THE ALLOCATION OF LOCAL GROWTH FUNDING

Possible methods and indicators

Background

The UK government intends to reform local growth funding. The plan is that a new structure will be announced at the Spending Review in the spring of 2025 for implementation from 2026-27 onwards.

The funding to be allocated is potentially substantial and a successor to the previous administration's 'levelling up' funds[1]:

Levelling Up Fund (three rounds)	£4,756m
UK Shared Prosperity Fund[2]	£3,412m
Towns Fund	£2,350m
Town endowments	£1,500m
Future High Streets Fund	£ 831m
Levelling Up Partnerships	£ 400m
Community Renewal Fund	£ 203m

In addition, in the last spending round the regions received around £3bn in EU funding carried forward and the devolved administrations received funding via the Barnett formula to compensate for the programmes (such as the Towns Fund) that didn't operate in Scotland, Wales and Northern Ireland. Adding all this together, around £17bn was allocated to 'levelling up' through to March 2026.

The reform of local growth funding is welcome. There have been too many funding schemes, often with overlapping objectives, and the short-term basis of funding – typically two or three years – has undermined strategic thinking and value for money. The government's intention to move away from competitive bidding is also welcome. Much time and energy has been wasted on unsuccessful bids and it is far from clear that competitive bidding has delivered better outcomes. But if bidding is to be phased out, future funding will need to be allocated by formula.

What needs to be kept in mind here is that the 'levelling up' funds were not spread evenly across the country. They were skewed towards the least prosperous parts of the UK:

[1] Source of financial data: HM Government
[2] Including £900m for 2025-26 announced in Autumn Budget 2024

	'Levelling up' funding[3] £ per head	GVA per head 2021 (UK=100)
Wales	377	74.1
North East	346	70.6
North West	265	87.4
Yorkshire & the Humber	262	80.5
East Midlands	257	80.3
West Midlands	225	81.2
South West	182	89.8
Scotland	165	90.5
Northern Ireland	157	79.4
East	139	89.3
South East	91	107.4
London	56	183.4

Consultation

Bearing in mind the sums at stake and the considerable interest in this funding among local authorities in all parts of the country, there needs to be full and timely consultation on the allocation formula. The formula needs to command confidence and the errors that characterised the identification of 'priority areas' by the previous administration need to be avoided.

The government should note that consultation of this kind is not without precedent. In drawing successive Assisted Area maps for example, most recently for 2014-20, to define the parts of the UK where businesses were eligible for regional investment aid, the government consulted on indicators and indeed on a draft map. There was little resulting criticism of the final maps.

There is time, ahead of the implementation of reformed local growth funding in 2026, to undertake a full consultation.

The present note is intended to offer early thoughts on what the government might propose. It builds on ideas and experimental statistics shared previously with government when a replacement for EU funding to the regions was under consideration.

[3] The figures here combine the seven 'levelling up' spending programmes but exclude roll-on EU funding, monies allocated via the Barnett formula and the £900m top-up to the UKSPF for 2025-26.

Geographical building blocks

If the primary objective of funding is to strengthen less prosperous local economies and thereby to raise employment, incomes and reduce deprivation, a sub-regional focus is appropriate. Local economies mainly operate at this scale – they cover areas larger than most unitary and lower-tier authorities but stop well short of standard statistical regions. The diversity in economic performance across the UK is also greatest at the sub-regional scale.

There are a number of ways in which sub-regions might be defined. Combined authorities, city regions and (in some cases) counties are plausible alternatives. In the largest counties, sub-regions might best be defined as groups of neighbouring districts (e.g. East Kent) especially where socio-economic conditions diverge.

If funding were to be allocated at this sub-regional scale it does not of course imply that specific initiatives might not operate at the local scale, right down to neighbourhood level. Exactly how and where money might be spent is a matter that local partners would need to determine.

Potential indicators

If the primary aim is to raise the economic performance of weaker local economies the indicators need to reflect:

(1) The output or productivity of local economies

(2) The strength of the local labour market.

