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Bridging the productivity gap after Brexit



In his monthly column, **Professor Frank Peck**, of the University of Cumbria's Centre for Regional Economic Development, looks at how to make our economy more efficient

At a time of continued uncertainty surrounding the outcome of Brexit negotiations, it seems opportune to consider one of the key challenges that will face the post-Brexit economy – the issue of competitiveness and its relation to productivity.

For well over a decade now, there has been a debate surrounding the national productivity gap.

Indeed, the UK's Industrial Strategy (2017) is constructed around what are described as the five foundations of productivity. So what exactly is this productivity gap?

As a concept, productivity is a

measure of efficiency – how well an economic system converts inputs into outputs.

Measurement of this is highly complex and is often reduced to labour productivity – the value of output produced per worker (or per hour). This is a narrow view but it has advantages in that there is data to compare countries and regions using a similar metric, Gross Value Added (GVA), per worker.

At the European scale, there are clear differences between EU member states and the performance of the UK on this measure is mediocre.

On GDP per hour worked in 2016, the UK was indexed at 99 (where the EU average equals 100).

'Manufacturing activities are capable of generating very high levels of output per worker because they are capital-intensive'

This compares unfavourably with countries that would be considered to be the UK's industrial competitors such as Germany (127), Netherlands (126) and France (125).

In recent years, it seems, the UK has excelled in creating employment, but disproportionately in low value-added activities.

Data on regional variations of productivity reveal that there are also significant differentials within the UK. In the North West region, for instance, GVA per hour worked in 2017 was £31 compared to the UK average at £33.7 and London on £44.7.

Drilling down to sub-regional scale, West Cumbria – which includes Furness – measured close to



the North West regional average (index 91.3 compared to 92) while East Cumbria was lower (84.1).

It is interesting to observe that West Cumbria appears to outperform many areas of Manchester, Merseyside and Lancashire and there are also parts of the North West considerably lower on this measure than East Cumbria.

These productivity gaps have been presented as a crisis by some, but a puzzle to be solved by others.

The puzzle lies in the fact that there are many causes of variations in labour productivity, some of which may not necessarily be linked to competitiveness.

Here are four of these:

Industrial structure

Industries vary in their levels of labour productivity. In general, manufacturing activities are capable of generating very high levels of output-per-worker because they are capital-intensive. Indeed, in some sectors, machines produce products while a large part of the labour force can largely be described as machine maintenance (as in chemicals or vehicles). Labour productivity will therefore vary between regions depending on the mix of industries.

Labour productivity varies between regions, depending on the mix of industries, with manufacturing tending to have a high GVA per worker, while it is lower in the service sector

A key reason for West Cumbria performing close to the regional average is due to industrial structure that is marked by above average employment in manufacturing.

Ownership structure

Studies have also shown that regions and sectors characterised by international ownership tend to be associated with higher productivity. This is due to the fact that such companies have access to wider corporate resources for investment in new technology. So long as there is long-term commitment to production, reinvestment in externally owned sites tends to create higher labour productivity.

Business size-structure

Larger businesses can benefit from economies of scale and more efficient divisions of labour that tend to be associated with higher levels of productivity. It is also the case that small and micro-businesses are more

common in some sectors than others and these tend to be associated with services that are labour intensive – visitor economies, local products, specialist retailing, food services. It is no surprise, therefore, that measures of labour productivity are below average in East Cumbria in particular.

Functional structure

Even within industries, functions vary in labour-intensity and value-added. Large corporations have been through many phases of regional restructuring across the UK in the past. Commonly, this has involved dispersing low value-added functions to peripheral regions while high value-added activities are retained in the core – creating regional divides in terms of business functions. Regions with a preponderance, for instance, of back-office functions will tend to display levels of GVA per worker that are below sector averages.

GVA per hour worked in the Sub-regions of North West England (UK=100 in 2017)

SOURCE: OFFICE FOR NATIONAL STATISTICS

Cheshire East	115.7
Cheshire West and Chester	105.6
Mid Lancashire	102.0
Greater Manchester South East	98.3
East Merseyside	96.0
Greater Manchester South West	95.2
Lancaster and Wyre	93.3
Sefton	92.5
West Cumbria	91.3
East Lancashire	87.4
Manchester	87.3
Wirral	86.7
Liverpool	86.5
Greater Manchester North East	86.0
Warrington	85.9
EastCumbria	84.1
Greater Manchester North West	84.0
Chorley and West Lancashire	83.7
Blackburn with Darwen	79.6
Blackpool	74.6

What this suggests is that a significant part of the variation in labour productivity can be explained statistically by the geography of industrial structure, ownership, business-size structure and business functions. Of course, there will be residual variation that cannot be explained in this way – where comparing like with like, businesses in some regions (or nations) outperform similar competitors located elsewhere.

What this suggests is the need for a balanced approach to addressing productivity divides – inducing appropriate structural change where resources allow, while also providing support to all businesses with plans to innovate, invest in technology and enhance skill levels in the workforce.