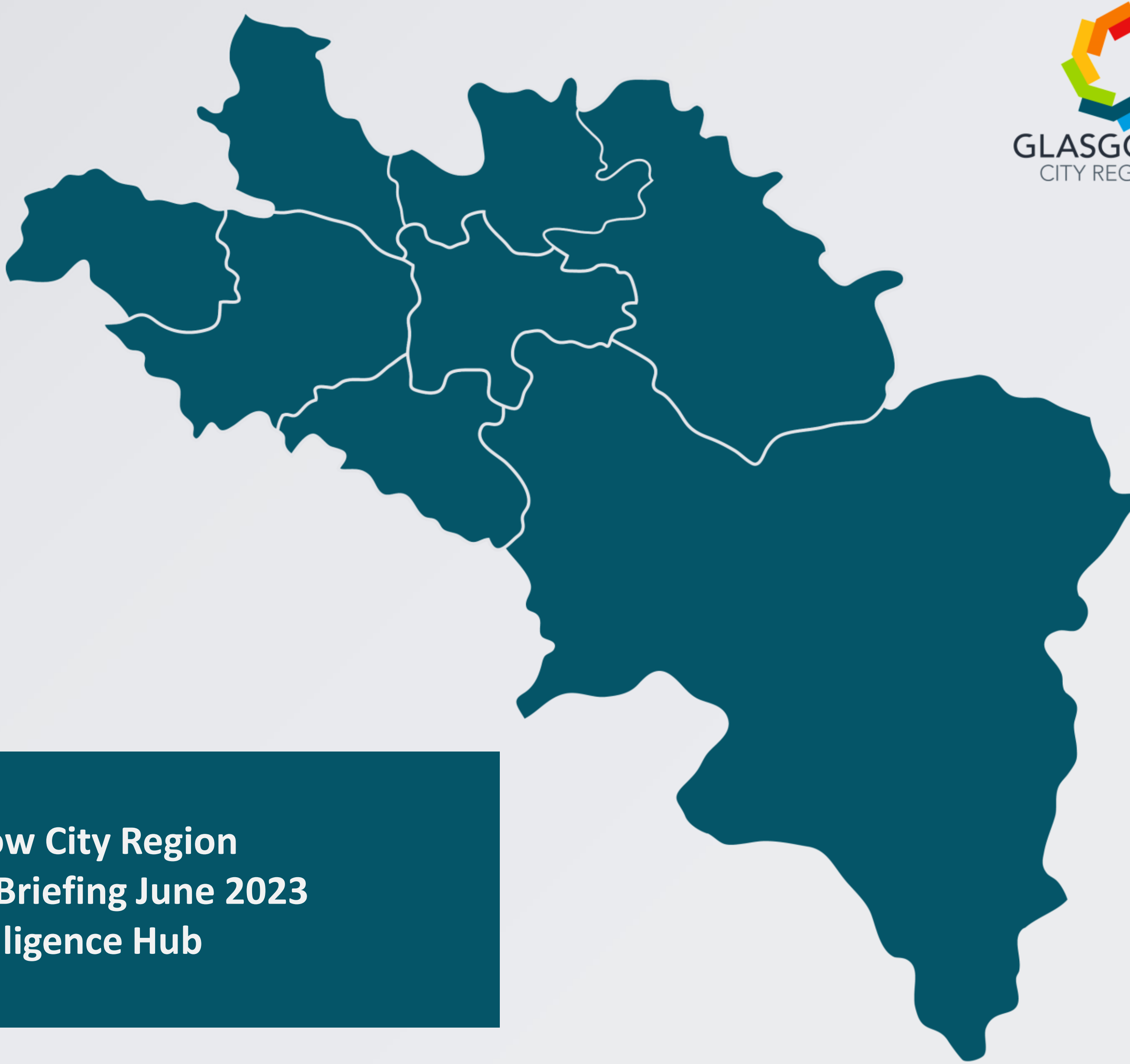


GLASGOW
CITY REGION

Glasgow City Region
Economic Briefing June 2023
Intelligence Hub

Summary

- The UK is experiencing persistent inflation, with a rate of 8.7% in May. Factors setting the UK apart from other advanced economies include a struggling job market and higher food imports.
- In an effort to tackle inflation, the Bank of England has increased the Base Rate to 5%, which has adversely affected mortgage holders, private renters and businesses.
- Research conducted by the Institute for Public Policy Research highlights the need for increased investment in both the private and public sectors to improve the country's growth and earnings prospects.
- The latest labour market statistics for Scotland indicate a decline in employment and a further rise in economic inactivity.

