OFFICIAL REPORT
AITHISG OIFIGEIL

DRAFT

Economy, Energy and Fair Work Committee

Tuesday 7 May 2019

Session 5

The Scottish Parliament
Pàrlamaid na h-Alba

Tuesday 7 May 2019

CONTENTS

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ECONOMY, ENERGY AND FAIR WORK COMMITTEE

15th Meeting 2019, Session 5

CONVENER

*Gordon Lindhurst (Lothian) (Con)

DEPUTY CONVENER

*John Mason (Glasgow Shettleston) (SNP)

COMMITTEE MEMBERS

*Jackie Baillie (Dumbarton) (Lab)
*Colin Beattie (Midlothian North and Musselburgh) (SNP)
*Angela Constance (Almond Valley) (SNP)
*Jamie Halcro Johnston (Highlands and Islands) (Con)
*Dean Lockhart (Mid Scotland and Fife) (Con)
*Gordon MacDonald (Edinburgh Pentlands) (SNP)
*Andy Wightman (Lothian) (Green)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Paul Brewer (Advisory Group on the Implementation Plan for a Scottish National Investment Bank)
Eilidh Dickson (Engender)
Benny Higgins (Advisory Group on the Implementation Plan for a Scottish National Investment Bank)
Robin McAlpine (Common Weal)
Alan McFarlane (Advisory Group on the Implementation Plan for a Scottish National Investment Bank)
Ray Perman (Royal Society of Edinburgh)

CLERK TO THE COMMITTEE

Alison Walker

LOCATION

The David Livingstone Room (CR6)

Scottish Parliament

Economy, Energy and Fair Work Committee

Tuesday 7 May 2019

[The Convener opened the meeting at 10:00]

Decision on Taking Business in Private

The Convener (Gordon Lindhurst): Good morning and welcome to the 15th meeting in 2019 of the Economy, Energy and Fair Work Committee. I ask everyone present to turn their electrical devices to silent to ensure that they do not interfere with proceedings.

Agenda item 1 is a decision on taking business in private. Does the committee agree to take items 3 and 4 in private?

Members *indicated agreement.*

Scottish National Investment Bank Bill: Stage 1

10:00

The Convener: Agenda item 2 is evidence taking from a number of witnesses on the Scottish National Investment Bank Bill. I welcome to the meeting our first panel: Benny Higgins, strategic adviser on the establishment of the Scottish national investment bank; and Paul Brewer and Alan McFarlane, former members of the advisory group on the implementation plan for the SNIB, as I think we will be shortening the name to. Thank you for coming in this morning.

First of all—and I think that these might be questions for Benny Higgins—what went into the development of the implementation plan? Have its 21 key recommendations been adequately reflected in the bill that is before Parliament?

Benny Higgins (Advisory Group on the Implementation Plan for a Scottish National Investment Bank): On the first of your two questions, our reasonably large advisory group drew skills and experience from various parts of the Scottish economy and business sector. One of our key advisers was Mariana Mazzucato, whose work on mission-related patient capital investment was a key part of what we were pursuing.

More important, we had a very large number of sessions with different participants and actors across the ecosystem in Scotland. I personally sat through many dinners, breakfast meetings and other sessions that attracted a huge number of people and which ensured that we could listen very carefully to what people thought were the issues that needed to be tackled. As we went through the implementation plan process, we were able to start test driving some of our thoughts. That approach proved to be very successful and gave us a good understanding of the issues that people thought had to be tackled, and we have carried much of that process into where we are now.

As for the 21 key recommendations in the plan, all of them have been accepted. However, I am perhaps not best placed to talk about the details of the bill; others are probably more qualified in that respect, and I think that you have already heard from some of them. From my perspective, though, the approach chosen in the bill is relatively light, which means that it will not get in the way of implementing the recommendations. I would just point out that not all of the recommendations are covered in the bill, which is enabling legislation that will allow us to do everything that we need to do.

The Convener: Do the other two witnesses wish to comment?

Paul Brewer (Advisory Group on the Implementation Plan for a Scottish National Investment Bank): I think that Benny Higgins has covered the matter very fully.

Alan McFarlane (Advisory Group on the Implementation Plan for a Scottish National Investment Bank): The broad thrust of the group's discussions is reflected in the bill, but, of course, the detail will be everything. No doubt some aspects of that will be the focus of the committee's own discussions. Working through that detail will be critical.

The Convener: Thank you.

Dean Lockhart (Mid Scotland and Fife) (Con): Good morning, panel. Other recent Government initiatives such as the Scottish growth scheme have made a supply of money and capital available to the economy, but uptake of those kinds of financing schemes has been insufficient, because of a lack of demand in the economy itself or an insufficient number of growing businesses to access the supply of finance and capital. Will that lack of demand continue to be an issue and, if so, how will the bank address it?

Paul Brewer: It is difficult to talk about supply and demand across the whole system of investment, because they vary a lot at different levels. You need different interventions at the microfinance level, where businesses are still developing their capacity to raise finance; indeed, often their understanding of what financiers are seeking requires to be developed before the finance can be raised. In comparison, with companies going into their second or third phases of financing, it will be a matter of investors looking very closely at their performance and products, investing larger amounts of money and taking greater risks.

If we can generalise broadly about Scotland, I would say that microfinance, business angels, the Scottish investment bank and so on compare very well with activities in any other jurisdiction that has them—Scotland is particularly strong on the angel investment network. However, once companies are getting into their second and third phases of growth, there are far fewer indigenous investors and companies have to look more widely for finance. That is not a bad thing in itself, but it means that those companies are competing in a much more crowded market.

Therefore, there are areas in which we need to stimulate demand or support companies to create demand that financiers will respond to, but there are other areas in which there are gaps, particularly for companies that are growing beyond the Scottish investment bank's capability to invest and which are looking for larger sums.

Alan McFarlane: Your question touches on one of the reasons why it is fundamentally a good idea to form this type of institution. Making funds available for a particular period and expecting demand for those funds automatically to be there is not how life works; instead, we are talking about forming an entity that is here for the long term and which is demonstrably patient, evergreen and continuing.

One of the things that is very striking about the British Business Bank's website is its recognition of having to make it clear to people what is available. It is great to have a programme at a particular time and hope for uptake, but there are no guarantees in that; having an enduring and continuing entity, which makes it its business to let everybody know that it is available, is a big step forward. Mr Lockhart is right that it would be great if there was more uptake, but I would not say that that damns anything.

Benny Higgins: Your question is very good. Obviously, a supply of capital does not solve anything unless there is sufficient demand.

I see the creation of the bank as doing more than adding an important new piece to the ecosystem in Scotland. There is also an opportunity for Scotland to use the bank as a catalyst for starting to unclutter the landscape and ensure that other parts of the apparatus—specifically Scottish Enterprise, Highlands and Islands Enterprise, the developing south of Scotland enterprise, other Government departments and various other bodies—work together properly. The next couple of years must be the time when we get all the pieces of apparatus working together in an uncluttered way. We have got to stop finding refuge in complexity and look for simplicity. There has got to be more effective collaboration than there has been.

We have a lot of strengths in Scotland—an obvious one is the university sector—but far too many of our great research projects that move into development get trapped at the micro capital level. That is because there is insufficient understanding of and support for how to use different kinds of finance equity and debt. The bank in itself will not solve demand—origination will come from some of the other parties that I mentioned—but we need to use the bank as a catalyst for resolving the issues. We have a great opportunity to do that; it would be a missed chance if we did not.

Dean Lockhart: That brings me on to the next question. You have touched on interaction with other agencies. The question of demand raises another issue. The bank will be a supplier of capital, but its reach can only go so far; getting the underlying stimulus, changing the culture and generating a more enterprising economy will need more than a supply of capital. How do you see that being done in order for the bank's mission to be successful? How will that interaction with the other agencies work in practice? Will demand and origination still sit with Scottish Enterprise and the enterprise agencies? What part might the bank have in stimulating demand?

Benny Higgins: We are working very closely at project level. To an extent, we are running a shadow bank, using the resources that are available from the building Scotland fund and other pools of resource. The Scottish investment bank that exists as part of Scottish Enterprise will come across. Origination will take place, but not in the bank itself.

We need to distinguish between the small and medium-sized enterprise sector and the long-term patient capital projects that will be mission related. The bank will work more on the origination in relation to the mission-related projects, while SMEs will be covered by the existing agencies, principally, and Government departments.

As the committee probably knows, the British Business Bank basically funds funders. That ability will be open to the Scottish national investment bank, so some such funding will take place. However, we also want to ensure that the bank provides direct investment. The origination engine will be other parts of the apparatus, which is why we need to work closely.

We are working hand in glove with Scottish Enterprise, as we will be with HIE for the rest of this year. As Alan McFarlane said, the devil is in the detail. It is easy to say where origination lies and that we need to work hand in glove—that sounds straightforward—but we need to work out precisely how we do that; that is what we are doing. Steve Dunlop, who is the relatively new chief executive of Scottish Enterprise, has shown his commitment to ensuring that our working relationship and collaboration get us to the right place.

Alan McFarlane: I used to work for one of the predecessors of the proposed bank. I hope that the committee will find it useful to hear that this work rests on 40 or 50 years of experience. As some of you will know, we have had the Industrial and Commercial Finance Corporation—it is now called the 3i Group—which was partly owned by the Bank of England. There has also been the Scottish development fund, under the Scottish Development Agency. Before George Mathewson left the SDA, he brought in some people who were specialists in investing in small businesses.

Dean Lockhart mentioned demand. Demand in the early 1980s was affected by the rapidly changing economy, and a lot of it involved management buy-outs. Some people might remember the Carron steelworks at Falkirk, and Scottish Development Agency finance and the private sector were instrumental in helping to buy out at least three divisions. There are not many examples of that today. Demand is changing because of technology, marketing and some of the other industries in which we are active.

I think that Dean Lockhart's question was how cyclical is the economy and how cyclical is demand, but I am afraid that I cannot help on those points. However, if we have a permanent institution, the likelihood of being able to match supply with demand rises. To this interested layman, it seems that the net effect of having a financial body that, ultimately, is not part of SE and which acts as a serious long-term investor will be good. It is highly likely that the bank will stimulate demand; the extent of that demand is the question.

Dean Lockhart: We can come back to the issue a bit later, because I do not want to hog the meeting, but my question was about structural issues, in relation to the missing middle. The committee has heard evidence that although we have many microbusinesses and a couple of very large businesses in Scotland, we need to scale up our support for the missing middle. The bank might be part of the answer, but it seems that a wider restructuring of the landscape is necessary in order to grow that missing middle. Perhaps we can come back to that issue later.

The Convener: Do any of the panellists want to comment now?

Paul Brewer: I would add only that Benny Higgins's distinction between investment in the SME sector and the mission-oriented element is very important. In the areas in which the bank will focus in order to make a real difference to our economy, it will need to bring in considerable expertise and to work as part of the whole ecosystem. Whether it is in low carbon or digital and data—in which we have fantastic academic expertise—the bank will need to work with academia, existing businesses and other investors to bring in considerable expertise, so that Scotland is seen as a place with a fertile investment environment. That is a different environment from the environment that supports SMEs, so the bank will need expertise in both areas.

Gordon MacDonald (Edinburgh Pentlands) (SNP): Over its first 10 years, the bank is to be capitalised with about £2 billion. What impact could that have on the Scottish economy?

10:15

Benny Higgins: I do not know the precise answer but, if we deploy £2 billion in the area of the market that has been referred to a number of times—in supporting the opportunity for SMEs to scale up—that can feed ambition. We need to have SMEs that are prepared to go from being microbusinesses to being more credible small businesses and then bigger businesses.

The hallmarks of successful economies in the 21st century will be focusing on carbon neutrality, automation, artificial intelligence and machine learning and responding to demographic changes. Scotland is well placed on some of that but not as well placed on other aspects. We have a good track record on renewables, but we have not industrialised the impact of what goes on in universities on data, robotics and automation, which is a great basis. As I said, the bank can play a part in opportunities to make such SMEs grow. On the demographic challenge, we start in a difficult place, because our demographic challenge is harder than the average. The bank needs to make contributions so that we are better placed.

