OXFORD ECONOMICS

Solent LEP economic outlook

March 2014

Final report

A report prepared for Solent LEP

OXFORD ECONOMICS

Contents

Executive Summary

Introduction

Oxford Economics were commissioned by Solent LEP in late 2013 to provide economic modelling support to the Solent LEP Board. This report presents the results of the analysis.

Macroeconomic environment

The outlook for growth is cautiously optimistic given the challenges present, not least the level of government debt across many of the world's most developed countries. We do however expect the two speed growth of developing and developed economies to continue.

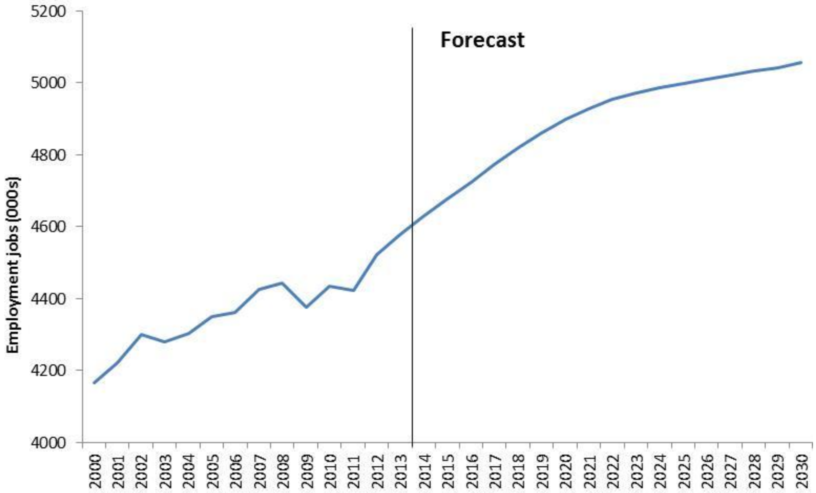
Our forecast for UK GVA growth of 2.4% in 2014 would represent the strongest outturn for seven years. Although the worst of the Eurozone crisis appears to have passed, any further escalation would risk tipping the UK back into recession due to the strong trade links and the potential for spillovers into the UK banking system. Encouragingly though, business investment and consumer spending levels have begun to increase, having remained low for the last 5 years as a result of economic uncertainty.

UK employment is forecast to be about 7% higher in 2023 than today, equivalent to an extra 2.3 million jobs. For sustainable, balanced economic growth, the UK must undergo an export and investment led recovery. This is why we expect growth to be led by exportable service sector activity.

South East to remain a key driver of UK growth

The South East has been one of the UK's top performing regions, and we expect the it to continue recording above average jobs growth over the forecast period with average annual employment growth of 0.83% compared to 0.68% for the UK average. Faster jobs and GVA growth reflect the structure of the South East economy which is geared more to growth sectors than those that have been shedding jobs or those reliant on restricted public spending.

Figure 1: Employment growth in the South East



Source: Workforce Jobs, Oxford Economics

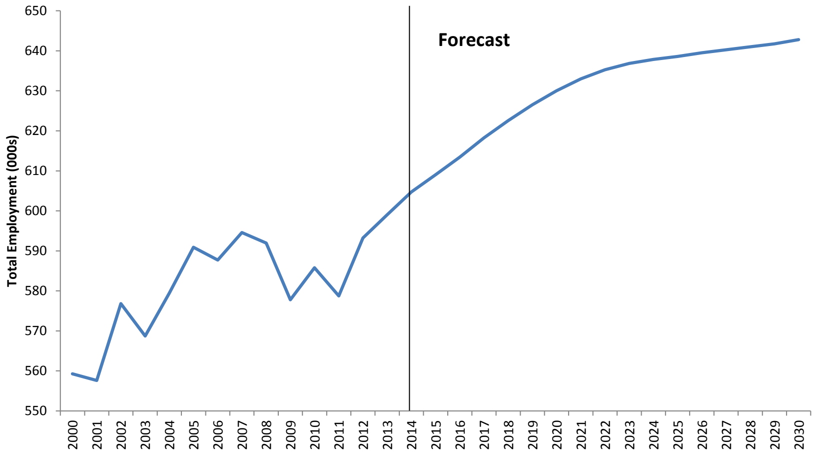
Despite the recent financial crisis and resulting recession, the labour market in the South East remains fairly tight. Resident employment rates in 2013 were 80.3% while the claimant unemployment rate was 1.8% in December 2013. Our baseline forecasts suggest spare labour will be reduced further with job creation.

The South East has traditionally been an attractive place for migrants and our labour market outlook suggests this trend will continue, albeit at slightly lower levels over the forecast period.

Solent economy expected to enjoy strong growth

The forecasts for Solent LEP are on the whole positive. Average employment growth of 0.72% per annum is expected to create an addition of 31,000 jobs by 2020. Over the period 2013 to 2030 this rises to 44,000 – growing at an average rate of 0.42% per annum. GVA in Solent LEP will follow suit, with positive year-on-year growth expected throughout the forecast period. GVA is forecast to rise at an annual average rate of 2.8% to 2030.

Figure 2: Solent employment, 2000 to 2030



Source: Oxford Economics

Employment growth in the outlook period is concentrated in the skilled services sectors (admin & support and professional, scientific & technical sectors) whilst manufacturing continues its decline. Consequently the Solent LEP economy (like the rest of the UK) will demand a more highly skilled workforce as this trend continues.

Table 1: Baseline employment growth in each sector (i.e. policy off outlook), 2000-08, 2008-13, and 2013-20 and 2020-23

	2000-08 (000s)	2008-13 (000s)	2013-20 (000s)	2020-30 (000s)
Agriculture, forestry and fishing	-0.6	-0.2	-0.4	-0.4
Mining and quarrying	0.1	0.1	0.0	-0.1
Manufacturing	-19.0	-4.7	-2.9	-6.9
Electricity, gas, steam and air conditioning supply	-0.7	0.0	-0.2	-0.2
Water supply; sewerage, waste management and remediation activities	0.7	-0.3	-0.1	-0.1
Construction	0.6	-3.7	4.7	3.8
Wholesale and retail trade; repair of motor vehicles and motorcycles	0.3	-3.3	4.8	-0.1
Transportation and storage	7.8	2.8	2.5	-1.1
Accommodation and food service activities	1.2	0.9	3.8	0.6
Information and communication	7.7	6.9	4.3	3.0
Financial and insurance activities	-2.6	0.0	0.2	0.1
Real estate activities	2.7	0.8	1.5	1.2
Professional, scientific and technical activities	8.7	6.2	6.8	3.7
Administrative and support service activities	8.3	-3.1	7.5	4.2
Public administration and defence; compulsory social security	-5.6	-5.4	-3.9	-0.3
Education	2.3	4.6	-1.4	0.5
Human health and social work activities	16.2	9.6	-0.5	2.9
Arts, entertainment and recreation	1.6	-2.1	2.5	1.5
Other service activities	2.9	-2.2	1.7	0.5

Source: Oxford Economics

At present the skills structure of Solent LEP lags behind the South East, with a significantly lower proportion of workers with NVQ4+ qualifications. A lower skilled workforce is a major contributor to the productivity gap that exists between Solent LEP and the South East. The skills gap with the South East must be addressed if the productivity gap is to be narrowed.

Though labour market will have little spare capacity

The strong growth in employment over the forecast period coupled with flat growth in the working age population will squeeze the labour market in the years ahead. The labour market tightening should push down unemployment rates from current levels, though additional demand for labour in Solent LEP will increasingly have to be satisfied by the inflow of migrants or a rise in the level of commuters into the area.

Preferred growth strategy offers labour market benefits

The Preferred Growth Scenario has a number of headline targets for the economy by 2020:

- An additional 15,500 jobs above base by 2020;
- GVA growth to rise to 3.5% pa
- An increase in productivity of £6,500 (including baseline growth);
- Increase employment rate from 78% to 80%;
- Increase economic activity rate from 80% to 81%;
- Raise the business birth rate from 3.6% to 4.1%;
- Raise the share of the working age population with NVQ 4+ skills from 32% to 36% by 2020; and
- Improve business survival rates.

Through the accompanying impact model to this report we are able to model the majority of the growth scenario. We exclude the skills target and business survival rate target. We find that the preferred growth scenario achieves the labour market targets. The 15,500 additional jobs pushes up resident employment rates and activity rates. However the labour market is already tight and the creation of 15,500 jobs quickly exhausts the available pool of unemployed.

Table 2: headline indicators in 2020, baseline versus scenario

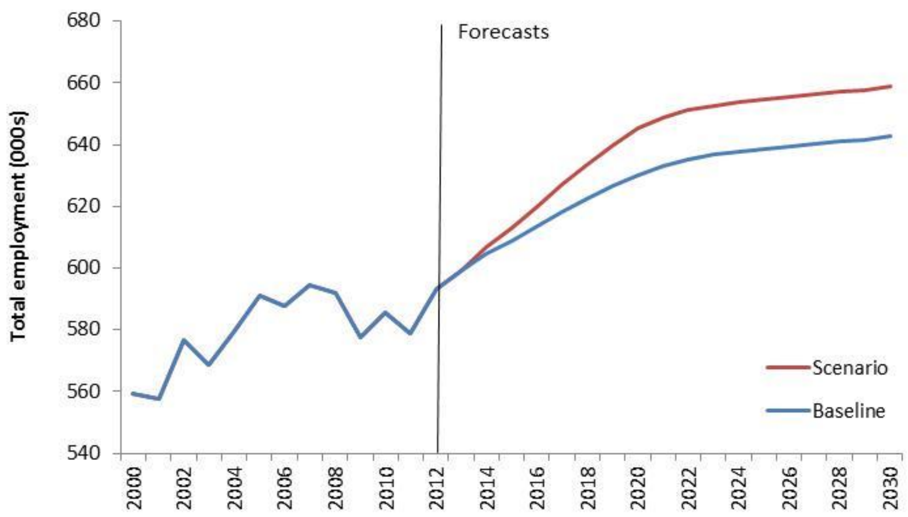
Key Indicators	Baseline	Scenario
Additional employment	N/A	15.53
Employment (pa)	0.72%	1.07%
Productivity (pa)	2.27%	2.28%
GVA % growth (pa)	3.01%	3.38%
Growth in productivity	N/A	£51
Productivity relative to South East	87.5%	87.6%
Economic Activity rate (%)	81.8%	82.8%
Resident employment rate (%)	80.0%	81.4%

Source: Oxford Economics

Note, we forecast productivity to rise by £6,450 under the policy off or baseline outlook.

Consequently the preferred growth scenario would result in a productivity increase of £6,500 over the period 2013 to 2020.

Figure 3: baseline and scenario employment levels in Solent



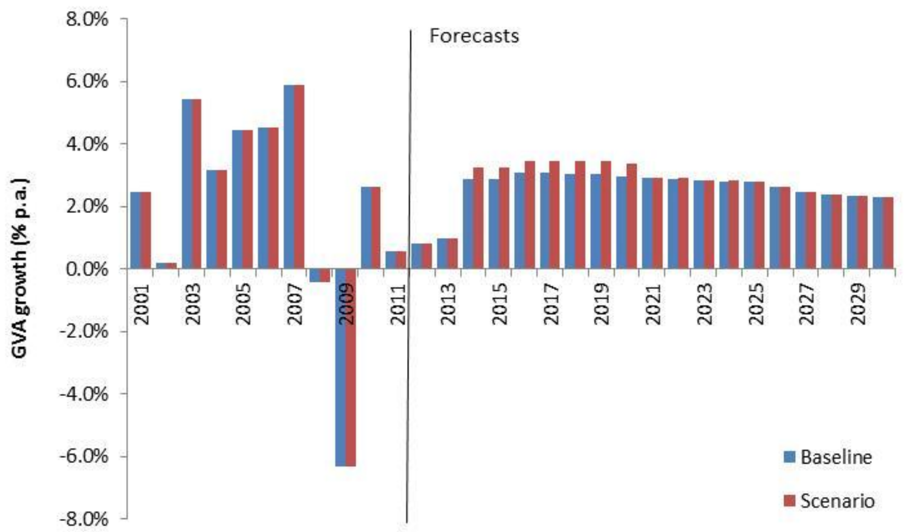
Source: Oxford Economics

As business compete with each other and bid up wage rates, the economy becomes increasingly attractive for migrants. Demand for labour is therefore increasingly filled by new migrants to the economy which in turn pushes up population numbers.

GVA growth target more difficult to achieve

Annual average GVA growth quickens from 3% to 3.4% given the additional jobs being created. Under the policy off scenario we forecast productivity to increase by £6,450 over the period 2013 to 2020. Under the preferred growth scenario productivity increases by a further £50 meaning the productivity gap with the South East improves by a relatively insignificant 0.1 pp.

Figure 4: Baseline and scenario GVA growth (% pa)



Source: Oxford Economics

A general uplift of skills in the economy is likely to be much more successful in raising productivity levels given the strong positive relationships between skill levels and productivity / wage levels. Though we should note that the literature suggests notable improvements in skill levels, and hence productivity, take considerable periods of time to be achieved. Consequently dramatic improvements in skills and productivity are unlikely to be achieved before 2020.

