

Response May 2010

## Delivering private sector growth

### CBI response to the economic renewal programme

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As the UK emerges from the worst recession since 1921, the Assembly Government must outline an ambitious all-government plan to grow the private sector and re-balance the economy. As Wales' economic recovery will be led by private sector investment, the Assembly Government must redirect all government activities towards a single goal of creating a more prosperous and sustainable private sector. A thriving private sector not only provides employment and sustains communities but it reduces the pressure on the state and supports wider social and environmental ambitions.

The Assembly Government must not miss this critical chance to put the Welsh economy back on track. Only the private sector can increase the country's prosperity and deliver a low-carbon economy. After a period of rapid public sector expansion and economic stagnation, a rebalancing of the economy is urgently needed. Growing the private sector must now be the Assembly Government's overarching goal.

The majority of Welsh businesses are exposed to global competition, and must keep driving up productivity to remain competitive. Businesses can only grow if the underlying business environment is supportive. It must be recognised that publicly-funded support services are not the main driver here.

Substantial rises in public spending are over for the foreseeable future. The Assembly Government's budget may be cut by over £2bn over the next three years but it must focus necessary fiscal consolidation on current spending, rather than on capital investment, which is vital to our future prosperity.

The Assembly Government must also make the right choices about those elements of public spending that are necessary to support jobs and investment in the future, and which therefore need protecting through a period of fiscal austerity. Obvious examples would include spending on skills, innovation, energy, next generation broadband and transport infrastructure.

Private sector growth is currently being hindered by the Assembly Government's dominant role. We must fundamentally reappraise what the proper role of the Assembly Government is in a modern global society. We believe the government should focus on what it can do best; focusing its activities on where it can add most value to the economy- such as supporting training and innovation. This also means it must stop doing things it does badly and allow Wales' third and private sectors the chance to grow.

The outcome of the economic renewal programme must not be 'business as usual.' The reforms that must take place are for the whole of the Assembly Government- not just the Department for the Economy. Government and business must now work together to grow existing and new companies in Wales.

This brief outlines the actions needed to deliver that framework for growth. The five main recommendations for the Assembly Government are:

- **Recognise the need for radical change.**
- **Make growing the private sector the overarching goal.**
- **Choose most effective deliverer of public services.**
- **Radically improve the business environment.**
- **Refocus business support.**

### Recognise the need for radical change

In our response to *A Winning Wales* in 2001, the CBI put forward a 'competitiveness strategy' built on four key pillars supporting economic success- transport, planning, the labour market and R&D. We highlighted these as four areas the Assembly Government could realistically improve. We continue to believe that it must begin to focus its efforts in these four areas if it wants to grow the economy.

#### **After a decade of rapid global growth and a doubling of the Assembly Government's budget, the Welsh economy remains weak**

- Wales remains the least competitive part of the United Kingdom *source: 2010 UK Competitiveness Index*
- Regional GVA per head in 2008 placed Wales as the lowest performing UK region- a position it has held since 1998 *source: Welsh Assembly Government*
- Relative prosperity in Wales has fallen over the last 10 years to 74% of the UK average *source: ONS*
- Manufacturing as a share of GDP has shrunk from 38% in 1995 to 17% in 2007 *source: ONS*
- Spend on R&D is 60% of UK average *source: UK Competitiveness Index*
- Public expenditure as a share of GDP has risen from 50% in the 1990s to almost 70% in 2010- *source: Centre for Economics and Business Research*
- Unemployment stands at 133, 000, up 25% on the same period last year- higher than the UK average. *Source: ONS*

In our response to *Wales: a vibrant economy* in 2006 the CBI again put forward a 'competitiveness strategy.' We called on the Assembly Government to make the private sector its number one priority and give the sector more room to develop and grow. Given the continued poor performance of the Welsh economy, we once again call on the Assembly Government to make growing the private sector its overriding priority.