The sum of £2 billion represents 1.3 per cent of gross domestic product; that is about in line with the figure for many national investment banks around Europe—particularly in smaller advanced nations, of which we must consider ourselves to be one—and is not unreasonable.

In the longer run, we will look at ways to leverage investment. Direct leverage would require a dispensation from the Treasury, but there are other ways of using the capital for leverage—through co-investment, guarantees and so on.

The impact is difficult to speculate on but, if we can manage to use putting £2 billion into the economy as the catalyst for getting the rest of the framework in place, it will give us a wonderful opportunity to make a big difference.

Gordon MacDonald: Will the £2 billion act as leverage for private investment in companies and other organisations?

Benny Higgins: One thing that is common is co-investment; that is what the Green Investment Bank did. There are many examples that encourage us about what the new bank will do. We have talked to such banks around the world—we visited KfW, we went to see the Irish bank and I will soon go to see the Finnish bank, which does similar things. We must look at and learn from other organisations.

Co-investment is one way in which we can create markets. The private sector's risk appetite is such that it will not invest in some of the long-term mission-related projects, because of the timelines that are involved. We hope that an anchor investment from the Scottish national investment bank will encourage more investment. That is there to be played out.

Alan McFarlane: The money is not entirely incremental. A report last year from Scottish Enterprise, which I am sure it sent to the committee, showed that £538 million of deals were done in Scotland and that the figure has been on an upward trend since 2012. The sum of £2 billion is £200 million per annum over 10 years. I do not wish to disagree with the chair of the advisory group—Benny Higgins is right—but it could be argued that the denominator is not the £170 billion that is Scotland's gross national product but 10 times that number.

To return to a question that Mr Lockhart asked, the approach could be significant if it is targeted, but it cannot be a blunderbuss. A key mission for the bank's board of directors, when constituted, will be to work that out.

To take the point about the middle, let us assume that there is a group of companies in Scotland for which £10 million would be the appropriate financing. I will be clear about the leverage that we are talking about. Traditionally, leverage means borrowing money against your own balance sheet, but that is not intended for the bank—the bill explicitly forswears that. Leverage will therefore mean influencing others to behave differently from how they otherwise would have behaved. There is clear evidence from Scottish Enterprise that the Scottish investment bank has been quite good at that already, through the co-investment fund. That is a solid foundation for optimism.

However, if the bank provides only £10 million for each company, it would be supporting only 200 hundred companies and would be ignoring the mission-related stuff. If those companies were the missing middle and were constituted differently, that would represent great success. That is what I mean by the detail in the numbers; it is the ambition measured by the actual funds available.

I add that it is very clear from the bill that the money is committed up to 2021. Bearing in mind that things change in politics, the more of a cross-party parliamentary commitment there is to the £2 billion the better. The commitment is £320 million, plus the £300 million that is coming from the Scottish investment bank's existing portfolio. If we run all of those numbers together, it is a stretch in parts, but they are not damning. There is a real basis for incremental improvement in the middle. Those are the kinds of numbers that I would be delighted for you to take away with you.

Gordon MacDonald: I am sure that some of my colleagues will talk about the mission statement and the focus of the bank. I have a couple of remaining questions. The financial memorandum highlights that in year one the operating costs will be £15.6 million, which rises to just over £25 million by 2025-26. Are the proposed levels of operating costs in the bank's first few years realistic?

Benny Higgins: Yes. We have modelled that on the basis of the nature of the activity and the number of people involved. It is our best guess. We have taken as many readings against similar organisations as we can, so we think that it is realistic.

Gordon MacDonald: Why does the Royal Society of Edinburgh say in its evidence that there could be problems with that level of operating cost?

Benny Higgins: You should ask it.

Gordon MacDonald: I intend to.

Benny Higgins: That is fine. All that I can say is that we have sought to be as realistic as possible about the cost structure. We think that, once established, the bank would have between 85 and a bit more than 100 people in its business and institution. The cost structure has been test driven by various people to ensure that we are in the right ballpark. There is a related issue around pay, which we have talked about and which will have to be dealt with before we are done.

Angela Constance (Almond Valley) (SNP): Good morning, panel. Like my colleague Mr MacDonald, I always like to cut to the chase. I wondered if any projections or modelling had been done on what the Government can expect for £2 billion of investment. Have there been any projections on the number of jobs created or supported, the number of businesses started or supported to grow, or the ratio of capital that can be leveraged?

Benny Higgins: That is another version of the question that was asked earlier: what do you get for your £2 billion and what will the impact be on the economy? I am not sure that I can do much better than the answer we gave earlier. We are working on what the bank's key performance indicators should be. One has to remember that we have to get back to the national performance framework, which outlines what we are trying to achieve in Scotland. The bank should play its part in delivering that.

Royal assent will probably be received around this time next year. By that point, we will have a chair, a board and an executive team. We still have a lot of work to do and have to start to develop the key performance indicators. However, at this juncture, we are not trying to project the number of jobs or businesses that will be created. We know that we need to create more jobs and businesses in Scotland, and that we need to help the microcap companies to become midcap companies and the midcap companies to become bigger businesses. This is a great chance to make a big impact in that respect.

Angela Constance: To be clear, I am not asking you to look into your crystal ball. Bearing in mind that reasonably solid work has been done that demonstrates, for example, that every £100 million of capital investment can support 1,400 jobs, there must be some sort of modelling, projections or aspirations about the ballpark figures on job creation and supporting businesses.

Benny Higgins: We do not have those projections at the moment.

Paul Brewer: It is really important that our starting point does not put a huge short-term burden of expectation on the deployment of resources, because the bank's whole purpose is to take a long-term view. When the bank is subject to regular scrutiny from ministers and their teams, and the periodic independent scrutiny that is proposed, it is important that there will be real thought about the balanced set of measures that will be looked at.

For example, with regard to jobs, it would probably be seen as a success if the bank in its early days funded another unicorn, such as a Skyscanner, yet that would lead to relatively few jobs. It would be a big economic success, and it would help the sector in which it operates to have high prominence and pull people into new jobs, but it would not create a lot of new jobs in itself. If the bank supported a more effective approach to care of the elderly through its investment, that would probably be likely to involve a high number of jobs per pound invested, because that sector is very people intensive.

The measures against which the bank will have to be accountable will have to cover quite a wide spread. If you were to start out with an expectation in the early days of such targets as jobs created, incremental GDP that has been generated or taxes put into the economy by the companies that are operating, for example, it would be difficult to target in a way that would be constructive to the bank's mission for the first few years until you could see how it was delivering. On the other hand, you will have to have robust scrutiny to make sure that it is delivering.

Alan McFarlane: I will start with the annual report of SE and the Scottish investment bank, which I presume went through an auditor before it was published. It says that it invested £43.5 million in 2017-18 in 147 Scottish companies. This bank will have a run rate of £200 million per annum, so if we call it £50 million, that is roughly four times more. That is where the demand question will come in. Are the companies there? Patience will be a virtue. Based on the whole book, not that one year, SE claims that a £300 million portfolio—that is the only number that I can extract from its accounts that equates to asset value—led to turnover of £400 million, which would be a factor of 1.25. Therefore, if £2 billion went in and delivered 1.25, Scottish GDP would not be £175 billion but nearer £180 billion.

A significant proportion of that turnover was export, some of which would be export to the rest of the United Kingdom, which is 3,400 jobs. Therefore, SE's numbers suggest that £88,000 of investment generates a job. I do not know whether that was its investment or leveraged via others, but the baseline must be the existing effort. The working assumption is that more is better, but it must be targeted, a propos the demand point.

Angela Constance: Okay; I thank you for that.

Alan McFarlane: You can thank SE for that.

Angela Constance: I am all for us having the courage to take a long-term view, as long as we are setting our ambitions high enough.

My final question is about something that I am sure the panel is well aware of, which is the good solid business case for getting more women into business. The committee has had a ream of evidence made available to it that addressing the gender balance and the number of women-led companies could have a positive impact, such as adding £13 billion to our gross value added. In the initial thinking about the bank's strategic purpose, what consideration has been given to targeted endeavours that would see growth in the number of women who participate in business in Scotland?

10:30

Alan McFarlane: I think that that is just a given these days. It is the best people in the best jobs. There is no notion now that any candidate would be debarred from a job, let alone debarred from entrepreneurial backing, on the grounds of race, creed, colour or gender. I do not want to be dismissive—I completely agree with you—but much has been achieved and only more can be.

I am optimistic that some of the demand will come from all walks of Scotland's population. If you are suggesting that a key element of the mandate should be that that is taken as a given, that would be a good thing. I am not implying that that notion is redundant but, in my day-to-day life, I do not see those barriers in any way operating any more.

Angela Constance: Organisations such as Scottish Women in Business and Women's Enterprise Scotland are able to demonstrate that, quite often, women face a lot of additional barriers to accessing finance for their companies, and assumptions about the types of businesses that they lead. Do you think that, in order to increase the number of women in business, consideration should be given to having a strategic focus on women in business, bearing in mind that that should not just be about rebranding what has not already worked?

Alan McFarlane: Since that evidence exists, yes. We all work in different industries. Some are way more integrated than others and there may well be other areas that we wish were up with best practice. Since the evidence is clear, it would be great to put in the bank's mandate that it should be open to all. Openness in society is one of those things that we hold dear. It would be even greater if the outturn was that way.

If you look at the British Business Bank's reporting, it is very hot on that area—that is, who it invests with, its staff make-up and so on. All that I am trying to convey is that, in many parts of the economy, why would anyone deny themselves access to the very best talent?

Benny Higgins: I will pick up on that, to reinforce everything that Alan McFarlane has said. There will be a broader question of what ethical code the bank will pursue. As I have said a number of times already, we have the opportunity to use the bank as a catalyst to make a larger change than simply creating a greater supply of capital—that, in itself, is a good thing, but the bank is also a great opportunity for us to change things.

We will be setting out to make sure that the bank embraces diversity in its broadest sense. You need to remember that, apart from all the moral reasons for pursuing diversity, cognitive diversity makes institutions better. It is the right way forward—it has got to be—and we have to lay down some markers about how we want to go forward in Scotland.

Andy Wightman (Lothian) (Green): Before I ask about governance, I will follow up Gordon MacDonald's line of questioning on investment. It is my understanding that the capitalisation of the bank up until 2021 will be provided through financial transactions. The rules, which are set by HM Treasury, are that those transactions can be used only for the provision of loans or equity to the private sector. Paragraph 17 of the policy memorandum says:

> "The Bank will lend solely to the private sector. It will not lend to public institutions including local authorities, government agencies or arms-length bodies."

However, there is nothing in the bill to stop the bank doing that, and there are no rules on financial transactions beyond 2021. After that point, resources will be voted on by Parliament. I am just wondering where the statement that banks should lend only to the private sector comes from and whether you agree with it.

Alan McFarlane: To be honest, when we were asking ourselves what the bank should do, we decided that it was to make sure that the bank makes a difference. Therefore, we are trying to address the issues that do not get tackled either well enough or at all at the moment. There are two specific areas in that regard. One is ensuring that, where we can stimulate ambition, businesses can grow from being small and move to a path in which they can become much bigger companies. The other relates to what the bank's mission should be. We have an opportunity to invest in areas so that we have the hallmarks of an economy that can succeed in the 21st century. That is what we discovered during our implementation plan phase, and the bank's focus will be to invest in private companies that will participate in those ways.

Andy Wightman: I understand that that will be the bank's focus. There is nothing in the legislation to prevent it from making such investments. Is it correct to say that nothing on that point is proposed in the draft memorandum and articles either?

Benny Higgins: Yes.

Andy Wightman: For example, if, in two or three years' time, ministers were to set a mission on infrastructure and housing, it is self-evident that the public sector, co-operatives and mutuals would be well placed to deliver that. If it chose to do so, would the bank be in a position to lend for that purpose?

Benny Higgins: Yes, absolutely.

Andy Wightman: Are we clear on that?

Benny Higgins: Yes.

Andy Wightman: So there is no strict legislative prohibition, and such lending would not be ruled out.

Benny Higgins: Absolutely not.

Andy Wightman: That is helpful. Thank you.