1 Background

1.1 Introduction

Oxford Economics were commissioned by Solent LEP in late 2013 to provide economic modelling support to the Solent LEP Board. This report presents the results of the analysis. More specifically it provides a discussion of:

- Recent macro trends and forecasts;
- An understanding of economic performance in the Solent LEP;
- Oxford Economics baseline outlook for the LEP using our December 2013 local forecast estimates;
- Estimates of a faster preferred growth scenario for the LEP; and
- Implications of this faster growth.

1.2 Previous research

In the Autumn of 2009, Oxford Economics were commissioned to update and refresh the Partnership for Urban South Hampshire (PUSH) economic development evidence base, including an assessment of the impact of the recession on the sub-region.

Aside from using a range of official data sources to track the economic performance and makeup of the PUSH region, this involved bespoke economic modelling of the linkages between the parts of PUSH, and between PUSH and the wider South East and UK economies.

This contributed to the formulation of the PUSH area economic strategy[1] by DTZ, subsequently adopted by the PUSH Joint Committee, comprising of senior representatives of the twelve constituent local authorities.

1.3 Structure of the report

This report takes the following structure:

- **Macroeconomic conditions:** this section provides a discussion of the macroeconomic environment. We provide baseline forecasts at an international, national and regional level;
- **Solent's baseline outlook:** this section provides a discussion of recent trends and the baseline outlook for the LEP. We provide some local authority level commentary, though the

[1] http://www.push.gov.uk/work/economic-development/economic-development-strategy.htm

detailed data is provided in the accompanying Excel impact model;

- **Preferred Growth Scenario:** in this section we provide the results of the preferred growth scenario for the LEP economy. We discuss the labour market impact and resulting demographic implications. We also briefly cover the impacts on GVA growth and productivity;
- **Summary:** this section provides a summary of our findings.

2 Macroeconomic conditions

This section provides a brief overview of the current economic environment at a global, UK and South East level.

Key points:

- The recession brought unprecedented change to developed economies with the 'new normal' environment becoming more reliant on export-led growth;
- The outlook for growth is cautiously optimistic given the challenges present, not least the level of government debt across many of the world's most developed countries, particularly in the Eurozone;
- The UK experienced a deeper and longer recession than many developed economies with its fortunes inherently linked to the Eurozone;
- For sustainable, balanced economic growth, the UK must undergo an export and investment led recovery;
- The UK labour market is likely to remain a key source of domestic risk, with the private sector struggling to create sufficient jobs to offset cuts in the public sector over the forecast period;

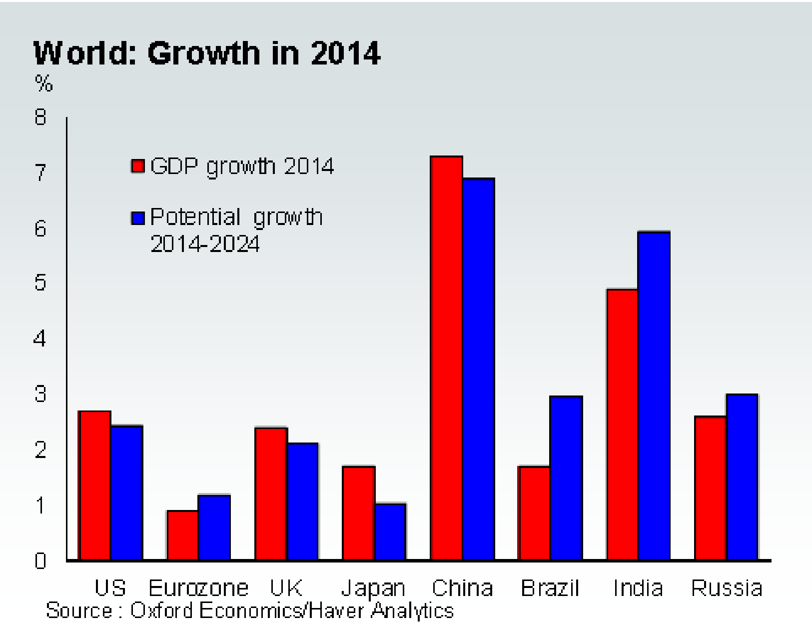
2.1 Global economy patchy

Overall, 2013 has been a disappointing year for global growth, with world output set to expand by a modest 2.1%. But growth has not disappointed everywhere – the US has seen sub-trend growth and key emerging markets have experienced a marked slowdown, but there have been strong rebounds in Japan and the UK. Our latest forecasts suggest this pattern of divergent growth trends will continue into 2014, among both the advanced and emerging economies.

Both the US and the Eurozone look set to end 2013 on a weak note with low growth in Q4. For the US this simply relates to a pause after strong Q3, but for the Eurozone more enduring problems exist.

We expect US growth to accelerate to a 3% annual pace by the second half of 2014, but the Eurozone is in danger of renewed recession; our forecast is for just 0.8% growth over 2014. The risk of a slide into deflation in the Eurozone may be a key theme next year.

Figure 2.1: Outlook for key emerging economies



Among the key emerging economies our forecasts suggest growth in China will continue at around a 7% pace next year, moderate by the standards of recent years. More serious underperformance is likely in Russia, India and Brazil – which appear to be facing structural impediments to sustained rapid growth.

Another area of divergence in 2013 has been policy settings. This too is likely to continue into 2014. Some emerging economies will continue with tight or even tighter monetary stances due to inflationary pressures and currency weakness, holding back growth.

This may be exacerbated by the Federal Reserve reducing its asset purchases (which we expect from early 2014) the fallout from which remains uncertain. Meanwhile, in the Eurozone policy is likely to be loosened further – but probably not enough to underpin faster growth – while aggressive monetary expansion will continue in Japan. One consequence of this is likely to be downward pressure on the euro and the yen during 2014.

Table 2.1: Annual GDP growth for selected economies

World GDP Growth % Change on Previous Year	2012	2013	2014	2015	2016	2017
US	2.8	1.9	3.1	3.2	3.0	2.9
Japan	1.4	1.7	1.8	1.4	0.9	1.1
Eurozone	-0.6	-0.5	0.8	1.4	1.5	1.6
of which:						
Germany	0.9	0.5	1.5	1.7	1.5	1.6
France	0.0	0.1	0.5	1.1	1.3	1.4
Italy	-2.6	-1.9	0.3	1.2	1.4	1.4
UK	0.3	1.9	2.6	2.4	2.6	2.6
China	7.7	7.6	7.3	7.2	7.2	7.2
India	5.1	4.7	4.9	5.1	6.0	6.6
Other Asia	2.5	3.3	4.3	5.2	5.0	4.6
Mexico	3.7	1.3	3.8	4.2	4.1	4.0
Brazil	1.0	2.2	1.7	2.7	3.2	3.4
Other Latin America	3.7	3.1	3.0	3.3	3.9	3.9
Eastern Europe	2.1	1.5	2.1	3.1	3.5	3.6
MENA	4.3	3.8	4.4	5.0	4.8	4.7
World	**2.3**	**2.2**	**2.9**	**3.2**	**3.2**	**3.3**
World (PPP)	**3.0**	**2.9**	**3.6**	**3.9**	**4.0**	**4.1**

Source: Oxford Economics

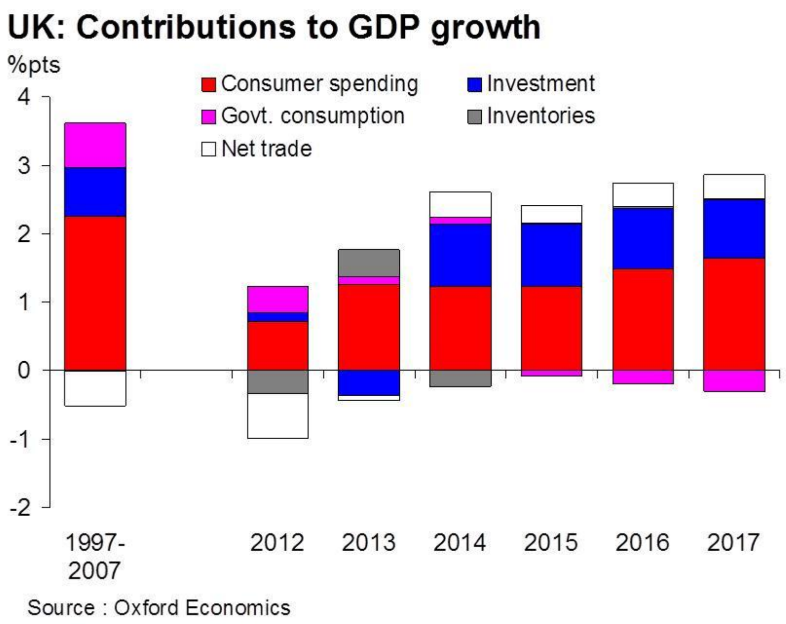
2.2 UK overview

The UK officially emerged from recession in Q1 2010, with historical revisions to GDP growth published by the ONS eliminating the previous technical double dip recession in early 2012. After several false starts, 2013 finally seen the UK recovery gather momentum, with growth steadily accelerating through the year. Though the recovery has been narrowly focused on the consumer and the housing market thus far, our forecast shows it slowly broadening out towards business investment and exports over the next two years. While the economy makes this transition, quarterly growth is likely to slow a little from recent rates, though our forecast of growth of 2.4% in 2014 would still represent the strongest outturn for seven years.

Although the worst of the Eurozone crisis appears to have passed, any further escalation would risk tipping the UK back into recession due to the strong trade links and the potential for spillovers into the UK banking system. Encouragingly though, business investment and consumer spending levels have begun to increase, having remained low for the last 5 years as a result of economic uncertainty.

Activity has steadily accelerated through 2013, culminating in quarterly GDP growth of 0.7% in Q4 2013. Wider economic data for Q4 had been more mixed. On the one hand the Purchasing Managers Index surveys had remained very strong at close to record levels implying GDP growth in excess of 1% in Q4. However, the Purchasing Managers Index surveys appear to have decoupled from other indicators. Retail sales fell sharply in October and were little better than flat on a three-month basis, while the CBI Distributive Trends Survey reported a sharp slowdown in sales growth.

Figure 2.2: Improving and more balanced growth in prospect

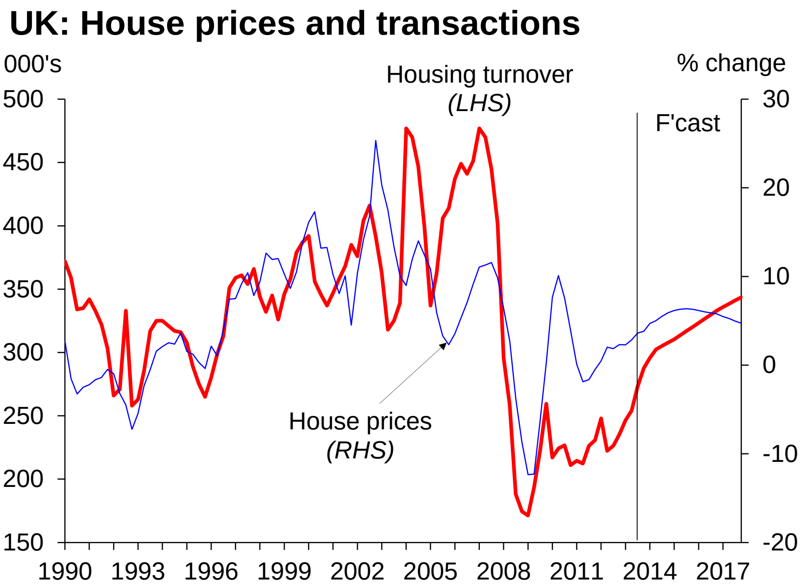


This apparent cooling of the consumer sector emphasises the importance of the recovery broadening out to investment and exports and recent survey evidence provides some encouragement that this is beginning to happen. This transition is unlikely to be smooth and we expect GDP growth to cool a little in the early part of 2014. Nevertheless growth next year and beyond will be supported by:

- **Stronger household finances** – the acceleration in consumer spending growth through 2013 came despite relatively weak growth in real household incomes, with households financing this additional spending by sharply reducing their rates of saving. This reflects stronger consumer confidence, which has lowered precautionary saving, and a steady decline in deposit rates, which has reduced incentives to save. The scope to reduce savings further is limited, but prospects for household incomes are brighter in 2014. Falling unemployment and the emergence of skills shortages in some sectors should put upward pressure on wage growth. At the same time, we expect inflation to cool to below 2%, reflecting weaker pressures from energy and food prices. These factors will increase household purchasing power - though this is process will be gradual and in the near-term consumer spending growth is likely to slow.
- **Increased housing market activity** – both house prices and activity have continued to recover, supported by the Help-to-Buy

scheme. We expect momentum to continue to build as household incomes strengthen and the impact of the mortgage guarantee part of Help-to-Buy is seen. However, in a sign of concern that a bubble might develop, the Bank of England has removed the mortgage lending incentive from its Funding-for-Lending Scheme. Many lenders had made little use of the scheme in recent quarters, so the impact on mortgage availability should be limited, but this does send a clear message that the Bank is willing to intervene should it feel the need to. We think that further intervention will prove unnecessary because there are signs that the stronger market has encouraged a robust pickup in house building. Our forecast shows a firm recovery in residential investment, with housing also supporting consumer spending through confidence and wealth effects. As a result, UK house prices are forecast to grow by 3.1% in 2013 and 5.3 % in 2014. On the back of improving economic prospects we expect UK house price growth to continue beyond. Indeed, UK house price growth is forecast to accelerate in 2015 (6.4%) and 2016 (6.0%). After 2016, UK house price growth is forecast to ease slightly to around 5% a year (see the figure below).

