



CCBT

✓c No

DEPARTMENT OF TRADE AND INDUSTRY
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JF4599

PS/ Secretary of State for Trade and Industry

20 October 1983

Prime Minister ④

John Kerr Esq
Private Secretary to the
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON
SW1P 3AG

To note this paper which is a
useful summary of the issues
and to agree X. (No need to
better with Annex).

Yes - but I hope the White Paper is fairly
well advanced. We do not
want a long gap between announcement
and publication. not
AT 20/10

As you know, my Secretary of State is due to present a paper on
Regional Policy at the NEDC meeting on 2 November. A draft has
already been discussed inter-Departmentally at official level,
and Mr Tebbit has now had an opportunity to consider this. I
now enclose a final draft, which incorporates a number of
amendments made by my Secretary of State in the interests of
producing a crisper document. I should be grateful if you, and
others to whom I am copying this letter and its attachment, could
let me know whether your Ministers are content with it.

X

2 My Secretary of State believes the NEDC meeting would be an
excellent opportunity to announce the Government's intention to
publish a White Paper, and hopes that the Chancellor and
colleagues will agree to this.

1

3 The NEDC Secretariat would ideally have liked the paper to
have reached them this week. Clearly this will not be possible,
but I should be grateful if you could me have any comments,
written or telephoned, by lunchtime on Monday.

4 I am copying this letter and its attachment to Andrew
Turnbull (No 10), Elizabeth Hodgkinson (Department of Education and
Science), John Lyon (Northern Ireland Office), Michael Reidy
(Energy), John Graham (Scottish Office), Colin Jones (Welsh
Office), John Ballard (Environment), Barnaby Shaw (Employment),
and David Heyhoe (Lord Privy Seal).

Yours ever

Colman McCarthy

M C MCCARTHY
Private Secretary

Encl

PAPER FOR NEDC BY THE SECRETARY OF STATE FOR TRADE AND INDUSTRY

REGIONAL ECONOMIC POLICY

As the Council will know, the Government are engaged in a review of regional economic policy. We shall publish the results of our review in due course.

2 Regional economic policy (REP) comprises a set of policies, listed in Annex A, designed to influence the geographical distribution of investment and employment. Many other policies are relevant to employment in the regions, but our review is concentrated on the policies identified in that Annex as "main stream REP".

3 The social case for aiming to reduce regional disparities in employment opportunities remains, and we said in our manifesto that we would continue to maintain an effective regional policy. The economic case however is now less clear-cut than ever before. During the 1960s and early 1970s the standard macro-economic argument for regional industrial policy at a time when labour was scarce in some areas but less so in others was that the encouragement of employment in the latter eased the pressure of demand ("overheating") in the former; and consequently that more employment and output could be achieved nationally for a given total demand and inflation level. The strength of this argument, however, is minimal at a time where there is higher unemployment in all regions.

4 There are other economic arguments for regional policy. One is that it is desirable to make regional economies more self-sufficient (and hence less dependent on public expenditure support) by improving their industries' capability to match the competition and to innovate. Another is the wish to encourage inward investment projects which are likely to strengthen the economy, by coming to the areas of high unemployment. Such projects may not only provide direct employment but may also help to spread managerial and technical skills, technological know-how and better industrial relations practices. EC rules limit more strictly the scope for offering financial incentives to attract such investments to other areas. If the UK had no regional policy, it would not qualify for Community payments from the ERDF, even on infrastructure projects. All the UK's major partners in the Community operate regional policies, and the European Parliament and the Commission attach great importance to regional policy as a means of knitting the Community together.

5 Regional policy, however, has a cost. Expenditure in Great Britain on the main measures totalled some £900 million in 1982/83 (Annex B). Most of these payments are simple transfers, but there are real costs as well. Expenditure on regional policy means that other candidates for expenditure lose out, or else

adds to the pressure for higher taxation or interest rates. Other economic distortions also impose costs: where regional policy has led in the past to the wrong choices of location by firms there has been damage to the national economy.

