Report to:	Economic Scrutiny
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Subject:	**Economic update and challenges**
Director:	Alan Reiss, Chief Operating Officer
Author:	Thomas Purvis (Economic Analysis Manager) Peter Glover (Economic Evidence Manager)

1. Purpose of this report

1.1. To provide supplementary evidence in support of the emerging West Yorkshire economic strategy.

2. Information

Latest economic outlook

2.1 In August, the Bank of England increased interest rates to 5.25% from 5%, by a margin of 6-3 (2 of the 3 opposition voters wanted to increase rates by 50 basis points to 5.5%). As part of the decision, a Monetary Policy Report was released which provided an update to economic forecasts by the Bank, as well as explanations why. These are below:

- Inflation is expected to be around 5% by the end of this year and is then forecast to fall to 2% by Q2 of 2025.
- Food inflation is expected to be considerably above 5% still by the end of this year (expectations from BoE agents is that it will be between 9 and 10%).
- GDP growth has been downgraded to 0.5% in 2024 (down from 0.75%) and 0.25% in 2025 (down from 0.75). There has been an increase in expectations for 2023 from 0.25% to 0.5%.
- Unemployment is expected to hit 4% by the end of this year, 4.5% by the end of 2024 and 4.75% by the end of 2025 (worse than forecast in May).

- A 2-year 75% LTV mortgage has an interest rate on average of 6.25% now, up 1.5% since May.

2.2 CPI in the 12 months to July 2023 was 6.8%, down from 7.9% in June (this does not mean that prices are falling, just that they are increasing less quickly). Challenges remain, however. Whilst CPI for goods slowed from 8.5% to 6.1%, service sector CPI increased from 7.2% to 7.4%. Core inflation (CPI minus energy, food, alcohol, and tobacco) remained unchanged at 6.9%. Food inflation has slowed down but continues to be in the double digits. It was 17.4% in the 12 months to June but fell to 14.9% in the 12 months to July. Anecdotally, petrol and diesel prices have started to increase again recently, after prices declined for much of the last 3 to 6 months.

2.3 On the 25 August, Ofgem announced the new Energy Price Cap for October to December 2023. The cap has fallen from £2,074 for July to September to £1,923 for October to December. It should be noted that some households will pay more than this, as the figure quoted above is for the average household use.

2.4 Households are responding to the increased interest rates and increased cost of living. In July, a net £400m was deposited with banks and building societies. For context, in October 2022 net deposits were around £9bn. Whilst net deposits are very low relative to historic rates, inflows into interest-bearing saving accounts are also higher than they have been for much of the prior decade due to the relatively higher interest rates on offer.

Persistent challenges

2.5 Sub-regional productivity figures for 2021 were recently released by the ONS. Between 2016 and 2021, GVA per hour worked in the UK increased from £33.50 to £38.30 (+14.3%), compared with an increase from £28.90 to £33 in West Yorkshire (+14.2%). Productivity challenges have continued to be a problem for the UK and West Yorkshire economy, as set out in more detail in the evidence pack for the Economic Strategy. However, the gap between West Yorkshire and the UK has increased when compared to pre-Financial Crisis levels.

2.6 West Yorkshire's underperformance on productivity is reflected in its performance on pay. Average pay in West Yorkshire is lower than the UK average; it has grown at a similar rate in recent years, but the deficit is not narrowing. As of July 2023, median monthly pay for employees in West Yorkshire was £2,144, 94% of the UK average of £2,274. The equivalent figure for Bradford is only 89%, whereas it rises to 98% in Leeds and 97% in Wakefield. Pay (unadjusted for inflation) has grown strongly in the 12 months to July 2023, by 8% for both West Yorkshire and nationally. At local authority level growth was strongest in Bradford (+9.5%) and Wakefield (8.9%). Pay has grown by 15% both nationally and at West Yorkshire level since the re-opening of the economy in July 2021. In recent months pay growth has been largely driven by increases for white collar jobs in the private sector.

2.7 The claimant count measures the number of people claiming benefits primarily because they are unemployed. After climbing steeply in 2020 with the onset of the pandemic, the claimant count fell steadily between early 2021 and late 2022. Since then, the number of claimants has increased at a modest rate reflecting the general economic difficulties. The West Yorkshire current count for July 2023 of 70,835, is 3,500 or 5% higher than in October 2022 but also 25% higher than its pre-pandemic level in February 2020. The claimant rate (ratio of claimants to the working age population) is lowest in Wakefield (3.6%) and highest in Bradford (6.6%), the latter having one of the highest rates of any local authority in England and well in excess of the national average of 3.8%.