Figure 2.3: Revival in the housing market



Source: Oxford Economics

- **Corporate confidence strengthening, supporting investment** – a wide range of business surveys are now reporting stronger sentiment and investment intentions. With larger firms, in particular, reporting strong financial positions with plenty of cash on balance sheets, this should lead to an increasingly strong recovery in business investment over the coming years.

- **Improving export outlook** – business surveys have reported an improvement in export demand since the summer, as the recovery in advanced economies has gained momentum. Our global forecasts suggest that this will continue, with annual growth in world trade (weighted by UK export shares) forecast to accelerate from 2.1% in 2013 to 4.6% in 2014 and 5.7% in 2015.

2.3 Longer term recovery still service led

The pace and composition of economic growth described above shape the UK sectoral employment outlook. UK employment is forecast to be about 7% higher in 2023 than today, equivalent to an extra 2.3 million jobs.

Professional, scientific & technical activities (an additional 601,000 jobs by 2023) and administrative & support service activities (554,000) are forecast to provide the largest absolute increases in jobs over the decade ahead. Most other sectors are expected to see employment rise over this period, including the relatively small but rapidly growing information & communications sector, and also a recovery for the long suffering construction industry.

Table 2.2: Sectoral employment growth in the UK, selected years

	1998-2008 (000s)	2008-2013 (000s)	2013-2023 (000s)	2023-2036 (000s)
Agriculture, forestry and fishing	-68	-24	-31	-32
Mining and quarrying	-12	8	-14	-20
Manufacturing	-1449	-218	-259	-461
Electricity, gas, & steam	-17	27	-13	-14
Water supply; sewerage, waste management	7	32	-13	-14
Construction	429	-277	325	248
Wholesale and retail trade	176	-100	272	44
Transportation and storage	195	67	169	-11
Accommodation and food service activities	267	79	221	31
Information and communication	247	105	238	133
Financial and insurance activities	91	-58	14	8
Real estate activities	192	58	161	106
Professional, scientific and technical activities	647	325	601	332
Administrative and support service activities	558	150	554	272
Public administration and defence	151	-177	-219	0
Education	573	171	-57	93
Human health and social work activities	796	383	40	275
Arts, entertainment and recreation	226	1	174	115
Other service activities	151	-74	128	54
Total	**3157**	**477**	**2290**	**1158**

Source: Workforce Jobs, Oxford Economics

The most significant reduction in absolute terms is forecast for the manufacturing sector, where more than 250,000 jobs are expected to be lost across the UK by 2023. At the aggregate level this reflects productivity advancements across the sector which means rising activity can be accommodated by fewer workers.

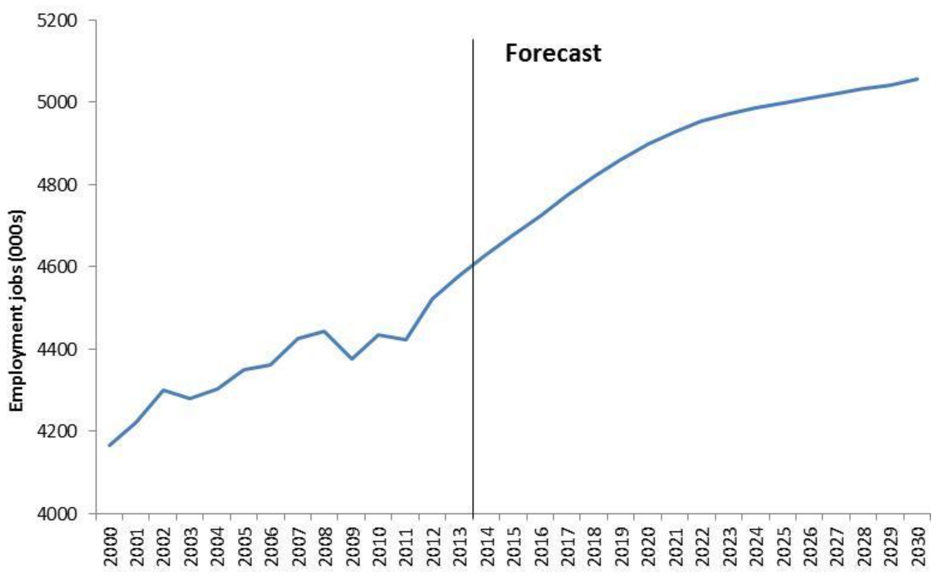
Parts of the public sector, most notably public administration and education are expected to employ fewer workers due to government spending restraint. The majority of cuts in these sectors will occur early in the forecast period, with a modest recovery, albeit to below current levels, over the longer term.

2.4 The outlook for the South East

2.4.1 Faster jobs and GVA growth

The South East has been one of the UK's top performing regions. Although it contracted in 2009, growth in jobs in 2010 brought employment in the region back to near its pre-recession peak. From 2008 to 2013, jobs in the South East grew faster than the UK average (0.37% per annum compared to 0.18% respectively). We expect the South East to continue recording above average jobs growth over the forecast period with average annual employment growth of 0.83% compared to 0.68% for the UK average.

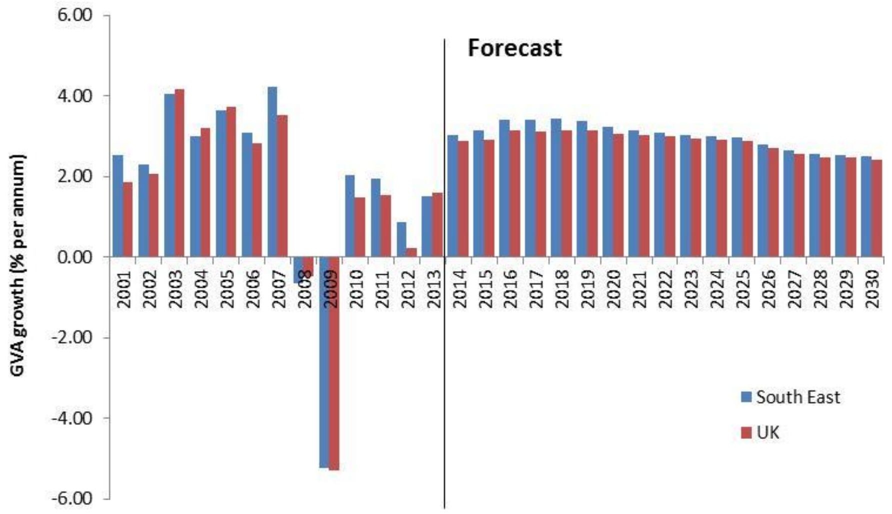
Figure 2.4: Employment growth in the South East



Source: Workforce Jobs, Oxford Economics

This faster jobs growth is reflected in the GVA data with the South East outperforming the UK average since 2010. Figure 2.5 shows that we expect the region to grow by 3% in 2014 and 2.1% in 2015.

Figure 2.5: Annual GVA growth in the South East

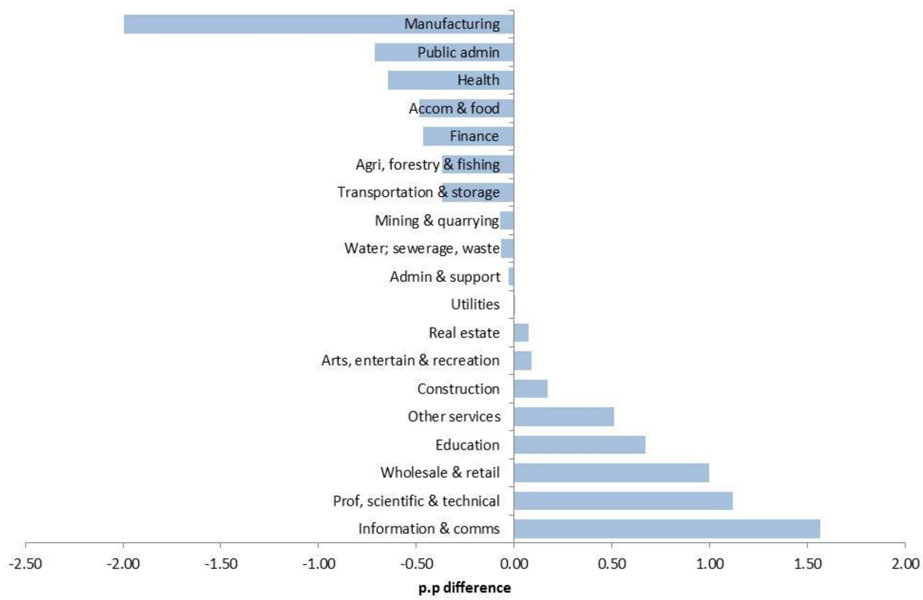


Source: Oxford Economics

2.4.2 Driven by the structure of the economy

Faster jobs and GVA growth reflect the structure of the South East economy. Figure 2.6 shows percentage point (pp) difference between the South East's sectoral employment shares and the UK's. Sectors with positive pp differences reflect areas of the economy where the South East has a larger proportion of jobs relative to the UK (and vice versa).

Figure 2.6: Structure of the South East economy relative to the UK



Source: Oxford Economics

An analysis of sectoral employment shows that the South East is less reliant on:

- Manufacturing that continues to shed jobs;
- Public administration which has been constrained by austerity measures; and
- Health which also faces a tight public spending environment.

On the other hand the South East is more reliant on "Information and communication" and "Professional, scientific & technical" sectors, both of which are key areas of growth for the wider UK economy.

Table 2.3 shows sectoral employment prospects in the region over the forecast period. Growth is driven by the service sector with Professional, scientific and technical activities creating 76,300 net new jobs from 2013 to 2020, Admin and support creating a further 67,400 jobs and information and communication creating 38,800 jobs. Consumer led sectors like retail, accommodation and food, arts, entertainment and recreation, and other service activities are also expected to grow, providing 117,900 jobs in the region.

Table 2.3: Sectoral prospects in the South East

	2013-2020		2020-30	
	Jobs (000s)	%	Jobs (000s)	%
Agriculture, forestry and fishing	-3.8	-11.0	-4.2	-13.6
Mining and quarrying	-0.8	-11.4	-1.8	-29.0
Manufacturing	-16.7	-6.1	-39.9	-15.4
Electricity, gas, steam	-1.5	-9.1	-1.8	-12.1
Water; sewerage, waste	-1.1	-4.3	-1.3	-5.3
Construction	42.1	14.3	33.6	10.0
Wholesale and retail	45.0	6.1	7.0	0.9
Transportation and storage	17.4	8.5	-6.0	-2.7
Accommodation and food	29.3	10.8	6.2	2.1
Information and communication	38.8	15.0	25.9	8.7
Finance	-0.5	-0.4	-1.5	-1.1
Real estate activities	18.4	23.4	15.2	15.7
Prof, scientific and technical	76.3	18.1	43.6	8.7
Admin and support	67.4	18.0	35.9	8.1
Public admin	-22.3	-12.1	-1.7	-1.1
Education	-10.6	-2.5	3.2	0.8
Health	-1.0	-0.2	23.5	4.3
Arts, entertainment and recreation	23.8	18.6	14.8	9.7
Other service activities	19.8	13.6	7.1	4.3
Total	**320.0**	**7.0**	**157.8**	**3.2**

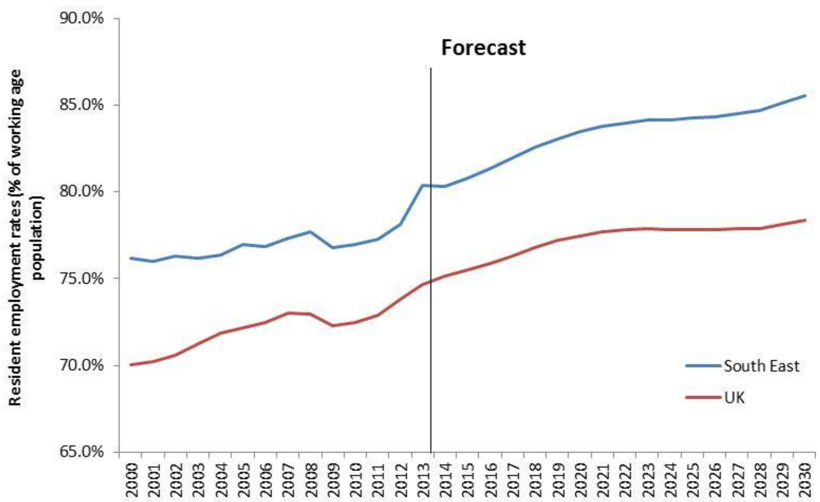
Source: Oxford Economics

The public sectors of public admin, education and health will act as a drag on the economy shedding nearly 34,000 jobs by 2020, while manufacturing and agriculture are also estimated to contract by over 20,000 jobs dampening performance.

2.4.3 Though the labour market is tight

Despite the recent financial crisis and resulting recession, the labour market in the South East remains fairly tight. Resident employment rates in 2013 were 80.3% (a full 5.7 pp above the UK average). In addition the claimant unemployment rate was 1.8% in December 2013 compared to 2.9% for the UK average.

