The Scottish Parliament
Pàrlamaid na h-Alba

Economy and Fair Work Committee

Kate Forbes
Deputy First Minister
and Cabinet Secretary for Economy and Gaelic

6 November 2024

Dear Kate,

Economy and Fair Work Committee pre-budget 2025-26 views

In advance of the proposed budget for 2025-26 coming forward next month, please find attached a summary of evidence received by the Committee and our views on spending and associated issues for the coming financial year.

Our pre-budget letter last year emphasised three areas where Scottish Government spend should be maintained: **support for business, support for women's enterprise** and **skills development.** These remain priorities for this Committee. This year, key barriers to delivery were highlighted to the Committee including **the lack of multi-year funding and the availability of housing to support jobs**.

The Committee notes that this year's Programme for Government aims to deliver in four main areas: eradicating child poverty, growing the economy, tackling the climate emergency and ensuring high quality and sustainable public services. Sufficient and effectively deployed capital spend will be essential to meet ambitions for economic growth, net zero and public service delivery.

Attracting and accelerating investment is a key aim of NSET. There are clear opportunities for Scotland's economy from public and private investment in infrastructure, housing, transport, innovation and workforce skills to support economic growth and wellbeing.

Given their roles in supporting economic and business growth, the Committee agreed this year's pre-budget focus would be Scottish National Investment Bank, the enterprise agencies and VisitScotland.

This letter also follows-up points made in the Committee's last pre-budget letter and the Scottish Government responses to them.

I look forward to receiving your response to this Committee's pre-budget views, and to taking evidence from you early in the New Year.

Kind regards

Claire Baker

Claire Baker MSP
Convener

Context

Scotland's economy (in common with the rest of the UK and other similar countries) has seen a sustained period of low growth and productivity against a backdrop of rising costs. There have been increased fiscal constraints for governments and households. Scottish Government capital spend funds City Region and Growth Deals, the enterprise agencies and capitalising SNIB. The majority of the Scottish Government's capital budget comes from the UK Government's Block Grant. One source of capital funding is Financial Transactions (FTs), also from the UK Government, for the purposes of equity or loan finance to private enterprises.

The new UK Government recently published its budget. Barnett consequentials have yet to be confirmed by the Scottish Government, but the UK Budget document notes that an additional £3.4 billion will be added to the Scottish budgetary envelope in 2025-26 (£2.8 billion in resource spending and £600 million in capital spending). At the time of writing, the extent of additional consequentials to compensate the devolved public sector for the increased cost of employer National Insurance contributions was unclear. The Committee asks the Scottish Government for clarification on this point as soon as this is available.

Evidence received

The Committee took evidence from SNIB, the enterprise agencies and VisitScotland, during September and October.

Their 2024-25 budget allocations were as follows.

£ million	Resource spending	Capital spending
SNIB	3.11	174
SE	131.8	79
HIE	27.9	23.2
SOSE	14.3	13
VisitScotland	38.6	5.2

Note that SNIB's capital funding consisted entirely of financial transactions.

Both Scottish Enterprise (SE) and SNIB rely heavily on capital funding. Most of SE's early-stage investment work has been funded through FTs. SE said there were no current demands on its capital budget that could not be met, but the position could change next year due to the inward investment pipeline and pace required. It said it would be helpful to have sight over future years' budgets and allocations.

SNIB has a commitment from the Scottish Government for £2 billion over 10 years. FTs have been SNIB's primary capital source. To date, SNIB has committed £650 million and continues to work on the basis that the full £2 billion capitalisation will be received. At the 2024-25 Budget, the Scottish Government assumed no further FT funding in the Block Grant beyond 2024-25, particularly significant for SNIB. The recent UK Budget did not provide any additional Barnett consequentials for FTs. SNIB told the Committee that this year's reduced budget had restricted its ability to invest, slowed pace and caused investment criteria to be tightened. SNIB said further cuts would impact its ability to crowd-in private capital and make a return on investment sufficient to cover its operating costs and that self-sustainability was at a critical point.

SNIB also called for a multi-year settlement to provide more certainty and pointed to a mismatch between annual settlements and the drawdown profiles of its investment commitments.

HIE and SOSE budgets are also capital-intensive; neither has had FT funding this year. HIE said other funding streams were becoming available, and it hoped to receive monies from offshore wind allocations. HIE and SOSE said short-term funding settlements had caused uncertainty and had hampered work. For example, HIE had not been able to support the Sumitomo project from its own budget. It envisaged being in that position more frequently, given budget constraints. HIE highlighted the contrast between capital crowded-in for large-scale renewables projects and capital available for SMEs.

On resource funding, SE suggested that any further reduction would mean only just being able to cover fixed costs, such as salaries and diligence on investments. Further efficiencies would be difficult, and it may need to consider stopping some activities it was legally obliged to undertake. HIE said resource funding reductions meant it was no longer able to provide revenue funding to support large capital projects, something it did previously. It also said it was now doing less evaluation of programme effectiveness.