Lack of demand remains the primary constraint on Welsh economic growth. The home market is small; one of the main difficulties facing businesses in the more peripheral parts of Wales is the small size of the local market, and the small population catchment area. Welsh businesses need to have access to large external markets - both in the UK and around the world. Rapid growth in market economies is associated with greater international trade and investment linkages.



Wales, however, does lead the UK tables on per capita economic development spend- and has done so for over four years. In 2009 the Assembly Government spent £107 per capita- £10 more than the North East of England Regional Development Agency and £77 per capita more than the South West Regional Development Agency. The Assembly Government has allocated £288m to economic development spend for 2010-11- some £140m more than was spent in 2001 by the WDA. This is down from a high of £388m in 2006-7. Since 2001, almost £2bn has been spent on economic development projects in Wales.

Against this backdrop, a fresh approach to growing Wales' economy is undoubtedly needed. The economy has not flourished under devolution, despite the government having sufficient policy and legislative tools to make a real difference.

## Make private sector growth our overarching goal

As shown above, the Welsh economy has underachieved. Even over the relative boom of the last decade Wales' economic growth has been sluggish at best. Wales can perform better than this and the achievement of that improved performance should focus the attention of every single person inside the Welsh Assembly Government.

We believe the solution lies in the Assembly Government making the economy its top priority. Its central purpose should be creating a more successful and vibrant country, giving opportunities for all Welsh people to flourish through increasing sustainable economic growth. Every Assembly Government policy should be measured against how it improves business competitiveness.

Greater economic growth will deliver more employment, improve people's quality of life as well as enable progress on social justice aims such as standards of education, health and the environment.

As the Bevan Foundation stated in *Setting the agenda: priorities for public policy in Wales 2007-2012*, 'the fact that Wales still has a higher percentage of people of working age not in paid employment than any other part of Britain has profound implication for economic and social prosperity, health and well-being of the whole nation, now and for the future.' In market economies such as the UK, it is the private sector that is the main engine of growth.

## The private sector is Wales' only hope for future growth

The private sector is where our focus must now be if Wales is to meet our overarching challenge of poverty reduction and increased employment. In the face of tough public sector spending cuts, growth, jobs and opportunity will be found in the private sector- not the public. The Assembly Government must seize this opportunity to restructure its activities towards the single goal of growing our private sector economy.

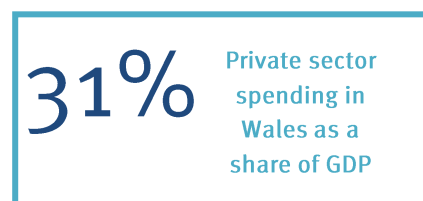
Small companies have an important role to play in that growth and they are critical to the economy of many of our towns. But Wales is in fact more dependent on large companies than England, and Assembly Government policies need to reflect this. While SMEs amount to 99% of all businesses in Wales it is our largest 1.8% of companies that contribute 69% of national turnover, employ over 53% of total private sector employment and spend billions a year with their Welsh supply chains. Corus, directly employs 7000 people in Wales but their business supports 35,000 SME employees.

## Wales has key advantages

- Part of the sixth largest economy in the world
- Tariff-free access to UK and EU markets
- Common UK framework of laws and regulations, though with an increasing policy divergence
- Positioned only two hours away from the biggest global financial centre
- Well-established industries
- Manufacturing productivity is 8.6% above UK average
- Highest employee retention rates in the UK
- A network of HE institutions across Wales
- Potential for growth in low-carbon goods and services
- An attractive physical environment
- Indigenous raw materials
- Huge potential for low-carbon growth
- The ability, through devolved government, to develop policies tailored to our needs

## The public sector is crowding out the private sector

The public sector has delivered benefits to the Welsh economy; it has been a buffer against the unforgiving winds of globalisation. However, it is now too dominant and is making it more difficult for the private sector to grow. The private sector in Wales struggles to find new talent due to the level of remuneration and pension offers promised by neighbouring public sector employers. In Wales the differential in favour of the public sector actually rises with earnings. This can make it very difficult for a company to attract the right skills to grow and expand.