Economic inactivity

2.8 Rising participation in the labour force was a key driver of economic growth during the 2010s but this was reversed by the pandemic. Twenty-three per cent of working age people in West Yorkshire are economically inactive compared with a national average of 21%. Inactivity in the region has been consistently above the national average since the global financial crisis and has increased in the aftermath of the pandemic. The current level of inactivity in West Yorkshire (based on Annual Population Survey for January to December 2022) is 35,000 or 11% higher than the equivalent figure in 2020 for working aged people and the rate has increased by more than two percentage points. Inactivity has increased fastest for those aged 50 to 64 and for people who are inactive due to long-term sickness. More timely figures at national level show that overall inactivity is now on a downward trend although the number of people who are inactive due to long-term sickness continues to grow and is at record levels.

2.9 There is a strong argument that efforts to raise labour market participation should extend beyond engaging the cohort of older workers who have left the labour force since the pandemic in an effort to encourage them to return; since this group includes a significant proportion who retired early from well-paid jobs and have housing wealth and private pensions to draw on. Moreover, many of this group left the labour market more than a year ago and the evidence suggests that this reduces the likelihood of them returning. Arguably, policy should instead adopt a broader focus, seeking to engage women with children, those affected by ill-health and disability and the broader range of older people.

NEETs

2.10 Based on the latest published figures, there was an average of 3,500 young people aged 16 and 17 who were Not in Education, Employment or Training (NEET) or whose status was not known in West Yorkshire during the months of December 2022 to February 2023. This equates to 6.2% of all 16- and 17-year-olds known to their respective local authorities, which is above the England average of 5.2%. The prevalence of NEETs varies across West Yorkshire local authorities, with some below the national average and some well above. Between 3% to 4% of 16- and 17-year-olds in Calderdale, Kirklees and Wakefield are NEET or not known, with the proportion increasing to around 7% in Bradford. The proportion is highest in Leeds at 9%, which is

similar to Liverpool and Sheffield (9% and 8% respectively) but higher than Manchester (6%).

2.11 The number and proportion of young people NEET or not known in West Yorkshire increased for the second successive year in 2022/23. The number increased by 420 or 14%, whilst the proportion of the cohort increased by 0.6 percentage points, from 5.5% to 6.2% (figures appear inconsistent due to rounding). Four out of five local authorities saw an increase in their number of NEETs in 2022/23, although the growth in Kirklees was marginal in absolute terms. Wakefield was the only local authority where the count of NEETs fell. Nationally, the increase in the number of young people NEET and not known in 2022/23 was similar to West Yorkshire at 14%.

2.12 Young people from an ethnic minority group are, in general, less likely to become NEET in West Yorkshire. Around 5% of young people from an ethnic minority were NEET or not known as of December 2020, compared with 6% of white young people. Asian / Asian British and Black / Black British groups both had rates below the overall average, although the proportion of young people with a mixed or multiple ethnic background who were NEET or not known was above average at 8%.

2.13 Nine per cent of young people with special education needs and disability (SEND)1 and 9% of young people in receipt of SEN support2 were NEET or not known as of December 2020 compared with 6% of the overall cohort.

Vacancies

2.14 Recruitment demand in West Yorkshire has been stronger than nationally since the pandemic and remains at high levels. There are some signs that the labour market is "softening" (e.g., the recent increase in the claimant count) but overall, the West Yorkshire labour market has remained resilient, and continues to outperform the national average in terms of recruitment activity. The monthly volume of online job postings in West Yorkshire in July 2023 was 157% higher than the average for 2019, whereas the equivalent national growth figure was only 82%. The monthly count was also 13% higher in July 2023 than in July 2022 compared with a national average increase of 7%.

2.15 Leeds accounts for nearly half of total vacancies (online job postings) in West Yorkshire. It also has by far the highest ratio of job postings to current employment in West Yorkshire, reflecting the fact that it has one of the most vibrant labour markets of any city in the north of England. It has a relatively tight labour market, as reflected in the ratio of job postings to unemployed claimants. However, Leeds' vacancy levels have been slower to recover and grow in the aftermath of the pandemic.

Economic imbalances within West Yorkshire

[1] A child or young person has special educational needs and disabilities if they have a learning difficulty and/or a disability that means they need special health and education support.
[2] Support given in school or college, such as speech therapy.

