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MAKING WALES BETTER
GWNEUD CYMRU WELL

Putting Businesses at the Heart of Levelling Up in Wales

About the author

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About the IWA

We are a think tank and charity, independent of government and political parties.

By bringing together experts from all backgrounds, we conceive ambitious and informed ideas which secure political commitments to improve our democracy, public services and economy.

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Our vision is to create a Wales where everyone can thrive.

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List of Abbreviations

BEIS	UK Government Department for Business, Energy and Industrial Strategy
CPI	Consumer Price Index (measure of inflation)
DIT	UK Government Department for International Trade
DLUHC	UK Government Department for Levelling Up, Housing and Communities
ERDF	European Regional Development Fund
ESIF	European Structural and Investment Funds
EU	European Union
LUF	Levelling Up Fund
OECD	Organisation for Economic Co-operation and Development
UKRI	UK Research and Innovation
UKSPF	UK Shared Prosperity Fund
WEFO	Wales European Funding Office

Executive Summary & Recommendations

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The transition from Welsh Government administered EU Structural Investment Funds (ESIF) to the programmes developed under the UK Government's Levelling Up agenda marks the most significant economic development policy change in recent years.

Between 2014-20, as part of a wider £400m annual ESIF investment, Wales received around £300m per year through the two main European economic development funds: the European Regional Development Fund (ERDF) and the European Social Fund (ESF). From the end of 2022 onwards, circa £200m per year will be made available through the new UK Shared Prosperity Fund (UKSPF), in addition to funding through the Levelling Up Fund (LUF) which, in the latest round, came in at £121m spread across projects in Wales.

These changes result in the power and responsibility for economic development shifting, in part, away from Welsh Government and towards UK Government, with the administering of funds through regional groupings of councils in Wales.

While the transition period for the UK departure from the EU ended over one year ago, it is still very early days in terms of redrawing the arrangements for economic development in Wales, and many challenges and opportunities lie ahead. The development of the UKSPF, due to run until 2025, and the second round of the LUF present just such an opportunity.

The IWA believes in developing a successful, clean, green and fair economy for Wales. Future efforts to address regional inequalities must fully respect the devolution settlement in Wales, and be based on evidence of what works, as we have previously laid out in our responses to the Levelling Up White Paper[1] and through our body of research.[2] In the here and now, however, we must seize on the opportunities presented by the new funding arrangements, whilst establishing a rigorous culture of constant learning and improvement to shape future programme design and investment.

1 IWA response to the 2022 Levelling Up White Paper

2 Watkins, J (2021) What does Levelling Up mean for Wales?, IWA

Recommendation 1

UK Government should allow and encourage Welsh regions to deliver both digital and literacy support as part of the Multiply programme. Numeracy support alone is unlikely to tackle the workforce skills issues currently facing Wales, and there is concern amongst further education providers around capacity to deliver solely numeracy support at short notice to the scale of the Multiply funding allocations.

Recommendation 2

UK Government should support lead local authorities with content and funding in order to engage with business specifically to raise awareness of the funds falling under the Levelling Up umbrella. Existing Wales-based engagement capacity within the Department for Business, Energy and Industrial Strategy (BEIS), the Department for the Levelling Up, Housing and Communities (DLUHC) and the Department for International Trade (DIT) should be utilised to deliver this additional support.

Recommendation 3

Welsh Government should build on existing programmes to engage with businesses in raising awareness of new regional structures and the phasing out of key business support packages as a result of the withdrawal of EU funding.

Recommendation 4

UK Government should provide additional funding to lead authorities as part of the UKSPF to bolster existing and develop new innovative forums for businesses to effectively and easily engage with local authorities on economic development planning.

Recommendation 5

Welsh regional lead local authorities should work with Welsh Government to pool funding for business support to develop pan-Wales programmes, including bolstering Business Wales, in order to provide consistent support for businesses across Wales and support links between businesses and local authorities.

Recommendation 6

Welsh and UK governments should build on the Organisation for Economic Co-operation and Development (OECD) 2020 report *The Future of Regional Development and Public Investment in Wales* and undertake an assessment of post-2024 capacity to provide agile financial support to businesses in Wales in need of support to grow or at risk of failure.

Recommendation 7

Innovate UK should undertake a learning exercise with businesses to gather the positive aspects of ERDF innovation funding and apply this learning to future innovation funding processes.

Recommendation 8

UK Government should resource lead local authorities to undertake real-time monitoring and evaluation of the UKSPF regional investment plans, in addition to annual UK level reporting.