The number of people employed in the UK public sector has increased to its highest level since 1992. According to the ONS, 30% of total employment in Wales is now in the public sector- compared to a UK average of 21%. In parts of Wales public sector employment is even higher, reaching 38% in Swansea and 33% in Cardiff. Last year, public sector employment in Wales actually rose by 8,000 while private sector employment fell by 45,000. This is not a sustainable approach to economic growth.

## Choose the most effective deliverer of public services

While the Assembly Government faces the impact of budget cuts and efficiency drives, people's expectations for public services continue to rise. Individuals and communities want and need more efficient and responsive services. They want innovative services that put them in control. Faced with the joint impact of reduced budgets and increased public expectations, the public sector must begin to redesign service delivery and act as a commissioner of services, rather than always as a provider. Strategic commissioning is more than just procuring services; it is about delivering a range of improved services with limited resources.

Elsewhere in the UK, government has already become a commissioner of services; where once most local services were delivered by the local authority, increasingly they're provided on behalf of the council by private companies, social enterprises or charities.

With Welsh public spending facing cuts, a credible strategy is needed to maintain services. This needs bold thinking about the structure of our public services and where and how new approaches are used to drive change.

Commissioning could deliver significant long-term savings for the Assembly Government as unlike England, Wales has been slow to adopt this approach. It would also help grow Wales' private and third sectors, providing a boost to the economy and local communities.

### Case study: crowding out of the private sector

A vehicle depot, owned by a Welsh local authority, has recently decided to utilise its spare capacity and open its doors to offer car servicing to the public and fleet servicing to local companies. It now competes unfairly with private sector garages in a part of Wales where business activity is already low. This is just one small example of the damaging impact of the public sector crowding out the private sector in Wales.

When deciding how best to deliver public services, the Assembly Government must create a level playing field that allows all providers to be chosen solely on the quality of the services they provide.

Under this approach, the government would rightly retain the responsibility for deciding spending priorities and for monitoring delivery standards. But the delivery organisation is that which can deliver best value, whether in the public, private or voluntary sectors. In order to maximise the opportunities for private sector growth, we believe there should be a presumption in favour of outside commissioning. The

economic renewal programme should identify growing this civic capacity as an explicit goal.

The CBI's report *Doing more with less* identifies a series of practical steps the UK government could take to increase efficiency while delivering better quality frontline services. The provision of non-core public services by the private and third sectors could save the UK government £30bn by 2015-16. This suggests savings to the Welsh public sector of c£1.5bn.

### Key barriers to private sector growth which must be addressed

- Slow and uncertain planning system
- Growing regulatory burden
- High energy costs
- Taxation- local and national
- Poor access to next generation broadband

### Recommendations to the Assembly Government:

- **Recognise the challenge:** The Assembly Government's economic renewal programme must recognise the scale of the challenge facing the Welsh economy and that economic growth can only be achieved by growing the private sector-not the public sector.
- **Commit to growing the economy above all else:** The Assembly Government must make fixing the economy its top priority. It must recognise the link between growing a prosperous economy and our wider social justice ambitions.
- **Grow third and private sector capacity:** The Assembly Government must commission a review of the Welsh public sector to identify areas where the commissioning of public services to the private and third sectors would increase efficiency and grow the economy while maintaining service standards.

## Radically improve the business environment

The Assembly Government must accept that firm-level intervention can only ever reach a very small minority of companies in Wales. Therefore its prime economic development responsibility must be to make the underlying business environment the very best it can manage. Such a goal must be the responsibility of every Assembly Government department – not just the Department for the Economy and Transport.

The importance of the business environment to a nation's competitiveness is well established. The World Bank's well regarded 'ease of doing business index' ranks the global economies based on the quality of their business environment. Since the index was created in 2001, over 800 academic papers have been written showing the strong link between improving these factors and economic growth.

