence as well as the intellectual arguments (Stiglitz *et al.* 2009; OECD 2009b, 2009c), as we will see in Chapters 2 and 3 especially as well as Chapters 4 and 5 of this book, all of the available interregional evidence from the UK also refutes the contention that widespread and beneficial economic spatial spread effects from London to other regions are evident in the UK. The evidence suggests that there are no real spread effects at all. To use the same metaphor, it appears that the ‘jam’ is either too viscous or the surface of the ‘Ryvita’ far too rough or porous for any economic benefits to spread to the rest of the country.

Second, as we will see in Chapter 6, if the UK is not even approximately an optimal currency area, then should the UK state be broken up into smaller constituent parts or should its governance system be largely reconfigured to reflect local and regional differences and to better cope with asymmetric economic shocks? Third, and following on directly from the first question, would

smaller national or regional polities be more successful in managing economic conditions in the modern era of globalisation than the current highly centralised UK state?

In the UK these are clearly not merely abstract philosophical questions, as evidenced by the recent Scottish vote on independence, although this is a discussion which actually goes much deeper and wider than just the Scottish case. Obviously, many of the independence, autonomy and devolution arguments within the four constituent nations of the UK reflect deeply held cultural and philosophical convictions (*The Times* 2014; *The Guardian* 2014b) and also some well-considered economic arguments. However, in the aftermath of the Scottish independence vote, what were previously just the domain of academics working on either constitutional issues or regional development issues these wider discussions about regional autonomy and devolution have now taken centre-stage within many UK domestic political debates and a complex continuum of regional–national–international governance and constitutional interrelationships are starting to be uncovered which previously have been largely below the surface. The governance and political aspects of the city-region devolution debates in England are closely related with the devolution debates in the devolved administrations of the three devolved regions of the UK, while the governance issues facing the three devolved regions are closely interrelated with the relationships between the UK and the EU in ways which are markedly different from those evident within England (Bogdanor 2015b; Emmott 2015). Indeed, not only are they related, but they are closely interrelated in myriad and complex ways.<sup>19</sup> At the same time, as we will see in Chapter 6, all of these governance debates are also intrinsically linked to economic geography and in particular to the UK's distorted and highly unequal economic geography (Morgan 2002, 2006, 2007). Yet, while these issues for decades were almost purely contained within academic circles, now that they have emerged in the popular press and mainstream political media these debates now go well beyond questions about the UK's internal economic geography, and also variously include wider discussions regarding the UK's place within Europe, its role in the global economy, and also the dominant and what is perceived as an increasingly disconnected role of London within the UK economic and political arenas (O'Brien 2012a, 2012b).<sup>20</sup> Rather than providing clarity, however, the rather unfortunate result of these various discourses is that many of the current independence and separatist debates within the four constituent nations of the UK now reflect a rather confused mixture and conflation of anti-globalisation and mercantilist trade narratives pitting 'us' against 'them' with populist narratives railing against 'metropolitan elites' (Little 2014) and 'London rule' or 'Whitehall rule' (Brown 2014, p. 184). In particular, to many observers much of the support for independence parties in all four constituent nations of the UK is either a reaction to, or builds upon, the perceived self-seeking dominance of the London economy (Little 2014; *Financial Times* 2014a; White 2014), a region which appears to benefit greatly from globalisation, which is perceived to drive up inequality

(Small 2014) by sucking in resources from the rest of the country (*Financial Times* 2014b; Coy 2014; *The Scotsman* 2014; White 2014)<sup>21</sup> and whose political and business elites including immigrant billionaires (*Standpoint* 2015),<sup>22</sup> multi-millionaires (Knight Frank 2015) and overseas property investors (Deutsche Bank 2014) all appear to be increasingly decoupled from the experience of much of the rest of the UK (O’Brien 2012a, 2012b), including even those in other prosperous areas.<sup>23</sup>

There is obviously debate and disagreement amongst different commentators about the veracity of these London characterisations<sup>24</sup> although as we will see in the coming chapters it is clear that some of these perceptions are not entirely without substance, and it would be a mistake to see these perceptions as deriving solely from the smaller and populist political parties. Indeed, both the wider public<sup>25</sup> as well as mainstream political parties also share many of these concerns and aspire to address these issues. According to the UK Prime Minister David Cameron our

economy has become more and more unbalanced, with our fortunes hitched to a few industries in one corner of the country, while we let other sectors like manufacturing slide ... We will help to rebalance our economy, ensuring that success and prosperity are spread more evenly across regions and industries ... Today our economy is heavily reliant on just a few industries and a few regions – particularly London and the South East. This really matters. An economy with such a narrow foundation for growth is fundamentally unstable and wasteful – because we are not making use of the talent out there in all parts of the United Kingdom ... And it doesn’t mean ignoring London ... but it does mean having a plan to breathe economic life into the towns and cities outside the M25.

(Cameron 2010).

These themes are also echoed by the Scottish Government’s First Minister Nicola Sturgeon who argued that

London has a centrifugal pull on talent, investment and business from the rest of Europe and the world. That brings benefits to the broader UK economy. But as we know, that same centrifugal pull is felt by the rest of us across the UK, often to our detriment. The challenge for us all is how to balance this in our best interests – not by engaging in a race to the bottom, but by using our powers to create long-term comparative advantage and genuine economic value.<sup>26</sup>

As we will see in Chapters 2 and 3, the economic dominance of the London economy within the UK state is now relatively greater than it has been at any time since the very early years of the twentieth century. Moreover, as we will also see in Chapters 4 and 5, much of this ascendancy is indeed related to globalisation, in which evolving global value-chains

and cross-border economic integration re-shape the relationships between the local, regional, multinational and global contexts. Today there are increasing tensions between the existence of individual nation-states, their ability to maintain democratic governance, and ongoing and increasing globalisation processes (Rodrik 2011). Yet, a resolution of these tensions does not imply a wholesale move towards greater protectionism and isolation, a movement which would be heavily counter-productive. Rather, it requires more nuanced and varied forms of multinationalism (Rodrik 2011). As such, some of the independence and devolution narratives currently circulating in the UK media and political circles ignore many of today's most fundamental economic mechanisms, and as such, many of the policy 'solutions' they propose are entirely unsuitable for addressing the long-term economic challenges that the UK faces. Therefore, developing a much deeper understanding of the relationships between the UK national state, its constituent nations, regions and cities, and the differential impacts of globalisation on each of these polities and spaces, is essential before we are able to point towards possible policy approaches or solutions.

Addressing these types of questions also involves dealing with public perceptions, many of which are based on little or no knowledge of the available evidence or data. Many currently crucial political decisions are being made with very little recourse to any real analysis of the likely impacts of these decisions. Problems involving mismatches of perceptions are particularly acute when regional and urban challenges are discussed in the popular media in the context of UK governance and institutional issues. For example, while the issues raised by the 'West Lothian question' have re-emerged with a vengeance in Westminster in political circles in the wake of the 2014 Scottish independence referendum, outside of the three devolved regions there currently appears to be little appetite for devolution amongst the English. Devolution and regional and city governance<sup>27</sup> issues of themselves tend to be far down the list of priorities of most English voters (Kellner 2014; *The Observer* 2014), while inequality, unemployment and the overall economic situation are all very high on the list of voters' priorities. Yet, while in the minds of today's voters these economic and social issues may seem to be largely divorced from questions of governance and local autonomy, as we will see throughout this book these issues are all very closely interrelated. Indeed, many policy-makers, private sector actors and civil society representatives already know this, and it is at the level of cities and regions rather than at national government levels that these various different parties most frequently interact with each other in order to bring about change (OECD 2014b). Not surprisingly, therefore, the pressure for greater governance decentralisation, devolution and reform within England at the regional and city levels is emerging from city and local governance authorities themselves.

