

Power up Scotland

Scottish Conservative
& Unionist Party

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Foreword

When I stood for leader of this party, I said I wanted to publish a plan for jobs in Scotland within my first month as leader. Today's report makes good on that promise.

This was not an artificial deadline. I set it because we require urgent action on jobs from the government in Scotland to help protect employment and seek out new opportunities for workers and their families.

The UK Government has done its share in this regard over the last few months. Its furlough scheme has supported 900,000 jobs in Scotland. It has loaned £2.3bn to some 65,000 Scottish firms. On top of that, it has provided £6.5bn of funding for the Scottish Government to use, as well as setting out creative ideas like the "Eat Out to Help Out" scheme.

Unfortunately, that sense of ambition has so far been lacking from the Scottish Government. Rather than setting out concrete plans for this autumn, it has seemed happier to revert back to its comfort zone, revelling in grievance and excuses. That won't help firms fill pay packets at the end of November. Ideas and action will.

Under my leadership, the Scottish Conservatives are 100% committed to setting out our own ideas for progress. I'm also 100% convinced that with the right action, and with both our Governments pulling together, there is nothing stopping Scotland from 'building back better'. I hope that this report today prompts the Scottish Government to act. I hope some of our ideas are taken up. If so, I stand ready to work with the government to get them implemented, so we can all help our country in its time of need.

Fundamentally, this report has these core principles at its heart:

We back cooperation, not conflict. Working with the UK Government at this juncture is key to saving jobs. Our constitutional differences are irrelevant. Now is the time to come together around a plan.

We back local, not national. Too much power is centralised in Scotland, and our remote and rural communities are suffering. We want to see control taken out of Edinburgh and handed back to people across our diverse nation.

We back long-term strategy, not short-term fixes. All crises provide an opportunity, now is the right moment for government to set a course for the next 10-20 years so we can truly build back better.

In just eight months' time, Scots will elect MSPs for the next Scottish Parliament. It's then that we'll decide our country's path for the next 5 years. As we seek to recover in the wake of the pandemic, I am clear about what our priorities should be. We need a parliament focused on Scotland's urgent needs. We need a parliament that champions action on jobs – with ideas on how we boost Scottish productivity, sell Scotland to the world, support our diverse regions and remote areas, and rebuild our country together. That's the positive debate we need in Scotland – not another five years on constitutional division.

This report sets out how we want to contribute to that positive debate. We publish it today in the hope it will stimulate real progress on how to take Scotland forward – and power up our nation in the years to come.

Douglas Ross
Leader of the Scottish Conservative and Unionist Party



How this report was compiled

This report is a Scottish Conservative paper prepared in response to the Coronavirus crisis, and prior to the end of the furlough scheme in October. It draws on advice and analysis from the Scottish Future Growth Council, chaired by Lord Dunlop, which was set up by the Scottish Conservatives in 2018 to advise the party on ways to boost productivity in the Scottish economy. The Council has taken extensive evidence over the last two years from business groups and third sector bodies. We would like to offer our thanks both to the Council and to consultees for contributing to the findings in this report.

Introduction

The Coronavirus pandemic has created an unprecedented economic crisis for nations right across the world. But some countries went into it better prepared than others. In Scotland, too much focus has been spent over the last decade not on a national project of economic renewal but on a nationalist plan to take Scotland out of the UK. That lack of focus is now costing us dearly. The Coronavirus pandemic shows the perils of failing to prepare – and the lesson as we begin to prepare for its aftermath is that we must now – all of us – focus entirely on making up for lost time.

The immediate priority is to protect jobs this autumn by helping businesses survive, and adapting our economy to living with the virus. Government must then rebuild for the long-term too. We must understand upcoming economic changes, such as changes in supply chains across the globe. We must tackle long-term failings in Scotland on productivity, skills, research, infrastructure and management. And we should redraw the way government enterprise support works so power is taken out of central government and pushed out to our regions. In short, we want to take power out of the hands of Ministers in Edinburgh and put power back in the hands of the people and communities of Scotland.

Our plan for jobs

Our plan is divided into 3 parts:

Part 1 assesses the SNP's record and sets out the key policy failures that have stymied Scottish growth.

Part 2 assesses the challenge Scotland faces as a consequence of the Coronavirus crisis.

Part 3 sets out our overall strategy for action and our recommendations.

Our key recommendations

We have divided our recommendations into two parts: policies for the emergency Coronavirus response, and long-term strategic plans for the future.

Emergency measures – within the next 12 months

Create new Scottish Job Security Councils.

Operating already in Sweden, the government would set up sector-based job councils in key Scottish industries around the country – such as oil and gas – to match laid-off workers with new jobs – to complement the work of existing Job Centres.

A hardship support fund for businesses.

A Government fund directed towards firms facing localised lockdowns, replicating the cash support they receive from furlough.

A town centre rescue plan. We need immediate measures to support our town centres with planning restrictions freed up and a new town centre adaptation fund.

Community “Right to Buy” schemes. If key employers in fragile areas face bankruptcy – for example local pubs – give first refusal to community and management buy outs.

A “Scotland First” procurement strategy.

As we leave the EU, it is time for government procurement to favour local businesses.

New Rural Growth deals. To arrest the growing gap between urban and rural economic activity, government should prioritise support for rural areas and smaller towns.

Longer term strategic goals

Boost Scotland’s “export” network both to wider UK and abroad. Create a network of trade offices elsewhere in the UK, an export mentorship scheme, and a turbocharged GlobalScot network.

To redraw government support, actions over the next 2 years include:

Reform Scottish Enterprise. Scotland’s main enterprise network should be aligned with City and Regional Deal areas, to better reflect Scotland’s distinct regional challenges.

Improve skills provision. We should give a new Scottish education guarantee to age 18, increasing diversity in vocational education provision, a huge expansion of adult learning, and a review of the Apprenticeship Levy.

Boost research. We want a new R+D target for Scotland, with better incentives for spin-out companies from universities, and new innovation funding.

Massive acceleration of infrastructure. With a new infrastructure body for Scotland, and a joint vehicle for the UK and Scottish Governments co-investment, we should press ahead with major new projects – with long-term plans including a 3 lane M8 and faster rail connections from the central belt to Aberdeen and Inverness.



Part 1: Tackling the SNP's low growth Scotland

Scotland's long-term low growth problem

When the SNP came to power 13 years ago in 2007, Scotland's economic growth was broadly in line with long-term trends. Scotland's GDP had grown by 2.6 per cent during 2006, keeping pace with the UK's GDP growth of 2.7 per cent throughout that year.¹ By midway through 2008, it was becoming apparent that Scotland's economy was slowing. In 2007, GDP grew by 2.2 per cent across the year, 0.5 per cent down on the year before. Across the UK as a whole, the economic picture was rather different as GDP increased by 2.9 per cent throughout the year.²

When the financial crisis hit, Scotland's economy, along with the rest of the Western world, slowed significantly. GDP, in 2008, grew by only 0.5 per cent in year and shrank by 1.7 per cent in the final quarter of the year. At the peak of the 2008-09 recession, Scotland's economy was falling farther and faster than that of the UK as a whole. GDP in Scotland fell by 4.8 per cent in 2009 whereas in the UK as a whole, the fall was slightly less at 4.6 per cent. As the year neared its end, the UK economy started growing again; by 0.4 per cent in the final quarter. Scotland too saw growth at the end of 2009 but only by 0.2 per cent.³

As the fog of the recession caused by the financial crisis began to lift, Scotland's recovery was demonstrably sluggish. In 2010 the UK economy as a whole grew by 1.4 per cent, whereas in Scotland GDP was only growing at 0.8 per cent.⁴

Scotland continued to trail the UK economy as a whole throughout the 2011 – 2016 Scottish Parliamentary term. At the end of 2014, after the independence referendum, Scotland's GDP growth was significantly higher than previous years at 2.7 per cent. But this was still 0.8 per cent behind the rest of the UK.⁵

Since 2016, it is not only GDP growth that has been sluggish. Business growth has also fallen behind the UK as a whole as well as the other home nations. Between 2017 and 2019, the number of businesses in Scotland grew by only 1.4 per cent compared to 1.9 per cent for the UK as a whole, 1.7 per cent in England, 3.3 per cent in Wales and 5.4 per cent in Northern Ireland.

Job creation statistics suggest a similar story. In Scotland, from the second quarter of 2007 to the end of 2019, the number of jobs grew by 4.9 per cent; the lowest of any nation in the UK and only a third of England. In Wales the number of jobs grew by 8.1 per cent over the period, while in Northern Ireland the number of jobs grew by 10.2 per cent. If Scotland had matched the UK wide growth rate of 10.2 per cent, there could have been an extra 261,000 jobs in Scotland's economy by the end of 2019.⁶

The final budgetary forecasts issued by the SFC and OBR, in February and March 2020 respectively, before the pandemic began, again highlighted that despite a general slowdown in both economies, Scotland was forecast to underperform. The SFC predicted only 1.0 per cent growth in 2020 compared to OBR forecasts for the UK as a whole that predicted 1.1 per cent.⁷

Both the SFC and OBR forecast a continued gap over the next few years until 2023. The SFC forecast Scottish growth of 1.1 per cent in 2021 and 1.2 per cent in 2022 and 2023, whereas the OBR forecast UK GDP growth of 1.8 per cent in 2021, 1.5 per cent in 2022 and 1.3 per cent in 2023.⁸

It is important to highlight that the most recent forecasts were made *before* the realities of the looming pandemic became clear, but the figures do continue to paint the same picture; that Scotland's economy has been stuck in second gear for some years.

Responsibility for this lost decade rests firmly with the SNP Government. It has been in office now for 13 years. As we will show, their time in office has been a missed opportunity, characterised by a lack of focus, strategic uncertainty, and a failure to deliver. It is not in the interests of the SNP to make devolution within the United Kingdom work for Scotland – this would only damage their ultimate goal of breaking up the UK. There has been a real cost to this for Scotland.