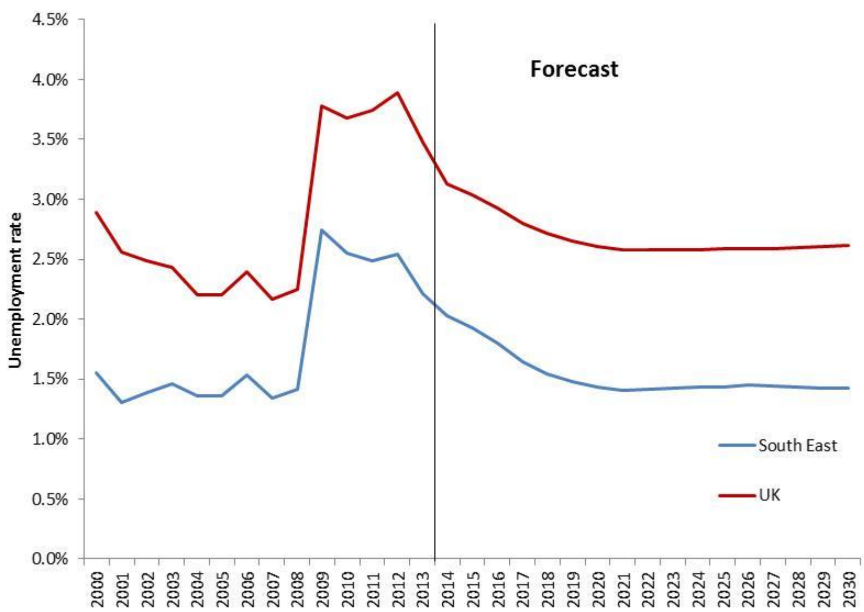
Figure 2.5: Resident employment rates in the South East and UK



Source: Oxford Economics

Our baseline forecasts suggest resident employment rates will continue to rise with job creation and the increasing number of people working past retirement age. As expected unemployment rates will continue their gradual fall before settling at around 1.4% at the end of the decade.

Figure 2.6: Unemployment rates in the South East and UK



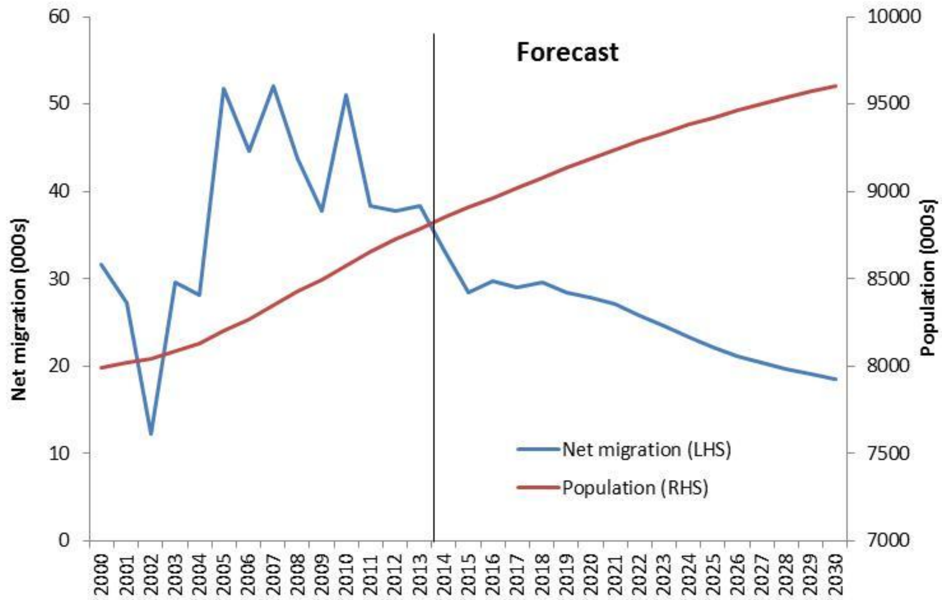
Source: Oxford Economics

With such little spare capacity in the resident labour market, growth in the economy will have to rely on two other sources of labour, commuters and migrants to the region.

2.4.4 What does this mean for population?

The South East has traditionally been an attractive place for migrants. A stronger economy relative to the national average and its proximity to London has contributed to the strong positive net migration trends of the region. Our labour market outlook suggests this trend will continue, albeit at slightly lower levels over the forecast period.

Figure 2.7: Net migration and population trends in the South East



Source: Oxford Economics

On the back of continued net-in-migration, the region's population is forecast to continue to grow. This is part and parcel of continued strong net migration flows to the UK as a whole, with the Oxford Economics forecast for net migration showing an annual net inflow to the UK of 140,000 per annum over the medium term, lower than the official projection of 165,000 per annum (see Annex B for a more detailed discussion).

3 Solent's baseline outlook

3.1 Introduction

This section provides an overview of Solent LEP's baseline outlook. The discussion covers demography, the labour market, sectoral prospects and wealth.

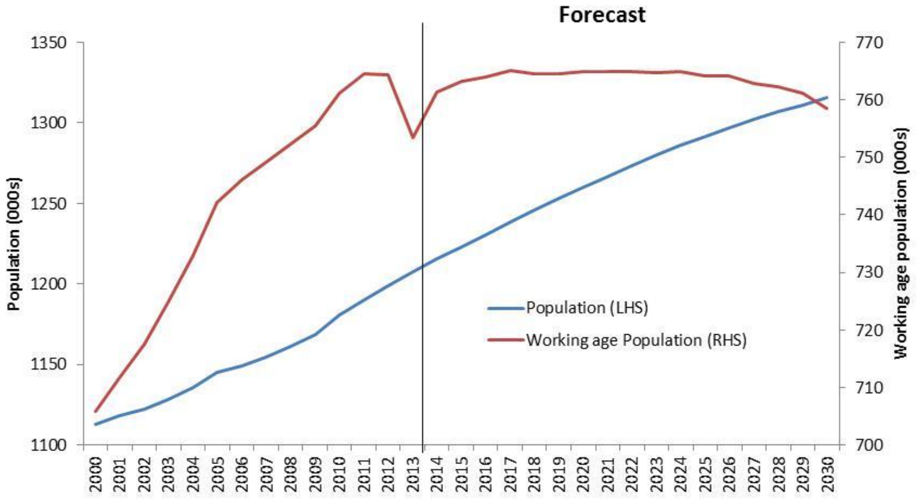
Key points:

- Population is expected to grow in the Solent LEP, however working age population (those aged 16 to 64) will be relatively stagnant and eventually start to fall;
- Net migration is expected to drive much of the growth in population (62% of population growth). A strong labour market will attract UK residents and foreign migrants;
- Baseline forecasts of employment growth (i.e. policy off forecasts) over the period 2013-2020 show robust growth of 0.72% per annum and an increase of 31,000 jobs;
- Consequently, resident employment rates are expected to improve on the back of employment growth and structural shifts in the economy;
- Spare capacity in the unemployed will fall relatively quickly signaling a tightening of labour market conditions;
- Growth is expected in exportable service sectors meaning the economy will become increasingly skills hungry. Though an analysis of skills reveals a skills gap with the South East average;
- Productivity levels have consistently lagged the South East average which will be partly due to lower skills of the resident population.

3.1 A growing population

Oxford economics forecasts a population rise of 53,000 in Solent LEP by 2020 and a further 55,000 by 2030. The rate of growth in the period to 2030 is estimated to be 0.51% per annum, only marginally trailing the growth rate in the South East of 0.52%.

Figure 3.1: Solent population and working age population, 2000 to 2030



Source: Oxford Economics

By local authority, Southampton is forecast to experience the largest population growth in absolute terms, growing by 21,100 in the period to 2030[2]. Representing an average annual rate of growth of 0.49% this falls short of the fastest growing local area, Test Valley, which is expected to grow at 0.77% per annum. New Forest is forecast to have the slowest rate of growth at 0.10% per annum with a population rise of only 1,300 in the period 2013-2030.

Working age population is forecast to grow in the short-term, rising by 12,000 in the 4 years to 2017. Thereafter the working age population is expected to remain relatively stable before tailing off post 2026.

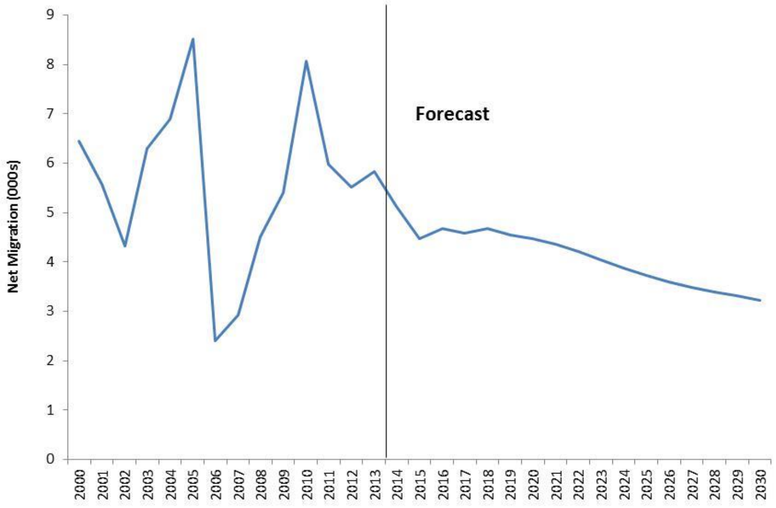
Migration is expected to be the key driver of population growth. We expect net inward migration to remain positive over the forecast period mirroring the general regional trend in the South East shown in figure 2.7. The appeal of Solent LEP to potential migrants is analogous with the South East, with its strong labour market and expected growth in future employment. The economic

[2] Oxford Economics produce their own forecasts of population which are economically driven and thus differ from the official population projections. Official births and deaths projections from 2012-based population projections are used but we have our own view on UK migration. At the local level, migration is linked to the employment rate forecast. If the employment rate within an area is falling too fast, migration reacts as the model assumes that people would not be attracted into this area to live, given that the employment prospects are weak. This approach ensures that the relationship between the labour market outlook and the demographic forecasts is sensible. This series is scaled to be consistent with the migration forecast for South East from the UK Regional Model. The total population forecast is then constructed using the forecast of migration and the natural increase assumptions. Natural increase for local areas is forecast based upon recent trends in both the historical data and the official projections.

attractiveness of Solent LEP is coupled with its scenic beauty and good transport links, make it an attractive area to live.

In the forecast period to 2020 the predicted average level of inward migration is 4,700 per annum. The arrival of 33,000 net migrants in this period accounts for 62% of the rise in population in Solent LEP in the decade ahead.

Figure 3.2: Solent net migration, 2000 to 2030

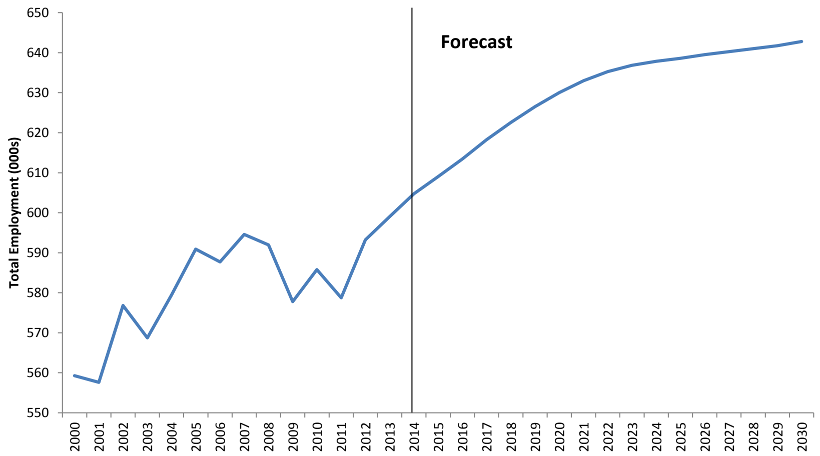


Source: Oxford Economics

3.2 Growth driven by the labour market

Baseline employment growth in Solent LEP is forecast to be robust in the years ahead. Over the period 2013-2020, Oxford Economics forecasts predict average employment growth under this “policy-off” outlook to be 0.72% per annum, with the addition of 31,000 jobs. Over the period 2020-23, employment growth is expected to slow to an average rate of 0.2% per annum with the creation of 12,800 jobs.

Figure 3.3: Solent employment, 2000 to 2030

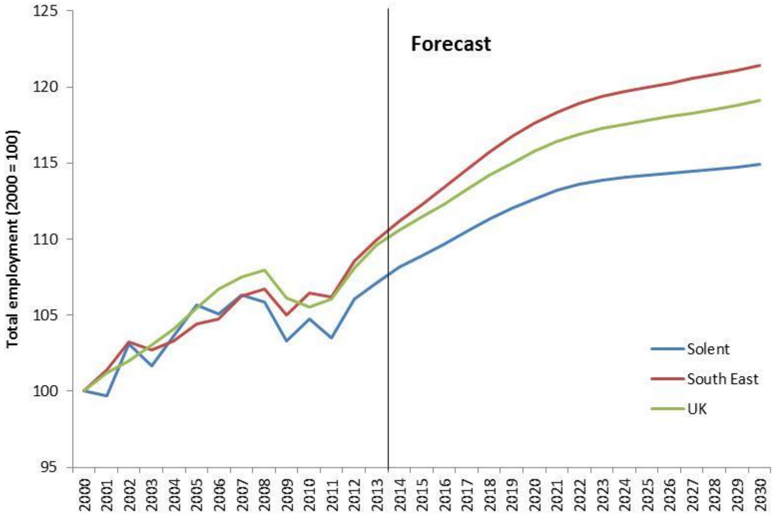


Source: Oxford Economics

Though strong employment growth is forecast in Solent LEP in the years ahead to 2020, the average growth rate of 0.72% per year still lags the South East which grows at 0.97%, though it does match that of the UK economy.