Numerous actors within the UK government arena are nowadays increasingly well aware of the serious inadequacies and misalignments of the current national governance situation and the imperative for mobilising actors at the

regional and city levels in order to drive growth. These arguments have been highlighted in ten major UK reports (Heseltine 2012; IPPR 2012, 2014; CBI 2012; RSA 2014, 2015; Adonis 2014; HoC 2014; ICLGF 2014, 2015) plus various more city-specific and metropolitan area reports (MIER 2009; PWC and Demos 2012; ResPublica 2014, 2015) as well as reports addressing the governance issues facing non-metropolitan and rural areas (NMC 2014, 2015; LGA 2015; Diamond and Carr-West 2015), and all of these reports which are set against the backdrop of a range of high-level international reports (Barca 2009; OECD 2009b, 2009c, 2011b, 2012, 2014b) echoing these same types of themes. Moreover, in the UK setting, these issues also link to many of the issues raised in earlier reports specifically addressing the challenges facing UK cities and urban areas (Scottish Executive 2002; ODPM 2004, 2006a, 2006b; DCLG 2011). These various reports all argue broadly that in the context of heterogeneous cities and regions and in today's economy, in order to best foster growth and development we need multi-level governance arrangements including wide-ranging local autonomy and decision-making powers implemented at the right spatial and local levels. Top-down and highly centralised governance systems can rarely provide such an environment. In small economies top-down centralised governance systems may be appropriate but in large and highly diverse economies such as the UK this is very unlikely to be the case. As this book will repeatedly argue and demonstrate on the basis of both UK domestic data as well as international comparisons, it is actually within England itself that the mismatches between economic development and governance are the most acute and so there is the need for major governance reform at the regional levels as well as at the level of the devolved administrations. Moreover, as we will see later on, any political movement towards 'English votes for English laws'<sup>28</sup> will have little or no effect whatsoever on these economic-institutional mismatches and because the problems are more fundamental and of much greater orders of magnitude than these largely philosophical-political arguments.

While some independence and devolution arguments are indeed well-founded on economic and social grounds, where this is not the case, however, it is likely that most of the rather spurious independence and devolution arguments are in a reality a result of a breakdown of public trust in central government and reaction to the perceived failures of central government. Indeed, in the aftermath of the 2008 global financial crisis, in many countries the levels of public trust in governments are now at very low levels (OECD 2013; European Union 2014a). The limited ability of national governments to respond effectively to the impacts of the 2008 global economic crisis has reduced the public's belief that national governments can deliver on their promises. Yet, until recently this was not the case. Perceptions of governments during the 'great moderation' between the mid-1990s and 2008 remained relatively sanguine as inflation was kept low by processes of globalisation which allowed for massive increases in the global supply of low wage labour, while misguided 'financial innovation' (Padoan 2012) combined

with benign monetary policy contributed to excessive risk-taking and inflation in asset prices. The UK, and the London economy in particular, was a principal exponent of this pattern. Yet, the aftermath of the 2008 global economic crisis led to a rude awakening in the fields of economics, finance, political science and international relations in that so much of the previously accepted analytical wisdom was found wanting (Padoan 2012). The fact that problems originating in just 3 per cent of US domestic real estate assets (Padoan 2012) could have wreaked such havoc across so many nations and for so long, has underscored the limitations of many previously accepted analytical frameworks and also the limited power of these frameworks in assisting national governments in the face of major and adverse global market movements (Wolf 2014a; Krugman 2014). Yet, in many cases this declining public trust in government and political institutions has moved beyond mere scepticism and increasingly is reflected in outright hostility towards political process and systems. Unfortunately, however, the adverse role which political decision-making – which is overwhelmingly based on domestic discourses – can also play in thwarting possible realistic responses, is also becoming increasingly evident in many countries.

In the European contexts, some of these independence discourses and narratives are pro-European but anti-central government at the national level, while others are primarily anti-European and pro-national government. Moreover, many of these different narratives are often rather contradictory with each other, drawing as they do from ideas and inspiration from quite different ends of the political spectrum, depending on the underlying agenda of the parties in question. However, what these independence and devolution narratives and discourses all share in common is a belief that the national institutional status quo is no longer appropriate for dealing with the twenty-first-century economic realities. In particular, they all share the idea that national central government is too remote and unaccountable from the public which elects it, and these beliefs are largely held in common, irrespective of whether the independence being sought is from either Westminster or Brussels as is the case in the UK versions of these narratives (*The Economist* 2015a), or from Ottawa, Madrid, Rome, Paris, Stockholm, or the institutions of the European Union.<sup>29</sup>

In the case of regional devolution or independence narratives, they naturally draw some of their leading themes from a similar pool of ideas as do the national independence narratives. However, there are also many aspects of the regional devolution or independence debates which differ greatly from those operating purely at the national level. Yet, although many of the currently popular regional independence or devolution narratives differ markedly from each other, they do raise fundamental concerns regarding the governance of regions, countries, groups of regions and groups of countries, in the modern era of globalisation. These concerns are actually very timely, in that differences in government and governance performance across countries have been very marked in the aftermath of the crisis and the role played by

sub-national governance in these responses has become increasingly apparent (OECD 2013, 2014b; European Union 2014a). In particular, the relationships between sub-national and national government are increasingly seen as being key to the effectiveness of responses to the crisis. Either the breakdown of central-regional governance relationships or the absence of strong and meaningful national-local governance relationships are increasingly understood as limiting the economic resilience of the national state in the face of adverse global market movements.

The experience of the UK with its highly centralised governance systems and limited local governance roles increasingly appears to be at odds with the economic realities of the UK. From an academic perspective, therefore, the enormous mismatch between the current economic geography of the UK and its governance systems and structures throws up many fundamental analytical questions and challenges regarding the wider relationships between geography and governance. The reason is that although the various political narratives questioning the performance of central government are largely cultural, philosophical and political in nature, as we will see in Chapter 6, common to all of these narratives are two underlying theoretical economic problems which are central to these political economy discussions in the UK and elsewhere. These are first the ‘optimal currency area’ or ‘optimal currency region’ (Mundell 1961) problem and second the ‘optimal size of a nation’ problem (Alesina and Spolaore 2005). What is important about these underlying theoretical economic arguments is that they do raise important questions regarding the suitability of the governance system of the UK in the current context, one which is characterised by almost unprecedented interregional differences. Indeed, the questions and challenges posed by these theoretical arguments regarding the role of the UK’s institutions and governance arrangements in shaping development relate not only to the specifics of the UK but more generally to broader worldwide discussions. The fact that the UK is such a patchwork of governance systems overlaying extreme interregional inequalities means that any answers and insights which can be gleaned from an analysis of the current UK context are also likely to lead to more general insights which will be applicable in many other national and international contexts.

## **1.2 The UK shift from ‘regional’ narratives to ‘local’, ‘urban’ and ‘city’ discourses**

The current and future discussions regarding governance issues in the UK are heavily shaped by nomenclature and terminology employed because the specific language used itself fundamentally frames the political debates. In the case of issues concerning the economic geography and governance of the UK there has been a major shift in recent years, and in particular since the Coalition government came to power in 2010, away from using the nomenclature of ‘local’ and ‘regional’ and instead in favouring the terminology of ‘local’, ‘city’ and ‘urban’ in official documents (BIS 2010; HM Government 2010, 2011; GOS

2013) and public discourses. The greater inclusion of ‘urban’ and ‘city’ in current terminology is very welcome as this potentially allows for a more nuanced and focused debate regarding the role of, and challenges faced by, our major centres of population, as well as increased awareness of the potential for community involvement in governance issues. However, whereas prior to 2010 terms such as ‘region’, ‘regions’ or ‘regional’ dominated UK official publications (DTI 1998, 1999; DCLG 2008; HM Treasury 2001, 2003; HMT, DTI and ODPM 2003) dealing with matters related to the UK’s internal economic geography and governance challenges, since 2010 these terms have almost disappeared entirely from the nomenclature of current official publications and political discourses. By late 2014 and early 2015 some regional and interregional terminology had again started to return implicitly into government and public discussions in the form of the expanded HS2 debates (DfT 2014a, 2014b) and also a ‘Northern Powerhouse’ narrative (HM Government and Transport for the North 2015),<sup>30</sup> somewhat echoing the prior ‘Northern Way’<sup>31</sup> narratives which had emerged a decade earlier before disappearing by 2010.