The core failings of SNP economic policy

Why has the SNP failed and allowed Scotland to fall behind relative to the rest of the UK – when all of the external factors affecting us, like the impact of the 2008-09 recession, apply equally across the whole country?

There are some external factors out with government control. The oil price peaked in 2014, and given the importance of the North Sea to the Scottish economy, this has had a chilling effect. It has exposed the false promises of the SNP during the referendum campaign for the deception it always was.

But these external factors are not the full story. SNP policy on economic development, tax, and investment has played a central role. And their failures in all these areas have stymied Scottish growth. The lack of imagination and ambition shown in the wake of the Coronavirus pandemic is not a one-off – it is the end result of a decade where the SNP has been asleep at the wheel of the Scottish economy.

We would pick out three key structural reasons as to why the SNP has failed Scotland on jobs and the economy:

SNP policy has over-centralised Scotland

SNP policy has, as a rule, centralised:

- Colleges were merged in 2015-16. A network of colleges was replaced with a structure effectively managed centrally, with fewer, larger colleges.
- Highlands and Islands Enterprise has a long-established reputation as an economic

agency that understands its geography and population. However, other than the new South of Scotland Enterprise, almost all enterprise policy is run from Edinburgh.

- Infrastructure decisions are taken by central government.
- Councils have limited economic development powers.

In recent years, only the City Deals represent a meaningful attempt to drive growth at a local level. But this was a UK Government initiative, which the SNP only reluctantly engaged in.

Hoarding power to itself with the aim of controlling Scotland's public landscape may have helped the SNP's political project, but it has been to the detriment of Scottish growth.

SNP policy has led to cluttered and unfocused thinking on economic development

Speak to job creators in Scotland, and there is a general consensus: the SNP Government, particularly under First Minister Nicola Sturgeon, has no strategic sense of direction. The SNP Government proposes multiple ends, without any sense of prioritisation (apart from – as the previous section suggested – drawing power to itself). The end result of this is confusion.

More than a decade after the SNP entered office the Fraser of Allander Institute at Strathclyde University published a commentary which noted the 'proliferation of strategies, advisory groups and discussion forums' and argued it was damaging economic growth. The FAI concluded that: 'Strategies and advisory groups are no substitute for good policy delivery based on evidence, data and impact.'⁹

Business leaders continually speak of the lack of cohesion in our economic development system. This can mean a lack of cohesion **between the various enterprise agencies**, a lack of cooperation **across the public, private and voluntary sectors** as well as a disconnect **between different levels of government and agencies** (national, regional, local).



The CBI, for example, notes that “to many firms, the support landscape appears cluttered and unclear – trade support services include Scottish Enterprise, Scottish Development International, DIT, and UK Export Finance.” Other conversations we had corroborated this view, particularly highlighting the disconnect between Business Gateway and Scottish Enterprise.

Overall, the size and complexity of the enterprise support framework across Scotland is remarkable and there are clear gains to be made from a significant simplification of the landscape.

SNP policy has driven away investment both through its use of devolved taxes, and the continuing fact of constitutional uncertainty

The devolution of tax powers to Holyrood was an opportunity for the Scottish Government to set out an ambitious and competitive message about Scotland. Scotland’s budget and public services could have benefitted from increased resources brought about by the pursuit of successful pro-growth policies. Instead, the SNP has used those powers purely as a tool to demonstrate political differentiation with the rest of the United Kingdom. It is tax policy that is neither progressive nor regressive, but essentially nationalist in nature. Given the opportunity Scotland had to set an open, pro-jobs agenda following the implementation of the Scotland Act, handing huge new power to the Scottish Parliament, this is a matter of deep regret – and the price has been paid in fewer job opportunities for Scots.

Equally, the continuing uncertainty over Scotland’s constitutional future leads to real-time damage on the Scottish economy. Investment decisions are being either put off or cancelled because of investor concern about the potential cost of separation. Consequently, Scotland is losing out to other nations and regions of the United Kingdom which are able to offer constitutional stability.

Fundamentally, Scotland under the SNP has deprioritised growth and economic development, and made it a tool in its constitutional agenda. Centralisation, the lack of strategic focus, and the deterrent effect of constitutional uncertainty are not accidents: they are a function of having a government in charge which is less interested in jobs than in its own political project.

This is the cost of the SNP.

Scotland’s missed opportunities – the productivity gap

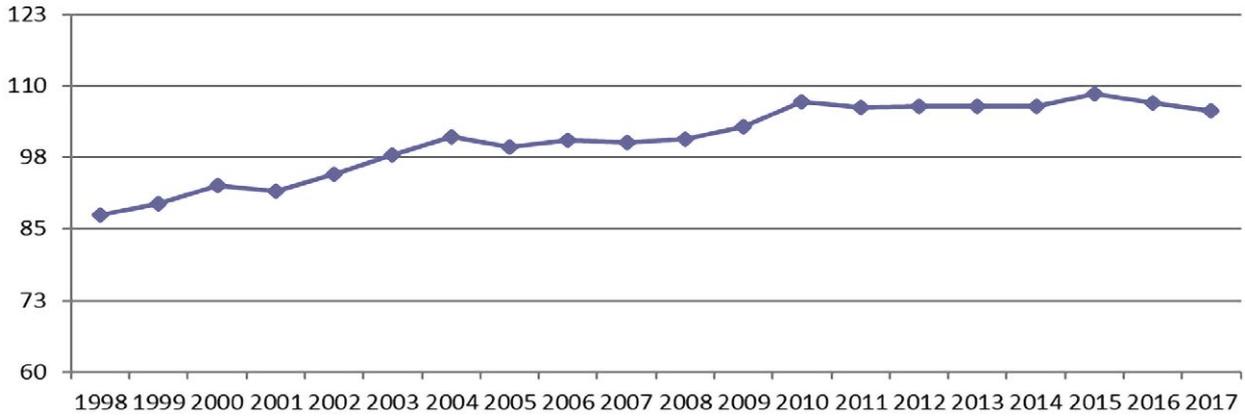
The lack of focus and competence on the economy has meant that the SNP – and the wider political debate in Scotland – has largely ignored the core weaknesses within Scotland’s economy. These challenges pre-date Covid and will still be there once the virus has been beaten. We argue that we must focus back on these weaknesses because all efforts to “build back better” hang on our ability to combat them.

What are they?

The key weakness we identify in this report is Scotland’s low productivity – the economic output we create per employee. The higher the output the higher the profit: meaning increased wages or more jobs. Increasing productivity, therefore, is not an end in and of itself. Increasing productivity can (and should) mean increasing economic growth, but also higher living standards.

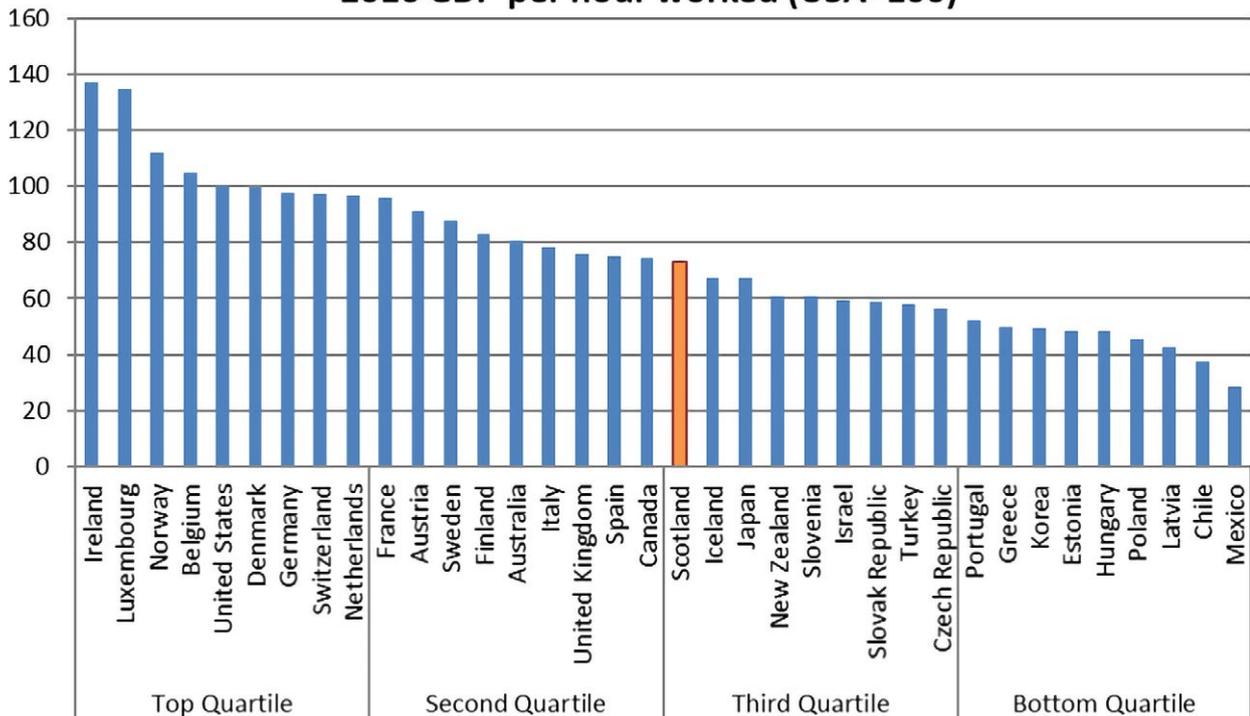
The labour productivity picture in Scotland since the SNP took power in 2007 has been poor. Scottish growth following the financial crisis has been subdued.

