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SPATIALLY REBALANCING THE UK ECONOMY: THE NEED FOR A NEW POLICY MODEL



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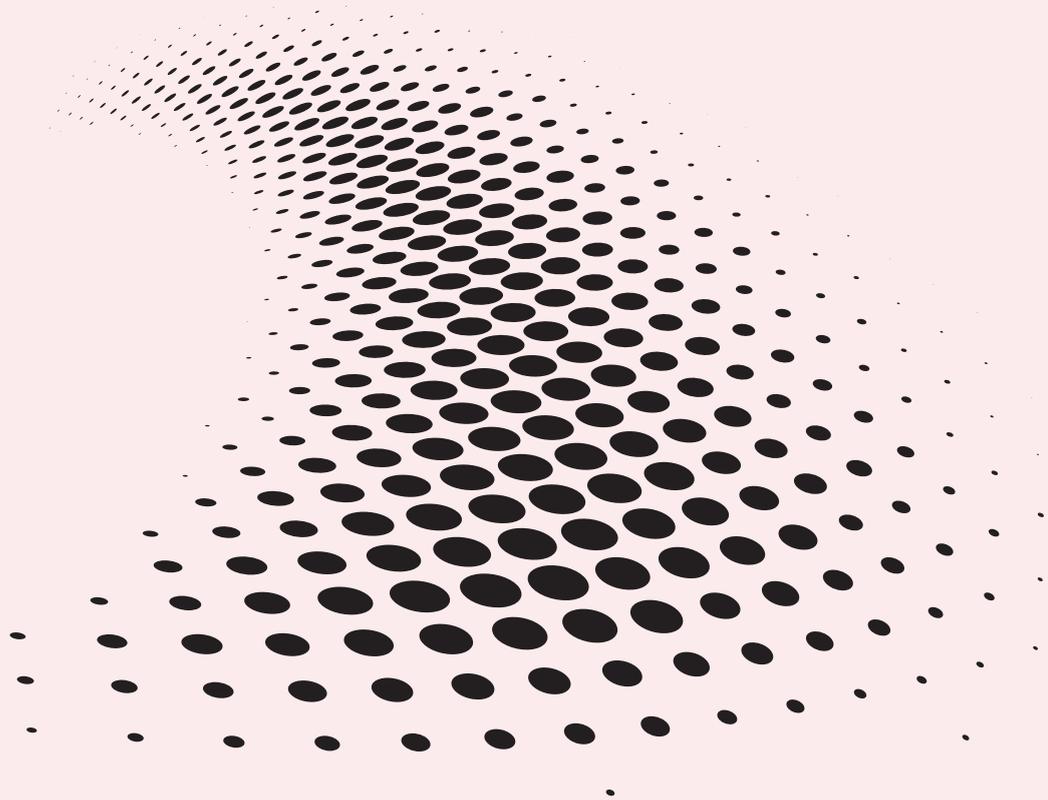
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SUMMARY

- The recent political concern over spatial economic imbalance in the UK is a rediscovery of a much longer standing problem that goes back a century or more, but which has intensified over the past three decades
- Regional disparities in economic performance in the UK are now greater than those found in any other European country
- The UK has had regional policies for nearly ninety years, but these have struggled to reduce spatial economic imbalance across the country
- This experience suggests that such policies have been based on an incorrect or inadequate diagnosis of the causes of that imbalance
- The rise of a 'new spatial economics' has challenged previous explanations of uneven regional and local economic development, and has highlighted the importance of spatial agglomeration, urban density, 'spatial sorting' of workers, and the dismantling of planning restrictions as key to urban and regional economic growth
- However, the approach is suspicious of policy intervention to secure greater spatial balance, and argues that, apart from freeing up planning, people-based policies are more effective than place-based policies
- In some variants, spatial imbalance is not only seen as economically efficient but also an equilibrium outcome
- While such ideas have more recently been used to argue for a major metro-region 'powerhouse' in northern England to rival London, they neither provide a comprehensive account of spatial economic imbalance in the UK as a whole, nor a convincing basis for reducing that imbalance
- Ultimately, spatial economic imbalance in the UK has to do with the progressive concentration of economic, political and financial power in London and its environs. The UK has one of the most centralized systems of public finance, policy-making and political control among OECD nations
- The UK's northern areas have the underlying potential to 'turn around' from the decline of their industrial base but this will require a step change in the level and control of the resources that are made available to them
- No significant or lasting reduction in spatial economic imbalance will be achieved without 'decentering' the key institutional structures that make up the UK's national political economy, involving:
 - The decentralisation and devolution of large sections of public finance to a new system of 'federated' regions or city-regions, going beyond the fiscal evolution suggested by Lord Heseltine
 - An explicit machinery within government to influence and monitor the spatial impact of central government expenditures and policies
 - New regions or city-regions as the key units of spatial economic governance, and locally accountable as such
 - The establishment of a national investment bank with a regional or city-regional organizational structure, which would focus explicitly on raising capital for SMEs, advanced manufacturing and infrastructure in the regions and city-regions
 - Reform of the UK tax system to align the objectives of spatial and sectoral rebalancing, for example through new instruments such as 'Advanced Manufacturing Bonds' with favourable tax treatment to increase the flow of funds into advanced manufacturing
 - A commission or similar formal body to be established to consider how best to achieve this spatial decentering of the national political economy, what the appropriate territorial units should be, and the powers they should have

1 INTRODUCTION: AIMS AND SCOPE

There is currently much interest in spatially rebalancing the UK economy, both at central government level and within the major cities, regions and nations of the country.¹ This pamphlet seeks to stimulate debate on this issue, with the aim of informing political discussion in the run-up to and aftermath of the UK General Election in May 2015. It begins by emphasizing the extent and persistence of spatial economic imbalance in the UK in its historical and international contexts, and the corresponding scale of the rebalancing challenge. It then examines what has become the prevailing academic view about the spatial structure of the UK's economy – a view that has been highly influential in government policy circles – and argues that this approach, though providing some useful insights, is rather limited as a basis for policies aimed at redressing that spatial imbalance. The pamphlet then goes on to argue that a fundamental rethink is needed both of the causes of spatial economic imbalance in the UK, and the nature and scope of spatial policy. The ongoing constitutional changes affecting Scotland as well as Wales and Northern Ireland, and the emerging call for devolution of fiscal and other powers to cities and regions in England present both a need and a major opportunity to undertake such a rethink.



¹ See, for example, HMG (2010) *Local Growth: Realising Every Place's Potential*, HMSO: London; HMG (2011) *Unlocking Growth in Cities*, HMSO: London; City Growth Commission (2014) *Unleashing Metro Growth: Final Recommendations of the City Growth Commission*, RSA: London; ResPublica (2014) *Devo Max – Devo Manc: Place-based Public Services*, ResPublica: Manchester.

2 THE SCALE OF SPATIAL IMBALANCE IN THE UK

The current concern over spatial economic imbalance in the UK is but the rediscovery of a long-standing problem. Regional disparities in economic and social conditions have been an entrenched and persistent feature of the UK landscape since the middle of the 19thC.² For much of the post-war period, successive Governments adopted the view that such spatial disparities were economically and socially undesirable, and pursued policies aimed at reducing them. In the context of the recent economic crisis and slow recovery, the spatially imbalanced nature of the UK economy has attracted prominent political attention, both as a contributing cause of the crisis itself, and as a factor potentially inhibiting future economic stability. As Prime Minister David Cameron noted in 2010:

Our economy has become more and more unbalanced, with our fortunes hitched to a few industries in one corner of the country, while we let other sectors like manufacturing slide. Today our economy is heavily reliant on just a few industries and a few regions – particularly London and the South East. This really matters. An economy with such a narrow foundation for growth is fundamentally unstable and wasteful – because we are not making use of the talent out there in all parts of our United Kingdom. We are determined that should change. That doesn't mean picking winners but it does mean supporting growing industries – aerospace, pharmaceuticals, high-value manufacturing, hi-tech engineering, and low carbon technology. And all the knowledge-based businesses including the creative industries. And it doesn't mean ignoring London...but it does mean having a plan to breathe economic life into the towns and cities outside the M25.³

Imbalance and inequality have also prompted concern among the Devolved Administrations. As the Scottish Government's First Minister, Nicola Sturgeon, recently said:

London has a centrifugal pull on talent, investment and business from the rest of Europe and the world. That brings benefits to the broader UK economy. But as we know, that same centrifugal pull is felt by the rest of us across the UK, often to our detriment. The challenge for us all is how to balance this in our best interests – not by engaging in a race to the bottom, but by using our powers to create long-term comparative advantage and genuine economic value.⁴

The scale of spatial economic imbalance in the UK has in fact been growing since the late-1970s, though it accelerated during the 1980s, and continued to increase in the 1990s and the debt-driven boom of the first decade of the 2000s (Figures 1 and 2). The geography of spatial imbalance has frequently been characterized as a 'North-South Divide' and, while this sobriquet is a simplification and has been much debated, the broad divergence between these two major areas is incontrovertible (Figure 3). And while London lagged in terms of growth up to the beginning of the 1990s, it then underwent a dramatic 'turnaround' to become the fastest growing region in the country (Figure 3).⁵

Further, the scale of spatial imbalance in the UK has increased faster than in other major European countries. The increase in the disparities in regional shares of GDP in the UK has far outstripped that in France, Spain, Italy and Germany, and also (at state level) that in the United States (Figure 4).

A number of arguments have been put forward to justify the view that at least some degree of greater spatial balance is desirable across the UK. The social argument has been relatively straightforward. Relatively slow-growing regions that fail to generate sufficient jobs for their residents tend to export their population to other regions through outward migration. Sustained outward migration, often by those who are the most enterprising, qualified and skilled, is ultimately very damaging to the economic potential and social cohesion of the origin regions.⁶ Since 70 percent of the UK's population live outside London and the South East, it would seem less than desirable that the preferred option is that those who cannot find work elsewhere should simply move to these latter two areas. Constraints on such labour mobility are well-known and rooted in the housing and labour markets, pensions system and social ties.⁷

² See, for example, Crafts, N. (2005) Regional GDP in Britain, 1971-1911: Some Estimates, *Scottish Journal of Political Economy*, 52, 54-64.