As will be seen throughout this book, the recent widespread removal of the nomenclature of ‘region’, ‘regions’ or ‘regional’ from many public policy discourses is very unfortunate and there are two reasons for this. First, the majority of ‘local’ neighbourhood issues operating within UK ‘urban’ areas relating to house price hedonic effects and the social segregation or mixing of neighbourhoods are not particularly different from those evident across the majority of the advanced OECD economies. While there may be a few specific features operating in the UK which are noticeable such as the role of the UK land use planning system, there are also many other countries with similar types of systems, and as discussed in Chapter 5, although the system has profound and often deleterious economic effects the operation of the system itself explains little regarding the issues raised in this book. In marked contrast, as will be argued throughout this book and in particular in Chapters 2–4, when it comes to economic geography it is the interregional situation within the UK that makes the UK case almost unique, and as such requires a great deal of analysis to understand why the UK is apparently so different to the vast majority of other OECD countries. Not only has there been a long-standing ‘north–south’ divide in the UK which has been articulated by economists and geographers (Fothergill and Gudgin 1982; Baker and Billinge 2004), but this divide has increased dramatically in the last two decades. In economic terms the UK is characterised by an incredibly strong core-periphery spatial structure whereby the ‘core’ was traditionally defined as the regions located to the south of an imaginary line drawn between the River Severn and The Wash and the periphery being those regions located to the north of this line (Balchin 1990; Baker and Billinge 2004; Dorling 2010).<sup>32</sup> In economic and wellbeing terms this basic divide now holds stronger than ever, except for the fact that an additional imaginary line demarcating the economic ‘core’ from the ‘periphery’ nowadays also exists, which is the line describing the border between northern English regions and Scotland. As we will see in

Chapters 2–4, unlike in earlier decades, Scotland is nowadays increasingly part of the ‘core’ along with the three southern English regions; while the northern and midlands English regions plus Wales and Northern Ireland make up an economic periphery which is becoming increasingly decoupled and dislocated from the core regions. This tripartite decoupling is also reflected on social and political levels as well fundamentally on economic grounds.<sup>33</sup> Obviously this does not mean that all problem areas are in northern regions and all prosperous areas are in southern regions (*The Economist* 2014g). Nor does it mean that every town or city north of the imaginary Severn–Wash line and south of the Scottish border exhibits lower income and wealth than towns located south of the Severn–Wash line or north of the Scotland–England border. Indeed, southern regions include some of the poorest local neighbourhoods, almost all of which are in London, while northern regions do include some of the most affluent local neighbourhoods. Of the poorest 50 UK neighbourhoods according to child deprivation figures, some 32 are located outside of the southern and eastern regions of England and of the 18 which are located in southern regions, all are in London. At the same time, the southern regions of England contain 31 of the top 50 least deprived UK neighbourhoods.<sup>34</sup> The result of this complex picture is that London contains some of the richest and poorest neighbourhoods in the UK (Dorling 2013a), while Cheshire is richer than Cornwall, Harrogate is wealthier than Hastings. Lowestoft<sup>35</sup> has lower incomes than Lancaster, East Kilbride is poorer than Knutsford, and Hackney has more deprivation than Hexham. Indeed, Cornwall is one of the poorest counties of the UK. As such, extending our imaginary Severn–Wash line back through the River Tamar may better capture some additional variations.

Yet, even allowing for these types of variations and exceptions, as we will see in Chapters 2 and 3 the general pattern described by the Severn–Wash line and the England–Scotland border is remarkably consistent at the broad interregional level and at also the urban level (Dorling 2013b). Moreover, this is an explicit spatial pattern which is evident in the context of a country which exhibits a largely monocentric type of spatial structure in that there is a regional coincidence of the centres of government, commerce and also trade routes. The confluence of these three dimensions in the same regions is almost unique amongst OECD countries and this is an explicitly spatial and regional feature. Therefore, an over-emphasis on ‘local’ and ‘urban’ and a widespread exclusion of the term ‘regional’ from the UK public discourses removes most of the explicitly spatial and geographical underpinnings of the economic challenges faced by the UK. As we see in Chapter 3, in order to understand what is taking place in large UK cities it is essential to discuss each city in the context of the region in which it is located. In the UK urban issues are fundamentally regional issues in a manner which is not the case in many other OECD countries, whereas the reverse does not hold to the same extent. UK regional issues are not necessarily urban issues to the same extent as they are in other OECD

countries, and unlike regional issues, UK urban issues are not particularly different to those evident in many other countries. Again, this of course is not to say that all urban (*The Economist* 2014g) or sub-urban (Dorling 2013a) areas in the south of England are prosperous nor that all of those in northern areas are poor. However, the correlation between urban issues and regional issues is so strong in the UK case, defined by an extraordinarily strong centre-periphery arrangement whose spatial structures are also closely related to governance structures, that to remove ‘regional’ from public debates is to miss most of the issue.

Second, it is the interregional situation which is now primarily putting so much pressure on the UK governance system, and not local neighbourhood or even urban issues. While economic issues are increasingly global in nature, and as we will see in Chapter 4 particularly those operating at the regional level, in contrast UK politics is becoming increasingly regional and local, with some of the UK’s most powerful political actors leveraging off sub-national regional power bases, purportedly defending the region or city against central government or international institutions (*Prospect* 2015). Therefore, regrettably, removing ‘region’ and ‘regional’ from the nomenclature of public debate limits the ability of public debate to accurately and effectively respond to the realities of the UK economic geography and the associated governance challenges being faced by the UK, which by OECD standards are now on an almost unprecedented scale and complexity. A much more fruitful way forward would be to have ‘local’, ‘urban’ and ‘regional’ terminology all as regular parts of the nomenclature of UK public discourses relating to the economic geography and governance challenges we face today. This is because nomenclature used in public discourses affects both the geography of perceptions and the perceptions of geography. When it comes to regional issues and their associated governance challenges, within the UK political debates many of the perceptions regarding both the underlying mechanisms and also the lessons which can be learned from both domestic observations and international observations are not only highly questionable, but also they tend to inhibit the search for improved and potentially workable governance solutions. As far back as 1983, Britain’s foremost social historian Asa Briggs bemoaned the scale of UK interregional disparities and argued that solutions for these could not be found with either purely local or national policies. The intermediate regional level is a crucial part of the UK social and economic story and institutional and governance issues will need to respond at this level as well as at the urban and local levels in order to be effective (Briggs 1983).

### **1.3 A problem of the geography of perceptions**

As mentioned above, one of the difficulties in having a discussion about UK interregional and governance issues, and particularly in the context of the challenges associated with modern globalisation, is that UK internal debates

tend to pay very little heed to lessons from other countries. The willingness and desire to learn from the policy experiences of other countries ought to be greater when it is understood that other countries exhibit significant advantages in particular policy arenas than we do. However, in the case of the UK this willingness tends to be very limited, and part of this is because there is such a widespread lack of awareness of the relative positioning of the UK economy on so many dimensions. Policy ideas and initiatives emerge primarily in domestic political economy debates which themselves are heavily influenced and shaped by the debates and discourses operating in the public media. Yet, ideas and experiences from other countries ought to partly shape these debates where it is clear that the domestic situation is weaker than elsewhere. However, many of the narratives operating in today's UK popular and tabloid press, and in particular Eurosceptic narratives, tend to frame discussions about the UK's current international economic challenges as though we were living sometime in the 1950s rather than the twenty-first century. In other words discussions start from an implicit assumption that the UK is fundamentally a dynamic and strong economy surrounded and, if anything, largely held back by weaker and largely sclerotic polities.<sup>36</sup> This was indeed true during the 1950s when the UK was the sixth richest country in the world and richer than all other European economies except for Switzerland, with UK productivity premia of between 10 per cent and 40 per cent above other western and northern European economies (Broadberry and Klein 2011). Yet, today's reality is totally different with the UK lagging behind almost all other advanced economies in terms of productivity levels and growth, as we will see in detail below. As such, claims that the UK might be the most prosperous economy by 2030 are likely to be pure fantasy (Wolf 2015) given the current dire productivity performance of the UK, the severity of the UK demand contractions in the aftermath of the 2008 crisis (Krugman 2015a) and many of the budget-related changes being introduced.<sup>37</sup> Therefore, before we can begin to put any flesh on a skeleton outline of the issues to be faced ahead in the rest of this book regarding the UK interregional economic and governance challenges, it is important to try to set out the broad economic and policy context and background in which these debates take place in order to assess the extent to which the UK may fruitfully learn lessons from other countries. This also requires us to reconsider some of the fundamental long-run national and international changes undergone by the UK economy and to accurately position the current UK in wider global trends.