The relative performance of Solent LEP to the South East and UK is shown in Figure 3.4. Solent LEP has taken longer to recover from the recession, with the South East and the UK already having surpassed pre-crisis employment peaks in 2012 whilst Solent LEP is only estimated to have achieved this in 2013.

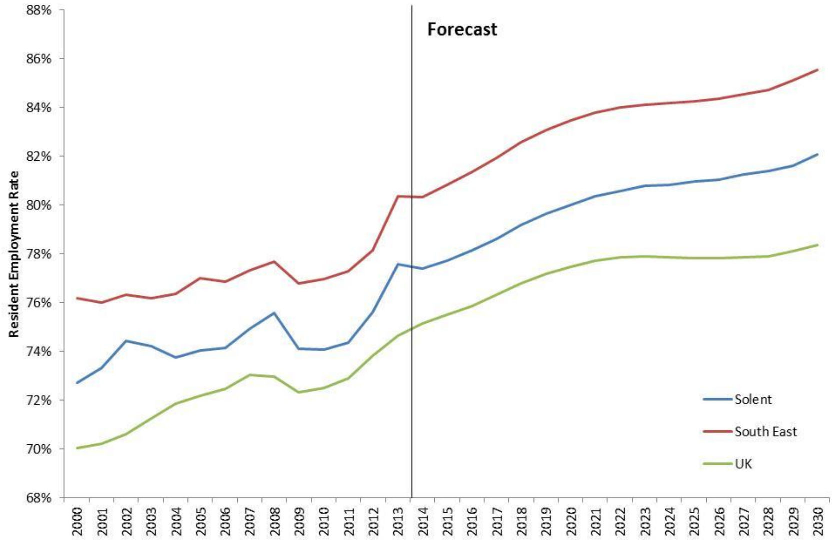
Figure 3.4: Employment growth in Solent LEP, South East and UK (2000 = 100)



Source: Oxford Economics

The global financial crisis and resulting downturn in the UK had a limited immediate impact on resident employment rates in Solent LEP. There has however been a steep increase in employment rates from 2011 to 2013 founded not just on stronger employment growth, but also a series of longer term structural shifts, which include greater female participation, the staged increase in the state retirement age for women, older workers delaying their retirement and pensioners returning to part-time work. These longer term shifts continue to push employment rates up over the forecast period.

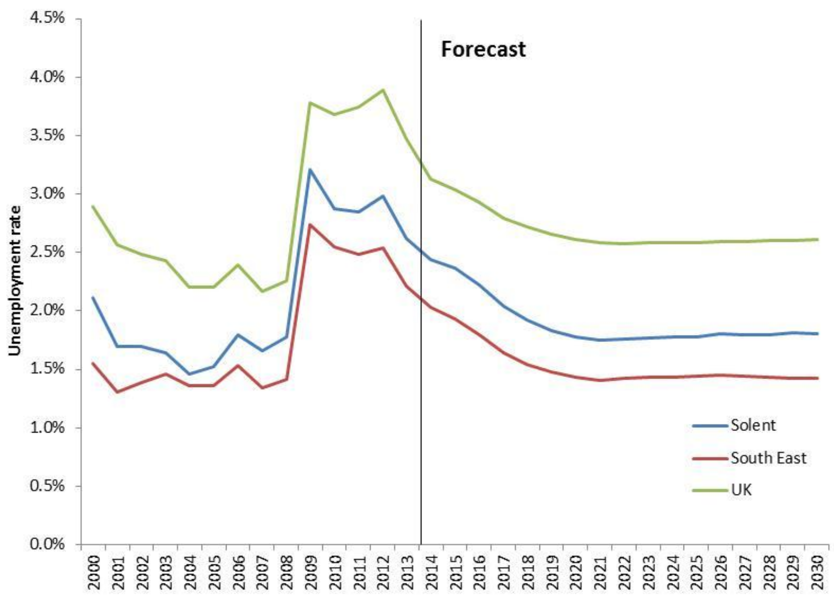
Figure 3.5: Resident Employment Rate for Solent LEP, South East and UK, 2000 to 2030



Source: Oxford Economics

Forecasts predict that claimant unemployment will fall in Solent LEP to 1.8% by 2020. The fall in the rate of unemployment of 0.8% matches the fall in claimant unemployment in the South East and is marginally behind the UK average of 0.9%. Post-2020 unemployment rates are forecast to remain flat across all 3 areas until the end of the forecast period.

Figure 3.6: Unemployment rates for Solent LEP, South East and UK, 2000 to 2030



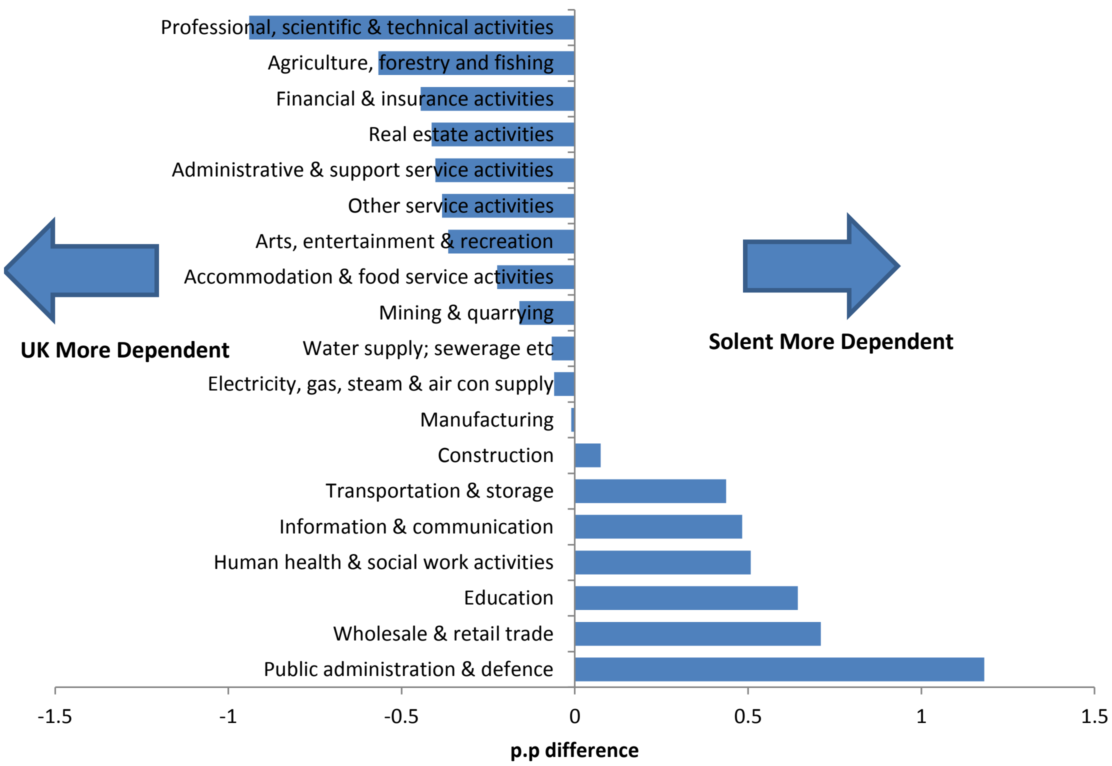
Source: Oxford Economics

3.3 High value added services to drive growth

When we compare the structure of the economy with the UK it is apparent that public services constitute a significantly larger proportion of employment in Solent LEP. Public services have a 2.3 pp higher relative concentration in Solent LEP – with Public admin 1.2pp, Education 0.6pp and Health & social 0.5pp higher.

As noted in the previous section the key growth sectors for the future are the professional, scientific & technical, admin & support and information & communication sectors. Though Solent LEP trails the average UK employment concentration in the professional, scientific & technical (0.9pp) and admin & support (0.4pp) sectors it has a higher concentration in the information & communication sector (0.5pp).

Figure 3.7: Relative Concentration Bar Chart Solent vs UK, 2013



Source: Oxford Economics

Under our baseline or business as usual outlook for Solent LEP, the strongest growth in the years to 2020 is forecast to be experienced in the admin & support and professional, scientific & technical sectors which are expected to grow by 7,500 and 6,800 jobs respectively. Looking into the decade 2020-30 the admin & support and professional, scientific & technical sectors still perform well but grow more slowly with the creation of 4,200 and 3,700 jobs respectively. The fact that the admin & support sector is forecast to create the greatest number of jobs is significant as the sector lost 3,100 jobs in the five years from 2008-2013.

Table 3.1: Baseline employment growth in each sector (i.e. policy off outlook), 2000-08, 2008-13, and 2013-20 and 2020-23

	2000-08 (000s)	2008-13 (000s)	2013-20 (000s)	2020-30 (000s)
Agriculture, forestry and fishing	-0.6	-0.2	-0.4	-0.4
Mining and quarrying	0.1	0.1	0.0	-0.1
Manufacturing	-19.0	-4.7	-2.9	-6.9
Electricity, gas, steam and air conditioning supply	-0.7	0.0	-0.2	-0.2
Water supply; sewerage, waste management and remediation activities	0.7	-0.3	-0.1	-0.1
Construction	0.6	-3.7	4.7	3.8
Wholesale and retail trade; repair of motor vehicles and motorcycles	0.3	-3.3	4.8	-0.1
Transportation and storage	7.8	2.8	2.5	-1.1
Accommodation and food service activities	1.2	0.9	3.8	0.6
Information and communication	7.7	6.9	4.3	3.0
Financial and insurance activities	-2.6	0.0	0.2	0.1
Real estate activities	2.7	0.8	1.5	1.2
Professional, scientific and technical activities	8.7	6.2	6.8	3.7
Administrative and support service activities	8.3	-3.1	7.5	4.2
Public administration and defence; compulsory social security	-5.6	-5.4	-3.9	-0.3
Education	2.3	4.6	-1.4	0.5
Human health and social work activities	16.2	9.6	-0.5	2.9
Arts, entertainment and recreation	1.6	-2.1	2.5	1.5
Other service activities	2.9	-2.2	1.7	0.5

Source: Oxford Economics

Further sectors to experience a marked turnaround since 2008-2013 are the construction and wholesale & retail sector. Construction is forecast to experience a reversal, from job shedding of 3,700 in 2008-2013 to growth of 4,700 additional jobs in the decade ahead. Likewise, a fall of employment in the wholesale & retail sector of 3,300 over the last five years is forecast to be reversed by the creation of 4,800 jobs by 2020. Though after 2020 growth in wholesale & retail is forecast to ebb with a minor contraction in the decade to 2030.

Continuing the same trend as that experienced over the last two decades, manufacturing will continue to decline. It is expected to lose 2,900 jobs by 2020 and another 6,900 jobs by 2030. In the period to 2030, manufacturing is expected to contract by 20.6% with the shedding of 9,900 jobs. The contraction of employment is set to continue into the future as the industry shifts from a higher labour to a more capital intensive, productive form of manufacture. There is certainly still a role for manufacturing in the Solent LEP, but it will compete on quality of output rather than cost and it will require highly skilled individuals. By 2030 manufacturing will account for only 5.9% of total employment in the Solent LEP, less than half the contribution it constituted in 2000 (12.8%).

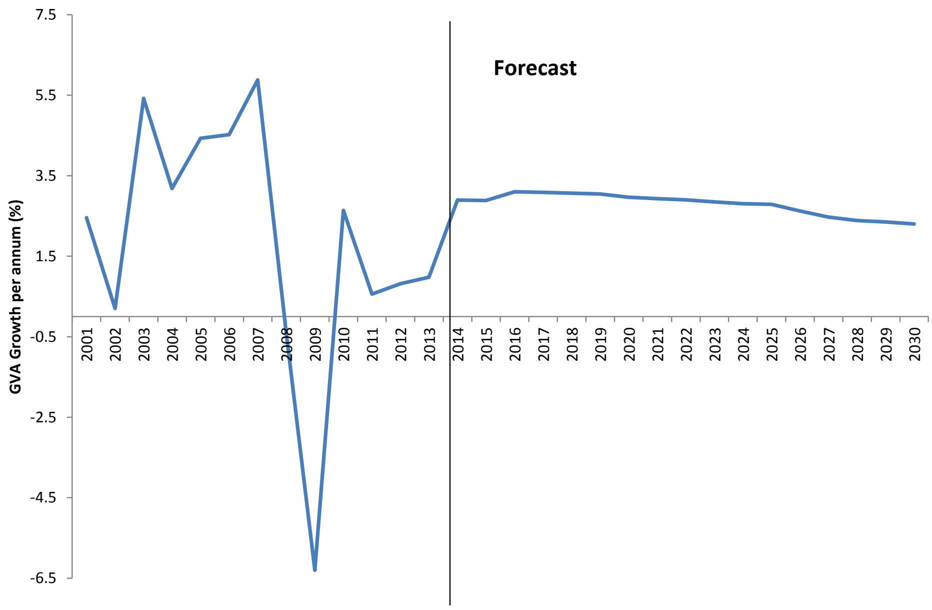
The public sector, chiefly public admin, is forecast to suffer heavy job losses in the years leading up to 2020 as government cuts to expenditure hit jobs. Across the public sector 5,800 jobs are expected to be lost – a loss of 3,900 jobs (10.9%) in public admin, 1,400 (2.5%) in Education and 500 (0.6%) in health & social care.

