

Fiscal Affairs Scotland Monthly Bulletin

March 2015

Topics covered in this issue:

The Scottish government's Economic Strategy

Alcohol related deaths across Scotland

London Challenge update

Recent Fiscal Affairs Scotland papers

The Scottish government's Economic Strategy

The Scottish government published an update to its overall economic strategy on March 3rd 2015.

Some of the key elements and issues it addressed included:

- the importance of reducing inequality while boosting growth;
- the importance of improving productivity;
- the role of a new Scottish Business Development Bank;
- an adjustment in its corporation tax strategy, moving away from across the board potential cuts to targeted ones.

It is worth considering each of these issues in more detail.

Inequality and growth

The principle thrust of the Scottish government's revamped economic strategy is its increased emphasis on reducing inequality while increasing growth.

This is a theme that has been much discussed of late and not just by the more traditional

In the short term, taxes and benefits will have a greater impact and here the revised strategy is largely silent. The Scottish government's position on those major tax powers it has, or soon will have, i.e. income tax, council tax and local business tax, are not discussed in the strategy. This is an odd omission when they clearly have the potential to play an important role in reducing inequality.

The recent OECD report on the UK, cited in the strategy, highlighted the problem of inequality in the UK and outlined some MB/2015/03

sources of left leaning governments and think tanks. A wide body of groups are now concerned with the negative impact that increasing inequality may have on future growth, from Davos to the OECD and the IMF to the US Federal Reserve.

However, the problem remains - what policy changes need to be put in place to stop, or reverse, the trends seen over recent decades, back to the 1970s?

In the case of the UK most of the increase in inequality arose over the 1980s and has, partly through government policy of redistribution, been largely flat, or falling, since.

In some countries with traditionally lower levels of inequality, like Sweden, recent decades have seen a bigger rise in inequality than in the UK or the USA, although it remains at much lower levels.

This reinforces the difficulty in trying to dampen or reverse such trends.

The Scottish government, rightly, puts an emphasis on education as a potential source of reducing inequality, particularly the importance of early years' interventions. However, this is a long term policy and will have little impact for at least a decade. The current scale of such early years funding may also still be insufficient, despite recent increases, to secure the benefits sought.

suggested policy changes to improve matters, including:

- making the self-employed subject to the same income taxes as employees, (as recommended in the Mirrlees Review);
- updating the property valuations of the council tax;
- removing preferential and zero-VAT rates, albeit with some adjustments to

protect the poor in relation to food and energy.

In terms of austerity, it is worth noting that the Director General of the OECD, commenting on the UK government's economic and fiscal policies said "*well done and keep going with the plan!*". Whether the Scottish and UK public view share the same view is a moot point.

Productivity

At the launch of the new strategy much was made of Scotland's 'improved' productivity position, relative to the UK. However, this claim rests on weak ground.

In fact, Scotland's productivity, relative to the UK, has see-sawed in the most recent years for which we have data (see Table 1). Relative to its 2007 nadir, it peaked in 2009, fell back in 2010 and remains at around that level in the latest year, 2013. Furthermore the improvement from 2007 to 2009 is more likely to be due to policies implemented prior to 2007, due to the lags involved, and appear to have more to do with falling employment than rapidly rising output at that time.

It should also be remembered that the data used to calculate this measure (GDP per hour), is not of the highest quality and so changes may be due to statistical 'noise' rather than 'real' changes. Furthermore, over the period concerned the Financial Services sector has been severely affected and the productivity data in this sector is particularly difficult to estimate.

It is also worth noting that the UK's productivity performance post the recession has been notably worse than most other countries. While the UK's productivity performance (in terms of GDP per hour worked and relative to the other members of the G7) improved between 1990 and 2004, almost all of that gain has since been lost, most of it post 2007. As a result, comparing

Scotland's productivity performance with that of the UK over recent years, even if it has had been thought to have been marginally better, may not be the most informative of exercises. (1)

As with inequality, finding ways to improve productivity is not straightforward. In its recent report on the UK, the OECD suggest:

- "*addressing excessive remuneration for GP's and increasing competition in health care provision*";
- "*supporting higher and more equal autonomy across school types and focussing investment and policies on disadvantaged children*".

Some of these proposals may look more attractive than others to the Scottish and UK governments and neither is easy to achieve.

The Scottish government also published some modelled examples of what might happen if certain improvements were to come about. One of these relates to the issue of total (or multi) factor productivity (2), a subject that was discussed in the last Monthly Bulletin. They find that a 0.1% a year improvement in this factor over a 10 year period (i.e., up from 1%, its 1997-2007 UK average, to 1.1%), could boost employment by 11,000. The key here is how to achieve such an improvement as this was little discussed in the report.