This month's spotlight is on innovation and measurement of economic wellbeing.

- **GCR Innovation Clusters:** New analysis from the Intelligence Hub using a variety of datasets identifies strengths in 36 emerging economy sectors. In terms of business concentration, GCR surpasses the UK Core City Regions in prominent sectors such as CleanTech, Net Zero, BioTech, and Internet of Things.
- **Innovation Assets:** Research emphasizes the importance of effective governance in innovation districts, enabling collaboration and maximizing their potential. Key factors for successful governance include co-design and co-investment, ensuring financial sustainability, and maintaining adaptability over time.
- **Beyond GDP:** The ONS has introduced a new measure of Inclusive Growth, which encompasses a broader range of economic activities and assets than gross domestic product (GDP) does, such as unpaid household services, ecosystem services and more.

Note: a Glossary of all the terms used in this report can be found at the end

The Outlook for the UK Economy

Despite managing to avoid a recession, the UK's economic prospects continue to pose challenges due to ongoing issues such as persistent inflation, unemployment, elevated interest rates, and a less-than-optimistic growth outlook.

Persistent inflation

- The rate of UK inflation was unchanged at 8.7% in May. According to OECD forecasts, the UK will have one of the highest inflation rates among G20 in 2023.
- What is setting the UK apart from other countries is mainly the jobs market which is struggling to recover from Covid-19, Brexit rules and economic inactivity due to ill-health. The UK also imports more than 50% of its food, which has been affected by rising raw material costs.

Weak Growth Outlook

- According to a recent report by the Institute for Public Policy Research (IPPR), there is a significant underinvestment of over £500 billion when compared to other advanced economies. The report highlights that both business and public investment in the UK are the lowest among the G7 countries. The IPPR cautions that the reluctance to invest will perpetuate a subdued growth outlook for the UK.

GDP

- Monthly GDP is estimated to have grown by 0.2% in April 2023, after a fall of 0.3% in March 2023.

Inflation

- The UK's annual inflation remained unchanged in May 2023 at 8.7%

Pay

- Real pay fell in February to April 2023, by -2.0% for total pay and by -1.3% for regular pay

Sources: The Guardian, ONS, IPPR

Scottish Growth Forecasts

The Fraser of Allander Institute has revised its growth forecast for Scotland, indicating a more positive outlook in the short-term compared to previous projections. However, their forecast for the medium-term has become more negative.

- The FAI's current projections indicate a growth rate of 0.5% for 2023, followed by an increase to 0.7% in 2024 and further improvement to 1.2% in 2025.
- These estimates represent a significant improvement for 2023 when compared to the available data thus far.
- However, the FAI's outlook for growth in 2024 and 2025 has become more negative due to the increasing probability of higher inflation and interest rates persisting for an extended period.

Scottish Growth Forecasts

	2023	2024	2025
Jun-23	-0.5%	0.7%	1.2%
Mar-23	-0.7%	0.9%	1.7%
Feb-23	-0.1%	0.6%	1.7%