2.16 There are significant socio-economic imbalances at local authority level within West Yorkshire. As the focal point of the regional economy, Leeds is typically the highest ranked of the five local authorities with regard to key economic indicators. This includes gross value added per head (Leeds is above the national average on this measure), employment rate, productivity level (value of output per hour worked), proportion of people qualified at a higher level and gross disposable household income per head. Leeds also has the most vibrant and tightest labour market in West Yorkshire (see above). Conversely, Bradford is often the worst performing of the five local authorities against many of these same key indicators. Calderdale, Kirklees and Wakefield tend to occupy the space between these two extremes, although they have distinctive strengths and weaknesses. For example, Calderdale has the highest density of private sector businesses relative to population whilst Wakefield has the highest average workplace pay in West Yorkshire. These differences are explored in more detail in the State of the Region 2022 report, which is currently being updated for October 2023 publication.

2.17 Differences at local authority level conceal important patterns at small area level. According to the English indices of deprivation 2019, 22% of neighbourhoods in West Yorkshire are among the 10% most deprived nationally, more than twice its "fair share" of deprived neighbourhoods. This rises to more than a third of neighbourhoods in Bradford. However, 24% of Leeds' neighbourhoods fall into the most acutely deprived decile, even though it has the highest proportion of neighbourhoods in West Yorkshire falling into the least deprived categories, demonstrating the large degree of socio-economic polarisation within Leeds.

Changes in work habits and effects of people being able to work remotely on local economy

2.18 Home and hybrid working is now a significant feature of working practice. According to figures from November 2022, around 9% of workers in West Yorkshire work exclusively from home, 31% work from home sometimes (hybrid) and 59% do not work from home at all. More than half of hybrid workers commute the full-time-equivalent of between 1 and 3 days a week. Although the prevalence of hybrid and home working had fallen slightly from six months earlier, the expectation among respondents was that exclusive home working might in future see a small reduction but this would be more than offset by an increase in hybrid working COVID-19 Transport Survey Wave 1 (westyorks-ca.gov.uk)

2.19 These changes in working patterns are also reflected in other data. Weekday footfall at Leeds rail station is currently around three- quarters of its pre-pandemic level, whilst Leeds' weekday radial traffic count is 13% below pre-pandemic. In addition, around 8% of total vacancies (online job postings) advertised in 2022 were for jobs with a facility to work remotely, rising to 9% for West Yorkshire vacancies (source: Lightcast).

2.20 The shift to remote working has had significant impacts on the economy. . Workers are spending more time in the residential neighbourhoods in which they live, and less time in the city centres where they work with consequences for locally consumed services, such as cafes, hairdressers and retail shops. It is

estimated that working from home will reallocate £3 billion in retail and hospitality spending from city centres to residential neighbourhoods in England and Wales. However, City centre activity will not necessarily be replaced by corresponding new outlets in the areas where people live and work remotely. These areas, where demand for locally consumed services has increased, can be affected by constraints on supply such as planning restrictions, low population density of the area and the availability of suitable accommodation.

2.21 The impact of these trends on West Yorkshire has been significant. According to one study, Leeds City Centre is the worst-affected area outside London with an estimated spending reduction of £35m per annum (-6%) and a loss of employment of 21,000 (including loss of 1,000 retail and hospitality jobs).

2.22 In the first half of 2023, 951 hospitality businesses (defined as Accommodation or Food and Beverage Service Activities) went into liquidation across West Yorkshire. This is 20% greater than the second half of 2022 when 793 went into liquidation, and 40% greater than the first half of 2022 when 682 went into liquidation. However, there is still overall growth in the number of businesses in this sector. In the first half of 2023 1,208 new hospitality businesses were registered in West Yorkshire. This is 35% higher than the number of hospitality start-ups in half one 2022 and half two 2022, which each had 894 new registrations.

Potential impact of artificial intelligence (AI)

2.23 The Combined Authority is working with Y-PERN (Yorkshire & Humber Policy Engagement & Research Network, an academic network) on a call for evidence to support development of the emerging Economic Strategy (see paper xx), part of this work includes consideration of the future of work and specifically the impact of AI in West Yorkshire. Therefore, the following provides an interim assessment which will be supplemented with additional evidence at West Yorkshire level.

2.24 Artificial intelligence (AI) is the ability of machines to perform tasks that are typically associated with human intelligence, such as learning and problem-solving. Its key applications include web search engines such as Google, recommendation systems such as those used by Amazon, speech recognition systems such as Siri and more recently generative and creative tools such as Chat GPT. AI models based on big data and machine learning can now supply answers to problems where formal rules are impossible to codify, and where humans have until recently had a comparative advantage in inferring decisions from their training or past experiences.