³ Cameron, D. (2010) *Transforming the British economy: Coalition strategy for economic growth*, Transcript of Speech, Prime Minister's Office.

⁴ Sturgeon, N (2014) Speech to Scotland's Business Sector, SSE Business Offices, Glasgow, Scottish Government 1 December, 2014.

⁵ For an analysis of how London has become increasingly detached from the rest of the UK economy, see Harvey, D. (2013) *London and the UK: In for a Penny, In for a Pound*, Special Report, Deutsch Bank, London.

⁶ See Rowthorn, R.E. (2010) Combined and Uneven Development: Reflections on the North-South Divide, *Spatial Economic Analysis*, 5, 363-388.

⁷ Owen, D. W. and Green, A. E. (1989) Spatial aspects of labour mobility in the 1980s, *Geoforum*, 20, 1, 107-126.

Figure 1: Regional Cumulative Percentage Point Differential Growth Gaps of GVA (2011 prices), 1971-2013

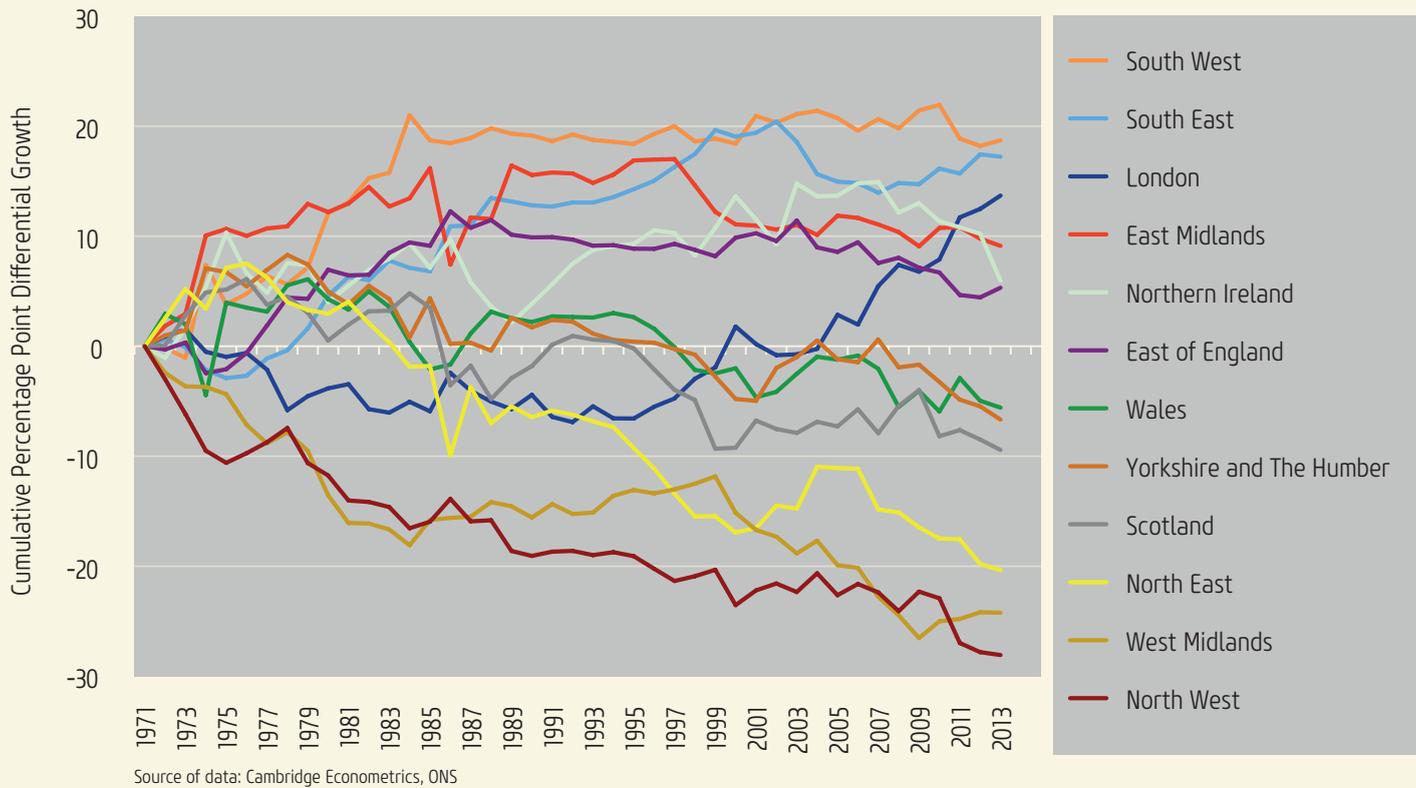


Figure 2: Regional Cumulative Percentage Point Differential Growth Gaps in Employment, 1971-2014

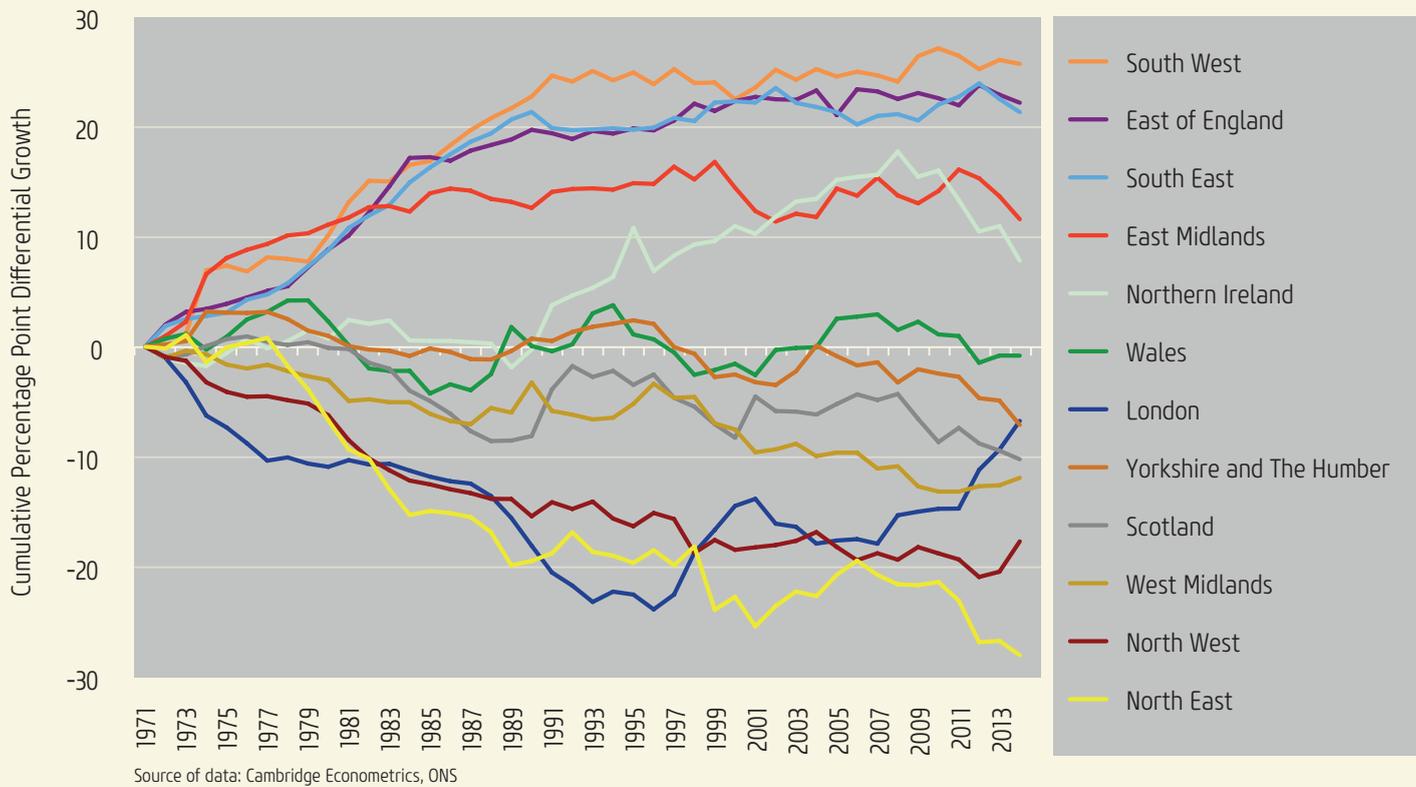


Figure 3: Cumulative Percentage Point Differential Growth Gaps of GVA (2011 prices): The North, South and London, 1971-2013

