

European and External Relations Committee

The EU referendum and its implications for Scotland

Written submission from Highlands and Islands Enterprise

Introduction

HIE welcomes the opportunity to respond to this call for evidence. We recognise that the influence and impact of EU membership on the Highlands and Islands is widespread and extends beyond HIE's remit. HIE's focus will be the impact of EU membership on the socio economic development of the region and consideration of the key elements of a beneficial future EU relationship. HIE recognises that there are currently many uncertainties regarding the process, timing and outcome of negotiation following the referendum. Our thinking will evolve as the process develops and we therefore look forward to a continuing dialogue over coming months.

Who are we?

Highlands and Islands Enterprise (HIE) is the Scottish Government's economic and community development agency for the north and west of the country. Our region comprises over half the Scottish land mass (including 94 inhabited islands) and is home to around 470,000 people.

HIE's role is to lead regional growth and development in line with Scotland's Economic Strategy (SES), improving competitiveness and building a fairer society across the Highlands and Islands.

HIE's approach to regional development is closely aligned to the national priorities described in SES: Investment, Innovation, Internationalisation and Inclusive Growth. We help build successful businesses, social enterprises and resilient communities; support the growth of industry sectors, and invest in the strategic interventions which create the conditions for a competitive region. Our current priorities, planned activities and budget information can be found in our Operating Plan 2016-19¹.

The impact of EU membership on the Highlands and Islands

The economic and social development of the Highlands and Islands has been materially impacted by UK membership of the European Union, particularly over the last 25 years. EU policy and funding continues to make an important contribution to our success. Furthermore, as a small region (in population terms) with a modest internal market, business success has been driven by selling into new markets – the UK and EU markets being particularly important – by people and talent attraction, including a significant number of EU nationals – and by inward investment, aided by our position within the EU market.

Businesses have been able to trade freely across the single European market of 500m consumers, enjoying tariff free market access and common product standards

¹ [HIE Operating Plan 2016-2019 Building our Future](#)

and regulations across the EU. Inward investors have made the Highlands and Islands their home within the EU market.

The Highlands and Islands has seen a substantial and welcome growth in population over the last 50 years – a 23% increase between 1965 and 2015, compared to 3% across Scotland as a whole. This has included significant inward migration from elsewhere in Europe. Businesses have been able to access the labour they need to grow – particularly important in food and drink and tourism sectors where a significant proportion of the labour force is from outside of the UK. Well qualified and talented people have moved to the region as new sectors such as energy and life sciences have emerged.

The Highlands and Islands has been a net beneficiary of EU funds over the last 25 years. The EU has been the principal driver in regional policy that has seen special attention paid to regions with lagging GDP (compared with the EU average) and / or particular economic and social challenges. Successive structural fund programmes have seen investment of almost €1bn of ERDF and ESF in the region, delivered through collaborative and co-ordinated programmes.

As a predominantly rural region, the Highlands and Islands has been a beneficiary of CAP funding, supporting agriculture and land based industries, environmental enhancement, rural business development and community support.

The Highlands and Islands has also participated in collaboration projects supported through EU competitive programmes such as Horizon 2020 and its predecessor R&D programmes, and a number of INTERREG transnational programmes

Immediate impact of the referendum decision

Following the EU referendum in June, there is little clarity on the next steps. This uncertainty is impacting on business confidence in the UK and across Scotland. The HIE Business Panel, surveyed in August, indicated the following²:

- More than half of businesses (55%) said that the EU referendum result had made them less confident about Scotland's economy
- Around 45% of businesses were less optimistic about future business prospects following the EU referendum result
- Around a third of businesses stated that they were more likely to delay investment plans (16%) or be less likely to invest (15%) as a result of the referendum outcome

Four further business panel surveys will take place over the next 12 months, giving HIE an opportunity to track changing business issues and attitudes as post referendum negotiations develop.

