

### **John Kay – briefing note**

The Committee wishes to assess the extent to which budget priorities address the Scottish Government objective of promoting sustainable economic growth. My objective in this note is to describe the elements of a framework for that assessment.

My starting point is that the growth of the Scottish economy is the product of the performance of Scottish business. Government can support business in three broad ways:

- by the provision of supportive infrastructure (including not just physical infrastructure but also social infrastructure, e.g. by education/policies which help workers develop appropriate skills).
- by financing sector specific support.
- through local policies, both of a macroeconomic kind (whether the overall stance is expansionary or contractionary) and of a microeconomic nature (the design of a policy).

Physical infrastructure issues mainly concern transport, telecommunications and other utilities (gas, electric, water etc.). Issues the Committee might want to consider include:

- to what extent is transport expenditure directed towards improvements which promote growth, rather to those that offer direct consumer benefit?
- to what extent do transport improvements direct activity from one area to another, as distinct from increasing activity as a whole.
- is public support for expansion of broadband access an effective use of public money?
- is energy policy (which needs to be considered both in a Scottish context and the context of Scotland's role in a UK energy system) sufficient to ensure supply security?

In relation to social infrastructure, two key issues in my view are:

- is the balance between different components of education expenditure, especially between higher education and the rest, the most appropriate for a sustainable growth strategy?
- is the development of affordable and social housing adequate to support Scotland's economic development needs?

My view of the appropriate industrial strategy for Scotland is that it should be based on the principle that small countries succeed in the world economy by exporting narrow specialisations on a global scale. The core principle – which I believe is recognised in general policy – is, despite the common disparagement of the phrase, to 'pick winners' i.e. to identify sectors in which Scotland has a genuine competitive advantage, and to promote those. It is important that there should be no wishful thinking here: the emphasis should be on sectors that are winners, not on ones that we would like to be winners. The principal items on such a list are financial services (despite obvious setbacks), energy support services premium food and drink, tourism, and possibly life sciences. The Committee (which may of course have a

different view as to what such a list might contain) should be asking, on a specific sector by sector basis, how the budget is relevant to the advancement of these industries.

The Scottish Government has limited levers in fiscal policy. Its macroeconomic influence is essentially confined to the effects of allocation and reallocation within an overall budget total and the primary policy tool here is relevant only to short term recovery issues, principally in the ability to focus expenditure on employment intensive, recession hit activities, notably construction. At the microeconomic level, it appears to me there has been some inclination to use the few instruments available to the Scottish Government to favour consumers over business. This is not necessarily undesirable or inimical to growth: it should be recognised that all taxes are, ultimately paid by people. The ideal business tax is one whose impact is largely exported; the worst business tax is one which falls on export activities and simply damages competitiveness. In between are those taxes which fall primarily on domestic economic activity, which are effectively an additional indirect tax on Scottish consumers, but may have adverse impacts on the conduct or behaviour of business in the process.