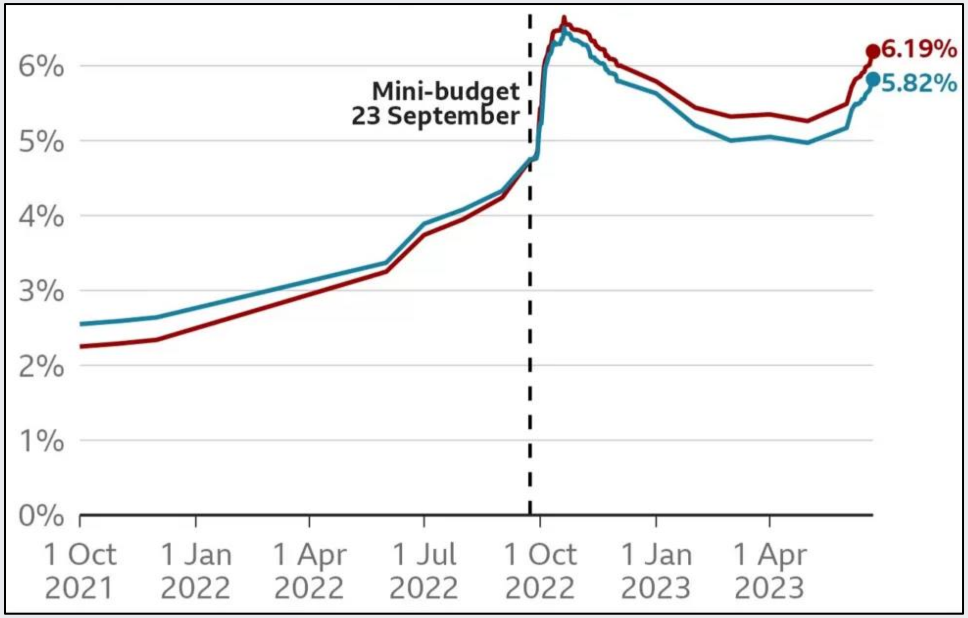
Source: Fraser of Allander Institute

Interest Rates

The Bank of England (BoE) has increased its benchmark rate to 5% from 4.5%. Financial markets now predict that UK interest rates will reach 6% by the end of 2023. There are concerns expressed that this strategy could potentially push the British economy into a recession.

- **Economy wide impacts:** Higher borrowing costs are expected to result in a decrease in households' disposable income and significantly reduce consumer demand.
- **Mortgage holders:** According to current market assessments, households planning to remortgage in 2024 could face an average annual increase of £3,000 or more in their mortgage bills (more analysis in the next page).
- **Construction sector:** As a result of higher mortgage rates housebuilders are cutting back on the construction of homes. According to the latest report on the construction sector, activity on residential construction sites declined in May to its lowest level since 2009, apart from when sites were locked down during the COVID-19.
- **Business impacts:** interest rate hikes will have a negative impact on access to finance, especially for SMEs. This is likely to postpone much needed investment in capital, skills and R&D.

Average interest on two-year and five-year fixed deals



Source: BBC

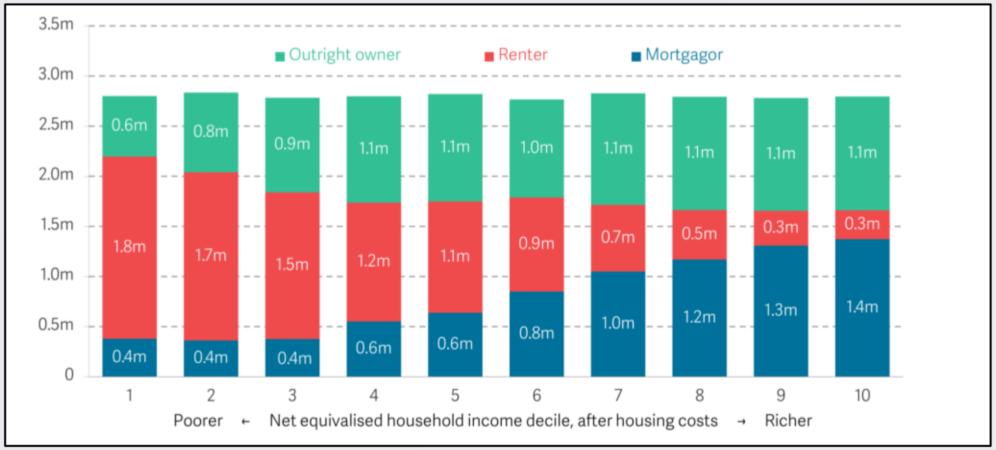
Sources: The Guardian, Resolution Foundation

Impact of Interest Rates Hikes on Mortgage Holders

A significant amount of mortgage distress is anticipated. However, the overall impact will be reduced due to a decrease in the proportion of households with mortgages, primarily among older homeowners and fewer young individuals owning homes.

- **Mortgage rates:** According to the latest market expectations for the Bank Rate, the Resolution Foundation predicts that the average rate for a ***two-year fixed rate mortgage will rise to 6.25% this year and will not decrease below 4.5% until the end of 2027***.
- **Scale of impact:** ***The impact of rising mortgage rates will be less widespread*** than in previous episodes due to a decline in the proportion of households with mortgages, attributed to older individuals who own their homes outright and fewer young individuals who own at all. Consequently, **the share of households with mortgages has fallen below 30%** (from 34% a decade ago)**.**
- **Distributional impact:** The Institute for Fiscal Studies said that the expected surge in costs is ***likely to hit hardest people in their 30s*** for whom payments will jump by £360/month (11% of disposable income). Moreover, analysis by the Resolution Foundation suggests that a larger share of higher-income households are going to be affected the most.

