08 January 2018

Dear Gordon,

**Scottish Parliament EJFW Committee – Draft Budget 2018-19**

Thank you for the opportunity to discuss the Economy, Jobs and Fair Work portfolio chapter of the Draft Budget at my Committee appearance on Tuesday 19 December. I agreed to follow up in writing on the following areas:

- To outline the correlation between immigration, unemployment, wages and skills;
- To provide information on what assessment has been made of the economic impact of cuts to non-domestic rates; and
- To clarify whether as a consequence of the reclassification of particular projects, £234 million of public borrowing will be spent on infrastructure projects, such as the Aberdeen western peripheral route.

Responses to these can be found in the attached annex.

In addition I agreed to share the details of the activities of the National Investment Bank with the Committee once these are confirmed. I would like to advise that the formal Implementation Plan from Mr Benny Higgins and his Advisory Group is not due before February, and I will therefore respond in due course.

Yours sincerely,

KEITH BROWN
To outline the correlation between immigration, unemployment, wages and skills

The impacts of immigration on the labour market can vary, depending on the skills of migrants, the skills of existing workers, and the characteristics of the host economy, as well as over the short and long run\(^1\). In theory, in the short-term, if migrant and host population skill levels are very similar, then immigration could increase competition in the labour market and drive down wages, potentially increasing unemployment in the host population. Conversely, if skill levels are complementary, then all workers would expect to see a rise in productivity and wages overall. Effects over the longer-term also vary depending on the characteristics of the economy. In periods of growth, immigration can cause labour demand to grow over the medium to long term, as the increase in the population boosts demand for goods and services and potentially investment to grow. This effect is likely to be subdued during periods of recession.

In line with the theory, available evidence\(^2\) for the UK has suggested that inward migration does not appear to have had a statistically significant impact on the average wages and employment opportunities of the UK-born population in periods when the economy is strong, although there is some evidence of labour market displacement when the economy is in recession. In addition, a recent summary of the macroeconomic effects of migration from the EU undertaken by the IMF\(^3\) reported that there is little evidence that EU migration has led to either job losses or lower wages for UK citizens. The report instead found the evidence to be more consistent with the notion that EU migrant labour has overall had a positive effect on the UK labour market - allowing UK firms to better match workers to jobs, allowing them to work more efficiently and boosting demand for overall labour.

In terms of impact on specific groups, evidence for the UK indicates that any adverse wage effects of migration are likely to be greatest for resident workers who are themselves migrants\(^4\). Finally, evidence also supports the theory that any displacement effects tend to dissipate over time, as the labour market adjusts\(^5\).

In terms of wage and skill levels, several studies in Scotland and the UK have found a 'U-shaped pattern' of wage distribution among migrants, with employment concentrated at the top and bottom of the occupational distribution curve. A body of Scotland-specific evidence exists on the use of migrant labour\(^6\).

Migrants, particularly recent EEA migrants, tend to be concentrated in hospitality and catering; in agriculture; and in food processing sectors. In general, migrants meet demand for low-skilled labour, and address sector-specific skills shortages at the higher end of the labour market. In addition, migrants act as a flexible supply of labour when demand exceeds local labour supply. However, in sectors such as agriculture, where employers find it difficult to source labour regardless of prevailing economic conditions, demand for seasonal migrant labour remains more constant.

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6. Ibid.
Overall then, attracting skilled migrants is key to ensuring Scotland’s future economic growth. The economic evidence suggests that migrant workers can fill skill gaps, complement the skills of domestic workers and help drive productivity improvements in the economy. Migration can also help mitigate the demographic pressures arising as a result of Scotland’s aging population.

Recent Scottish Government modelling undertaken for the response to the Migration Advisory Committee looked at the economic contribution of EU citizens to the Scottish economy⁷. This work found that on average, each additional EU citizen working in Scotland contributes a further £34,400 in GDP. This analysis implies that the total contribution by EU citizens working in Scotland is approximately £4.42 billion per year.

**To provide information on what assessment has been made of the economic impact of cuts to non-domestic rates**

The SFC’s report “Scotland’s Economic and Fiscal Forecasts, December 2017” does not comment in detail on the economic impact of the business rates measures announced by the Scottish Government on 14 December.

The Scottish Government is absolutely committed to supporting business and growing Scotland’s economy – in this budget we have more than doubled our spending on economic growth, with spending per head now more than £100 higher in comparison with the UK government.

Our reforms to the non-domestic rates system will ensure that Scotland provides the best possible environment for businesses to start-up grow and scale-up. We are providing the most competitive reliefs package in the UK – worth a record £720 million; using CPI rather than RPI to calculate the annual uplift in the poundage – as requested by business; protecting the Small Business Bonus Scheme – lifting 100,000 properties out of rates altogether; and continuing to provide better support for SME’s than elsewhere in the UK.

The economic impacts of measures to increase business growth and productivity are structural and long-term in nature, and policy decisions have been informed by both the Barclay review and our own wide engagement with industry. The impacts of the rates growth measures, including on future rates income estimates, will be kept under review as evidence becomes available.

**To clarify whether as a consequence of the reclassification of particular projects, £234 million of public borrowing will be spent on infrastructure projects, such as the Aberdeen western peripheral route.**

As set out in the Draft Budget 2018-19 the intention is to borrow £450 million to invest in infrastructure and support our capital investment plans in 2018-19.

The reclassification of NPD projects to the public sector following ESA10 resulted in capital budget cover being required over the construction period, rather than through revenue budgets over the life of the NPD contracts of 25-30 years. In 2017-18 the capital budget cover that was required was £234 million. This was factored into the capital allocations within the 2017-18 Draft Budget which included the expectation that we would utilise the full £450 million in borrowing available in 2017-18.


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Four of the five projects affected by reclassification have already completed or will complete construction by the end of 2017-18 therefore no further budget cover is required for these in 2018-19, in relation to the NPD element. The only budget for the NPD projects in 2018-19 is £33 million for Balfour Hospital in Orkney. It should be noted that although this project was planned to be an NPD project and was affected by ESA10 it was further behind in procurement than the others therefore the majority of this project is capital funded with only a small NPD element of £5.1 million.