3.4 Sustained GVA growth

After two successive years of GVA decline in 2008 and 2009, Solent LEP has posted positive GVA growth. GVA growth is forecast to rise from its estimate of 1.0% in 2013 to 3.0% in 2030. However, this rate of annual growth is predominantly experienced in the short-run with GVA growth in 2016 forecast to be 3.1%. Thereafter, it is expected to grow but at a diminishing rate until 2020, with this trend continuing towards 2030.

GVA growth in Solent LEP is forecast to grow at an average rate of 2.8% per annum in the period to 2030. This rate of growth means Solent LEP lags the average annual UK GVA growth rate of 2.9% per annum and 3.0% per annum for the South East.

Figure 3.8: Solent GVA Growth (2000-30)



Source: Oxford Economics

The fastest growing local authority in Solent LEP was Winchester, which experienced an annual average GVA growth rate of 3.4%. Test Valley is the second fastest growing local authority with an annual GVA growth rate of 3.2% - along with Winchester they are the only areas that surpass the growth rate of the South East. The slowest growing local area is New Forest with an average GVA growth rate of 2.4 per annum.

Table 3.2: GVA Growth, 2013-2023

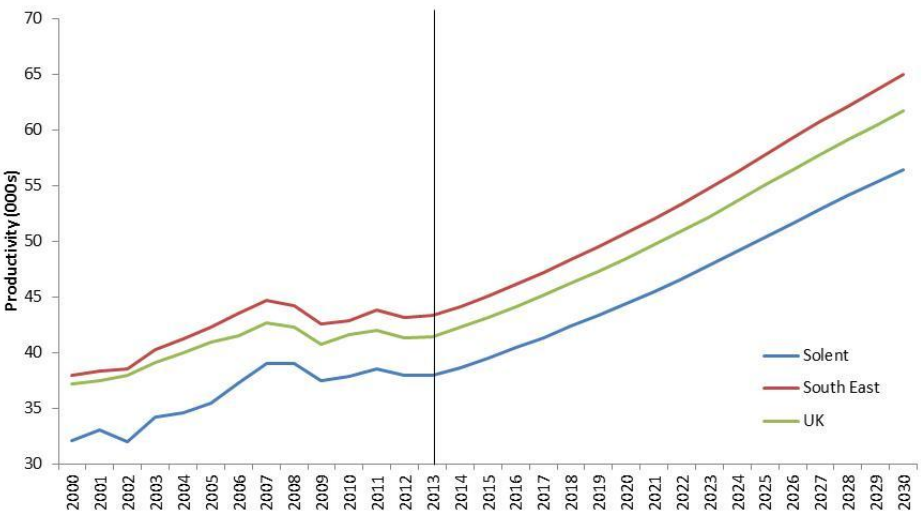
	GVA Change 2013-2030 (% per annum)
Eastleigh	3.0%
Fareham	2.8%
Gosport	2.5%
Havant	2.7%
Isle of Wight	2.6%
Portsmouth	2.6%
Southampton	2.8%
East Hampshire	3.0%
New Forest	2.4%
Test Valley	3.2%
Winchester	3.4%
Solent LEP	**2.8%**

Source: Oxford Economics

3.5 Productivity Gap

Average productivity in Solent in 2013 was nearly £38,000. Under our baseline forecasts we expect it to rise by just over £6,450 by 2020 (i.e. to £44,400). The average level of productivity in the Solent LEP is expected to grow by 17% in the years 2013-2020 and by another 27% by 2030, equating to an average growth rate of 2.4% per annum.

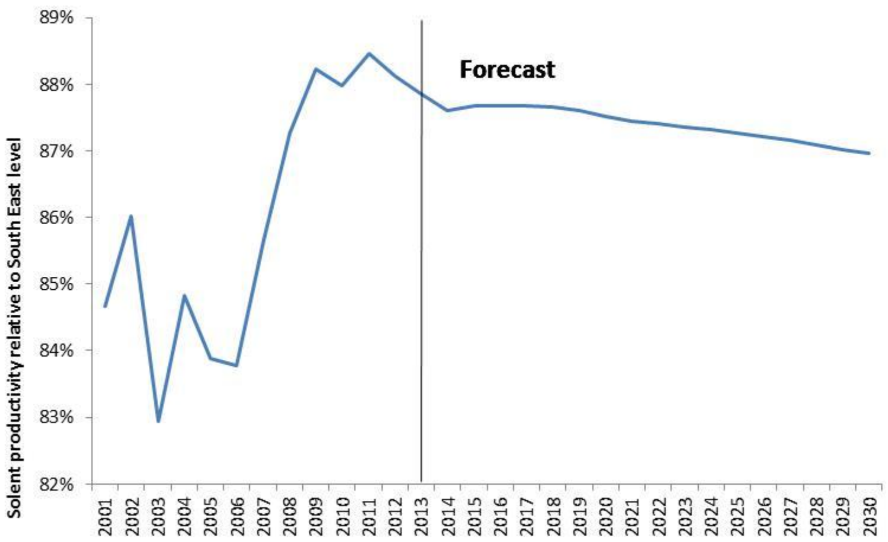
Figure 3.9: Solent productivity (2000-30)



Source: Oxford Economics

Though Solent LEP experiences strong growth in productivity, this is mirrored by the South East which also grows at an average annual rate of 2.4%. The equitable growth rate in each area results in a very marginal widening of the productivity Gap between Solent LEP and the South East.

Figure 3.10: Productivity Gap, Solent vs South East (2000-30)

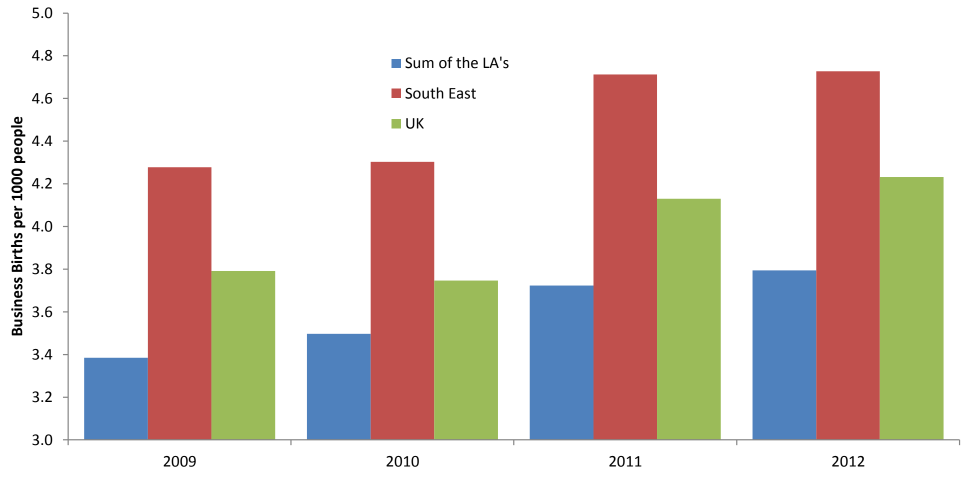


Source: Oxford Economics

3.6 Business data

Business births have grown in Solent local authorities from 3.4 per 1,000 people in 2009 to 3.8 in 2012, rising by 12% over the four years (note the business birth data used in this section includes the whole local authorities of East Hampshire, New Forest, Test Valley and Winchester, rather than just the parts that fall within the Solent LEP boundary). The average for the Solent local authorities falls significantly short of the number of business births across the UK and the South East. In the UK business births stood at 3.8 per 1,000 people in 2009, increasing to 4.2 by 2012. The South East is more entrepreneurial still, having 4.3 business births per 1,000 of the population in 2009 rising to 4.7 in 2012.

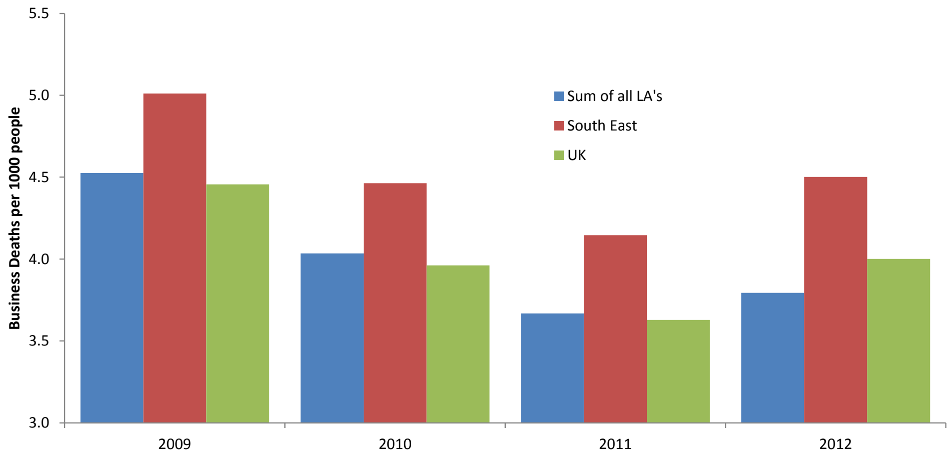
Figure 3.11: Business Births (per 1000 people), Solent's whole local authorities, South East & the UK (2009-12)



Source: ONS business demography 2012 and APS

Business deaths decreased across all three regions from 2009 to 2011 but rose in the year to 2012. From 2009 to 2012 Business deaths fell from 4.5 to 3.8 per 1,000 of the population in Solent's whole local authorities, in the South East business deaths fall from 5.0 to 4.5 and in the UK they fall from 4.5 to 4.0.

Figure 3.12: Business Deaths (per 1000 people), Solent's whole local authorities, South East & the UK (2009-12)



Source: ONS Business Demography 2012 and APS

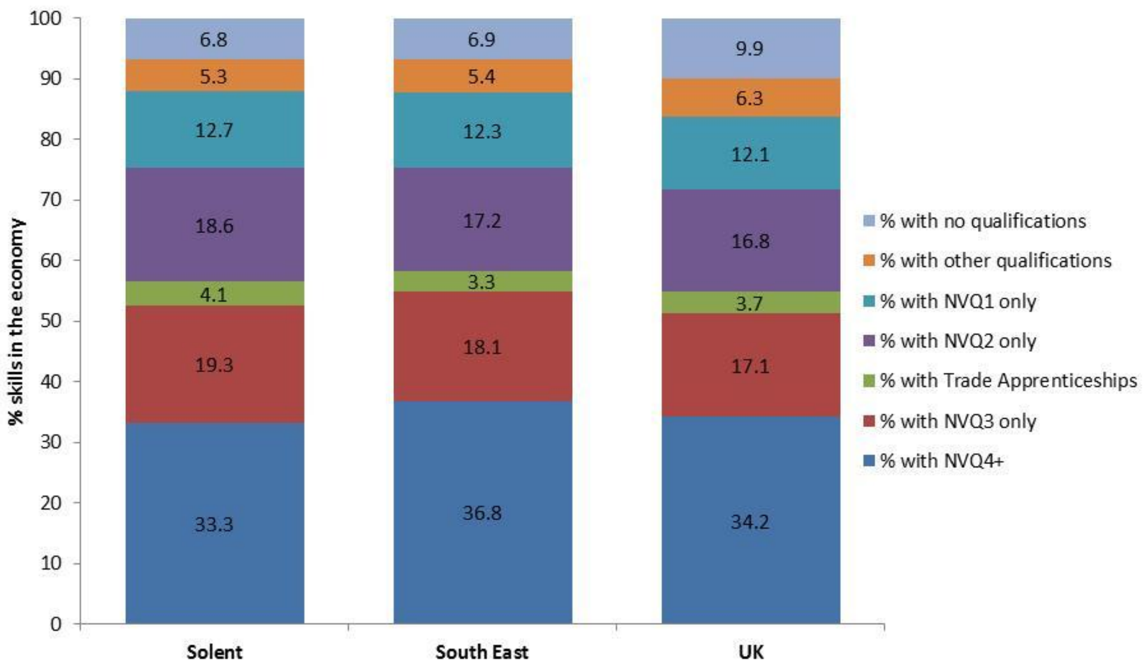
3.7 Skills supply

The analysis of sectoral growth earlier showed that the economy will continue to become increasingly skills hungry. However the working age population was not expected to continue growing. Consequently it is important that new entrants to the working age population are highly skilled to fuel demand from local businesses. It is also important that residents with no or low levels of qualifications are encouraged to upskill. In addition the decline in traditional activities in favour of new exportable service sectors means there is likely to be a requirement for retraining.

The most common skill level in Solent's whole local authorities (again the skills data refers to whole local authorities despite the Solent LEP boundary cutting through four of them) is the highest skill qualification NVQ 4+, which constitutes 33.3% of the working age population. This is notably below the South East average of 36.8% and the UK average of 34.2%. By contrast the Solent LEP has a larger share of the working age population skilled to NVQ level 2 and level 3.