Number of households that are mortgagors, renters or outright owners, by income decile: UK 2019-2020



Source: [Resolution Foundation]

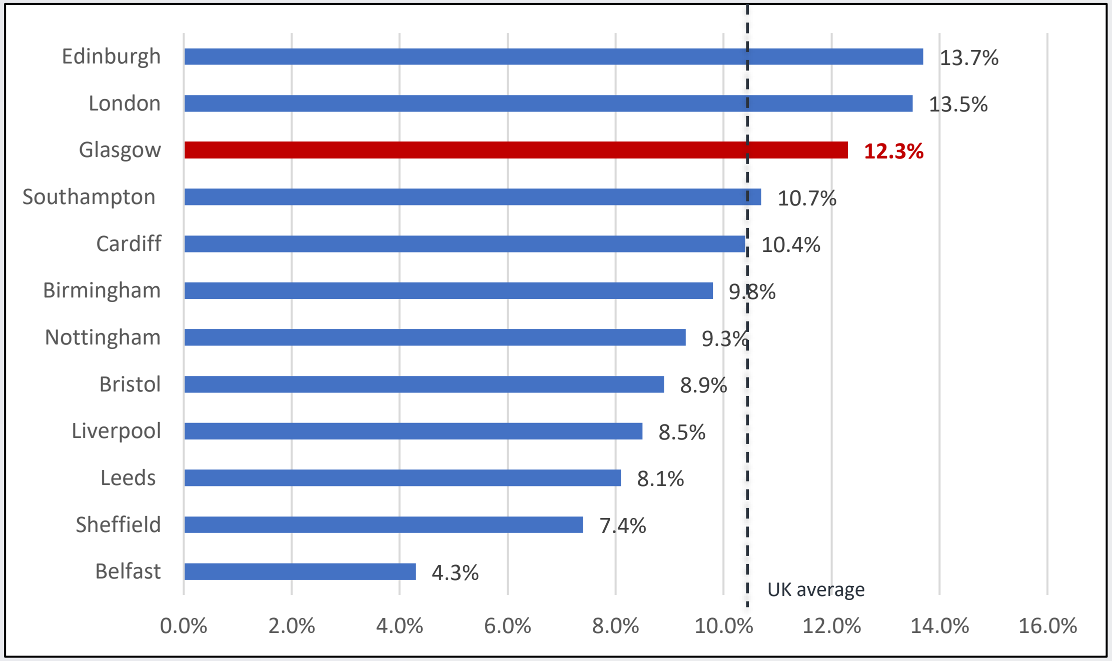
Sources: [Resolution Foundation, 17 June 2023,] [Institute for Fiscal Studies], June 2023

Rent Inflation

According to Zoopla data, rents have been growing faster than wages for nearly two years. Affordability of renting has been at its worst for a decade. Rents in Glasgow over the last year have grown faster than the UK average.

- The current share of income allocated for rent has risen slightly to 28.3%, compared to the average of 27% over the past decade. Even a small increase in percentage can have a notable impact on individuals' finances.
- The pressure of rising mortgage rates faced by landlords, as well as higher demand for properties than the number made available, have combined to raise the costs for tenants. According to Zoopla, there are 20% to 40% fewer properties to rent in most regions than there were before the pandemic.
- It is likely that the higher interest rates will continue to feed into higher rents, disproportionally impacting low-income families and young people.

Increase in rents from April 2022 to April 2023



Source: *[Zoopla (BBC)]*

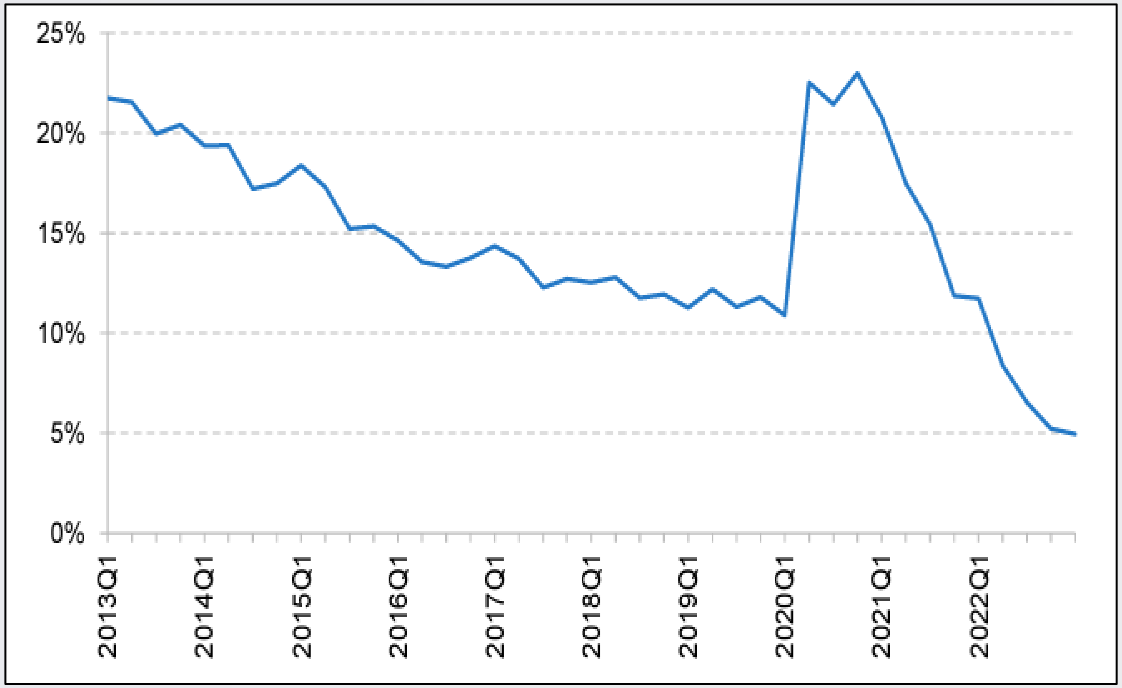
Housing Affordability for Low-Income Households

