2 THE LABOUR MARKET CONTEXT

The performance of the region needs to be seen within the context of the international and national economic climate. In this section we consider the trends and developments at the level of the UK economy and some international comparisons. Also included in this section are the key findings of the 2004 HLMR.

2.1 THE NATIONAL ECONOMIC CLIMATE

The UK economy continues to perform well with Gross Domestic Product (GDP) now having grown for 50 consecutive quarters. For 2004 as a whole, UK GDP rose by 3.1 per cent, its fastest rate of growth for four years. Business investment accelerated in 2004 and private consumption continued to grow at sustainable rates. GDP is expected to grow by 3 to 3.5 per cent in 2005 as the remaining slack in the economy is absorbed and the output gap is closed around the end of the year. Growth is then expected to return to between 2.5 and 3 per cent in 2006, in line with the economy's trend rate[5].

The HM Treasury report, *Benchmarking UK Productivity Performance*[6], published in October 2004, summarises recent trends in UK productivity performance. It looks at the output gap estimates published by the OECD, which assess performance across the UK, US, Germany and France, particularly in 1995 and between 2000 and 2002, when these countries were on a similar point on the economic cycle.

Progress over recent years, particularly 2000 to 2002, has been stronger than original estimates had suggested, with the UK making progress in narrowing the output per worker gap. The report suggests that, since 1995, the output per worker gap with France had narrowed from around 21 per cent to 13 per cent in 2002, and that the gap with Germany has also closed.

It also suggests that the UK is making progress in narrowing the output per hour gap. The gap with Germany has narrowed from around 23 per cent in 1995 to 16 per cent in 2002. The gap with the US is also smaller at around 19 per cent as US workers tend to work more hours, on average, and have less holiday entitlement than their European counterparts. However, as French workers also tend to work fewer hours, on average, than in the UK, a considerable productivity gap remains with France, on a per hour basis, of around 32 per cent.

The UK is performing relatively well in terms of output per person of working age, with performance significantly stronger than in Germany and similar to performance in France. This reflects the relatively strong employment position within the UK. The UK has the highest employment rate of the G7 countries with 74.5 per cent of the working age population in employment, compared to 71.2 per cent in France and 68.4 per cent in Germany. The report also suggests that, whilst the gap between the UK and US is still substantial, it has narrowed on the output per person of working age measure to around 25 per cent. This demonstrates that it is possible to achieve high levels of productivity alongside strong rates of employment.

[5] HM Treasury, *Budget 2005*, HM Treasury, March 2005.
[6] HM Treasury, *Productivity in the UK 5: Benchmarking UK Productivity Performance*, HM Treasury, October 2004.

There is also evidence to suggest that there have been improvements in business investment as a percentage of GDP in the UK and that the advantage other countries had in having had better investment is falling[7]. It has been the case that countries such as Germany and France had greater levels of productivity because they saved and invested more, earlier than the UK. As capital productivity represents this past investment, high capital productivity is preferable as it means a good investment return. It is argued that the US has higher levels of capital productivity because it uses its capital more intensively and/or focuses on a smaller number of high return projects at the possible expense of labour productivity[8]. The US also has the other advantage of a large single market with a low population density and a low cost of land.

The UK has also been enjoying a time of relative economic stability, a key component of long-term economic growth. The UK has had a long history of economic boom and bust and there are suggestions that this has been more evident in the UK than in other European countries[9].

2.2 THE SOUTH WEST – A SUMMARY OF THE 2004 REPORT

The 2004 report[10] found the South West to have a healthy labour market and on the range of indicators set out in the framework, healthier than any other region with the exception of the South East. The region has:

- a high degree of labour demand;
- a well-qualified workforce; and
- efficient and equitable functioning between the demand and supply sides of the market.

However, the analysis also concluded that the South West was operating ‘healthily’ but within a low skills equilibrium. Productivity in the region is relatively low, employers are reporting few skills gaps, and are having little difficulty in finding the skills they need from the available workforce. Whilst the overall picture is a healthy one, the South West is also far from being a homogenous region. Marked differences in outcomes are evident for the far south and west, and northern parts of the region, with the far south and west tending to be less productive with higher unemployment and lower earnings than the north.

[7] Turner A, *Growth, Productivity and Employment*, Centre for Economic Performance, LSE, September 2000.
[8] Ibid.
[9] ibid.
[10] IES, *South West Healthy Labour Market Review* 2004, IES, June 2004. The 2004 report can be found at: http://www.swslim.org.uk/research/database/searchresults_detail_page.asp?ResearchID=1930

TABLE 2: *Summary of indicator analysis*

Broad Outcome Indicators	
Employment	High employment, a high number of jobs per working age resident and relatively self-contained.
Balance and quality	Over-representation of distribution, hotels and restaurants, and the public sector. Under-representation in financial intermediation and business services. Occupational structure similar to the national picture. Employment in knowledge intensive sectors is below average. Full-time earnings below average.
Output and productivity	Low productivity and large divide between the north and south of the region.
Labour market functioning	Low levels of unemployment and long-term unemployment, Small differentials in employment by gender, disability and ethnicity.
Closer to Policy Indicators & Learning Targets	
Businesses in the region	High rate of business generation. High rate of business de-registration.
Research and development (R&D)	Above average R&D expenditure overall and by business and government. Expenditure by Higher Education is low.
Vacancies and skills	High proportion of vacancies which are hard-to-fill but the lowest proportion of vacancies that are hard-to-fill for skills-related reasons. Low proportion of employers reporting skills gaps.
Qualifications of the workforce	Highly qualified workforce. Low levels of the workforce without qualifications.