It is likely that the productivity gap with the region is due in large part to this skills profile. A detailed analysis is however outside the scope of this study as it requires an analysis of not only what the relative economies do, but how they do it (the approaches uses techniques like shift share analysis).

Figure 3.13: Skills Composition of the Economy for Solent's whole local authorities, South East and UK for 2012



Source: APS

3.8 Summary

The forecasts for Solent LEP are on the whole positive. Average employment growth of 0.72% per annum is expected to create an addition of 31,000 jobs by 2020. Over the period 2013 to 2030 this rises to 44,000 – growing at an average rate of 0.42% per annum. GVA in Solent LEP will follow suit, with positive year-on-year growth expected throughout the forecast period. GVA is forecast to rise at an annual average rate of 2.8% to 2030.

The strong growth in employment over the forecast period coupled with flat growth in the working age population will squeeze the labour market in the years ahead. The labour market tightening should push down unemployment rates from current levels, though additional demand for labour in Solent LEP will increasingly have to be satisfied by the inflow of migrants or a rise in the level of commuters into the area.

Employment growth in the outlook period is concentrated in the skilled services sectors (admin & support and professional, scientific & technical sectors) whilst manufacturing continues its decline. Consequently the Solent LEP economy (like the rest of the UK) will demand a more highly skilled workforce as this trend continues.

At present the skills structure of Solent LEP lags behind the South East, with a significantly lower proportion of workers with NVQ4+ qualifications. A lower skilled workforce is a major contributor to the productivity gap that exists between Solent LEP and the South East. The skills gap with the South East must be addressed if the productivity gap is to be narrowed.

4 Preferred growth scenario

This section provides a discussion of the preferred growth scenario for the Solent LEP.

Key points:

- The preferred growth scenario includes a mix of labour market and wealth targets;
- Labour market targets are achievable given our modelling assumptions;
- Wealth creation targets are much more difficult to achieve and will require a general skills / productivity uplift across the current workforce;
- The labour market is already tight and the creation of 15,500 jobs quickly exhausts the available pool of unemployed;
- Demand for labour is filled by new migrants to the economy which in turn pushes up population numbers.

4.1 Growth targets

The Preferred Growth Scenario had a number of headline targets for the economy by 2020:

- An additional 15,500 jobs above base by 2020;
- GVA growth to rise to 3.5% pa
- An increase in productivity of £6,500 (including baseline growth);
- Increase employment rate from 78% to 80%;
- Increase economic activity rate from 80% to 81%;
- Raise the business birth rate from 3.6% to 4.1%;
- Raise the share of the working age population with NVQ 4+ skills from 33% to 36% by 2020; and
- Improve business survival rates.

Changes to direct employment and productivity, and the associated indirect and induced impacts are estimated in the modelling. The effects on migration, activity rates, unemployment, wealth etc. are all estimated.

Changes to birth and survival rates are not explicitly modelled as they do not affect the labour market or wealth targets set out above. In addition the modelling does not currently cover changes to the skills profile of the current labour supply in the Solent LEP.

4.2 How do we model the scenario?

The economic model is primarily a labour market model. The first step is to input the additional direct jobs we want in the Solent LEP. Note this is not 15,500. The direct jobs will create indirect and induced impacts and therefore the direct jobs figure needs to be below the overall target.

These direct jobs are allocated across each Local Authority using their current and future shares of sectoral employment in the LEP. Using local sectoral productivity (which we can adjust to take account of improved skills) and national GVA to output ratios, the model estimates the likely output and GVA from these direct jobs.

It then calculates the indirect and induced impacts (output, GVA and employment) for each local authority. The model then estimates who is likely to take the jobs, i.e. unemployed, commuters or migrants:

- 2001 Census commuting patterns are used (these can be updated when new ones are available) to work out commuting effects; and
- the impacts on the unemployed and migration are estimated together as the formula stops unemployment rates falling to unfeasibly low levels and resident employment rates rising to unfeasibly high levels by bringing in migrant workers.

Additional migrants will obviously push up population and working age population levels. We assume that some migrants will bring their families and therefore the impact on population and working age population are larger than the number of jobs taken by migrants.

4.3 Key assumptions

The model includes 85 sectors of the economy. We have assumed growth in employment in a selection of sectors, based on the previous growth strategy's focus of marine & maritime, advanced manufacturing, visitor economy and transport and logistics. A discussion with Solent LEP also highlighted the need to expand our coverage to exportable private services and construction.

At a high level we took:

- A selection of manufacturing sub-sectors, focusing on high value added activity;
- Construction related sectors;
- Transport and communication related sub-sectors;
- Accommodation, food, creative and sport sub-sectors to reflect tourism related activity; and
- A selection of high value added exportable private services (e.g. finance, engineering, R&D, etc).

We assume that by 2020 they gradually grow by an additional:

- 3.5% for construction sub-sectors;
- 5% for manufacturing sub-sectors;
- 7.5% for transport and communications, and tourism related sub-sectors; and
- 10% for exportable private services.

We typically allocate direct jobs across Solent local authorities based on their current share of the LEP's sectoral jobs. So for example if a local authority had 10% of the LEP's finance jobs and the growth scenario created 1,000 new direct finance jobs, then the same local authority would be allocated 100 of these new jobs. This systems allows us to capture:

- the location choices of sectors and agglomerations; and
- while also ensuring that where a local economy does not have jobs in a given sub-sector, it is not allocated these types of jobs.

Discussions with Solent LEP revealed on going efforts through the City Deal to secure more jobs in the two cities of Portsmouth and Southampton. Consequently we have added a system to allocate more jobs to the two cities.

We have assumed Portsmouth and Southampton have an additional 25 percentage point increase in employment across all sectors of the economy (excluding agri and fishing). Once the model scales out sectoral employment shares, the 25 percentage point boost to the two cities fall. The system essentially provides a small improvement in overall resident employment rates in the two cities (discussed in more detail below).

In much of a similar way to the original work undertaken for PUSH we have assumed the growth scenario is accompanied with improvements in productivity of new jobs. We have assumed that a skills strategy results in a 20% increase in productivity levels of new jobs by 2020. This increase is phased in from 2014 to 2020. The productivity uplift is concentrated in tradable activity and therefore excludes agri, retail, personal services, accommodation, etc.

4.4 Headline results

Table 4.1 sets out our headline results. At a high level the Preferred Growth Scenario is successful in achieving the labour market related targets. By 2020 the economy has just over 15,500 jobs, growing at annual average rate of 1.07% (up from the 0.72% in the baseline forecasts). This pushes up the economic activity rate from 81.8% to 82.8% in 2020 and increases the resident employment rate from 80% in the baseline to 81.4%.

Table 4.1: headline indicators in 2020, baseline versus scenario

Key Indicators	Baseline	Scenario
Additional employment	N/A	15.53
Employment (pa)	0.72%	1.07%
Productivity (pa)	2.27%	2.28%
GVA % growth (pa)	3.01%	3.38%
Growth in productivity	N/A	£51
Productivity relative to South East	87.5%	87.6%
Economic Activity rate (%)	81.8%	82.8%
Resident employment rate (%)	80.0%	81.4%

Note, we forecast productivity to rise by £6,450 under the policy off or baseline outlook.

Consequently the preferred growth scenario would result in a productivity increase of £6,500 over the period 2013 to 2020.

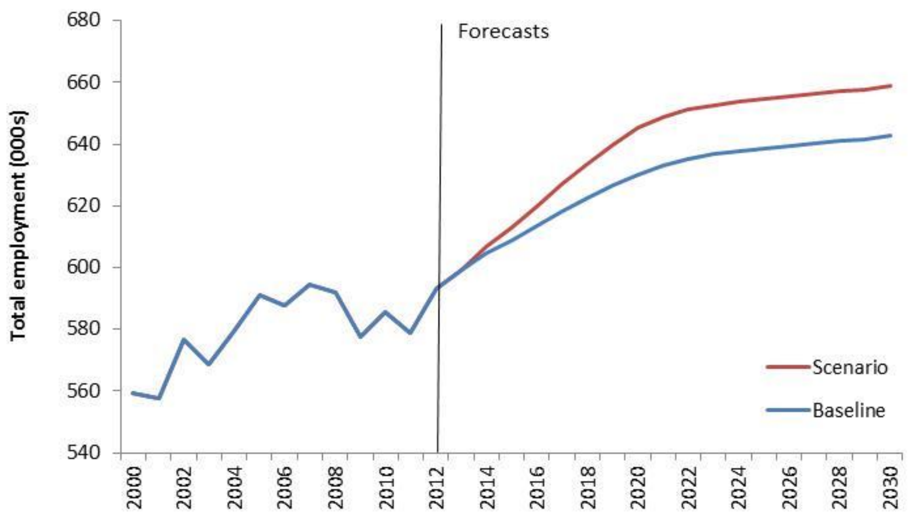
Source: Oxford Economics

Although the productivity target is achieved by 2020, the aspirations for 3.5% GVA growth are more difficult to achieve.

4.5 Tight labour market conditions attract migrants

From 2014 to 2020 we forecast the Solent LEP would create 25,300 jobs under the baseline outlook. Under the preferred growth scenario our selected sectors experience faster growth from 2014. By 2020 the employment levels are some 15,500 above the baseline position (or an additional 2.5% above our baseline level). Consequently from 2013 to 2020 we estimate a net increase of 46,500 jobs in the preferred growth scenario.

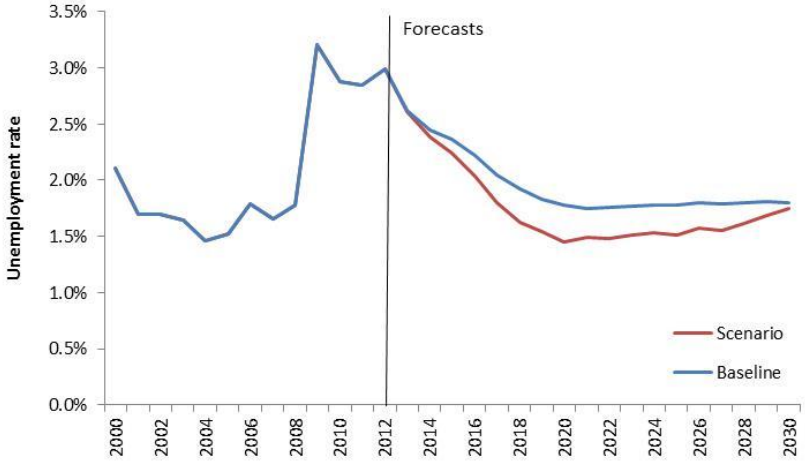
Figure 4.1: baseline and scenario employment levels in Solent



Source: Oxford Economics

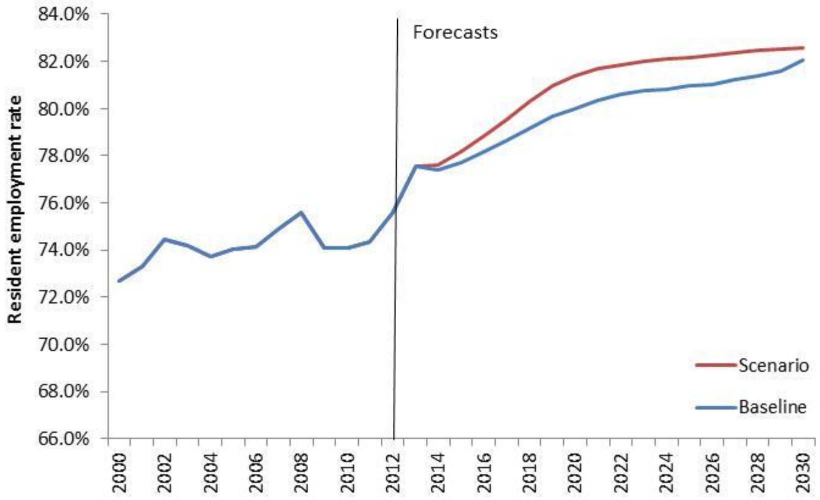
To fill these jobs an additional 2,300 residents are taken off the ranks of the unemployed. Unemployment rates fall from 2.4% in 2013 to 1.5% by 2020 (below the baseline rate of 1.8% in 2020). At the same time the resident employment rate is pushed up to 81.4% by 2020 (some 1.4 pp higher than the baseline estimate). Consequently the preferred growth scenario achieves the jobs, resident employment rate and economic activity rate targets.

Figure 4.2: baseline and scenario unemployment rates in Solent



Source: Oxford Economics

Figure 4.3: baseline and scenario resident employment rates in Solent



Source: Oxford Economics

These tight labour market conditions in Solent's local economies mean that additional migrants are attracted in. In such a market businesses will compete with one another for scarce labour bidding up wage rates and making the economy increasingly more attractive to migrants.

