BACKGROUND

The decisions taken within last week’s Budget have been shaped by the Scottish Government’s Purpose of creating a more successful country, with opportunities for all of Scotland to flourish, through increasing sustainable economic growth.

Our focus on delivering this Purpose is even more crucial in these tough financial times.

Over the period 2010-11 to 2014-15, the Scottish budget is being cut by the UK Government by 12.3 per cent in real terms. Our capital budget – a key driver of economic growth – will bear the harshest reduction, with a real terms cut of 36.7 per cent.

We are prioritising support for growth and we are working hard to create the jobs our people need. We are targeting our efforts at –

- boosting public sector capital investment;
- improving access to finance and encouraging new private investment;
- enhancing economic security to support confidence across the Scottish economy; and,
- taking direct action to tackle unemployment.

However, we lack many of the key job creating powers open to other governments. We have therefore urged the UK Chancellor to also take decisive action in these priority areas to protect growth. The UK needs a Plan B for recovery.

ECONOMIC CONDITIONS

The effects of the global financial crisis continue to impact on the world economy. Our own economy entered recession in mid-2008 before returning to growth in late 2009. During the recession, output fell by 5.7% (peak to trough) in Scotland, compared to 6.3% in the UK.

Scotland’s labour market performance has improved over the year. During the most recent 3-month period Scotland was the only part of the UK with falling unemployment. Over the past 12 months, unemployment has fallen by 33,000 in Scotland compared with an increase of 44,000 across the UK as a whole. Scotland now has the highest employment rate of any UK nation and a lower unemployment rate and higher economic activity rate than the UK.

The most recent PMI survey signalled that private sector activity expanded for the 8th consecutive month in August. The index (where above 50 marks an expansion) was 52.7, higher than the UK equivalent figure of 50.6. Scotland also recorded a more positive reading on the most recent Bank of Scotland Labour Market Barometer with a value of 53.9 compared to the UK figure of 50.9.

It is clear however, that the global economic recovery remains fragile and Scotland cannot expect to be immune from such pressures.

At this stage of the economic cycle, securing sustained economic recovery is therefore the most important challenge that we face. Our Budget gives clear priority to efforts which will accelerate economic recovery and protect jobs.
BOOSTING PUBLIC SECTOR CAPITAL INVESTMENT

Capital investment is key to economic recovery. Investment is usually one of the first elements of the economy to contract during a recession. However, it is also vital to growth as it not only provides a timely boost to economic activity and jobs but it creates a legacy of assets which can have long-lasting economic benefits.

Despite a greater than 36% cut to our capital budget over the next four years from the UK Government, we are prioritising investment in Scotland’s infrastructure through a range of initiatives including –

- Taking forward an ambitious programme of new investment – including major new projects such as the New South Glasgow Hospitals and the Forth Replacement Crossing (the largest civil engineering project in a generation which will support 3,000 jobs);
- Boosting our traditional capital budget by:
  - switching an average of over £200 million per year from resource budgets to boost capital programmes;
  - taking forward a new pipeline of revenue financed investment worth up to £2.5 billion, to be delivered through the Non-Profit Distributing (NPD) model;
  - implementing innovative measures such as Tax Incremental Financing (TIF), the National Housing Trust (NHT) and investment through the JESSICA Fund; and
  - taking a proactive approach to public sector asset management through the Scottish Future Trust (SFT) led hub programme.

Taken together, these initiatives mean that despite these sustained cuts to our capital DEL budget, our overall capital investment programme will now grow in each of the next three years. By 2014-15 our level of investment will be 25% higher than in 2011-12.

IMPROVING ACCESS TO FINANCE AND ENCOURAGING NEW PRIVATE INVESTMENT

The recovery is being held back by weak private sector investment, indeed, overall investment in the UK remains some 15% below pre-recession levels. Evidence shows that while many large companies have significant cash holdings or can access capital markets directly, for most Small and Medium-sized (SME) companies bank lending remains the key source of finance.

