



ABERDEEN ECONOMIC POLICY PANEL REPORT

DECEMBER 2022

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Foreword

This is the Panel's fifth annual report and the second of its second three-year term. In producing this report and in making its recommendations, the Panel has monitored and considered developments in the North East, Scottish, UK, and international economies. The Panel has undertaken its own analysis and considered research relevant to its work.

The Panel's approach has been to review the latest data to gain an up-to-date picture of the North East economy, building on the broader longer-term trends described in previous reports.

The Panel has also provided a forum for discussing emerging issues concerning the future prosperity of the Aberdeen and Aberdeenshire economies with key stakeholders.

Panel members have met with various stakeholders, including Aberdeen and Grampian Chamber of Commerce (AGCC); Aberdeen City Council political leaders and officers; Aberdeenshire Council political leaders and officers; Aberdeen City and Shire Hotels Association; Aberdeen Harbour Board; Aberdeen International Airport; Bon Accord Centre; BP; Burness Paull; CBRE; Deloitte; ETZ Ltd; Federation of Small Businesses (FSB); Knight Frank; KPMG; Net Zero Technology Centre; Offshore Renewable Energy Catapult; Oil and Gas Authority; Oil and Gas UK; Opportunity North East (ONE); P&J Live; Pinsent Masons; Robert Gordon University; Royal Bank of Scotland; Ryden; Savills; Shell; Skills Development Scotland (SDS); Union Square; University of Aberdeen; and VisitAberdeenshire.

Although the views in the report are that of the Panel, the assistance of Aberdeen City Council, external stakeholders, and local industry in preparing this report has been greatly appreciated.

Notes

Geographic definition

For the purposes of the analysis, the North East refers to the Aberdeen City Council and Aberdeenshire Council local authority areas.

Bond rating

Moody's awarded Aberdeen City Council an Aa2 rating with a negative outlook in October 2016. This rating was one notch below the UK Government and is the third highest level out of 21 categories, placing the Council in a high-grade investment bracket. The rating is reviewed by Moody's on an annual basis. Aberdeen City Council has had an A1 rating since 2020 and the outlook was downgraded to negative in October 2022.

The annual credit rating assessment involves an analysis of the Council's financial and institutional framework, as well as an assessment of the economic performance of Aberdeen and the wider region. In terms of the economic analysis, and as in previous years, the independent economic commentary in this report is used to not only support the Moody's annual review, but also to help inform investors over the medium-to-long-term economic outlook of Aberdeen and wider region.

The Council approved the appointment of an Economic Policy Panel in March 2017 to provide independent commentary on the state of the Aberdeen economy in the form of an annual report each year from 2018 to 2020. The Panel has since been reappointed to produce a further three annual reports from 2021 to 2023.



The Panel

Dougie Peedle: As well as being a member of the Aberdeen Economic Policy Panel, Dougie is the economist member of the Armed Forces Pay Review Body and Head of Economics and Valuing Nature at the RSPB. He was also recently an Economic Associate for Pro Bono Economics and Head of Policy for Scottish Wildlife Trust. From 2004 to 2018 he was Chief Economic Adviser to the Government of Jersey and prior to that worked for 10 years in London as Deputy Chief Economist at EEF, International Economist at Rio Tinto and Senior Economist at the CBI. He is a graduate of the University of Aberdeen and the Scottish Masters Programme in Economics.

Professor Graeme Roy: Graeme is Professor of Economics and Dean of External Engagement in the College of Social Sciences at the University of Glasgow. Graeme is a former director of the Fraser of Allander Institute (FAI) at the University of Strathclyde, and a former Senior Civil Servant in the Scottish Government.

Due to other work commitments Dr Hanan Morsy, a former Panel member, left the Panel in August 2022.



Summary

The global economy faces its second economic shock in a little over two years. This time last year, the Panel's report spoke of increased optimism of a return to growth after the COVID-19 pandemic.

However, high inflation driven by surging food and energy prices and the implications for the cost-of-living has ushered in another global slowdown and likely recession in the UK. The North East economy is not immune to such pressures. With the energy sector playing an important role in the local economy the impact of the recent spike in energy prices has brought renewed activity for many businesses, but other sectors have faced a considerable increase in costs, loss of earnings, and a further period of uncertainty and instability.

This new set of economic trends providing yet more turbulence for the local economy reinforces the Panel views from previous reports of the importance of maintaining a long-term focus for the strategic approach to Aberdeen's economic development. That is, a focus upon diversification, investing in key areas of comparative strength in the region and improving the core enabling factors of an economy – skills, connectivity, and an attractive sustainable environment to live and work.

This year's recommendations are listed in full below. They are the views of the Panel. The Panel are grateful for the insights and reflections from the many stakeholders that met from across the region during the development of this year's report and the assistance of Aberdeen City Council officers.




2022 Recommendations

In previous reports, the Panel has made a series of recommendations that it believes will support the continued prosperity of the North East economy. Many of these recommendations remain as relevant today as they did when the Panel first made them.

For 2022, the Panel reaffirms the importance of this advice. The Panel has, however, identified a set of new recommendations which, whilst building on past recommendations, offer updated insights relevant to the current context. These recommendations flow from the Panel's assessment of economic conditions – both now and in the future – and its discussions with key stakeholders. These new recommendations are presented below.

1. The Panel recommends that the Council coordinate a time-limited review to identify which sectors may be under the greatest pressure from the current macroeconomic climate – including rising costs and prices, labour shortages, availability of capital finance and falling consumer demand. The Council should, involving discussions with national policymakers, identify options for targeted, temporary, and timely support and assess whether they can assist these sectors through the downturn and at the same time reinforce the strategic approach to placemaking in Aberdeen.
2. The Panel welcomes the development of the Regional Economic Strategy report and recommends:
 - There is strong buy-in from all stakeholders across the community
 - A focus upon the long-term challenges and opportunities facing the region, with built in flexibility and adaptability to change
 - It should be one plan, not time bounded and designed so that it refreshes going forward.
 - It is accompanied by detailed implementation and resource plans
 - There are key measurable outcomes, and a process for monitoring and evaluating progress - drawing upon North East Performs – across all the key aspects of place making (economic, social and environmental).
3. The recent initiatives to support the regional labour market are welcome but the skills challenges facing the local economy have been compounded further by the rise in inflation and labour market shortages that have proliferated across the UK economy. The Panel reiterates its recommendation from last year of the value in developing and publishing an updated skills strategy which builds on the approach at the national level, supports the direction of the new Regional Economic Strategy and the strategic direction set out in the Route Map to Aberdeen the Place. It should be SMART and supported with a clear delivery plan.
4. To achieve sustainable and long-term energy security, policymakers and business leaders must continue to take bold decisions to support an accelerated Just Transition toward new and green energies. The risk that recent uncertainty poses to energy transition in the region must be recognised by all stakeholders and addressed to ensure that the region's approach to net-zero is not derailed. This requires renewed collaboration between all tiers of government and industry, aligning behind agreed policy outcomes.

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- An aerial photograph of Aberdeen, Scotland, showing the city's skyline and a large ship docked at a quay. The ship has 'DCF' and 'Techno-Pac' visible on its side. The image is overlaid with a semi-transparent white box containing text.
5. The Panel welcomes the approach being taken in the Aberdeen City Centre and Beach Masterplan and other initiatives but as set out last year, encourages a greater pace of change and holistic approach to developing ‘Aberdeen the Place’.

The Route Map the Panel advocated in both the 2020 and 2021 reports should aim to be progressed more quickly and build on the approach in the new Regional Economic Strategy. It must also be supported by and reflected in other key strategies and have buy in from across the community.

It will help set the overall strategic approach for the region in the long-term and help coordinate action. There is both a clear economic imperative and a clear demand to move more quickly on redeveloping the city, taking critical decisions and setting out the plan for change.

6. The performance of TECA has understandably been influenced by the pandemic and cost of living shock, and will be one of the factors contributing to the funding gap. Post-pandemic, ACC should deliver an assessment of how it – and other recent key investments - are performing against its objectives and how it can inform future plans for investment in infrastructure.
7. The Council should continue to update its Medium Term Financial Strategy work, particularly in the light of changing funding outlooks. This should include examining spending commitments and revenue options.
8. The Panel observes the increasing focus of national policymakers to prioritise investments in key localities subject to national priority guidelines and successful bids from local areas such as through the Just Transition Fund, UK Shared Prosperity Fund and Levelling Up Fund. It is important that Aberdeen is ready to respond to these opportunities building upon the agility of local policymakers, flexibility and partnership working. In addition, the region needs to plan for how it will resource the planned initiatives around the economic strategy and development of Aberdeen the place.