Much of the provision on the bank's governance is set out in company law, which is overlaid by the statutory provisions in the bill. Parliament will also have a role. I want to ask about ownership. The bill makes it clear that ministers would be the only members of the bank. In Germany, for example, the Länder account for 20 per cent of the membership of that country's national development bank, KfW. Is there a role for other bits of government—particularly local government—in the national investment bank? Have you thought about that?

Benny Higgins: We considered different models. We believe that the best way to serve the Scottish economy in the long run is to have clear and unequivocal ownership by the Scottish Government. We looked at alternatives, but we concluded that that is the best model.

Andy Wightman: Can you supply us with more information on your evaluation?

Benny Higgins: We can probably come back to the committee on that; we can certainly look out some of the papers that we considered. However, we had extensive conversations about ownership models, and we judged that a bank that is 100 per cent owned by the Scottish Government is the right answer.

Andy Wightman: Okay. Thanks.

Alan McFarlane: The obvious difference is that some Länder have populations of upwards of 5 million: we must look at the economic unit in which the bank will operate. The structure in the UK now is that the British Business Bank can operate in Scotland—it already has on its website a number of examples of Scotland-based companies that it supports. Therefore, I think that diversity—I think that you were implying diversity not only in ownership, but in operation generally—is quite well served.

We must also remember that a lot of the angel investment in Scotland comes, in essence, through the public purse, through tax relief. Therefore, I am content that there is a huge amount of diversity in public sector involvement across the SME sector's activity in Scotland.

At this stage, an obvious suggestion might be that HIE, SE or others should have stakes. About 20 minutes ago, Benny Higgins commented on the benefits of focus: I consider that, for where we are now, those benefits outweigh the benefits of multiple ownership. I would never say never to multiple ownership, but today the argument is strongly in favour of a single point of ownership and contact.

Andy Wightman: I clarify that I was not suggesting multiple ownership or involvement of bodies such as Scottish Enterprise that are governed by Scottish ministers. My question was purely about local government.

Another part of the bank's governance would be the so-called advisory group. It has been discussed, but it will not be on a statutory footing—the bill says nothing about it. The Royal Society of Edinburgh has advised against giving the body a significant role, and others have questioned what role it might play and whether there might be a clash with the role of the bank's board. Will you elaborate on the thinking behind the proposal for an advisory board? If that board is to play a significant role, should it be set out in the bill?

Benny Higgins: I will start and my colleagues can perhaps join in. First, we must be very clear about the advisory group, and just take a step back. There will be a strategic framework, which I see as being an envelope within which the bank will operate; we seek to create an envelope that will allow the bank to be operationally independent. The bank will have a board and an executive team to pursue its aims within a risk appetite that would be set out in that envelope, but some reserved matters would go back to ministers.

The genesis of the advisory group was the belief—as we found when we talked to people—that it is important to have a voice that can advise ministers on the bank's operation and how it is pursuing its strategy.

However, we have to be very clear about this: if we want the institution to be a bank, we need bankers to run it—there is no alternative to that—and we have to make sure that they can operate independently within the envelope. An advisory board will have a voice to inform ministers, as the owners of the bank, but it will not inhibit the bank's day-to-day operation.

Paul Brewer: There are advisory boards that have been given quite significant power and say in organisations that have a public sector mission—for example, Network Rail and Welsh Water. However, when very diverse voices contribute to a body that has to make decisions, it can be difficult for the body to be an effective decision maker. Bodies sometimes find themselves being led by a chairman's view because they cannot get everyone else to agree.

Benny Higgins emphasised the importance of ministers hearing a diverse group of voices advising them on the bank, but if we wire that directly into decision making, or into supervision of decisions, it will be difficult to make things work at the practical level.

I will briefly come back to Mr Wightman's point about investment in public bodies. Wiser minds than mine on public sector finance will have to verify this, but I suspect that if the bank started investing directly in public sector bodies, that part of the budget would be scored in a different way and would, potentially, come out of capital resources and deplete the finance that would be available for other uses of those resources. The financial transactions budget, however, is clearly delineated for the private sector and is additional to the Government's other resources. It would therefore be possible that a body could end up in the same place as it would have been if the money had been put in directly by Government, rather than by the bank.

Andy Wightman: I will follow that up later. I am not sure whether the Scottish ministers have the power to provide financial transactions that are not backed by the Treasury.

Paul Brewer: No—

Andy Wightman: So, the money would be resource.

Paul Brewer: Yes—it would be resource money if it were put in directly.

Alan McFarlane: Benny Higgins has continued to be involved in the year since the implementation plan was published. I have not; I have had to go back and refresh everything.

There is clearly a role for an advisory board, but I argue that it should come much later and that it need not be there right up front. The Scottish national investment bank will use the same model as the Development Bank of Wales and the British Business Bank. Its board of directors will have all the responsibilities under the Companies Act 2006 that directors of any company would have. The annual audit will have to address solvency, whether it is a going concern and so on.

The bank will make losses for the first three or four years, so it will be imperative that there is an extremely close and confident relationship between the board of directors and the shareholders, who will be the Scottish ministers. To have an audience of fans baying for the manager to be sacked three games in would be the worst possible outcome.

It seems to me that the time to have an advisory board is once the bank is up and running, has established itself and has answered the very big questions that Benny Higgins addressed about some of the mission-led work. Despite having been involved in the plan, I would want to put in an advisory board further down the track, rather than at the start.

Let me underline this: the responsibilities of directors might have been abrogated in far too many British—nay, Scottish—companies in recent years, but they are serious and onerous obligations. Vesting the bank in the proposed structure brings many things, one of which is infinitely greater clarity about investment making and performance.

I will disagree slightly with the chairman again. I get the point about bankers, but the SNIB will not be a bank in the sense of being a body that borrows money. I argue that we need people with an investment focus—although people might say, "He would say that, given his background". A combination of credit evaluation for loans and investment capability is exactly what Scottish Development Finance Ltd had under the Scottish Development Agency, so the approach builds on past experience. That structure, with the obligations under the Companies Act 2006, provides powerful bulwarks to the Scottish Government in making investments; it is a different governance regime from that which currently exists through Scottish Enterprise and the SIB.

10:45

Andy Wightman: Finally, can Mr Higgins clarify that the proposed advisory group will advise ministers but not the bank?

Benny Higgins: The group will have a voice. I think that we have to be very careful about the word “advisory”.

Andy Wightman: Okay. We will set aside “advisory” and accept that the group will have a voice. However, is it the case that it will advise ministers, and not the bank?

Benny Higgins: The group will not advise the bank. That is the way I see it.

Andy Wightman: Right—

Benny Higgins: Can I just say something else? The strength and effectiveness of the institution will inevitably depend on the quality of the people who we get to be the chair, to be on the board and—especially—to take the senior executive positions. If we create an environment in which another board is meddling in decision making or strategic development, we will not get the right kind of people.

Andy Wightman: No one is suggesting that.

Benny Higgins: I know—I am just making that point. I accept Alan McFarlane’s point that the advisory group might not need to be there on day 1, but there is a need to respond to the desire of a broad church of people who would like to have a voice that ministers hear as they go through the strategic cycle. I also agree with Alan McFarlane that although this is not about traditional banking, we need people with investment and banking experience: we need to get the very best people who are committed to making a success of the SNIB.

The Convener: I do not want to spend a lot of time on this, but Alan McFarlane made a point about directors’ duties and so forth. I am not entirely persuaded by that argument. Is it possible for you to provide something in writing following the meeting to give us an idea of how you envisage all that working, in relation to the bank?

Alan McFarlane: If you do not mind, convener, I will not do that. I will just direct you to the Companies Act 2006 page, which is on the United Kingdom Government’s website, in respect of the duties of directors.

The Convener: I am fully aware of the duties of directors, but the question is how effective they will be in terms of what is being set up.

Alan McFarlane: That goes back to the point that was made about the calibre of the folks whom you want to have to implement the project. In a sense, the greatest power is resignation. They must be people who are independent minded to the maximum amount, who agree with the principles that are being promoted, who agree with the work and who take responsibility for carrying it forward. They will receive the mandate from Scottish ministers and then say “We’ll get on with this, but we’re accountable.”

All that we are hearing is that disclosure by public companies now is getting ever bigger: disclosure on gender equality, on economic and environmental impacts and on pay disparity. I presume, but I might be wrong, that the new entity will be expected to report on the companies in which it invests. The best standards of disclosure now are extremely high, so anyone taking on the responsibility of signing that Companies Act document to say, “I will sign the annual report and accounts of this organisation” is—I repeat—undertaking to adhere to a degree of transparency that I understand is not currently available through the accounting models that are applied to Scottish Enterprise and similar public bodies.

The Convener: All right. We will move on from that.

Jamie Halcro Johnston (Highlands and Islands) (Con): Is the panel confident or satisfied that the Scottish Government’s consultation on the investment bank included enough businesses of all sizes, and enough communities, individuals, trade unions and so on, in development of the bill? Have the key concerns that came up during that consultation been addressed?

Benny Higgins: The consultation was open—it was open to anybody to contribute. We had a very large number of contributions from a wide range of respondents. I am certainly satisfied that anyone who wanted to put forward an opinion or view, or to raise a concern, had the opportunity to do so. As I said, we have also been speaking informally to as many people as possible. I am delighted that there is very broad support for the bank across the political spectrum and the Scottish economy’s ecosystem.

Some issues were raised. There were questions about whether the bank will be big enough, and how we will operate pay policy—whether it will be within public sector pay policy, and how many people will be within that policy and how many will not be. It was asked whether there would be an ethical code and what the approach to missions would be. People wanted to know how many missions there would be and how we would develop more. Those are all legitimate questions that were asked within almost universally strong support for the bank.

Jamie Halcro Johnston: How have those areas of concern been addressed in the development process?

Benny Higgins: We continue to work on each of them, as we speak. An ethical code will be put together and we have started conversations on creating a pay policy.

We have already covered the question of scale. If more money was available to invest in the economy, it would be possible to go further, but I think that £2 billion strikes a decent balance between aspiration and impact. We are working our way through all the issues.

Jamie Halcro Johnston: Colleagues will follow up on ethical investment later on, so I will move on to another area. It was mentioned earlier that there had been engagement with HIE. How has the regional aspect been incorporated into the consultation and development process? Some regions of Scotland might feel that there is a focus on the central belt. Has that been taken into account? How can we ensure that the bank does not focus on the more traditional areas of investment and that Scotland's regions are included, too?

Benny Higgins: At this juncture, it is important to understand that, fundamentally, the project is about building the capability to do the right thing for the Scottish economy. In about a month, I will visit the HIE board to talk through what we are doing and what opportunities there will be for HIE. We think that it is really important that the bank should have the opportunity to participate in investments across Scotland, so the agenda outside the central belt will be important. We are not yet in a phase in which we are executing that change, but it is clear that it is an important part of what we have to do.

Jamie Halcro Johnston: Angela Constance touched on the role of women and the need to make sure that the structure of the bank is such that it provides opportunities for women. How can you ensure that other aspects of diversity—I am thinking, in particular, of young people, small business owners, ethnic minorities and the third sector—will, as well as having been involved in the consultation, be represented in the bank's future activities?

Benny Higgins: As Alan McFarlane, Paul Brewer and I said earlier, as we move forward, we have an important chance to make sure that all those areas get appropriate investment. We cannot imagine that the bank will solve every problem, but it will be a critically important additional piece of apparatus.

I come back to the point that the creation of the bank also provides an opportunity for us to ask how HIE, Scottish Enterprise, the new south of Scottish enterprise agency and Government departments can start to pull together in a different way to ensure that we tackle all the issues that have been mentioned.

The Deputy Convener (John Mason): As you will gather, the convener has had to leave to attend another committee meeting, so I will convene the meeting temporarily. As Angela Constance has already asked her questions, we will move on to Jackie Baillie.

Jackie Baillie (Dumbarton) (Lab): Evidence that has been given to the committee suggests that the mission approach will be complex to introduce and difficult to operate and evaluate. What is the panel's view on that?

Benny Higgins: I do not agree with whoever said that.

Jackie Baillie: It was not you, clearly.

Benny Higgins: No, it was not.