Real output per hour (2007=100)

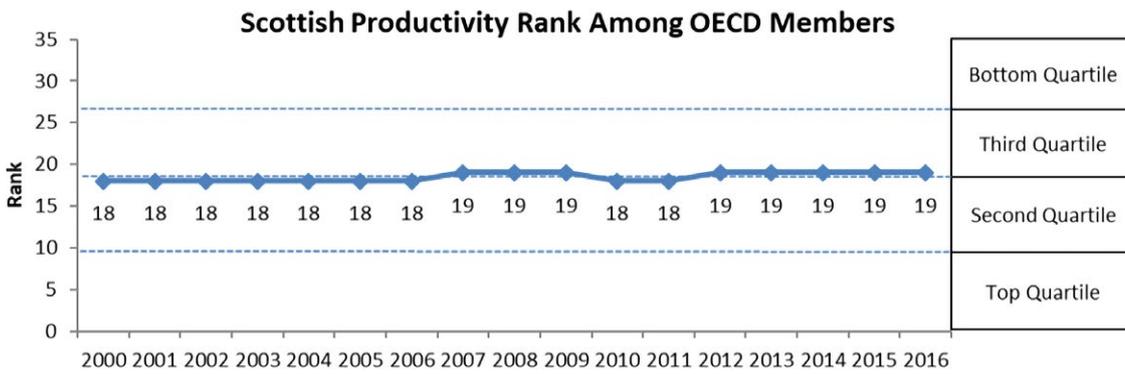


In 2007, the Scottish Government set a target to be in the top quartile of OECD countries for productivity by 2017. The latest figures show that not only does Scotland remain around the middle of the OECD productivity table, the gap between the top quartile and Scotland's position has not closed at all since 2000.

2016 GDP per hour worked (USA=100)

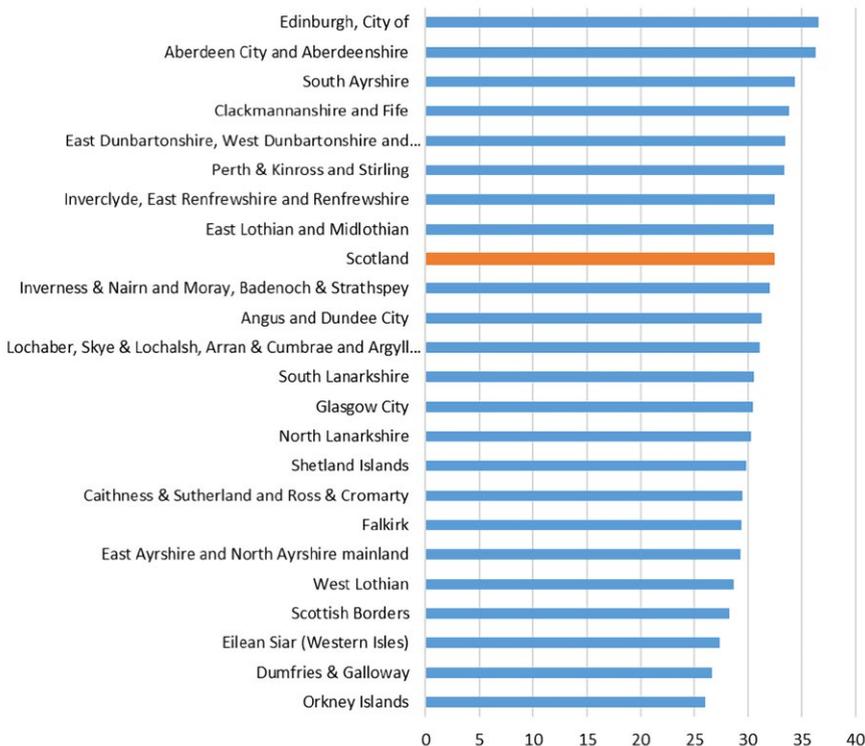


Understanding differences within Scotland



The table shows that the UK’s productivity record is only marginally better – but given the extra public spending per head, particularly on economic development, Scotland should be doing better. Just as bad, the figures show that – within Scotland – regional variance on productivity is significant. CBI Scotland, in their *Pursuing Prosperity* publication, found that the most productive local authority area in Scotland is 50% more productive than the least productive local authority area.”¹⁰ The difference is 43% when we only look at mainland local authorities. What is most concerning though is that the difference between regions in Scotland is among the largest compared to other intra-regional differences in the rest of the UK¹¹.

GVA per hour worked (£) - 2016



There is a reason for this. Looking at the drivers of productivity, some of the reasons between the large variance can be attributed to the differences in levels of connectivity, innovation and skills between rural and urban areas, as well as the pattern of employment in sectors that differ in productivity – for example, financial services based in Edinburgh or the oil and gas sector in the North East.

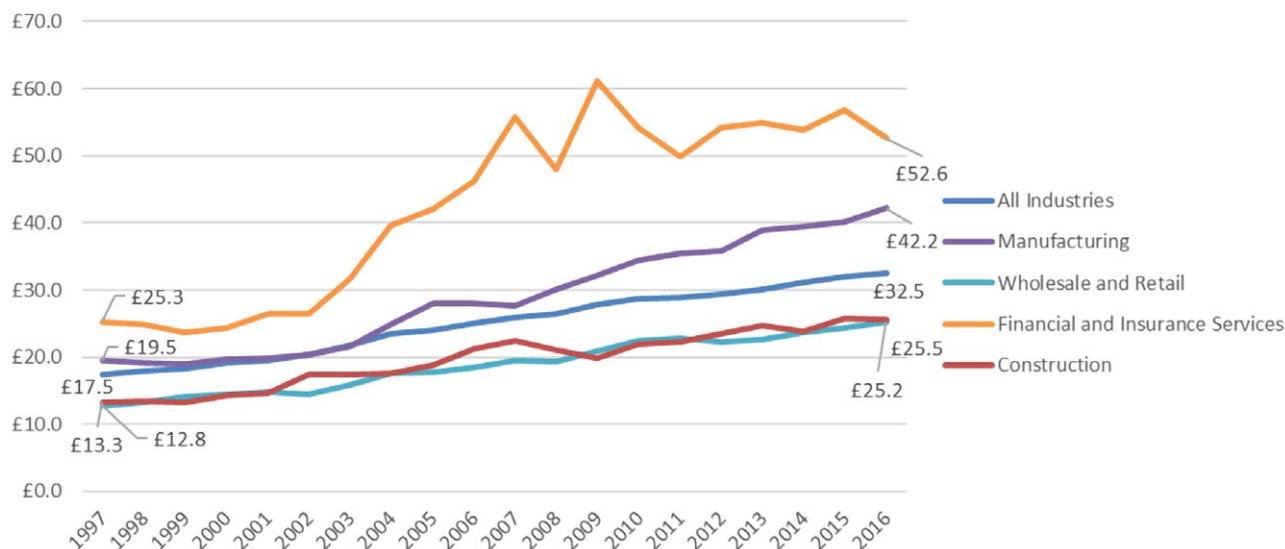
It is this difference between sectors and the changes in the patterns of employment within sectors that account for the recent productivity performance in Scotland. The David Hume Institute, in their *Wealth of the Nation* publication, concluded that:

“Between 1997-2017, employment growth has skewed away from Scotland’s most productive sectors, the financial and manufacturing industries. As a result, many Scottish jobs are now concentrated in “less knowledge-intensive” services and “low-medium tech” manufacturing firms, which happen to be less productive”¹²

The DHI goes on to say that while this pattern is the same in the UK as a whole, it is more pronounced in Scotland.

The table below shows how labour productivity differs amongst selected industries in Scotland. It follows that a drop in manufacturing employment, coinciding with a spike in retail employment will negatively impact national labour productivity¹³.

Output per hour worked in selected industries (£)



The solution

We believe that in order to tackle the productivity issue in Scotland, we need to not only look at national targets and policy, but work with businesses to address regional differences in performance, work with sectoral productivity leaders, and take steps to improve productivity on an individual business level.

Some of our most successful industries are demarcated regionally. Oil and gas in the North East, whisky in the Highlands and Islands or financial services in Edinburgh and Glasgow. Tourism, while a Scotland-wide industry, different regions cater to different kinds of tourist – hiking in the Highlands, skiing in the Cairngorms, fishing in Aberdeenshire, music and sport in Glasgow or history in Edinburgh. We see merit in encouraging regions to take the lead in economic development, driving innovation through competition and thus, in turn, support some of our most productive industries.

In summary, productivity has been one of the chronic weaknesses of the Scottish economy, even before the pandemic. High productivity underpins wage growth and more secure incomes for working people. Improving productivity is important – but given the importance of differences within Scotland, it should not be a single, national approach that ignores major differences in the Scottish economy: it should understand major regional and sectoral differences, and understand the importance of improvements within each company.

We need a government in Scotland which is focused on delivering this goal.

This requires a focus on:

- Freeing up our regions from national control
- Boosting research and development
- Upskilling people so they can enjoy more fulfilling work, and have more productive careers
- Connecting Scotland better

Over 13 years, the SNP has shown itself utterly inadequate to the task.



Part 2: The Coronavirus and the Scottish economy

Part 1 focused on the failures of the SNP's economic policy and the core long-term challenges facing Scotland. But the Coronavirus pandemic has now created a new reality for us to confront. We cannot rebuild our economy unless we are clear-sighted about the unique problems the virus causes, the way it changes economic activity, and the new demands it places on policymakers.

The Pandemic as a natural disaster

We should start by understanding that **the pandemic has not created a normal recession:**

- The pandemic forced the entire economy to be locked down. Normal market incentives were completely disrupted. The survival of a business was not linked to its underlying viability before lockdown, but to its exposure to public health restrictions and consumer responses to the coronavirus. In this sense, the virus is more like a natural disaster than a recession: an immediate, unexpected shock that affects everything.
- The first priority has been to support the economy through what has been a period of suspended animation – which is what the various grant, loan and furlough schemes are designed to achieve. **The immediate aim has been to preserve as much of the economy as possible, so that growth can resume when public health permits it.** The usual debate over deficits and debt has been entirely absent. Everyone accepts that deficit-financed spending is necessary to reduce scarring effects.
- As lockdown eases, the difficulty policymakers face is to understand which businesses are still facing pressure through no fault of their own, and which are capable of finding a new equilibrium in a

changed economy. The challenge becomes calibrating support to allow growth to resume – while understanding that the virus has not yet been defeated.