Taking the output/productivity of local economies first:

Gross Value Added (GVA) per head
This is a sound measure of the size of a local economy in relation to its resident population, and a familiar one because of its long-standing role in the allocation of EU funding. It works tolerably well at the sub-regional scale but not for smaller units because of net commuting. Statistics are published by ONS.
VERDICT: A good choice

GVA per job (or per hour worked)
This is a better measure of productivity (though one that generally reflects the mix of industries and occupations) but a poor measure of local prosperity because it ignores the big differences in the proportion of the workforce that is not in employment. Again, statistics are published by ONS.
VERDICT: GVA per head is better

Regarding measures of the strength of local labour markets, some options are distinctly better than others:

> ***Unemployment rate***
> This is the traditional indicator of labour market slack. These days the official preference is for the ILO measure from the Labour Force Survey (LFS), which counts those who have looked for work in the last four weeks and are ready to start in the next two weeks. The key problem is that ILO unemployment is now low in most places whilst there are far more adults of working age who are 'economically inactive'.
> VERDICT: An increasingly flawed measure
>
> ***Employment rate***
> The 'employment rate' – the share of adults of working age in employment – provides a fuller view but as a measure of the strength of local labour markets is distorted by the uneven distribution of economically inactive students, who are concentrated in the cities.
> VERDICT: A possibility, but only if students are excluded
>
> ***Economic inactivity rate***
> This is the share of adults of working age who are neither in employment nor looking for work. Now that the big numbers out-of-work are economically inactive rather than unemployed it's a good measure of the strength of local labour markers but to provide a reliable local picture students again need to be excluded – DWP did this recently in its *Get Britain Working* White Paper.
> VERDICT: Another possibility, but only if students are excluded
>
> ***Out-of-work benefit claimant rate***
> This is wider than unemployment because it brings in a total of more than 5m working age adults, including the 2.8m out-of-work on incapacity benefits who are concentrated in less prosperous areas and often 'hidden unemployed'. Can be assembled for local areas from DWP data.
> VERDICT: A strong contender

A complication with the first three of these indicators (unemployment, employment, economic inactivity) is that they would normally be taken from the Labour Force Survey. Declining response rates have recently brought LFS data into question at the national level (as ministers have acknowledged) and at the sub-regional and local level the small sample sizes have always meant that the annual data is erratic, requiring several years' data to be pooled to provide a more reliable picture.

In view of the shortcomings of LFS data for local areas, there are considerable merits in using DWP benefits data instead. The DWP data is a robust administrative count, available right down to the very local level.

Less helpful indicators

There are a number of indicators that, despite their usefulness for other purposes, would probably be inappropriate in allocating local growth funding.

Low pay
There are jobs paying low wages in all parts of the UK and the gap between rich and poor is not a good guide to the overall prosperity of a local economy, as London shows only too well. Median earnings by sub-region are more helpful.
VERDICT: Not the sharpest of indicators

Household income
Gross Disposable Household Income provides a wider view than just wages, but because it adjusts for taxes and benefits it is a step removed from measuring the strength of the local economy.
VERDICT: Not ideal

Qualifications
The share of working age adults with a degree (or NVQ4 or above) sharply differentiates between places but is better for sub-regions rather than districts because of residential sorting. In all areas, 'no qualifications' is these days a small and declining group of mainly older workers who left school before qualifications became the norm.
VERDICT: Of value if the right skills indicator can be defined.

Indices of Deprivation
The Indices of Deprivation have superficial attractions because they are detailed and available right down to neighbourhood (LSOA) level. However, they stray a long way from measuring the economic well-being of local areas. Alongside economic and labour market variables they add in indicators of health, housing, crime and the environment. In practice too, the Indices often reflect residential sorting between rich and poor neighbourhoods, especially within the big cities. A focus on the poorest neighbourhoods rather than the poorest sub-regions would therefore skew funding towards London. A further complication is that the Indices of Deprivation in the four nations of the UK are not compatible in content or timing.
VERDICT: A poor measure of the strength of local economies

Population density
High population density is not necessarily associated with high productivity or prosperity (see several northern cities) and low density is not necessarily an indicator of economic disadvantage (see several rural areas).
VERDICT: Avoid