CONFIDENTIAL A

(4)

Prime Minister

MR SCHOLAR

PA MCS 5/7

17 June 1983

For discussion at your next regular meeting with the Chancellor?

cc Mr Mount
Sir Alan Walters

Yes ms

MCS 23/6

THE REVIEW OF REGIONAL POLICY

Decisions will have to be taken soon on regional policy if the full benefits - greater cost-effectiveness and substantial savings - are to be achieved much before the end of this Parliament. If these reforms are to be thorough-going ones, as we hope, they will dismay the Scots, Welsh and others. It would therefore be better to face this problem sooner rather than later.

The Policy Unit's view of regional policy is that it operates against the national interest. To the small extent that it actually works, the policy diverts investment, often at very high costs per job, from locations which industry prefers, thereby reducing efficiency. Many of the jobs concerned have not proved to be secure, partly because of poor industrial relations. 'Regional Trends' reveals that the North and Wales had the highest rates of industrial disputes in the period 1977-81 and the worst levels of unemployment in Great Britain in 1982. Conversely, East Anglia and the South East had the lowest rate of disputes and the lowest rate of unemployment. To some extent, the policy taxes the successful regions and insulates the less successful from the predictable consequences of their own behaviour and anti-business attitudes. Since the Government is committed on political grounds to maintain a regional policy, let it at least absorb far less money and use that money more effectively.

The Prime Minister asked that MISC 14 should continue to supervise the review of regional policy (your letter of 8 March) and that she would consider how discussions should be handled when the Chancellor reported back. My advice is that the Prime Minister should have a private word with the Chancellor in the next week or so, before MISC 14 takes a follow-up report from officials, to ensure that the MISC 14 discussion does not close off any options. My reason for suggesting this is

Put on agenda

that the officials' report will not offer a radical change in regional policy. It will offer one, very sensible change of substance (lopping off automatic grants for replacement investment) but will suggest instead that the savings from this be devoted to additional selective assistance. The report's proposals are likely to make only a small dent in the manifest absurdity of regional grants - their bias towards capital-intensive projects, such as ethylene crackers, which absorb enormous grants and employ a handful of people, in areas with exceptionally high levels of unemployment. This bias cannot in the longer term even be said to help the economies of the assisted areas. Capital-intensive industries happen also to be slower growing than the average.

The officials' report will offer combinations of capital and job-related grants as a step towards more neutral incentives but the presentation of these options will be heavily slanted towards capital grants because the regional policy practitioners prefer them: capital grants are thought to be 'predictable', whereas job grants are less so, because they depend on projects' ultimate success (an advantage surely?). Job-related grants will have little scope to bite, perhaps on as little as 6% of investment in the assisted areas. The danger I foresee is that MISC 14, on which the regional interests are strongly represented, will decide in favour of an expensive and ineffective, capital-biased option, which might, as an illustration, provide for 20% automatic capital grants for around 90% of investment in new projects, reinforced by selective assistance, up to high cost-per-job limits (£17,000 +) for new and replacement investment, and grants for new technologies of up to 50%. The opportunity to save £200 million or more a year from the £460 million cost of regional support could be lost.

The Prime Minister might suggest to the Chancellor that he tries to steer MISC 14 towards two conclusions: 1) To ask officials to cost a more job-orientated option than any suggested in the officials' report. The job-related element will be the key to presenting a cheaper regional package; 2) as a stop gap measure, using discretion under existing legislation to withdraw grants for replacement expenditure and for new projects which fail to create a given number of new jobs per £ million of grant.

NICHOLAS OWEN