There is also uncertainty over the availability of EU funds in the current 2014-2020 programme, including the European Structural and Investment Funds (ESIF)

² HIE Business Panel Survey July – August 2016

allocated to Scotland and EU competitive funds. This has a potentially detrimental impact on businesses, academic institutions, communities and individuals. While the recent UK Government announcement³ has provided a degree of short term certainty, indicating that structural and investment funds (ERDF, ESF, EAGGF, EMFF) approved prior to the UK Treasury Autumn statement will be honoured, CAP support will remain at current levels until 2020 and any competitive funds secured before the UK leaves the EU will be honoured. Further clarity, particular on the treatment of structural and investment funds, is required as a matter of urgency.

HIE suggests that a number of measures could be considered to bring greater clarity to this and to maximise the impact of current EU funds to Scotland and the Highlands and Islands:

- Maximise the approval of funds across all of the Investment Priorities identified in the Operational Programme
- Extend the timescale for existing operations (currently end of 2018) to facilitate full spend of existing commitments
- Take a flexible approach to facilitate approval of new commitment in strategic interventions, supporting activity beyond the end of 2018 and up to the end of the current programme period
- Consider increasing intervention rate where this can aid the effective use of funds

Medium / Long term post Referendum issues and challenges

It is beyond the remit of HIE to recommend alternatives to Scotland's current position within the EU as part of the UK. It is however, possible to identify some of the key issues and challenges for the Highlands and Islands as the post referendum negotiation process evolves. In broad terms, there are three issues of particular importance to the socio economic development of the Highlands and Islands:

Access to Markets

- The EU single market is worth £11bn per annum to Scotland and is the main destination for Highlands and Islands exports. It is particularly important for some of our growth sectors such as food and drink and our location in the single market is attractive for inward investors. Access to the European market is currently free from tariffs and customs arrangements and businesses operate in an environment where common standards apply. Retaining easy access to the single market is fundamental to the export competitiveness of our businesses.
- Export markets outside Europe are also important to the region's businesses and they enjoy access to over 50 markets through EU negotiated trade deals. It is important that post referendum arrangements are not detrimental to this market access in the short term. In the longer term, while a UK outside of the EU may be free to negotiate bilateral trade agreements with other countries, this is likely to be a complex and time consuming process resulting in many years of uncertainty.

³ HM Treasury - [HM Treasury letter](#)

- European and overseas markets are also sources of imported raw materials for Highlands and Islands businesses. This supply will also be impacted by trading arrangements and exchange rates
- Trade in services is an increasingly important element of regional exports and is likely to grow in importance, given the widening availability of fibre broadband. The European single market in digital services, although not fully developed, is likely to present new opportunities (as well as greater competition) for service businesses.
- Increased internationalisation of Highlands and Islands businesses is a key driver of regional economic growth and is particularly important to a region like the Highlands and Islands. Businesses that operate internationally are more productive and more likely to innovate. Retaining easy access to European and global markets is a priority for Highlands and Islands businesses.

Attraction of talented people to live work and study in the region

- The Highlands and Islands is a sparsely populated region with people attraction as one of its main objectives. The region has attracted a significant number of EU nationals to work and study here. While exact numbers are not available, estimates suggest there are over 10,000 living, working and studying in the Highland Council region alone.
- Businesses in the Highlands and Islands rely on overseas labour in a number of ways. In some sectors such as food and drink and tourism, EU nationals make up a significant proportion of the labour force. Analysis by the Scottish Tourism Alliance shows that across Scotland as a whole 24% of employees in hotels and 30% in restaurants are migrant workers, many of them from Europe. Similarly, an estimated 39,000 EU nationals work in the Scottish Food and drink industry. In other sectors, the ability to source the right skills from an EU labour market is important.
- Equally important is the mobility across Europe of researchers and students, both made possible by free movement of people throughout the EEA. The former is aided by transnational collaboration on research and development, supported by Horizon2020, the latter by the Erasmus+ programme, providing support for student exchange.
- HIE has specific objectives to attract (young and talented) people to live, work and study in the region. It is imperative, therefore, that the Highlands and Islands (and Scotland) retains an ability to collaborate with partners on research projects and to facilitate student exchange.