- We face a particular problem around reduced consumer confidence due to specific health concerns. In a 'normal' recession, governments would often try to stimulate the economy, and put money in people's pockets one way or another, so that they go out and spend: in this situation, many people will not go out and spend unless they feel safe.
- This means that the role of government in Scotland is not just as an economic policymaker: it also shapes what happens through its language, attitude and message. It has a crucial role in creating confidence in Scotland – in its public health processes, and in being a good place to do business.

Understanding the stresses on business

Crucial to our response to the Coronavirus pandemic is an understanding that it will affect some parts of Scotland and some sectors more than others. As this table suggests, **the impact varies hugely.** It presents a policy challenge which is to offer support at each end of the spectrum: grants, write-offs and direct funding to those who simply cannot survive, restructuring for those who face some pressure, through to normal growth capital and finance for those who can access capital and have a brighter future. Understanding these nuances is essential for policy.



Sector: projected Covid19 impact by sector

Sector	Share of UK Economy	OBR initial assessment of loss of output
Agriculture	0.7	0
Mining, energy and water supply	3.4	-20
Manufacturing	10.2	-55
Construction	6.1	-70
Wholesale, retail and motor trades	10.5	-50
Transport and storage	4.2	-35
Accommodation and food services	2.8	-85
Information and communication	6.6	-45
Financial and insurance services	7.2	-5
Real estate	14.0	-20
Professional, scientific and technical activities	7.6	-40
Administrative and support activities	5.1	-40
Public administration and defence	4.9	-20
Education	5.8	-90
Human health and social activities	7.5	50
Other services	3.5	-60

(This table is derived from the OBR's central Coronavirus scenario, published in April. At an early stage in the pandemic, this was necessarily speculative, but it has withstood events relatively well.)

One further point here is notable: even sectors which can continue to operate with social distancing faced a huge drop in income.

This is a reminder again that the virus has second-order effects – the recession which follows lockdown. For an open economy like the UK's, this is going to be an economic challenge which far outlives the first peak of the virus.

The potential for Coronavirus to change economic activity

To further complicate the picture, the coronavirus may fundamentally change economic activity. While there is little point making firm predictions, understanding the scale of possible change as a result of the virus is important. There may be meaningful risks and opportunities for Scottish businesses – and this kind of analysis should play a more direct role in shaping future economic policy.

These changes could include:

Changes to global supply chains

The coronavirus came at a wider point of reflection on trade across the developed world. Politically, after a long period of integration and open trade a backlash emerged. In some places, like the USA, this has taken on an aggressive, isolationist approach. But almost everywhere, there is a renewed understanding that governments must balance the benefits of free trade with targeted support for those it left behind.

In the business world, offshoring has matured from a practice that was seen as purely about cost-cutting, to something that is seen as one tool to be used discerningly. A business function like administration, call centres or IT might have been automatically outsourced 15 or 20 years ago, whereas today, a more sophisticated balance of in-country and off-shore functions is more likely.

Many businesses, particularly those in manufacturing, food and drink, retail and construction are all still heavily reliant on global supply chains. The global context has started to change in the past two years, as a nascent trade war between the USA and China has brewed, and crucial Scottish sectors like whisky and textiles found themselves victim of tariff retaliation between the EU and USA.

These trends meant that even before the Coronavirus, there was a growing mood for reassessing global business links. There was early talk of ‘reshoring’, keeping supply chains short, and a much wider awareness of the geopolitical risks of business abroad.

The point we have to understand is a subtle one. **We might not be able to predict exactly how global supply chains will change as a result of the virus. But almost every established company and almost every country will be looking at its supply chains in a new light and will be trying to manage risks.** The point is that old patterns are being disrupted: there are opportunities for countries which can quickly establish their place in what follows.

Changes to travel and migration

Global travel and migration collapsed as countries across the world closed borders and imposed lockdowns. **There is no knowing what kind of movement patterns will return as restrictions are eased.**

It is possible that the habit of international travel resumes as soon as people feel safe – and that the habits of holidays abroad and regular business travel quickly return. Or, it is possible that concerns over public health mean a permanent reduction in travel, both from and to Scotland.

This could have a severe impact on the Scottish economy, given the importance of tourism and hospitality. At the very least, domestic tourism would need to substantially increase to counteract lost income from international tourism.

Migration also stopped in the short term. Some crucial sectors in Scotland make extensive use of migration: hospitality, care, and agriculture in particular. Some adapted their business models to take account of this, such as campaigns for UK workers to enter agriculture. Others, like some hotels, saw a drop in migration coincide with support through grants. In the mid and long-term though, it is unclear what kind of changes firms might consider, not least as it is unclear when (or even if) migration trends may resume.

There is, however, a significant opportunity to play to Scotland’s strengths. The rest of the UK is already Scotland’s most important tourism market. Within the UK, the relative price of property, the availability of space and shorter commutes than most cities elsewhere in the UK, are all hugely attractive. SNP tax policy and constitutional uncertainty has reduced this attractiveness, but with a virus that requires many people to spend extended periods of time working from home, Scotland’s natural advantages may have new relevance.

Accelerating trends in business tax

Non-domestic rates have been a policy challenge for some time. The shift to online retail over the past ten years has seen a growing gap between firms with physical premises who pay rates, and those who are purely online and do not.

Rates also create a strong incentive for companies to avoid investing in their facilities, as it could lead to an increased rates bill. They take little account of different rents across Scotland and are designed in such a way that ignores any interaction between rents and rates. Revaluations are flashpoints for businesses, and the appeals process is slow. Many businesses outside the central belt feel they pay a disproportionate share of the total.

At the same time, the Scottish Government has become increasingly reliant on unusual accounting practice with rates income to pass its budgets. In two successive years, the Scottish Government has brought forward projected income from NDR to fund immediate spending. This was an increasingly unsustainable practice, even before the virus.

In this light, the Scottish Government’s 2018 Non-Domestic Rates Act represented a missed opportunity to think hard about the future of local business tax.

The Coronavirus may well make delivery-on-demand and online retail even more common. Some firms will face the prospect of paying rates on a premises, when their only income comes from stop-gap online sales.

Most businesses will have to change their premises to allow social distancing. For some businesses, this could create a perverse incentive where investing in their property changes its rateable value.

In short, **the Coronavirus makes the long-standing issues with rates even more obvious.**

Rates are not a tax designed to encourage growth, or reward businesses doing the right thing. A reassessment of business property taxes is now even more urgent.

Changes in the world of work

Recessions often bring about cultural changes in the workplace. After the 2008-09 financial crash, for example, the 'gig economy' of short-term and part-time work accelerated.

We do not yet know how the coronavirus will change perceptions of work: it might be that the enforced lockdown has led many more people to find mini-jobs and informal work to supplement their income. Some may take advantage of lockdown, furlough or redundancy to launch their own businesses. Many firms will now be much more open to working from home and other forms of flexibility. People might, in general, be much more focused on work-life balance.

On the other hand, it might be that the value of large employers who can offer security – and which were more easily reached by public support schemes compared to self-employed people – prompts a shift back towards big firms and long-term roles. Companies may reflect that dispersed teams are only suitable for certain sorts of work – and many workers may even value the reestablishment of workplace routines and culture.

These changes in attitudes are unpredictable, but they may have a big impact on the Scottish economy. A significant value shift in favour of different types of work would change how our economy functions – and how policy should try to encourage an economy of security.

Changes in economic geography

The past 20 years have seen a bifurcated labour market: an increasing gap between the people and places with the skills and connections to take advantage of a small, nimble, services-led economy – and those who without them fell behind.

The importance of correcting some of this was beginning to be understood. Concepts of 'levelling up', 'left behind places' and 'inclusive growth' had entered the mainstream.

The coronavirus has the potential to accelerate these trends. Urban areas are more likely to have services, technology and office jobs in which people can work from home easily. They are easier for delivery companies to serve. Small businesses have a population density of customers in which switching to home delivery is more practical and sustainable.

Rural areas and small towns have some crucial strengths in a pandemic: the attractiveness of isolated housing, the relative ease of social distancing for outdoor businesses, and in many cases a strong, close-knit community used to looking after each other. But tourism is a huge part of the rural economy. Many smaller towns have a handful of major employers which act as an economic anchor – individual factories, hotels, distilleries, transport connections or facilities like a market or processing plant are typical. If that institution cannot operate safely, it has a disproportionate effect on the surrounding area.

This means that as policymakers discuss the economic recovery, it has to be with a sense of geography. Many of the big economic trends cannot be changed, but **the impact on places which already feel economically marginalised can, and should, be a priority.**

Conclusion

At the time of writing, it is impossible to predict which of these effects will be permanent and which will be fleeting. But we can all agree that resuming economic growth as soon as possible is vital. As well as underpinning economic security for families and individuals and financing strong public services, growth is also the difference between paying off the cost of the virus quickly, or slowly; and the long-term effects in taxes being moderate, or severe.

A simple model by the Institute for Government, for example, concluded that ‘crudely, a 0.5% improvement in the UK’s growth capability in the years ahead enables this point to be reached with 2% of GDP less tax rises – a huge amount.’¹⁴

For Scotland, it is the *relative* success of the Scottish economy compared to the rest of the UK that informs its tax revenues, due to the operation of the Fiscal Framework. Our budget is protected from a big UK-wide shock like the coronavirus – the quality of the Scotland-only response by the Scottish Government is the crucial factor in influencing the budgetary impact in Scotland. Establishing a good growth trajectory is essential for public service funding over the next decade.