It is vital therefore that we encourage new private sector investment, not only by improving access to finance but also by providing the right conditions and opportunities to attract new and sustainable investment to Scotland.
We are limited in our powers in this area – particularly with regard to bank finance - and the UK Government must act and ensure that banks meet their lending commitments. However, we are taking forward a range of initiatives including -

- Establishing the **Scottish Investment Bank** which is open, investing and lending to Scottish companies – however, this cannot be expected to fully take the place of private bank lending.
- Alongside this, the £70m **National Renewables Infrastructure Fund** aims to tap into the appetite in the private sector to invest in renewables in Scotland. This forms parts of over £200 million of investment in Renewables committed in the Spending Review.
- Working to **attract major new private investment** to Scotland building on recent successes with Amazon, Gamesa, Dell, State Street, Vion, Doosan Power, Ryanair, EasyJet, Tesco Bank, Virgin Money, Blackrock, INEOS/PetroChina and Mitsubishi Power Systems.

**ENHANCING ECONOMIC SECURITY TO SUPPORT CONFIDENCE ACROSS THE ECONOMY**

To combat the uncertainty that is facing households and businesses, action is needed to help provide greater economic security and protection, as far as possible, from rising prices.

- Our **pay restraint policy** will continue to support thousands of public sector jobs across Scotland;
- Alongside this we are up-rating the Living Wage to £7.20 and providing a £250 pay award for those earning the lowest in the public sector to support households in these tough financial times;
- In recognition of the challenges faced by households in these tough financial times, we will continue to implement core economic and social commitments through our ‘social wage’ –
  - abolition of prescription charges; free higher education; free personal care; no bridge tolls; protection of health budgets; and, concessionary travel.
- Our tax policies, including retaining the **Small Business Bonus Scheme**, our commitment to match the **English poundage** and freezing council tax, will help Scottish households and businesses at this difficult economic time.

**ACTION TO TACKLE UNEMPLOYMENT – PARTICULARLY AMONGST YOUNG PEOPLE**

In addition to all of these measures, the Scottish Government is taking direct action to tackle unemployment and ensure that people who are out of work or underemployed - particularly our young people – have access to the right training, skills or education opportunities to meet their needs. We are taking forward a range of measures including -

- Our new **Opportunities for All** initiative which will ensure that every 16-19 year old who is not in work, a Modern Apprenticeship or education will be offered a place in education or training;
- Delivering **46,500 training opportunities** – the vast majority of which will be targeted at young people;
- Funding a record **25,000 Modern Apprenticeship** new starts in each year of this Parliament;
- Maintaining **bursary support** to help young people remain in college and training;
- Creating **14,500 pre-employment training opportunities**;
- Completing the roll-out of **Activity Agreements** to help our most vulnerable young people remain in education and training; and
• Continuing to fund the **Educational Maintenance Allowance** – something which has been abolished in England.

**OTHER KEY INITIATIVES**
Alongside the measures set out in our Spending Review, the Government Economic Strategy published on 12 September 2011, establishes the foundations for long-term economic prosperity with a focus on Growth Companies, Growth Markets, and Growth Sectors and securing the benefits from the low carbon economy. Key initiatives include -

• introducing **four Enterprise Areas** in Scotland;
• providing advice and support to help **SMEs grow, hire staff and take on apprentices**;
• promoting **Scottish exports** - with a target to deliver a 50 per cent increase in exports by 2017;
• streamlining investment in **innovation and commercialisation** to boost productivity and translate great business ideas into great business practice;
• establishing a **Next Generation Digital Fund** to accelerate the delivery of superfast broadband across Scotland with a particular focus on rural areas;
• continuing to implement the modernisation of the **planning system**;
• developing a **Cities Strategy** to support more effective collaboration to optimise their growth;
• developing a **Regeneration Strategy** to help our most disadvantaged communities; and,
• maximising the public sector’s contribution to the economy through smarter use of **public procurement**.

**CONCLUSIONS**
The actions set out above, and in our Government Economic Strategy, demonstrate the range of initiatives and policies the Scottish Government is taking forward to help accelerate the recovery, support jobs and establish the foundations for long-term sustainable economic growth.

A number of key challenges remain, particularly in the labour market and the risks from continued global uncertainty and sluggish growth in our key trading partners. We believe however that the actions we are taking are crucial in supporting the economy at a time of economic and financial hardship.

Scottish Government
September 2011
The Centre for Public Policy for Regions (CPPR) published a report on 22 September offering a commentary on the Scottish Spending Review and Draft Budget 2012-13. This appendix sets out the Scottish Government's position on issues raised by the CPPR's paper and subsequent media coverage.