6 In this light we must question the overall cost effectiveness of such expenditure: What effect do regional incentives have on firms' investment decisions? To what extent is regional policy successful in raising the level of investment and employment in the Assisted Areas (AAs)? It has been estimated that after full allowance for deadweight expenditure and displacement effects in the AAs themselves, regional industrial policy may have created about half a million jobs in the AAs during the 1970s at an average cost of around £34,000 per net job, taking account of regional multiplier effects. However, these estimates are currently being revised. Nor should the displacement effect of jobs created by regional policy on jobs elsewhere be underestimated. To the extent that regional policy simply transfers, at public expense, jobs from one part of the country to another, it is clearly of negative overall national economic benefit, as opposed to social benefit. Equally we must question whether regional policy instruments are aimed at the right targets, and whether they are focussed properly to give long-term help to the areas most in need, at a time when the nature of the regional problem has been changing in some respects. (See paragraph 10).

7 Nor can regional policies be viewed in isolation from national economic policies. If they are incompatible with national economic policies it is unlikely that they can be effective. It is necessary, therefore, to ensure that regional policies are based on analysis of regional disadvantage and identification of its underlying causes. Regional problems have usually arisen in areas highly dependent on contracting traditional industries. Industrial structure and the rate of new firm formation are clearly relevant, and the economies of the AAs seem weak in respect of both innovation and new firm formation. This does not provide the whole explanation and peripherality has its part too.

8 The persistence of large local disparities of unemployment rates indicates a poorly working labour market. Whilst migration and wage-flexibility should lead the labour market to correct this they have not done so. Migration happens to a considerable extent already but it has its dangers. Substantial outward migration over long periods can create its own problems, especially if the emigration is selective and leaves behind mainly a dependent population; or under-utilized infrastructure which is duplicated in receiving areas. Wage flexibility, on the other hand, could and should be increased. Real wage levels which are incompatible with the demand for labour create unemployment both regionally and nationally. Regional differentials in wage rates have in fact tended to narrow over

the past ten years and reverse differentials (e.g. wages high in areas of high unemployment) have been observed.

9 The current pattern of unemployment rates by standard region is set out in Annex C, which also shows how the relative positions of the regions have changed over the past ten years. This does not tell the whole story, since the standard regions have no particular economic validity, and "regional problems" may exist at sub-regional level.

10 Council noted, when they last discussed the subject, that the nature of the regional problem had changed in recent years. It is now seen more as a problem associated with certain conurbations. The interaction of regional industrial policy with urban policy therefore needs to be carefully integrated. The Urban Programme, administered in England by DoE and in Scotland and Wales by the respective Secretaries of State, comprises both social/environmental measures and economic measures which are directed at stimulating the local economy, chiefly by the provision of industrial sites and buildings. The problems of remote rural areas, sparse in population, require separate and different treatment.

11 Although the regional problem is now more closely associated with certain conurbations than hitherto, it is still striking that the main areas on which regional policy has been focussed for the last 50 years have not overcome their long-term problems of unemployment and adverse industrial structures. This emphasizes the need to ensure that the instruments of regional policy are effective in stimulating self-sustaining economic activity in those areas.

12 The current review of regional economic policy is made against this background.

13 The Regional Development Grant (RDG) scheme has been criticised in particular for not being job related and for over-concentration on manufacturing industry, a criticism which has force in cases in which large amounts of grant have been paid to highly capital intensive projects that have created few jobs and would probably have gone ahead in the same location without assistance.

14 We give due weight to those considerations, but the predictability of the present scheme has its advantages in influencing firms' investment decisions. In addition grants linked to capital investment can encourage improved competitiveness.

15 The argument that assistance should not be confined to manufacturing activities alone also has weight, and we recognise the importance of the service industry. But regional incentives have no relevance to service activities which compete mainly for local customers or whose location is determined predominantly by local factors.

16 The present AAs map is open to criticism on the grounds that many non-Assisted Areas have rates of unemployment above the

average for the present Development Areas. The present map certainly does not reflect the current distribution of unemployment - and its revision is under consideration. Unemployment is not of course the only criterion of need and areas should not be designated solely on grounds of unemployment rates which may be transient.