**1.8% = 69%**

**Wales' largest companies contribute 69% of our national turnover**

As the First Minister stated in *Time to lead* '...it is large companies that bring the research and development and the added value and train the specialist engineers and others that we need to compete for the high value jobs, these companies-like Corus, British Gas, Airbus, BT and General Dynamics... are what I would call the anchor companies of our economy'. We agree with the First Minister. As the statistic above shows, Wales is more depended on large companies for jobs and investment than England. Wales' anchor companies are valuable employers, we need to understand their pressures and do all we can to help overcome them.

### CBI's definition of an 'anchor company'

- Large economic weight
- Major Welsh employer
- Invests in employees
- Invests in innovation
- Environmentally aware
- Responsible supply chains
- Contributes to local community and society

**'It is large companies that bring the added value that we need to compete for the high value jobs, these companies are what I would call the anchor companies of our economy'.**

**Carwyn Jones, First Minister**

In order to secure a new kind of relationship with anchor companies we believe Welsh Assembly cabinet ministers should be twinned with anchor companies, leading on relationships with those industries and acting as an informed voice around the cabinet table.

An established measure of the business environment is the 'the UK Competitiveness Index' produced annually by UWIC. The results for 2010 place Wales as the least competitive region of the UK. This is despite the last 10 years seeing unparalleled government action to support economic growth. Since 1999, Wales has had two economic development strategies, a doubling of the Assembly's budget, £250m of Communities First funding, £2bn of economic developing spending, £3.5 billion of European funding, and a further £3.5bn of European convergence funding over the period 2007-2013. It is clear that past efforts, while well intentioned, have not yet delivered the improvements we all hoped to see. The Assembly Government must grasp the opportunity presented by the economic renewal programme to realign all government activity towards the single goal of creating a more prosperous, competitive and sustainable private sector.

For CBI members, a competitive business environment must have a responsive planning system, high educational standards, a demand-led skills system, twenty first century infrastructure, support for innovation and entrepreneurship, effective public procurement and better regulation and legislation. Improving these key areas- which are all within the devolved competence of the Assembly Government- would strengthen the economy and also help our transition to a low-carbon economy. If this chance is grasped, the Assembly Government has a real opportunity to restore Wales' competitiveness with other parts of the UK and Europe.

### Infrastructure

An essential part of a competitive economy is reliable and modern 21<sup>st</sup> century infrastructure. Businesses need modern roads, rail, air and ICT infrastructure in order to support their global activities. Companies are increasingly making investment decisions based on a country's ability to offer modern, attractive and efficient infrastructure that connects them to major markets.



Efficient roads remain a constant priority for business across the whole of the UK. It is critical that the infrastructure is in place to underpin business efficiency and competitiveness. And the priority is to connect Welsh business with its key markets.

Over the last ten years, Wales' investment in infrastructure has lagged. Local government has a £5bn infrastructure gap with England, including schools and housing, and the cancellation of the new M4 leads many in the business community to question the ability of devolution to deliver major infrastructure projects. The Assembly Government must work with the private sector to launch an ambitious Wales-wide PPP programme which seeks to radically modernise Wales' infrastructure and capture the knock-on benefits for Wales by leveraging in private investment. The wider economic benefit of such investment has been highlighted by the Assembly Government's own research.<sup>1</sup>

There is a danger that capital spending will be increasingly squeezed as the pressure mounts to maintain current spending. This should be resisted, but it will be easier to maintain infrastructure investment if partnerships with the private sector are embraced.

The strategic capital investment fund, established in 2008, was a promising start. Its commitment to 'use public-private partnerships where appropriate to deliver our priorities' was very welcome.<sup>2</sup> However, we are not aware of any further progress. If Wales is to benefit from efficient and effective citizen-focused services the economic renewal programme is a golden opportunity to take a fresh look at the role innovative PPP projects could play. A Wales-wide PPP infrastructure programme would greatly increase the scale and pace of current plans to improve the physical infrastructure of many of Wales' schools, hospitals and roads.

The challenge is to create the right environment for PPPs to flourish – PPPs need strong political will, the right commissioning skills and a fair market for suppliers to operate. The case for PPPs should be articulated in terms of benefits to the public, for example, improved learning environments for children and social regeneration. Further consideration about how the public and private sectors can collaborate more closely to deliver types of PPP projects, and to understand how we can capture the best lessons from elsewhere, and avoid the mistakes, is also needed.