Table 1: Scottish Productivity, 2007 to 2013, relative to the UK (=100)

	2007	2008	2009	2010	2011	2012	2013
Per hour	92.6	94.1	98.1	96.9	96.3	97.6	96.8

Source: ONS, Labour Productivity, December 2014

Scottish Business Development Bank

The Scottish government has reaffirmed its desire to develop a Scottish Business Development Bank (SBDB). This is a clear

signal that it remains committed to solving a hitherto difficult funding issue, namely, ensuing Scotland's small and medium sized enterprises (SMEs) have access to finance for growth that the current banks are unwilling, or unable, to support.

Two key challenge in delivering this much discussed idea still need to be addressed. First, is the delivery of a banking entity such as the SBDB possible within current EU State Aid rules? Secondly, can the development of such a business bank be achieved quickly to allow for it to contribute to the delivery of the economic strategy? Given the complexity of banking regulation within which the SBDB would have to operate, securing regulatory approval will be neither quick nor easy.

Corporation Tax Strategy

Any cut in the general rate of corporation tax is likely to produce an initial reduction in tax revenues. The medium to long run benefits that may arise are dependent on the size of the cut being enough to attract new businesses to set up in Scotland. Deciding what size of a cut is enough to achieve this is an inexact science. Hence, there would have been a risk over how long, if at all, it would have taken corporation tax income to return to previous levels. This uncertainty would have been compounded by the upcoming devolution of this tax power to Northern Ireland.

Of course, at present all of this is hypothetical as the UK government retains control over corporation tax.

Conclusion

The Scottish government's Economic Strategy is to be welcomed, and more details are due to emerge in the coming months. However, the causal pathways by which some of its key outcomes are to be achieved, namely reducing inequality and improving productivity, remain vague.

Alcohol related deaths across Scotland

There are many influences on productivity. On the labour quality side this includes the general health of the workforce. Here Scotland's record is poor, with relative low healthy life expectancy and high rates of 'bad habits'.

In recent years successive Scottish governments have attempted to address such issues as excessive smoking and drinking through a series of policy initiatives. One high profile outcome, which might reflect the success of such initiatives, is the number of alcohol related deaths (ARDs) being recorded.

In February, the ONS published the latest figures on ARDs across the UK (see 'Alcohol-related Deaths in the UK, Registered in 2013', published 11/2/15).

The figures continue to highlight the decline in Scottish ARDs seen since the mid-2000s, a pattern not seen in other constituent countries of the UK. For men, the Scottish ARD rate (deaths per head of population) remains higher than elsewhere, but the differential has fallen from over double the rate seen for England to around 50% higher. For women, the rate has fallen from around double that of England to around a third higher. Furthermore, whereas Scotland use to have the highest regional ARD rate, now it is not dissimilar to that seen in the North West of England.

The ONS also published its latest analysis of adult drinking habits across Great Britain (see 'Adult Drinking Habits in Great Britain, 2013', published 13/2/15). This survey-based analysis found that the proportion who 'drank in the last week' was slightly lower in Scotland (56%) than in GB (58%) and the proportion who 'drank on at least five days in the last week' was considerably lower in Scotland (6%) than in GB (11%). However, it also found that 'on the heaviest drinking day in the last

week' Scots tended to consume more than the GB average (by 5 percentage points, based on a variety of drinking levels).

This 'relatively' good news in terms of Scotland's alcohol consumption patterns reinforces recent trends, as outlined in the most recent edition of 'Monitoring and Evaluating Scotland's Alcohol Strategy' (4th edition published by NHS Health Scotland in December 2014), which looks at trends in alcohol consumption and alcohol related illness in Scotland.

After years of worryingly large increases in alcohol related illnesses from the mid-1990s to the mid-2000s, the last decade has seen declines in such illnesses. Not only have ARD's dropped in recent years in Scotland but so too have the number of alcohol-related hospitalisations and alcohol liver disease hospitalisations.

Although this data provides a good picture for Scotland as a whole, the picture is not identical across all of Scotland. Table 2 shows ARDs by Scottish Health Board areas, for some specific years over the period 1979 to 2013. (3) (4)

Some of the most notable points to emerge are:

- the large rise in ARDs across Scotland from the early-1990s to the mid-2000s;
- the significant fallback in ARDs in more recent years;
- the variation in increases in this period as a whole, with Greater Glasgow standing out as having the smallest increase while Lanarkshire and Fife having the highest;
- while most Health Boards have seen declines from their mid-2000s peaks, some remain very high, including Fife and Borders.

Looking in more detail, across local authorities rather than Health Boards, highlights some even more surprising results. At this level, the

number of ARDs in Glasgow in 2013 (189) was virtually identical to that seen in 1979 (187), although its population fell by around 15%, and almost half the level seen in the peak year of 2006 (345), since when its population has risen by around 5%.

Similarly, local authorities, like Inverclyde, now see a similar, or lower, number of ARDs than back in 1979. Others, notably East Ayrshire, both North and South Lanarkshire and West Lothian, still see well over double the number of ARDs than occurred in 1979.