**Business Rates**

*The CPPR have asserted that the Spending Review means Scottish businesses will not share in the Scottish Government’s desire to cap tax pressures on consumers (as a result of projections for Non-Domestic Rates Income – or business rates – over the spending review period).*

Non Domestic Rates Income is estimated to grow by £493 million by 2014-15 compared with 2011-12. The figure of £849 million quoted in media reporting on the CPPR report is a misleading aggregate over three years, a product of double and treble counting. Out of the £493 million growth, only £40 million from the proposed Public Health Levy represents an additional increase in the rates for occupied properties. The remainder is made up of inflation, changes in the level of economic activity and appeal losses as part of the Revaluation cycle. No occupied property faces any increase other than from these factors.

The Scottish Government will continue over the spending review period to match the English poundage rate and to maintain the most generous package of reliefs available anywhere in the UK, worth on average more than £500 million per annum over the 2010-15 revaluation cycle. Central to that relief package is the continuation of the Small Business Bonus Scheme, supporting tens of thousands of properties.

Growth in Non Domestic Rates Income (NDRI) is made up of four elements:

- Over half the increase is accounted for by the impact of matching the English poundage rate through the application of the most recent Office of Budget Responsibility (OBR) estimate of RPI inflation, of over 12% between 2012 and 2015. Increasing NDRI in this way is standard practice across the UK. Matching this increase, through the Scottish Government's commitment to match the English poundage, was the delivery of a manifesto proposal promoted vigorously by, among others, CBI Scotland: "CBI Scotland’s over-riding demand of non-domestic rating is that Scotland retains poundage rate parity with the rest of the UK." CBI Scotland ‘Energising the Scottish Economy’.

- An estimate of the impact of changes in levels of economic activity and changes to the outcomes of appeals, given where we are in the revaluation cycle we expect there to be higher levels of economic growth as we move through the spending review period and appeals will be settled at different stages over the three years. These estimates lead to a reduction in assumed income in earlier years and growth in later years. They do not reflect any changes in the burdens placed on individual businesses.

- Revenue from changes to the empty property relief regime (£18 million in 2013-14 and 2014-15). This will introduce incentives to bring vacant premises back into use and reduce the prevalence of empty properties in Scotland’s town centres, while still maintaining empty property relief at more generous levels than available in the rest of the UK. The Scottish Government is proposing retention of full rates relief (100%) for vacant listed and industrial
properties and propose to offer 10% relief (as opposed to the current 50%) for standard empty premises, after the initial 3 months rates free period. This is significantly more generous than on offer in England.

- A Public Health Levy on large retail properties that sell tobacco and alcohol, projected to realise £30 million in year one, rising to £40 million thereafter. The money raised will support the preventative spend measures set out in the Budget to help address Scotland’s long running health and social problems associated with alcohol and tobacco use.

The CPPR stated that the availability of future funds to Local Government is less certain, as they rely on NDRI. This is not true. Scottish Government guarantees to provide local government with the combined total of NDRI and Resource funding

Comparison with previous rates collected over a 4 year period

It may be helpful to put these measures in context. Over the 4 year period 2003-04 and 2006-7 there was a 13.3% rise in NDR income collected when the RPI inflation index during that period was 8.8%. This demonstrates there is growth in income without other changes. The RPI comparison over the comparable 4 year period 2011-12 and 2014-15 period is 12.6%, significantly higher than in 2003-04 to 2006-07.

Previously there was also a 29% rise in rates collected between 1999-2000 to 2006-07.

Between 2005-06 and 2008-09, the actual income collected by local authorities remained broadly constant as the administration in office at that time reduced the poundage rate in order to reintroduce parity in the poundage rate. The poundage rate in Scotland was higher than that which applied in England in each year since 2000-01 until 2007-08.

Efficiencies

The CPPR report suggests there is doubt about the veracity and deliverability of the Scottish Government’s efficiency savings.

The Scottish Government has a proven track record on efficiency. Outturn figures for 2010-11 have just been finalised and these confirm we have delivered almost £2.3 billion savings against our £1.6 billion target, having exceeded our targets in 2008-09 by £300 million and 2009-10 by £400 million.