## Next generation broadband

We agree with the First Minister that digital technologies are a big driver of innovation and growth in the whole economy. A modern digital infrastructure promotes the fast and easy flow of

ideas and information allowing better communication and collaboration between businesses and with their customers. The digital economy will play a pivotal role in Wales' economic recovery and future competitiveness.

A world-class digital infrastructure will be an essential enabler of this knowledge economy and is therefore critical if Wales is to emerge from the recession as a world leader. But access to broadband is not just about achieving commercial goals; it can also play a fundamental role in achieving wider public policy objectives such as the transformation of public services and enabling the transition to a low carbon economy.

Convergence funding provides a critical opportunity for the Assembly Government to deliver next generation broadband access for the poorest parts of Wales. Wales is now the only part of the UK not to have used EU funding to reduce digital exclusion by delivering high-speed fibre access to qualifying areas. Northern Ireland's next generation broadband project is on track to successfully deliver up to 10Mbps speeds to 85% of businesses.

Increasing access is not just about infrastructure. Ultimately increased take-up and use of digital services by both citizens and businesses will be created by demand for high quality digital services and content, skills to utilise the technology, and confidence in the safety and security of the digital environment. These factors are just as important as the infrastructure elements of the strategy and the government has a key role in stimulating demand.

## Planning

Improving the performance of the land use planning system is one of the key challenges for facilitating sustained future economic growth in Wales.

Planning is possibly the one area where there has been virtually no improvement in service, despite increasing costs. Industry still faces lengthy delays in processing applications, and the quality of the service and advice offered differs considerably throughout Wales. In short, the problems faced by business by the planning system remain as great as ever. This issue was highlighted in our 2006 response to Winning Wales where once again we suggested improvements in planning policy, as well as recommendations to support planning procedures. We call again for these same reforms in this response.

A presumption in favour of quality development must be the starting point accompanied by policies to stimulate investment to meet the most important requirement for Wales at present, which is to boost economic performance.

The recent review into the planning application process was a useful beginning but there remain serious problems that must be solved. The review has suggested some useful technical improvements but Wales needs a strategic, forward looking independent review of the planning system that supports economic growth and the transition to a low-carbon economy.

We believe there is a case for a more strategic approach to large energy infrastructure projects, especially renewable energy. We

<sup>1</sup> *The Economic Impact of Large Scale Investments in Physical and Intellectual Infrastructure A Review of International Evidence*

<sup>2</sup> [http://www.assemblywales.org/bus-home/bus-guide-docs-pub/bus-business-documents/bus-business-documents-written-min-state/dat20080512-e3.pdf?langoption=3&ttl=Strategic%20Capital%20Investment%20Framework%20\(PDF%2C%2025-3kb\)](http://www.assemblywales.org/bus-home/bus-guide-docs-pub/bus-business-documents/bus-business-documents-written-min-state/dat20080512-e3.pdf?langoption=3&ttl=Strategic%20Capital%20Investment%20Framework%20(PDF%2C%2025-3kb))

support the Infrastructure Planning Commission (IPC) which promises a more effective approach for very large projects. Wales needs a similar joined-up approach for slightly smaller, but no less more important, projects. We are not calling for a replica of an IPC but an approach which takes the key benefits of an IPC and applies it to Wales' unique situation. Urgent reform of Wales' planning system will enable Welsh business to continue to invest with confidence in a new generation of energy efficient technologies.

### Education and skills

In a globalised economy the skills of our people are a vital resource. Developing our skills base is key to business competitiveness, and to realising the goal of higher growth and sustained employment in Wales. Business has a responsibility to develop the abilities of its own staff – but the task of raising our skills levels must be a partnership between employers, government and individuals.