17 The extent of map coverage requires careful judgement. In the belief that a significant increase in map coverage would only dilute the effectiveness of assistance our policy has concentrated on the areas of most need. It may be argued that differential rates of automatic grant (in SDAs and DAs) help focus assistance on the areas of most need, but equally, a single inner tier would be both simpler and avoid overfine distinctions of degrees of need.

18 We do not consider that the creation of new agencies would improve the administration of regional policy although we recognise the need to improve the co-ordination of all those involved. In particular we have taken steps to minimise overlap or conflict between urban policy measures and regional industrial assistance.

19 The need is to develop a regional policy taking account of valid criticisms of the present instruments and map, and of developments over the decade since policy was last substantially revised. Regional policy must work to improve industrial competitiveness, and it must be cost-effective. Its main aim must be to reduce regional disparities in employment opportunities by improving the performance of the regional economies without causing net harm to that of the national economy, or merely transferring problems at taxpayers' expense.

20 This paper outlines some of the thinking in our approach to a future regional policy. We invite Council's views on that thinking. Council members might like to comment in particular on the following questions:

- (1) What action can be taken to encourage labour markets to adjust fully?

How much might geographically pay variations help to increase employment in disadvantaged areas? How can the CBI and TUC help labour markets to adjust more fully?

- (2) What should be the characteristics of a system of regional investment incentives?

Expenditure on regional development grants is currently some four times greater than that on regional selective assistance. Is this balance right or should the proportion spent on an automatic grants scheme be

smaller? Towards which sectors of industry should investment incentives be primarily directed? To what extent should the assistance be linked to the job effects of investment?

- (3) To what extent should the impact of regional assistance be concentrated on areas most in need?

At present nearly 9 per cent of the working population live in Development Areas and another 13 per cent in Special Development Areas. Should the main instruments be focussed more on the areas of greatest need, or should a wide spread of assistance be considered?

N T

REGIONAL ECONOMIC POLICY
INSTRUMENTS IN GREAT BRITAIN

The Assisted Areas

1 Regional aid is available in Assisted Areas - the Special Development (SDA), Development (DA) and Intermediate Areas (IA). In defining these areas the Secretary of State is required by the Industrial Development Act 1982 to "have regard to all the circumstances actual and expected; including the state of employment and unemployment, population changes, migration and the objectives of regional policies". The present Government have pursued a policy of concentrating aid on areas of greatest need and have had most regard to the balance between two criteria, unemployment and location. With a few exceptions Assisted Areas are defined in terms of Travel to Work Areas. The present Assisted Area map is appended to this Annex.

Regional Development Grant (RDG)

2 RDG is an automatic grant payable at 22% in Special Development Areas (SDAs) and 15% in Development Areas (DAs) towards capital expenditure incurred in providing - :

- (i) New buildings or works (other than mining works) and adaptations of existing buildings, on premises used wholly or mainly for qualifying activities in SDAs and DAs.
- (ii) New machinery or plant for use in such premises.

3 The qualifying activities are the manufacturing activities described in Orders III - XIX of the Standard Industrial Classification (SIC) 1968, together with certain repair activities, the processing of scrap and waste materials and scientific research relating to any other qualifying activities. Grant is not paid on items of plant and machinery costing less than £1,000 (reduced to £500 for assets provided on small premises employing less than 100 people). Grant is not paid on schemes of buildings or works costing less than £5,000. In the case of buildings, grant may be paid to whoever provides the building, which may be the occupier or the developer, including local authorities and new town development corporations. In the case of plant and machinery, grant is paid to the provider including the provider of an asset for hire on qualifying premises.

4 RDG is claimed retrospectively on expenditure incurred or defrayed and it is tax-free. The scheme is administered through the Regional Development Grant Offices of the Department of Trade and Industry.

Regional Selective Financial Assistance (RSA)

5 RSA can be made available under Section 7 of the Industrial Development Act 1982 to encourage industrial and commercial projects which have good prospects of viability and which will improve employment prospects in the Assisted Areas (including the Intermediate Areas). RSA is available in addition to RDG in DAs and SDAs. To qualify for assistance towards capital expenditure (normally for manufacturing projects) the applicant must show that there is an employment benefit, and that it seems likely to strengthen the regional and national economies, (the efficiency criterion) and that assistance is necessary for the project to go ahead (either at all or in the form or on the timescale proposed) i.e. that the project is "additional".