According to the Institute for Fiscal Studies, private rents will become increasingly unaffordable for those on low incomes if benefit freezes are maintained.

- Following the pandemic, the local housing allowance (LHA) rates, which determine the maximum housing benefit available, were raised to the 30th percentile of local rents. At that time, around 23% of rental properties listed on Zoopla were affordable* for individuals receiving housing benefits.
- However, since then, the LHA rates have remained unchanged in monetary terms, while the rents for new rental properties have increased by more than 20% on average.
- Consequently, ***in the first quarter of 2023, only 5% of private rental properties were affordable for individuals relying on housing benefits.*** This decline in affordability has been observed throughout the country.

Note: Affordable properties were defined as those with rents that could be entirely covered by housing benefits.

Percentage of private rental properties on Zoopla affordable on housing benefit



Source: [Institute for Fiscal Studies, 27 June 2023]

Headline Labour Market Statistics

Employment is rising in the UK but falling in Scotland. Those inactive due to long-term sickness increased to new record high levels. At the same time, overall vacancies remain high, but are falling in hospitality, retail and in information/technology.

Table 1: Labour Force Survey estimates from February to April 2023

	Unemployment (%)	Unemployment (ppts) Quarter Change	Employment (%)	Employment (ppts) Quarter Change	Economic Inactivity (%)	Economic Inactivity (ppts) Quarter Change
Scotland	3.1	0.0	74.6	-1.8	22.9	1.9
UK	3.8	0.1	76.0	0.2	21.0	-0.4

Source: ONS, Labour Market Overview June 2023, Scottish Government Labour Market Statistics June 2023

The UK's labour market recovery has been led by older people

- According to the Institute for Employment Studies, recent increases in employment in the UK have primarily been driven by older individuals, specifically men aged 65 and above. Interestingly, the gap in employment rates between older men and women is now *widening*, which is a new development compared to previous records.
- The level of economic inactivity among individuals under the age of 50 has remained relatively stable in recent months. Among young people aged 16 to 24, there was a significant rise in unemployment at the start of the pandemic as more individuals chose to pursue further education. This trend declined as the economy reopened but has now shown a slight increase once again.

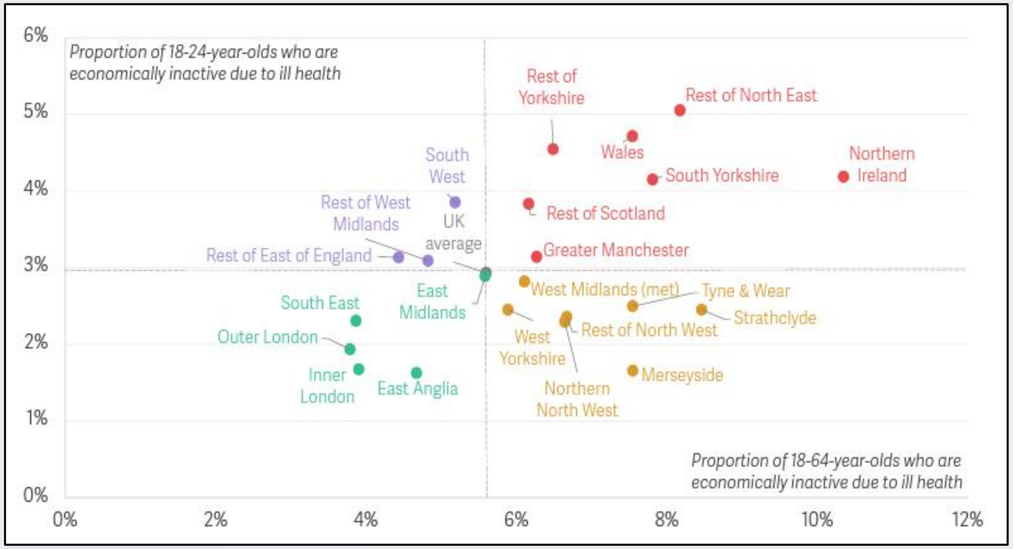
Source: IES Briefing, Labour Market Statistics June 2023