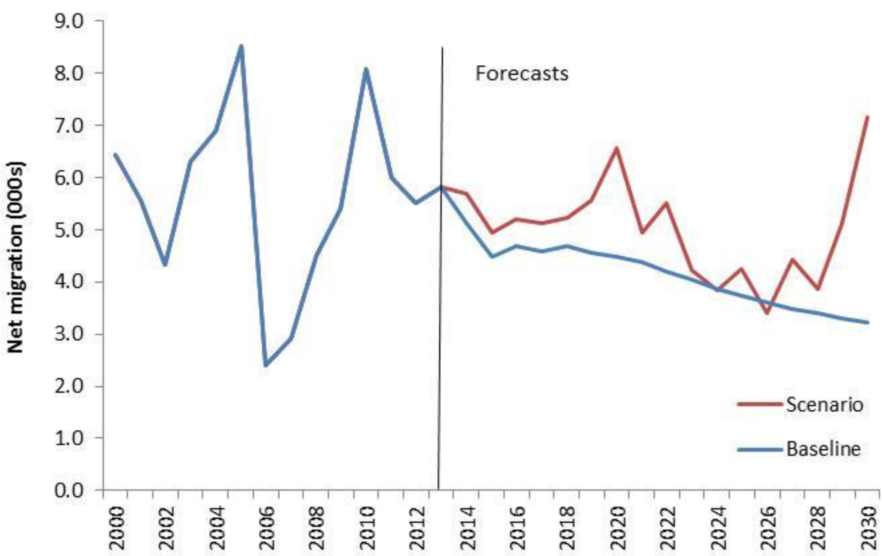
Figure 4.4 plots both our baseline and preferred growth scenario estimates of net migration for Solent LEP. From 2013 to 2020 we estimate an additional 5,200 migrants are attracted in to the Solent LEP economy.

The volatile nature of the scenario forecasts reflects the scenario model's system for capping resident employment rates. The system operates at local authority level and as resident employment rates rise towards a pre-determined maximum, the model assumes local business can't find the required labour locally. Consequently we bring in more and more migrants to keep resident employment rates at sensible levels.

Linked to this the model has an unemployment rate system to ensure it does not fall below historic minimums. Once a local economy reaches this rate of unemployed, the model will again look to bring in migrants to take job opportunities.

Migrants then become residents in the next year and in effect push up population numbers and push down resident employment rates (assuming all other things equal).

Figure 4.4: Solent LEP migration forecasts

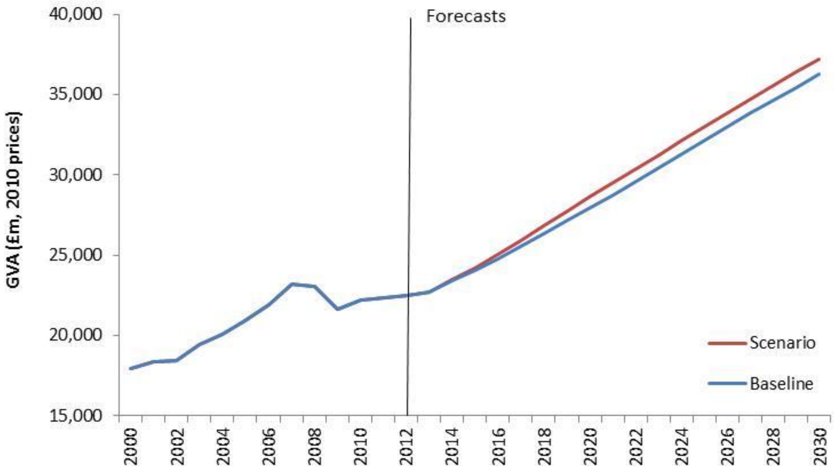


Source: Oxford Economics

4.6 Higher levels of GVA but productivity relatively unchanged

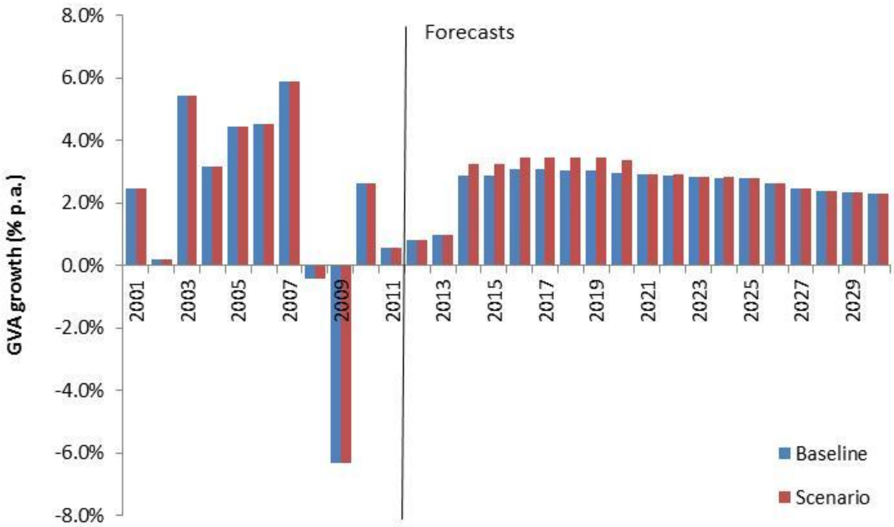
Intuitively, additional jobs in the economy generate additional GVA (Figure 4.5). By 2020 GVA has increased by £722m (in 2010 prices). Annual average GVA growth over the period increases from 3% to nearly 3.4% just short of our target rate (figure 4.6).

Figure 4.5: Baseline and scenario GVA levels (£m 2010 prices)



Source: Oxford Economics

Figure 4.6: Baseline and scenario GVA growth (% pa)

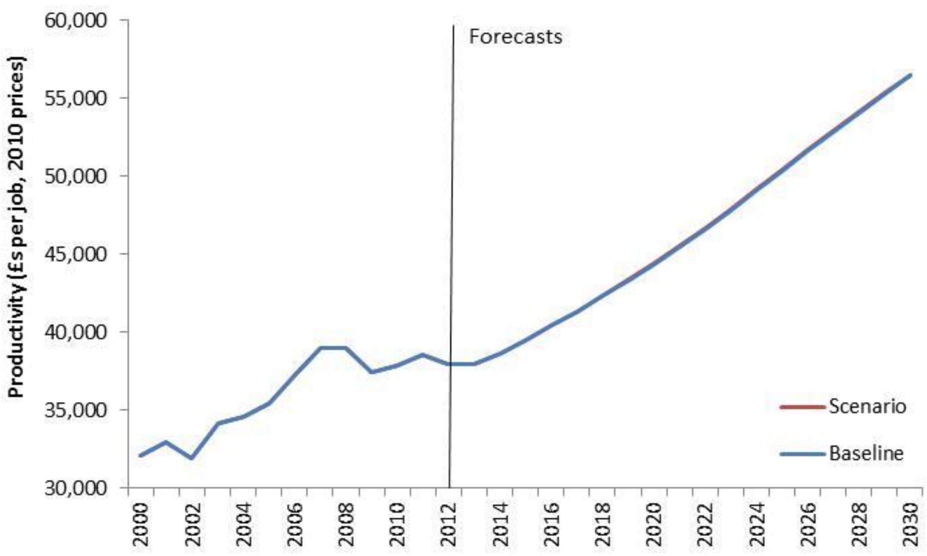


Source: Oxford Economics

As noted earlier we expect productivity to increase by £6,450 over the period 2013 to 2020 under the policy off outlook. Under the preferred growth scenario productivity increases by a further £50 meaning the productivity gap with the South East improves by a relatively insignificant 0.1 pp.

We have not modelled the skills improvement target of the preferred growth scenario. A general uplift of skills in the economy is likely to be much more successful in raising productivity levels given the strong positive relationships between skill levels and productivity / wage levels. Though we should note that the literature suggests notable improvements in skill levels, and hence productivity, take considerable periods of time to be achieved. Consequently dramatic improvements in skills and productivity are unlikely to be achieved before 2020.

Figure 4.7: Baseline and scenario productivity



Source: Oxford Economics

4.7 Implications

The preferred growth scenario achieves the labour market targets. The 15,500 additional jobs pushes up resident employment rates and activity rates. However the labour market is already tight and the creation of 15,500 jobs quickly exhausts the available pool of unemployed.

As business compete with each other and bid up wage rates, the economy becomes increasingly attractive for migrants. Demand for labour is therefore increasingly filled by new migrants to the economy which in turn pushes up population numbers.

Wealth creation targets are much more difficult to achieve. Annual average GVA growth quickens from 3% to 3.4% given the additional jobs being created and productivity rises by an additional £50 to achieve the £6,500 growth target.

5 Summary

5.1 Macroeconomic environment

The outlook for growth is cautiously optimistic given the challenges present, not least the level of government debt across many of the world's most developed countries. We do however expect the two speed growth of developing and developed economies to continue.

Our forecast for UK GVA growth of 2.4% in 2014 would represent the strongest outturn for seven years. Although the worst of the Eurozone crisis appears to have passed, any further escalation would risk tipping the UK back into recession due to the strong trade links and the potential for spillovers into the UK banking system. Encouragingly though, business investment and consumer spending levels have begun to increase, having remained low for the last 5 years as a result of economic uncertainty.

UK employment is forecast to be about 7% higher in 2023 than today, equivalent to an extra 2.3 million jobs. For sustainable, balanced economic growth, the UK must undergo an export and investment led recovery. This is why we expect growth to be led by exportable service sector activity.

5.2 South East to remain a key driver of UK growth

The South East has been one of the UK's top performing regions, and we expect the it to continue recording above average jobs growth over the forecast period with average annual employment growth of 0.83% compared to 0.68% for the UK average. Faster jobs and GVA growth reflect the structure of the South East economy which is geared more to growth sectors than those that have been shedding jobs or those reliant on restricted public spending.

Despite the recent financial crisis and resulting recession, the labour market in the South East remains fairly tight. Resident employment rates in 2013 were 80.3% while the claimant unemployment rate was 1.8% in December 2013. Our baseline forecasts suggest spare labour will be reduced further with job creation.

The South East has traditionally been an attractive place for migrants and our labour market outlook suggests this trend will continue, albeit at slightly lower levels over the forecast period.

5.3 Solent economy expected to enjoy strong growth

The forecasts for Solent LEP are on the whole positive. Average employment growth of 0.72% per annum is expected to create an addition of 31,000 jobs by 2020. Over the period 2013 to 2030 this rises to 44,000 – growing at an average rate of 0.42% per annum. GVA in Solent LEP will follow suit, with positive year-on-year growth expected throughout the forecast period. GVA is forecast to rise at an annual average rate of 2.8% to 2030.

Employment growth in the outlook period is concentrated in the skilled services sectors (admin & support and professional, scientific & technical sectors) whilst manufacturing continues its decline. Consequently the Solent LEP economy (like the rest of the UK) will demand a more highly skilled workforce as this trend continues.

At present the skills structure of Solent LEP lags behind the South East, with a lower proportion of workers with NVQ4+ qualifications. A lower skilled workforce is a major contributor to the productivity gap that exists between Solent LEP and the South East. The skills gap with the South East must be addressed if the productivity gap is to be narrowed.

5.4 Though labour market will have little spare capacity

The strong growth in employment over the forecast period coupled with flat growth in the working age population will squeeze the labour market in the years ahead. The labour market tightening should push down unemployment rates from current levels, though additional demand for labour in Solent LEP will increasingly have to be satisfied by the inflow of migrants or a rise in the level of commuters into the area.

5.5 Preferred growth strategy offers labour market benefits

The Preferred Growth Scenario has a number of headline targets for the economy by 2020:

- An additional 15,500 jobs above base by 2020;
- GVA growth to rise to 3.5% pa
- An increase in productivity of £6,500 (including baseline growth);
- Increase employment rate from 78% to 80%;
- Increase economic activity rate from 80% to 81%;
- Raise the business birth rate from 3.6% to 4.1%;
- Raise the share of the working age population with NVQ 4+ skills from 33% to 36% by 2020; and
- Improve business survival rates.

Through the accompanying impact model to this report we are able to model the majority of the growth scenario. We exclude the skills target and business survival rate target. We find that the preferred growth scenario achieves the labour market targets. The 15,500 additional jobs pushes up resident employment rates and activity rates. However the labour market is already tight and the creation of 15,500 jobs quickly exhausts the available pool of unemployed.

Table 4.1: headline indicators in 2020, baseline versus scenario

Key Indicators	Baseline	Scenario
Additional employment	N/A	15.53
Employment (pa)	0.72%	1.07%
Productivity (pa)	2.27%	2.28%
GVA % growth (pa)	3.01%	3.38%
Growth in productivity	N/A	£51
Productivity relative to South East	87.5%	87.6%
Economic Activity rate (%)	81.8%	82.8%
Resident employment rate (%)	80.0%	81.4%

Source: Oxford Economics

Note, we forecast productivity to rise by £6,450 under the policy off or baseline outlook.

Consequently the preferred growth scenario would result in a productivity increase of £6,500 over the period 2013 to 2020.

As business compete with each other and bid up wage rates, the economy becomes increasingly attractive for migrants. Demand for labour is therefore increasingly filled by new migrants to the economy which in turn pushes up population numbers.

5.6 GVA growth target more difficult to achieve

Annual average GVA growth quickens from 3% to 3.4% given the additional jobs being created. Under the policy off scenario we forecast productivity to increase by £6,450 over the period 2013 to 2020. Under the preferred growth scenario productivity increases by a further £50 meaning the productivity gap with the South East improves by a relatively insignificant 0.1 pp.

A general uplift of skills in the economy is likely to be much more successful in raising productivity levels given the strong positive relationships between skill levels and productivity / wage levels. Though we should note that the literature suggests notable improvements in skill levels, and hence productivity, take considerable periods of time to be achieved. Consequently dramatic improvements in skills and productivity are unlikely to be achieved before 2020.

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