There is an argument for us not having very many missions at the start. This might not be the best analogy but, this time next year, we want to give birth to a bank that will develop over the decades ahead of us. There are tectonic shifts taking place in the world economy, and they must be reflected in how we manage the Scottish economy. Carbon neutrality, automation and demographic change are the obvious candidates.

We therefore need to create a process that allows the Government to understand where the mission focus for the bank should be. That mission focus will change over time, and, as I have said, there is an argument for not having too many missions. Carbon neutrality is a very obvious focus and I think that, as we go through the process of deciding which issues to focus on, that will be one of them.

We have to ensure that, with the investments that we make, we find refuge in simplicity, not complexity, and in doing the right thing. The other issues that I have mentioned will be strong candidates, too, alongside, for example, social housing, which is an important part of what needs to be done in the Scottish economy. In all the businesses that I have been part of, we have tried to find simplicity as far as possible; it is easy to have complexity, which can often be a refuge, because it can be a place to hide in. We must not hide in complexity—we have to make big decisions, get them right and move on with a clear strategic focus. It is in our own hands to keep all this simple.

Paul Brewer: You always start with complexity when you are trying to prioritise limited resources in areas where there is huge scope to deploy them, but the determining missions for the bank will be incredibly important from two dimensions. The first is their relevance to achieving the national performance outcomes that you are aiming for, and the second is their effect in that respect. I agree with Benny Higgins that deciding what to prioritise might be difficult, but if you start with too many missions, you will probably underachieve in all of them.

I remember the Green Investment Bank causing great frustration in its early days over the things that it was not investing in. It did not invest in green technologies, for example, and it was very focused on investing in projects that brought technology into reality. That was probably the right decision in light of the effect that the bank had. It made a very significant difference at scale to the flow of finance into offshore wind, whereas many of the technologies that it was being strongly encouraged to support were part of a great span, many of which succeeded and many of which did not, and if it had put resources into those technologies, it would have drawn off a huge amount of its capability. The national investment bank will have only limited resources, and it will be effective only if it prioritises where it places them.

Alan McFarlane: Investment is about choice, but there are a lot of competing options. One difficulty is that the term "mission" is undefined—by which I mean not in the bill but in wider life. We have no common grasp of what we mean by it. Certainly, as Benny Higgins has indicated, there are a few commonly agreed missions without the term "mission" having been agreed.

It is slightly naughty, but I think that the best way of approaching this is to think about what you do not want to do. If there were, say, still a coal mine in Scotland, and it wanted to expand, would SNIB invest in it? If Ineos got the chance to frack, would you fund a community organisation that wanted that to happen? Obviously, some of those questions answer themselves, but then there are the more ticklish issues, such as oil supply. If somebody in Scotland made the best vaping cigarette, would you invest in that? My experience of ethically based investing and working with clients from all religious and philosophical backgrounds on how such an approach might be implemented is that such questions are generally problematic but individually usually much easier to deal with.

The British Business Bank has a very good mission and, when we frame the missions in Scotland, we could take some of the ambitions such as having a less carbon-intensive economy and indicate how those two aspects might interact. However, this matter must be left to the bank's board and management to decide, because it will be their job to deal with the friction between optimism and the reality of what is available to be done and to turn that into wealth and job-generating businesses. It is the most patronising answer that I can give you, but it is absolutely true as far as day-to-day activity is concerned.

Jackie Baillie: So you would not put anything about the mission on the face of the bill, because you would want to retain the flexibility to deal with that over time. However, you have said that the whole thing needs to be owned by Parliament, too.

11:00

Alan McFarlane: It is a classic example of where the dialogue will occur through the annual report and accounts of the organisation, and the dialogue between its shareholder and the company that is created by those shares.

As Benny Higgins said, you start with one or two missions—all the consensus of all the consultation indicates that people are broadly behind that—and indicate how friction happens and where tension occurs between the Government will and the practice of the bank in its day-to-day investments. I am a great believer that friction creates heat but also light, and that that is the way to go forward.

You can start with, "If I ruled the world, it would be great if all this happened," but we both know that it is not like that. Nonetheless, it would be appalling not to have high ambition at the outset. The question is how much ambition in what form, and how it hits the road between the board of directors, the executive and the shareholder.

Jackie Baillie: Let me continue with the theme of ambition. In my head, that is certainly about how the Government ensures that what happens is legitimate and delivers societal value, which is one of the objectives.

I have always believed that assessing social costs and benefits is very much at the heart of economic appraisal. If we consider how that appraisal is currently done for a particular project, for example, we would assess net present value against Her Majesty's Treasury's green book. What approach will you take to assessing societal value?

Benny Higgins: We are still to agree precisely how we do that. We recognise that it is an important part of what the bank is being created to achieve. It is work in progress.

Jackie Baillie: But that is key to realising whether this additionality works for the economy of Scotland.

Benny Higgins: It is essential, yes.

Jackie Baillie: But you have not yet done anything with it.

Benny Higgins: We have the national performance framework, which is a very important starting point. We have to address how we measure the bank's progress against that national performance framework.

Jackie Baillie: Has the green book approach featured in any of the discussions or debate?

Benny Higgins: It has been part of the conversation. However, the national performance framework is the output that we are trying to achieve. We have a national performance framework for a reason. I say very apolitically that I think that it is very progressive.

Jackie Baillie: We also have the green book for a very good reason, which has been there for while and has been updated.

Benny Higgins: It is not being ignored.

Jackie Baillie: You say that it is not being ignored—I would appreciate evidence as to how it is being considered. I do not know whether Alan McFarlane or Paul Brewer has anything to add.

Alan McFarlane: I have nothing to add. Benny Higgins has been carrying the ball. However, I can say that the topic came up in relation to wider impact and wider discussion. Forgive me, but I would put the question back to you: are you content with the SIB's current reporting? Would you like more?

Jackie Baillie: Indeed.

Alan McFarlane: If that is the baseline, start with what you have and make it better.

Jackie Baillie: We have—

The Deputy Convener: A couple of people want to come in with supplementary questions. Do you want to continue?

Jackie Baillie: No, it is fine. I will let people come in with supplementary questions.

The Deputy Convener: I will let you come back in if we have time.

Andy Wightman: As we are scrutinising the bill, I am curious about how section 2 specifies that the bank's objects are set out in legislation and shall be subject to resolution of Parliament, meaning that Parliament has to sign off on the objects of the company. However, in section 11, there is no such role for Parliament to approve the strategic missions, which will simply be laid before Parliament.

Alan McFarlane: Do you mean in the bill itself?

Andy Wightman: Yes. Given the potential significance of the strategic missions, should ministers also have to seek a resolution of Parliament to approve those, or is there a good reason for not providing for that?

Benny Higgins: We have to be careful not to assume that the three of us who are sitting here—not even me, who has been the strategic adviser to the project—are experts on the positioning of the bill. Others are probably better qualified to talk about how the bill was put together precisely the way it was. However, it has been put together to ensure that it gives the opportunity for the smoothest and strongest governance and running of the bank. As Andy Wightman said, it would be up to ministers to choose the missions; that is the way the bill has been proposed.

Andy Wightman: Do you have a view on whether Parliament should approve those missions?

Benny Higgins: I agree with the bill as proposed. I think that we could overintellectualise it by having to go through a parliamentary process to address the missions. There are big obvious missions that we need to pursue in this country. Alan McFarlane rightly said that the expression may not be very well—or uniquely—defined. However, we know that we have to aim for carbon neutrality and respond to the other issues that we talked about earlier.

Andy Wightman: You say that we need to do that, but there are different views on what we need to do. A resolution of Parliament is not a complex parliamentary procedure; it is merely a resolution that is debated and voted on. It is not like the procedures today; it is not legislative.

The objects in section 2 are subject to resolution. One would not anticipate the objects—however they end up—changing often, if at all. That is fair enough. The mission will be more flexible, and will be reviewed. Are you clear that that should not be subject to the same process?

Benny Higgins: I have no decision-making power.

Andy Wightman: I am asking for your view.

Benny Higgins: I am expressing my opinion that this makes perfect sense.

Andy Wightman: That is fine.

Alan McFarlane: Paragraph 11 of the financial memorandum, which is what I thought that Mr Wightman was talking about, although I now know that he is not, refers to the "mission-based approach" and highlights the vastness of the aim, which is

"to support transformational change across a number of 'grand' socio-economic challenges" that we can agree exist, although I take the point that we may disagree about how to address them. The financial memorandum then states:

> "It is envisioned that the Bank will respond to these missions through its Investment Strategy."

That is my point about the friction. The wish is expressed, and the means are in part willed in the creation of the bank. The means must respond with what they can achieve.

Andy Wightman: No, my question—

The Deputy Convener: We have another supplementary. Is that a final point?

Andy Wightman: That is fine.

Dean Lockhart: I want to move from the macro to the micro, from the mission investments to investments in private sector business. Will investments in individual companies be purely merit based, or will the bank also have a regional allocation for investment to make sure that each region gets a roughly pro rata share?

Benny Higgins: At the moment, the assumption is that investments will be merit based, but we will have to make sure that we pay due attention to stimulating the right kind of demand across the country. There is no desire for the bank simply to serve the central belt, as was suggested earlier. It will be critical to monitor the levels of investment that are being made in the different regions in Scotland. At this juncture, we are not trying to force feed certain regions. We are encouraging the right kind of demand and feeding that demand.

Dean Lockhart: Will a return on investment or a hurdle target be established early on to make sure that investments are creative?

Benny Higgins: Yes. For the avoidance of doubt, the bank is being set up to make a return on capital. We have not yet set out the precise numbers associated with that and we have to take into account also the comments made about societal benefit, but the intention is that the bank will make a return on capital. Some of the issues relating to long-term patient capital will be interesting—in some examples, there will not be an existing market with which to make comparisons on returns. Setting out precisely what the returns need to be is work in progress.

Alan McFarlane: The British Business Bank uses clear numbers for its expected returns, which are from the British Venture Capital Association. I want to underline that the bill makes it crystal clear that it is expected that the organisation will not be cash neutral in costs until 2023. There will be red ink spilled in its annual reports and accounts every year until 2023. That is why I said at the beginning that, if you want long-term patient capital, you have to have long-term patient investors.

Paul Brewer: I want to underline that point, which comes back to the gap that we talked about. A lot of venture capital and private equity investors have time horizons on their funds. They have investors standing behind them who want to see a return in five to seven years, sometimes to the point at which a fund has a hard-closed end date and has to realise its investments in that timescale. In the ROI that is set, it is very important that the national investment bank does not have those time pressures, because that would influence investment behaviour in ways that would work against the outcomes sought.

The Deputy Convener: I have a few questions, which will be the final ones. How distinct are the missions? Is it possible that they overlap with one another? The German investment bank has a couple of missions—climate change and the environment, and globalisation and technical progress. I see those as potentially overlapping quite a lot. Do you see the missions as distinct, so that this bit of money will go to this mission and that bit of money will go to that mission, or is it about looking at all the missions and seeing whether the investment fits a number of them?

Benny Higgins: We should not set out to make hard-and-fast rules about that. The point is that the missions are the direction of travel to make sure that we do the right things in the economy. I mentioned earlier that we have been in dialogue with other national investment banks. We must be careful not to try and be like any one of them in particular, because the bank must be bespoke for our needs in Scotland. In particular, KfW is an interesting case study, but it has been around since after the second world war. It is a huge institution and it is probably not the best place for us to look for most of our learnings. There are better comparisons in other, similarly small, advanced economic nations.

It is inevitable that there will be examples of investments that we make that serve different missions, such as a crossover between carbon neutrality and automation. However, the purpose of the missions is to give us guide rails to allow the investment strategy to unfold within the operationally independent bank.

Paul Brewer: On that subject, the bank's resources come in two forms: one is the capital and the other is the people. We absolutely need people who have the knowledge, experience and capability to have an impact through investing in the missions. I cannot anticipate what the bank will do, but I would be surprised if it makes hard allocations of capital between the missions, because it is about getting the maximum overall outcome. However, the people who bring the expertise to the missions will all speak to one another and, although the missions might overlap, I suspect that overlapping investment is unlikely to be an issue.

