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From The Secretary of State for Wales

The Rt Hon Peter Walker MBE MP

CT/6954/89

25 May 1989

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PUBLIC EXPENDITURE SURVEY 1989: WELSH OFFICE

Following consideration of the programmes within my responsibility I am writing to you in accordance with the PES guidelines.

I have examined the existing provision available to me for my Industry programmes very carefully. I have done so against the background of the progress that we have been able to make particularly in the last two years; of the problems that we continue to face; and of the huge opportunities that are opening up especially as we approach 1992.

The Single European Market offers the prospect of enormous investment opportunities in the United Kingdom. I want to ensure that Wales is able to take every possible advantage of this. It will continue the essential diversification of the narrow industrial base; create jobs and reduce unemployment (with savings in unemployment benefit to the Exchequer); benefit our trade deficit; help to improve the performance of our own manufacturing sector with beneficial effects for inflation; improve the perception of the attractiveness of Wales and increase confidence in Wales.

There is still a long way to go before home based production will be able to respond in a more effective way to the demand generated by domestic consumers.

The Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON SW1P 3AG

/The benefits of

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The benefits of attracting an even greater share of inward investment are obvious. If you just take five of the larger inward investments that we have obtained from Japan, Germany and America I believe that when they are in full production the balance of trade will be improved by about £1 billion a year. Moreover, by attracting this investment to areas of relatively high unemployment, growth can be achieved without fuelling inflation unlike investment in areas where the tightness of the labour market prohibits growth without creating wage inflation.

On economic, political and cultural grounds the UK is of course well placed to take advantage of increasing investment. But competition will be increasingly fierce and strong regional incentives will still be needed if we are to maintain and increase our share.

Regional assistance must be administered more flexibly. None of our competitor countries within the Community attaches the same prominence to demonstrating the "need" for regional support; and nor do other countries apply the formal cost per job ceilings. I entirely agree with what Tony Newton says about this in his letter to you of 15 May.

It is also essential that the basic infrastructure should be available for potential investors as the momentum of investment decisions accelerates rapidly over the next few years.

I therefore wish to pursue a strategy in which I will further reduce unemployment in Wales, for it still exceeds 100,000 and there are areas where male unemployment is well over 15%. This strategy will be effective if over the next three years I pursue a programme in which those firms looking for a location in Europe can quickly make decisions to locate in Wales. The total cost of that programme is minute compared with both the savings in public expenditure arising from the reduction in unemployment and social security costs and with the receipts that the Revenue will enjoy thereafter from Corporation Tax and taxation of those concerned.

Welsh Development Agency

My bid for the WDA is £28.3m - £19.5m - £14.9m. Essentially this is to enable the Agency to acquire and develop sites, provide additional factory building, clear more derelict land and undertake environmental and urban improvements.

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All of this, together with increasing the resources available to the Agency's marketing arm (now Welsh Development International), is aimed at taking advantage of the opportunity provided by the potential to increase the flow of inward investment into Wales. In particular this strategy will focus on those parts of Wales which still contain unemployment blackspots and where private sector participation continues to need encouragement.

Within the bid I must have £10m pa to allow the Agency to continue with its current baseline factory building workload of 150,000 sq metres a year because of increased construction costs - a cost increase driven principally by overheating in the South of England. Price rises on this scale cannot be absorbed by the Agency whose costs have been independently assessed as already being 11% below those of other developers in the Principality. Without this we will lose an estimated £120m of private investment and 2750 job opportunities.

I need £8m pa to enable the WDA to acquire and service strategic sites in key positions which will help the areas where unemployment is highest. I have in mind here particularly the development opportunities along the Heads of the Valleys road and capitalising on the opportunities arising from our investment in improving the A55 in North Wales. The resources would open up 150 acres of land a year for inward investment projects. The related injection of private capital is likely to exceed £500 million.

