SUBMISSION FROM THE SCOTTISH CHAMBERS OF COMMERCE

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.

Scottish Chambers of Commerce welcomes the opportunity to input into the Economy, Energy and Tourism Committee’s inquiry into the Scottish Government’s Draft Budget for 2012-13 and Spending Review. 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. 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.

What is the outlook for the Scottish Economy over the next three years and what are the major risks?

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.

Strathclyde University’s Fraser of Allander Institute have forecast Scottish economic growth at 0.8% in 2011, 1.5% in 2012 and 1.9% in 2013 but it is possible that these predictions could be revised over the coming weeks. 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 continues to highlight the difficulties of rising costs in a market where it is difficult to pass these on to customers. 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.

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.

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1 Fraser of Allander Economic Commentary, June 2011
2 Scottish Chambers of Commerce Quarterly Business Survey Q3 2011, October 2011
Has the Scottish Government adopted the most appropriate priorities in this budget for the year ahead and over the period to 2015 – particularly in the division of resources between social programmes and investment in education and infrastructure?

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.

In terms of revenue budgets, the Scottish Government must look to their Central Purpose of delivering increased sustainable economic growth and measure spending priorities against this. 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.

In terms of education, the Scottish Budget has maintained Higher Education funding but funding for Further Education is reduced amid plans to develop more regionalisation in terms of college services. The Chamber network has expressed some concern over this, particularly in view of the high quality of linkage that exists in many places between local colleges and local businesses. These connections need to be prioritised within the Government’s spending plans.

The budgets of the Enterprise Agencies have enjoyed some degree of protection – is this appropriate and how should the Enterprise Agencies focus their resources to promote recovery and growth?

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 programme 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.

**Resources for Renewable Energy projects to be spent through SE and HIE have been substantially increased – how can these resources be most effectively deployed?**

We welcome the 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 developments, 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.

**Resources available to VisitScotland have been increased – is this appropriate and how should they be applied?**

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. 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.

**Will the continued reduction in spending on social housing investment frustrate attempts to reduce fuel poverty by slowing the rate of improvement in the housing stock?**

SCC supports the construction of affordable housing throughout Scotland, both in the social rented sector and in terms of low cost ownership options. We believe that this accommodation is required in our economy and that its construction could deliver much needed work in our building trade. Alongside transport, affordable housing represents the best return on investment for public projects. Ways must be found to encourage future development of this nature.

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3 Hospitality: driving Scotland’s local economies. British Hospitality Association, October 2011
How will fuel poverty be affected by increased reliance on relatively expensive renewable energy?

Scotland has a wealth of renewable energy resources, but these are increasingly coming at a cost. Scotland is almost uniquely placed in Europe as a source of wind and tidal generated electricity, and it is rightly seen as a major opportunity for Scotland and Scottish business, particularly in the area of offshore wind generation capacity. However the costs of these projects is going through the roof, a recently announced second round project in the Irish Sea speaks to an investment of £1.6bn for a windfarm of 389MW capacity - this is £4.1million/MW which is 25-35% more expensive than the next closest technology and 25% more expensive than the estimates of 18months ago. According to Mott McDonald, the costs of generation from these windfarms are now approaching 19p/KWh. Compare the current wholesale spot price of Gas of between 1.75-2p/KWh.

Mott McDonald in a report on the DECC website\(^4\) are projecting an electricity price of 25p/KWh as a result of these costs, with the other sources of generation being brought up to this base by the addition of the costs of Carbon Capture and Storage – which is in itself unknown at the moment - and the imposition of so-called Carbon Taxes. The Scottish Government have committed to have the majority of generation coming from this very expensive source by 2020. This is indeed a very significant opportunity for Scotland, but only if the cost base is right. If as a consequence the rest of the economy is disadvantaged then perhaps such a total commitment is misguided. This stresses the importance of a balanced energy policy.

Business rates are to be increased in line with inflation – will this represent an increased burden on business and will it affect business performance in general and how will the tobacco and alcohol levy affect the retail sector in particular?

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

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. We hope that the UK Government will refrain from passing on the whole of this increase and that the Scottish Government will follow suit. If the UK Government carries on with the full 5.6% increase, then we would urge the Scottish Government to minimise the rise north of the border.

The second worrying aspect of business rates costs is the plan to limit Empty Property Relief. Currently empty premises 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%, 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.

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.

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 them on this.

**It is assumed that over the period to 2015 economic growth will deliver significantly increased rates income. Is this realistic in the light of economic prospects?**

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)\(^5\). 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.

**What are the implications of the shift of some £200m pa in revenue spend to capital – both for investment and services and for economic growth?**

As mentioned earlier, SCC welcomes the shift from the revenue budget to the capital budget both as a means to deliver best value economic growth and as part of a general shift in Government spend from consumption to investment. There is room for the trimming of some non-essential services but overall service levels need not suffer if the Government takes the advice of the findings of the Independent Budget Review and the Christie Commission. If transport infrastructure investment is prioritised, then the Government can maximise the economic impact of capital investment.

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\(^5\) Scottish Government Press Release, 27 September 2011
Conclusion

Scottish Chambers of Commerce are happy for this submission to be published and attributed to us. We are happy to assist the Committee in expanding on any of these issues.

Scottish Chambers of Commerce
October 2011