John Mason (Glasgow Shettleston) (SNP): Now that the convener has returned, I will continue. Another word that has been used is “ethical”. That has been mentioned already this morning. The thought is that the bank will invest in an ethical way. However, the word “ethical” is difficult; at least, let us say that people understand different things by it. What do you understand by the bank investing in an ethical way?

Alan McFarlane: A good place to start is the principles for responsible investment, which the United Nations has promulgated across the investment industry. Those principles fit in with the UN sustainable development goals, which I am sure are very familiar to committee members. Then there are the ethics of upholding the law and the questions about openness and society.

To answer your earlier question, it is not possible to have a bank where there is a silo of carbon neutral, a silo of this and a silo of that. It ties in with the shareholder and client making clear the outcomes that they desire and saying, “Evidence your path towards those and evidence the manner in which you are conducting yourself.”

The classic example is that some religious traditions prohibit interest but others do not. Different religious traditions have different attitudes towards some health products. Investment people are familiar with dealing with the client’s mandate. If the Scottish ministers can say that the UN sustainable development goals are a really good, broad framework, plus some other things, that will help a lot to guide the board of the institution as to how to conduct itself.

John Mason: However, you can imagine someone standing up in Parliament and saying that the bank is claiming to be ethical but a particular decision is not ethical. Is the answer just that it will be reviewed at the end of the year?

Alan McFarlane: It is unanswerable, because we are dealing with axiomatic assumptions about ethics, not an investment question.

Benny Higgins: We will document an ethical code for the bank, so that will be documented. That will not prevent arguments about whether that code has been followed.

John Mason: That might be a topic that we will come back to. I will leave it for now.

To wrap up on some practical questions, one or two people have suggested that we have quite a tight timetable to get the legislation passed, get things into effect and get the board in place. Do you have feelings about that? Are you relaxed about where we are?

Benny Higgins: When I speak to all my colleagues who are involved in the project, there is an awareness that it is a tight timetable, but there is also a degree of confidence that we can push through. The first vote will be scheduled for September, the second will probably be in November and the final vote will be in March. In parallel with that voting schedule, state aid consideration will be going through. It is independent but not unrelated, so we are reasonably confident that the bill will get to royal assent by this time next year.

In parallel, we must build a bank, not just get a bill through. We must get the people involved and the business set up. We are going through detailed design authority meetings. The process of looking for a chair is just about to kick off. Finding a chair will unfold into finding the rest of the board, a chief executive and other senior executives. I do not take it for granted that that will be a straightforward process. Let us say that I am hopeful that, if we get going now, we can follow through and get it done in the schedule to which I have just referred. It is not easy. There are some unknowns. My concern is more about getting the right people, because the organisation or institution will ultimately be as good as the people who run it.

John Mason: Thank you very much.

The Convener (Gordon Lindhurst): Thank you very much to all our panel for coming in today. I will now suspend the session to allow for a change of witnesses.

11:16

Meeting suspended.

11:22

On resuming—

The Convener: We move to the second panel on the Scottish National Investment Bank Bill. I ask members to declare any interests that they may have.

Angela Constance: In the interests of transparency, I declare that I am in the process of joining the board of Common Weal. It is a non-financial interest, but given that one of the witnesses is from that organisation, I thought that I should declare it.

The Convener: Thank you. I welcome Robin McAlpine, director of Common Weal; Eilidh Dickson, policy and parliamentary manager at Engender; and Ray Perman, who is a fellow of the Royal Society of Edinburgh.

The rationale of the bank is to improve Scotland’s innovation performance and to enhance the access of small and medium-sized enterprises to finance. What do the panel members think of that rationale? Also, are they satisfied with the objectives of the bank, as set out in section 2 of the bill?

Robin McAlpine (Common Weal): We are happy with the bill. This project has been close to our hearts for a long time and we have been following it closely. I feel confident about how it has been taken forward.

The most important thing for me is that we avoid looking at it too much from the producer side. For example, the objectives are useful in outlining what the bank is going to do, but it must be demand led and we must encourage people to come forward. The objectives are broadly right; we just have to make sure that there is sufficient demand in Scotland to meet them. That is partly about signalling that the objectives are what the bank is looking to support.

All the way through, I have been quite clear that missions will change and adapt and must be interpreted openly as we go along. I would have liked to see a little more emphasis on lending to the public sector, assisting the finance of public infrastructure and working with local authorities, housing associations and others. In a couple of places, the current wording of the bill implies slightly more than I would have liked that the bank will be just an SME bank.

However, broadly, we are happy with the bill. As I said, the key thing is about stimulating demand, being helpful and flexible and developing the right suite of lending to ensure that demand comes forward and that it signals the kind of projects and work that we hope people will come forward with.

Eilidh Dickson (Engender): We are slightly more concerned about the objects that are listed in the bill, not necessarily because there is anything wrong with them but because they focus primarily on the core economic aspects of the bank rather than the social wellbeing and environmental impact that the bank is supposed to have. The bank is supposed to be about doing something different and releasing untapped potential, but that does not translate into the objects as they are currently listed. We believe that, without an equality and non-discrimination objective, there will be no radical change in the way that things are currently done in the economic development field.

Ray Perman (Royal Society of Edinburgh): Our position is set out in our written submission. We are broadly supportive of the bank's objectives. We think that they should be clear. We disagree with Robin McAlpine on investment in infrastructure, because a decision was taken early on not to incorporate the Scottish Futures Trust, which deals with infrastructure, into the bank, so there should be a clear division between the two. The bank will not do any lending—although it is called a bank, it is an investor rather than a bank.

Broadly, we think that the objectives are clear, although we have reservations about the mission-led side of things. I agree with the point that Alan McFarlane made in the previous evidence session that the bank should start off with a single simple mission and maybe build on that later, rather than start with a weight of expectation that might be difficult to meet.

Dean Lockhart: I asked this question of the previous panel. We have had previous policies and initiatives from the Scottish Government to supply capital and finance to the Scottish economy but, as Robin McAlpine referred to, there has not been sufficient demand. The previous witnesses seemed to think that the bank can play a role in increasing demand, but I am not entirely convinced by that, because the bank will not originate or go out and find business; its job is to supply money to business that is found by other agencies. Overall, how can we stimulate demand for finance? How can other agencies deliver businesses to the bank so that the bank can finance them?

Ray Perman: You are absolutely right that, as Benny Higgins alluded to, the bank will not originate deals and will therefore have to work closely with those agencies and private sector bodies such as the commercial banks to bring people forward and stimulate demand to take up the capital. It is important that the bank makes links between the existing economic agencies and other stakeholders at the beginning.

I will give an example from the UK. I was chair of an advisory group to the department for business in London for eight years. In 2005, we set up an organisation called Capital for Enterprise to do the sort of things that the British Business Bank does now. Capital for Enterprise did not have a particularly grab-me name. It had a pretty high profile in the investment industry but, generally, among companies, it was an unknown quantity. Merely renaming it with a much clearer name as the British Business Bank—although the bank has now expanded its activities—gave it visibility, which was important. Just the publicity around renaming what is currently the Scottish Investment Bank as the Scottish national investment bank and then building on that foundation to expand it could have a positive effect.

11:30

Eilidh Dickson: I agree that there is some work to be done on awareness raising. There will be a role for the precursor funds in that regard.

I disagree that we should be looking at and building on what we already have, because the current structure of economic development in Scotland does not reach everybody. Ms Constance already referenced the potential GVA of women's businesses in Scotland, and we know that that will not necessarily come from sectors that are prioritised in the Scottish Government's economic growth strategy.

It also has to be about looking at other sectors, other ways of doing it and other types of business, and dismantling some of the additional barriers that are in place for people who are looking to access finance but who might not have a traditional business. They might be working in childcare or the care sector in a business without a huge amount of growth potential, so they might be discouraged even from seeking funding in the first place from the private and public actors that already exist.

Robin McAlpine: Early on, we were driven to develop the proposals through conversations with a lot of small and medium-sized businesses. One of the things that we came across again and again was that they were scared of banks—that may or may not be fair, but I think that there is a lot of fairness there—and saw them as predatory. It was a period in which a lot of small businesses had come out the wrong side of lending arrangements with banks. On top of that, we talked to other businesses that, in my eyes, had viable business proposals, but the lending horizons—the terms on which or periods for which the banks were willing to lend—were not conducive to encouraging those businesses to come forward.

It will be important to say, "This bank's sole purpose is to support you—it is not a profit-generating bank and we are not going to extract profit. Our only purpose in existing is to help your business grow and become better, and to be long-term partners with you." Simply sending out that message will have a positive effect on a lot of businesses that are nervous about bank borrowing and are not coming forward for that reason. Those concerns are probably even stronger in the social enterprise and co-operatives sectors, which we should want to grow substantially in Scotland.

An important factor with regard to there being a fund here or a grant or pocket of money there is that the bank should be here in 100 years. It should become to Scotland what Germany's national investment banks have become, which is a fundamental, permanent part of the German economy that people assume will always be there to support long-term development activity. As well as getting lending terms right, creating the right lending horizons for small businesses and making all those things work, the message that that is how we want the bank to work will build demand.

I genuinely believe that to be the case. We are already talking to people in small businesses and telling them that the bank and its opportunities are coming, and people are showing an interest. One of the most important things that the bank can say is that it will be a place where people can build their business over time, that it can be trusted, that it will work with businesses as a partner and that people should look again at ideas that they had in the past and were perhaps nervous to develop. That is the first and most important thing that the bank can do.

Dean Lockhart: We heard evidence from the previous panel that the bank's investment policy will be merit based—that investment will be made on an individual, case-by-case basis and that there will not be pro rata distribution of investment around Scotland's regions. Is that the right approach?

Ray Perman: It is absolutely the right approach. There is a danger in pro rata allocation. We saw that in the UK with the regional venture capital funds that were set up in the early 2000s along the lines that you suggest—that is, regions were given an allocation of money. Some regions ran out of money—they had more demand than supply—while other regions had a shortfall in demand. In one case—I think that it was the south-west of England—the costs of administering the fund were greater than the amount invested. The National Audit Office produced a coruscating report on the running of those funds.

The money should be held centrally, but it should go where the demand is. Stimulating demand in areas that have not traditionally come forward with investment propositions is a very important job, and it should be done, but just to arbitrarily allocate the money in advance of seeing the demand will, I think, be counterproductive.

Robin McAlpine: I agree. A theme that I will probably mention a couple of times is the bank sometimes being seen as a one-stop shop for fixing everything, when it will just be a source of funding. As such, it should be giving the right kinds of packages to the right kinds of projects. It will not invent or direct the projects, and it will not travel around the country saying, "We're going to invest here." It has to be demand driven. Getting different regions of Scotland to increase the demand pool is a different task, and it is a task for local authorities and the local arms of Scottish Enterprise.

As for lending, I accept that it is one thing at a time and that this will not happen quite yet, but we really do not want small businesses largely borrowing from a central bank in the centre of the town. We need a local banking network that creates the kind of support that small businesses need. If you are a hairdresser, you will need to cash up and therefore you will need a relationship with a good banking network. We would argue that we should not assume that every microbusiness will go to the Scottish national investment bank for lending purposes and that we could do with a better local banking network. We will be coming forward with proposals for a mutual or public local banking network not only to sustain banking services in the communities in Scotland that are losing such services but for the sole purpose of making it clear that having a long-term relationship with a nearby bank is the best solution for a lot of small businesses. The national investment bank can play a very important role in supporting and capitalising, but it cannot do everything.

I absolutely agree that Scotland has a problem with differentials of investment in different regions—indeed, I see that everywhere I go—and it is important for the bank to monitor in regional terms where its investment goes. However, it must be driven by demand, and if there is demand failure in a region—if people there are just not coming forward—that needs to be addressed by the rest of the public agencies that are supposed to be working in economic development. The bank has to lend on the basis of the business cases that are brought to it, and if they do not come, that will not be a failure on the part of the bank.

Eilidh Dickson: We do not have a position on whether the bank should take a regional approach, but one question that we would ask is: how will merit be assessed?

Gordon MacDonald: Before I ask my own questions, I want to go back to demand. The RSE's 2014 report "The Supply of Growth Capital for Emerging High-Potential Companies in Scotland" says:

"Banking regulations have introduced more stringent risk criteria

and

"reduced access for small companies to conventional overdraft or term lending arrangements",

which have

"had a significant effect on the capitalisation of early-stage companies."