£7.5m in 1990/91 and £4.5m in 1991/92 is required to meet the immediate need for factory provision and projected demand, while allowing for increasing private sector activity in the more prosperous areas of Gwent, South Glamorgan and Clwyd. The additional budget would enable the WDA to commission 25,000 sq metres in 1990/91 and 15k sq metres in 1991/92.

Associated private investment is projected at £50m and the job potential at 1300. By 1992/93 the policy of pushing the Agency's new rentals to commercial levels (the Agency exceeded its £21 per sq metre target in 1988/89 by £4 per sq metre) should be yielding major dividends in increasing private development still further.

As you know we have recently accelerated pit closures in Wales and two major closures have been announced since we last discussed public expenditure. This has inevitably added considerably to the stock of land needing to be reclaimed.

/My officials will

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My officials will let yours have further details of these bids and the other smaller elements designed to enable the Agency to tackle the problem of dereliction on private land located next to major industrial estates and main strategic routes, particularly in the South Wales Valleys; accelerate the process of urban renewal in the Valleys; strengthen its international marketing arm; and allow it to withdraw from the provision of utility services on its estates which require a once for all capital cost to bring the infrastructure up to an acceptable standard before it can be handed over to the appropriate authorities. The resources released by this latter change allow me to contain my bids to the levels I have indicated.

The WDA's receipts are already running at a very high level but, as you will recall, I have been able to identify additional receipts of £3m in 1990/91 and £5m in 1991/92, rising to £6m in 1992/93. In order to continue to encourage the Agency to generate as high a level of receipts as they can secure I very much want to allow them to retain these receipts and I have assumed in formulating my net public expenditure bids that they will do so. Without this the Agency's land reclamation programme would have to be reduced by some 500 hectares over the next 3 years, totally undermining our strategy of clearing the bulk of the dereliction by the mid 1990s. I have asked my officials to let yours have the details.

Regional Selective Assistance

My bid is for £12m - £16m - £27m. This reflects the anticipated level of growth in Wales and the changes in the operation of RSA to which Tony Newton referred in his letter to you of 15 May. We cannot go into the fight to secure more inward investment with self imposed restraints which our competitors will increasingly use to their advantage. I therefore believe very strongly that the changes that we are proposing should be made; as I say, my PES bid reflects this.

Regional Enterprise Grants

I have a bid for £1.5m in 1991/92 and £2.5m in 1992/93 against the background of the consideration being given to extending the Recharbon areas.

/Development Board

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Development Board for Rural Wales

My bid is £1.7m - £1.8m - £1.9m. These figures assume the retention of certain additional receipts. The bid is to fund a 3 year Enterprise and Action initiative in rural areas. The objective is to stimulate enterprise in the deeper rural areas of the Board's territory where the problems of rural deprivation are most acute and where the difficulties of agricultural adjustment are greatest. The programme would include the provision of village workshops and enterprise centres, business advice and expansion schemes, school-industry liaison and enhanced social development support.

Regional Development Grant

I naturally expect to be able to identify savings in 1992/93 as the RDG schemes draw to an end. I have asked my officials to undertake further analysis of the claims that have been submitted and the likely pattern of expenditure and I will write to you again about this with our best forecasts as soon as I can.

Flexibility

I referred earlier to the need for more flexibility in the operation of RSA and in the application of regional assistance support measures generally. I will want to discuss with you in the Survey how this might be achieved so that we can deploy the resources available in a way that is best suited to developing and changing circumstances. A summary of all my industry bids is set out in the attached table.

Departmental Management Plan

I shall be writing to you in the next few days about running costs and the Departmental Management Plan.

I now turn to other programmes.

Home Improvement Grants

As I explained in my letter of 13 March the combination of low incomes and bad housing is such that the new mandatory housing grant system will be much more expensive to implement in Wales than in England. Under these circumstances, and contrary to what you imply in your letter of 28 March, it will be quite impossible for me to meet the additional demands that this system will impose from either my existing baseline or any formula consequentials that may be forthcoming.