Obviously the UK is a member of the group of approximately 40 or so countries which by global standards are regarded as the rich and advanced economies. Yet within this group the UK is currently ranked between the 25th and 28th richest country in the world, depending on whether we use IMF, World Bank, OECD or CIA data. Multifactor productivity growth in the UK between 1985 and 2007 more than matched the majority of advanced OECD economies, but the reversal of productivity growth experienced by the UK in the aftermath of the 2008 global financial crisis was amongst the most severe of

any industrialised economy,<sup>38</sup> with UK growth 2009–2012 ranked 25th in the OECD and far below both the EU and OECD averages.<sup>39</sup> As such, today the UK exhibits: only just above average GDP per capita scores when compared against the 28 countries of the European Union, including those in Eastern and Southern Europe; below average GDP per capita per hour scores and also GDP per worker scores in comparison to the Eurozone; below average GDP per capita scores and also GDP per worker productivity scores in comparison to the EU-15; and below average GDP per capita productivity scores when compared with the 34 OECD countries (OECD 2014c). The only EU-15 countries which were part of the EU by 1995 with lower GDP per capita than the UK are Italy, Spain, Portugal and Greece. Indeed, overall GDP per capita levels for the UK are currently only between 5 per cent and 10 per cent above Italy and Spain, respectively (OECD 2014c) and are actually some 3.7 per cent below the average for the 34 OECD countries (OECD 2014c). Moreover, today the UK's GDP per worker levels today are actually below those of Italy and Spain (OECD 2014c; Dolphin and Hatfield 2015). In fact, without Greater London's productivity premium, which as we will see in the next chapter is currently more than 77 percentage points above the UK average, the overall GDP per capita of the UK would be more than 4 per cent below Italy (including the Mezzogiorno) and equal with Spain. This is the reality that most UK public debates either largely ignore or are largely unaware of. As of today the UK is the 13th or 14th richest country in Europe,<sup>40</sup> the 10th or 11th richest country in the EU, and the most unequal western and northern European country in terms of income inequalities. While most economic discussions in the popular media automatically compare the UK with our northern and western European countries or with North American competitors, in reality without the productivity premium of London all of our most appropriate economic comparisons would be with southern European and Mediterranean countries. The productivity and prosperity benefits of the core regions of the UK largely fail to spill over or translate to the UK's non-core regions, and the aggregate effect of this is poor overall national productivity performance. This failure to diffuse productivity gains throughout the national economy and the inhibiting effect that this has on overall growth is a major part of the UK regional (and national) economic problem.

These realities are reflected in a variety of other statistics. In terms of innovation, the overall UK innovation systems appear reasonably strong by global standards.<sup>41</sup> However, the UK is still not regarded as an innovation leader and instead is described as an 'innovation follower' whose innovation system is only ranked 7th in the EU (European Union 2014b). The level of proficiency of the UK secondary school population in mathematics, reading and science skills ranks 16th in the OECD at almost exactly the OECD average levels and only 12th in Europe (OECD 2014d). In terms of the percentage of the UK population who are working in private and public sector research roles the UK ranks 13th in Europe and 11th in the EU, just very slightly above the overall EU-28 average.<sup>42</sup> Meanwhile, in terms of the proportion of R&D

personnel and researchers within the business sector the UK ranks only 20th in the OECD, 15th in Europe and 13th in the EU, and actually below the overall EU-28 average.<sup>43</sup> Similarly, both the UK's gross domestic expenditure on R&D and also the business expenditure on R&D are now below the average for both the OECD<sup>44</sup> and the EU-28 (OECD 2014e) and both have fallen from slightly above the EU-28 average in 2000 (OECD 2014e). Of the R&D which is undertaken in the UK, the UK exhibits the second lowest share of R&D which is domestically financed of any advanced economy (OECD 2014e). Even more surprisingly to many observers is the fact that, although the UK now has relatively the 5th highest number of university graduates in the OECD and attracts the second highest number and proportion of foreign students in the OECD,<sup>45</sup> at the same time UK expenditure on higher education relative to GDP ranks only 22nd in the OECD and the level of university R&D as a percentage of GDP is lower in the UK than the EU-27 average and only fractionally above the OECD average (OECD 2014e).<sup>46</sup> Moreover, even adjusting for different industrial structures and the greater role played by the service sector in the UK than in many other economies, the broad picture does not significantly alter (Hughes and Mina 2012).<sup>47</sup> The overall effects of these low R&D and skills-related scores are that, as with the UK productivity data, the only EU-15 countries<sup>48</sup> with relative lower scores for the number of researchers in the business sector than the UK are Italy, Spain, Portugal and Greece, and this is also the case for the gross and business R&D expenditure shares (OECD 2014e). In other words, these UK patterns and rankings regarding R&D and skills are also almost exactly repeated in terms of the UK's GDP per capita relative to its competitor countries.

Other manifestations of the UK's poor productivity performance are reflected by the fact that today the UK does not contain a single company in the world's top 100 global innovators (Thomson Reuters 2014) and only two in the world's top 50 R&D investors, which is the same number as Sweden and Switzerland (European Union 2014c). For comparison purposes the USA has 19 companies, Japan has 9, Germany has 8 companies, France has 2 companies and Italy has 1 such company in the global top 50 R&D investors (European Union 2014c). Amongst the major corporate R&D investors the total UK corporate R&D expenditure is currently 86 per cent of that of France and only 41 per cent of that of Germany (European Union 2014c). In terms of the attractiveness for international R&D-related investments the UK is perceived to be only two-thirds as attractive as France, half as attractive as The Netherlands, less than one-third as attractive as Germany, and even ranks slightly below Poland (European Union 2014d). Overall, what we see is that on a broad range of criteria related to skills, technology and productivity, the UK is just an average performer in comparison to both the EU and the OECD, and weaker on many productivity-related aspects than the majority of the world's and also Europe's advanced economies.

In part the domestic and popular misperceptions which view the UK as fundamentally a dynamic and strong economy surrounded by sclerotic and

less dynamic countries are a natural result of the UK's island status and former Empire history, which still heavily colour many domestic cultural and political narratives. More importantly, however, the overwhelming majority of opinion-formers within the UK media and political circles – including the press, think-tanks, consultancies, political advisory bodies, world-class research centres, and heritage institutions – live and work in London or its surroundings. This is also an inevitable result of the UK having such a centralised state in which the largest city is also the seat of government and the dominant centre of business. As such, this provides a context in which national public debates and opinions are likely to be heavily shaped by the experience of the capital city.<sup>49</sup> The day-to-day experience of the vast majority of highly influential people is shaped and moulded by being resident in the highly prosperous regions of London and the South East whose productivity, wealth and disposable incomes in comparison to the rest of Europe are indeed reflective of the 1950s relationships between the UK and the rest of Europe. Unfortunately, as we will see in Chapters 2 and 3, these relationships do not hold even approximately, for more than half of the UK population.

As such, many of the political and cultural narratives currently dominating UK media and political circles reflect problems of the geography of perceptions as much as anything else. Moreover, these problems of the geography of perceptions are both domestic problems – in that they tend to ignore most of the UK's internal geographical inequalities – and also international problems – in that they tend to ignore the geographical patterns of productivity surrounding the UK. As such, in reality these backward-looking types of narratives are wholly unreasonable for a serious discussion about the UK's internal and external interregional relationships in that they frame such debates in settings which are totally unrealistic and unreflective of the current international and global economic settings. Realism is essential and accuracy is paramount if we are to have a meaningful discussion of these complex and important issues. Moreover, we haven't even begun to discuss why the UK's economy is positioned where it is today and why it is so profoundly different to where it was in the early twentieth century.

For our purposes here, what is important is to position the UK correctly in terms of economic performance in order to identify the extent to which observations and lessons from other countries may be instructive for re-imagining and re-visioning the UK economic and governance system. Most countries which are more successful and richer than the UK have much lower levels of interregional inequality. As we have already seen, while the UK exhibits a very high degree of interregional as well as national inequality, if this was associated with very strong economic performance then in some quarters or circles this may be perceived as providing some sort of defence or justification for this phenomenon along the lines of the schema trotted out in the 2009 World Development Report (World Bank 2009; Barca *et al.* 2012). However, as we have already seen, the poor overall performance of the UK economy suggests that the UK interregional inequalities are not a result of any natural

or automatic trade-off between interregional inequality and economic performance, but rather reflect deep-seated structural problems within the UK economic system. Moreover, these economic and structural problems are now increasingly spilling over into political problems. Indeed, insights from the most extreme case of interregional inequality, namely Thailand, suggest that regional spillovers are not simply economic and monetary in nature, and negative governance externalities are far more intractable once they reach a certain threshold. While the UK is as yet nowhere near the Thailand experience it is certainly no longer natural to assume that if things continue to progress as they are that the largely unitary and top-down UK state is viable in the long run. Other countries have much to teach us and those which probably have the most to teach us are generally geographically very close to us.