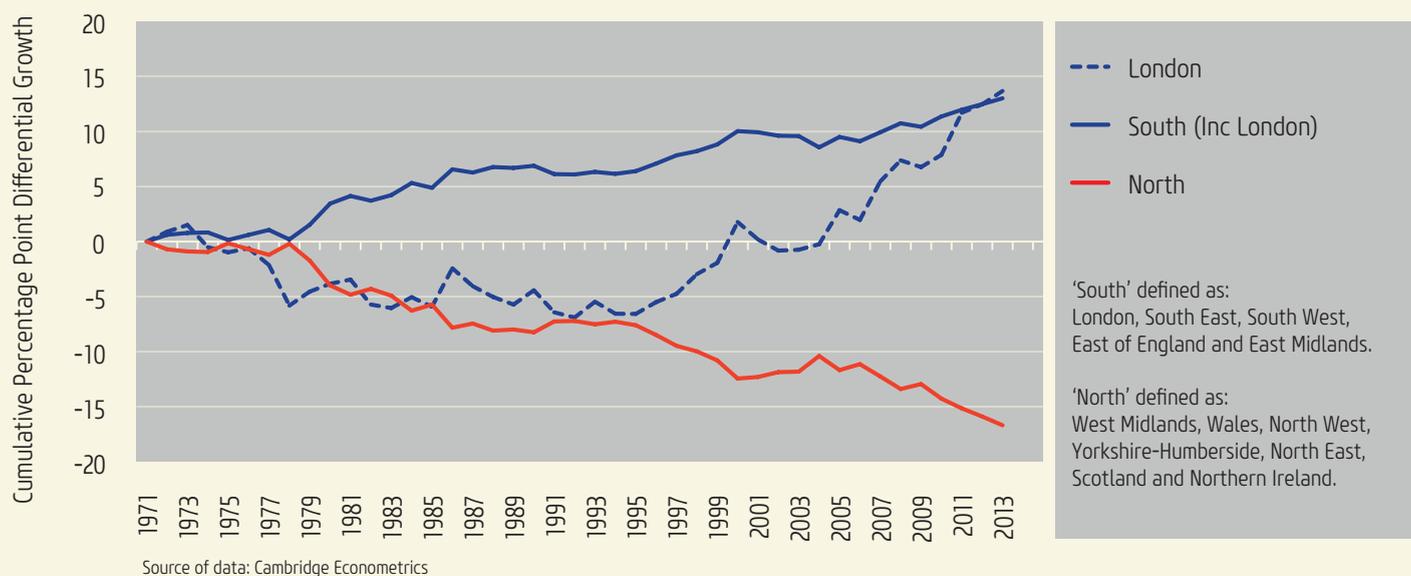
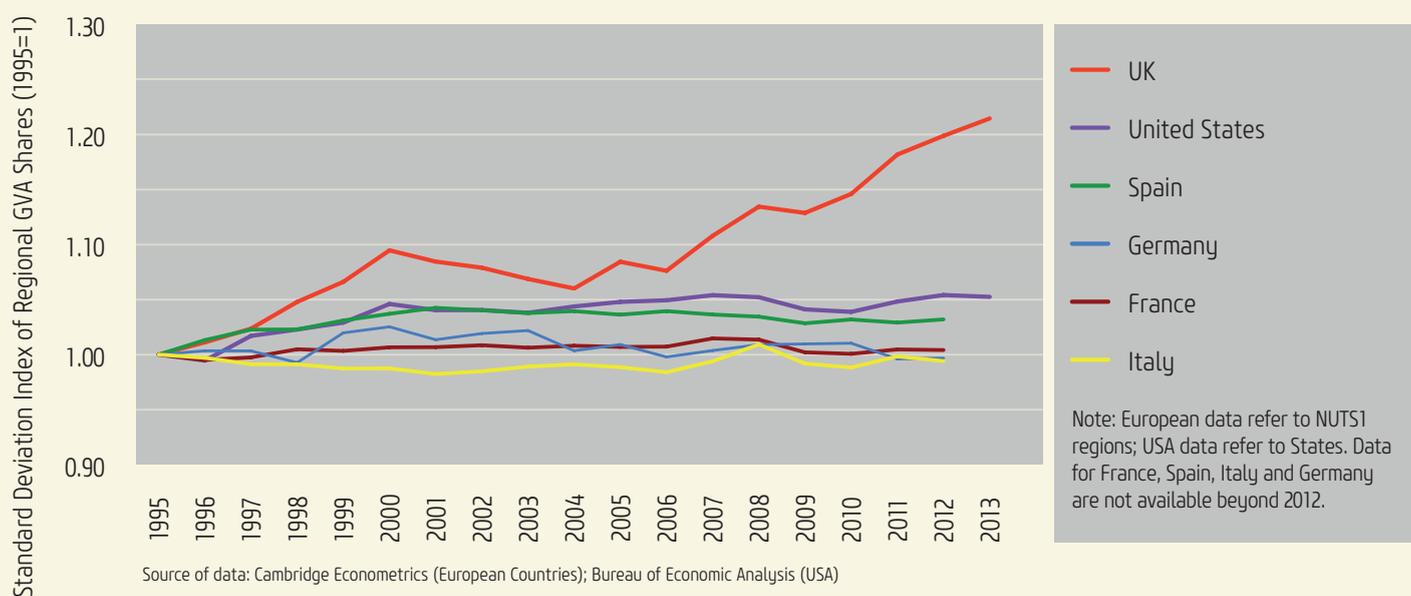
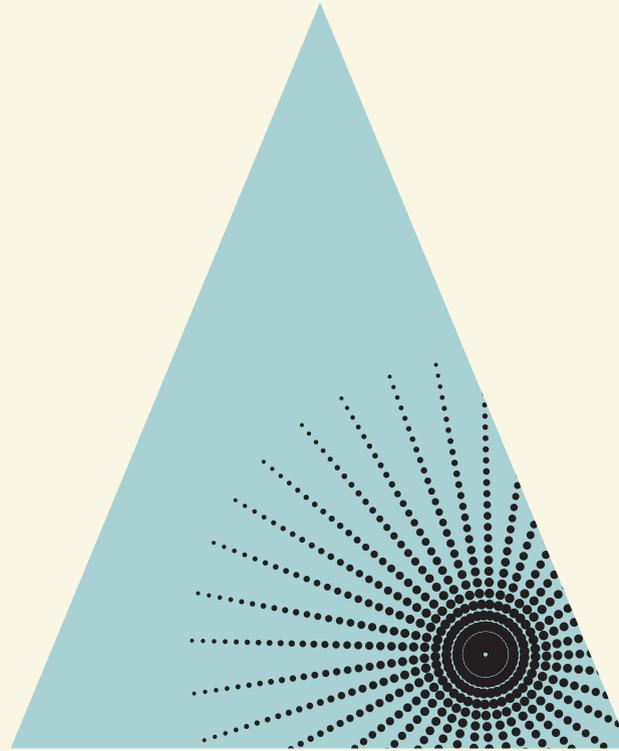


Figure 4: Spatial Imbalance in the UK and other Major European Countries Compared, Indexed Standard Deviation of Regional Shares of National GVA, 1995-2013





The economic efficiency argument has been that a more spatially balanced and even distribution of demand across the country enables the UK's resources to be used in a way that is more conducive to sustainable national growth. A more even rather than concentrated geographical distribution of economic activity also lowers the inflationary pressures in factor markets that would otherwise curtail national growth.⁸

Whether based on the social equity argument or the national efficiency rationale, the UK has had some form of regional policy aimed at securing a more spatially balanced pattern of growth and prosperity for close on 90 years. Yet spatial disparities across the economy have not only persisted, but have actually widened over the past three decades. There are various possible reasons for this lack of impact. First, it could be that since their inception seventy years ago post-war regional policies have never been pursued with sufficient vigour and intensity, that the requisite levels of resources have never been committed. Alternatively, second, it might be argued that despite reasonable levels of commitment, the impact of regional policy has been consistently outweighed and counteracted by the effects of other, ostensibly 'non-spatial' policies, such as general government spending, fiscal and monetary policies, and the like, which have tended to favour south-eastern parts of the country – what Lord Heseltine back in the mid-1980s called 'counter-regional' policies. A third possible explanation is that the policies themselves have not in fact been the correct ones to begin with and that they have not been based on a coherent and convincing diagnosis and explanation of the spatial problem they were intended to solve. For much of the post-War period, the underlying theory was a kind of spatial Keynesianism, the belief that the cause of the problem was a lack of demand for the products and industries of northern regions. In the 1980s, the theoretical rationale shifted to a supply-side argument that the northern regions of the country were lacking in entrepreneurship, innovation and skills.

Over the past decade or so, the theoretical underpinnings of regional policy have shifted once again. One body of theory that has exercised significant influence in recent years on the UK government's approach to spatially rebalancing the national economy is the 'new spatial economics', a combination of ideas from the New Economic Geography (NEG) and the New Urban Economics (NUE). This set of ideas has become the prevailing conceptual framework, in as much that its basic arguments appear to lie behind much of the current Government's thinking about local growth.⁹ Yet whether it provides a more convincing and effective basis for solving the growing gap between the South and North of the country is debatable.¹⁰

⁸ Gardiner, B., Martin, R. and Tyler, P. (2011) Does spatial agglomeration increase national growth? Some evidence from Europe, *Journal of Economic Geography*, 11, 6, 1-28.

⁹ See for example, HM Government (2010) *Local Growth: Realising Every Place's Potential*, Cm 7961, London: The Stationery Office. Also, Government was a co-founder and co-funder of the LSE-based Spatial Economics Research Centre, whose research work is firmly NEG and NUE in orientation, and intended to provide theoretical support to Government thinking on the spatial structure of the national economy.

¹⁰ There is of course a large corpus of research in what we can broadly call 'regional studies' that does not subscribe to NEG or NUE, and which has somewhat different explanations of uneven regional growth and development. Here a whole plethora of ideas and concepts has appeared in recent years, from clusters, to regional innovation systems, to production networks, to smart specialisation, to local leadership, to name but some, many such concepts also being used to draw policy implications. The shortcoming with this literature, however, is that it lacks synthesis and integration, so

that policy discussions become largely a matter of local 'pick and mix'. Certainly, as yet it fails to offer either a coherent account of the UK's long-standing problem and pattern of spatial economic imbalance, nor a convincing framework for redressing that imbalance (see Martin, R.L., 2015, *Rebalancing the Spatial Economy: The Challenge for Regional Theory*, paper presented at the Regional Studies Association Winter Conference, London, November 2014; submitted to *Territory, Politics and Government*).

3 SPATIALLY REBALANCING THE ECONOMY: THE LIMITATIONS OF THE PREVAILING THEORETICAL FRAMEWORK

Although NUE and NEG differ in their precise focus and arguments, they share a number of common features, assumptions and principles. For example, both types of model draw heavily on the notions of increasing returns and external economies of agglomeration, are predicated on the inevitable spatial unevenness of the geographical distribution of economic activities, and both operate with an equilibrium view of economic life. NEG-type models deal with the trade-off between forces making for the spatial agglomeration and concentration of economic activity on the one hand, and the spatial dispersal of activity on the other. Increasing returns promote agglomeration, while congestion costs and market crowding effects tend to work in the other direction, promoting spatial dispersion. The relative strength of these effects, together with the degree of firm and worker mobility and the costs of transport, determine the eventual spatial outcome, which furthermore is an equilibrium outcome. In principle, according to the value of the relevant parameters that capture these various effects, NEG models can predict a spatially balanced economic landscape (with activity equally distributed between regions). However, this particular equilibrium is not overly stable, and there is an inbuilt bias in these models to predict spatial economic imbalance, with economic activity agglomerated in just one or a few regions.

