



INCLUSIVE GROWTH  
COMMISSION

**new  
economy**



# Measuring inclusive growth

Methodology Note  
September 2016

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## 1 Introduction

- 1.1 This note summarises results of an analysis to estimate the potential economic and productivity benefits from adopting a more inclusive approach to economic growth using existing economic indicators (namely GVA and GVA per capita). As the interim report for the RSA Inclusive Growth Commission notes, there are problems with GVA and other existing economic indicators as they do not directly measure inclusive growth, particularly in terms of wealth inequality and in the spread of economic prosperity. A focus solely on GVA as a measure of impact would be counterproductive.
- 1.2 That said, GVA is the current mainstream measure of economic impact and from a Government perspective showing the GVA impacts of an inclusive growth agenda will be important, not least because of the link between GVA and tax receipts. Research has also shown that GVA per capita is correlated with indicators of economic and social well-being. GVA growth is therefore likely to be a necessary, but not sufficient, indication of a more inclusive approach to growth. Put another way, falling GVA is unlikely to be correlated with a more inclusive economy or society.
- 1.3 Further work will be undertaken as part of the RSA Inclusive Growth Commission to develop more accurate data and measurement of 'quality GVA', as well as strengthening our analysis of the impact of adopting a more inclusive approach to growth in the UK.

## 2 Methodology

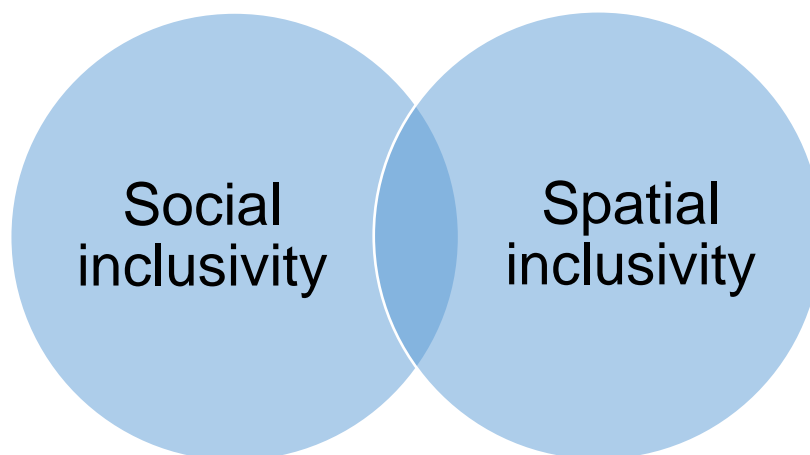
- 2.1 To calculate the impact of a more inclusive approach to growth we have estimated the impact of more balanced levels of productivity – measured by GVA per capita – across the UK. GVA is an aggregate statistic designed to reflect the value of output generated by organisations in an area less the value of inputs used in the production and delivery process. Simplistically, GVA is calculated by adding up all profits made by firms and all wages earned by workers in an area.
- 2.2 GVA per capita was the preferred method of measuring disparities in regional performance by the government when the Regional Development Agencies were in existence. It is still the key indicator that the EU uses to determine which areas are eligible for the highest level of support (such as access to Regional Aid). By sharing total GVA across all residents (whether or not they are directly contributing to GVA) it gives an indication of the economic performance of a whole place. This has the benefit of encouraging a focus on initiatives within an area that get residents into work, as well as interventions that support people and businesses to become more productive and hence generate more profits and wages. However, since GVA per capita can be boosted by getting residents into any form of work, as this increases GVA but does not change the population by which it is divided, a weakness is that it does not necessarily focus interventions on creating high value jobs. Generally, GVA per capita will also be higher in areas with high commuting and a low resident population (such as central

London), or in areas that have a low dependent population (i.e. low numbers of children/students and retired people who are less likely to contribute to GVA). The latter issue can be controlled to some extent by looking at GVA across functional economic areas.