#### **1.4 International benchmarking of the modern UK economic context**

From a policy perspective, in order to make any headway in deepening our understanding of the current UK interregional inequalities and their likely evolutions over the coming decades requires that we set these discussions against the backdrop of profound structural change within the UK economy during the last century, and in particular, over five decades. From this vantage point, it is well known that for much of the nineteenth century the UK displayed the highest levels of GDP per capita for any country, and it was only in the last decades of the century that both Australia and New Zealand overtook the UK (Maddison 2006). During the first decade of the twentieth century US GDP per capita also overtook that of the UK (Broadberry and Klein 2011; Maddison 2006) and as we will see in Chapter 2 this was a period of significant UK interregional inequalities. In the first decade following the First World War both Switzerland and Canada overtook the UK, although the UK and Switzerland also continued to leapfrog over each other throughout the 1930s.

In the post-war years between the 1950s and early 1970s the UK economy grew at its fastest rate for any comparable period in the previous century or centuries (Briggs 1983). However, even during these years the growth rate of the UK was typically only 50–60 per cent of the growth rate of other European economies (Briggs 1983), and this remained the case even as the UK higher education system was doubling in size during the 1960s following the recommendations of the 1963 Robbins Report (Briggs 1983). In the post Second World War era Switzerland's GDP per capita emerged as being systematically higher than that of the UK (Broadberry and Klein 2011) and from the 1950s onwards the GDP per capita of other countries also began to exceed that of the UK. By 1973, at the time of the UK's accession to the EEC Common Market, GDP per capita in the other EEC economies of Belgium, France, West Germany,<sup>50</sup> Denmark, The Netherlands and Luxembourg had also overtaken the UK GDP per capita levels, as had the non-EEC country

of Sweden (Broadberry and Klein 2011). This was also a period of declining UK interregional inequalities. As we will see in Chapter 4, during this post-war era the UK increasingly shifted away from its former Empire and Commonwealth trading partners in favour of greater trade and economic integration with other European economies, culminating with the UK's entry into the EEC Common Market in 1973. This changed the UK's internal economic geography (Overman and Winters 2005, 2011) in favour of the southern and eastern regions. In the wake of the first oil price shock of 1974, the mid-1970s to early 1980s was a period characterised by numerous industrial disputes and a breakdown of the previously benign industrial relations between workers and management in many parts of the UK economy, being replaced instead by widespread adversarial relationships.

UK manufacturing also suffered an especially harsh period during the monetarist high interest rate regime of the early 1980s following the second oil price shock of 1981. The decade was characterised by numerous examples of long-standing and successful British manufacturing and engineering companies either entering liquidation or being bought out by foreign buyers (Comfort 2012). In marked contrast, since the 1980s employment in economies such as the UK is increasingly accounted for by service industries. Yet, the relative size of the shift away from manufacturing and towards a service-dominated economy has been greater in the case of the UK than almost all of its major international competitors (Comfort 2012). The rise of London-centred international financial services as a perceived cornerstone of the future UK economy has been widely discussed in numerous arenas (Casson and McCann 1999), along with the rise of other types of business and commercial services. As we will see in Chapter 4 these domestic structural shifts away from manufacturing and in favour of service industries have also been reflected in shifts in the composition of UK exports and imports. However, there is significant heterogeneity of the performance of service industries. Services such as finance, business services and personal services exhibit low-productivity growth but increasing employment shares, while distribution services exhibit constant employment shares and rapid productivity growth (Jorgensen and Timmer 2011). Since the 1980s national and international productivity growth has been driven far more by activities such as logistics, manufacturing and information technology than by personal, business or financial services (Jorgensen and Timmer 2011). As such, although service industries account for the lion's share of employment activities, many of them contribute very little to aggregate productivity growth (Jorgensen and Timmer 2011). Ironically, these low-productivity-enhancing sectors are the very sectors on which the UK economy has been expected to base its future prosperity.

During the 1970s and 1980s the associated adverse regional shocks associated with these structural changes were asymmetric in that they were heavily oriented towards those regions which were outside of the southern regions of England while the southern regions were relatively more oriented to the emerging service industries (Leunig and Overman 2008). UK manufacturing

was increasingly seen in many political circles as being out-dated and UK manufacturing in particular as being especially so (Comfort 2012). However, as we will see in Chapter 2 the GDP per capita differences between UK regions remained largely constant during this period. Instead, the emerging differences in regional fortunes were manifested primarily in terms of greatly differing regional unemployment rates, and as a result, it was during this period that discussions about the ‘north–south’ divide started to emerge with a vengeance on both economic (Fothergill and Gudgin 1982; Harrison and Hart 1993) and also political economy grounds (Brown 1989).

Market deregulation continued apace throughout the 1980s and early 1990s and as we will see in Chapters 2–4, all aspects of the UK economy were affected in numerous and diverse ways by the shocks associated with modern globalisation which emerged from the early 1990s onwards. By 1990, the EU economies of Finland and Austria had also overtaken the UK in terms of GDP per capita, as had the non-EU economy of Norway, and by 2000, the list also included Ireland (Broadberry and Klein 2011). Although by the early 1990s the former West Germany had out-performed the UK in terms of GDP per capita for almost three decades and was more than 12 per cent richer per capita than the UK by 1990 (Broadberry and Klein 2011), not surprisingly the GDP per capita of the reunified Germany fell below that of the UK from the 1990 date of reunification.<sup>51</sup> However, by 2008 even the reunified Germany also exhibited higher per capita GDP than the UK, and has continued to do so ever since (OECD 2014c). Indeed, even allowing for the enormous resources involved in upgrading the former East Germany, the reunified Germany today exhibits a GDP per capita advantage over the UK which is almost exactly the advantage that West Germany displayed over the UK in 1990 (Broadberry and Klein 2011). In the wake of the 2008 crisis, the UK has made remarkably little long-term economic progress in comparison to its peer economies. In fact, the only country since the end of the Second World War that was previously richer than the UK and which the UK has subsequently overtaken in terms of GDP per capita is New Zealand, which the UK surpassed in the late 1980s (McCann 2009; Maddison 2006). Moreover, even in this case, although the productivity gap that the UK had over New Zealand reached some 20 per cent at the turn of the millennium (McCann 2009), in the wake of the 2008 crisis the gap had been almost closed again by 2012 (OECD 2014c).

It was from the early 1990s onwards that increasing UK interregional disparities really began to emerge. Between 1999 and 2007 the UK economy experienced almost a decade-long growth surge with annual productivity growth averaging 2.3 per cent (Wolf 2014b), which was faster than any other large OECD economy (Maddison 2006; OECD 2014c) and this allowed the UK to almost regain parity in terms of GDP per capita with both Canada and Australia in 2004 (OECD 2014c). As UK growth started to slow after 2004 both of these countries maintained a small productivity lead over the UK, but this gap widened significantly after the 2008 crisis. Indeed, following the