1 Economic Performance

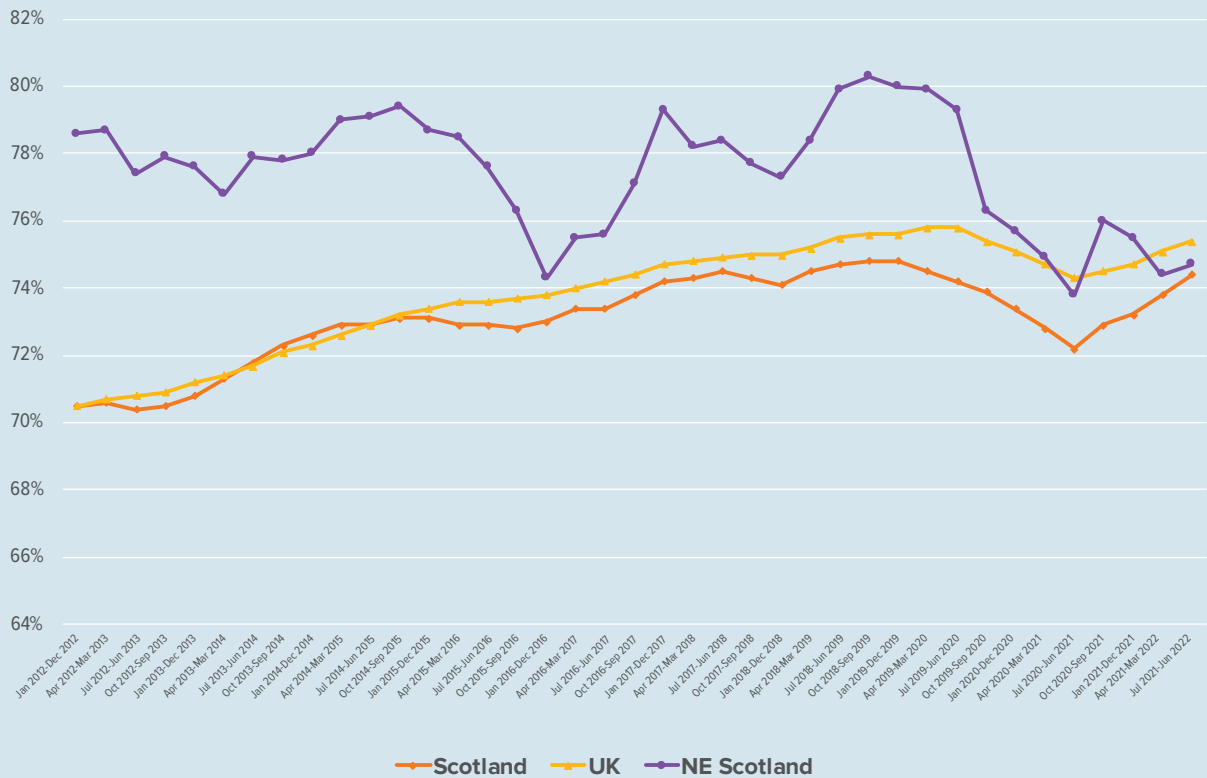
A year ago, the outlook for the global, UK and North East economies had been relatively healthy. The expectation had been that 2022 and 2023 would see the economic recovery accelerate after the pandemic. Earnings were rising, unemployment was falling, and by late 2021/early 2022, both the UK and Scottish economies had recovered to near their pre-pandemic levels of economic output.

The outlook today, driven, in part, by a global energy shock, now looks more challenging. Both the Bank of England and the Office for Budget Responsibility believe that the cost-of-living crisis has tipped the UK into recession. The UK economy is projected to contract through to near the end of 2023, with real household incomes projected to fall at their fastest rate since records began.

The North East economy will not be immune from such pressures. Whilst it starts from a strong base, with GVA and average earnings levels higher than the national figures, it has faced several challenging years. For example, over the last two years, the Panel notes that employment rates in the North East have fallen at a steeper rate than in Scotland and the UK. Employment fell by 16,600 across the North East from 2019 to mid-2022. Employment in Scotland as a whole only fell by 19,600 in this period¹.

Employment rate - Aberdeen City, Aberdeenshire, Scotland & UK (2012-2022)

Percent of resident-based population aged 16 to 64
Source: ONS



The Panel also heard from stakeholders of broader indicators of economic performance. For example, whilst levels of entrepreneurship, innovation and internationalisation remain high, demand for business properties remains weaker than in other cities in the UK and retail footfall continues to underperform. Key stakeholders in the energy sector indicated that the recent rise in oil and gas prices has led to improved labour market conditions, particularly in earnings. But at the same time, increased costs, higher taxes, and skills shortages have acted as a brake on expansion rates.

¹ NE Performs: Annual Population Survey.

Forecast comparison, GDP growth rates (%)					
	2022	2023	2024	2025	2026
Scotland - GDP					
Scottish Fiscal Commission	5	-1.2	0.7	1.9	2.1
Fraser of Allander Institute	3.6	-0.6	0.8		
UK - GDP					
Bank of England	4.25	-1.5	-1.00	0.5	
Office for Budget Responsibility	4.2	-1.4	1.3	2.6	2.7
Independent Forecasts*	4.2	-0.9			
World - GDP					
International Monetary Fund	3.1	2.7	3.2	3.4	3.3

Source: Scottish Fiscal Commission: Dec 2022, Fraser of Allander Institute: Oct 2022, Bank of England Monetary Policy Report: Nov 2022, *Independent Forecasts by HM Treasury: Nov 2022, Office for Budget Responsibility: Nov 2022, International Monetary Fund: Oct 2022

Looking forward most independent forecasters predict a recession in the UK and Scottish economies next year. The North East Economy will likely see a similar contraction in economic output. In their most recent reports, the Scottish Fiscal Commission and the Fraser of Allander Institute have downgraded their forecasts for Scotland. At a UK level, forecasts have been sharply downgraded by the Bank of England and the International Monetary Fund, as well as lower global GDP forecasts.

The Panel notes that business and consumer confidence measures report a similar picture. Business confidence in both Scotland and the UK has turned negative in Q3 2022, for the first time since 2020². Four in ten businesses believe their profitability will reduce over the next 12 months³. Only a minority of businesses now expect an increase in business activity over the next six months⁴.



² The Institute of Chartered Accountants: Q4 2022. Link. Please note that no data was gathered in Q3 of 2020 due to the pandemic so a dashed trend line has provided a link to connect the Q2 to Q4 of 2020.

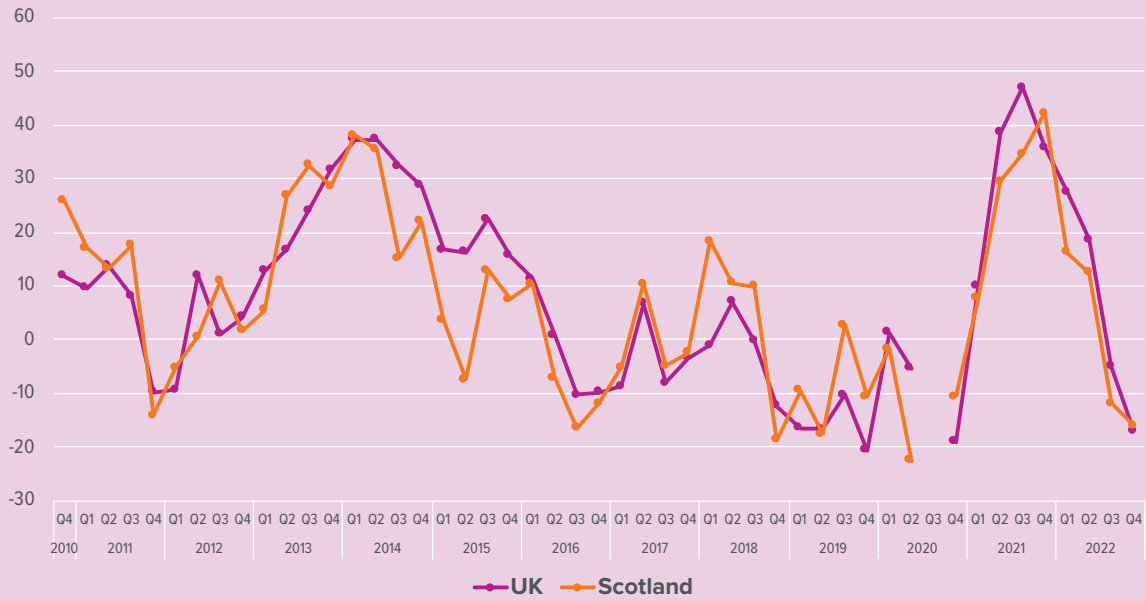
³ British Chambers of Commerce: link

⁴ Fraser of Allander Scottish Business Monitor, Q3 2022.

Trends in UK and Scottish business confidence: Q4 2010 - Q4 2022

How would you describe your confidence in the economic prospects facing your organisation over the next 12 months, compared to the previous months?

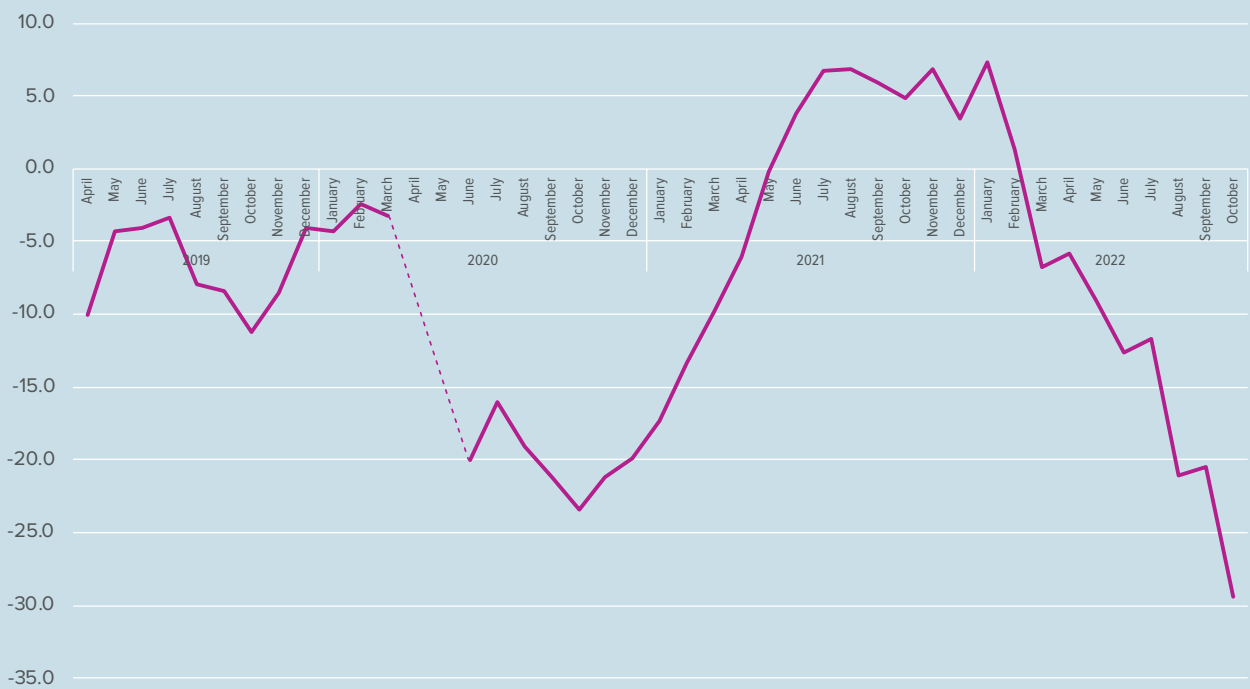
Source: The Institute of Chartered Accountants



The combination of falling real incomes and rising costs have pushed UK consumer confidence into negative territory in September 2022⁵, with Scottish consumer sentiment showing a broadly similar pattern⁶.