2.25 There is a significant level of **uncertainty surrounding the current and future impact of AI in the labour market,** as well as the most suitable policy actions to promote an effective and equitable use of AI. AI represents a marked departure from previous examples of automation in that it significantly expands the range of tasks that can be automated beyond routine, non-cognitive tasks and it is a general-purpose technology that will have a widespread impact on sectors and occupations. Its speed of development (particularly the latest wave

of generative AI such as Chat GPT) is also unprecedented contributing to the limited understanding of its future impact at this stage and adding to its potential for disruption.

2.26 **Higher-skilled occupations are most exposed to recent advances in AI**, including: business professionals; managers; science and engineering professionals; and legal, social and cultural professionals. This extends the potential scope of automation considerably beyond what had previously been possible, and it is primarily higher-paid occupations requiring higher than average education or training, whose core functions rely on accumulated experience to reach decisions, that are most exposed to AI. Higher skilled occupations of this kind have been the chief source of net employment growth in the national economy and at West Yorkshire level in the last two decades.

2.27 There is **little evidence** from the national and international literature **to show a negative impact from AI on employment levels so far**, which may reflect the low adoption of AI technologies as well as a reliance on voluntary workforce adjustments by business rather than redundancies. There is some evidence that AI creates new tasks and jobs for higher skilled workers who have the capability to work with AI. Available data suggests that the overall impact of AI on productivity has also been limited to date but case study evidence examining specific applications of generative AI finds larger effects on productivity.

2.28 The **strongest impact** of AI has so far been **on job quality**. On the one hand it can reduce tedious tasks leading to greater worker engagement; on the other it can change the way work is monitored and managed impacting workers' privacy and autonomy in the workplace. The automation of simple task can also leave workers in a more intense, higher-paced environment. AI is being used to support recruitment decision and its adverse impact in terms of bias could be far greater by virtue of the volume and velocity of the decisions it takes, which could systematise and multiply bias, with a particular impact on socio-demographic groups who are often disadvantaged in the labour market already.

2.29 Turning to the AI sector itself, estimates by the DataCity suggest that there are around 3,000 UK companies, employing 129,000 people and total turnover of £45bn. Roles in the sector offer pay that is 19% higher than the average salary. With average company growth per year of 6% the AI sector offers significant economic opportunities. However, AI firms have not received additional investor attention in recent years and the amount of venture capital funding is not increasing as fast as for other emerging economy sectors. West Yorkshire has a substantial number of businesses operating in the AI sector and as detailed in the forthcoming Digital Blueprint this presents a significant opportunity for the region. According to analysis by the DataCity there are 93 AI-focused businesses in West Yorkshire, with combined turnover of £220m. To set this in context, however, Manchester local authority, one of the few AI hotspots outside London and the southeast of England, has 92 businesses with combined turnover of £789m.

2.30 Artificial intelligence presents a range of issues with regard to economic inclusion. The impact of these issues could be different in character to the effects of previous waves of automation.

- Workers with AI skills who actively develop or maintain AI systems earn a substantial wage premium, even over similar workers with in-demand skills (for example, software skills).
- Workers who use AI but are not directly involved in its development may in future find themselves squeezed into a shrinking set of simpler tasks, which could put downward pressure on their wages (although there is no empirical evidence of this happening so far). There could be a significant impact on the pay and career opportunities of well-educated professional workers, whose roles are susceptible to displacement by AI, in contrast to previous rounds of automation, which principally affected people in lower and intermediate skilled occupations in administration and also unskilled and semi-skilled manual roles.
- So-called algorithmic management of workers can lead to higher work intensity, reduced human interaction and an impact on privacy where use of AI involves data collection on workers or how they do their job.
- There is also a risk that AI systems can multiply and systematise human bias in decision-making around the treatment of workers.
- AI can also increase accessibility and job satisfaction for workers traditionally disadvantaged in the labour market, such as workers with disabilities (e.g., through use of live captioning systems for deaf and hard of hearing people).

Impact of green economy / decarbonisation

2.31 There are a number of ways in which the green economy can be defined. In a study recently commissioned by the Combined Authority a mission-based approach was adopted, reflecting the approach taken by the national Green Jobs Taskforce. This means defining the green economy around activities that play a significant role in achieving net zero and other environmental objectives. The mission-based definition comprises 8 broad policy categories as follows:

- Climate adaptation
- Green professional and research services
- Homes and buildings
- Industrial decarbonisation
- Low carbon transport
- Natural environment
- Power
- Reduce, reuse, recycle and repair.