In NUE models, the focus is very much on the benefits and advantages that accrue from the *density* of activity and population within cities: density is claimed to increase interaction, spill-overs, market opportunities, productivity and wages. Particular emphasis is put on the agglomeration of human capital: a city's success depends on having a highly skilled and well-educated workforce, and the more successful is a city (in terms of high wages, high productivity and so on) the more it will be a magnet in attracting such workers. Agglomeration again plays a central role, as a source of key increasing returns and external economies effects that raise the productive performance of firms and workers in a city and its hinterland. Furthermore, NUE theorists view the spatial agglomeration of economic activity primarily as a market-led process, the outcome of the spatial 'sorting' of rational and highly mobile workers in possession of perfect information towards the more productive, higher-wage city-regions. The argument is that once 'individual' effects (such as the education, skill and occupation) of workers are 'controlled' for, 'place' effects are negligible, and real spatial economic disparities (in real product wages for example) all but disappear. Thus according to one such analysis:

our general finding is that most of the observed regional inequality in average wage in Britain is explained by 'sorting' or 'people' rather than 'places'. Our preferred estimates, which include the individual fixed effects, suggest that the contribution of individual characteristics to variation in wages is between 100 to 850 times larger than the contribution of area effects (Gibbons et al. 2011; 760).¹¹

The attraction of NEG and NUE models to national (and some local) policy makers is perhaps not surprising. They suggest that market forces, as they are captured in such models, need not lead to spatial economic balance, but to the natural spatial agglomeration of economic activity, and that such an outcome is not only an equilibrium one, but one that raises national economic performance, provided congestion costs do not outweigh the increasing return effects of agglomeration.

As an internal UK Treasury paper put it:

Theory and evidence suggests that allowing regional concentration of economic activity will increase national growth. As long as economies of scale, knowledge spillovers and a local pool of skilled labour result in productivity gains that outweigh congestion costs, the economy will benefit from agglomeration... policies that aim to spread growth amongst regions are running counter to the natural growth process and are difficult to justify on efficiency grounds, unless significant congestion costs exist (HM Treasury 2007: 20, emphasis added).¹²

¹¹ Gibbons, S., H. G. Overman and P. O. Pelkonen (2011) Area disparities in Britain: understanding the contribution of people versus place through variance decompositions, *Oxford Bulletin of Economics and Statistics*, 76 (5), 745-763.

¹² HM Treasury (2007) *Regional disparities and growth in Europe*, Mimeo (author C Lees), HM, Treasury, London.

A further acceptance of this view is evident in the more recent UK Government paper on *Understanding Local Growth*, which develops its arguments firmly on the basis of NEG theory:

This new understanding [the New Economic Geography] of how economics works across space also alters the expected equilibrium. As both people and firms move to areas of high productivity there will be no simple convergence of productivity levels. Even with fully functioning markets, there can be an uneven distribution of economic performance, and persistent differences that are not necessarily due to market failure (Department of Business, Innovation and Skills 2010: 23).¹³

There is no doubt that the NEG and NUE-type thinking that gives rise to such views can be highly persuasive, and difficult to contest. NEG models have a mathematical exactitude and quantitative elegance that impresses policy-makers anxious for robust and 'hard' evidence upon which to make decisions, and which differs sharply from the less quantitative, often more narrative and qualitative based approaches that are frequently found in regional studies and economic geography, and which tend to be dismissed by the new spatial economists as lacking rigour and robustness. Further, NEG-type models have the advantage of being employed to conduct 'what-if' type analyses, for example predicting the likely outcome of major infrastructural investments in lagging regions or improvements to the connectivity between cities – such as the controversial High-Speed 2 rail project linking London with Birmingham, Manchester and Leeds. And it is easy to see how the ideas from the new spatial economics can be harnessed by policy-makers to argue for more agglomeration – both in London itself, and as the justification for a 'northern metro-region powerhouse' (Manchester-Leeds-Sheffield-Liverpool) of the sort championed by the Chancellor of the Exchequer and City Growth Commission.

Yet, notwithstanding its undoubted power, some crucial questions surround this prevailing spatial economics framework. It may be that some of the predictions of NEG and NUE models accord with certain empirical facts about the UK's economic landscape. But do these models offer a full and credible explanation of the problem of spatial economic imbalance?¹⁴ Do the economics of agglomeration in any case capture the fundamental causes of the UK's spatially unbalanced economy? Are there limits to the benefits of agglomeration? Would the promotion of a 'northern metro-region' of a critical mass and scale to act as an economic counterweight to London be sufficient, of itself, to deliver a more spatially balanced economy? What about other cities, regions and nations in the UK?

Although NEG theory acknowledges that as the spatial agglomeration of economic activity increases so congestion and related costs may come into play, relatively little is known about such costs, or when they offset the benefits of agglomeration. Indeed, there is a tendency either to ignore such costs, or to assume that UK cities could expand appreciably before these costs would outweigh the benefits of agglomeration. So it has been argued that most of the UK's second-tier cities (such as Manchester, Glasgow, Sheffield, Liverpool, Birmingham and Newcastle) are underperforming precisely because they are 'too small'.¹⁵ It is even argued that London itself should be bigger.¹⁶ In relation to the latter, it is also argued that the very high costs of working and living in London are due not to congestion and other negative externalities associated with agglomeration, but mainly due to restrictive planning rules which have constrained the supply of housing and land – in other words to failures arising from interfering with the free working of factor markets.¹⁷

Yet again, while it is the case that productivity tends to increase with size of city, there may be limits to this relationship. Likewise, increasing the density of activity within city-regions may not necessarily produce the expected productivity gains. For example, empirical studies for the USA and for Europe indicate that, typically, a doubling of local employment or population density increases local productivity by between 2-6 percent; very few studies find an increase of 10 percent or more.¹⁸ This seems a very modest effect indeed. To add to this overwhelming finding, Krugman, the prime architect of NEG, has himself begun to question the force and benefits of increasing returns effects associated with the spatial agglomeration and concentration of economic activity:

there's good reason to believe that the world economy has, over time, actually become less characterised by the kinds of increasing returns effects emphasized by new trade theory and new geography. In the case of geography, in fact, the peak impact of increasing returns occurred long before the theorists arrived on the scene (2009: 569).¹⁹

¹³ BIS (2010) *Understanding Local Growth*, BIS Economics Paper No. 7, October, BIS: London.

¹⁴ Martin, R.L. (2011) The 'New Economic Geography': Credible Models of the Economic Landscape? In Leyshon, A., Lee, R., McDowell, L. and Sunley, P. (Eds) *The Sage Handbook of Economic Geography*, London: Sage, pp. 53-71.

¹⁵ Overman, H. (2012) Are Britain's 'Second Tier' Cities Too Small?, SERC Blog, 12 October.

¹⁶ Ganesh, J. (2015) Disunited kingdom: London in a world of its own, *The Financial Times*, 2 March, The Financial Times: London.

¹⁷ Cheshire, P. and Hilber, C. (2008) Office Space Supply Restrictions in Britain: The Political Economy of Market Revenge, *Economic Journal*, 118, 529, 185-221.

¹⁸ See, for example, Ciccone, A. (2002) Agglomeration Effects in Europe, *American Economic Review*, 46, pp. 213-227; Rappaport, J. (2007) Consumption Amenities and City Population Density, *Research Working Paper 06-10*, Federal Reserve Bank of Kansas City; Abel, J.R., Dey, I and Gabe, T.M. (2011) Productivity and the Density of Human Capital, *Staff Report No 444*, Federal Reserve Bank of New York.

¹⁹ Krugman, P. (2009) The New Economic Geography, Now Middle-Aged, *Regional Studies*, 45, pp. 1-7.

What of the NUE idea that the increasing agglomeration of economic activity in London and the surrounding South East is but the outcome of a market-driven 'spatial sorting' of workers, and that place effects are all but irrelevant? Of course workers will move to where jobs are more plentiful and wages higher. This is hardly a novel finding. In this sense, people obviously make places. But to argue that place exerts no influence on people seems too simplistic, regardless of the sophistication of the techniques used to arrive at that conclusion. People and place effects interact in complex, historically and culturally constituted ways. Places – their inherited economic, educational, physical, environmental and social structures – shape the opportunities available to local residents, whose qualities then feed back to influence these same structures. A high-skill and dynamic local economy will tend to produce the spill-overs and institutional and cultural forms that reinforce that locality's high-skill environment; and conversely in a low-skill less-prosperous local economy. Disentangling the relative contributions of people- and place-based effects is extraordinarily difficult, and tends to miss the point. Place-based policies can benefit local people, just as nationwide people-based policies can have widely varying outcomes from place to place. And people move to particular areas not just for jobs or higher wages, but also because those places are pleasant locations in which to live: they have attractive physical, public, environmental and cultural assets. Krugman has argued that there is a case for place-based policies; for example, he suggests that the local provision of high quality education institutions and infrastructures – key components of what he calls locally-specific 'fundamentals' – can indeed be a valid focus of regional and urban policy.²⁰

Our concern with the prevailing interpretive framework used to analyse the UK's spatial economy, and which has informed much central (and some local) government policy thinking in recent years is not so much that it is preoccupied with the benefits of agglomeration, but that it has an overly economic view of agglomeration. The problem is that NEG and NUE models are essentially 'placeless': they are abstractions whose mathematical forms are largely context and history free, strangely disconnected from the concrete national political economy within which they are applied and used. Context and history are, however, crucial.²¹

Think back to the UK's economic landscape in the second half of the 19th century. Our northern cities and regions, together with London, were centres of industrial growth and innovation, the engines of Victorian economic success. The UK had a regional banking system, a system of regional stock markets, and local municipal councils (powerful ones in the case of the big cities) funded mainly by local taxes. What has happened over the past century? Our banking system became increasingly centralised in just a handful of banks, all headquartered in London; the regional stock markets became absorbed by the London Stock Exchange; local authority funding has become overwhelmingly controlled by central government in London for England, and by the Devolved Administrations in Edinburgh, Cardiff and Belfast for Scotland, Wales and Northern Ireland respectively. The centralization of political and financial power, as well as national economic policymaking in the UK capital is echoed (to a lesser extent) at a lower level by the centralizing tendencies of government and policymaking in the devolved capitals at the expense of local government. Widely demonstrated and recognised across research and policy circles²², the UK is now one of the most spatially centralised nations, politically, financially and economically, in the OECD group.²³

And, in political terms, the limits of what can be achieved to address economic and social development within such a centralized and dysfunctional system are being recognized across the political spectrum.²⁴ The progressive self-reinforcing agglomeration of the main institutions and levers of our national political economy configures and explains much of the wider problem of spatial economic imbalance with which we are now confronted.

