Scottish Government

Scottish Spending Review 2011 and Draft Budget 2012-13

Written Response by Scottish Chambers of Commerce

1. Scottish Chambers of Commerce (SCC) is Scotland's largest business representative organisation, representing over 10,000 businesses employing over half of the private sector workforce, with one hundred and seventy staff in the offices of its twenty one constituent member Chambers.

2. Scottish Chambers of Commerce welcomes the opportunity to respond to the Scottish Government's Scottish Spending Review 2011 and Draft Budget 2012-13. The Scottish economy is currently in a crucial phase as it battles to maintain growth following the longest and deepest recession in a generation. As the Scottish Government sets about its spending plans, we recognise the challenges they face against a backdrop of reducing public sector budgets as the UK Government pursues essential deficit reduction plans. The Eurozone and other western economies also continue to give cause for concern in terms of Scotland's capacity to avoid a return to recession. That said, the Scottish Government still has, in real terms, the same spending power that it had seven years ago and it is a fact of the devolved settlement that budgets can go down as well as up.

Overview

3. The Scottish economy continues to experience a number of challenges stemming from the recent recession, including difficulties in access to finance, falling levels of public spending and investment, a sluggish housing market, low consumer and business confidence and rising costs.

4. Strathclyde University's Fraser of Allander Institute have forecast Scottish economic growth at 0.4% in 2011, 0.9% in 2012 and 1.6% in 2013.[1] Scottish Chambers of Commerce's own Quarterly Business Survey, itself produced in partnership with the Fraser of Allander Institute, has recently revealed a sharp drop in business confidence looking forward and contunies to highlight the difficulties of rising costs in a market where it is difficut to pass these on to

[1] Fraser of Allander Economic Commentary, November 2011

customers.[2] This is putting pressure on margins and making investment more difficult. SCC expects Scottish economic growth to continue to be marginal for some time to come and trading conditions will be difficult for many businesses.

5. On a more positive note, our manufacturing exports have been strong throughout much of the recession and post-recessionary period, reflecting the weakness of Sterling and the strength of our lean manufacturing sector. The continuation of this strength is of course reliant on the health of our exporting markets and economic growth overseas, which is largely outwith our control. It is also important to note that Scotland's tourist industry continues to benefit from the rise in domestic tourism.

The 2012-13 Budget and Spending Review

Capital Spending

6. The Scottish Government and the Scottish Executive before it have become accustomed to year on year real terms increases in their budgets. This is unlikely to have been sustainable indefinitely and as the UK Government moves to restrict public spending in order to tackle the deficit, Scotland is bearing its share of public spending cuts. From a business perspective, the most worrying aspect of this was the reduction in capital budgets by 36% over four years, since it is capital investment that delivers the best long term boost to our economy. We welcome the fact that the Scottish Government have sought to mitigate the fall in capital spending by diverting revenue spend towards capital. We also welcome the fact that the importance of capital spend has been recognised by the Scottish Government in creating a cabinet post for Infrastructure and Capital Investment. The key now is to ensure that capital spend is targeted effectively. SCC's priority is for investment in transport projects, as we believe these would deliver the maximum long term economic benefit for Scotland.

7. Scotland's private sector businesses will drive economic growth in our country and government's role must be to facilitate and support that growth. Infrastructure investment is a key tool for government in achieving this end. There is ample evidence to suggest that investment in infrastructure is a vital contributor to productivity, growth and economic competitiveness and, in particular, the OECD has stated that investment in transport, telecoms, water and electricity infrastructure has a greater impact on output than most other types of capital investment.[3] The Eddington Report in 2006 highlighted the high economic returns generated by tackling congestion and bottlenecks and by focusing on international connectivity.[4]

8. Against this background, SCC believes that the achievement of the Scottish Government's Central Purpose, that is "To focus government and public services on creating a more successful country, with opportunities for all of Scotland to

[2] Scottish Chambers of Commerce Quarterly Business Survey Q3 2011, October 2011
[3] Infrastructure to 2030: Telecom, Land Transport, Water and Electricity, OECD (2006)
[4] The Eddington Transport Study, HMSO (2006)

flourish, through increasing sustainable economic growth", can only be achieved effectively if infrastructure investment is at the very heart of government policy.