With regard to VisitScotland, a strategic change programme is underway, including disposal of the iCentre network over the next two years, ending the Quality Assurance schemes for tourism and business events and taking forward a digital-first approach. In September, the Scottish Government confirmed in-year reductions of £0.8m to VisitScotland's marketing budget. VisitScotland told the Committee this in-year reduction had meant it was unable to carry out certain activities during the rest of this year, in particular paid activity, relying instead on in-house resource. It had scaled back activity in growth markets such as Canada, Australia, and China to focus on the core markets of the US, UK, France, and Germany. VisitScotland pointed to the competitive environment in which it operates, and the marketing spend of Ireland, its nearest competitor.

Committee conclusions and recommendations

Give the difficulties caused by short-term funding settlements, the Committee asks the Scottish Government to look further at the possibility of multi-year funding to allow for longer-term planning.

The Committee is supportive of SNIB and its work and recognises that until now it has been heavily reliant on capitalisation from financial transactions. The Committee asks the Scottish Government to confirm how it proposes to capitalise SNIB in future.

The Committee is aware that discussions continue about accounting rules that place restrictions on SNIB's ability to reinvest proceeds. SNIB has said that unless a solution is found, it will always be dependent on state funding, contrary to Parliament's intention. The Committee believes it is imperative that a solution is found. The Scottish Government is asked to set out how it will progress this.

SNIB continues to seek authorisation from the Financial Conduct Authority to manage third party capital alongside capital from the Scottish Government. In June 2023, SNIB told the Committee that its application was "being actively looked at". SNIB recently highlighted the importance of receiving FCA authorisation to enable it to directly allocate private capital to projects it finances, alongside the capital it receives from the Scottish Government.

The Scottish Government is asked what assistance it is providing with efforts to secure necessary authorisation.

The Committee was previously advised of discussions between enterprise agencies to identify potential opportunities for greater interagency collaboration on common functions. Given current funding constraints, the Committee believes this work is vital. The Scottish Government is asked for a progress update on this work and how next year's budget will support efforts in this area.

The Committee was also advised last year that work was underway to reform delivery of economic development support in Scotland, including considering of the role of the Scottish Government, enterprise agencies and other partners. The Committee would be grateful for an update on this work and how next year's budget will support this work.

The Withers review recommended that enterprise agencies should take responsibility for supporting businesses with skills and workforce planning. This would require enterprise agencies to broaden their approach. Given the importance of an appropriately skilled workforce to Scotland's economy, the Committee calls for skills development and workforce planning to be sufficiently funded to enable this vital work to be undertaken at a scale and pace required. What is the Scottish Government's current thinking on the recommendation that enterprise agencies taken on the responsibility for supporting businesses? To what extent will next year's budget support and resource changes to the skills development and delivery landscape?

In the report following its Town Centre and Retail inquiry, the Committee highlighted the importance of support to businesses to build digital capabilities. The Committee asks the Scottish Government to make clear in next year's budget the specific provisions intended to deliver this support and what outcomes this spend is expected to achieve.

The Programme for Government pledges to implement key recommendations from Ana Stewart and Mark Logan's review of gender equality in entrepreneurship. The Committee again requests that the Scottish Government disaggregates monies for women's business support in the budget, sets out what the monies will be used for and confirms the size and profile of the Pathways Fund.

The Scottish Government has said it remains committed to the £500 million 10-year Just Transition Fund programme for the North East and Moray. In its inquiry report, the Committee queried the Fund's future sustainability and asked the Scottish Government to look further at the possibility of multi-year funding to allow for longer-term planning. The Committee also called for a mix of sustained revenue and capital funding for the Fund, with sufficient revenue to support capacity-building in communities and to ensure small businesses and community-based initiatives could be supported. The Committee requests that next year's budget makes this provision.

Tourism is vital to Scotland's economy and sustainable tourism has been identified by the Scottish Government as a growth sector, with comparative advantage and potential to deliver increased productivity and growth. The Committee recognises that the impact of removing VisitScotland marketing campaigns, due to funding withdrawal is felt immediately.

The Committee has previously called on the Scottish Government to protect VisitScotland's international promotional spend and was disappointed with this year's in-year budget cut. The Committee would be concerned to see further cuts to the VisitScotland budget.

The Committee recently completed an inquiry into the disability employment gap highlighting that budget cuts had strained employability resources and contributed to funding delays for local authorities. This had impacted on service delivery. The Committee expects next year's budget to re-prioritise employability spend.

SE told the Committee it makes a return of £25 gross value added for every £1 invested. HIE estimated that tax revenue generated over three years was two and half times its budget. The Committee notes this but emphasises that particularly in times of tight financial settlements, it is critical to be able to evidence what is being achieved by public investment and expenditure.

Being able to evidence what is achieved by public funding will be important for measuring the success of the Scottish Government's National Strategy for Economic Transformation. The Auditor General for Scotland has said there should be a clear link between NSET and the budget, with NSET driving budget decisions across Government. The Committee calls for more coherence across Scottish Government portfolios and expects to see much clearer links between NSET and all other Scottish Government strategies and the Scottish Government's budget documents.

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