While ARDs have come down they remain relatively high in Scotland, and particularly in Glasgow, in comparison to the UK and Northern English cities. They are also strongly socially patterned with rates much higher in the most deprived areas. So although there have been large declines in ARDs, Scotland, the west of Scotland and more deprived areas still have significant problems and relatively high rates of harm.

The recent trend in ARDs does not fit particularly well with data from a variety of sources on alcohol consumption. For example, retail based data shows consumption in Scotland did not start to decline until 2009, later than in England & Wales (E&W). Despite the decline in E&W being sharper and coming earlier, it has had little impact on ARD rates on those countries, unlike the decline seen in Scotland. Interview based survey data and household spending surveys on alcohol consumption are also difficult to reconcile with changes in ARDs.

It should be emphasised that the link between consumption and harm is not always easy to make because deaths can be affected by short-term binge-related factors, long-term over-consumption and age cohort effects. For these reasons the timing of the downturn in consumption and mortality is not necessarily going to be consistent across the UK.

Analysis in the latest annual report ‘Monitoring and Evaluating Scotland’s Alcohol Strategy’ suggest that the recent decline in ARDs may, in part, be explained by a combination of: declining consumption, itself connected to declining affordability; an increase in alcohol services provision; and the ban on quantity discounts on the off-trade. However, they also found little evidence of greater understanding of the dangers of alcohol or that changes in alcohol licensing, had, as yet, made much of an impact.

The Scottish government's recent reduction of the drink drive limit and the (potential) introduction of minimum pricing may also have a positive impact in reducing population levels of consumption.

The latest annual report also recognises that further work is necessary in order to understand a variety of still puzzling findings. Amongst these are: the differing patterns over time of ARDs versus consumption; the degree to which Scotland out-consumes other parts of the UK, and how this is distributed across the population; and the rapid rise and fall of ARDs across Scotland?

The benefits seen from reducing the ill effects relating to over-consumption of alcohol will be seen most in terms of health service savings and improvements in well-being. There is also a clear economic benefit from having a healthier, and so more reliable and productive, workforce.

Table 2: Alcohol Related Deaths (ARDs) over time for Scotland and by Health Board

	1979-81	1991-93	1998-2000	2004-06	2011-13	% change overall	% change since peak
SCOTLAND	616	613	1,223	1,512	1,142	85	-24
Greater Glasgow	260	187	445	507	335	29	-34
Lothian	80	83	160	197	140	75	-29
Lanarkshire	64	80	156	210	176	175	-16
Ayrshire	40	39	81	101	77	93	-24
Tayside	35	48	74	113	85	143	-25
Grampian	32	49	84	94	82	156	-13
Highland	29	39	68	90	68	134	-24
Fife	27	28	60	72	74	174	3
Forth Valley	23	33	54	62	54	135	-13
Dumfries & Galloway	10	12	18	30	18	80	-40
Borders	7	7	12	15	17	143	13

Source: General Register Office for Scotland, website (see - vital events/deaths/alcohol-related)

London Challenge update

In Decembers Monthly Bulletin (MB/2014/03), we looked at analyses of explanations for the performance improvement seen in London schools in recent years.

In February the Scottish government announced its own plans to learn from this success. This comes as part of the Scottish Attainment Challenge, with funding of £100 million available over 4 years. It is, in part, based on the London Challenge initiative and aims to improve educational outcomes in Scotland's most disadvantaged communities.

Again this is a welcome initiative, not just in terms of early years interventions, but also in terms of learning lessons from others successes. However, caution is also needed. As our previous analysis highlighted, the 'London Effect' is not well understood and there are a variety of possible explanations, of which a number may well have contributed to the final outcome. Indeed some researchers believe that the whole of the London Effect can be explained by the changing ethnic make-up of London's schools. While this may be too pessimistic a view it reinforces the need to take care when apportioning scarce resources in a key area of, underfunded, public policy.

Recent Fiscal Affairs Scotland Papers

The following paper have also been published by Fiscal Affairs Scotland over the past month and is available from our website at www.fiscalaffairsscotland.co.uk.

- Local Government Funding Challenges Analysis Paper

NOTES

- (1) It is worth noting that in the Scottish government's first economic strategy the Scottish productivity target was to rank in the top quartile for productivity against our key trading partners in the OECD by 2017.
- (2) TFP measures any increase in output as a result of how efficiently labour and capital are being utilised. In other words it equates to gains in output resulting from improvements in technology and management. The Scottish government notes that, over the period 1997 to 2007, TFP growth in the UK averaged 1%. However, since 2007 it has detracted from growth overall.
- (3) Three year averages are shown as the data can vary year-by-year and this averaging helps compensate for any outlying results.
- (4) The 3 island Health Boards are not shown as the numbers involved are very small (under 10).



Contact details

John McLaren m: 07429 508 596
e: john.mclaren@btinternet.com

Jo Armstrong m: 07740 440 766
e: jo@jo-armstrong.co.uk

Charity details

Fiscal Affairs Scotland SCIO
SC044827

Website fiscalaffairsscotland.co.uk