6 Manufacturing projects initially fall into two broad categories.

- A - new projects and expansions which create additional employment
- B - projects, e.g. for modernisation or rationalisation, which maintain or safeguard existing jobs.

Assistance is normally provided in the form of a grant towards fixed capital expenditure, paid in (normally annual) instalments related to the defrayal of the expenditure. Very exceptionally assistance may be given to meet cash flow requirements. Grants are discretionary and are negotiated as the minimum necessary to bring about the benefits associated with the project. While working capital costs do not attract assistance they are taken into account in deciding what is the "minimum necessary". RSA is administered by the Department of Trade and Industry and the Scottish and Welsh Offices for their respective areas.

7 Exchange Risk Cover on medium term foreign currency loans at favourable fixed interest rates from the European Investment Bank or the European Coal and Steel Community. Under this scheme the borrower takes on only a sterling liability; the Government carries the exchange risk in return for a premium calculated as a percentage of the outstanding principal of the loan.

8 The In-Plant Training Scheme is operated as a self-contained scheme under Section 7. Under the scheme assistance is available where training is an essential part of a project which qualifies for S7 support. The grant covers 40% of eligible costs - the wages of trainees and instructors plus the net cost of materials - and attracts a matching 40% assistance from the European Social Fund (ESF).

9 The Office and Service Industries Scheme (OSIS) is a discrete scheme operated under Section 7, offering selective grants to encourage office and service industry projects which would not otherwise go ahead in the Assisted Areas. Primarily the eligible industries are those in Orders XXII to XXVII of the SIC, which includes transport and communications; distributive trades; insurance, banking, finance and business services; professional and scientific services; and others. The normal Section 7 criteria (paragraph 5 above) must be met, except that, it is not normally necessary to demonstrate that projects will strengthen the national economy. Until the mainstream S7 scheme grant is not related to capital expenditure but simply to the number of jobs created. Assistance cannot be given for job preservation. It is further restricted to projects which serve wider than local markets or which serve manufacturing industry.

10 Forms of OSIS Assistance:-

- (i) a negotiable grant to the employer for each job created subject to maxima of £8,000 per job in SDA, £5,000 in DA's and £2,500 in IA's.
- (ii) a fixed grant of £2,000 tax-free for essential employees moving with their work for not more than 30% of the jobs created at the new location.

11 RSA can take just one of the forms outlined above, or it can be negotiated as a package (although OSIS and mainstream project grant cannot normally be combined). The total package must amount to no more than the minimum necessary, and is contained by internal and EC limits.

Advance Factories

12 Advance factories are provided in Assisted Areas in England and in Rural Special Investment and other areas (on behalf of the Development Commission) by English Industrial Estates (EIE), in Scotland by the SDA and HIDB and in Wales by the WDA and DBRW. Letting policies follow normal commercial practice and, except in special circumstances, investments are expected to show minimum rate of return on gross rental. Rent-free periods are available at discretion; such assistance will be taken into account in any associated RSA.