As noted above, economic debate over the past ten years has taken place in a context of low unemployment and underwhelming productivity. The financial crash of 2008-09 did not, in relative terms, lead to high unemployment – while in the years since, unemployment has fallen to record low levels. Median wage growth, however, remained broadly flat, and productivity growth emerged as a chronic weakness. These successes and failures reflect the merits and costs of the UK’s labour market model: a fiercely competitive, immensely adaptive, flexible system that permits swift job flows to emerging and new industries, but has lacked the combination of state-led and private-sector led efforts to drive productivity increases over the long-term.

Unemployment is now spiking. Productivity is not, in itself, a priority for companies who are trying to survive. But they may well be taking actions that make them more productive overall: smarter use of technology, focused use of staff, new distribution channels.

If, over the next 12-18 months, most of the economy can avoid going back into lockdown, and if unemployment and short-term scarring effects are reduced, then productivity will remain a crucial challenge. If the next decade is to build on the last, we will need to capitalise on the job-creating potential of the UK’s labour market model – but with renewed focus on productivity and wage gains across the country.

All of this means that policymakers will need to address both short-term challenges, while also working on much longer-term issues. **We have to focus both on survival and preserving the growth capacity of the Scottish economy – but also start improving our long-term record on productivity, too.** This is a uniquely challenging environment.

Part 3: Our overall strategy and recommendations

So far our report has outlined the failures of SNP control, identified the need to boost productivity over the long-term, and set out the very specific challenges we face in the short-term as a result of the Covid pandemic.

Tacking this will be an enormous challenge. Fundamentally we must end the confusion, centralisation, and strategic drift. We face the task of rebuilding from the virus from this relatively weak position. The first job is to avoid another decade of dithering and lost opportunity.

We want a strong diverse society, all rooted in a growing economy of higher wages which means we can invest in public services. We must now find a path for Scotland that delivers this basic promise.

This is why perhaps the most important economic policy that could benefit Scotland is to put the decade of constitutional uncertainty we have gone through behind us. At the time of writing, the First Minister has once again declared that she proposes to put a second independence referendum in her manifesto next year. That is her prerogative, but the SNP must recognise that actions have consequences. Those consequences are to chain an economic dead weight onto Scotland which will ensure we remain in the same slow-lane that the country has occupied for much of the last decade.

Nothing, therefore, would help Scotland's immediate economic outlook more than the election of a government which took that referendum off the table. It is why the Scottish Conservatives will go into the 2021 Holyrood election on a pledge to put that constitutional uncertainty behind Scotland, so we can rebuild together as a nation. The Coronavirus crisis has only underlined the urgency of that need.

But a strategy which only emphasises the word “No” cannot – and should not – be enough for any political party seeking the trust of voters and businesses over the coming 5 years. That is why the strategy outlined in this paper sets out a detailed and coherent set of recommendations on the way forward for our country.

As outlined in the introduction of this report, that plan must contain both short-term emergency measures that can help Scotland in the immediate term, while also setting a strategic course for the long-term. This is what we seek to do.

Our recommendations are therefore divided into two parts.

Firstly, the emergency and short term measures we believe can be used to support the Scottish economy over the coming 12 to 18 months, as we begin to recover from the impact of the virus.

And **secondly**, the major long term reforms that can reverse the underlying failings of the SNP's decade in power – over-centralisation, confusion and a lack of focus. These measures take advantage of Scotland's existing strengths, developing our exports, accelerating infrastructure and – as identified earlier – boosting Scotland's low productivity.

Our recommendations are therefore as follows.



Recommendations

1. Emergency and short-term measures

Create new Job Security Councils across Scotland

Already operational in Sweden – which has some of the best retraining and re-employment rates in the world – Job Security Councils are agile, sector-specific “Job Centres” where work coaches help to match skills to new job opportunities.

With the expected rise in unemployment over the coming months, we need government to step up efforts to find new jobs, especially for young people. Job Councils in sectors such as oil and gas would help provide quick re-skilling opportunities for people – so that the “Covid Generation” is not left behind.

Hardship support for businesses facing further lockdowns

It looks likely that small, localised lockdowns will be possible, as smaller outbreaks occur even in a wider context of reduced transmission.

The economic impact of this should not be underestimated: even if normal life has otherwise resumed, to place a local economy into lockdown again even for a matter of weeks could be critical for businesses, particularly in rural and fragile economies.

The experience of the first wave is that simple grants are effective and immediate, and avoid the reluctance of small kinds of business to take on debt.

The Scottish Government should therefore develop a hardship support fund for further lockdowns. Where a local lockdown occurs, grants to business should be provided.

Reward public health protection

Rates revaluations take place every three years. They may have an adverse effect on decision-making in small firms: because companies know their rates bill might go up, they may avoid investing in premises.

An economy which manages the virus will require firms of all sizes to make physical changes to their business. At the lower end, this is installing screens or offering antibacterial gel. But some changes will be significant, particularly ventilation, different seating arrangements, changing entrances and exits, new flooring or washing facilities, or facilities like factories or distribution centres having to take up a bigger footprint. Many firms will worry this kind of action could lead to a higher rates bill.

This type of adaptation should be encouraged, not penalised, through the rates regime.

Either a new small fund for adaptation should be created, the next rates revaluation postponed until 2024, or the remit of the assessors should be changed to exclude Coronavirus-specific changes.

We have seen too many businesses fail to receive government support during this crisis because of their rateable value. The previous revaluation continues to hang over many firms and their ability to appeal the revised ratings was slow and bureaucratic. The appeals system must be overhauled to quickly and fairly review all the evidence presented by businesses who have concerns about their rateable value.



Help town centres adapt

The physical layout of many town centres will have to adapt to permit safe trading.

We propose two complementary policies:

- Planning restrictions should be freed up. Pavement cafes, different signage, floor markings and outdoor shelters all have planning implications. Councils are best-placed to judge how to balance the new requirements with preserving the built environment – particularly in sensitive heritage areas. They should be assisted, though, by greater scope to temporarily waive regulations if required.
- A Town Centre Adaptation Fund. Councils could bid for funding for improvements such as:
 - Widening pavements and walking and cycling routes
 - Scrapping car park charges
 - Pop-up park and rides

Better digital support for companies with an E-Commerce Task Force

COVID-19 and social distancing means firms need more support to go digital, and trade online. Our ambition is to make Scotland *the 'E-Commerce Capital of Europe'* by establishing an E-Commerce Task Force involving leading digital teams from Universities, Colleges, the private sector and digital graduates who may otherwise not be able to find employment.

The need for Scotland to rapidly increase the level of online trade and services was apparent before the crisis. According to Nora Senior (Chair of the Scottish Government Strategic Board), only 9% of Scottish firms fully embed digital in their operations, compared to 24 per cent in the rest of the UK and 34 per cent in competitor countries.¹⁵

Building the digital capabilities of small businesses will be critical for the future prosperity of local economies, given the acceleration

in online sales and the potential anxiety of customers to shop locally.

Since the pandemic began, the absence of support to help business go online – and manage not just front-end online sales, but also supply chain, distribution and stock management – has become all the more critical. There are no public agencies in Scotland capable of delivering this online revolution.

As digital sales will become crucial for firms' survival in the next phase of the pandemic, we are calling for the creation of a specialised team (**an 'E-Commerce Task Force'**) to help move 5,000 to 10,000 firms a year online to increase trade with existing and new domestic and export markets.

The FSB has also proposed a peer-to-peer innovation scheme, to help businesses learn from each other and avoid reliance on a handful of expensive consultants to drive digital transformation. We see this as complementary to the taskforce – one option would be for the taskforce to work through local chambers of commerce or Business Improvement Districts, to offer training that then allows businesses to support each other.

For those businesses that have already adapted their business models, the key policy task is to lock in productivity gains: we also see the taskforce as securing and further improving the digital operations of those who have already managed the first transition to e-commerce.

Encourage domestic tourism

Until international tourism resumes, domestic tourism will be vital.

At the minimum, a marketing campaign in the rest of the UK to attract more visitors should be implemented.

Beyond this, a welcoming message from the Scottish Government – instead of talk of borders – is required.

A “Scotland First” procurement plan

Procurement changes may sound like a technical, niche aspect of policy, or something that can wait until the economy has recovered. But the Scottish public sector spends over £11 billion each year buying goods, services and works.¹⁶ The sheer size of this purchasing power is therefore a tool that can be used to achieve various policy ends – including supporting economic recovery from the virus.

Importantly, it does not require any new systems to be set up. All the elements of a better procurement system are there: relatively small tweaks could open up opportunities for smaller firms in Scotland who are on the brink. Procurement should be seen as part of not just building resilience for the long-term, but as a practical, immediate tool to support Scottish firms.

Feedback from business organisations was clear that the **complexity of the system discourages** especially smaller organisations and businesses to enter into and benefit from public sector contracts. The Public Contracts Scotland (PCS) website has made things simpler, but we feel there is still scope to make it more accessible – the design is dated and it could be better categorised.

Another theme that came across strongly was that procurement decisions are often no longer led by a best value approach, but can be predominantly guided by lowest cost. This is understandable, but is not the right strategic approach long-term. Similarly, we have also heard that the procurement system as a whole does not allow for innovative solutions. Procurement contracts are always given out for goods or services, whereas an innovative way would be to procure for solutions to given problems. We believe there is scope for this to be tried in Scotland.

A more specific issue that has been highlighted is that of supply chain payments. Several examples can be found where larger players who win procurement contracts do not meet their obligations to their suppliers. There is no reason why the system could not include a kind of yellow/red card system for late payments which would temporarily ban companies from bidding

for contracts if they do not meet their obligations to SME suppliers.

Better procurement to help firms adapt to the new normal could include:

- **Procurement led by Best Value, not Lowest Cost**

One of the biggest long-term changes we believe needs to happen is a return to seeing public procurement as a tool to achieve the best possible value rather than automatically the lowest cost. This means taking into account broader considerations, including community benefit, SME inclusion or environmental measures. There have been recent attempts to gear the procurement system in this direction, but with very few results from what we can see. Other recommendations broadly linked to this would be:

- **Procurement of Solutions Rather than Goods or Services**

We need to introduce innovation into the procurement system just as much as it needs to be promoted into the economy as a whole. We would like to see public agencies pilot procurements of solutions rather than just goods or services, which would allow creative businesses to come up with an approach rather than a single service.