Of course the success of London brings benefits to the rest of the country, although measuring the precise 'economic balance sheet' between London and the rest of the UK is hampered by the lack of data on the flows of trade and finance between the nations, regions and cities of the country. The fact is, of course, that economic growth is not some simple 'spatial zero-sum game'. There is not some fixed amount of economic growth or activity that can be distributed across the UK space economy. It is not a case of holding back prosperous areas like London and the Greater South East in order to promote activity in the less prosperous cities and regions of the country. But it is a matter of ensuring that the less prosperous regions and cities are able to realize their full economic potential. To do this they need proper and fair access to the public and private resources necessary to gain a 'second wind' of more sustainable growth and development, to use Krugman's graphic phrase.²⁵ And this means that there is a need to examine the extent to which economic, financial and political power – at UK level – is too centralised and concentrated in London; whether the 'economic playing field', far from being level, is too tilted in London's favour. The challenge for policy is that spatial economic imbalance in the UK has itself become institutionalised in our national political economy. Appealing to the narrow economics of agglomeration alone is not likely to address the more fundamental and systemic causes of our spatially unbalanced economy.

²⁰ Krugman, P. (2005) Second winds for industrial regions? in D. Coyle, W. Alexander and B. Ashcroft (Eds.) *New Wealth for Old Nations: Scotland's Economic Prospects*, Princeton University Press: Princeton, 35-47.

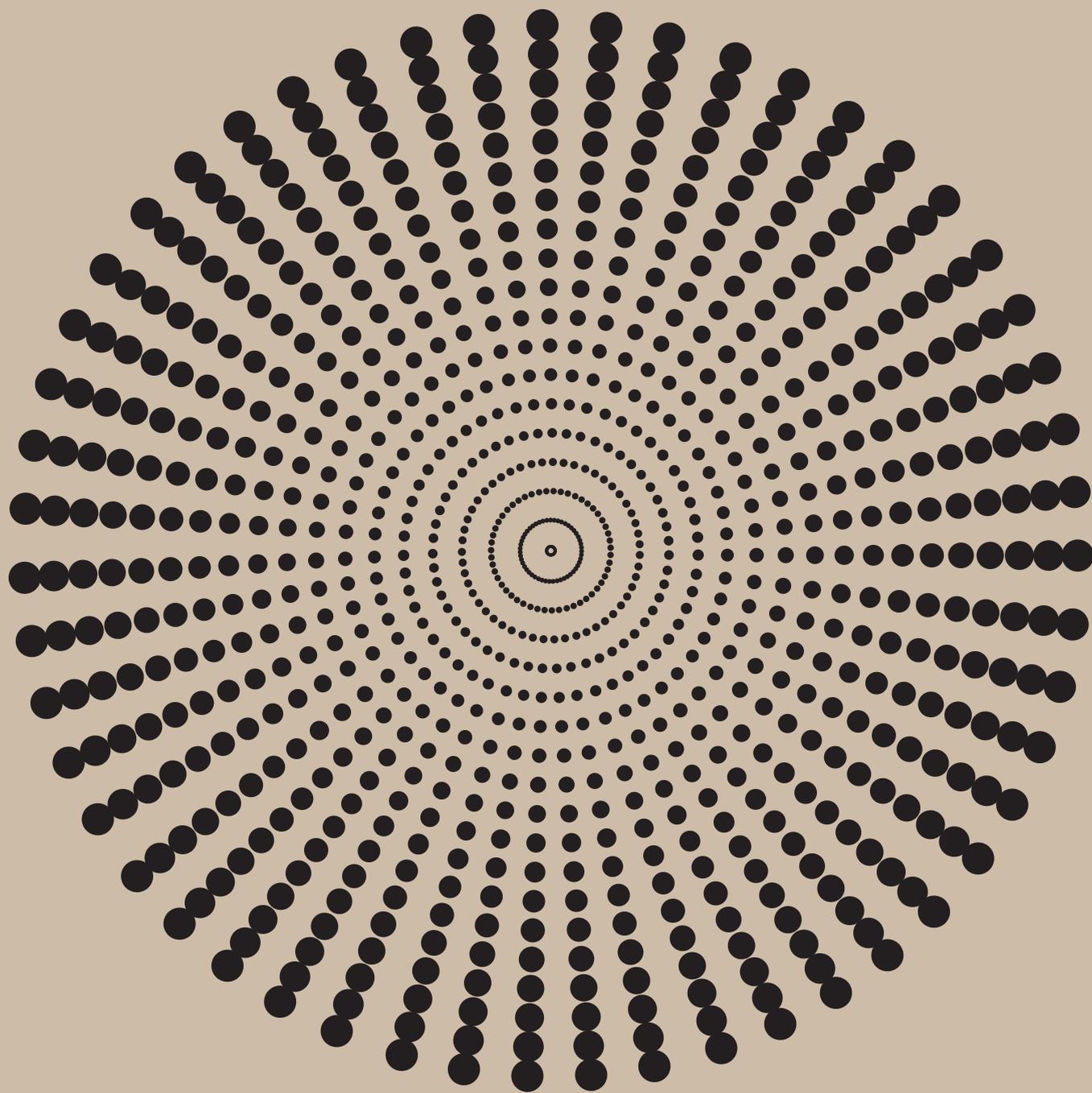
²¹ Garretsen, H. and Martin, R. (2010) Towards more credible (new) economic geography models: taking geography and history seriously, *Spatial Economic Analysis*, 5, 127-160.

²² See, for example, Communities and Local Government Committee (2014) *Devolution in England: The Case for Local Government*, HC 503, House of Commons: London and London Finance Commission (2014) *Raising the Capital*, London Finance Commission: LSE.

²³ OECD (2014) *Regional Outlook 2014*, OECD: Paris.

²⁴ See, for example, HMG (2014) *The Implications of Devolution for England*, December, HMG: London, Geoghegan, J. (2014) Lib-Dems 2014: City-regions and counties best devolution model, says Communities Minister, *Planning Resource*, 7 October; Ferguson, M. (2014) Miliband unveils plans for 'English Devolution Act', *LabourList*, 31 Oct.

²⁵ Krugman, P. (2005) Second winds for industrial regions? in D. Coyle, W. Alexander and B. Ashcroft (Eds.) *New Wealth for Old Nations: Scotland's Economic Prospects*, Princeton University Press: Princeton, 35-47.



4 TOWARDS A NEW POLICY MODEL

What is needed is a thoroughgoing reassessment of the UK's spatial political economy. This would not eschew the significance and role of such processes as agglomeration, but would place these within an interpretative framework that assigns key importance to the form, operation and spatial organisation of the nation's core institutions, governance structures, political arrangements and policy-making machinery. Spatially rebalancing the UK economy is not just about (yet) another round of spatially-focused policy programmes and initiatives seeking to promote the advantages of agglomeration in cities outside London, better co-ordinating economic and spatial planning between the constituent parts of the UK, boosting innovation in the regions, or improving the infrastructures of city-regions outside the south of England, necessary and important though such interventions might be.²⁶ At this potentially decisive moment, it must also be about more fundamental change, about the need to undertake a long-overdue spatial rebalancing of the nation's institutional and governance architectures.

To put the issue simply, the critical task is to *spatially decentre the power structures that drive and manage economic growth and development*. As we have argued above, those structures have become increasingly concentrated in, orientated towards, and controlled from London and its environs. Unless we have a greater spatial balance in those structures, the national economy itself will remain spatially unbalanced. The solution, we suggest, is a long overdue introduction of a federal or semi-federal model of economic and fiscal governance. Some version of regional or city-regional federalism is increasingly the norm in almost all other western advanced economies. Many European countries moved in this direction from the 1980s onwards.²⁷ Although the UK has moved down the path of devolved powers for Scotland, Wales and Northern Ireland and London since the late 1990s, it has failed to develop the kind of institutionalised frameworks used in federal systems (e.g. Austria, Germany, Switzerland) or countries with devolved systems of government (e.g. Italy, Spain) to coordinate policy objectives and instruments for territorial imbalance across the constituent parts of the UK.²⁸ Further, the devolution process has failed to attenuate the highly centralised fiscal and governance structure in England.

However, an historic and potentially formative opportunity is opening up. Further constitutional change in Scotland, with the promise of more devolution of fiscal and policy powers, has been initiated by the Smith Commission, and new powers have been announced for Wales. This has encouraged new thinking in England about moving beyond the increasing plethora of largely uncoordinated local and city-based initiatives introduced in recent years (such as the LEPs, the Local Growth Fund, the new Enterprise Zones, and the City Deals) towards a new spatially devolved model of economic development. Already in 2012 Lord Heseltine argued for the devolution of £49 billion of central Government spending each year. The Chancellor's idea of stimulating a 'northern powerhouse' based on the 'super metro-region' of Liverpool-Manchester-Leeds-Sheffield has itself stimulated a call for 'metro-devo' not only by Greater Manchester, but also by other cities. Both the Coalition Government and the Labour Party (if elected in May 2015) have committed to devolving control over limited public monies to Manchester.

Together, these developments suggest that constructing a new spatially devolved model of political-economic governance within the UK is emerging. However, while they are steps on the right direction, this movement has all the hallmarks of *ad hoc* policy development and piecemeal reform, in which some nations, regions or local areas might be granted certain devolved powers while others will not – a highly uneven, unequal and potentially unstable and divisive settlement that may do more to promote further spatial imbalance rather than work towards ameliorating it. We could all too easily end up with a geographically chaotic and divisive system, an outcome unfortunately all too characteristic of the tradition of 'muddling through' in how policy initiatives and reforms tend to be managed in the UK. Rather, what is needed is a coherent and comprehensive UK-wide strategy and long-term plan for addressing spatial imbalances that recognises the new constitutional realities with respect to the Devolved Administrations, and which also offers decentralisation to regions or city-regions in England within a federal territorial structure that covers the whole of the UK.