9. It is easy for businesses to come up with a shopping list of transport projects that would make a positive impact in terms of Scotland's economy. However with budgets becoming tighter, the real challenge is to prioritise projects in order to deliver the maximum economic benefit. We believe that transport projects deliver a high return on investment in terms of economic benefit and that the Government must recognise this fact. The budget for network strengthening and improvement is set to rise over the next three years but the budget for road improvements is set to fall, with structural repairs remaining steady. By far the largest portion of the motorways and trunk roads budget is of course the Forth Replacement Crossing. We believe that, though expensive, this project is absolutely vital for the Scottish economy and that, whilst annual costs rise towards £359m by 2014-15, the costs of allowing the current Forth Road Bridge to close to traffic could exceed £1 billion per year and therefore this continues to represent good value to the people of Scotland. There are many other road projects our members would like to see implemented and these need to be pipelined in a sensible and strategic manner, with detailed plans for projects over the next five years, indicative plans for projects 5-10 years off and aspirational plans for projects beyond that point up to a horizon of 20-25 years. This would allow greater predictability, allow the construction sector the opportunity to plan ahead and ensure that we have the skills base available to deliver on our plans.

10. In terms of rail, the Edinburgh-Glasgow Improvements Programme will be delivered using Network Rail's Regulatory Asset Base (RAB). This is a welcome initiative and will assist in delivering a faster and more comprehensive rail service network in Central Scotland. We cannot however allow rail services in the rest of Scotland to deteriorate and improvements are needed in both frequency and journey time between Inverness, Aberdeen and the Central Belt if we are to encourage greater use of public transport and improve connectivity between Scotland's cities. Further network enhancement is also needed other areas, such as Fife and Kilmarnock, if regional transport is to be adequately addressed. We would encourage further use of the RAB to enable further network enhancement where appropriate. It will also be important to utilise the forthcoming ScotRail franchise tendering to leverage higher levels of investment in our rail network.

11. In terms of infrastructure funding more generally, we believe that the Scottish Futures Trust has developed into a high quality organisation that is already making a big difference in terms of both value for money and the way in which government looks at infrastructure spending in Scotland. It is a crucial tool in ensuring effective infrastructure spend in Scotland.

12. SCC believes that there is a real need for affordable housing in communities across Scotland and that Government at a local and national has a key role in facilitating this investment. We welcome the Government's commitment to deliver 30,000 affordable homes between now and 2016 as this could make a real difference to families and to the construction sector.

13. Scotland lags behind the rest of the UK and major competitor nations in the availability of both superfast fixed line broadband and in the provision of 3G cellular telecommunications. It is essential that Scotland prioritises investment to bring our digital communications up to and beyond the standards of our competitors if we are to maximise our economic potential. We cannot afford to be left behind and this could deliver a particularly strong boost to our remote and rural areas and to our tourist sector. SCC has been lobbying the UK Government to try to secure additional funds for the roll out of superfast broadband in Scotland.

Revenue Spending

14. In terms of revenue budgets, the Scottish Government must also look to its Central Purpose. At a time of reducing budgets, priorities will necessarily compete and it is important to scrutinise and weigh the economic impact of spending commitments. Against this background, it is difficult to see the value in offering, for example, free public transport to employed persons over 60 years old or offering free prescriptions to those who can afford to pay. Such measures are a frequent cause for concern among Chamber members.

15. The Further Education budget has, again, been reduced significantly. We are in agreement with the Scottish Government that this sector has the potential to deliver more efficiently. We would, however, want to see that the proposed reforms to the way the sector is managed, including the move to regionalisation of provision management, do not reduce provision or undermine colleges' role in communities or as providers of a suitably skilled workforce for Scotland's businesses. More detail on this point will be provided in our submission to the Scottish Government's consultation on its pre-legislative paper, "Putting Learners at the Centre". We are more than happy to supply this further detail if that would aid consideration of this budget proposal.

16. Scotland's Enterprise Agencies have a strong track record in supporting growth and we welcome the fact that this continues to be recognised by the Scottish Government. Both Scottish Enterprise and Highlands and Islands Enterprise are working to deliver for high growth businesses in key sectors and also for the wider business community. SCC's partnership with SE and HIE in delivering the Business Mentoring Scotland programme throughout the country is a good example of how a relatively small amount of investment can deliver for Scottish business. This progamme alone has now assisted over 6,000 businesses in Scotland. We are comfortable with the focus on growth businesses for the Enterprise Agencies' prime focus but as localised connectivity becomes less of a priority, new ways must be found to engage with the rest if the business community.