Recommendation 9

UK Government should ensure that branding for funding made available through the UKSPF and LUF are clearly identifiable as originating from UK Government.

Recommendation 10

UK Government should lay out the audit process for the UKSPF and LUF.

Putting Businesses at the Heart of Levelling Up in Wales

Introduction

As part of our work focusing on economic development and the UK Government Levelling Up agenda in Wales, the IWA held a roundtable discussion on 23 June 2022. This was the first in a series of related roundtables and focused on the impact of the UK Shared Prosperity and Levelling Up Funds on businesses in Wales. It was attended by representatives from individual businesses, business representative organisations, further education representatives, local government, Welsh Government and UK Government.

The discussions held at this roundtable, in addition to the IWA's body of research on Levelling Up[3], make up the contents of this white paper and inform our recommendations.

As the implementation of the Levelling Up agenda and associated funding programmes continue, the IWA intends to continue convening discussions, supporting concerted action and monitoring the progress of all governments and stakeholders in order to pursue our aim of a successful, clean, green and fair economy for Wales.

3 Watkins, J (2021) What Does Levelling Up Mean for Wales?, IWA

Background

Despite the recent passing of the sixth anniversary of the referendum on the UK's membership of the EU and 18 months on from the end of the transition period, the constitutional and fiscal impacts of Brexit on Wales are only beginning to materialise.

The UK Internal Market Act 2020 and UK Government's Levelling Up agenda have begun to redraw the control, funding and accountability landscape of regional economic, social and cultural development. As part of the UK's membership of the EU, Wales received £2.1bn through the ERDF and ESF combined, during the latest 2014-20 seven-year funding round of ESIF. These funds are managed by the Welsh European Funding Office (WEFO), a Welsh Government agency. As a condition of the 2020 Withdrawal Agreement between the EU and UK, WEFO continues to distribute existing EU funds until the end of 2023, as part of UK Government's intended tapering of European funding.

The ERDF focuses primarily on support to small businesses and on research and innovation, with a secondary interest in decarbonisation. The ESF provides for initiatives and investment to increase employability and skills. At roughly £300m per year, the two funds provided for a significant proportion of the total regional development investment in Wales. To place these funds into context, and although economic development activity is undertaken through other budget sections, the amount set aside for the 'Economy' in Welsh Government's Budget 2022 was £485m.[4]

The process of UK Government design and implementation of funding programmes to support both the staged loss of EU funding and address regional inequalities began shortly following the EU Referendum result.

Following a previous announcement in 2017, the 2019 Conservative manifesto promised:

> *'a Shared Prosperity Fund, to ensure that the people of the UK do not lose out from the withdrawal of EU funding... and to replace the EU programme with one that is fairer and better tailored to our economy'.*[5]

This pledge built on three years of debate over how to replace the circa £2.7bn of European Social and Investment Funds received per year between 2014-20[6], of which Wales received around four times the UK average on a per person basis.[7]

Another key element of the 2019 Conservative manifesto was the concept of 'Levelling Up', an intention to reduce regional inequalities, both economic and social, across the UK. The initial funding response came in late 2019 in the form of the Towns Fund, a £3.6bn pot to which 101 places in England were invited to apply for improvements to infrastructure, focusing on skills and

4 Senedd Research - Welsh Government Final Budget 2022-23
5 2019 Conservative and Unionist Party Manifesto
6 Welsh Affairs Committee (2020) Wales and the Shared Prosperity Fund
7 Welsh Affairs Committee (2020) Wales and the Shared Prosperity Fund

enterprise, regeneration and connectivity.[8] This formed the predecessor to the current Levelling Up Fund.

The 2020 UK Spending Review initially committed £4bn for a Levelling Up Fund in England and £800m for the devolved governments between 2021-25. However, following the passing of the UK Internal Market Act 2020, the direction changed to a UK wide Levelling Up Fund, with a pledge to allocate at least £800m to Wales, Scotland and Northern Ireland.[9] This signalled a significant shift in the governance of Wales, with UK Government undertaking direct investment in areas wholly within the competence of the Senedd and Welsh Government for the first time since 1999.

March 2021 saw the publication of the prospectus for the first round of the LUF.[10] Under the first round of the LUF, local authorities in Wales could apply to UK Government for capital projects focused on:

- Transport investments
- Regeneration and town centre investments
- Cultural investment.

Twelve of the 22 local authorities in Wales submitted one or more bids to the first round of the LUF, of which six authorities were successful, receiving a total share for Wales of £121m, 7% of the total £1.7bn awarded across the UK.[11]

In February 2022, UK Government published a white paper providing the detail behind the goal of Levelling Up the UK by 2030.[12] This document laid out 12 cross-UK Government missions ranging from productivity to crime, skills to housing.