Youth Worklessness Due to Ill-health

New research from the Resolution Foundation is exploring the prevalence of youth worklessness due to ill-health in different parts of the UK. It finds that economic inactivity due to ill-health is heavily concentrated among those with low skills and in small towns and villages.

- Over the past decade, the number of 18-24-year-olds unable to work due to ill-health has nearly doubled. The most significant difference in worklessness due to ill-health is observed between larger cities and smaller towns. Research shows that young individuals residing in major cities like Cardiff, Glasgow, or Liverpool are less likely to be workless due to illness.
- This spatial variation in youth worklessness is primarily influenced by the migration of young people from smaller settlements to core cities and the protective effect of higher education, rather than inherent differences in the places themselves.
- Additionally, there is evidence indicating that poor educational outcomes play a significant role in this disparity. Alarmingly, 79% of 18-24-year-olds who are unable to work due to ill health possess qualifications only up to GCSE-level or below, compared to one-third of all young people.

Proportion of 18-64-year-olds and 18-24-year-olds who are economically inactive due to ill-health, by region 2020-22



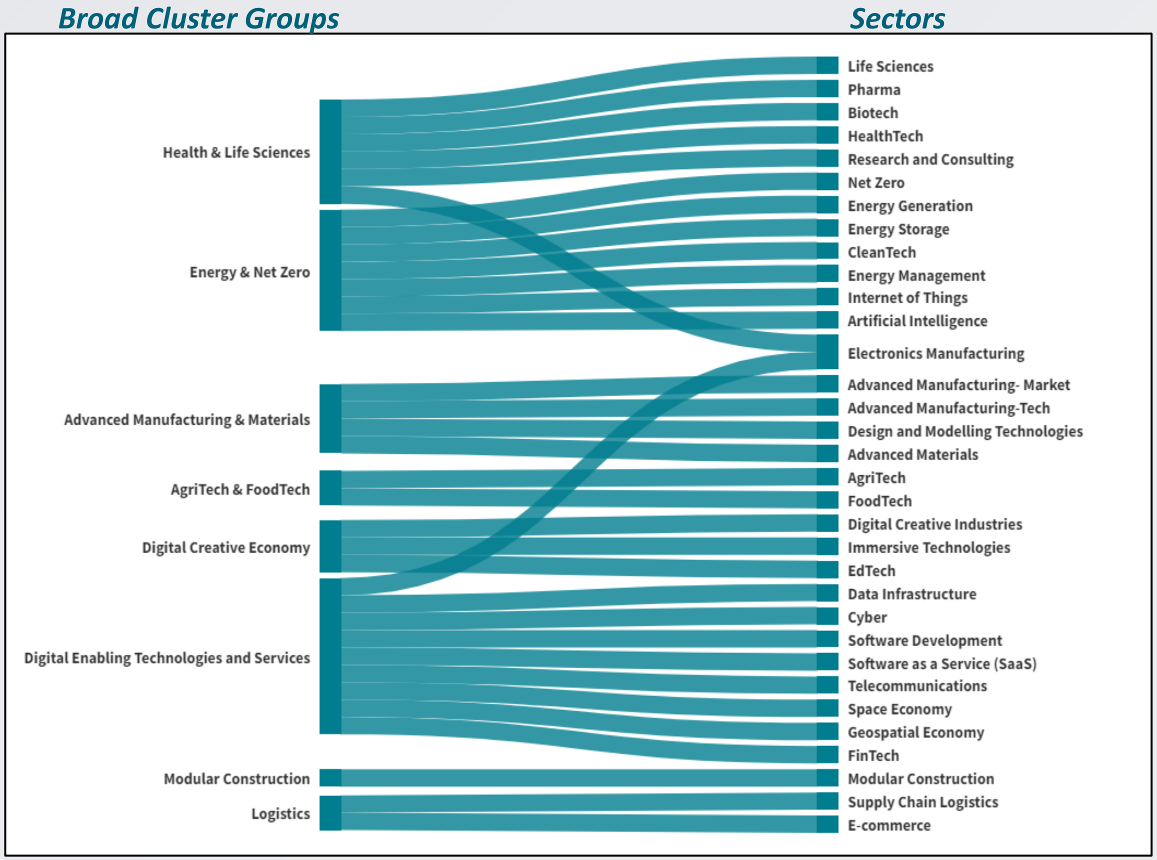
Source: [Resolution Foundation](), June 2023