Scottish consumer sentiment indicator: Apr 2019 - Oct 2022

Source: Scottish Consumer Sentiment Indicator: Scottish Government



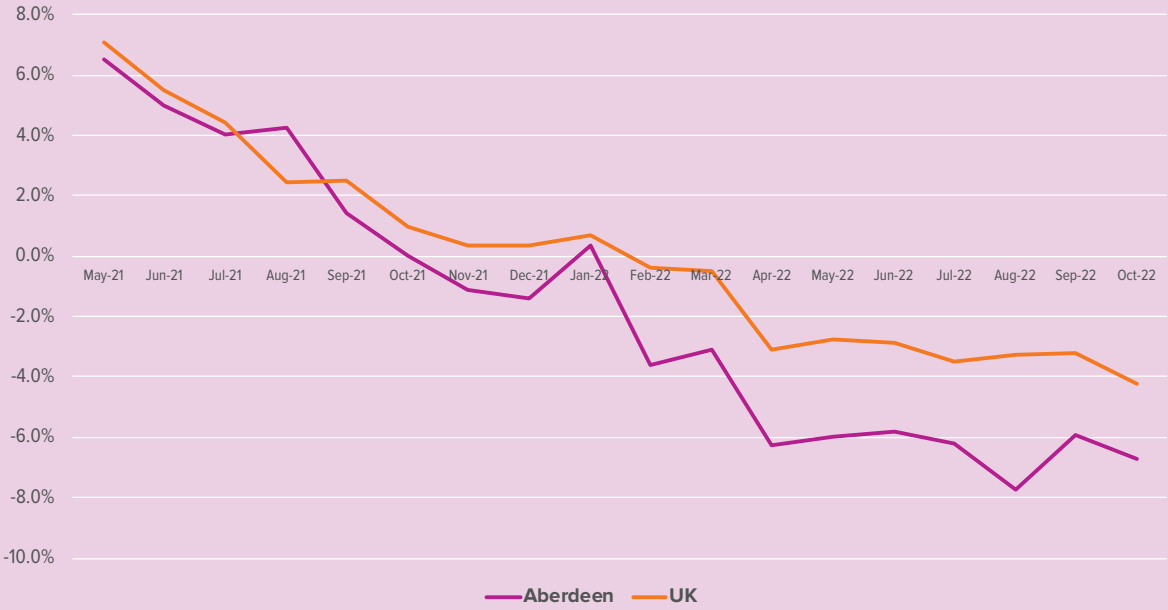
⁵ Growth from Knowledge, Consumer Confidence Barometer, September 2022: (Records began in the 1980s)

⁶ Scottish Government, Consumer Sentiment Monthly Data, October 2022. Dotted line link - no data was gathered for April and May 2020 due to the pandemic so a trend line has provided a link from March to June 2020.

The Panel heard from stakeholders that the current cost-of-living crisis is already impacting the region. Indeed, there are some signs that real median pay has fallen more sharply in Aberdeen than in the UK, as illustrated below. This is likely due to the concentration of workers in the energy sector in Aberdeen and the fall in employment during the pandemic. On average, people’s wages in Aberdeen are £129 a month lower than in October 2021 (in real terms), the 3rd biggest drop in monthly earnings in Scotland and the 6th largest drop in the UK⁷.

Median real wage growth (year on year) Aberdeen City and United Kingdom: May 21 - Oct 22

Source: Centre for Cities inflation data and ONS: PAYE median pay



Several stakeholders told the Panel that the effects of the economic slowdown, and the impact of rising prices, were different across sectors. The report examines how key sectors have been faring in the next section.

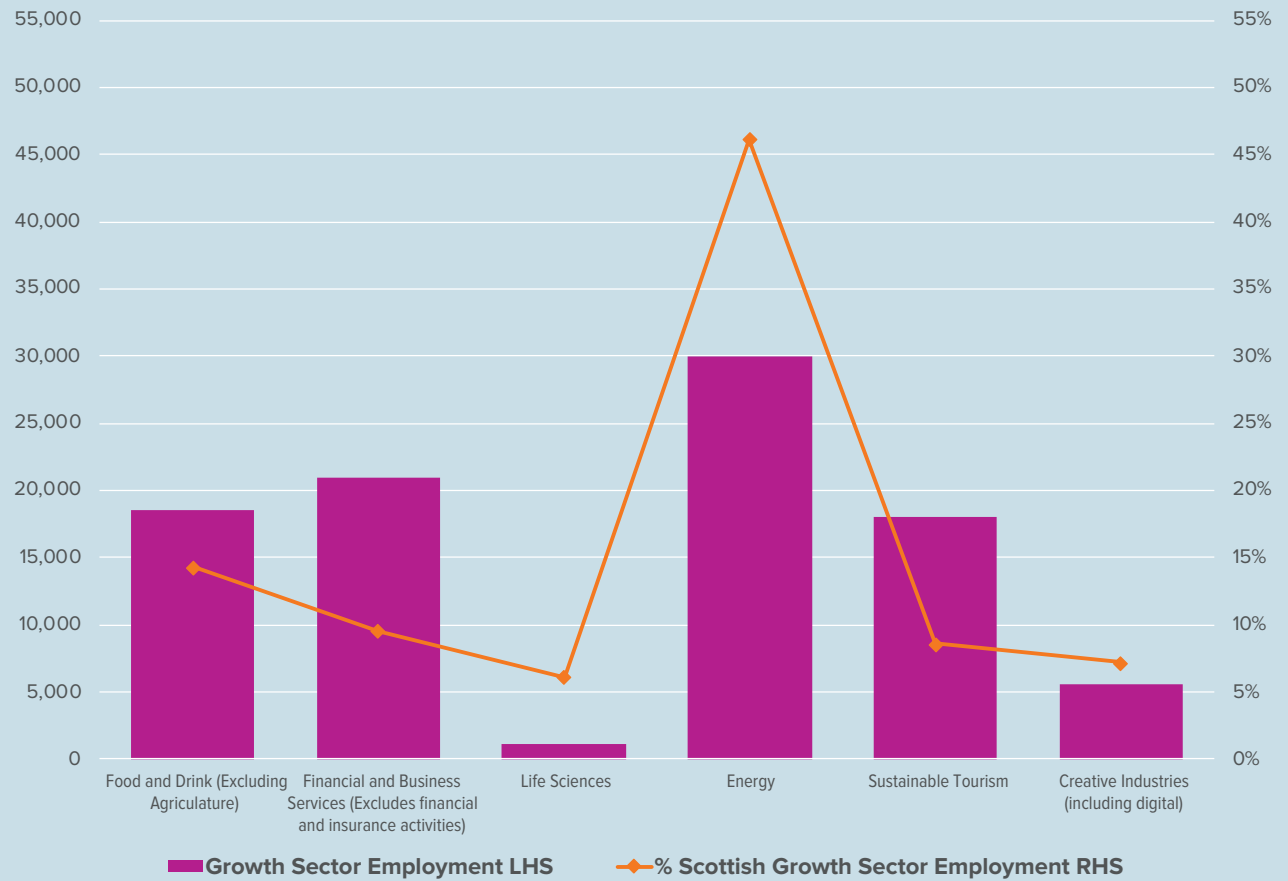


⁷ NE Performs: Median HMRC PAYE data and Centre for Cities Cost of Living Tracker October 2021 to October 2022.

2 Diversification: Key Sector Performance

Growth Sector Employment & Share (%), North East, 2021

Source: Scottish Government Growth Sector Statistics



In previous reports, the Panel has stressed the importance of investing – at scale – in key sectors and business activities where the North East economy has a comparative advantage. Such an advantage helps the region be competitive in attracting skilled workers or securing new investment.

For over five decades the North East has been anchored around the oil and gas sector (see chart above). This has helped to propel the region to be one of the most prosperous in the UK, with higher average earnings than most other parts of the country.





Image © Felix Mooneram

Oil and gas will remain an important part of the region's economic environment for decades. However, policymakers and businesses in the region have a clear consensus on the need to diversify. This includes transitioning into new forms of renewable energy and supporting the growth of other high-value jobs and businesses in other non-energy sectors.

The Panel has been observing the efforts of the region – supported by organisations such as Opportunity North East, the Higher and Further education sectors and the Aberdeen and Grampian Chamber of Commerce – to grow key sectors of strength beyond oil and gas, including tourism, food and drink, life sciences, agriculture and fishing, and the creative industries. This approach is embedded within the Aberdeen City Region Deal, and the Panel expects this approach to be reaffirmed in the upcoming Regional Economic Strategy. Alongside this, the Panel has noted the investment in the digital and technology sector in the region, including leveraging from the strong graduate base within the city itself.