There is no space here to set out such a proposal in full detail. Rather, our focus is what seems to us to be some foundational issues, or building blocks, in relation to such a structure, namely: decentralizing and devolving governance, institutionalising spatial economic balance as a policy objective, decentralizing public administration, fiscal devolution, and establishing a national regionally-organized investment bank.

²⁶ Bailey, D., Hildreth, P. and de Propris, L. (2015) Mind the Gap! What Might a Place-based Industrial and Regional Policy Look Like? In D. Bailey, K. Cowling and P. Tomlinson (Eds.) *New Perspectives on Industrial Policy for a Modern Policy*, Oxford University Press: Oxford; Northern Economic Futures Commission and IPPR North (2012) *Northern Prosperity is National Prosperity: A Strategy for Revitalising the UK Economy*, IPPR North: Newcastle.

²⁷ See Harvie, C. (1994) *The Rise of Regional Europe*, London: Routledge.

²⁸ Examples of such frameworks include the Federal-State Joint Task 'Improvement of Regional Economic Structure' (Germany), the standing Spatial Development Coordination Conference (Austria), and the Federal-Canton coordination functions of the State Secretariat for Economic Affairs (Switzerland).

4.1 Decentralising and devolving governance in England

The asymmetrical and uneven nature of governance arrangements in the UK is acute. Enhanced decentralisation of the UK's centralised governance system in England, could provide the greater freedoms, flexibilities, resources and fiscal capacity required to enable meaningful decisions to be made and funded at appropriate scales. Some kind of road map for decentralisation in the UK would be beneficial to the spatial rebalancing agenda. The road map could outline the vision, direction and speed of travel and address the limitations of the current ad hoc, piecemeal and uneven deal-based approach. The current approach has created uncertainty, generated short-term demands for governance bodies and partners to articulate their propositions, underpinned perpetual reorganisation and only modestly begun to change the structures and cultures of centralisation ingrained in UK political economy. Such an initiative could build upon the UK House of Commons Political and Constitutional Reform Committee's current enquiry into the future of devolution in the UK in the wake of the Scottish independence referendum result and the revived interest in a federal UK.²⁹

A basic question, of course, concerns the most appropriate geographical basis for such devolution or decentralisation. Ideally, the spatial units should be functional economic regions, but practically would need to be built up from existing administrative areas. The former eight English Regional Development Agencies (RDAs), which were based on Government Office Regions, were abolished by the Coalition Government partly on the very grounds that they did not represent meaningful economic units and were too large and unaccountable.³⁰ The thirty-nine Local Enterprise Partnerships, based on groupings of local authority districts, that have been established in place of the RDAs as the basis for the Government's Local Growth Agenda, are supposed to be more meaningful in economic terms. But many of the LEPs are no more functionally meaningful than the former RDAs, many are somewhat arbitrary alliances, several of them overlap, and many are too small. An alternative approach is to think in terms of city-regions, or what in most cases would be regional groupings (systems) of interconnected cities and their surrounding hinterlands. The emerging 'metro-region' of Liverpool-Manchester-Leeds-Sheffield may well be one such. *But the challenge is to partition the whole of the UK into economically meaningful city-regions and associated hinterland areas.* The City Growth Commission (2014) has identified some 15 major cities across the UK that could be the cores or joint cores of surrounding linked regions for governance, fiscal and economic policy purposes.³¹ But this proposal would leave much of the East of England and South West regions without such units. What is needed is a thorough-going enquiry into how best to define and delineate a nation-wide system of city-regional areas that could function as a devolved governance structure capable of controlling total local public spending, with legal powers to enact joined-up government, power over local property taxes, and powers to reinvest proceeds and savings locally. Such city-regions should be democratically constituted, with elected mayors and assemblies. Marrying bottom-up and top-down institutional reforms, such functional economic groupings will need to be articulated with the emergent administrative map of local authority collaborations emerging across England.³²

4.2 Institutional framework for coordinating policies for spatial imbalance across the UK

In the debate about constitutional change, the focus on which powers should be devolved (and the argument about whether they are too little or too much) has arguably crowded out discussion about frameworks for policies in which governments at different levels (UK, Devolved Administration) should have a common interest. Addressing spatial imbalance is one of these policy fields: Currently, England, Scotland, Wales and Northern Ireland each pursue their own regional and local development policies to reflect their different political and policy priorities. Where a UK-wide issue arises – for example the allocation of EU Structural Funds, or the negotiation of the UK regional aid map – it is dealt with on an ad hoc basis.

What is missing is an institutional framework that could initiate and pursue the more ambitious agenda of spatial rebalancing. At its most basic, such a framework could set high-level political objectives and policy targets for a more balanced economic development of the UK; it could develop the kind of 'national planning framework' for the whole of the UK which has been created in Scotland (now in its third iteration); it could coordinate the decentralisation of public administration; and it could establish objectives and priorities for UK-wide infrastructure investment. As noted above, there are models in other countries. A formal system is the Joint Task 'Improvement of Regional Economic Structures' in Germany (*Gemeinschaftsaufgabe Verbesserung der regionalen Wirtschaftsstruktur*) that brings together the Federal Government and State (regional) governments to set out an annual framework plan, with a calibrated voting system to ensure consensus across the levels of government. An informal model is the Austrian 'Spatial Planning and Development Conference' (*Österreichische Raumordnungskonferenz*) that coordinates national strategies and the territorial development interests of different levels on a voluntary basis. More generally, there are lessons from countries like Norway which produces a White Paper for each new government – based on extensive research, evaluation and analysis – on the state of regional disparities and the priorities for regional and local development across the country.

²⁹ Blick, A. and Jones, G. (2010) *A Federal Future for the UK: the Options*, Federal Trust for Education and Research: London.

³² Paine, D. and Smulian, M. (2015) Is this the future shape of local government?, *Local Government Chronicle*, 26 February, LGC: London.

³⁰ Pike, A., Coombes, M., O'Brien, P. and Tomaney, J. (2014) Austerity states, institutional dismantling and the governance of sub-national economic development: the demise of the Regional Development Agencies in England, *Unpublished Paper*, CURDS: Newcastle Upon Tyne.

³¹ City Growth Commission (2014) *Unleashing Metropolitan Growth*, London: Royal Society for the Arts.

4.3 Decentralisation of public administration and employment

Another key element is decentralization of the centre of government and the deconcentration of the departments of state and civil service from Whitehall in London to other parts of the UK. Such arguments for public sector dispersal have been revisited periodically – the most recent of which was undertaken in 2010 by the UK government – as part of the decentralization of public administrative activities and institutions beyond the centre to connect with the UK outside London, increase Whitehall’s spatial awareness, and reduce costs.³³ A new round of public sector dispersal is timely in the current moment, connecting and reinforcing the broader decentralization of governance advocated here. The same principles should govern an assessment of decentralization of public administration within Scotland, Wales and Northern Ireland.

4.4 Fiscal devolution

As the United Kingdom has sought to come to terms with the spatial consequences of its industrial decline much has been learned about how to enhance the rate of local economic growth. Local areas start with an inherited pattern of land use and a resource base and institutions that were tailored to another era. The legacy of the past can weigh heavily, and adjusting to new futures is difficult. In the last thirty years the challenge in many areas has been to bring about economic, physical and social renewal and reorientation against a backdrop where much of their existing stock of floorspace, human and physical capital was configured to produce goods that either no longer exist or are now made elsewhere in the world.³⁴ In order to achieve such renewal and re-orientation, sustained and substantial effort on several fronts is required, including the promotion of entrepreneurship, innovation, investment, and human capital formation (education and skills), as well as modernising infrastructure.³⁵

At the present time local growth initiatives across the United Kingdom are often struggling to gain traction given the scale of the task of economic transformation and adaptation. New ways have to be found to increase the level of resources that can be levered into or retained and pooled to help promote the local growth process and thus speed up the pace at which change can occur. Local authorities in particular are very constrained in their ability to obtain the resources they need. Most of the resources that they receive are hypothecated and allocated on a population basis. UK government departments and the Devolved Administrations still tend to influence and control key decisions in relation to mainstream budgets in the areas of skills, health, housing, business support, and much more.

In the UK the proportion of tax set at the local level in the United Kingdom is equivalent to 1.7% of GDP.³⁶ This compares to 15.9% in Sweden, 15.3% in Canada, 10.9% in Germany, and 5.8% in France. In addition, the proportion of tax revenues to local government as a proportion of total national tax revenue has actually been falling for forty years, from just over 11% in 1975 to 4.9% in 2012.³⁷ The UK is out of line with most other comparable OECD countries where, if anything, the proportion has either remained broadly the same or increased, sometimes quite dramatically as in the case of Italy and France through meaningful fiscal decentralisation (see Table 1).

In the face of a severe relative lack of resources compared to virtually any other comparator country and faced with the need to address considerable changes to their physical fabric and labour markets, local authorities across the United Kingdom have been forced to rely on relatively inadequate discretionary resources – either from UK government in England, or the Devolved Administrations in Scotland, Wales and Northern Ireland – to deliver their local growth agendas and/or work with central government bodies such as the Homes and Communities Agency. They have often had to apply for packages of support from central government that have usually been made available through specific policy initiatives like City Challenge and the Single Regeneration Budget. In other cases, central government has made funding available through initiatives such as Development Corporations and Enterprise Zones.

³³ Smith, I. R. (2010) *Relocation: Transforming Where and How Government Works*, HM Treasury; London; Hope, N. and Leslie, C. (2009) *Challenging Perspectives: Increasing Whitehall’s Spatial Awareness*, New Local Government Network: London.

³⁴ Baxter, C. et al (2007) *Enterprising Places: Sustaining Competitive Locations for Technology-Based Activity*. CMI. Programme on Regional Innovation.
http://www.landecon.cam.ac.uk/pdf-files/cv/pete-tyler/copy_of_PRI_ENTERPRISING_REPORT1.pdf

³⁵ Gardiner, B., Martin, R.L. and Tyler, P. (2013) Spatially unbalanced growth in the British economy, *Journal of Economic Geography*, 13, pp. 889-928.