Contracts Preference Scheme

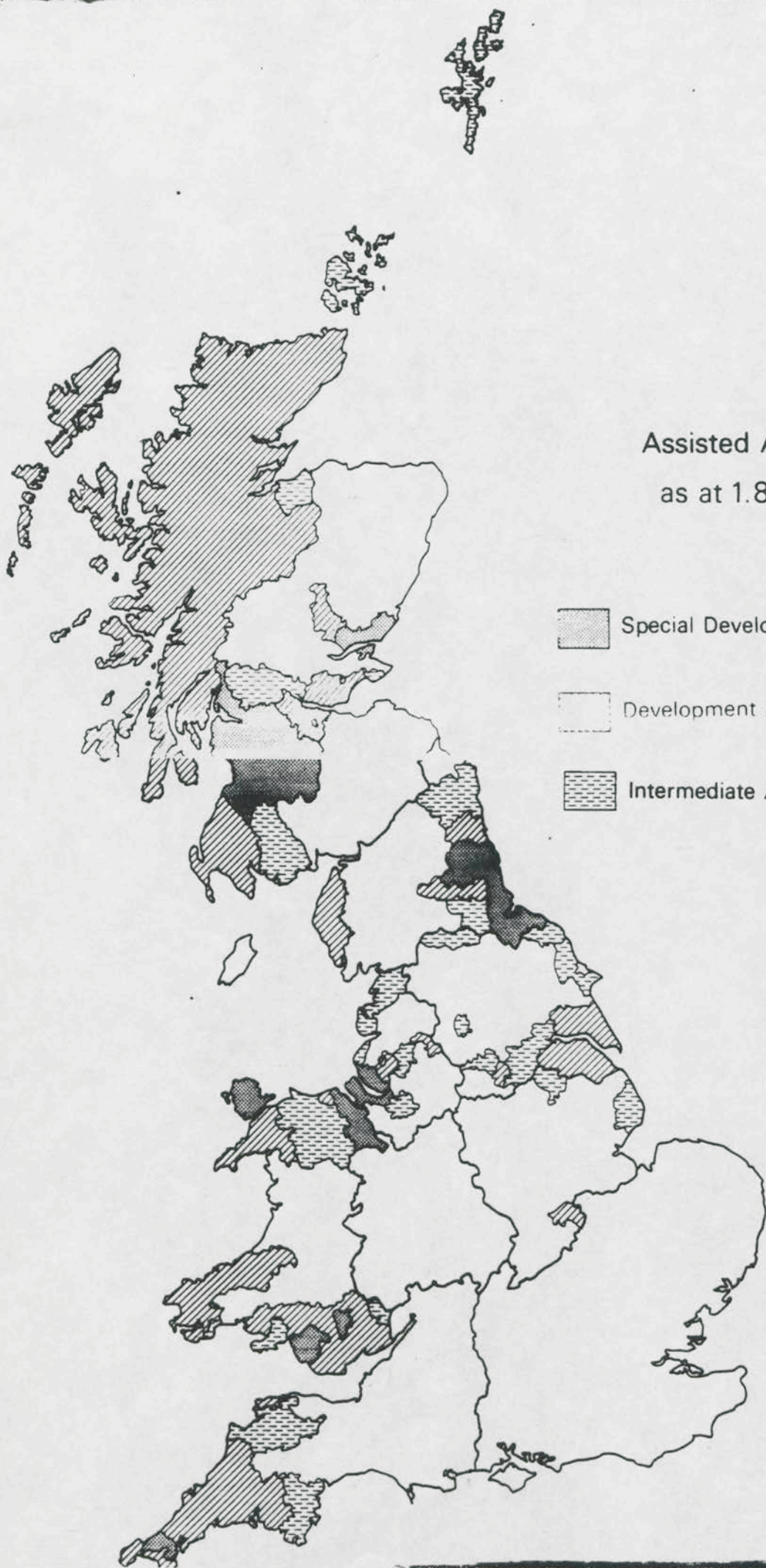
13 Government Departments, nationalised industries and other bodies will place contracts with firms in SDAs and DAs in preference to those elsewhere provided that all other considerations are equal.

Other Regional Industrial Aid




14 The SDA, WDA, HIDB have powers to make equity investments in industry in their areas; in England their power resides in the regional role of BTG. HIDB and DBRW can also provide grant aid. Loans at commercial or concessionary rates for small rural firms are available from the SDA, WDA, HIDB, DBRW and CoSIRA. Small firms advisory services are provided by all these bodies and nationally the DTI Small Firms Service.

Derelict Land (Clearance)

15 Local authorities in England are eligible for grants of 100% of the approved cost of reclaiming derelict land in the Assisted Areas and Derelict Land Clearance Areas (DLCAs). Elsewhere in England the grant is available at 50%. Individuals, companies, public utilities and nationalised industries in the AAs and DLCAs are also eligible for grant of 80% of the approved cost. EIE are eligible for 100% grant in the AAs. Derelict land clearance in Scotland is carried out directly by SDA; in Wales the WDA uses local authorities as its agents.