As a result,

"Growth aspirations have had to"

depend on

"equity investment."

Is that the gap that the Scottish national investment bank is trying to fill? Are the criteria that were highlighted back in 2014 still applicable today, and, if so, are they suppressing demand?

Ray Perman: I think that the criteria are still applicable, and I do not think that the position has eased any. I imagine that that will be one of the gaps that the national investment bank will try to fill.

I should emphasise that the SNIB will generally be an investment bank that will make equity investments. It might do some lending; Scottish Enterprise and the Scottish Investment Bank invest a small amount in lending rather than in equity investment or long-term patient capital. I imagine that the vast bulk of the money invested by the national investment bank will be equity and patient capital; it will not be lending in cases where the lender needs to get the money back, and sometimes quite quickly. It will be patient capital.

Robin McAlpine: It is in relation to exactly those kinds of gaps and barriers in parts of the lending or equity environment where there are problems. We have been working on this for five years now, and we are quite excited by and have quite a clear idea in our heads about the projects that might come forward. What I have found really encouraging is that we keep talking about projects that we did not think would come forward, and I expect to see quite an interesting and diverse range of projects and enterprises.

I think that some of the barriers can be addressed. I will give another example. We talked to a company that was looking to expand. It so happened that its bank had just pulled out of investments in retail properties—the bank had been burned on a couple of things and because it had been stung too much by overpriced commercial property investments, it made a blanket decision not to invest in such properties. The company was looking at a property and had a very strong business case, but the bank, which was a big bank, said that it was not investing in that category at the time, so the company could not get the lending.

What was the company to do? Would it close its account and go to another bank or would it just not bother with the property? There is a wide range of barriers to people coming forward. A lot of it is to do with confidence; other issues involve straightforward strategic decisions by commercial banks at any given moment. There is a range of reasons why there is potential that does not come forward and look for the investment that will help it to grow.

I still come across such examples. We keep coming up against people who say that they did not do something because such issues. That surprises us, because we would have thought that they would have come forward to get lending. However, there are genuine barriers. I do not think that the committee will talk to a lot of medium-sized enterprises that say that everything about their equity and lending environment is exactly as they would like. The bank will be part of completing that jigsaw.

Gordon MacDonald: What impact do you hope the £2 billion investment over 10 years will have on the Scottish economy?

Robin McAlpine: We would like the investment to be substantially larger. One of the reasons why it is important that it is not just an SME lending bank is that SME lending is quite risky—SMEs across portfolios are quite risky. As far as I am concerned, we should first move as quickly as possible to ensure that the bank's lending is not counted against Scotland's public sector borrowing requirement, and we need Treasury dispensation for that. As soon as that happens, we can start to leverage additional capital—for example, from pension funds. I would like to see the bank aiming to have a loan or equity book that involves perhaps 70 per cent going to housing and public sector infrastructure, which are really safe, solid and profitable investments. That would mean that it can take much more of a chance with the 30 per cent that is SME lending.

Even if we get it right, £2 billion over 10 years is not transformative for an economy such as Scotland's. It should be more than that, but you have to start somewhere. We have been working closely with the team that is developing the bank, and I think that they are right in saying that, as a nation, the first thing that we need to do is demonstrate that there is genuine demand. I hope that we can then go to the Treasury and ask for dispensation, which will enable the bank to capitalise more fully and effectively. We will be able to do that if we have evidence that there is demand and that Scotland has an economy that is capable of absorbing that kind of advanced investment.

Everything has to start somewhere and £2 billion is a good starting point, but we are much more ambitious for the bank's future than that. We think that there is very large scope to bring in pension funds and a number of other investors, and once you do that you are looking at a scale of 10 times-plus what the bank can lend. When we get there, Scotland will start to have a bank that is changing the economy fundamentally.

Eilidh Dickson: We have taken no position on whether the £2 billion is sufficient. More important for women and for gender equality more generally is how and where that £2 billion is utilised. In the past, the committee has recommended that spend on care and childcare should be designated as part of infrastructure spend. That would have a long-term enabling effect on women's economic participation, as well as being of direct benefit, given their current high prevalence in those industries and their take-home pay. For us, it is not so much about how much investment is made as about where and how investment is made, taking the long-term, wide view on freeing up participation in other parts of the market that you are not necessarily looking at.

Ray Perman: The bank has the capacity to make a substantial difference to the Scottish economy, and not only in new company formation—we do pretty well in Scotland at starting new companies but, as our colleague Benny Higgins said earlier, we have done less well in growing companies to a reasonable size and, importantly, keeping ownership and decision making in Scotland. Part of the reason for that—but not the whole reason—is to do with access to finance. The Scottish national investment bank will most commonly invest alongside the private sector as a co-investor. It will catalyse a lot of private sector funds so that it can make an impact that will be much bigger than the amount of money that the Government puts into it.

11:45

Gordon MacDonald: I raised the question of operating costs with the earlier panel. The RSE has raised a question over the £25 million, which is the mid-point. What are the RSE's views on that and how does it justify its criticism?

Ray Perman: We came to that conclusion for a couple of reasons, one of which is purely arithmetic. The bank will have about 100 people and £25 million is £250,000 per person, which seems a very high figure to us. In comparison, the operating costs of the British Business Bank are about 50 per cent higher for a bank that is over twice the size of the proposed bank. The £25 million therefore seemed to be a very high expectation of costs for the proposed bank. In particular, what stood out is the sponsoring department; the implementation plan says that it will have 40 people from the civil service, not from within the bank, with a cost of £4 million a year. That seemed rather excessive for monitoring a bank that will have only 100 people.

Gordon MacDonald: What level of rate of return would the bank require in order to cover its costs?

Ray Perman: I have not done the arithmetic, but I think that the British Business Bank has a target rate of return for its cost of capital of 2.5 per cent or perhaps a bit less and has achieved just more than that. On the rate of return for the Scottish national investment bank, it would be a good discipline in the long term to at least cover its running costs and its cost of capital, but it should not look to earn a commercial rate of return.

Taking the British Business Bank as a model, it invests alongside the private sector at the same level of risk; that is, if an investment fails, both the private sector and the public sector take the same hit, and the public sector does not take more of a loss than the private sector. That lesson was learned from very early investments by the UK Government.

For successful investments, the British Business Bank would expect to earn a return that covers its costs and its cost of capital, but it allows the private sector to make an enhanced return. It therefore cedes part of its commercial return to the private sector as an investment to bring more private sector funds into the total investment of the British Business Bank.

I imagine that the Scottish national investment bank would want to look at a similar framework, although it might not be exactly the same. However, in the long term—I think that Alan McFarlane said that the expectation was that it would be 2023 before the bank would break even—the bank should look to cover its costs and its cost of capital. Being a patient investor means not maximising the return from investments.

Gordon MacDonald: You said that the Scottish national investment bank should model itself largely on the British Business Bank. That bank has substantially increased its rate of return in recent years. Over the past four years, its rate of return has been an average 3 per cent, but in 2017-18 it was 4.7 per cent and in 2016-17 it was 4.1 per cent. Taking the average of 3 per cent, I calculate that by 2023 the Scottish national investment bank's costs would be covered.

Ray Perman: I do not think that you can go on individual year figures, because there might have been—

Gordon MacDonald: That is why I am taking the average of 3 per cent over four years.

Ray Perman: However, the two figures that you gave for the higher return may have been impacted by the fact that those particularly successful investments were sold that year. Other years may have a lower rate of return because there were not successful investments in that year.

Taking a longer-term view, the bank should aim to cover its cost of capital and its running costs but not to make an enhanced return, or it would not fulfil the expectations about taking risk or putting capital into areas that are currently undercapitalised.

Andy Wightman: I want to follow up Ray Perman's point about loans. The bill makes it clear that the bank will be empowered to provide loans, but the question of how much the bank should make loans as opposed to investment is not covered anywhere. Your response to the first question about not making loans was your view, in effect, but do we have any indication of what is expected?

Ray Perman: Making loans is an expensive business if it is done on a micro scale, because the loans need to be processed and monitored and the money needs to be got back. I do not think that the bank will be set up to do that on any big scale. It cannot compete with the commercial banks and should not do so. I wholly take Robin McAlpine's point that commercial banks have not done themselves any favours by how they have behaved, particularly towards small businesses, and in their activities generally over the past 10 or 20 years. However, expecting the Scottish national investment bank to replace bank lending is unrealistic.

The bank could make a difference in specific areas of lending in which there is deficiency at the moment. I have given the example of the Scottish growth fund, which is essentially a mezzanine fund—it makes loans, but in specific cases for growing companies. That has been quite successful and the Scottish national investment bank might want to build on that example.

Robin McAlpine: May I come in on that point? The world is filled with countries that have large mutual banking networks—the hard private commercial banking model in the UK has done nothing but create risk and massive profits and all sorts of problems. It was said that the banks have not done themselves any favours; some of the commercial banks have acted criminally in the past 15 years.

It is important to have a sense of scale. The bank will not transfer everything straight away. It will have £2 billion over 10 years, which will not change everything. I emphasise that this is the first step in creating an institution that should exist for many generations, as far as I am concerned. We should be more open minded about where it will go to; we may have a quite different lending framework in the future.

On the point about equity versus loans, I agree that microbusinesses and even most small businesses benefit from being near their banking and being close to people. One of the biggest failures in the banking network is the breaking of the long-term relationship between small businesses and the lending managers by a lot of banks. Those supportive and positive relationships helped small businesses to grow, but they are losing trust because of what they have read about how the banks operate.

The first thing to say is that the Scottish national investment bank is a bank, and it must operate like a commercial bank—I have said this over and over. If it starts to subsidise loan rates to below something that looks broadly like a fair market, it will get into trouble with European Union competition laws, so it cannot heavily subsidise interest rates to increase or decrease rates of return.

However, the bank could create a suite of lending and equity investment packages that are tailored to the demand that comes forward. For example, a housing association or a small community housing project might wish to borrow—if it can—mortgage style over 30 years; it would find that quite difficult to do with the existing commercial banks. We have modelled that costing; the Scottish national investment bank could lend over 30 years at rates that would comfortably come in under European competition rule problems but would enable mass public rental house building in Scotland, not by subsiding but by offering different forms of loans.

The bank could give other kinds of loan—there are examples—when it thought that, for example, a medium-sized business had a solid business proposal. If it recognised that the business's investment was to be heavy and the time that it would take for the business to grow such that it got the returns might be a little longer, the bank could provide a phased package in which loan repayments started a bit lower and climbed over the relationship period.

On gender, the bank might very well give weight to certain public goods—for example, if it wanted more enterprises to be led by women. It might give a slight weighting to enterprises that did certain things that were particularly good for the economy. However, the loans must be commercial and the behaviour must still be roughly in line with the broad market.

The most important thing will be that the bank listens incredibly carefully to its customers and potential customers. It must arrange its lending or its equity into packages that are best suited to the enterprises and projects that it lends to. Once it does that, it will compete not by being cheaper but by being better and more aligned to the businesses' needs. The bank should be intended to maximise not profit but development; that is where the value will come from.

Andy Wightman: Robin McAlpine touched on a point that I raised with the previous panel. Benny Higgins made it clear that the bank will not be prohibited from lending to the public sector, but it is not expected to do so. That view is probably predicated on the idea of lending to existing public organisations, such as local authorities. However, there are state-owned enterprises, such as Sweden's Vattenfall, that have been around for 100 years, so the idea that we will not fund enterprises that are designed to transform the energy system, for example, just because of the ownership model seems strange. In the private sector, we have one of the biggest forms of patient capital—pension funds, which play a huge role in investing in housing across Europe. What are the panel's views on the scope for and role of the bank to invest in public-led enterprise?

Robin McAlpine: I reiterate that there is a big opportunity. The public sector is a reliable and stable repayer of its loans. I promise that I am not applying to run a bank but, if I did, one of the first things that I would look at is the enormous scope for patient lending to public house building in Scotland. I repeat that we have costed that; with borrowing over 30 years, high-specification houses could be built and rented at below market rates, without public subsidy.