The second round of the Levelling Up Fund, which focuses on the same investment priorities as round one, closed for bids from local authorities on 6 July 2022.[13]

The three years since the conception of Levelling Up have seen the UK change, in some ways beyond recognition. The coronavirus pandemic, the end of the EU transition period and significant global economic uncertainty in part caused by the war in Ukraine have led to a cost of living crisis not seen in five decades. A combination of demographic change, emigration of EU nationals and an increased number of working age people leaving the workforce have combined to deliver a labour market in which many businesses are failing to grow, or even contracting due to lack of available workers. The CPI rate of inflation is set to hit 11% in 2022,[14] further compounding household budgets and reducing discretionary spending. In this drastically changed context, Levelling Up must not only reduce inequalities in the longer term, but arrest economic decline in the immediate term.

8 MHCLG (2020) Towns Fund Prospectus
9 HM Gov (2021) Levelling Up Fund Prospectus
10 HM Gov (2021) Levelling Up Fund Prospectus
11 DLUHC, Levelling Up Fund: First Round Successful Bidders
12 DLUHC (2022) Levelling Up the United Kingdom
13 HM Gov (2022) Levelling Up Round 2: Prospectus
14 Bank of England: How High Will Inflation Go?

The UK Shared Prosperity Fund

Following on from original UK Government announcements in 2017, the launch of the Community Renewal Fund in 2021 and publication of the Levelling Up white paper in February 2022, the prospectus for the UKSPF was published in April 2022.[15]

The UKSPF is designed to succeed ESIF across the UK but is not a like-for-like replacement. The £2.6bn allocated regionally across the UK up until March 2025 is intended to support the UK Government's Levelling Up agenda, not directly replicate the priorities of the EU Regional Development or Social Funds.

According to UK Government, the UKSPF intends to:

> *'Boost productivity, pay, jobs and living standards by growing the private sector, especially in those places where they are lagging*
>
> *Spread opportunities and improve public services, especially in those places where they are weakest*
>
> *Restore a sense of community, local pride and belonging, especially in those places where they have been lost*
>
> *Empower local leaders and communities, especially in those places lacking local agency.'*

Further:

> *'The primary goal of the UKSPF is to build pride in place and increase life chances across the UK. This aligns with Levelling Up White Paper missions, particularly: "By 2030, pride in place, such as people's satisfaction with their town centre and engagement in local culture and community, will have risen in every area of the UK, with the gap between the top performing and other areas closing."'*[16]

Under the UKSPF, regions are invited to develop investment plans detailing how they intend to use their allocated funds and to submit these plans to UK Government for approval. Investment proposals should follow the three priorities laid out in the UKSPF Prospectus:

- Community and Place
- Supporting Local Business
- People and Skills.

15 DLUHC (2022) UK Shared Prosperity Fund: Prospectus
16 DLUHC (2022) UK Shared Prosperity Fund: Prospectus

Multiply

As part of the UKSPF framework, UK Government intend to deliver a UK-wide adult numeracy programme, Multiply. £559m of the total £2.6bn UKSPF funding has been allocated to the delivery of this programme, which will be administered on the same regional basis in Wales as the wider UKSPF and intentions for delivering the programme are to be included as part of the wider regional investment plans.[17]

Business and further education representatives told us that the skills development required to address the current gaps in their workforce go beyond improving adult numeracy. Literacy was cited as a barrier to both gaining employment and effectively engaging in further training and learning, including in numeracy. Similarly, digital skills were raised as crucial to both improving access to work and learning, particularly as digital delivery is core to the Multiply programme.[18]

Recommendation 1

UK Government should allow and encourage Welsh regions to deliver both digital and literacy support as part of the Multiply programme. Numeracy support alone is unlikely to tackle the workforce skills issues currently facing Wales, and there is concern amongst further education providers around capacity to deliver solely numeracy support at short notice to the scale of the Multiply funding allocations.

17 DLUHC (2022) Multiply in Scotland, Wales and Northern Ireland

18 DLUHC (2022) Multiply in Scotland, Wales and Northern Ireland

Delivery of the UK Shared Prosperity Fund in Wales

In Wales, UKSPF funds are allocated to four regional strategic geographies, coterminous with the existing four City and Growth Deals. Allocations for up to March 2025 have been decided as follows:

- Cardiff Capital Region £278.5m (of which £48.1m is allocated to Multiply)
- Mid Wales £42.4m (of which £7.3m is allocated to Multiply)
- North Wales £126.5m (of which £21.8m is allocated to Multiply)
- Swansea Bay £137.8m (of which £23.8m is allocated to Multiply).