But the Panel notes that many of these sectors will be negatively impacted by the cost-of-living crisis and UK-wide recession. It also notes, informed by its discussion with stakeholders, that the effects may not be distributed uniformly across sectors.

- 1. The Panel recommends that the Council coordinate a time-limited review to identify which sectors may be under the greatest pressure from the current macroeconomic climate – including rising costs and prices, labour shortages, availability of capital finance and falling consumer demand. The Council should, involving discussions with national policymakers, identify options for targeted, temporary, and timely support and assess whether they can assist these sectors through the downturn and at the same time reinforce the strategic approach to placemaking in Aberdeen.**

In what follows, the Panel provides a summary of key discussion points raised during its engagement with stakeholders in key sectors. These points are designed to summarise this engagement rather than an exhaustive review of performance.

Tourism

On balance, industry stakeholders informed the Panel that the sector had witnessed a year of relative stability following the disruption caused by the pandemic. Demand had picked up, although business tourism and events remained relatively weak.

Most of the recovery in demand appears to have come from the domestic market, with the lucrative international market still lagging behind⁸. Passenger volumes at Aberdeen International Airport are recovering, but data obtained for the Panel shows demand is still only 70% of pre-pandemic levels.

Stakeholders indicated a weakening optimism for the coming months. Twin pressures of increased costs – including transport – and labour availability are negatively impacting the sector. Many of the challenges facing the sector, particularly with regard to skills, are not new. The Panel therefore continues to support the work of ONE and other partners in its efforts to boost skills in the sector, including the new ONE-led Hospitality Apprentice North East (HANE).

The Revenue generated per Available Room (RevPAR) for Aberdeen hotels in 2022 was £40.85 to the end of October 2022, up from £36 in 2021, and now exceeding the £40.20 mark from November 2019. Occupancy rates remain below pre-pandemic levels.

The Panel welcomes the publication in August 2022 of the refreshed Destination Tourism Strategy with its aspiration for the North East to establish itself as a leader in Scottish tourism with longer lengths of stay, and higher spend per head⁹.

Several stakeholders told us that there is the belief that “Aberdeen city is used as a base and not as an attraction itself”. There is an appetite across the sector to be more ambitious about the regeneration of the city post-pandemic, particularly if the aim is to attract greater numbers of city-style tourism. Event 365 has the potential to encourage passengers from the new cruise ships arriving at the Harbour to come into Aberdeen. Delivery of the Destination Tourism Strategy is all-important and needs to be monitored and adjusted as opportunities and risks emerge.

We heard of more general support for stimulating demand in the wider region. This includes Visit Aberdeenshire promoting Aberdeen to the tourism supply chain through hosting the annual UK Inbound Convention for leading trade buyers.

The immediate cost-of-living crisis will likely make the next 18 months challenging for the tourism sector. These challenges will be multifaceted, from likely reduced visitor demand and spending and increased costs of doing business and attracting/retaining skilled workers. A continued focus on high-quality tourism experiences and investment in skills will be critical to its long-term future. This aspect should be considered in the sector review recommended above.



⁸ The Panel notes that this is not just limited to the North East. VisitBritain has for example, downgraded its 2022 forecast for inbound travel to the UK, with only 52% of 2019 levels expected.

⁹ Destination Aberdeen & Aberdeenshire: A Framework for Growth 2022-2030

Food and Drink

The Panel heard how post-lockdown the North East food service sector experienced a sharp increase in activity. The Panel was updated on a range of positive initiatives in the region, including Opportunity North East business-led support programs for the food and drink industry. Stakeholders did however, highlight several challenges facing the sector. Again, many of these are familiar to other sectors in the region (and indeed, across the UK). The Panel heard of vacancy rates in some businesses being as high as 20% on occasion, leading to some labour-intensive processors turning away business and simplifying product ranges. Energy costs are high in the sector, even in normal times, with the recent spike in prices having a disproportionate impact upon running costs, particularly those relying upon cooking and refrigeration activities. There also appear to be some sector-specific challenges, including supply blockages – perhaps related to EU-Exit – in packaging, some ingredients, haulage capacity, and a shortage of export containers.



Image © Felix Mooney/rpm

Life Sciences

The Panel was updated on the plans to continue to grow the life sciences sector in Aberdeen. This is an excellent example of a sector that could be key in the future of the North East economy. It creates highly skilled, high-value added jobs and builds on the comparative strength of the region as a hub of skilled labour. The North East hosts over 10% of Scotland's life sciences companies, many of which are plugged into the university community.

The Panel heard how the pandemic caused disruption in several research areas, but that employment has continued to rise since then. The latest estimates are that direct job numbers in the sector – excluding the indirect jobs that this activity supports or the research activities within the Universities and Research Centres – have increased from 775 to 1,100 from 2019 to 2021¹⁰. The Panel also heard how the pandemic had created exciting new opportunities in areas such as health therapies.

¹⁰ Scottish Government Growth Sector statistics

Digital

As the Panel has indicated in previous reports, the digital sector is not only an important sector for the region in its own right, but also has the potential to help underpin strong high-value growth across many other sectors, from energy transition through to tourism.

Digital transformation is taking place across key sectors, including a new agritech programme with two demonstrator farms established in the region and a process change accelerator pilot for food and drink manufacturing businesses.

The Panel was pleased to hear of the ongoing development of the ONE Tech Hub that is now home to various strategic partners, including Innovation Centres, Barclays Eagle Labs and the Scottish 5G Centre. The Panel also welcomed the news that it is to be the focal point for the roll-out of the Scottish Government's Tech Scaler programme in the region.

More generally, the growing range of support for founders and businesses delivered by Opportunity North East – and the general support from across the business community in the North East - during the year is positive. This has included the delivery of several pilot accelerator programmes in partnership with CodeBase and Tech Start-up.

We also heard how the City Region Deal will be investing in a 5G network in the Port of Aberdeen and a 5G private network in Huntly in the Scottish Agricultural Organisation Society. The City Region Deal is also looking at options to address areas of the region with no fibre connectivity.

Creative Industries

The Panel has written before about how the Creative Industries in Aberdeen had been showing welcome evidence of growth, driven in particular by ongoing expansion in the digital sector, in the run up to the pandemic. The sector, arguably more than any other key sector in the region, was severely impacted by the pandemic and lockdowns. That being said, stakeholders told the Panel how the outlook had – until recently – been picking up. Theatre and concert venues were reporting healthy ticket pre-sales. The Spectra Festival of Light, which returned to Aberdeen earlier this year attracted record numbers. Visitors to the Art Gallery and Maritime Museum show a return to pre-pandemic levels for both venues over the summer.

The positive outlook has been tempered by the fall in consumer demand and rising energy costs. The Panel observes that across the UK, as evidenced by high-profile announcements of creative industry firms, festivals and theatres requiring recent financial support, conditions in the sector remain hugely challenging.





Image © Felix Mooneeram

Energy

The Panel discussed the outlook for the important energy sector with key stakeholders. The spike in energy prices has led to increased demand and activity within the sector. Government's renewed focus in achieving greater domestic energy supply has seen a marked upturn in activity with the likely approval of further licenses for exploration and production, with 79% of companies expecting revenue to rise in 2023. The Panel heard from a range of sources that firms remain optimistic about recruitment over the medium term, with 65% expecting to increase staff headcount over the next three years¹¹.

Traditional barriers remain, however. Skills shortages continue to be a significant challenge in the sector. This is across all skills areas, but particularly in high-skilled engineering jobs. Interestingly, there is little evidence that increases in energy prices has led to a similar jump in employment. However, since April 2022, there have been significantly fewer redundancy notifications in the sector than in previous years¹².

Stakeholders told us of a range of issues the sector has been facing, including inflationary pressures and the availability of capital financing. Predictability in policymaking was highlighted as a barrier to confidence and investment in the sector, both in terms of the fiscal regime and in support for a managed transition to renewables.

¹¹ AGCC Energy Transition Survey: 36th Edition: November 2022 (data from September 2022)

¹² PACE Notification Data: August 2022 – North East Performs



3 Broader Developments in the North East Economy

In previous Panel reports from 2018 to 2021, alongside the recommendations to focus on areas of key strengths, it was stressed that it was important to develop the core fundamental enabling factors that make a region economically successful. Many of these, including, skills, a commitment to innovation, connectivity to key markets and a culture of collaboration between public and private sectors have defined the North East economy for decades. These strengths have, in many ways, set it apart from other regions in the UK.

The Panel's recommendations were designed to look beyond near-term developments given the nature of the region's structural challenges and opportunities.

Within the context of EU-Exit, the pandemic, and the cost-of-living crisis, many of the opportunities and challenges identified in previous reports have become even more important to address. We stress the urgency for ambitious reform at a pace that reflects the scale of change needed in the regional economy.

We examine these challenges in more detail here.

A new Regional Economic Strategy

Last year, the Panel recommended the renewal of the Regional Economic Strategy for the North East. It should seek to build on the progress made in recent years in key areas of diversification, skills and the transition to net zero. It should also be developed in partnership with key stakeholders and the broader business community. It must put Aberdeen, the place, at its heart and focus on the region's approach to sustainable, inclusive economic development and improved wellbeing.

The Panel has been informed that a new Regional Economic Strategy is being written and is scheduled to be published in the Spring. Whilst welcome, this is slightly later than the Panel had anticipated.