2008 global economic crisis the decade-long period of fast UK growth came to an abrupt end. Indeed, the UK has since faced amongst the most severe declines and medium- or long-term losses of economic potential of any major OECD economy (Ball 2014; Bank of England 2014; *The Economist* 2014f, 2014g, 2014h) with output per hour falling at a trend rate of 2.2 per cent per annum between the first quarter of 2008 and the third quarter of 2014 (Wolf 2014b). Yet, unlike many southern European economies, although the UK has experienced dramatic losses of productivity since 2008 it has only experienced limited associated increases in unemployment, which have since been falling (Wolf 2014b; *The Economist* 2015b). Taken together these observations lead to what is variously described as the UK ‘productivity puzzle’ (Bank of England 2014) or the UK ‘productivity mystery’ (Pessoa and Van Reenen 2014). Both the UK service industries and the UK production industries have faced severe productivity declines greater than in almost any other major OECD economy (Wolf 2014b). Most analyses of these issues focus on sectoral and firm-level analyses and examine the effects of factor substitution and labour market dynamics (Riley *et al.* 2015; Bryson and Forth 2015; Dolphin and Hatfield 2015). In particular, while UK productivity growth prior to the 2008 crisis was driven by the professional services, manufacturing, banking, retail and information and communication sectors, since the crisis the worst affected sectors have been professional services, telecommunications and computing, banking and finance, and manufacturing.<sup>52</sup> In other words, most of the same sectors which spearheaded productivity growth prior to the crisis have since spearheaded the productivity declines. There have been very recent productivity improvements in both the medium- and high-technology transport-manufacturing sectors as well as in low-technology sectors such as the administration and support sector, while the worst performing sectors are still finance and insurance and chemicals and pharmaceuticals.<sup>53</sup> Labour hoarding was apparent in manufacturing in the wake of the crisis as firms were concerned about losing skills, but this cannot explain ongoing productivity weaknesses (Berkeley *et al.* 2011). The increasing role of part-time work also cannot explain these productivity declines because they also are apparent in the output per hour data (Wolf 2014b). Moreover, neither can wage declines in the financial markets be the sole reason because the declining productivity effects are also very apparent in many areas of manufacturing (Wolf 2014b), although some areas of manufacturing such as automobiles are displaying strong productivity recovery well beyond pre-crisis levels (SMMT 2015). Nor can weaknesses in the UK’s credit system be the major culprit as the financial system is recovering (Wolf 2014b). Rather, one of the best guesses as to the reasons for this apparent ‘productivity puzzle’ (Bank of England 2014) is related to the highly deregulated nature of the UK labour market and the rising costs of business capital costs (in spite of almost zero base rates) which have encouraged firms to substitute labour for new capital investment (Pessoa and Van Reenen 2014). This argument suggests that during the Great Recession the UK economy has absorbed much of the adverse shock effects

of the crisis over recent years in terms of falling productivity and real wages rather than primarily in terms of rising unemployment (Bank of England 2014), as has been the case in countries located on the southern and eastern fringes of Europe. Yet, even after the shock-absorbing effect of a more than a 25 per cent post-crisis devaluation<sup>54</sup> of Sterling between mid-2008 and early 2009 the UK's export performance has barely improved at all and effectively no 'rebalancing' (Hunt 2013) of any form has taken place since.<sup>55</sup> As such, the fact that the UK's productivity performance remains poor even in the upturn of 2014 weakens the rather optimistic arguments in certain quarters that the UK will soon emerge again as a relatively strong dynamic economy (Wolf 2014b).

Indeed, the scale of the UK productivity 'puzzle' or 'mystery' can be underlined by the fact that although it is widely understood that in the aftermath of the 2008 global economic crisis Spain, Ireland and Italy suffered some of the worst economic declines amongst all of the advanced economies, in reality during the post-crisis period 2008–2012 all three countries experienced stronger GDP per capita growth than did the UK during the same period (OECD 2014c), as did even Japan (Wolf 2014b). Today the UK exhibits GDP per capita per hour levels which are 11 per cent below the Eurozone average and only just equal to the EU-28 average, including the central and eastern European countries (OECD 2014c), while GDP per worker levels are currently ranked only 13th in the EU. Indeed, some 207 million people within the EU, or 47 per cent of the population of the rest of the EU, now live in countries which are richer than the UK. This figure for the whole of Europe rises to some 221 million people or 49 per cent, if we also include the EFTA countries. By western and northern European standards as well as EU-15 standards the UK is a relatively low achiever. As we have already seen, overall GDP per capita levels for the UK are currently only between 5 per cent and 10 per cent above Italy and Spain, respectively (OECD 2014c) and are actually some 3.7 per cent below the average for the 34 OECD countries (OECD 2014c), while UK GDP per worker levels today are below those of Italy and Spain. GDP per hour worked in the UK is lower than in Italy and almost 25 per cent lower than in France.<sup>56</sup> Although in part lower worker productivity partly reflects a trade-off between productivity and employment (Wolf 2014b) the UK today exhibits both worker productivity and total GDP per capita which is still at least 15–30 per cent below that of other northern European economies and North American economies with similar levels of unemployment to the UK. Moreover, there are no signs as yet that the picture is changing as the UK's current performance is the worst relative to our competitors since records began in 1991.<sup>57</sup> In reality, the UK as a whole is a far poorer country and a much weaker economy than is reflected in many of the London-centric narratives circulating in the national popular press.

There are of course some grounds for optimism. Although between 2007 and 2012/13 the UK under-performed relative to both the Eurozone and the OECD as a whole (OECD 2015b), after a six-year period of little or no growth

in 2014 the UK economy posted GDP growth of somewhere between 2.5 per cent and 3 per cent and again for the first time passed its pre-crisis levels of nominal output in early 2014, reaching some 2.1 per cent above the pre-crisis levels by the third quarter of 2014 (Wolf 2014b). During the same year UK wage growth for those already in work contracts for more than one year also began to outpace the growth in living costs for the first time in six years, with future expectations of productivity employment growth improving across all UK regions.<sup>58</sup> However, real wages for those on short-term or recent contracts continued to fall,<sup>59</sup> with the poorest households facing the fastest cost of living rises.<sup>60</sup> Poverty amongst working households is now on a greater scale than those households which are out of work or retired (*New Statesman* 2014) due to the scale of under-employment rather than just unemployment. Indeed, even allowing for recent improvements,<sup>61</sup> the observed patterns and trends in wage and productivity performance mean that many observers doubt whether we will again return to the type of economy buoyancy enjoyed between 1997 and 2007. Instead they argue that we may well have entered a period of ‘secular stagnation’ (*The Economist* 2014h; Coutts and Gudgin 2015) characterised by long periods of slow growth (Krugman 2014), low innovation and investment and poor productivity performance (Wolf 2014b), all of which are exacerbated by rising income inequalities (Summers 2013) and adverse demographic change. Of particular concern is the decline of the working age population relative to the retired population (*The Economist* 2014g). The sharp downward shift of the UK’s productivity performance since 2008 has also led to downward revisions to the long-run growth expectations of the UK economy and to heavily downward-adjusted expectations regarding the medium-term fiscal position of the UK (Adam *et al.* 2012; Amior *et al.* 2013). These downward growth expectations also underpin the wide-ranging fiscal retrenchment which the UK is undergoing between 2010 and 2020. These current discussions regarding the UK’s ‘productivity mystery’ or ‘productivity puzzle’ are very important for helping to understand both the current behaviour and likely future prospects of the UK economy.

For the purposes of this book, however, a much deeper, more wide-ranging and a far more long-standing productivity ‘puzzle’ or ‘mystery’ is why the productivity and prosperity benefits in one part of the UK so consistently fail to spill over or transmit to other parts of the UK in a manner which is almost unique amongst advanced economies. As we will see in Chapters 2 and 3, when compared with OECD and EU comparator regions and cities it is abundantly clear that the long-run productivity gains achieved in the core regions of the UK have simply failed to transmit to the non-core regions of the UK over more than four decades. Given that the non-core regions account for almost half of the UK population, the overall effect is that UK national productivity growth is consistently weak, and the UK as a whole is a much poorer country and much more unequal country than public and media debates assume. The result of this is that today within Europe the UK is the only large country with EU-NUTS2 regions in all five quintiles of

GDP per capita and at the level of EU-NUTS3 regions the degree of inter-regional inequality is even greater (Armstrong and Ebell 2015). Moreover, this situation is worsening in the aftermath of the 2008 crisis because the private sector ‘credit crunch’ (Parkinson *et al.* 2009) and the subsequent public sector cutbacks associated with the UK national fiscal consolidation are adversely affecting economically disadvantaged regions relatively even more severely than more prosperous regions (Oxford Economics 2008; Parkinson *et al.* 2009; Beatty and Fothergill 2013; Ward 2013a, 2013b; SPERI 2015)<sup>62</sup> while potentially offsetting and corrective policy schemes have in reality to some extent also favoured the more prosperous regions (Pike *et al.* 2013, 2015). Yet, rather than being a recent or current issue,<sup>63</sup> as will become clear in Chapter 2 the evolution of these UK interregional productivity disparities is a long-run phenomenon over four decades, and not simply a result of the 2008 crisis.