2.32 The study estimates total employment of 73,000 across these eight categories in West Yorkshire. This is equivalent to 7% of total employment in the region, which is slightly higher than the national average of 6%.

2.33 The biggest categories in employment terms include Power – with 21,000 jobs, the main component of which is power generation from renewable sources. Homes and buildings also comprises around 21,000 jobs. This

category comprises retrofit, building of energy efficient homes, installation of devices like heat pumps. Green professional and research services, which includes green finance and relevant research, and development activity is also substantial with nearly 10,000 jobs. Industrial de-carbonisation includes energy efficiency in industrial settings and electrification of industrial processes with employment of 8,500 – activities like CCS and hydrogen production are also notionally part of this category and are expected to become important in future.

2.34 The report also examines prospects for the green economy, presenting projections of employment for 2030 and 2050 based on a high, low and central scenarios. Based on the central scenario, which takes into account the changes in industrial structure that would be needed to deliver net zero rather than a continuation of recent growth performance total employment in the green economy is expected to double between 2020 and 2030, with net growth across all eight of the policy the categories. Power and Homes and buildings will still be the biggest activities in employment terms in 2030 but the fastest growing areas between 2020 and 2030 in percentage terms are expected to be Low Carbon Transport and Green professional services. Low carbon transport is projected to grow by 400% or 21,000 in absolute terms, whilst Green professional and research services is forecast to expand by 171% or 16,000.

2.35 The projected level of growth in the green economy does not represent net growth for the whole economy. It will be partially offset by job losses elsewhere. The report identifies industry sectors that have the highest carbon intensity and therefore the biggest exposure to the transition to net zero. Nearly 100,000 jobs fall into this category, around 9% of total jobs in West Yorkshire. The biggest concentrations of employment are in construction, transport and elements of manufacturing. Clearly, there is an overlap with our green policy categories. Some of the people working in these carbon-intensive sectors will be able seamlessly to redeploy their skills within their current sector of employment – for example, the construction sector has the largest exposure to carbon intensive activities, but large numbers of workers will be required in activities like retrofit and green construction.

2.36 Nonetheless there is potential for large-scale dislocation arising from the transition to net zero and the ambition is to avoid the long-lasting negative impacts associated with previous industrial restructuring seen in the ‘80s and ‘90s. There is also an equality and diversity aspect to this. For example, in West Yorkshire people from ethnic minority groups are strongly represented in carbon intensive sectors.

2.37 Overall, the transition to net zero presents significant economic challenges and opportunities. The decarbonisation of the economy will require a substantial increase in employment in key sectors and this will have important skills implications. There is also an opportunity for West Yorkshire to capitalise on existing strengths in areas like manufacturing and finance. The shift away from carbon-intensive activities presents challenges for economic inclusion.

Conclusion

2.38 This supplementary evidence reinforces the picture of long-standing challenges facing West Yorkshire, including under-performance on productivity, economic imbalances within the regional economy and relatively low levels of labour force participation. In addition to this there are further disruptions examined by this paper relating to remote working, artificial intelligence and the transition to net zero which will have a far-reaching impact on economic prospects and economic inclusion. These, along with further challenges and opportunities considered within the wider evidence base will be addressed through the economic strategy.

3. Tackling the Climate Emergency Implications

3.1 The report considers the implications for West Yorkshire's green economy arising out of the transition towards net zero. This will be explored further in the Economic Strategy as it is developed.

4. Inclusive Growth Implications

4.1 As part of its core purpose the Economic Strategy will set out a pathway to a more inclusive economy in West Yorkshire.

5. Equality and Diversity Implications

5.1 Promotion of equity and diversity in West Yorkshire is central to the Economic Strategy. It will consider how current inequalities and barriers can be tackled as part of the process of unlocking stronger economic growth in West Yorkshire.

6. Financial Implications

6.1 There are no financial implications directly arising from this report.

7. Legal Implications

7.1 There are no legal implications directly arising from this report.

8. Staffing Implications

8.1 There are no staffing implications directly arising from this report.

9. External Consultees

9.1 No external consultations have been undertaken.

10. Recommendations

10.1 That the Economic Scrutiny Committee notes this additional evidence with a view to informing the discussion around the content of the emerging Economic Strategy.

11. Background Documents

None.

12. Appendices

None.