The Council is developing a Wellbeing dashboard within North East Performs, as recommended in the 2021 Panel report. This will support the North East's approach to the Wellbeing economy. The dashboard is well-timed given the Scottish Government's focus on Wellbeing, which has created a national Wellbeing Economy Monitor to complement existing traditional economic metrics¹³. We would encourage both the inclusion of wellbeing and inclusivity metrics in the performance monitoring of the Regional Economic Strategy. For future projects the Council should ensure that these metrics are included in the monitoring and evaluation.

The Panel was told of the approach outlined in the City Region Deal's Benefit Realisation Plan, which sets out a framework for measuring and capturing progress to deliver against economic, social, and environmental objectives. This framework will provide a blueprint for measuring progress against regional strategies.

2. The Panel welcomes the development of the Regional Economic Strategy report and recommends:

- **There is strong buy-in from all stakeholders across the community**
- **A focus upon the long-term challenges and opportunities facing the region, with built in flexibility and adaptability to change**
- **It should be one plan, not time bounded and designed so that it refreshes going forward**
- **It is accompanied by detailed implementation and resource plans**
- **There are key measurable outcomes, and a process for monitoring and evaluating progress - drawing upon North East Performs – across all the key aspects of place making (economic, social and environmental)**

¹³ Wellbeing Economy Toolkit, Scottish Government, November 2022

Skills and labour supply

As outlined in previous reports, the skills base of the region is arguably the most important enabler of economic prosperity over the long run.

Aberdeen, and the wider North East, starts from a strong base. It has a highly educated and skilled workforce. However, the Panel heard of growing skills shortages across the region. Concerns over the impact of the UK's exit from the EU and the region's ageing workforce are increasing. These are particularly of concern in the social care, hospitality and food, drink and agriculture sectors. 61% of energy companies in the region say access to skills will be one of the defining issues in the year ahead¹⁴.

The changing demographics of the region will pose an increasing challenge to the underlying health of the North East economy. In recent decades, the region has been a net importer of people from both the rest of the UK and from overseas. But growth in the working age population in the region is estimated to have turned negative in recent times.

Working aged population - North East Scotland and Scotland: 2004-2021

Source: ONS Sub-National Mid-Year Population Estimates



¹⁴ AGCC Energy Transition Survey 36, November 2022

This combination of a shrinking working age population and skills shortages is arguably the greatest challenge facing the region at the current time.

Given the Panel's interest in the skills and demographic outlook for the region, it spent considerable time discussing the current situation with key stakeholders. It also was updated on progress across several skills related activities in the region. The Panel notes:

- The work by the Council – in partnership with stakeholders including Skills Development Scotland – to develop a renewed regional skills strategy to support the new Regional Economic Strategy.
- The Scottish Government's independent review of the skills delivery landscape.
- The delivery of a £14.3 million, Scottish Government North-East Economic Recovery and Skills Fund, that will help inform projects being brought forward under the £500 million Just Transition Fund.
- The publication of a report - 'Making the Switch' – by Robert Gordon University which provided a welcome assessment of the future skills needs of the offshore energy industry.
- The work by regional partners to enhance digital skills at all levels and across all age groups.

3. The recent initiatives to support the regional labour market are welcome but the skills challenges facing the local economy have been compounded further by the rise in inflation and labour market shortages that have proliferated across the UK economy. The Panel reiterates its recommendation from last year of the value in developing and publishing an updated skills strategy which builds on the approach at the national level, supports the direction of the new Regional Economic Strategy and the strategic direction set out in the Route Map to Aberdeen the Place. It should be SMART and supported with a clear delivery plan.



Resilience

As discussed in previous reports, Aberdeen and the North East has a reputation for being one of the most prosperous and dynamic parts of the UK.

Entrepreneurship

The Panel notes that, despite recent challenges, the region continues to perform strongly compared to other regions in the country on indicators of entrepreneurship. Aberdeen City ranks the best in Scotland for patent applications per capita¹⁵ and has a strong record in research and development^{16 17}.

On certain indicators however, recent trends have been less positive. Business start-ups per 10,000 working adults in the North East have historically outpaced the Scottish average. But since 2020, average start-ups have fallen to 6 start-ups per 10,000 in the North East, compared to 6.7 in Scotland as a whole¹⁸.

¹⁵ Centre for Cities: Patent Application Rate 2015- 2020

¹⁶ Business Expenditure on Research and Development 2020

¹⁷ Higher Education Statistics Agency, 2019/20

¹⁸ BankSearch (up to September 2022)

A continued focus on connectivity

Physical and digital connectivity of a region to key national and international centres of business activity is crucial. The Panel recognises that Aberdeen's location, and its current transport infrastructure compared to key competitors, makes connectivity an ongoing challenge for the region. Previous reports have documented, and welcomed, recent investments in the region including the Aberdeen Western Periphery Route and ongoing projects around enhanced connectivity links to the South Harbour, improved rail services between Aberdeen and the Central Belt and the dualling of the A96 between Aberdeen and Inverness.

However, our stakeholder consultations revealed renewed concerns over the connectivity of the region. This appears in several forms. For example, there remain limited direct links to major European hubs and rail and road access to central Scotland have only seen limited improvement in recent years.

The Aberdeen Harbour Expansion Project commenced operations on 60% of the new facility in October 2022 following delays associated with the pandemic. The completion of the remainder of the facilities including the Balmoral western quay is expected by May 2023. The long-term benefits of the expansion are expected to flow from new investment and business to support decommissioning and cruise ships handling which is expected to begin in 2023. Other opportunities including offshore renewables development from the current ScotWind licensing rounds should commence in 2024 and beyond. The new harbour will also be integral to the region's ambitions in hydrogen, supporting the infrastructure for hydrogen generation offshore, pipelines onshore, storage and connectivity to export pipelines.



Business pressures

The Panel heard that firms have shown resilience in coping with the COVID-19 crisis, supported by national and local support schemes. However, stakeholders told us that since these schemes have closed the wider economic uncertainty and squeeze on cashflows has impacted business confidence in the North East, particularly amongst small businesses. Rising costs from increased input prices are inevitably being passed on to customers with three quarters of the region's businesses responding in August and September 2022 they planning to increase prices in the next three months¹⁹.

The Panel heard from stakeholders that business rates could remain a challenge for some businesses in the region. More recently, new announcements have provided mixed news. The draft rateable values published in November 2022 show there is variability with some rateable values rising and others falling in Aberdeen. Overall, the draft rateable values on Union Street will fall by an average of over 29% from April 2023. The average fall for retail and hospitality sectors in Union Street is over 39%. The December 2023 Scottish Budget shows the poundage remains unchanged which means that for many businesses in these sectors, their rates bills should show a fall from April 2023. Against this, for some businesses the newly adjusted Small Business Bonus may be less beneficial.

The Panel has already highlighted in this report the additional need to look at opportunities for time limited sector support given the many challenges businesses face from the current economic climate. The Panel feel this would be the best way to target any additional support and should be the first option considered.

¹⁹ Aberdeen and Grampian Chamber of Commerce Monthly Bulletin, November 2022

Net Zero

Energy companies highlighted to the Panel that uncertainty (both economic and policy) could be a barrier to energy transition and in achieving the UK and Scottish targets of achieving net zero by their target dates. Survey data shows that half of companies reported in September 2022 that the current political and regulatory environment was now a barrier to diversification, up from 24% a year ago²⁰.

More positively, the report also finds that UK energy companies believe 47% of their work will be out with oil and gas by 2030 and that 70% of firms are actively diversifying from oil and gas at present. A quarter of companies (25%) will be net zero by 2030, but 34% have yet to commit to a strategy at all.

The Panel was told of a range of activity to support the energy transition. This includes ETZ Ltd, which leads the region's energy transition ambition to grow a new energy cluster with a focus on offshore wind around the South Harbour expansion. We also heard of Aberdeen City Council's partnership with BP²¹ to create Scotland's first scalable facility capable of producing green hydrogen. A key challenge remains around the considerable skills requirements to meet energy transition and the further investment needed to deliver them.

There have been positive developments in meeting the Panel's previous recommendation from 2020 to ensure that the transition to net zero continues at pace. As well as addressing the transition within the energy sector it also requires the prioritisation of the transition of the wider city economy to low carbon sectors and activities and the transformation of the city itself to net zero through greener travel, enhanced energy efficiency, and provision of accessible and connected green space. These are critical ingredient for placemaking in Aberdeen.

The Panel heard that a Net Zero Leadership Board and Delivery Unit formed of representatives of organisations based or working in Aberdeen have co-created a Net Zero Aberdeen Routemap²², setting the pathway towards a net zero city by 2045. Six enabling net zero strategies accompany the Routemap and cover Buildings and Heat, Energy Supply, Mobility, Circular Economy, Natural Environment and Empowerment. The Aberdeen City Council's, Net Zero, Environment and Transport Committee will monitor the delivery of all services and functions relating to net zero, the environment and transport²³.

There has also been the launch of an Aberdeen Climate and Nature Pledge in 2022, seeking wider participation and commitment to net zero ambitions for the city, as well as to the climate resilience goals under Aberdeen Adapts.

It is recognised a just transition will require a blend of skills, resources, innovation, technology, supply chain diversification, capacity building and a significant level of action. The Panel were informed of the introduction of a range of hydrogen, electric and hybrid vehicles in the Council fleet; expansion of district heating, putting in place the connections to capture heat from the developing energy from waste plant; as well as the use of technology to target effective interventions for buildings.

4. To achieve sustainable and long-term energy security, policymakers and business leaders must continue to take bold decisions to support an accelerated Just Transition toward new and green energies. The risk that recent uncertainty poses to energy transition in the region must be recognised by all stakeholders and addressed to ensure that the region's approach to net-zero is not derailed. This requires renewed collaboration between all tiers of government and industry, aligning behind agreed policy outcomes.