Assisted Areas
as at 1.8.82

-  Special Development Areas
-  Development Areas
-  Intermediate Areas

EXPENDITURE ON MAINSTREAM REP IN GB

£m (1982 Prices)

<u>Main Instruments</u>	<u>75/6</u>	<u>76/7</u>	<u>77/8</u>	<u>78/9</u>	<u>79/80</u>	<u>80/1</u>	<u>81/2</u>	(Outturn) <u>82/3</u>
(a) Regional Development Grants	748	857	707	667	463	589	679	690
(b) Regional Selective Assistance	152	90	81	165	105	85	84	90
(c) Land and Factories in England	60	36	35	42	40	40	40	28
SDA and WDA expenditure on Land and Factories	14	36	58	93	113	128	136	93
Regional Employment Premium	494	456	5	-	-	-	-	-
<hr/> Total for Main Instruments	<hr/> 1469	<hr/> 1475	<hr/> 886	<hr/> 967	<hr/> 721	<hr/> 842	<hr/> 939	<hr/> 901

NOTES

- (1) The Table excludes assistance to Northern Ireland which is treated separately from other regional expenditure. Assistance to Northern Ireland currently totals about £400m per annum. Total UK regional expenditure in 1982/83 was therefore about £1.3bn.
- (2) Both the RDG expenditure and the total for 1982/83 include an exceptional item of about £150m caused by the abolition of the deferment of payment of RDGs introduced in 1979/80. The corresponding figures for 1979/80 are of course lower because of the introduction of that deferment of payment.

UNEMPLOYMENT - REGIONS - SEPTEMBER 1983THOUSANDSEASONALLY ADJUSTED excl school leavers

	Male	Female	All	Change since August	Percentage of all employees		
					Male	Female	All
South East (Greater London)	490.9 (250.4)	203.2 (99.0)	694.1 (394.4)	+ 3.3 (+ 1.1)	11.1 (11.3)	6.3 (6.5)	9.1 (9.3)
East Anglia	51.5	22.0	73.5	+ 0.4	11.8	7.5	10.0
South West	122.3	58.1	180.4	+ 2.6	12.7	8.3	10.8
West Midlands	242.1	92.7	334.8	+ 1.0	17.8	10.3	14.8
East Midlands	127.0	51.4	178.4	+ 1.1	13.4	7.9	11.1
Yorks & Humber	194.4	76.8	271.2	+ 1.1	15.8	9.4	13.3
North West	299.3	114.4	413.7	+ 0.1	18.4	9.9	14.9
North	155.2	56.9	212.1	+ 2.0	19.9	10.9	16.3
Wales	114.5	44.6	159.1	+ 0.4	18.0	10.6	15.1
Scotland	217.0	96.3	313.3	+ 0.3	16.8	10.2	14.0
GREAT BRITAIN	2,017.6	818.7	2,836.3	+ 9.9	14.7	8.5	12.2
Northern Ireland	85.0	31.8	116.8	+ 2.3	26.9	13.2	21.0
UNITED KINGDOM	2,102.6	850.5	2,953.1	+12.2	15.0	8.6	12.4



10 DOWNING STREET

From the Private Secretary

DSG

cc: DES
NIO
D/N
SO
WO
24 October 1983
DOE
DM
WPS

REGIONAL ECONOMIC POLICY: DRAFT NEDC PAPER

The Prime Minister is happy with the paper which your Secretary of State wishes to present to NEDC. She has commented, however, that he should announce the Government's intention to publish a White Paper only if the latter is likely to follow reasonably quickly. She has also noted your Secretary of State's minute of 21 October on the timetable for producing the Assisted Area map. When we spoke on the telephone, we agreed it would be helpful if you could produce a further note drawing together the timetable for announcing the White Paper, publishing it and the tabling of the legislation.

I am copying this letter to those who received yours of 20 October.

MR. A. TURNBULL

Callum McCarthy, Esq.,
Department of Trade and Industry.

JTP



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

24 October 1983

Callum McCarthy Esq
Private Secretary to
the Secretary of State for Trade & Industry
1-19 Victoria Street
LONDON SW1H 0ET

Dear Callum,

REGIONAL ECONOMIC POLICY: DRAFT NEDC PAPER

The Chancellor is quite content with the paper on regional policy which your Secretary of State is proposing to circulate for the NEDC meeting on 2 November, and he hopes that other colleagues will share his view. He feels it is important that the Government should be able to present a united front on this issue at NEDC.