Lead local authorities for each region are responsible for the development of an investment plan between April and August 2022. During this period, they are expected to engage with other local authorities and stakeholders in their region.

Lead local authorities must submit their investment plans to the UK Government by 1 August 2022. The UK Government will approve investment plans from October 2022, and approval is needed before any funding is provided. In 2022-23, funding will be paid once the local investment plan has been signed off. In 2023-24 and 2024-25, payment will be at the start of the financial year. Lead local authorities will be asked to return any underspends at the end of each financial year.[19]

Regions in Wales will receive a Multiply allocation as part of their annual payment, with UK Government requiring separate reporting and monitoring for this.

UK Government expects investment and outputs to be achieved in line with the investment plans. UK Government reserves the right to withhold or delay payment and alter payment cycles from 2023-24 onwards where there are performance or other issues with delivery.

19 DLUHC (2022) UK Shared Prosperity Fund: Prospectus

What does this mean for business?

Perhaps unsurprisingly, given the short timetable for development of regional investment plans, we heard that there is low awareness amongst businesses of the overall transition from EU to Levelling Up funding, including the development of UKSPF regional investment plans. Efforts should be made by Welsh and UK Governments to support increased understanding amongst businesses, as a necessary precondition for effective engagement between businesses and lead local authorities throughout this UK SPF period and in the run up to any successor in 2025.

Recommendation 2
UK Government should support lead local authorities with content and funding in order to engage with business specifically to raise awareness of the funds falling under the Levelling Up umbrella. Existing Wales based engagement capacity within BEIS, DLUHC and DIT should be utilised to deliver this additional support.

Recommendation 3
Welsh Government should build on existing programmes to engage with businesses in raising awareness of the withdrawal of EU funding.

Businesses raised the lack of existing strong relationships with local authorities outside the specifically-tasked structures of the City and Growth Deals. These are themselves variable in their engagement with businesses and particularly smaller businesses. Businesses are used to working closely with national bodies such as the Development Bank of Wales and Business Wales, rather than their local authorities. Further to this, many businesses lack capacity to engage effectively with their lead local authority, or with multiple authorities should they operate in more than one region.

On the other side of the relationship, we heard concerns about the capacity of local authorities to engage with businesses. We heard how council economic development departments have withered over the past decade, with high value skills in investment and business support planning lost. This will likely affect not only the ability for councils to effectively engage with businesses during the planning stage for investment plans, but also their capacity to offer support and guidance over the next three years. This may also be compounded by the short timeframe under which lead local authorities are expected to develop and submit regional investment plans under the UKSPF.

However, some representatives explained that councils have existing local economic development plans which, when combined, are likely to form the basis of regional investment plans. This provides some reassurance, but businesses reiterated previous concerns around the efficacy of engagement and planning capacity forming the local plans.

Four percent of regional allocations under the UKSPF are earmarked to support the costs of administering the Fund.[20] However, this is unlikely to provide both the necessary and timely support required for councils to rebuild their economic development capacity and effectively engage with businesses in addition to the day-to-day administration of the Fund.

Recommendation 4
UK Government should provide additional funding to lead authorities as part of the UKSPF to bolster existing and develop new innovative forums for businesses to effectively and easily engage with local authorities on economic development planning.

Recommendation 5
Welsh regional lead local authorities should work with Welsh Government to pool funding for business support to develop pan-Wales programmes, including bolstering Business Wales, in order to provide consistent support for businesses across Wales and support links between businesses and local authorities.

20 DLUHC (2022) UK Shared Prosperity Fund: Prospectus

Business at the Heart of Levelling Up

Immediately prior to the onset of the coronavirus pandemic, small and medium size enterprise (SME) employers provided over half a million jobs in Wales.[21] Employees of SMEs and sole traders make up over two-thirds of the private sector workforce. The ability of these businesses to innovate and grow is crucial to Levelling Up in Wales and in particular the delivery of the first stated aim of the UKSPF:

> *'Boost productivity, pay, jobs and living standards by growing the private sector, especially in those places where they are lagging.'*[22]

In order to grow the private sector, we need to shore up the viable businesses already established in Wales. A combination of the withdrawal of government support available during the pandemic, global supply chain issues, workforce shortages and rising input costs are likely to manifest in business failures during 2022 running at a level one-third above pre-pandemic levels.[23] In the context of this challenging environment, we heard concerns from businesses over the capacity of local authorities, Welsh and UK Governments to provide agile support to businesses. Businesses require absolute clarity over where to request and how to access support.