The big gap in public house building for rental is that we still have to subsidise every house, because nobody does mortgage-style lending for large public sector housing developments. If that is not a mission that Scotland should be cracking on with, I do not know what is. I genuinely do not know why anybody would be dogmatic about who the bank was lending to. If someone had a proposal to transform Scotland in the way that was wanted, why would the bank not lend to them?

Ray Perman: I have no problem with the Scottish national investment bank lending to public sector organisations if the proposition is good.

Andy Wightman: The RSE's submission expresses concern about the proposed advisory group's role, which I discussed with the previous panel. The RSE's concern is that the group will interfere inappropriately with the bank's workings, but it is expected to be an advisory panel for ministers. The policy memorandum makes it clear that the advisory group's chair is intended to be a non-executive member of the board. The RSE drew our attention to its consultation responses in 2017 and 2018, which I have not read, but will you elaborate on your position?

Ray Perman: We raise two problems. One is efficiency—Benny Higgins went into detail about the fact that having two people interfering in the running of the bank will not be an efficient way to run it.

Our larger concern is about accountability. What will be the chain of accountability if there is an advisory group and the bank's board—both of which will contain at least one common person—as well as the minister and the bank's executive? The chain of responsibility should go from the executive, through the board, to the shareholders, in the shape of the minister. That should be clear so that we know where responsibility and accountability lie. It will blur things if an advisory group is advising the minister, and one member of that group is also a member of the board.

12:00

Andy Wightman: I accept that, for the sake of argument, that is probably not a good idea. Earlier, Benny Higgins mentioned missions in relation to carbon neutrality—which is an obvious area—automation, demographics and social housing. If you were the Scottish ministers and had to decide for yourselves, given that the bill does not provide for Parliament having any role in approving any missions, would you not see an advisory group having a role in advising ministers on how they should frame their mission instructions?

Ray Perman: That would be entirely for the minister to decide. If the minister wanted that advice, that would be fine.

Andy Wightman: You have no fundamental objection to an advisory group.

Ray Perman: No. Our objection is not to the group that would advise the minister; the problem is the blurring of the accountability and responsibilities of the board.

Andy Wightman: Okay. It is very helpful that you have clarified your objection.

Eilidh Dickson: Some of the confusion is about what the advisory board is anticipated to do and about how it will be structured differently from the bank's executive board.

There is a question about expertise, particularly given the underrepresentation of women and others who have multiple characteristics of disadvantage in the finance sector and in economics. There might be a role for an advisory board in picking up some of the different expertise that is not captured within an executive board. As Mariana Mazzucato says in her paper, there might be a role for civil society in building consensus for missions, as the bank will need to have a considerable amount of social licence for it to invest public funds.

Therefore, there is a role for an advisory board, but I agree that we need to crystallise who will be on it, how it will be structured differently and what its role will be.

Robin McAlpine: I am very happy with the bill. It is broadly fine, but it might need a few tweaks. We did not make an awful lot of comments about the bill, and I have a high degree of confidence in the team that is doing the building work. We are very relaxed about the bill, because I think that the work is going well.

However, we would definitely have gone further on governance. When we wrote down our first proposals, the dotted line from the advisory group did not go to the ministers but went straight to the board, and I would still like that change to be made. The group should be advisory, not instructive. Although the ministers will be the shareholders, the bank will be a limited company, so the board will have all the legal responsibility for the successful operation of the company. The minister will be able to fire the board if they are not happy, but they will not be a member of the bank's governing executive.

We wanted the advisory group to feed straight into the board for a specific purpose. Initially, we proposed that there should be a tripartite advisory group that would pick up the broad missions. A third of the members of the group would be representatives of medium-sized enterprises. That would give the people who approach the bank to borrow a clear voice in how the bank should be run. Another third of the members would represent local authorities, housing associations and public sector bodies, and the final third would represent the public good element; that would include trade unions, and gender and so on would be taken into account. It is about finding a balance.

The bank's board will have a strong fiduciary duty to operate like a proper bank. It will need to make hard decisions and say that it cannot do something because, lovely though it is, it does not meet the bank's lending or financial criteria. To balance that out, we wanted there to be an advisory board that focused on customers—the customers being Scotland as a whole, including the private and public sectors. We suggested taking that approach to address the fear that banks can sometimes be a little tin-eared when it comes to their fiduciary duties. Such an advisory board would mean that its members could regularly say to the bank, "We represent the people to whom you are supposed to be lending, and this thing that you're doing isn't helping us. It could be done better, and this would be a great thing to try."

I take the point about conflicts of interest. I am not particularly bothered about who is sitting where, but the board of the bank should have a direct line to a group of people who are saying, "We represent the people you should be serving and we want to give you some advice. It is now for you to take that advice—or not to take that advice, because you are the board of a limited company."

Andy Wightman: There are various views on that issue, which we will explore further. However, do you think that provision for such an advisory board should be embedded in the bill, or should that be left to the board and ministers to work out?

Robin McAlpine: I always have the concern that long-term initiatives such as this need to be protected from politicians. Do not take that personally. It is just that the point of the bank is 10, 20 or 30-year time horizons, whereas, with the best will in the world, the point of politicians is often four and five-year time horizons. The purpose of the advisory board is to provide a voice that is not based on three or four-year cycles—

Andy Wightman: I understand all that. Do you think that the advisory board should be provided for in the bill?

Robin McAlpine: Again, we would have said that it is tripartite—

Andy Wightman: But do you think that the existence of an advisory board should be provided for in the bill?

Robin McAlpine: Yes, absolutely. I would go further and say that the advisory board should exist—

Andy Wightman: By statute?

Robin McAlpine: By statute. I would also say that its purpose, content and members should be such that we do not drift to a point in the future where, for example, the board gets filled up with appointees from the existing financial services sector. That is what I mean by that.

Eilidh Dickson: The short answer is yes. I think that the advisory board should be in the bill, for the reasons that have been outlined.

Ray Perman: I am relaxed about whether it is in the bill or not, frankly.

The Convener: That is a wide range of views. Jackie Baillie, did you have a follow-up question?

Jackie Baillie: Yes, but I am assuming that my questions are next anyway. I will segue into them, if that helps you, convener.

The Convener: We will let you do that.

Jackie Baillie: Fantastic. First, I should say to Robin McAlpine that I have been a member of the Scottish Parliament for 20 years, so four or five years is not in my timeframe.

I will pick up on something of substance that Andy Wightman raised. You and I will remember about 10 or 11 announcements that the bank was coming. The reason why it is able to be here is largely because of financial transaction money. The strings attached to that money means that it can be lent only to the private sector. The advisory group started off saying that the bank will not fund public projects. Clearly, your ambitions for housing and all the rest of it fall to the wayside unless the funding is opened up. Is that fair?

Robin McAlpine: You need to clarify that with the team. I understand that the team is already talking to housing projects. It is public sector money that is coming in. As I understand it, the team is saying that they are not going into local authority large-scale public infrastructure lending—they are not yet lending for the purposes of building schools, hospitals or roads. Straightforwardly, an awful lot of the initial first demand is coming from housing. I know some people who have been fairly close to this whose biggest worry, because the bank will be demand led, is that it has the potential to turn into a housing bank, which would not be a good thing. Housing is in there, but I do not think that wider public infrastructure is yet.

Jackie Baillie: We will clarify that, because, like you, I think that that is an ambition that the bank should have.

I come to the mission approach. Some of the evidence provided to the committee suggests that a mission-based finance approach will be complex to introduce and difficult to operate and evaluate. Do you share that view?

Ray Perman: We think that the bank should be mission led, but that it should start with one mission, because the suggested missions in the consultative document are big, important areas and they deserve to be done properly. To try to set up a bank from scratch—or very nearly from scratch—to fulfil all those ambitions will set it up to fail. We would prefer the bank to start with a single, simple mission, and to get on top of that mission before it expands into doing other things.

Robin McAlpine: It is almost certainly legally necessary that the bank has a mission. We did the original proposals on this, and one of the most significant barriers that you have got to get over is European Union competition laws. One of the three ways that the bank will get round those competition laws is to be mission driven rather than profit driven. If it is not mission driven, it will appear profit driven, and that will be more problematic in Europe. Saying explicitly that the bank must be mission driven is part of the structural set-up that enables it to take a unique place in the marketplace. As a result, that is essential and necessary.

My key concern is that we do not mistake being mission driven for simply asking, “Have you made Scotland carbon neutral yet?” It should be about things that move us in the direction of the mission, not necessarily about things that achieve it. I absolutely take the point about not loading the bank with missions and expecting it to do everything, but what if it says, “We want to invest in green energy and in women-led enterprises, and we want to anchor businesses in Scotland”? The last is something that I see as a mission, because the fact is that we have too many successful businesses that grow to a certain scale and sell out, and then the intellectual property moves abroad. One mission, therefore, should be to anchor medium-sized and growing enterprises in Scotland.

The point is that the bank can have multiple missions, just as long as no one is pretending that it is supposed to achieve and complete them by some given deadline. I think that it is capable of following more than one mission at a time in its lending decisions, but it is not the Scottish Government—it is not meant to change everything all by itself. I am quite relaxed about how the term “mission” should be interpreted, and the bank should be, too, and I really hope that politicians give it some leeway and do not attack every lending decision when it starts to make them. After all, not every decision will make every person happy.

Eilidh Dickson: We support the mission-driven approach, but we are slightly concerned that that approach has not yet been sufficiently articulated. It is not clear what a mission would look like, how long its lifespan would be, the technicalities of it, what would happen if multiple missions overlapped or contradicted each other and so on. Even the process for recalling them is not set out in the bill or, indeed, in the policy memorandum, and some work needs to be done to ensure that we all know what is being talked about.

The success of any missions specifically for women depends on how gender can be mainstreamed into the process, which is another reason for articulating the process better. We have recommended that the bill include an equality and non-discrimination element and that the mission process refers to the core objects to ensure that everything is singing from the same hymn sheet. If that does not happen, we might, in responding to a mission, end up with the objects falling by the wayside or with a concentration on the SME or lending elements of the bank’s decision making instead of on the large-scale challenges.

Jackie Baillie: I am curious as to whether you think that some of the missions should be set out in the bill, or included in the strategic framework in order to give ministers and the bank flexibility. After all, some of the big, strategic core objects can get lost if they are not fed right through the process. Perhaps the missions are one level removed from that—I do not know—but the issue that we are grappling with is what should or should not be in the bill.

Ray Perman: We would be more comfortable with their being in the strategic framework, rather than in the bill.

Eilidh Dickson: If missions are supposed to be medium to long-term challenges but not permanent aspects of the bank’s development work, they should probably be set out in the strategic framework, but the process needs to be articulated.

Robin McAlpine: If the bank is going to be here 100 years from now, I hope to goodness that we will still not be sitting here, saying, “Let’s try to get women an equal place in the workplace.” I assume that the missions will change, and I do not think that you will want to change them by having to put in place primary legislation that amends the bill. The bill should mention public good very broadly, but what that will mean for any given generation will, I think, change.

Jackie Baillie: It is safe to say that neither you nor I will be here in 100 years’ time.

Finally, to wrap this up, I note that Robin McAlpine has talked about public good. I do not know whether you saw that I explored with our previous panel of witnesses how they would assess that sort of thing. Assessing social costs and benefits is, for me, at the heart of economic appraisal, but I have to say that I was not convinced by the answers that I heard. For example, there has been no discussion of substance about the Treasury’s approach through the green book. How are we going to measure some of this stuff in order to decide where to invest? Have you provided any information to the Government on that?

Robin McAlpine: In our original work, we conceived of this as a bank that would look in many regards like a commercial bank, which would mean that people would come to it with requests for equity investment or loans, and we suggested that each request be assessed against broad mission statements about what the public good was. If, for example, providing more affordable and high-quality public rental housing was in the public good, something that moved in that direction would meet that goal.

We suggested that the bank should be reasonably subtle about it and say that those things would give additional weighting. I absolutely agree that missions will conflict. It would be nice if everything was endlessly neat and tidy, but it is not; there will be occasions on which an encouraging, developing Scottish business will source a product from a place that we would prefer to be a little more ethical.