²⁰ AGCC Energy Transition Survey 36, November 2022

²¹ www.insider.co.uk/news/aberdeen-city-council-confirms-bp-26138593

²² www.aberdeencity.gov.uk/net-zero-aberdeen

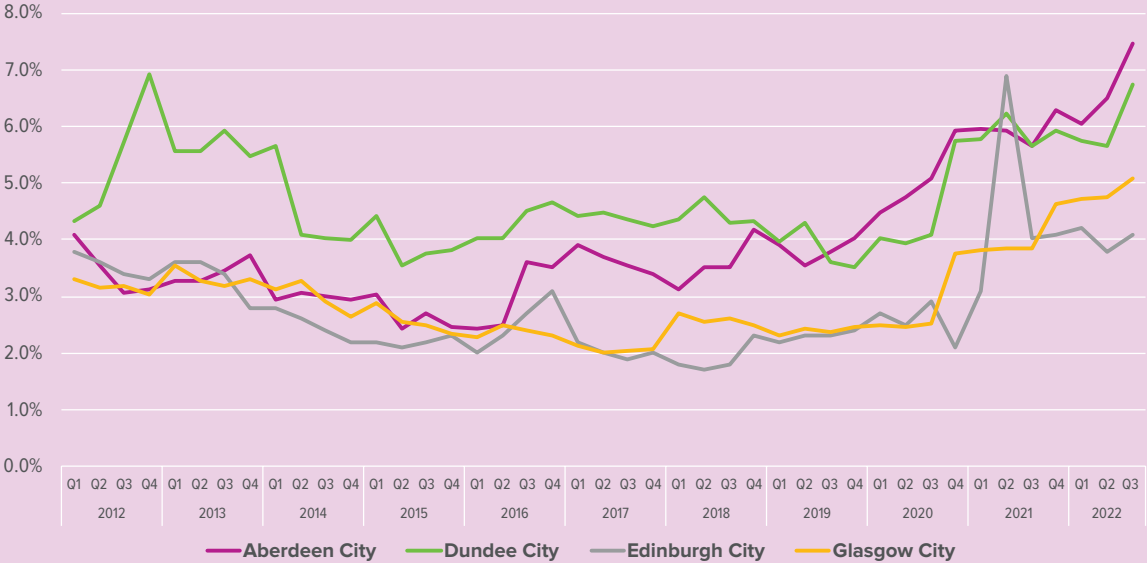
²³ <https://committees.aberdeencity.gov.uk/mgCommitteeDetails.aspx?ID=685>

Aberdeen the place

As previously mentioned, Aberdeen has been hit particularly badly by the pandemic and recent rise in inflation. This has impacted upon the wider economy with a number of indicators pointing to an exacerbation of the decline in the city centre. Aberdeen is no different from almost all UK cities in facing such challenges. However, retail vacancy rates, shown below, in Aberdeen City are the highest out of Scotland’s four biggest cities and show a larger increase than any of the other three largest cities in Scotland²⁴.

Retail market vacancy rates: Aberdeen City, Dundee City, Edinburgh City and Glasgow City - 2012 - 2022

Source: CoStar



Aberdeen faces an even more acute commercial office market, having the highest commercial office vacancy rates of the four cities since Q4 of 2018, reaching 14.1% in Q3 of 2022, rising 3.6% since Q1 of 2020²⁵.

These recent trends put even greater emphasis on the 2022 City Centre and Beach Masterplan. This has been informed by the Scottish Government’s City Centre Recovery Task Force Report which, co-produced, with the Scottish Cities Alliance, set out the impact of Covid-19 on city centres. The report recognises that the immediate priorities to support city centre recovery must include the harms caused by the pandemic, empower communities and places, and support inclusive and sustainable economic development. For Aberdeen, this is likely to mean maximising the economic, social and environmental benefits of the city centre and supporting the creation of employment. A key part of this is supporting connections through clean and efficient active travel and transport routes.

We heard that Aberdeen City Council is currently consulting on potential designs for the city centre as part of the Aberdeen City Centre and Beach Masterplan. The Panel was also told that a Council report on how to deal with the growing number of empty shops on Union Street was presented in December 2022.

However, feedback from some of our stakeholder consultations suggests a degree of frustration over the speed of progress on the Aberdeen City Centre and Beach Masterplan which is seen as critical to regenerating the city.

5. The Panel welcomes the approach being taken in the Aberdeen City Centre and Beach Masterplan and other initiatives but as set out last year, encourages a greater pace of change and holistic approach to developing ‘Aberdeen the Place’.

The Route Map the Panel advocated in both the 2020 and 2021 reports should aim to be progressed more quickly and build on the approach in the new Regional Economic Strategy. It must also be supported by and reflected in other key strategies and have buy in from across the community.

It will help set the overall strategic approach for the region in the long-term and help coordinate action. There is both a clear economic imperative and a clear demand to move more quickly on redeveloping the city, taking critical decisions and setting out the plan for change.

²⁴ CoStar: October 2022

²⁵ CoStar

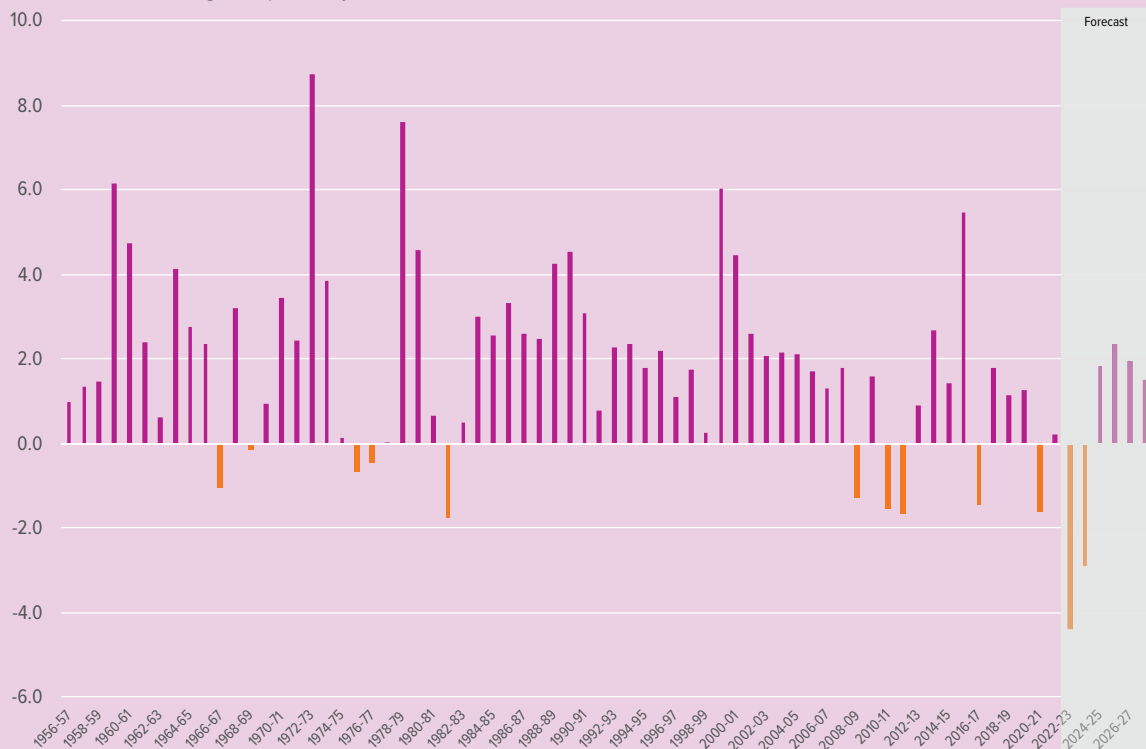
Inclusivity

Cost-of-living crisis

With high energy and food costs driving inflation it is expected that living standards will fall this year and next across the UK. Real household disposable income (RHD) per person in the UK is forecast to fall 4.3% in 2022-23, which would be the largest fall since records began in 1956-57, followed by a 2.8% fall in 2023-24. Therefore, living standards in the UK are forecast to see a cumulative 7.1% fall from 2021-22 to 2023-24, taking RHD per person to its lowest level since 2013-14²⁶ and an unprecedented rate of decline.