- **A Personal Approach to Procurement**

We also think that it should be best practice to organise “Meet the Buyers” events for the larger procurement projects, so that contractors can directly develop relationships with the contracting party. This is inspired by London 2012, where direct engagement between “buyers” and “suppliers” was viewed very positively.

- **Improve Public Contracts Scotland**

The PCS website is dated and should be refreshed in line with the unified design of the enterprise agencies we suggest above. It should also be categorised better around value of contracts and sectors to make it easier for businesses to find opportunities relevant to them.



- **A Dedicated SME Portal for the Biggest Projects**

In addition to the updates to the PCS website, we also think there is merit in mirroring the London Olympic approach, where each large-scale infrastructure project should seek to create a dedicated website/portal for interested SME suppliers.

- **A Yellow/Red Card System for Supply Chain Payments**

A card (warning) system should be introduced that would result in companies that fail to pay their supply chains (SMEs) on time being temporarily blacklisted from bidding for public contracts, with the time being increased based on repeat instances.

Use City Deals to help small towns and rural areas

The Coronavirus has the potential to accelerate geographical changes in favour of cities, away from rural areas and small towns.

We believe that the best way of supporting small towns is to see them in geographic context. Some small towns could have a future as commuter towns, or as small service centres – if they had better connections to larger cities. Some have a future as retail and service hubs for the immediate area – if they had investment in their physical infrastructure and local transport links. Some are isolated and have lost major employers, so need new institutions, retraining, or strong public services to support the population. City-regions are at the right spatial level to understand how best to make these choices. Growth deals offer the chance to back up these strategic decisions with cash: so that no place is left behind.

This is the reason growth deals are so important: they place investment at the right level to both boost growth, and ensure every part of Scotland is included.

That focus is even more important after the Coronavirus. Below, we set out a longer-term plan to regionalise enterprise support to follow growth deal boundaries. In the more immediate future, both UK and Scottish Governments should:

- Ensure that governance arrangements for the deals are as robust as possible, balancing clear decision-making with accountability and involvement of all local partners.
- Ensure that Covid-19 does not delay projects, as far as possible.
- Consider growth deal structures for the investment of any further support funding, such as skills funding.

Campaign to get inward migration from the rest of the UK

Scotland has a number of sectors reliant on migration. It is not yet clear when, if at all, international migration flows might resume. But despite the SNP's best efforts, Scotland's attractiveness as a place to live and work is even higher in the pandemic – especially for people in London who work in services, but cannot afford space or large property. There is huge potential to tempt more people from within the UK, even if international migration does not pick up to pre-Covid19 levels.

We should mount a full marketing campaign within the rest of the UK, to encourage more people to move to Scotland.

Community and staff ownership of key economic assets

The priority for small businesses has to be to help as many as possible to survive. We should not plan on the basis of failure.

However, even with support, many small firms will still face difficult conditions. Some will unfortunately become unviable.

There is an existing legal infrastructure in Scotland for communities to take ownership of property in certain circumstances. The intention is to build community resilience and local economies and in general, we believe that the legislation balances these aims with respect for property rights and a dynamic economy.

This provides a potential model for managing key economic assets as the economy finds a new equilibrium.

It is not that the state cannot take ownership of firms. But the record of managing nationalised firms is woeful. The intentions might be good, but the structural issue with government management of companies is that all too often, those good intentions are not realised. The experience of BiFab and Ferguson Marine, for example, is that ultimately communities were left disappointed – and jobs lost – because of mismanagement by central government. Central government in Scotland is also deeply central-belt focused. For places in the South of Scotland, North East and Highlands and Islands, the idea of a major local employer being run from Edinburgh will not be welcomed.

For some smaller towns, there is also the simple challenge of relative scale: central government might find it easy to identify large employers in distress, but some high streets will be damaged by much more granular stresses: individual shops being boarded up, small but socially important businesses failing.

Community ownership, co-operatives and management buy-outs therefore have a role.

We should draw up a set of criteria – possibly in legislation – to identify which firms or economic institutions have an unusually large community presence. This could be a single employer in a remote area, for example, or in small towns, perhaps a big hotel, or even a pub.

If a business in that category expects to file for bankruptcy, then first refusal for purchase from the administrators could be offered to a consortium of local people, staff, or management.

This would not halt the necessary process of new firms emerging, and jobs and capital flowing to higher-growth sectors, as the economy recovers: the criteria would be tightly-defined, and a buy-out would require a hard-headed business plan from potential co-operative owners. The Scottish Government could offer seed funding or loans but otherwise stay out of operational decisions and not take any long-term risk. Many businesses will, ultimately, prove unsustainable even with support, and other support for the individuals and communities affected is still required.

But the potential is there for a model which secures anchor institutions in fragile communities – but avoids businesses being run from Bute House. That is, we believe, a worthwhile aim.

2. Long term strategic goals

Having set out our ideas for the short-term, the recommendations in this final section are for the medium to long term. If we are to “build back better”, then planning for these measures needs to begin now. That way we can be assured that, when the crisis is over, Scotland will be better prepared to take advantage of the clear opportunities that will open up in the post-virus world.

Our strategic recommendations fall under five categories: exports, rebuilding government support, skills, research and development, and infrastructure.

a. Radically expand Scotland’s exporting capacity

By ‘exports’, we mean Scottish firms selling into other places, including the rest of the UK. Scotland has some of the greatest brands and goods on the market anywhere in the world. It is time to sell Scotland to the world.

The potential for growth in Scotland is clearly there. For example, CBI Scotland research¹⁷ found that at least 8% of firms in Scotland have characteristics similar to other firms in their sector that are currently exporting, but do not export themselves. Furthermore, as CBI Scotland note, “some local authorities have a higher proportion of firms that export than others, and this provides another part of the puzzle as to why there are differences in regional productivity.” Lastly, according to the latest Small Business Survey Scotland report, in 2016, 16 per cent of SMEs in Scotland reported that they had sold goods or services outside of the UK in the last 12 months. In the UK as a whole, 18 per cent of SMEs had exported goods or services in the last 12 months.¹⁸

A good example is Enterprise Ireland, the country’s main economic development agency, is continually aware of global trends with rules of

business engagement primarily based around a client's export strategy. If a business is not willing or able to grow outwith the home market, then support (financial or otherwise) is not provided by the national agency. Local authority-led agencies provide support to home-focused businesses.

Another lesson from Ireland is its ability to harness its diaspora. There are an estimated 30 million people around the world who can claim Scottish ancestry. Many first and second generation emigrants maintain a strong (emotional) connection to Scotland, which could be harnessed in support of an export-led growth strategy.

We know that one of the main issues companies face when thinking about exporting globally is the lack of foreign market intelligence. Many companies in Scotland simply do not have the international perspective to recognise demand in a foreign market. It is to this end that GlobalScot was created. The initiative boasts that currently more than 600 GlobalScots across 50 countries are delivering support, with an average of 1,000 contacts made every year.¹⁹ However, considering the potential of the diaspora as a whole, this does not strike us as terribly impressive.

Furthermore, we believe GlobalScot can often be a mile wide, but only an inch deep. We have seen numerous examples of emigrants making contact, signing up and then there being no follow up. We have also heard of examples where expertise was lacking and the contact made was irrelevant. We have to conclude that this is a valuable asset that is currently being wasted and feel very strongly that GlobalScot needs to be reinvigorated.

Our detailed export recommendations are:

Create trade offices in the rest of the UK

Increasing trade between Scotland and the rest of the UK by 5 per cent would result in a £2.5 billion increase in GDP and thousands of new jobs. We propose delivering this through the establishment of Scotland-rUK Trade Offices in key regions across the UK.

There are 32 trade offices for Scotland across the world. However, there is only 1 for the rest of the

UK market – which accounts for more than 60 per cent of our trade.²⁰ There are 11 economic regions across the rest of the UK where these trade offices could be located and increase Scotland's trade.

Scotland's trade with the rest of the UK is worth £50 billion per annum compared to £16 billion with the EU.²¹ More than 60 per cent of Scotland's trade is with the rest of the UK²². Increasing trade with the rUK market by 5 per cent is the equivalent to increasing trade with the EU by 17 per cent.

Export Mentorship Scheme

We need to encourage Scottish companies who are first class at exporting to act as a catalyst for the long tail of small and medium sized companies in the supply chain who currently do not even think about exporting. This could be done by part-funding a member of staff to nurture these companies and inject more commercial know-how.

National Export Campaign and Competition

In order to emphasise the importance of exports in Scotland's new economic strategy, we envisage a high profile campaign and competition to encourage new scale up companies to show off their contribution to A Global Scotland. Those with the biggest scalability potential could receive tailored intensive support from enterprise agencies and sector leaders. We also note the existence of Scottish Enterprise's EDGE competition in this area, which could either be complemented or adapted in a new format.

Create a Scottish Exporting Institute

The government should work with the private sector to establish a Scottish Exporting Institute. Its key role would be around training and certification, which could also generate revenue and be largely self-financing. The government's role should be one of ensuring access e.g. through bursaries or ensuring quality through the accreditation process. It could also be linked to incentives, whereby an Institute kite mark could give a company preferential access to other services and support.

Boost regional internationalisation capacity

Internationalisation is an important strand of City and Growth Deals across Scotland. As part of our strategy of decentralisation, a network of International Trade Advisers should be embedded in the new emerging regional structures to provide a more accessible service to businesses thinking for the first time of exporting and also to advise on the development of regional export plans.