The Chancellor also agrees that the Council meeting provides a good opportunity to make known the Government's intention of publishing a White Paper. It will of course be important to be clear before then about the timing of the revision of the assisted areas map and of legislation so that a clear indication can be given of when the White Paper is likely to issue.

I am copying this letter to those who received yours.

Yours sincerely,

Margaret O'Mara

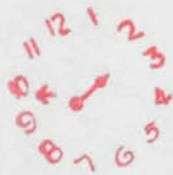
MISS M O'MARA
Private Secretary

NBPM
AT 24/10

gk no

with AT

24 OCT 1983



From: THE PRIVATE SECRETARY



NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

M C McCarthy Esq
Private Secretary to Secretary
Of State for Trade and Industry
Department of Trade and Industry
1-19 Victoria Street
London SW1H 0ET

24 October 1983

Dear Callum

My Secretary of State has seen the paper for NEDC which you circulated with your letter of 20 October to John Kerr. Mr Prior had hoped to be able to attend the Council meeting himself, but is unfortunately not now able to do so. In these circumstances he has asked me to suggest two slight elaborations of the draft paper you circulated, to pick up points which he believes have already been raised in the earlier discussions. The two suggestions are;

- at the end of paragraph 13 add;
"Conversely to have concentrated excessively on labour intensive schemes would have been to risk encouraging the development of industries which could not, in the long term, have been internationally competitive. A key objective of REP must be to attract viable industries which make full use of the new technologies".
- in place of the final sentence of paragraph 16 insert;
"Unemployment is not, of course, the only criterion of need and areas should not be designated solely on grounds of unemployment rates which may be transient - consideration such as structural decline and peripherality are also particularly relevant".

I am copying this letter to John Kerr and those who received copies of your letter of 20 October.

Yours ever

Dave

D A HILL

P.S. As I told you over the phone these have not yet been cleared by Mr Butler, who will be CAM. He will be at the NEDC meeting. I will let you know as soon as they are cleared.

12 JUL 1983



From: THE PRIVATE SECRETARY



NORTHERN IRELAND OFFICE
GREAT GEORGE STREET,
LONDON SW1P 3AJ

M C McCarthy Esq
Private Secretary to Secretary
Of State for Trade and Industry
Department of Trade and Industry
1-19 Victoria Street
London SW1H 0ET

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12 JUL 1983





NBPM
AT 24/10

✓NO

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

M C McCarthy Esq
Private Secretary
Department of Trade and Industry
1-19 Victoria Street
LONDON
SW1H OET

24 October 1983

Dear Calum,

NEDC DISCUSSION ON REGIONAL ECONOMIC POLICY

Thank you for copying to me your letter of 20 October to John Kerr enclosing the final draft of your Secretary of State's paper for the NEDC discussion on 2 November.

My Secretary of State is generally content with the paper as a basis for discussion but would like to suggest three specific changes, as follows:-

1. In paragraph 3, last sentence, amend "minimal" to "reduced". It is accepted that the macro-economic argument is less persuasive at a time of general recession, but to describe it as minimal goes too far.
2. In paragraph 6, the penultimate sentence, "To the extent.....social benefit" seems an oversimplification of a complex issue and could be omitted without affecting the general line of reasoning in the paragraph.
3. In paragraph 17, the reference to a "single inner tier" may not convey much to those not involved in the recent discussions. "A single rate" would be simpler.

I am copying this letter to the recipients of yours.

Yours sincerely,
John Graham

J S GRAHAM
Private Secretary

24 OCT 1983

11 12 1
2 3 4
5 6 7
8 9 10



10 DOWNING STREET

From the Private Secretary

20 October, 1983

NEDC

I wrote to you on 17 October recording the Prime Minister's view that she would be willing, in principle, to chair an NEDC meeting but did not think the suggested date in February was suitable. She has now considered the alternative dates which you put to us and she would be willing to chair the 2 May meeting.

ANDREW TURNBULL

Miss Margaret O'Mara,
H.M. Treasury

K