Efficiency savings have been re-invested in services. For example, development of Child and Adult Mental Health Services; Community Nursing services for older people. £5.1 million of savings from Police Central Government funding helped develop the Gartcosh Crime Campus and the new forensic science laboratory in Dundee.

Throughout, the Scottish Government has adopted an assurance process involving Accountable Officers that is in line with Audit Scotland’s preferences. The Government has always made clear that public bodies should report publicly on their plans to improve the efficiency of public services, actions undertaken and results achieved. The guidance is explicit that efficiency claims should be supported by auditable evidence to demonstrate they have not resulted in service cuts - and that they can be subject to scrutiny by Audit Scotland.
Health Budget

The CPPR paper suggests that the Scottish Government is not meeting its commitment to protect the Health revenue budget and that significant cuts are being made to other Health budgets (e.g. general medical, dental and ophthalmic services).

The Government has delivered the election manifesto commitment to pass on Barnett consequentials to the Health budget in Scotland. For the period 2012-13 to 2014-15 the Spending Review shows planned annual increases in the Health resource budget of £249 / £293 / £284 million. These exactly match the Barnett consequentials arising from increases in Department of Health spending set out as part of the UK Spending Review 2010.

As set out in Table 7.02 of the Budget document, NHS Territorial Boards will have real terms increases in each year of the spending review. NHS Boards funding is increasing by 2.9 / 3.3 / 3.1 per cent. They will have £720 million more in 2014-15 than they had in 2011-12, or an additional 9.5%.

The budget document makes clear that allocations for 2012-13 to 2014-15 for General Medical Services have still to be decided and are subject to UK pay negotiations with the professional groups concerned. They are therefore presented as “flat cash” in the budget document, with provision for potential additional costs included within the portfolio budget as a whole.

Allocations for General Dentist Services and General Ophthalmic Services have been held at 2011-12 levels and we expect any additional costs will be offset by efficiency savings agreed with these professional groups.

Higher and Further Education

The CPPR report states that funding for Higher Education offsets the Barnett formula implications of cuts in Higher Education funding in England, but that there are large cuts in funding for Further Education.

The Scottish Government is delivering free access to higher education and is committed to delivering a minimum income guarantee for students of £7,000 a year.

The Government is investing an additional £76 / £115 / £135 million in Scottish universities over the spending review period, with real terms increases of more than 5% in each of the three years. This level of investment will maintain Scotland's world leading position in university research.

The Government is increasing the concentration of SG funding on research excellence and aligning research to national priorities. This will consolidate the majority of research funding in a smaller number of universities with a track record of world-leading research that levers the greatest levels of research funding from other sources and maximises economic impact.

Through Opportunities for All, the Scottish Government has given a guarantee of a place in education or training to every young person aged 16-19 if they are not currently in education, training or employment.
The Government will also invest in college infrastructure during the Spending Review, including funding for new college estates in Glasgow, Inverness and Kilmarnock through the Non Profit Distribution model – projects with a total capital value of some £300 million.

Scottish Water

*The CPPR reports suggests there is a risk of delay or cancellation of aspects of Scottish Water’s investment programme, or of increases in water charges, as a result of the funding allocations in the spending review.*

The Scottish Government considers Scottish Water to be a public sector success story. Due to savings and extra efficiencies, the Government has been able to reduce its lending to Scottish Water without compromising the delivery of improvements to services.

The Spending Review shows the Government will lend £100 / 140 / 200 million to Scottish Water over the next three years. Scottish Water has confirmed that it expects to be able to complete its capital programme, investing £1.7 billion to achieve this.

Scottish Water is performing well as a public sector organisation. Average household charges are £32 lower in 2011-12 in Scotland than in England & Wales. (in Scotland average £324 per annum). Charges will reduce in real terms over the 2012-15 period.

Scottish Water has also consistently outperformed its efficiency targets. It was tasked with reducing costs by £1.5 billion in the period 2006-10 period. It outperformed this target providing additional efficiencies and benefits worth £175 million – around £12 for every household per year.

By 2015, Scottish Water will provide one of the best value for money water and sewerage packages in the UK. Over the period 2006-10 standards of service have improved by 76% - meaning that levels of service are now comparable with England and Wales. Scottish Water is expected to match the best performing companies by 2015.