Favourable policy and funding environment

- The Highlands and Islands has been a major beneficiary of EU resources over the past 25 years, particularly through successive structural funds programmes and CAP funds, and also through participation in other EU programmes such as Horizon 2020 and its predecessors and the various INTERREG programmes. These funds and the policies that underpin them, will continue to be important to

the Highlands and Islands. The region has also benefitted from an EU approach to Competition Policy that has given public agencies significant state aid powers to invest public funds in addressing the development challenges in the Highlands and Islands.

- **Regional Policy** – the EU has been the principle driver of Regional Policy in Europe over the past 25 years. Such policy has focused on regions where GDP per capita lags the EU average and on regions addressing specific and permanent challenges of geography and demography. The Highlands and Islands has benefitted from investment of almost €1bn in structural funds since 1990, through successive programmes delivered in a strategic and collaborative way. HIE and our regional partners have already begun to consider the future shape of Regional Policy (discussion on this has already started in Brussels). While the responsibility for regional policy will not become clear until post referendum negotiations progress, a continued focus on the specific development challenges and opportunities of regions like the Highlands and Islands, backed up by appropriate resources, is necessary, irrespective of where responsibility lies.
- **Agriculture / Rural Policy** – as a predominantly rural region, the Highlands and Islands is a major beneficiary of CAP funds – Pillar 1 providing direct support to farmers and crofters and pillar 2 providing funds for rural development, including LEADER. CAP supports productive farming as well as environmental and social “public goods”. Agricultural incomes, including CAP support, underpin many marginal rural communities and reductions in future funding could have detrimental impacts on the sector and on community sustainability. As with Regional Policy, it is not clear where the responsibility for agriculture and rural development will reside in the long term. HIE will therefore focus on identifying the specific requirements of the region and engage with policy makers to develop innovative and effective policy that addresses the particular issues in the Highlands and Islands.
- **Collaboration funds (eg INTERREG, R&D funds (Horizon2020))** – Collaboration with EU partners is an important benefit of our EU membership. Highlands and Islands organisations have collaborated extensively with European partners on a range of INTERREG and R&D projects. HIE is a partner in an INTERREG Europe project looking at cluster development and a Cross Border innovation support project (with Northern Ireland and the Irish Republic). There is also extensive regional participation in the Northern Periphery and Arctic INTERREG programme and our universities value their involvement in Horizon2020 R&D projects. Such partnerships give the region access to new ideas and new thinking as well as funding.

The ability of regional partners to engage and collaborate with their European counterparts will become more difficult if access to these programmes is not possible. It is important, therefore that access to these programmes is retained to ensure institutions across the region are able to participate in collaborative research and development programmes, and maintain and develop their attractiveness for both talented people and funding in the longer term.

Conclusion

The EU referendum outcome has resulted in a period of intense uncertainty that is having a material impact on the Highlands and Islands, its businesses, organisations and people. EU membership has delivered a range of benefits to the Highlands and Islands and there is a significant risk that some or all of these benefits may be lost in the period of post referendum negotiation and thereafter. HIE's view is that:

- Short term uncertainty that still exists about the accessibility of EU funds should be addressed as a matter of priority and steps taken to maximise the use and benefit of current EU funds
- The benefits to the Highlands and Islands resulting from EU membership are recognised and steps taken to ensure that future arrangements concerning market access, access to skills and labour and future policy and funding arrangements address the challenges and opportunities in the Highlands and Islands.

Post referendum negotiations will be complex and lengthy. HIE looks forward to participating in a continuing dialogue, ensuring that the region has a strong voice as the process evolves.