17. We also welcome the Scottish Budget's focus on Renewable Energy projects, since Scotland has much to gain in the longer term through the exploitation of our extensive natural resources for the harvesting of energy. The priority at present should be to ensure that Scotland is geared up to service the growing offshore wind industry, ensuring that our ports and surrounding infrastructure are up to the task of serving an industry that has the capacity to deliver significant economic

benefits to Scotland. In doing so, we must win over competing post developments in eastern England and in continental Europe. Despite the focus on the potential of renewable energy developements, we must also continue to recognise that Scotland has long standing expertise and supply chains in other energy technologies, and these must continue to be developed.

18. Scotland's tourist industry is extremely important to our economy. Our hospitality industry directly employs over 220,000 people and, indirectly, a further 120,000 – in total, some 8.6% of Scotland's jobs. It accounts for £7.9 billion in turnover and £4 billion to the Scottish economy in wages and profits. In addition, it has the capacity to create 46,000 more jobs over the next decade if given the right support[5]. VisitScotland has a key role to play in this and must build upon the excellent work that has been done in terms of marketing Scotland across the globe. At home this must be supported by Government working with the industry to boost broadband and 3G coverage and to develop Scotland's potential as a modern and connected tourist economy designed to serve 21st century tourist needs.

Business Rates

19. There are three elements of the Scottish Government's proposals that will affect the amont of business rates that our members will be paying over the next three years.

20. The first is the annual inflationary increase. The UK Government normally increase the business rates poundage in England based on September's RPI figures and the Scottish Government have committed to at least matching the English poundage rate. This September's RPI was 5.6% - it's highest rate in over 20 years and, according to the Governor of the Bank of England, most likely at its peak. At a time when our businesses are having to contend with other rising costs, we believe that such an ill timed increase in the rates poundage is unwarranted. Unfortunately the UK Government has passed on the whole of this increase and the Scottish Government have decided to follow suit. Given that this 5.6% rate of RPI inflation was higher than anticipated, this will undoubtedly affect the expected revenues from business rates and this may afford room for future amendment to the budget in terms of non-domestic rates.

21. The second worrying aspect of business rates costs is the plan to limit Empty Property Relief. Generally, empty premises currently receive a 100% relief on rates for the first 3 months and then 50% thereafter. Government plans are to limit the later relief to just 10% for many businesses, raising £16 million per year from 2013-14. Our members have expressed their concern that this is the wrong move at the wrong time. In the current economic climate, limiting Empty Property Relief will do little to ensure that properties are tenanted and will act as a disincentive to speculative development. The experience in England, where this relief was limited some time ago, has been that it has had little or no effect on the letting of properties and indeed that some properties have been demolished in order to avoid the tax.

[5] Hospitality: driving Scotland's local economies. British Hospitality Association, October 2011

22. The third change is the introduction of a Public Health Levy – a rates supplement to be applied to large retailers selling both alcohol and tobacco. We do not yet have enough information from the Scottish Government about the operation of this levy to comment fully upon it, however a number of initial concerns have been raised by our members. The application of the levy seems arbitrary and, if it is a Public Health Levy, why is it so narrow? Other members are concerned that the supermarkets may pull back from local projects such as Business Improvement Districts if they are targeted in this way. We are concerned at the lack of consultation that has taken place before the proposal to introduce this scheme, the lack of detail that has been revealed so far on its application and the lack of commitment to the introduction of a Business Regulatory Impact Assessment to examine the implications of the levy.

23. In the longer term, we welcome the Scottish Government's commitment to a review of Business Rates more generally and we look forward to working with the Government on this.

24. As a proportion of the Scottish Government's total budget, the amount raised from Business Rates will rise from 7.8% this year to 9.3% in 2014-15. By 2014-15, the Scottish Government are predicting that they will be receiving £482 million more in business rates than they receive today (an increase from £2,182m to £2,664m)[6]. However only £335 million of this can be accounted for by inflation and the revenues generated by the reduction in Empty Property Relief and the introduction of the Public Health Levy. This leaves £147 million which can be accounted for by economic growth or variations on appeals expectations. Business is rightly concerned that should the Government fail to recoup this sum, they may face a further tax raid through business rates. Given that economic forecasts for the next three years are being downgraded, this is a realistic fear.

Scottish Chambers of Commerce
December 2011

[6] Scottish Government Press Release, 27 September 2011