Innovation Clusters

To support the Innovation Accelerator Programme, the Intelligence Hub has undertaken analysis using a variety of datasets to identify an ecosystem of strengths in the emerging economy for GCR based around nine broad groups. These broadly align with the innovation priorities of the National Innovation Strategy 2023-2033.

- **Business Concentration:** Among these sectors, the Region secures top ranking in Net Zero, Energy Generation and CleanTech as well as BioTech and Internet of Things.
- **Investment:** Based on investment data analysis, it is evident that GCR has attracted more investment in its market sectors. In the past three years, the sectors that have received the highest volume of investment are ***FinTech, Net Zero*** *and* ***Space Economy*** from the market sectors*, and ***Electronics Manufacturing, BioTech and Quantum and Photonics*** from the enabling tech sectors.
- **Assets:** In terms of academic expertise, the academic institutions within Glasgow City Region are prominently involved in research funding within fields such as ***clinical medicine, electronic engineering and mechanical engineering.***

Sources: Data City, Dealroom



*Note: This is based on a taxonomy co-produced with various stakeholders. See more on the glossary and Appendix I

FDI & Assets

Research highlights that for an innovation ecosystem to fully realize its potential, it is vital to attract Foreign Direct Investment (FDI), as well as establish robust innovation districts that serve as magnets for FDI and facilitate the inflow of international capital, expertise, and market access.

Assets- Innovation Districts

- Research highlights the significance of governance in innovation districts and stresses the need for districts to adopt effective governance models. By doing so, districts can leverage the strengths of their various actors, facilitate collaboration, and overcome challenges to realise their full potential.
- Drawing lessons from international innovation districts, the research points to seven factors that contribute to effective governance:

1. **Co-design and co-invest for effective governance.**
2. **Identify the right degree of independence.**
3. **Allow diversity of voice and view.**
4. **Strategically involve government based on local conditions.**
5. **Tie governance to land.**
6. **Design a financially sustainable model.**
7. **Ensure flexibility—a governance model that can adapt over time.**

Source: Global Institute on Innovation Districts, June 2023

Investment

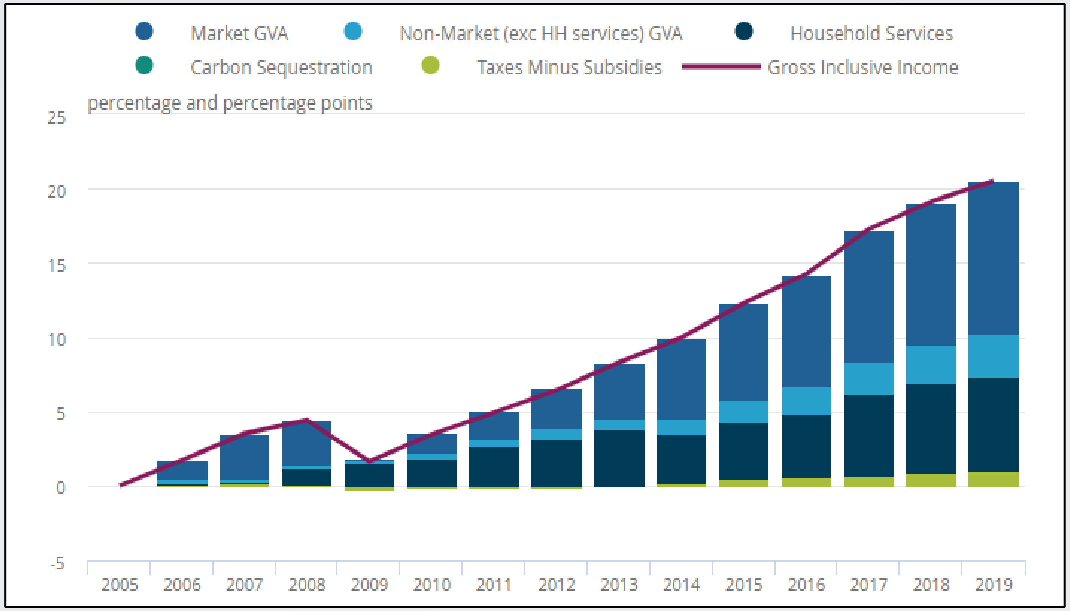
- According to the latest Foreign Direct Investment (FDI) data, Scotland has emerged as the leading FDI destination outside of London. Scotland's share of the total inward investment projects by the UK rose from 12.3% in 2021 to 13.6% in 2022 (*Source: Scottish Financial News*) .
- Scottish Enterprise has pointed out that Glasgow specifically attracts projects focused on research and development (R&D) and technology. ***The importance of prioritising the Region's strengths and establishing supply chains that would encourage investments to remain in the area, was also emphasised*** *(Source: The importance of Glasgow and Edinburgh in the Scottish Economy, Centre for Cities even 20/6/23)*.