Yet, exactly why the productivity and prosperity benefits in the core regions so consistently fail to spill over to other non-core parts of the UK is a puzzle and a mystery, and a key point of discussion in Chapters 4 and 5 of this book. As we will see over the years there have been many suggested explanations. However, the currently widening UK interregional inequalities cannot be solely or even primarily the result of three decades of structural shifts from manufacturing to modern service industries. In terms of sectoral shifts, by value-added the UK still contains the ninth largest manufacturing industry in the world, although this is down from the UK’s 1990 ranking of fifth since being overtaken by France, Italy, China, Brazil and South Korea (MGI 2012). Yet, many of today’s UK manufacturing sectors are still highly productive, most notably the UK automobile industry (SMMT 2015). Similarly, as we have already seen, many service industries contribute very little to productivity growth and the UK is no exception in this regard (Dolphin and Hatfield 2015). In terms of regional shifts, countries with relatively much smaller service industry bases and larger manufacturing sectors than the UK such as Germany, Japan, Korea, The Netherlands, Sweden, Austria and Finland all experience much smaller interregional inequalities than the UK and all of these countries have also fared much better than the UK in the aftermath of the 2008 crisis.<sup>64</sup> Moreover, their observed interregional inequalities are not particularly characterised by spatial distinction between manufacturing and service industries. Other explanations, beyond overly simple sectoral explanations, need to be sought to understand both the poor productivity performance of the UK and the current interregional inequalities.

Today, although in total size the UK economy is the third largest in the EU the UK ranks only 10th or 11th in terms of productivity and per capita incomes. However, as we have already seen, it exhibits: only just above average productivity scores when compared against the 28 countries of the European Union, including those in Eastern Europe; below average productivity per worker per hour scores in comparison to the Eurozone; below average productivity scores in comparison to the EU-15; and below average

productivity scores when compared with the 34 OECD countries (OECD 2014c). As we see, today the UK's productivity performance is only marginally higher than in Italy or Spain and the current productivity gap between countries such as The Netherlands, Germany, Austria and the Scandinavian economies is approximately the same as the productivity gap between the UK and the Czech Republic (OECD 2014c). The same is true for Australia and Canada (OECD 2014c). More starkly, the current productivity gap between the USA and the UK is only marginally greater than the current productivity gap between the UK and Turkey (OECD 2014c).

These observations suggest that the UK economy as a whole is a far weaker and less productive economy than much of the London-centric press appear to be aware of or to acknowledge. Indeed the UK's productivity performance was barely mentioned in the 2015 general election debates in the UK media.<sup>65</sup> What is more remarkable is how little any of the economic and policy changes experienced by the UK over four decades have altered the relative performance of the UK economy. The 1970s was a difficult decade for the UK economy (Briggs 1983) and this was followed in the 1980s with major changes in many areas of the economy. The difficult industrial relations and inflationary experience of the 1970s along with the deregulation and privatisation agenda of the 1980s and early 1990s tend to lead to highly polarised views and memories even many years later (Marr 2007), and people who experienced these years still tend to hold firm views as to the justification, efficacy and outcomes of government policies. Yet, in comparison to other northern and western European economies and also in comparison to the USA, the relative levels of UK productivity in 2000 were almost exactly the same as they were in both 1990 and 1973, the year the UK joined the Common Market (Broadberry and Klein 2011). In fact, in each case they fell by only a fraction of one percentage point. As we have already seen during the years following the millennium the UK economy grew in comparison to most of our European and OECD competitors, but most of these relative gains have since been wiped out in the aftermath of the 2008 global economic crisis. Again, as we have already seen, the UK economy is now relatively weaker than it was in 1970, 1990 or 2000. Importantly, however, even prior to the 2008 global financial crisis, relative to our main European and OECD competitor countries the UK had hardly advanced any further than its position in 1970 or 1990, and adjusting for labour quality the UK has since declined even further in real terms since 2008 (Krugman 2015b).

For many people these data might appear rather puzzling, as they do not correspond to their preconceptions, leading to something of a conundrum. In particular, claims that the changes wrought during the 1980s redefined the UK as a leading competitive economy appear to be totally unfounded. As such, people who view the widespread economic changes implemented wrought during the 1980s and early 1990s as being both transformational and positive for the UK economy, and London in particular, might question how it could be that these changes have had such little aggregate impacts on

the UK economy? Similarly, beliefs that the long-run economic performance of the UK was undermined by these 1980s changes are also unfounded. In particular, those with personal experiences of the 1980s deindustrialisation (Rowthorne and Wells 1987) might wonder why the adverse effects in aggregate were so much less than they might have expected?

As will be explained throughout in this book, many of the clues providing answers to this conundrum are related to where we are in regional terms. The transformation of the UK economy since the late 1980s and early 1990s has benefited almost exactly one-half of UK economy while for the other half of the economy there is no real evidence of any specific benefits related to these changes. That this is the case is evident both at the regional level and at the urban level, but most importantly, which urban areas display which outcomes depends on which regions the cities are located in. London in particular has benefited from the effects of modern globalisation to a greater extent than most other cities in the world, an experience unparalleled elsewhere in the UK. Although London and the rest of the UK may exhibit some level of demographic convergence<sup>66</sup> regarding patterns of ethnic diversity and composition this is one of the very few areas of social or economic convergence between the capital and the rest of the UK. As such, the strong economic performance of one-half of the UK since the late 1980s is counter-balanced by a much weaker performance on the part of the other half of the UK economy. The combination of these two trends pulling in different directions is that the UK has barely moved forward at all in comparison to competitor countries over the last 40 years, as confirmed by the international data.

As already mentioned above, when discussing economic issues in an international context, many commentators and opinion-formers in the UK's popular press and political circles are heavily, and probably overly, swayed by their daily experience of the success of London and its surroundings, which gives rise to a problem of the geography of (erroneous) perceptions. These misleading and erroneous perceptions are reflected by frequent popular press discussions regarding London's performance relative to New York or Hong Kong in a manner in which the performance of London is taken to reflect the performance of the UK (which it is not), and London's supposed pre-eminence in European cities (even though Paris is as large and richer and seven other European cities are also richer than London). In reality many of these commentators and opinion-formers are largely unaware of how weak are the UK's productivity levels and how narrow the economic gaps are between the UK and countries such as Italy and Spain and how large they are between the UK and the other northern European economies. In other words, discussions linking London and New York or Hong Kong are of little use in analysing UK economic issues because the London regional economy does not even remotely represent or reflect the UK economy as a whole. As we will see in Chapters 2–4, an over-emphasis within the London-centric UK media and political circles on the role played by London in the UK economy tends

to be very misleading and to paint a very distorted picture from what happens in the UK as a whole.

What becomes very clear in Chapters 2 and 3 is that the vast majority of the UK's poor productivity performance and productivity puzzle (Bank of England 2014) or mystery in the aftermath of the 2008 global economic crisis is contained in the 'non-core' regions outside of London and the south of England, with the possible exception also of Scotland. Moreover, to the extent that in the UK poor regional economic performance is also closely associated with poor urban productivity performance, as we will also see in Chapter 3, the UK cities facing severe productivity problems are those cities located in these same non-core regions. The regional dimension of the weak UK productivity performance has been strangely absent in the recent official government publications of HM Treasury, BIS the Department for Business, Innovation and Skills, and other various influential publications (Aghion *et al.* 2013)<sup>67</sup> discussing the UK's productivity, innovation and competitiveness. Yet a moment's thought serves to illustrate the issue. While there are frequent discussions in the press regarding the current UK productivity 'puzzle' or 'mystery', few commentators are heard bemoaning the poor productivity performance of London and its hinterland regions. The reason, as most people understand, is that these regions do not exhibit serious underlying productivity problems, because as we will see in Chapter 4, London has been in the vanguard of the transformations wrought by modern globalisation. As such, much of the UK productivity problem is not fundamentally a UK 'national' problem, but rather a *regional* problem, experienced by all but one of those regions which faced severe de-industrialisation in the 1980s. It is only a national problem to the extent that the aggregated national productivity performance is weakened. Similarly, as we will also see in the forthcoming chapters, the buoyant performance of the London economy and to a lesser extent its hinterland regions is also not a 'national' success story, but rather a *regional* success story. It is only a national success to the extent that the national productivity is strengthened, although the available evidence in Chapters 2, 3 and 5 suggests that few if any of the benefits of the 1990s resurgence of London have spread beyond the southern regions of England. As such, the combined effects of this dividing and decoupling, whereby one-half of the UK experiences economic buoyancy and one-half of the UK experiences economic sluggishness, are that the aggregate long-run national effect is almost zero, when compared to our main European and OECD competitors.

