A couple of snapshots - Wales in 1988 and in 2008

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When the *Welsh Economic Review* published its first edition in 1988, Dr Gwyn Jones had just been appointed as Chairman of the Welsh Development Agency (WDA). The WDA (now merged into the Welsh Assembly Government) had been established in 1976 to encourage business development and investment in Wales. At the time of his interview with the *Review* Dr Jones stated that the Agency's aim was to make Wales one of the most prosperous countries in Western Europe. A key mechanism to spur development was foreign direct investment, and WINvest had been very successful in achieving this; Wales having only 5% of the population had managed at that time to attract 20% of UK inward investment. However, Dr Jones was also keen to emphasise that small indigenous businesses were important, with 14% of the working population in self-employment in Wales compared to 11% in the UK as a whole.

Twenty years ago, the UK was the fastest growing economy in Europe growing by 3.6% during 1988. The EU was growing more slowly at 2.5%. Meanwhile, growth in the USA (at 3.3%) was closely aligned with the UK. Japan had grown strongly in the 1960s and 1970s, but its troubles were just beginning in the 1980s. A strong yen in 1985 was creating export difficulties and so interest rates were lowered, contributing to a financial bubble to which the government then responded with interest rate rises, up to 6% in 1990. Thereafter, Japan's economy shrunk, with interest rates at 0.5% between 1995-2000 failing to provide the required stimulus, and prompt banks to increase their lending. Latest figures suggest Japan's economy is now in recession.

Back in 1988, *Welsh Economic Review* commentators attributed strong UK GDP growth to retail sales, with *'the rate at which consumer credit is being extended being an important reason for the boom in consumer spending'* (*Welsh Economic Review* Volume 1, 1988). Hence, our love affair with spending is old news, having consequences that are all too easily forgotten and seldom learned from. In the late eighties, the mortgage market was just beginning to relax lending terms so that buyers could acquire 100% mortgages. This fuelled the housing market, and raised house prices. Does this sound familiar? As inflation took off, interest rates were forced up to subdue consumption, then making life difficult for mortgage holders and impossible for potential buyers; homeowners were experiencing negative equity and buyers did not bother to enter the market, so it stalled. The average price of a house in the South-east was £105,000. By 1992, this had fallen to £74,000. Negative equity is bad news today just as it was bad news twenty years ago.

Turning now to the indicators shown in Table 1, we can see that Wales's population has increased slightly over the period in absolute terms, while Wales's share of the UK population has declined slightly.

Government officials, politicians and economic commentators have for a long time considered GDP per head to be a convenient way to measure relative regional prosperity, and indeed in the 1980s and 1990s Wales was a GDP target driven economy, seeking to diminish the prosperity gap between it and the rest of the UK. Today, most would see this to be an implausible challenge, for how could Wales hope to outpace the economic engine room of London and the South East, suffering as it does from the disadvantage of being peripheral, with few headquarters, an increasing dependency on footloose contact centres for employment, a relatively high reliance on public sector employment, and persistently low participation in the workforce. None of these characteristics can easily be turned round or converted into wealth, let alone the super-growth that is needed to catch up with the most prosperous of the UK regions.

Wales's predicament is also illustrated by the observations of the economic think-tank Oxford Economics, who state '*based on people who resided in Wales, tax revenues of £19.3bn were raised in 2006-07. This compares to Government expenditure of £28.4bn – a net drain of minus £9.1bn*'. It is not so much that Wales is a net drain, it is more that many of the UK regions including Wales fare poorly compared with a very rich capital city and surrounding south east. The key issue as much now as twenty years ago is the unequal distribution of growth and prosperity throughout the UK, making regional redistributive policy

Table 1: Key Welsh Economic Indicators 1988 and 2008

Key Indicator	1988	2008[1]
Area (km^2)	20,779 (8.6% of UK)	
Population in Wales	2.8m (5% of UK)	3m (4.95%of UK)
GVA per head as % of UK	86[2]	77[3]
Economic Activity Rates (%)[4] (working age 16-59/64, All)	73.3	75.5
Unemployment Rate (%)[5]	10.5	6.7
Household Income /hd (£) as % of UK	86.9	86.9
Average male earnings (UK =100)	91.2	84.2
Average Female earnings (UK = 100)	92.8	90.2
Number of Foreign-owned manufacturing enterprises	236	350[6]
Employment in Foreign-owned manufacturing enterprises	51,300	64,500[6]

1: Latest available data. This may not be for 2008.
2: GDP
3: GVA, 2006
4: 1988 activity rates from the labour force survey
2007 activity rates from the Annual Population Survey
5: 1988 source is Department of Employment, 2008 is ILO rate, July-September
6: 2007 data – estimates.

as much a necessity as it ever was; if only to prevent discontent in the outer reaches of the UK that lie outside the M25.

Successive Welsh Assembly strategy documents appear to show a gradual distancing from GVA targets, and now the catch-up process is much more an aspiration than a goal. The latest published 'prosperity indicator' GVA/head data for 2006 show that Wales now languishes well below Northern Ireland, and is at the bottom of the productivity league. Wales' share of UK GVA/head stands at 77%, compared to 86% of UK GDP/head in 1988. A wide gap is now wider than ever.