³⁶ Parliament UK (2014) *Devolution in England: The Case for Local Government*, Communities and Local Government Committee.
<http://www.publications.parliament.uk/pa/cm201415/cmselect/cmcomloc/503/50305.htm#note31>

³⁷ OECD (2015) *Tax Policy Analysis*.
<http://www.oecd.org/ctp/tax-policy/revenue-statistics-levels-of-government.htm>

Table 1: Tax revenues attributable to Local and Regional Government as Percentage of Total Tax Revenues

| COUNTRY | 1975 | 1995 | 2012 |
|-----------------------|-------------|------------|------------|
| United States | 34.2 | 33.1 | 35.8 |
| Spain | 4.3 | 13.3 | 42.1 |
| Denmark | 30.4 | 31.9 | 26.9 |
| France | 7.6 | 11.0 | 13.2 |
| Italy | 0.9 | 5.4 | 16.4 |
| Japan | 25.6 | 25.3 | 24.7 |
| Germany | 31.3 | 29.0 | 39.8 |
| United Kingdom | 11.1 | 3.7 | 4.9 |

Source: OECD (2015) Tax Policy Analysis

More recently, City Deals have reflected the same process except the UK government has increasingly sought to ensure that specific targets are met, which has further added to the difficulties and complexities that local authorities face in securing funds. While the Devolved Administrations have established strategic economic development frameworks, in England the allocation of resources, most recently to Local Enterprise Partnerships as part of the Growth Deals, again essentially reflects much the same process. What now exists is a plethora of piecemeal, largely unconnected forms of centralized support (mostly allocated locally on competitive basis), that do not add up to a systematic, sufficiently-funded or coherent strategy for spatially rebalancing the economy – a situation recognized by the National Audit Office.³⁸

It was in recognition of this overly-centralized and under-resourced state of affairs, that Lord Heseltine identified some £49 billion of central government spending on skills, infrastructure, employment, housing, regeneration and business support, that he considered could and should be devolved directly to city-regions. While the Government accepted most of Heseltine's recommendations,³⁹ and in response has set up a Local Growth Fund, the scale of resources committed to the latter is only just over £2billion. More important is its pledge to bring the total resources under the strategic control of the Local Enterprise Partnerships to £20billion by 2021.⁴⁰ This commitment would certainly be a significant move towards fiscal devolution. But it would still fall far short of the scale required. It is not just a case of devolving certain areas of central government spending to the city regions, but also one of permitting such areas to retain their local receipts from property taxes, business taxes and local services. Manchester alone estimates its receipts to be around £17billion per annum. And it is far from clear that the system of LEPs is necessarily the most appropriate spatial governance structure through which to achieve this goal. As stated above, many LEPs are not economically meaningful units, nor are they directly accountable as such to local electorates. Yet, as the Government stresses, the issue of local governance is key to the devolution of fiscal resources.

Thus while there is a welcome emerging recognition of the case for a less centralized and better integrated system of public finances in the UK, this historical opportunity needs to be pursued with greater commitment and coherence of purpose. Accountability, transparency and clarity on where money is raised and spent, where this is decided and how it can be used to stimulate and incentivise sustainable growth and development are critical. Equalisation and safety net principles need to be retained too in the context of further decentralisation and localization of the governance and fiscal system. Such reforms may risk opening up further spatial imbalances and fiscal disparities between more and less prosperous places with stronger or weaker tax bases. The more vulnerable places with greater needs will require support to prevent their exposure within any more decentralized system.

Much work has already been done to explore the potential of these kinds of reforms. The Commission on the Future of Local Government, for example, has called for greater devolution of powers and funding over the drivers of productivity, skills, transport and innovation as part of creating greater civic enterprise by local authorities.⁴¹ Working with the principle of fair outcomes across London and the country as well as the desire to render the governance of financial decision-making more accountable to residents and businesses in London, the London Finance Commission suggested the further devolution of fiscal powers including the increase of revenue streams under local control. These include property taxes and eventually the 'full suite' of council tax, business rates, stamp duty land tax, and capital gains property disposal tax, and reduced restrictions on borrowing for investment.⁴² This same reasoning is no less applicable to other city regions cross the country.

Concrete innovations for fiscal decentralisation across the UK would be meaningful progression of place-based settlements for local authority groupings that are multi-annual, multi-sectoral and provide the opportunity to integrate, connect and provide more certainty for longer-term utilisation and management of (national and local) public sector revenues and assets.⁴³ Work on such place-based arrangements including 'Total Place' and 'Community Budgets' has already explored the possibilities and reforms in this area and the Local Government Association has called for long-term and place-based finance as the default method of funding with appropriate flexibilities, freedoms and reforms built in.⁴⁴

³⁸ NAO (2014) Funding and Structures for Local Economic Growth, NAO: London.

³⁹ Specifically 81 (in full or in part) of Heseltine's 89 recommendations (HM Treasury, 2013, *Government's Response to the Heseltine Review*, Cmnd 8587.

⁴⁰ HM Treasury (2013) *Investing in Britain's Future*, Cmnd 8669.

⁴¹ Commission on the Future of Local Government (2012) *Final Report*.

⁴² London Finance Commission (2013) *Raising the Capital*, Report of the London Finance Commission: LSE.

⁴³ Blond, P. and Morrin, M. (2014) *Devo Max - Devo Manc: Place-Based Public Services*, ResPublica: London.

⁴⁴ House of Commons Communities and Local Government Committee (2013) *Community Budgets*, Third Report of Session 2013-14, HC 163, House of Commons: London Community Budgeting; Local Government Association (2015) *The LGA's Budget 2015 Submission*, LGA: London.

4.5 Decentralising the financial system

The overly centralized and concentrated financial system in the UK has long been recognized as a consistent and deeply entrenched cause of spatial imbalance within the UK. To compound the problem, UK banks have long ago shifted their lending activities away from industry, in favour of lending to other financial institutions and the mortgage market. Back in 1950, some 65 percent of bank lending was to industry; by 2010 that had fallen to a mere 15 percent. Over the same period lending to financial companies has increased from 10 percent to 38 percent, while mortgage lending, which was zero in 1950, accounted for 40 per cent of lending in 2010.⁴⁵ Expressed another way, bank loans accounted for only 18 percent of industry financing in the UK in 2010; this compares to a corresponding figure of 45 percent in Germany.

The difficulties faced by small- and medium-sized firms in raising capital has been a topic of recurrent concern in the UK. The Government has made much of the need to stimulate advanced manufacturing, as part of its concern to rebalance the economy. Many specialist advanced manufacturing firms are small or medium sized. Some targeted initiatives have been introduced to support the SME and advanced manufacturing sectors, such as the advanced manufacturing supply chain scheme, but the scale of funds committed (£213 million⁴⁶) are able to make only a modest contribution to the task of rebuilding UK manufacturing. If the UK is serious about increasing its presence in advanced manufacturing, the funding of new investment is an issue that urgently needs to be addressed. To this end, there would seem to be a very real opportunity to use the tax system in the UK to align the objective of more spatial rebalancing with that of more sectoral rebalancing. Government could establish new 'Advanced Manufacturing Bonds' with favourable tax treatment to increase the flow of funds into advanced manufacturing firms, some of which might be available as a result of recent changes to pensions. Many northern cities still have significant manufacturing potential and increased investment in this sector would assist them with their growth agendas.

Moreover, there is evidence that the geographically skewed nature of the capital markets operates in a spatially biased way, creating funding and financing gaps especially for SMEs and firms in economically weaker and peripheral localities and regions. Globalization, technological innovation, competition and mergers and acquisitions have accentuated such centralization and concentration. The UK's financial system is overwhelmingly concentrated in and controlled from London, and national monetary policy (such as interest rates) has tended to be biased towards the concerns of the capital's financial nexus.⁴⁷ Experience from Germany suggests that a more regionally decentralized financial system is associated with a

greater regional evenness in the allocation of funding to small firms. The German banking system has a significant regional dimension, and, as is well known, has traditionally had a close relationship with industry. Likewise, the spatial organisation of the German venture capital, involving several major centres, contrasts with the situation in the UK, where the venture capital industry is overwhelmingly concentrated in London and the surrounding South East (these two regions contain some 75 percent of the nation's venture capital firms, and account for over 60 percent of venture capital investment).⁴⁸

The uneven access to finance has prompted the Scottish Government to propose a Scottish Business Bank (replacing the Scottish Investment Bank within Scottish Enterprise) and there is a similar debate in Wales about replacing Finance Wales with a Development Bank for Wales. These debates, and emerging institutions, provide lessons for regionally focused investment institutions for other parts of the UK that would focus on raising funds for financing long-term productive assets and employment creation, especially in the areas of SMEs and infrastructure.⁴⁹ Clearly there are issues to be resolved around what form such institutional arrangements might take, such as the remit of the bank, its capitalisation, how it might raise additional funds, its governance structure and potential hurdles to be overcome in setting it up, in particular gaining approval under the EU's state aid rules. However, models exist in the form, for example, of the German KfW, Finnvera in Finland, or the US Small Business Administration.⁵⁰ But what would be a crucial to its remit would be the funding of SMEs in the regions outside London and the South East, given that these latter regions are already well served by the existing centralized financial system. Regional lending data shows that SMEs in London have huge net positive deposit balances while in many other regions the reverse is the case. A new public investment bank in England would thus need to have an explicit regional structure to its organization in order to be close to the local SMEs seeking funding. Such an institution would provide the sub-national focus that is missing for all parts of the UK, and could help ensure a more spatially balanced allocation of finance to private sector activity.⁵¹ And as the German system demonstrates, a more spatially decentralized banking structure need not compromise the credit rating of the institutions concerned.⁵²

Such radical changes would be the first steps towards a more comprehensive and thorough-going shift in the UK's political economy towards spatial rebalancing. Calls were made over a decade ago for 'decentering the nation' and, to date, only limited and modest progress has been made, especially in England.⁵³ The current juncture is potentially more propitious for reviving that call.⁵⁴ Our argument is that a decentralised framework, involving the meaningful extension of devolution in governance, public finance and the financial system, would not only connect to a growing groundswell of support for more decentralization,⁵⁵ but should form a key step towards a properly spatially federated structure.