12:15

I do not think that the bank should say, “You are a great Scottish business that is growing and creating genuinely high-quality jobs, and broadly you are doing public good, but there’s this one part of your business that isn’t, and until you do X or Y we are not going to lend to you.” That would be a mistake. That is why I say that we need a little bit of leeway, and that in conversations with people that the bank is lending to, it should say, “Okay, we will lend to you but could you look at your procurement of that element of your business, because, in time, we think that that will be seen as a strong negative against your enterprise." I do not think that the bank should be saying, "Until you source only ethical cotton for whatever you are doing, we will definitely not lend to you."

That is my view; people need a degree of leeway. We thought that the best option would be to give additional weightings to enterprises that meet certain types of goal. For example, one might say that in an absolute head-to-head, a woman-led enterprise might be given a little more weighting than an alternative bid that looked almost identical in every other way. Rather than being dogmatic about it, the bank says, "We incline more to lend to your enterprise, the more we judge it to be hitting our missions," rather than "Here's a tick box. You've crossed the threshold. You now qualify."

Ray Perman: The short answer is that we have not given much thought to that at the moment. The committee will be aware that Scottish Enterprise and the Scottish Investment Bank have a methodology for gauging impact. Social Investment Scotland, which Jackie Baillie set up when she was communities minister 20 years ago, has a different but good and thorough methodology. It is important that the bank consults widely on the methodology that it is going to use and collects and monitors the figures in order to give an indication of the impact of the investments that it makes.

Eilidh Dickson: Part of the success of the bank will be the extent to which it can mainstream gender into all of its activities, not just through the recipients of the finance. I talked about the wider impact that treating care as infrastructure investment could give us. That is not just good practice; that is a legal requirement that the bank will face. Data will be a key part of that, and we know that the current actors are not great at collecting, publishing and disaggregating their data. The bank will have to work on that very quickly, as part of its monitoring criteria.

There is good practice. The Scottish Government is working on a gender index as part of its alignment with the European gender equality index from the European Institute for Gender Equality. It would be good if that piece of work could align with those metrics in some way, and more generally.

The Convener: We have very brief follow-up questions from Andy Wightman and then Angela Constance.

Andy Wightman: On the question of the mission in section 11, it is not intended that the mission-setting process or the mission itself should be subject to a resolution of Parliament. Do you think that Parliament having a role in agreeing those would add to or hinder the process? Should there be parliamentary scrutiny of the mission or should it be left to ministers?

Ray Perman: The RSE has not made a statement on that, but personally, I think that it would enhance the credibility of the missions if there were a resolution of Parliament behind them.

Robin McAlpine: I agree. The missions will not be changed on an annual basis—we are probably looking at five-year time frames. I cannot see that taking the missions through Parliament once every five years would add a lot to the process. The missions would have to align to Government objectives and, inevitably, governments and strategic objectives will change. I am a fan of democracy; if the Parliament gets behind the missions, that would be a good thing.

Andy Wightman: I have a brief question on equalities if there is time, convener.

The Convener: We will move on to Angela Constance and come back to that if we have time.

Angela Constance: I have a few questions for Ms Dickson.

Tapping into all the talents is not just the right thing to do, it is the smart thing to do for businesses and our economy, so I want to pick up on some aspects of Engender's written submission. You can correct me if I am wrong, but my impression is that you feel that the equality impact assessment was a bit of an afterthought.

Eilidh Dickson: We have pretty major concerns about the equality impact assessment for the bill, not least that it is not formatted like an equality impact assessment. An impact assessment should be a process for gender mainstreaming, as we were discussing earlier. It is not just a bureaucratic, tick-box exercise.

The idea is that the policy is articulated, research is done, and changes are seen as a result of applying the information that has been garnered. We had two consultation processes, an implementation plan and several announcements before the equality impact assessment was even published, and that was alongside the bill as already drafted. There is very little evidence that the equality impact assessment has informed any aspects of the bill. We see no reference to equality or the securing of equality intentions in the bill as it is drafted.

I should also say that the equality impact assessment that was published does not cover all the protected characteristics. It covers only two, and even then, it is in particularly niche strands of the bank's activities and not the wider economic impact that I have talked about a bit.

We are pretty convinced that, in order to meet even the basic legal requirements set out in Equality and Human Rights Commission guidance, the equality impact assessment will have to be redeveloped. The missing sections will have to be added and the whole process of analysis will have to be redone.

Angela Constance: Obviously this committee's role is to raise that with the Government, as appropriate. Do you have any on-going involvement with the Government to get the equality impact assessment into shape?

Eilidh Dickson: We are speaking to officials about that.

Angela Constance: Thank you. You also spoke about anchoring in the bill's core purpose and principles a meaningful commitment to equality, and that being referenced back into the strategic framework and the approach taken by the missions. Where do you think there has been a lack of consideration of that in the work that was done to design the bank and in the bill, which could be improved on?

Eilidh Dickson: We responded to both of the Government's consultations on the bill—the recent one and the initial consultation, back in 2017, which was before I started working at Engender. However, that work was done across the women's sector.

As consulted on, the implementation plan had a much broader intention, which seemed to find its way into the consultation on the bank's social role. It does not speak specifically about gender, but there was a notion that the bank's vision should be about untapped potential, responding to climate change and some of the other big social issues that Scotland faces at this time. That does not necessarily seem to agree with the bill. As I have already said, the bank's objects focus narrowly on the economic aspects of the bank's work. To some extent, that is understandable, but we have lost that wider vision of how all the different policy areas interact and should interact when the bank is in operation.

The bill will be strengthened by having that purpose or vision, and we have recommended how it could be further strengthened. We need something that entrenches why we are doing this, why we need something radically different and why we are not just returning to the same actors and making tweaks around the edges.

I have also made recommendations that relate to the bank's objects. Equality and non-discrimination are not included in the bill, and that does not translate through to meaningful action. The EQIA is a pretty good example of how the public sector equality duty has worked only so much.

Close the Gap has done some excellent work on compliance with the public sector equality duty. Having a legal duty for the bank will keep it at the top of everyone's mind and will allow for the underpinning of the development work that will have to straddle all the bank's different activities in the future.

Angela Constance: You touched on methodology issues such as how assessments and measurements are done and your understanding of merit. Will you say a bit more about how, in a practical sense, diversity and merit are two sides of the same coin that do not necessarily pull apart from one another like polar opposites?

Eilidh Dickson: Sure. If we were to start from the basis that everything is currently merit based, as the previous panel hopes is the case, we would not be in the situation that only 28 per cent of public executive directors are women. The figure should not be as low as that—it is just over a quarter. We have a wealth of evidence, some of which I refer to in our written submission, on the ways in which equality is good for growth, but the reverse is not necessarily always true.

I do not know whether that answers your question. Perhaps I have not picked up on the avenue of thought that you would like me to expand on.

Angela Constance: I was keen to give you the opportunity to pick up on some of the issues that were raised earlier. However, I am conscious of time, convener, and, in the interests of equality, I am also keen to hear from the men on the panel.

Robin McAlpine: I have no disagreement with that, and I defer on the legal aspects.

In the long term, we must use the full power of Government and all its agencies to tackle the issues. What worries me and makes me a little nervous—this coming from a leftie like me—is that people might think that the national investment bank can fix those issues on its own. It cannot—it will be a source of funding. It can fund in a way that is more conducive to addressing the issues, but it cannot fix them on its own. Those are perfectly reasonable suggestions about how it can do it better. The only thing that has worried me in its development is people saying, "Great—now we've got a national investment bank, that's Scotland decarbonised and gender equal." No—we have a source of finance that is more conducive to making those things happen, but we cannot take our foot off the pedal on any of the other issues.

Ray Perman: I do not dissent from anything that Eilidh Dickson said. I certainly agree with the point that, if something is in legislation, it gets done, and, if it is not in legislation, it often gets overlooked.

John Mason: I would like to press a little bit more on some aspects that we have touched on.

On the balance between the objects and missions, the objects include

"investing in inclusive and sustainable economic growth",

which is pretty vague. The Conservatives might take that as meaning, "Focus on the economy and throw away the environment," while the Greens might take it as, "Focus on the environment and throw away the economy." Do we need something a bit more specific in the bill? We hope that it will go through all the political cycles and remain fairly consistent. Are you convinced that we need no more detail in the bill?

Eilidh Dickson: Inclusive growth is referred to a lot, appearing in the economic strategy and other related policy frameworks, but it has not been defined. There is an Organisation for Economic Co-operation and Development definition that is sometimes relied on, but there is no sense yet that we have a clear direction for what we mean when we talk about inclusive growth. Do we mean "everything"? Do we mean "everything" sometimes? Do we mean "gender" sometimes? Do we mean "placemaking" sometimes? "Inclusive growth" is not sufficient in itself to guide that kind of work.

John Mason: Can we rely on what comes below the bill to look after that, or should we have a bit more about it in the bill?

Eilidh Dickson: We should place the social and environmental impacts that the bank could have in the legislation, otherwise who is to say whether it will still deliver them in 10 years' time?

John Mason: Mr McAlpine, you seem relaxed about not having too much in the bill.

Robin McAlpine: Yes. The recommendation of the Committee on Climate Change has the word "growth" in it, but, in 100 years, we will not still be growing in the way that we are growing now. I could take up that issue.

I will put it simply: we could have a lengthy national debate about the meaning of the public good now or later, or we could do both. This is an autopilot thing. We will not find a perfect definition that will last for the next 100 years, so we can press the button and go on. I am relaxed about this because—Eilidh Dickson is right—different Governments will have different interpretations, and the definition will change. Such is democracy.

12:30

With the governance structures and the instruction that the bank is arm's-length and has a long-term horizon, I am currently reasonably reassured and relaxed that the bank has enough leeway to respond to changing political imperatives while maintaining a more long-term strategy, which the bank itself will set.

I would love to come up with some sort of proposal that would create a set of objectives and missions that would be agreed on by everybody for the next 30 years, but that is not realistic. There will be an on-going negotiation, which I think is healthy.

Personally, I am caught between the fact that putting more on the face of the bill now may restrict what the bank does and the fact that putting less on the face of the bill now may mean that it does less to maintain the public good benefit of the bank that I might like to see. I do not think that there is a final answer to that. As I said, it is a political negotiation for today, tomorrow and the day after that as well.

John Mason: I understand that the Royal Society of Edinburgh is very strong on the idea that there should be just one mission to start with.

I asked the previous panel whether it is the case that the missions are all quite distinct from each other and that we should consider them separately or whether it is more the case that they all overlap with each other. For example, a couple of the German bank's missions are climate change and environment and globalisation and technological progress, which I see as very much overlapping. How strongly do you feel that there should be only one mission? My fear is that we would concentrate on the low-carbon economy and ignore inclusive growth, thereby getting the balance wrong.

Ray Perman: You are right that all those missions are important and universal, and that there is a tremendous amount of overlap. I go back to your earlier point that the bill should not be prescriptive and that the missions should be set in the strategic framework and reviewed from time to time. The basic mission of getting more investment into companies and more economic growth—however we define that—in Scotland is the right single mission to start with. To overlay on that mission the transition to a low-carbon economy and the amelioration of the effects of an ageing workforce and other missions would be to load too much on to the bank in its early stages. We should start simple and see how we get on.

John Mason: You are arguing not that we should just forget about those issues but that they should be put on the back burner or to the back of our minds, or something like that.

Ray Perman: I am certainly not arguing that we should forget them, because they are very important. I might be arguing that they are so important that we ought to give additional thought to how they could be achieved. However, expecting a new institution to do all of those things from day 1 is probably unrealistic.

John Mason: That is a fair point, and it touches on timescales. My final question is whether the timescales are realistic for setting up the bank, getting people in place and ensuring that the board is properly representative.

Ray Perman: We are not close to the detail in the way that the previous panel was. However, Benny Higgins seemed to be fairly relaxed about the timescale, and we must take the view that he is right and that the bank can be set up in that time.

The Convener: I thank our panel very much for coming in today. We will now move into private session.

12:34

Meeting continued in private until 12:54.

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The deadline for corrections to this edition is:

Thursday 6 June 2019

Published in Edinburgh by the Scottish Parliamentary Corporate Body, the Scottish Parliament, Edinburgh, EH99 1SP

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