As we will see throughout this book the UK economy is increasingly dislocating, dividing and decoupling into two largely separate economies and one's perceptions regarding how changes of the 1980s and 1990s have impacted on the UK and its role in the world depend almost entirely on where one is geographically located within the UK. This issue regarding perceptions is also critical concerning internal UK debates. The Scottish independence and devolution agendas have now put the issues of the UK's internal governance on a different footing from previously and now governance devolution

and decentralisation in city regions as well as the devolved administrations reflect mainstream political discourses. Moreover, these various different devolutionary pressures are also likely to lead to changes in the nature of, if not the role of, the state. Again, how one views these issues is also likely to be largely shaped by where one is located. On the one hand, there is evidence that England and Wales are decoupling from Scotland in terms of their mutual perceptions of the benefits of union.<sup>68</sup> At the same time, perceptions of the centralisation of the UK state and its role in favouring the London economy over many years differ according to whether one is located in London and the ‘south’ or in ‘the north’.<sup>69</sup> Yet, while there now appears to be no doubt that major changes to the UK internal governance arrangements are in the process, exactly what role these changes will play in re-shaping the long-run economic geography of the UK also depends on the actual forms and scale of the diverse devolution arrangements, and on exactly how the agreed governance changes relate to the underlying economic fundamentals.

On these important and current issues there is now a great deal of commentary and debate in the popular press and the media. However, in comparison to the popular and political narratives, there is surprisingly little by way of any systematic assessment of these issues, little real analysis of the actual wide-ranging evidence regarding these matters, and no overall framework for shaping the discourses. Yet, there is an enormous amount of evidence on these matters which is nowadays publicly available, but much of it is either ignored or under-utilised, and public debates therefore tend to over-emphasise the ideas of a small number of high-profile and popular publications or of a few specific and high-profile sources of commentary and opinion. The obvious danger here is that major policy decisions become overly dependent on narrow narratives and on political discourses which are too tightly framed. As this book will consistently argue, however, the UK interregional issues are fundamentally economic issues, not political or constitutional issues, although they do have profound political and constitutional implications, as is now becoming clearly evident. Therefore, the explicit intention of this book is to provide a much-needed and systematic analysis of the nature, causes and consequences of the UK’s interregional inequalities and imbalances and to do this in a way which underpins a robust framing for these discussions in the popular and political discourses.

## **1.5 Conclusions**

This chapter has outlined the case that the UK does indeed face a serious regional and national economic problem relating to the scale of the UK’s interregional imbalances and the apparent inability of the government system to respond in a manner which reflects the wishes and needs of local communities. The UK is increasingly dislocating and decoupling internally and this puts immense strain both on the legitimacy and effectiveness of the UK’s governance systems, as well as limiting the overall productivity

growth of the country as a whole. The Scottish independence referendum has thrown these issues into sharp relief and the allied governance and devolution trends in other parts of the UK also reflect growing tensions and strains within the UK's governance system. Yet, the issues are so fundamental and wide-ranging that even if Scotland eventually does choose to leave the union, as we will see throughout this book, the overall arguments here barely change at all.

## Notes

- 1 “Time for a Civic Surge”, *The Economist*, 6 June 2015; “Spreading their Wings: English Cities”, *The Economist*, 6 June 2015.
- 2 Quoted in Stark *et al.* (2013).
- 3 See [www.bbc.com/news/uk-30520065](http://www.bbc.com/news/uk-30520065).
- 4 We all know that the old model of trying to run everything in our country from the centre of London is broken. It's led to an unbalanced economy, it's made people feel remote from the decisions that affect their lives. It's not good for our prosperity, it's not good for our democracy.  
George Osborne announcing on 14 May 2015 that a bill for English city devolution is to be included in the first Queen's Speech of the new Parliament following the 2015 UK general election. See “George Osborne Outlines City Devolution Plan for England”, [www.bbc.com/news/uk-politics-32726171](http://www.bbc.com/news/uk-politics-32726171).
- 5 “Bagehot: Not Just a Hatchet Man”, *The Economist*, 14 March 2015.
- 6 These analyses run counter to much of the previous orthodoxy which had assumed that inequality was necessary for growth, instead arguing that the evidence does not support this contention. However, some commentators have questioned the veracity of these analyses arguing that they do not necessarily imply that inequality is bad for growth. However, this is a slightly different argument to saying that inequality is necessary for growth. See: Giles, C., 2015, “Inequality is Unjust – It is Not Bad for Growth”, *Financial Times*, 19 August.
- 7 As reflected in the 2014 Richard Dumbleby Lecture entitled “A New Multilateralism for the Twenty First Century” given by the Managing Director of the IMF Christine Lagarde on 3 February 2014. See: [www.imf.org/external/np/speeches/2014/020314.htm](http://www.imf.org/external/np/speeches/2014/020314.htm) and in National Intelligence Council (NIC 2012) report.
- 8 [http://report.mitigation2014.org/spm/ipcc\\_wg3\\_ar5\\_summary-for-policymakers-approved.pdf](http://report.mitigation2014.org/spm/ipcc_wg3_ar5_summary-for-policymakers-approved.pdf).
- 9 See also: “Monitoring Economic Performance, Quality of Life and Sustainability” jointly produced by the French ‘Conseil d'analyse économique’ and the German Council of Economic Experts, December 2010. Available at: [www.cae.gouv.fr/IMG/pdf/095\\_ANG.pdf](http://www.cae.gouv.fr/IMG/pdf/095_ANG.pdf).
- 10 See: [www.oecd.org/document/10/0,3746,en\\_2649\\_201185\\_42393354\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/10/0,3746,en_2649_201185_42393354_1_1_1_1,00.html).
- 11 See: [www.whitehouse.gov/sites/default/files/omb/assets/memoranda\\_2010/m10-21.pdf](http://www.whitehouse.gov/sites/default/files/omb/assets/memoranda_2010/m10-21.pdf); [www.whitehouse.gov/blog/2010/06/30/place-based-investments](http://www.whitehouse.gov/blog/2010/06/30/place-based-investments); [www.eda.gov/pdf/CEDS\\_Flyer\\_Whit\\_Background.pdf](http://www.eda.gov/pdf/CEDS_Flyer_Whit_Background.pdf); <http://yosemite.epa.gov/opa/admpress.nsf/0/75E1F57EB6D0FCEC8525788CA0063A5CB>.
- 12 Brazil, Russia, India, Indonesia, China and South Africa.
- 13 [www.smith-commission.scot/wp-content/uploads/2014/11/The\\_Smith\\_Commission\\_Report-1.pdf](http://www.smith-commission.scot/wp-content/uploads/2014/11/The_Smith_Commission_Report-1.pdf).
- 14 Indeed, the idea that different parts of the UK might be governed in different ways by different people goes back to the 1880s (King 2015).

- 15 These realities whereby some professional players and coaches switch between codes but supporters and club members inhabit quite different social networks, also largely hold in other countries where both codes of rugby are played, such as Australia, New Zealand, France and Samoa.
- 16 Neville, G., “The North is Being Cut Adrift in English Football – and I Fear the Damage May be Permanent”, *The Daily Telegraph*, 25 September 2015.
- 17 “This General Election Will be Fought Along Regional Lines”, *Financial Times*, 4 January 2015.
- 18 In Part 1 of the Evan Davis BBC television programme *Mind the Gap: London vs the Rest* which was broadcast on Monday 3 March 2014, BBC2 at 21.00–22.00.
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- 48 Which were part of the EU by 1995.
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- 50 Part of the difficulty of assessing the long-run performance of the UK economy relative to other comparators, and in particular European comparators, is because of changing boundaries and borders, and estimates need to adjust for these changes. Broadberry and Klein (2011) provide estimates for the period 1870–2000 which explicitly control for these changes.
- 51 The former country of West Germany with some 63 million people was merged in 1990 with the former East Germany, a country whose population of 16 million was one-quarter of that of West Germany but whose GDP per capita in 1990 was also only one-third of that of West Germany (Broadberry and Klein 2011). The reunification involved enormous fiscal transfers over more than two decades from the western to the eastern German regions.
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