/I therefore have

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I therefore have no alternative but to register a specific bid. I have already let you have my initial assessment of what the costs of the new system are likely to be in Wales. I understand that these figures are still subject to change, however, in the light of discussions currently taking place between officials.

Housing Revenue Account Subsidy

My letter of 20 March explained why I could not accept that future adjustments to the Housing Revenue Account Subsidy baseline should be derived by means of the Block formula, and indicated that changes to provision - including those arising from the application of a different rents policy - should be agreed by means of a separate negotiation. In the absence of any indication to the contrary since then I assume that you are content with this proposal.

As with Home Improvement Grants I am not yet in a position to submit a fully quantified assessment of the necessary changes to the HRAS baseline. I obviously want to ensure that the technical assumptions underlying this are consistent with those being adopted by Nick Ridley. Our officials are in touch about this. As soon as the position has clarified and I have had the opportunity to consider the implications for rent guidelines I shall write to you again.

Local Authority Receipts

You recognised during last year's Survey the perverse effect of the disproportionate level of local authority capital receipts in England on my Block resources. Due in part to the introduction of the New Planning Total, it is too early to judge whether my Block is likely to be further adversely affected. I certainly hope not. But clearly if it is I shall need to take this up with you in the course of this year's Survey.

Other Matters

There is one other matter to which I should refer at this stage. You will know from the previous two Surveys how concerned I am about the pressures which I face in the social programmes which fall within the Block, and this is likely to be the more so this year with the need in particular to ensure that resources are available to implement the NHS review.

Last year I raised with you the particular difficulty that arises because I always have to divert additional resources, over and above the formula consequential, into NHS pay as a result of the older age structure in the NHS in Wales.

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There may be other issues which will arise from the proposals that will be put to you by colleagues and their implications for the formula arrangements, but you will appreciate that I cannot even get a sighting shot on these until I have seen the bids from colleagues. I may need to return to this later in the Survey.

You have asked me to report any new or increased contingent liabilities that are likely to arise during the Survey period. The only such liability so far identified arises from the possible effect upon the water table in South Cardiff of the Cardiff Bay Barrage. Consultants employed by the Development Corporation estimate that some £6 million may be required to cover the costs of possible remedial works. Your officials are already aware of this. Whilst it is not certain that this liability will materialise during this survey period I thought you would nonetheless wish me formally to advise you of it at this stage. The £6 million is, of course, already included in the estimated total Barrage costs of £113 million.

I am copying this letter to the Prime Minister.

PUBLIC EXPENDITURE SURVEY 1989
INDUSTRY, ENERGY, TRADE AND EMPLOYMENT

£000's

	1990/91			1991/92			1992/93		
	Baseline	Bid/ Saving	Revised Baseline	Baseline	Bid/ Saving	Revised Baseline	Baseline	Bid/ Saving	Revised Baseline
<u>Industry</u>									
WDA (Net)	73.734	+28.271	102.005	75.319	+19.471	94.790	77.202	+14.907	92.109
DBRW (Net)	10.269	+ 1.670	11.939	10.527	+ 1.770	12.297	10.790	+ 1.945	12.735
DBRW - Housing Subsidy	2.463	-		2.530	-		2.593	-	
Regional Selective Assistance	61.171	+11.800	72.971	62.700	+16.200	78.900	64.268	+27.000	91.268
Regional Dev Grant 1	.614)			.629)			.645)		
" " " 2	42.985)	To follow		33.659)	To follow		34.500)	To follow	
RDGs to LAs	.021)			.021)			.022)		
Regional Enterprise Grant									
1 Investment	5.600	-		5.740)			5.884)		
2 Innovation	1.800	-		1.845)	+ 1.500	9.085	1.891)	+ 2.500	9.275
Misc Support	.389	-		.402	-		.412	-	
<u>Employment</u>									
LA Careers Service									
Credit Approvals	.372	-		.381	-		.391		
Specific Grants to LAs (current)	1.823	-		1.868	-		1.915	-	
	201.241			195.621			200.513		



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