Turbocharge GlobalScot

The huge potential of our diaspora means that there are significant gains to be made in reforming how Scotland's enterprise agencies harness our diaspora community. To give it the prominence we believe it deserves, we believe that GlobalScot should be turbocharged, with a proper hierarchical management structure and full time staff based in international offices. These should work with long-established international offices of professional bodies as well as the extensive alumni networks of our universities etc. Such a renewed GlobalScot initiative should then embark on a proper recruitment drive to seek to at least double the current number of sign-ups.

b. Rebuild Government Support

All economic literature is clear about the importance of solid institutions that command a broad base of support – such as Enterprise Ireland or the Australian Productivity Commission. We believe Scotland's enterprise network is functioning well, largely due to the high quality of staff that are working within agencies. Our focus is on reforming the structures so that it better serves Scotland's diverse economy and gets our country moving forward again.

Keep business support local

Business Gateway (BG) should remain local, working within an aligned regional enterprise support network. Where practical, offices should be located in highly visible locations and digital access for clients improved. It should primarily provide start-up advice, but also be more flexible

and pragmatic in providing ongoing business support (legal, regulatory, procurement etc.) to a broader range of SMEs. Its remit should be broadened to include a social dimension, just like HIE to consider the sustainability of local communities. Its funding should be ring-fenced via specific grants for councils to reflect the importance and the priority of direct business advice services. The Scottish Government should also draw up guidelines on contracting BG services out, learning from best practice.

Reform Scottish Enterprise (SE)

We recommend that Scottish Enterprise should be regionalised and aligned with other elements of economic development and enterprise support and restructured to make it more effective and client friendly. **Regional Agencies** should mirror growth and city deals, complement and support the work of **Highlands and Islands Enterprise** and the emerging **South of Scotland Enterprise** agency.

- They should be aimed at scale-ups and boosting exports, including to the rest of the United Kingdom.
- They should drive the creation of Global Centres of Excellence in their respective regions to support inward investment.
- They should also be responsible for direct financial assistance in their regions, up to a set value where the national agency would step in.

The restructuring of Scottish Enterprise would include refocusing under two pillars, namely **Scottish Enterprise International (SEI)** and **Scottish Enterprise National (SEN)**. **Scottish Enterprise International (SEI)**, being better aligned to the broader objectives of Scottish Enterprise and therefore the economic development framework as a whole, will undertake the activities and responsibilities currently undertaken by Scottish Development International (SDI).

Roll out Regional Partnership approaches Scotland-wide

If we are to make progress on economic growth, we need to improve the collaboration between the public, private and voluntary sectors. In our view, this should be led by regional partnerships that bring sectors together. We do not propose a specific model, but note that the Scottish Government's Enterprise and Skills Review examined the various options that could be used while encouraging the creation of regional partnerships.

We believe "encouragement" will not be enough, but nonetheless are not prescriptive in what model would be chosen. Formal "Enterprise Partnerships" (as in England) or looser ONE-style arrangements are some of the options that are available. The key principle should be leveraging private sector expertise as well as funding to achieve our economic objectives.

Progress Inter-Agency Collaboration Review with Urgency

Business funding and advice does not just come from the Scottish public sector, but a range of UK government agencies as well. The relationship between these agencies needs to improve just as much as the relationship between Scotland's enterprise agencies.

The UK Industrial Strategy White Paper proposed an inter-agency collaboration review, but as far as we can see this has not been actioned. We would urge the two governments to progress this as a matter of urgency.

One further advantage of our proposed regionally-driven strategy is that it provides an opportunity to build on the collaboration established between the UK and Scottish Governments and their agencies in the context of City and Growth Deals.

A New Performance Measuring Tool

A refreshed economic strategy with an economic and productivity growth aim and with exports at its core should be coupled with a new way of measuring the performance of government policy in the economic development area. This

should include a disaggregated analysis of inputs, outputs and outcomes for each initiative across enterprise agencies, continuous monitoring, regular Parliamentary reporting and improvement. We envisage this to be done with the help of external analysis rather than through internal government channels. Enterprise agency KPIs should be aligned with this.

c. Skills

Skills and education policy is a huge area. It ranges from primary and secondary education, through further and higher education to lifelong learning and continuous professional development in the workplace. We have decided to focus in on what we felt was the most significant area of policy – **how does our skills system need to change to improve Scotland's long-term productivity?**

Our main finding is that we need to **devise a flexible skills development system, that is responsive to a fast-paced evolving global market and that does not just focus on children and young people but caters for needs through life**. In addition, to be able to expect the unexpected, we need to improve how we teach transferable skills – to be questioning, analytical, and able to think creatively. This is the key to anticipating and driving innovation in Scotland.

Some of our recommendations are quite specific, while others are broad and require further detailed work. All of them are designed to achieve one primary objective – **ensuring Scotland is able to develop skills today, for the jobs of tomorrow**.

A Training guarantee to age 18

The Scottish Government should replace the current school leaving age of 16, with a new skills participation age of 18. This would require every pupil to continue in a form of skills development until the age of 18 – this could mean an apprenticeship, a traineeship while employed, further or higher education. The key aim of the policy is to prevent young people get stuck in a low skilled employment cycle straight out of school. It will require an expansion of the training offer in Scotland, where we make further recommendations.

Increase Diversity in Vocational Education Provision

Rebalancing academic and vocational education will require a shift in funding, but also a shift in government policy, away from a top-down approach to education provision towards a more diverse, decentralised and demand driven one.

A Government-supported Vocational School in Every Scottish Region

As a first step, the Scottish Government should legislate to clarify that it can centrally support schools through grant funding – the current legislative position on this is unclear. It should then seek to set up a network of vocational schools to realise the potential of pupils who do not excel in a purely academic environment, similar to the now defunct Newlands Junior College in all Scottish regions and further, depending on demand.

A Network of Second Chance Centres

Currently, there is a lack of provision for adults who for whatever reason failed to get any qualifications at school to re-enter education. We recommend that a new network of Second Chance Centres is set up with public funding that would offer students of all ages the opportunity to gain basic qualifications in a personalised and flexible setting. Some colleges already provide a few such qualifications through evening classes, but Second Chance Centres would be a way of expanding, focusing and publicising these, with appropriate funding attached.

New Institutes of Technology

The Government should work with some of Scotland's leading employers, universities and colleges to set up Institutes of Technology, which would be tailored to provide students with skills to match employers' needs.

Foundation Apprenticeships to be Available in Every School

The Scottish Government should continue to expand the Foundation Apprenticeship programme and aim to have them on offer in every secondary school in Scotland.

Level 4 Flexible Qualification aimed at Transferrable Skills

In addition to the expansion of Foundation Apprenticeships, the Scottish Government should introduce an additional pathway for pupils at Level 4, aimed at transferrable employer-led skills, with similar levels of employer engagement.

Paid Internships for Every S4 Pupil

In the interest of exposing school pupils to the world of work, the Scottish Government should fund a paid internship for every S4 pupil for one or two weeks during the summer holidays. With a salary paid by the government, the costs would be in the region of £10-20m annually.

Flexible Higher Education Degrees

The Scottish Government should work with universities to develop incentives for the introduction of more flexible higher education degrees. This should involve changes to the current funding formula to ensure that the introduction of shorter degrees would not disproportionately impact a university's finances. In addition to shorter degrees, incentives should be developed to encourage the introduction of industrial years as part of some degree structures to give students in-depth real world experience of industry.

A Lifelong Learning Revolution

Boosting lifelong learning should become one of the key objectives of the Scottish Government. This will require policy, funding and cultural shifts, but the arrival of Industry 4.0 makes this of critical importance.

Boost Adult Skills Participation Rates

To facilitate the shift towards lifelong learning and focus government policy, the government should introduce a new adult skills participation target as part of the national performance framework. This could be in the 25-39 age bracket, or much wider, targeting the 25-64 age range.

Personal Learning Accounts for all Workers

Changing individual behaviours will be challenging, but as a first step, the Scottish Government should introduce Personal Learning Accounts for all employees. These would operate like a Skills ISA – encouraging people to invest in their own skills development, supported by government and co-funded by employers. PLA's could build on the existing Individual Training Accounts, with direct Government funding still targeting the lowest paid and lowest skilled workers. Broader tax incentives could be introduced in cooperation with the UK Government.

d. Research and Development

Scotland is fortunate to be home to some of the world's best universities with high quality research output. In fact, our Higher Education Research & Development spend as a proportion of GDP is well above the OECD and EU average²³, surpassing the spend in the UK as a whole as well as in countries like Germany. Where Scotland lags behind, however, is in R&D spend by our businesses. Unlocking the research within our universities and linking it with the commercial world, is crucial to our long term productivity and economic growth and while governments in the past have attempted to address this they have not made significant progress.

In other words, this is not a new problem. It has been regularly examined by expert groups since the early years of the Scottish Parliament. One such study, by the Scottish Science Advisory Council, summed up the issue as follows:²⁴

“The outputs of Scotland's universities (research, consultancy, trained PhD graduates) are not being captured by Scottish industry, which in turn exerts little influence on the research undertaken in academia. This mismatch between supply of academic research output and demand from industrial R&D is at least a missed opportunity whose correction could improve our economic performance.”

The problem is that **competing interests, complex landscapes and wrong incentives** hamper innovation from entering the market. On one hand, there are difficulties in commercialising intellectual property and there is a convoluted process which researchers and investors have to go through. On the other, there are examples of businesses looking for innovative solutions that were available within university departments, with no one to facilitate the link. Our recommendations seek to address both of these issues.

A Scottish Government R&D Expenditure Target

Given the importance of innovation expenditure to productivity and economic growth, the Scottish Government should set a policy target for R&D expenditure in Scotland. We suggest 2.4% of GDP to be achieved by 2026 – a year ahead of the UK Government's target. A target would focus government efforts across several policy areas. It should be accompanied by an increase in direct government innovation grants, given the estimated positive impacts on business innovation, GVA and employment. Furthermore, policies need to be put in place which would increase business expenditure in research and development – and some of our other recommendations provide a starting point for this.