⁴⁵ Bank of England (2014) *Understanding the Fair Value of Bank Loans*, Financial Stability Paper No. 31, Bank of England.

⁴⁶ Department of Business Innovation and Skills (2013) *Advanced manufacturing supply chain fund to create thousands of new jobs*.
<https://www.gov.uk/government/news/advanced-manufacturing-supply-chain-fund-to-create-thousands-of-new-jobs>

⁴⁷ Harvey, O (2013) *London and the UK: In for a Penny, In for a Pound*, Special Report, Deutsch Bank, London.

⁴⁸ Martin, R.L., Berndt, C., Klagge, B. and Sunley, P. Spatial proximity effects and regional equity gaps in the venture capital market: evidence from Germany and the UK, *Environment and Planning, A*, 27, 1207-1231; Martin, R L. (2013) *Financing Business in Slow Growing Regions: Is there a Case for Local Capital Markets?* Discussion Paper, North East LEP Independent Economic Review.

⁴⁹ See, for example, Skidelsky, R., Martin, F. and Wigstrom, C.W. (2011) *Blueprint for a British Investment Bank*, Centre for Global Studies, London; Dolphin, T. and Nash, D. (2012) *Investing for the Future*, London: IPPR; Merlin-Jones, D. (2012) *Extended Lending: The Case for an State-Backed Investment Bank*, London: Civitas; Tott, N. (2012) *The case for a British Investment Bank: A report for Labour's Policy Review*, London: The Labour Party.

⁵⁰ The German KfW is a state-owned bank with various functions, but its two main activities are financing housing and environmental projects, and providing funds for SMEs. It covers over 90 percent of its borrowing needs in the capital markets, mainly through bonds that are guaranteed by the national government. This allows KfW to raise funds at advantageous conditions. Its exemption from having to pay corporate taxes due to its legal status as a public agency and unremunerated equity provided by its public shareholders allow KfW to provide loans for purposes prescribed by the KfW at lower rates than commercial banks. KfW is not allowed to compete with commercial banks, but it facilitates their business in areas within its mandate.

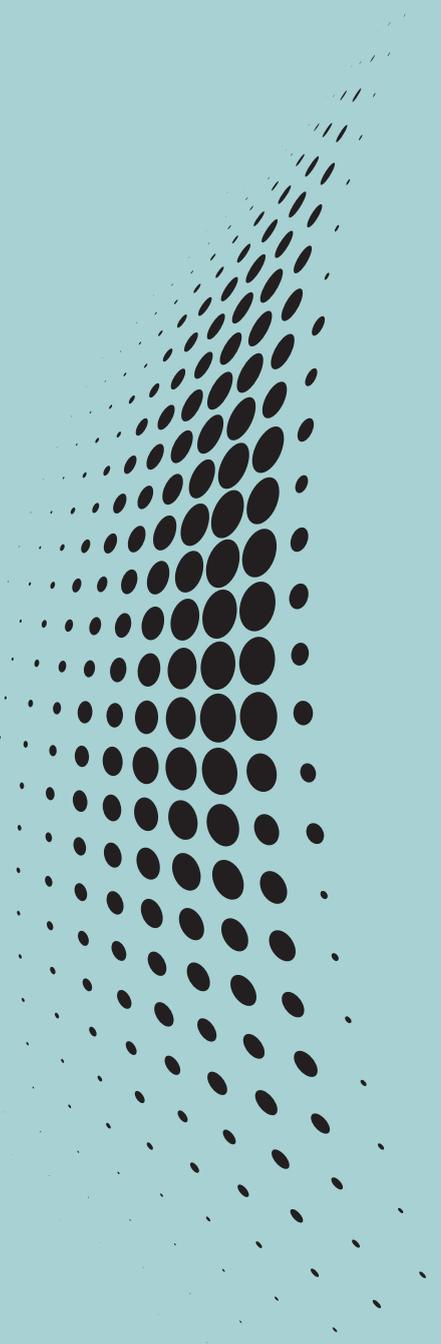
⁵¹ Klagge, B. and Martin, R. (2005) Decentralized versus centralized financial systems: is there a case for local capital markets?, *Journal of Economic Geography*, 5, 4, 387-421

⁵² Moody's Investor Services (2013) German development banks: strong public sector support and legal framework underpin Aaa-Aa1 ratings, *Special Comment*, 19 July, Moody's Investor Services: Frankfurt.

⁵³ Massey, D., Amin, A. and Thrift, N. (2003) *Decentering the Nation: A Radical Approach to Regional Inequality*, Catalyst: London.

⁵⁴ IPPR North (2014) *Decentralisation Decade: A Plan for Economic Prosperity, Public Service Transformation and Democratic Renewal in England*, IPPR North: Newcastle.

⁵⁵ City Growth Commission (2015) *Devo-Met: Charting a Path Ahead*, London, City Growth Commission.



5 A CALL FOR ACTION

Whether considered at the regional, local or urban scales, entrenched and persistent spatial disparities in economic and social conditions are a strategically important issue for all the major political parties in the UK. The current UK Government is keen to show that the recovery from the recent crisis and recession is nationwide, and argues that “North and South are now pulling in the same direction”.⁵⁶ Pulling the same direction is not the same thing as pulling together equally, however, let alone a question of the North catching up with the South. As we have briefly shown in this pamphlet, the growth gap between the South and the North (and indeed between most of the cities in the South and most of those in the North⁵⁷), is long-standing and cumulative. As we have also argued, the problem goes well beyond the economics of urban agglomeration and is rooted in the spatially biased nature of the national political economy. It is time to start thinking about radical changes to that national political economy. A perspective firmly rooted in the nations and regions outside London is called for, and in this regard the Regional Studies Association, with its academic and policy membership across the UK, is particularly well placed to lead this rethink. Other nations, cities and regions confronting such forms of spatial imbalance and dominant city-regions can learn from and contribute to this wider international policy debate.⁵⁸

Whatever the outcome of the General Election in May 2015, the elected Government should think boldly and radically about the constitutional and institutional arrangements for the whole UK. The increasing array of fiscal and other powers being granted – to different degrees – to the Devolved Administrations of Scotland, Wales and Northern Ireland are welcome recognition of the demand for change. There is an equally valid case for devolving powers of this sort to the regions or city-regions across England, to permit them to harness their economic potential to full and best effect, and begin the much-needed steps towards constructing a nation-wide spatially federated system of public finance and economic governance, variants of which have long existed in most other advanced economies. How to achieve this goal, what the most appropriate territorial units should be, and what powers they should have, are all issues that require considered and informed deliberation, of course. But arguably, unless the UK moves in this direction, the spatial imbalance that has long characterised the national economy will continue to persist, to the detriment of both the regions and cities outside the greater south east, and the country as a whole.

⁵⁶ “North-South divide ‘is history’ says Clark” (Greg Clark, Minister for Cities, quoted in *The Management Journal for Local Authority Business*, 22 January, 2015).

⁵⁷ See Martin, R.L., Tyler, P. and Gardiner, B. (2014) *The Evolving Economic Performance of UK Cities*, Working Paper 5, Foresight: The Future of Cities, UK Government Office for Science; *Cities Outlook 2015*, Centre for Cities, London.

⁵⁸ UK Commission for Employment and Skills (2011) *Rebalancing the Economy Sectorally and Spatially: An Evidence Review*, UKCES: Wath-upon-Deane.

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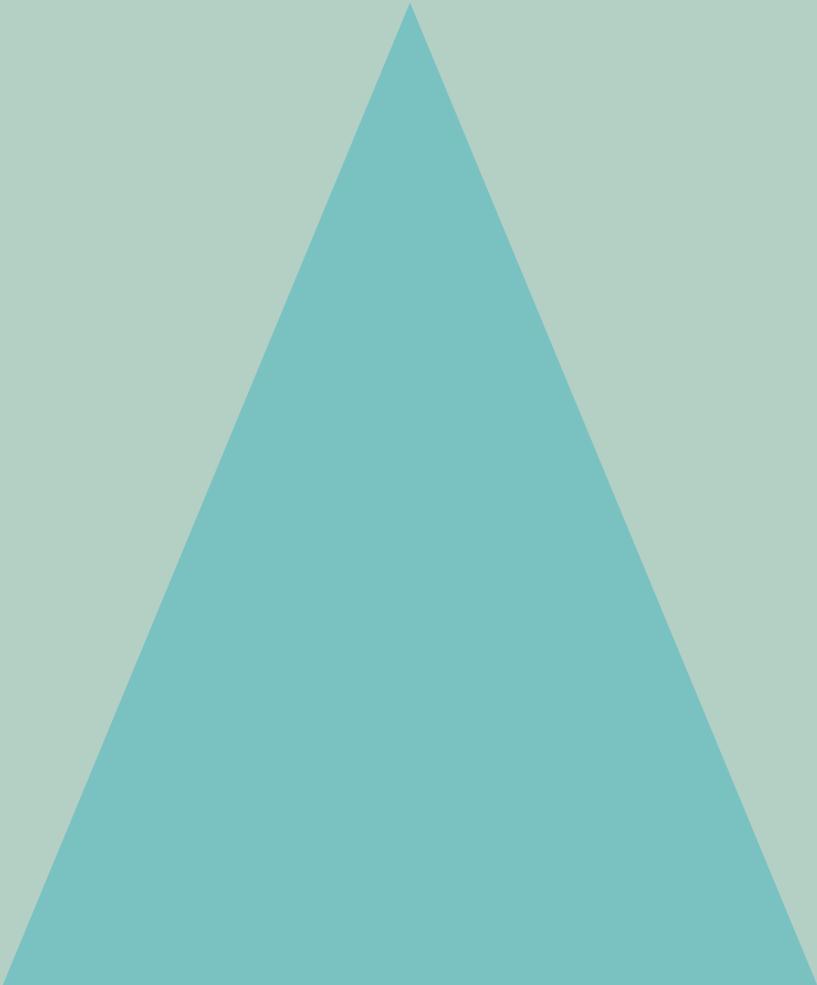
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