Real household disposable income per person, fiscal year growth rates - UK: 1956-57 - 2027-28

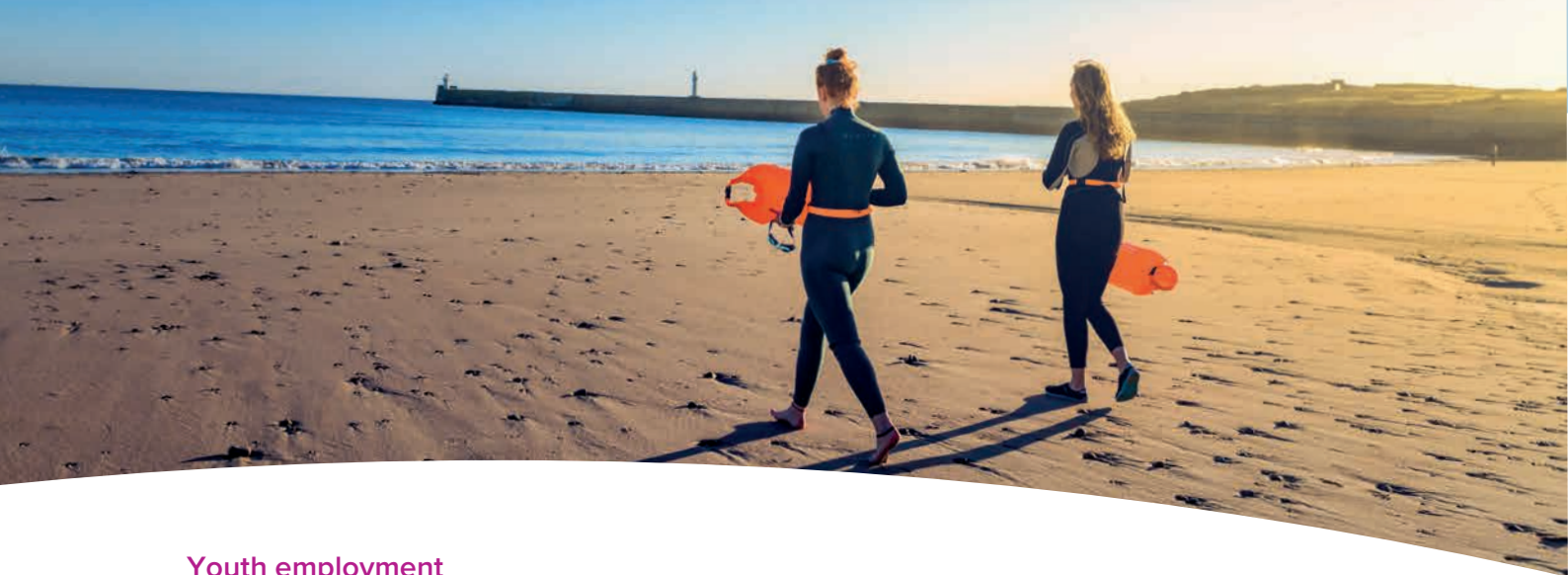
Source: Office for Budget Responsibility



The cost-of-living crisis is also expected to impact disproportionately on those on lower incomes who spend a higher proportion of their income on these items and this was reflected in what we heard from our stakeholder engagement.



²⁶ Office for Budget Responsibility - November 2022

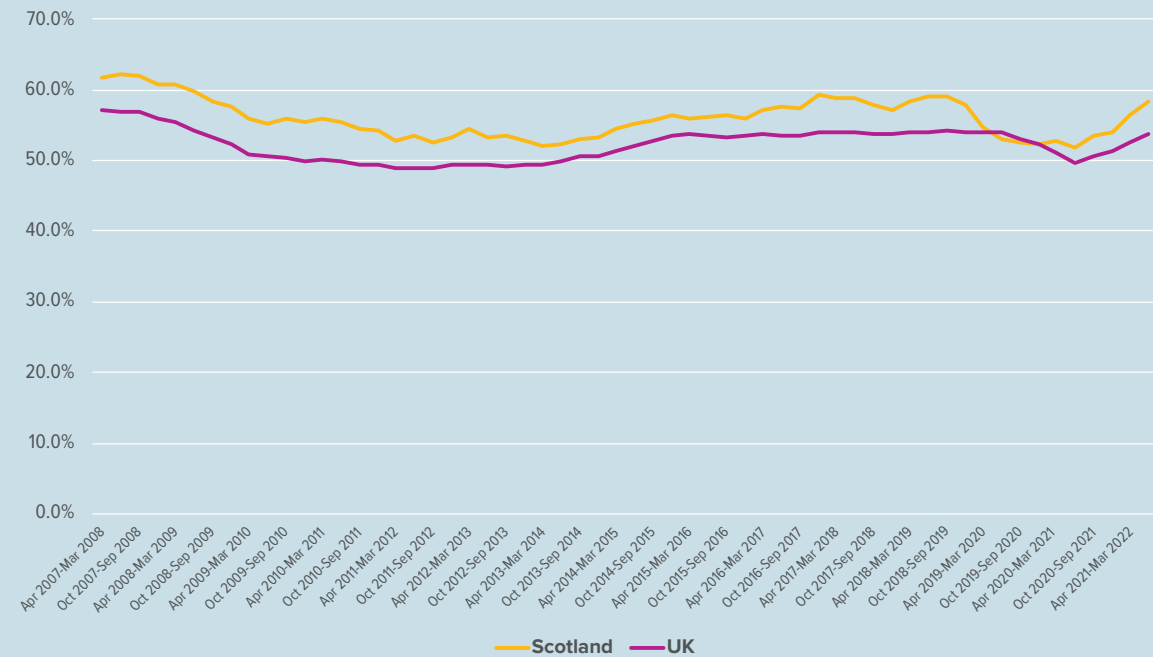


Youth employment

Across the country, one group that has experienced significant disadvantage since the pandemic is young people. In Scotland, the youth employment rate (age 16-24) fell by nearly 10 percentage points to just over 50% during the pandemic although it has subsequently recovered. Aberdeen’s youth employment was among the highest rates of all local authorities in Scotland pre-pandemic and has fallen to among the lowest by mid-2022²⁷.

Youth (16-24) Employment Rate: Scotland and UK - 2007 - 2022

Source: ONS



Younger workers are over-represented in industries most affected by the lockdown restrictions within the services sector, such as retail, food and accommodation, and hotels.

The Panel notes the formation of Aberdeen City Council’s Anti-Poverty and Inequality Committee which will monitor and determine the Council’s contribution to alleviating and mitigating all forms of poverty and inequality in the city²⁸. Given the unprecedented nature of the expected falls in the standard of living and the inequitable distribution of the impacts across the population, the Panel welcomes this. The Committee will need to consider action taken by UK and Scottish governments and highlight the challenges locally for key groups and the longer-term costs that can be associated with such trends.

²⁷ Annual Population Survey Data

²⁸ <https://committees.aberdeency.gov.uk/mgCommitteeDetails.aspx?ID=683>

4 Long Run Financial Position

Council officers told us how the Council has introduced its Financial Resilience Framework and considered as part of the Medium Term Financial Strategy (MTFS) the future for Scottish Government funding going forward. This is now supported in the medium term by the Scottish Government's Resource Spending Review (RSR) published in May 2022. The Council expects, as a result of the National Care Service (Scotland) Bill, that the value of funding will be altered in the medium term by the transfer of funding and associated costs/liabilities from local government. This will change the shape of the Council in the long-term future and its resources and this has been analysed and modelled as part of the MTFS, 2022.

The Council (in line with all other UK councils) is projecting a funding gap for future years. The Council does not control all of its income and real terms funding reductions forecast mean that the cost base of the Council also has to reduce. The impact of the pandemic continues but of greater effect is energy, pay and price inflation, the cost-of-living crisis and providing support to the increasing number of people seeking resettlement here from Ukraine.

The Event Complex Aberdeen (TECA) is a multi-hundred million pound project that aims to attract millions of visitors a year. The ambition of TECA by year ten of operating is to contribute an additional 4.5 million visitors, £113 million of visitor spend, 352 full-time-equivalent permanent positions and £63m net GVA to the Scottish economy. Activity was interrupted by the pandemic but 120 large events are expected to have taken place in 2022 including concerts, conferences and hospitality events which have picked up significantly since Spring 2022. This is expected to continue into 2023 with more live concerts, conferences, and events, including SPE Offshore Europe 2023 in September. However, the results for the individual elements of TECA have been impacting cashflow and the Council has had to adjust its financial planning assumptions. For instance, the cost of energy and heat production has substantially increased and hotel REVPAR from the site is around half that anticipated in the original business plan.

6. The performance of TECA has understandably been influenced by the pandemic and cost of living shock, and will be one of the factors contributing to the funding gap. Post-pandemic, ACC should deliver an assessment of how it – and other recent key investments - are performing against its objectives and how it can inform future plans for investment in infrastructure.





The Panel have been informed that the Council’s cost base will increase to meet future obligations (debt repayments, pay and price inflation, contractual uplifts, demand and demographic pressures etc.) and a savings programme has been developed by transformation and service redesign leading to savings options to address the projected deficit.

The table below shows the impact of income and expenditure assumptions and scenarios which the Council propose to offset through its Savings Programme.

General Fund Budget Gap	Budget 2022/23	Forecast 2023/24	Forecast 2024/25	Forecast 2025/26	Forecast 2026/27	Forecast 2027/28
	£m	£m	£m	£m	£m	£m
Upside Scenario	0	34	38	40	43	47
Central Scenario	0	53	87	114	126	134
Downside Scenario	0	106	132	157	184	211

Source: Aberdeen City Council

The Council will monitor future UK Government funding announcements and any consequential impact these bring to Scottish Government funding levels.

The Panel heard that £150m of Capital Investment from the Council is being planned to fund the City Centre and Beach Masterplan but additional funds will be required from partners and other external funding sources (levelling up funds, etc) over the next 5 years to address future phases. The region will thus need more finance and powers to fund this.

7. The Council should continue to update its Medium Term Financial Strategy work, particularly in the light of changing funding outlooks. This should include examining spending commitments and revenue options.

5 Broader Policy Agenda

Finally, the Panel has noted that there have been several important developments in the broader policy agenda that will impact upon the region. Many of these 'national' initiatives place considerable emphasis upon local solutions and 'place'. This provides an opportunity for regional policymakers to shape and influence government decision making.

This includes:

Green Freeports

The UK Government has announced the creation of a series of Green Freeports across the UK. Green Freeports are designed to boost innovation and inclusive growth within communities. Up to two Green Freeport designations will be awarded in Scotland.

The region submitted a bid in June 2022, which highlighted opportunities for the region for private sector investment and growing the economy around key industries.

Securing a North East Scotland Green Freeport has the potential to help support the region's ambitions in the transition to net-zero and boosting international trade opportunities.

Scotland's National Strategy for Economic Transformation

In early 2023, the Scottish Government published a National Strategy for Economic Transformation (NSET). This new economic strategy aims to transform Scotland's economic model in the next decade in the areas of economic growth, environmental sustainability, quality of life and equality of opportunity and reward.