Low participation or economic inactivity has been identified as a core contributor to the UK and Wales GDP/GVA differences, which have long challenged policy makers. Even in 1996, activity rates for Wales for persons of working age were 4 percentage points below the UK. Low participation is, to an extent, an inheritance from the past: a vestige from the industrial coal and steel shake-out of the 1980s and earlier when whole communities were rendered jobless. As a result the participation gap between Wales and UK in terms of male economic activity was particularly striking. This feature still exists today, and the marginal improvements that have been achieved over time can be linked to the fact that female participation figures are much closer to the UK average. Massive industrial restructuring is history, and cannot forever be called to account for low activity in Wales, unless perhaps, economic inactivity as a way of life can cross the generation divide.

Meanwhile, historical data relating to economic participants shows that unemployment was high in the late 1980s, but has tended to be relatively low in the last decade. This is a reflection of respective government philosophies, and particularly reveals the policy effects of Labour's drive to 'full employment' partially secured by high levels of public spending. With the spectre of recession looming, rising unemployment is already in evidence with the current government's good record on employment soon to be severely challenged. Maintaining 'full employment' may be a strong underlying motive for the Chancellor of the Exchequer to promote a 'big' government and Keynesian spending policy reflex, as the financial crisis deepens.

The Coming and Goings Section of the *Review* which features business arrivals and departures usually does not require much paring down; a process that does apply in this edition with many more departures than usual. Each tells its own story. Financial Services Data Management (a firm which provides advice on debt) is expanding its call centre workforce by 200 and moving to a new office location in Swansea. Meanwhile, HBOS announced in August that it intends to close its mortgage service centre in Cardiff, with the loss of 150 jobs as part of a streamlining process. A couple of firms making doors and windows announced job losses and a sofa company is moving from Wales to a lower cost base in Eastern Europe. In the Nineties recession private sector activities had a strong tendency to retrench to the core, and this is likely to reoccur, as branches of services industries seek to cut costs and retract their feelers.

A withdrawal of cheap lending (which used to pay for the new house *and* its contents), a seized housing market, falling house price and worse – negative equity - in Wales, as elsewhere throughout the UK, infiltrates the whole economy as people make do with what they have got, cut their expenditure on DIY and all manner of household goods, furniture, doors and windows and buy less and cheaper food, and so on. The trouble is that if everyone stops spending, including those who have no immediate need for caution (disgruntled savers with small or no mortgages and secure-ish jobs), then the downward vortex is accelerated.

Back copies of the *Welsh Economic Review* remind us that in 1988, Wales still had a coal industry, employing 9,900 people and producing 6 million tonnes of coal from 11 collieries. Three fifths of this output was burnt in the power stations at Uskmouth and Aberthaw, with the then British Steel Corporation buying a further fifth. The rest was used for domestic purposes, and other local industrial use with the remaining 10% exported. In January 2008, it was announced that Tower Colliery in Hirwaun, (the last of the deep mines in Wales) was officially closed. The colliery was uniquely owned by its workers after they courageously invested their redundancy money in the buy-out.

Tower Colliery estimated there to still be around 250m tons of coal remaining in Wales, comprising half of the UK's identified reserves. There is the prospect of Energy Build Holdings (mostly owned by Cambrian Mining PLC) accessing a seam at Aberpergwm that could provide decades of operation and hence employment, and certainly some of Tower's ex miners may be transferring to this drift mine. How much of Wales's remaining coal reserves will be exploited now or in the future depends on energy prices. Some commentators believe that, if the remaining reserves were nationalised and preserved for a future when carbon capture was perfected and energy priced considerably higher than now, Wales could be sitting on a 'gold' mine rather than a coal mine. But that is a remote prospect.

Meanwhile, the current financial crisis (partially seeded by high fuel costs) is still unfurling. In 2008, our broadcast media is structured in such a way that it depends on news to fill large chunks of available band width, and the credit crunch has inevitably provided more grist for this voraciously hungry news mill. People will be asking how will the recession affect Wales?

For those who do not recognise Wales as an economic entity (i.e. not having separate national accounts) the recession will be perceived as hitting the UK and Wales as a singular event. Other commentators have observed 'a silver lining to the poisonous cloud of toxic assets choking the financial system' because the recession will have a proportionately more profound impact on the very rich south east, while Wales will plough on much as before, enjoying as it does a measure of protection afforded by relatively high public sector employment. Hence, there are regional nuances to the financial crisis. Reliance on high public sector employment means that choosing a public spending recovery route (favoured by Gordon Brown) could indeed provide some protection in Wales, as those with relatively secure income and employment can help underpin the economy with their household expenditure and so on. But none of us is immune.

As 2009 approaches there is less buoyancy, and less optimism than in 1988, but if this article had been written before the run on Northern Rock, it would still have contained a downbeat message as last year the aggregate borrowings of individuals in the UK exceeded their aggregate earnings.

During the lifetime of the *Review* most have experienced or are able to remember a few recessions, and therefore know that recovery is a matter of time. If, throughout the inevitable hardships of the coming months, there is pressure to become less wasteful and more resourceful, then Wales will emerge better prepared for the long-run.

The article which follows this was written by Brian Morgan in 1991 when he was Chief Economist at the Welsh Development Agency and Wales was showing signs of emerging from the last recession. It should offer assurances that even as all bubbles eventually burst then so do all recessions recede.