Introduce a Boiler Plate Intellectual Property Licensing System

There are many unnecessary delays in the translation of research into commercial opportunity, mostly caused by competing interests of the various agents involved. One key factor is lengthy negotiations over equity stakes or royalties with universities. The Scottish Government should negotiate a standard set of terms and conditions, which would create a boiler plate licensing system that would provide clarity, stability and simplicity to investors.

Incentivise Spin-out Formation in Scotland

In addition to creating a standard set of licensing conditions that universities would have to adhere to when licensing intellectual property, there are other steps that we believe would incentivise the creation of spin-out companies from research departments across Scottish institutions.

University Spin-out Employment Grant

We have discussed the value of incentives to be put in place that encourage the speedy creation of spin-out companies and employment. One such incentive would be a new spin-out employment grant, targeted specifically at spin-out companies that employ skilled labour. These should benefit both the employer and the institution. An option would be to provide £5,000 to both the business and the university for every skilled job created.

Spin-out Company Business Rate Exemptions

Some of our evidence suggested that financial incentives could encourage more businesses to be set up as spin-out companies. We therefore suggest the introduction of a new business rates exemption for spin-outs. Of course, not all spin-outs will require physical property, especially property that attracts significant rates, but nonetheless some will (e.g. those requiring floorspace for a lab). We envisage the exemption to be time-limited to around 5 years, with the possibility of an extension on application.

Scottish Government Business Fellowships

We have also heard of the issue of academics wanting to have a research position to come back to, whilst also wanting to dedicate time to a spin-out. The Scottish Government should introduce a mechanism that encourages researchers to take a risk and dedicate time to a spin-out. We would like to see 3 or 5 year business fellowships being introduced, which would secure a researcher's institutional position as well as their salary, but allow them to fully focus on the spin-out business.

Provide Additional Innovation Funding for Scottish Institutions

In addition to targeted incentives, there is also scope to boost the overall level of funding that the Scottish Government provides to research institutions. This funding should be intertwined with economic development as that is its primary objective.

A New Scottish Government Innovation Funding Stream

The Scottish Government should introduce a new funding stream for universities that is specifically targeted at commercialisation of IP. This should be provided in addition to the existing research funding, but could be modelled on the dual support system – with one part provided as a grant based on various innovation weightings and the other a competitive award scheme. We propose that, in the first instance, this is comprised of the funding raised by the tuition fees paid by EU students after the UK leaves the EU.

Reform the Research for Excellence Framework

In the long term and, crucially, UK-wide, the REF needs to be reformed to gain a harder edge, taking into account IP translation more than it does now. It should also more regularly stay up to date with the fast-moving changes in industry. The REF today is a huge undertaking that needs to be simplified, perhaps by utilising innovative techniques (e.g. AI and machine learning).

e. Infrastructure

Vital to longer-term productivity is infrastructure and connectivity, and our recommendations here focus on **transport and digital connectivity**. The importance of infrastructure is not only recognised throughout academic research on productivity and growth, but increasingly so by policy-makers across the UK. In consequence, we have seen the UK Government set up the National Infrastructure Commission in 2015, with the Scottish Government following last year with the Infrastructure Commission for Scotland.

This increased focus on infrastructure is to be welcomed, because statistics show the UK has been lagging behind our OECD competitors on infrastructure investment for decades.²⁵ Between 1995 and 2003, the UK was in the bottom 10th percentile of government investment in non-financial assets of all OECD nations. In this period, government expenditure on GFCF (Gross Fixed Capital Formation) made up just 1.8% of total GDP.

In the years since 2003, this average has increased to 2.7% of GDP and the UK has climbed out of the bottom 10th percentile of OECD countries, but still remains one percentage point lower than the OECD average. As a result of this under-investment, the World Economic Forum ranks the quality of the UK's infrastructure 24th in the world, down from 19th in 2006. This puts us towards the bottom of the group of G7 nations.²⁶

Recognising the importance of capital investment, the Scottish Government in 2018 announced a National Infrastructure Mission and has committed to increase annual infrastructure investment so it is £1.5 billion higher per year (£6.7bn) at the end of the next Parliament (2025-26) than in 2019-20. This investment is to be funded through a variety of sources – primarily through the government's capital grant, borrowing powers or other innovative schemes (e.g. PFI or NPD). In part, it is made possible by a large increase in the UK Government's capital grant which is projected to increase by 25% in real terms over the course of this parliament.

It is now time to consider how this money is best spent to improve productivity and boost economic growth. Our discussions lead us to

conclude the key is **to turbocharge investment to improve connectivity between regions and industrial clusters in Scotland** and thus creating an alternative magnet for private investment – a **Scottish Dynamo** – that can compete with the Northern Powerhouse and the Midlands Engine.

There is clear evidence which shows the broader productivity benefits of improving transport links between large cities. Furthermore, international examples of large conurbations across the EU and the USA that provide a critical mass of workers and industry clusters show how focused investment can unlock wider benefits for the surrounding areas and the country as a whole. In addition, in a Scottish context, it is important that rural connectivity is not left behind to allow our tourism industry to continue to grow sustainably.

On transport infrastructure, we reach three key conclusions:

- Firstly, it should be a long-term objective of the Scottish Government **to build on the existing Edinburgh/Glasgow axis**, with significantly improved connectivity between the two and several new population centres in between. With the right incentives in place, this will serve as a magnet for international investment, with knock on benefits for surrounding areas.
- Secondly, **an additional transport axis should be created between Aberdeen and Edinburgh and Inverness and Edinburgh** that enables higher line speeds to reduce journey times, with additional benefits unlocked for Perth and Dundee.
- Thirdly, a **dedicated tourism infrastructure fund should be set up, with further work done to explore the reintroduction of local rail lines**, in addition to improved connectivity to the North of Scotland.

Digital infrastructure is, if anything, even more important and should be one of the most important priorities of any government. And while responsibility for roll out is shared with the UK Government, there are steps – beyond just boosting funding – the Scottish Government could take to make progress.



Put the Infrastructure Commission on a Statutory Footing

Similar to the Office for Budget Responsibility and the Scottish Fiscal Commission, the Infrastructure Commission for Scotland should be put on a statutory footing, with its independence guaranteed and the Commission's functions set out in primary legislation. Such a step would make the Commission's work accountable to the Scottish Parliament rather than the Government, allowing it to work in the long-term, bypassing the short-termism of the Parliamentary cycle. The membership of the Commission should also be boosted, with complementary skills represented. Members should be able to assess relative cost and benefit of projects but also more practical issues in relation to on the ground delivery.

Deliver a Regionally-Driven Infrastructure Vision for the Future

In line with our overall view on the need to regionalise our structures, we believe the Scottish Government should compel each Scottish region to produce a 30 year infrastructure vision, which would identify transport projects, new population centres and new industrial clusters in the region. The Infrastructure Commission should then have an additional evaluative role to guide the government's funding plans.

Back a Joint UK-Scottish Infrastructure Investment Vehicle

The individually-negotiated City and Growth Deals brought together devolved and reserved competences, by uniting all levels of government to jointly agree on regional investment projects. We believe there is scope to extend this approach further and would urge the Scottish and UK governments to design a new infrastructure investment vehicle, which would allow infrastructure projects of national importance in Scotland to be jointly funded and be jointly overseen. One of the options would be to invest in high-speed rail connecting Edinburgh and Glasgow with English metropolitan areas.

Transform Scotland's Rail Capacity

We believe a significant amount of the projected increases in Scotland's capital budgets should be invested in improving our rail infrastructure. This has both economic and environmental benefits – two principles that will guide future spending decisions.

Connect Scotland's Cities

We believe that significant productivity and growth improvements would stem from investing in the connectivity between Glasgow, Edinburgh, Aberdeen and Inverness. As a long-term objective, we believe that these four cities should be brought closer together along two axes. Edinburgh and Glasgow should be linked by faster rail and an extended, three-laned M8 (plus hard shoulder), with further population centres planned in between, alongside new industrial clusters. Aberdeen, Inverness and Edinburgh should also be linked by faster rail, improving what is a notoriously poor link between these cities.

A Scottish Smart Travel Card

The Scottish Government should work with its partners in local government and the private sector to develop a truly integrated transport system. As part of this, it should introduce a Scottish Smart Travel Card, which would utilise contactless technology and be usable across all modes of domestic transport.

Position Scotland as a Leader in Satellite Internet

Building on Scotland's established centres of excellence in space technology, Scotland should be at the forefront of satellite-delivered internet connectivity. The Scottish Government should work with the private sector and UK regulators to make Scotland the ideal base for this technology before wider application. This should also result in remote areas of Scotland benefitting from fast internet speeds without relying on the current broadband delivery plans.



Conclusion

These recommendations represent the first tranche of our proposals ahead of the Holyrood elections on Scotland's economic recovery. They do not touch on devolved tax policy which we will return to at a later date. Nonetheless, on the emergency response required now – and on the big strategic calls that must be made to help Scotland grow over the long-term, we believe they set a course for action which will help Scotland grow.

It should be noted that all of our recommendations could be enacted now, without the recourse for fresh legislation or “more powers”. As the pandemic has shown, the Scottish Government already has extensive power to follow its own course as it sees fit. It is not a lack of power which is stopping the Scottish Government from pressing ahead with a radical new agenda for Scotland, it is a political strategy which wants to cast Scotland as helpless to respond.

We disagree. Working together in collaboration with our friends and partners around the United Kingdom, devolution has provided Scotland with a platform for action that it can utilise now, for the good of all.

On skills, exports, infrastructure and research, it is the Scottish Government which holds the key to Scotland's future success. We urge Ministers to take that chance and get the country back to growth.

This is a time of crisis for Scotland – but a moment of opportunity too. It is up to the SNP Government to set out whether it is capable of rising to the challenge of both. The Scottish Conservatives most certainly are.



Endnotes

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- 21 (*UK Government*, 29 January 2020, [link](#))
- 22 (*Fraser of Allander*, 5 February 2020, [link](#))
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