- 2.3 At a UK level, per capita GDP (the national equivalent of GVA, which includes taxes and subsidies which are not easily measured at the sub-region level) is lower than other leading European countries, standing at, €31,500. It is behind countries such as Luxembourg, Switzerland, Norway, Ireland, Austria, Germany, Denmark, Sweden and Belgium. This is only marginally above the Euro-area average of €31,300. It is also behind the United States.
- 2.4 The gap in performance of the UK is the result of both people and place factors. The UK's high level of economic inactivity and unemployment means that its human capital is under-utilised. If the UK's employment rate was to increase to 80% (which has been an aspiration for past Governments, Conservative and Labour), this would result in an additional 2.3m people moving into the labour force. Assuming these people all contributed the existing average GVA per job, the UK's overall GVA would grow by £119.5bn and GVA per capita would rise by 7.4% to £26,800.
- 2.5 GVA per capita also varies significantly between and within regions, reflecting:
- different sectoral structures;
  - different levels of value added between regions within the same sector (e.g. London's financial services are, generally, more productive than financial services in the North due to the types of activities undertaken within these sector);
  - different levels of worklessness and unemployment; and
  - differences in regional prices, as costs tend to be higher in some parts of the UK (particularly London and the South East), which feeds through into higher wages and therefore higher GVA.
- 2.6 The importance of the latter should not be overstated, as higher costs are largely a reflection of more productive places and firms being willing to pay more to be located in these areas.
- 2.7 Annex 1 sets out the key factors which contribute to increased GVA per capita. This highlights that, at the national level, GVA per capita is able to show the impact of social inclusivity as set out in the RSA Inclusive Growth Commission Interim Report, namely:
- "Socially: [inclusive growth] benefits people across the labour market spectrum, and is able to target groups that face particular barriers to sustained, high quality employment, particularly ethnic minorities, long-term unemployed people and people with disabilities.
- 2.8 When analysed at a sub-national level it is also able to show the impact of the second:
- "Spatially: [inclusive growth] addresses the inequities in growth, opportunities and outcomes that persist between different parts of the country and within economic

geographies. For example, between major city centres and smaller towns and cities within the city-region geography.”

- 2.9** Bringing this analysis together, we can see that the two types of inclusivity are interlinked and mutually self-supporting, as illustrated in the Venn diagram below. In GVA terms a more inclusive economy would be one in which more people are employed in higher productivity (and higher paying) sectors with economic output and growth more evenly distributed across the country. It is possible to estimate and thereby illustrate the scale of the potential impact of a more inclusive economy using regional GVA per capita figures. At a NUTS1 level (regions) GVA per capita ranges from £42,670 in London to £17,570 in Wales. GVA per capita for the UK as a whole is £24,960. If each NUTS1 region were to reach at least the current national average – assuming that this is an achievable aspiration for the UK – then the UK’s total GVA would be £191.5bn higher.
- 2.10** The tax to GVA ratio is currently 0.38:1 (i.e. for every £1 of GVA created the Government collects 38p in taxes). The increase set out above would therefore generate £73bn in additional tax revenue for the Exchequer.



- 2.11** To put these figures in context:
- the current combined GVA of the core city regions of the North of England is £184.1bn;
  - total welfare spending in Great Britain was £190bn (i.e. all in- and out-of-work benefits, including the state pension and personal tax credits entitlements); and
  - across Great Britain, government currently spends £17.9bn on key out-of-work benefits (ESA/IB, Lone Parent Income Support and JSA); £28.7bn on in- and out-of-work tax credits; and £24.3bn on housing benefits.

### **3 Conclusions**

- 3.1** GVA per capita is an imperfect measure of productivity and is a poor measure of an inclusive economy. However, it is a widely used and easily understood proxy. Were the economy to become more inclusive it is all but certain that this would lead to an increase in GVA per capita through increased employment levels and/or improvements to wages and profitability. Taking a longer-term view about how this could manifest in terms of social and spatial inclusion, a reasonable estimate of the potential impact would be an increase in GVA of £192bn per year.

Annex 1: GVA per capita framework