Recommendation 6

Welsh and UK governments should build on the OECD 2020 report *The Future of Regional Development and Public Investment in Wales* and undertake an assessment of post-2024 capacity to provide agile financial support to businesses in Wales in need of support to grow or at risk of failure.

UK Government rightly identifies innovation as the key to driving economic growth.[24] This is particularly relevant in the current context of workforce shortages and heightened input costs.

Businesses told us that access to innovation funding is crucial to their development. Although they described it as overly-bureaucratic and inflexible in some other regards, businesses considered funding through the ERDF for business innovation as straightforward to access. Conversely, we heard that accessing funding through Innovate UK, part of UKRI, proved more difficult, with the process being described as 'opaque'.

In order to achieve private sector growth in Wales and deliver on the goals of the UKSPF, it is important for businesses to have clarity over where to access innovation funding and for this funding to be available, with those making decisions clearly understanding the local context.

Recommendation 7

Innovate UK should undertake a learning exercise with businesses to gather the positive aspects of ERDF innovation funding and apply this learning to future innovation funding processes.

21 Welsh Government (2021) Longitudinal Small Business Survey 2019

22 DLUHC (2022) UK Shared Prosperity Fund: Prospectus

23 Astradius Insolvency Forecast 2021

24 BEIS (2021) UK Innovation Strategy

Monitoring and Evaluation

The UKSPF will deliver £2.6bn in funding across the UK, in addition to the LUF and other programmes. Considering the level of public money being invested, and the novelty of the programmes, it is important that a culture of constant learning is established as early as possible.

The UK SPF prospectus states:

> *'We are developing a national approach to evaluation, including a scoping study in partnership with the What Works Centre for Local Economic Growth. The evaluation methodology cannot be fully specified until we have received investment plans and understood the range of activities to be funded. This may include pooling or synthesising data from several different areas.'*[25]

Whilst we welcome this more bottom up approach, taking into account the intentions of each region, a UK-wide evaluation and monitoring process must take into account the devolved context in Wales and be sufficiently resourced to gather meaningful, real time learning both to inform the successor to the UKSPF in 2025 and support improved decision making over the next three years.

Recommendation 8

UK Government should resource lead local authorities to undertake real-time monitoring and evaluation of the UKSPF regional investment plans, in addition to annual UK level reporting.

25 DLUHC (2022) UK Shared Prosperity Fund: Prospectus

Accountability

Under the Wales Act 2017, Welsh Government and Senedd Cymru hold broad responsibility and powers over economic development in Wales, with specific powers reserved at a UK level in order to maintain the integrity of the UK, such as fiscal policy.[26] The Welsh Government cabinet includes a Minister for Economy and the Welsh Government budget contains a corresponding budget grouping. As a result, Welsh residents should be able to hold Welsh Government accountable for measures taken to improve economic development of the country, with an understanding that external forces at a UK and global level also play a part in any economy's performance.

However, powers under the UK Internal Markets Act 2020 powers are being used by UK Government to provide direct economic development investment, through local authorities, to Wales' regions in policy areas that are otherwise devolved. In addition to concerns over potential duplication of interventions between Welsh, UK and local governments, we heard and we share concerns about which level of government is ultimately accountable for which intervention.

In particular, to ensure democratic accountability, we believe it is necessary to have clarity for businesses and the wider public over where funding has originated and how it has been allocated. Additionally, it should be made clear how the various funding programmes under the Levelling Up umbrella are to be audited, to which standards and by which audit body.

Recommendation 9
UK Government should ensure that branding for funding made available through the UKSPF and LUF are clearly identifiable as originating from UK Government.

Recommendation 10
UK Government should lay out the audit process for the UKSPF and Levelling Up Fund.

26 Law Wales, Economic Development: What is devolved?

Conclusion

The success of individual businesses is key to the achievement of the UK Government's Levelling Up agenda in Wales. Through our roundtable discussions, we repeatedly heard concerns about the complex challenges faced by businesses in Wales and the confusion caused by the significant changes underway as the UK and Wales transition away from EU funding and begin to operate within the era of Levelling Up.

Everyone involved in and seeking the success of the Welsh economy must continue to look forward. European investment is now in the past, and whilst we must learn from its positive aspects, now is the time for all governments, civil society and business to pull together to drive Wales forward.

The IWA looks forward to holding further discussions with other sectors across the Welsh economy in the coming months and years, acting as a convening force and holding all governments to account, as new post-Brexit challenges and opportunities continue to arise.