As the Scottish Government rolls out its plans for NSET, this is likely to create new opportunities (and choices in prioritisation) for regional policymakers.

Implications of UK and Scottish budgets

Both the UK and Scottish Governments have recently published detailed budget plans for next year. Whilst the focus has, understandably, been upon the cost-of-living crisis there have been a number of developments for economic policy.

These include the potential for Investment Zones to be established in different parts of the country and continued investment in 'levelling-up'. There is also increased funding for the Just Transition Fund in the North East and Moray as well as an additional £244 million for the Scottish National Investment Bank so that it can continue to invest in Scottish businesses, projects and communities across all three of the missions set for it by Scottish Ministers: Net Zero, place and innovation.

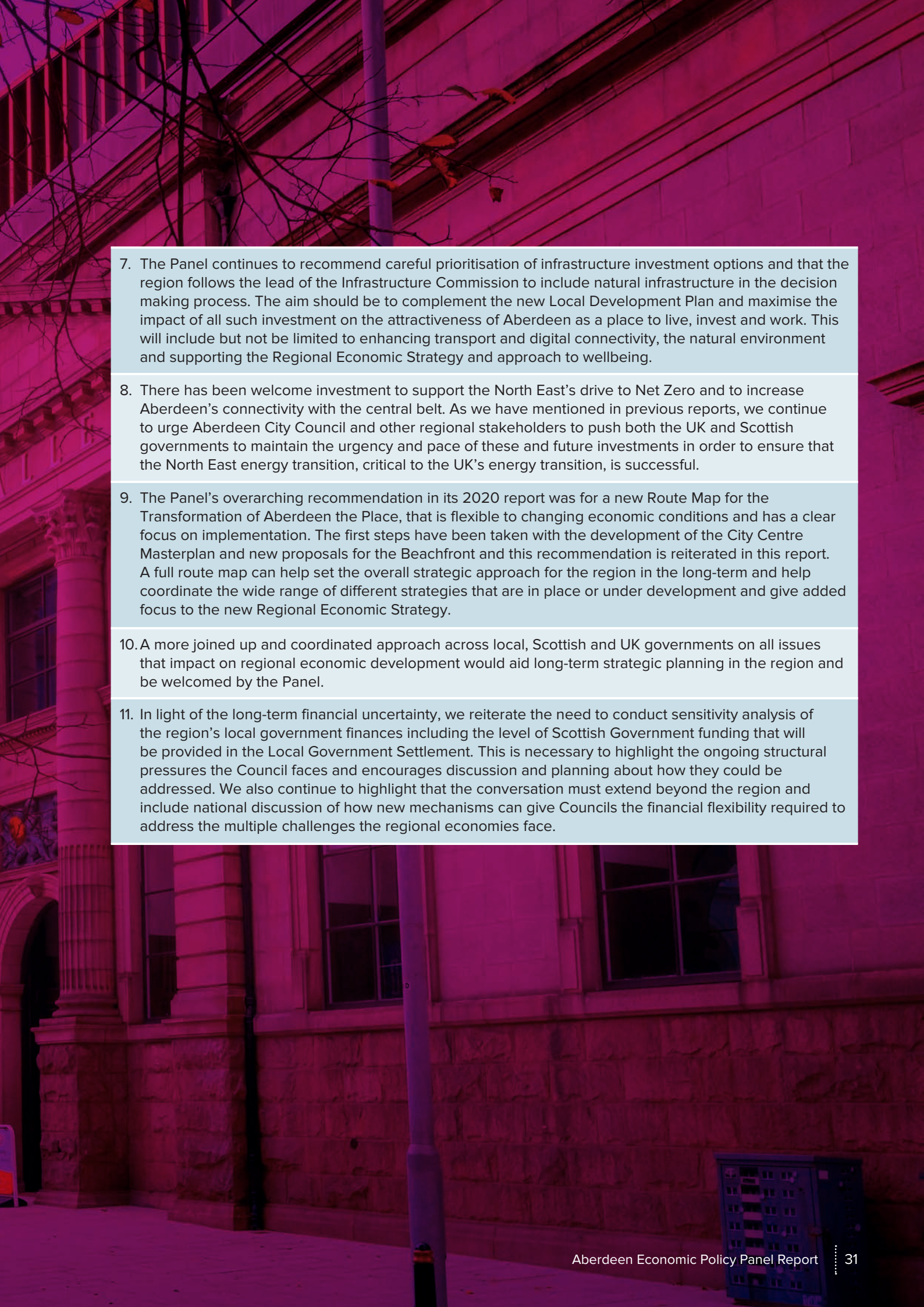
8. The Panel observes the increasing focus of national policymakers to prioritise investments in key localities subject to national priority guidelines and successful bids from local areas such as through the Just Transition Fund, UK Shared Prosperity Fund and Levelling Up Fund. It is important that Aberdeen is ready to respond to these opportunities building upon the agility of local policymakers, flexibility and partnership working. In addition, the region needs to plan for how it will resource the planned initiatives around the economic strategy and development of Aberdeen the place.



6 2021 recommendations

There has been considerable progress across a number of last year's recommendations but there are still aspects where further progress is required. This is reflected in the choice of many of this year's recommendations where continued progress is urged. For ease of reference last year's recommendations are repeated below.

1. With the Scottish Government due to publish this year the National Strategy for Economic Transformation for the next ten years the Panel are of the view that 2022 is the right time to renew the strategy for the North East. The approach must build on the progress made in recent years and continue to concentrate on long-term priorities. It must put Aberdeen the place at its heart and focus on the region's approach to sustainable, inclusive economic development and improved wellbeing. This should be underpinned by a clear implementation plan with detailed SMART objectives.
2. On diversifying the economy, the Panel concludes that since our first report the long-term challenges facing the North East economy have intensified given the prolonged downturn in the oil and gas sector, Brexit, the transition away from the dependency on oil and gas and the pandemic. This means that diversification is even more important for the long-term success of the North East economy. This requires a continued focus on the region's growth sectors but, as said last year, a need to go further and faster in attracting new businesses and people from outside these sectors reinforced by the approach to making Aberdeen the Place an attractive location to live, work and invest both now and in the future.
3. The Panel welcomes recent initiatives to support the regional labour market but would reiterate the pressing need to develop and publish an updated skills strategy following engagement with all stakeholders and that takes account of the existing skills gaps and is tailored towards future labour market demands. The strategy must support the approach in the renewed Regional Economic Strategy and the strategic direction set out in the Route Map to Aberdeen the Place. It should be SMART and supported with a clear delivery plan. The new strategy should join up the range of existing activity such as the skills pathfinder and build upon the existing collaboration across public sector, industry and educational institutions.
4. We still welcome the partnership approach that exists in the North East, with numerous bodies including the Councils and ONE making a significant contribution to the long-term resilience of the North East. It is vital the Council continues to prioritise economic development and diversification as this will be key to building resilience in the long run. The Panel's recommendations for a renewed focus on the region's approach to sustainable, inclusive economic development and improved wellbeing and a new route map for Aberdeen the Place will help embed greater resilience in the economy over the longer-term.
5. The Panel welcomes the further development planned for North East Performs and the Net-Zero Dashboard as this monitoring and evaluation is an essential part of developing resilience in the changing economy. We reiterate the need to take the lead by defining the North East's approach to Wellbeing and embedding this in the Regional Economic Strategy. The economic strategy needs to reflect the region's wellbeing values and have them amongst the objectives of the strategy.
6. The COVID-19 pandemic has exacerbated inequality and brought additional challenges to inclusion. The Panel recommends that the development of a renewed Regional Economic Strategy in 2022 provides the perfect opportunity to expand on the region's approach to fostering inclusion and further embed it in the region's economic approach.

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7. The Panel continues to recommend careful prioritisation of infrastructure investment options and that the region follows the lead of the Infrastructure Commission to include natural infrastructure in the decision making process. The aim should be to complement the new Local Development Plan and maximise the impact of all such investment on the attractiveness of Aberdeen as a place to live, invest and work. This will include but not be limited to enhancing transport and digital connectivity, the natural environment and supporting the Regional Economic Strategy and approach to wellbeing.
 8. There has been welcome investment to support the North East's drive to Net Zero and to increase Aberdeen's connectivity with the central belt. As we have mentioned in previous reports, we continue to urge Aberdeen City Council and other regional stakeholders to push both the UK and Scottish governments to maintain the urgency and pace of these and future investments in order to ensure that the North East energy transition, critical to the UK's energy transition, is successful.
 9. The Panel's overarching recommendation in its 2020 report was for a new Route Map for the Transformation of Aberdeen the Place, that is flexible to changing economic conditions and has a clear focus on implementation. The first steps have been taken with the development of the City Centre Masterplan and new proposals for the Beachfront and this recommendation is reiterated in this report. A full route map can help set the overall strategic approach for the region in the long-term and help coordinate the wide range of different strategies that are in place or under development and give added focus to the new Regional Economic Strategy.
 10. A more joined up and coordinated approach across local, Scottish and UK governments on all issues that impact on regional economic development would aid long-term strategic planning in the region and be welcomed by the Panel.
 11. In light of the long-term financial uncertainty, we reiterate the need to conduct sensitivity analysis of the region's local government finances including the level of Scottish Government funding that will be provided in the Local Government Settlement. This is necessary to highlight the ongoing structural pressures the Council faces and encourages discussion and planning about how they could be addressed. We also continue to highlight that the conversation must extend beyond the region and include national discussion of how new mechanisms can give Councils the financial flexibility required to address the multiple challenges the regional economies face.