Beyond GDP- Measuring Economic Wellbeing

The ONS has introduced a new measure of Inclusive Growth, which encompasses a broader range of economic activities and assets than gross domestic product (GDP) does, such as unpaid household services, ecosystem services and more.

- Between 2005 and 2019, gross inclusive income (GII) in the UK grew by 20.5% in volume terms, including 1.2% growth in 2019.
- GII grew more slowly than GDP, which grew 22.1%, primarily reflecting weaker contributions from unpaid household work. Net Inclusive Income (NII) grew by 17.5% in volume terms.
- Around half of growth in gross inclusive income since 2005 can be attributed to the market sector*.
- These data represent experimental work in progress estimates of beyond GDP measure of economic progress; capturing a wider range of activities than GDP.

Contributions to growth in gross inclusive income from 2005 to 2019, UK



Source: ONS

*Market GVA includes gross value added for the market sector as defined in the national accounts, plus the value of investment in intangible capitals (e.g. branding, design, firm specific training)

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Glossary

Gross Domestic Product (GDP): The total monetary value of final good and services produced in a country in a given time period.

Consumer Price Index (CPI): Is a weighted-average of a basket of consumer goods and services purchased by households. Changes in measured CPI tracks changes in prices overtime.

Unemployment rate: Unemployed people are out of work but actively looking for a job and available to start work in the next two weeks. It is measured as the number of unemployed people divided by the number of economically active population (those in employment and those unemployed).

Economic Inactivity rate: Economically inactive people are out of work but are not actively looking for a job. The headline inactivity rate is calculated by dividing the inactivity level for those aged from 16 to 64 divided by the population for that age group.

Economic inactivity due to ill-health: Economically inactive people whose primary reason for being out of work is ill-health.

Glossary

Market sector: refers to the industry segments focused on delivering products and services to end consumers or specific target markets e.g. FinTech, Life Sciences, EdTech

Enabling technology sector: The enabling tech sector comprises businesses that provide critical infrastructure, tools, and services to a variety of market sectors. These companies often offer foundational technologies and resources necessary for other industries and sectors to thrive e.g. Cloud Computing, Cybersecurity, Artificial Intelligence

Innovation District: Innovation districts play a significant role in fostering and supporting an innovation ecosystem. These districts are physical locations or areas within a city or region that are designed and curated to concentrate innovation-related activities, resources, and collaboration among various stakeholders.

Appendix I. Identifying Sectors and Taxonomy

The list was discussed with stakeholders (such as UK Innovate, Invest Glasgow and Glasgow City Innovation District) and agreed as below.

Market Sectors (verticals) ⇅

- Advanced Manufacturing - Market
- Ed Tech
- Food Tech
- Modular Construction
- Space Economy
- Agri-Tech
- Energy Generation
- Health Tech
- Net Zero
- Supply Chain Logistics
- Clean Tech
- Energy Storage
- Life Sciences
- Pharma
- Telecomms
- Digital Creative Industries
- Fin Tech
- Med Tech
- Research & Consulting (Science / Eng)

Tech Sectors (horizontals) ⇆

- Advanced Manufacturing – Enabling Tech
- Advanced Materials
- AI
- Bio-Tech
- Cyber
- Data Infrastructure
- Design and Modelling Tech
- E-Commerce
- Electronics Manufacturing
- Energy Management
- Geospatial Economy
- Immersive Tech
- Quantum and Photonics
- Sensors
- Software Development
- Internet of Things
- Software as a Service