

Enterprise and Innovation

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West Midlands
Regional
Observatory

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Context

The West Midlands Economic Strategy (WMES), *Connecting to Success*, reveals a £10 billion output gap between the region and the UK average, based on Gross Value Added (GVA) per head. It goes on to identify some of the key challenges which contribute to that gap. Two areas where it identifies challenges are Enterprise and Innovation. In response, Advantage West Midlands commissioned the Observatory to develop a three year programme of work around the challenges identified in the WMES, to complement the existing programme of work on skills. Work began in June 2008 and a number of important outputs have already been delivered.

Enterprise

Our work on Enterprise aims to identify the degree that relative regional performance in the different aspects of enterprise - productivity, new business formation, business growth, enterprise culture and strategic positioning - have on the output gap. To guide the detailed research programme, a data and strategy sub-group of the Enterprise Board has been established. Chaired by Prof. Stephen Roper, it also includes representatives from the four Centres of Expertise. This group has agreed a series of reports to be completed by the end of 2009-10 which will look at 4 broad themes:

- A detailed analysis of industrial structure and how it can explain the relative economic performance of the region;
- An assessment of the socio-demographic profile of new business start-ups
- A review of the typology of existing businesses and an assessment of the contribution of fast and high growth businesses
- A review of the value-added strategic positioning of the region's largest firms

Over the last decade, regional output has grown less quickly than the national average. That means that the region's output gap has grown. The main reason for this is the lower productivity of the region's businesses. The first report in the series looked at the extent to which this was down to the mix of industries which make up the regional economy. This found that the region had a low share of each of the most productive industries. In some cases, such as chemical manufacture or utilities, the high capital costs as well as the regional geography make it difficult for us to compete. However, the most important of these highly productive sectors is financial services. This sector is dominated by London and it accounts for nearly a third of the output gap.

This highlights one of the key strengths of London's economy. The capital has by far the highest output per head in the country. Indeed, if London is excluded from the national figures, the West Midlands output gap is only around half as big. Apart from financial services, the other major contributor is other business services. The region has a low share of this sector and it is not as productive as in most other regions. This is partly because the region has fewer people employed in the more senior occupations, which generate the most value added.

The second report in the series looks at new business start-ups. This also shows that the region has seen slower growth in the number of VAT-registered businesses than the national average. More positively, nearly one in three new businesses are in the productive business services sector, and the number of such businesses is growing faster than elsewhere. Self-employment rates are also low by national standards, and this applies across most demographic groups. However, the region does have relatively high levels of early-stage entrepreneurial activity, particularly amongst young people, which may lead to higher growth in future.

These patterns do vary across the region. Productivity and business start-up rates are both higher in the south and east of the region, for example in Solihull and Warwickshire. This is also where the highest concentration of business and professional services are to be found. Start-up rates are low in some urban areas, such as the Black Country and Stoke-on-Trent, whilst the north of the region has the lowest levels of productivity.

Innovation

Our work on innovation aims to identify the degree that relative regional performance in the different aspects of innovation contributes to the region's output gap. The programme covers a wide range of innovation, not just traditional areas such as research & development and product innovation, but also covering process innovation, innovation in services and new markets.

Results from the work have been presented to the Innovation and Technology Council (ITC) and an advisory sub-group of the ITC helps to steer the work. This should ensure that the results that we produce will have an impact on regional policy around innovation.

Work has focused on three main areas of analysis:

- Benchmarking the region's innovation performance against other regions across a range of indicators
- Understanding the performance of some of the key sectors and markets in the region where innovation activity is particularly concentrated
- Analysing survey evidence to understand the key drivers of innovation performance

Benchmarking shows that in many respects the region lags behind national performance on innovation, although we outperform the EU average. A growing proportion of our firms are actively innovating and they attribute an increasing proportion of their turnover to innovation. However, expenditure on innovation is lower than in most other regions.

One of the barriers to innovation in the region is the relatively low proportion of people with high-level skills amongst the population. Even those with the right skills aren't always used well, with the region's private sector businesses employing fewer graduates than those elsewhere. Cost can also be a barrier to innovation, as can a lack of willingness to co-operate with other businesses or with researchers in universities.