The points we highlighted in our previous responses remain valid today – such as the need to improve the availability and quality of careers guidance, education business links, and tackling employability skills. Businesses continue to struggle with the poor levels of basic skills and employability skills of those entering the workforce, and already in work. Educational attainment levels remain a continuing source of concern, and companies are now talking as much about education and schools, as they have talked about skills in the past.

A recent OECD report ranked Wales' secondary school pupils below 33 other countries for standards in mathematics and in 28th place for reading. In a world where level 3 skills are fast becoming the minimum level needed for employment, this is simply not good enough. Wales must take radical action to improve the quality of basic skills in primary and secondary schools. The Assembly Government should commit to significantly improving Wales' PISA rankings within the next five years.

The Leitch Review on skills provided a wake-up call for business and government. Its call for a 'radically simplified' demand-led system where funding should follow employer need has not been fully implemented in Wales. We support many of the aims in the Assembly Government's latest skills strategy 'investing in skills' but business has yet to see the full impact of this policy change. We welcome the aspiration of the strategy for a more demand-led education system, however, the chosen approach of a board is a weak version which has little chance of success. Welsh companies are increasingly concerned by the lack of direct funding for skills and training in Wales. Companies in England are able to access such funding and are therefore at a competitive advantage.

The Assembly Government needs to put more purchasing power directly with companies as they are in the best position to determine their own skills and training needs. The Assembly Government must reform the training system to enable

employers to directly drawdown skills funding and spend with the provider that best meets their needs or carry out the training in-house.

Further education colleges are well-established as a major source of training provision. Many already have strong links with employers. The government needs to do more to support colleges to work more effectively with businesses, putting learners and employers in the driving seat to reinforce a demand-led approach. Colleges could become useful 'hubs' for local industry, assisting them with the economic recovery process.

### Innovation

A competitive business sector needs excellent universities to produce the graduates, postgraduates, research and innovation that are required to drive economic growth and deliver prosperity. In our response to the Assembly Government's 2001 economic development strategy 'Winning Wales,' and its successor strategy 'Wales a vibrant economy' in 2006, the CBI stressed the need to develop innovation activity in Wales. In 2010, there remains the same need to increase capacity for R&D activity in Wales so as to support existing industries in Wales, and to attract new higher-value industries.

#### Business priorities for higher education

- Support high-quality research and teaching in increasingly challenging circumstances.
- Raise the numbers and quality of graduates in science, technology, engineering and maths (STEM).
- Ensure all graduates have employability skills.
- Improve the environment for university-business collaboration on research and innovation.
- Encourage more workforce training.
- Support diversity of missions in the HE system to cater for an ever-wider range of student and business needs.

Success for Wales in the global economy will increasingly depend on the development of high-value added sectors in services and manufacturing. These in turn will require a highly trained workforce rich with graduate-level skills- universities are critical to this process. The Assembly Government needs to ensure universities in Wales are suitably resourced and supported to meet growing business needs.

At present Wales trails its competitors in most sectors on both R&D spend and innovation. We are well behind other EU countries, but also most parts of the UK. The problems appear to be deep-rooted and will require significant real incentives and encouragement to turn around. In many cases the focus will need to be placed on getting business to start R&D activity in the first place. For others, growing activity from a base that is

below international benchmarks and, in a few cases, giving real support to world-class R&D players so that they continue to prosper. It must be fully recognised that innovation is as relevant to traditional industries as it is to more traditional R&D based operations.

Strengthening the environment for partnerships in collaborative research and innovation between universities and business is also key. This requires the funding bodies to recognise excellent research that is business relevant, as well as a strategic approach to the pricing of research, taking account of the long-term benefits of the relationship to both sides. This also means introducing innovation vouchers into Wales that would support industrial competitiveness by incentivising demand-led innovation of products and processes in Wales.

### The Welsh pound

The public sector in Wales spends over £5bn a year buying goods and services from suppliers. Wales has a growing reputation as one of the most difficult places in the United Kingdom for public procurement- this has to change. The Assembly Government must commit to reviewing how procurement policy could better support the private and third sectors in Wales and how the tendering process could be streamlined.

In order to remove bureaucracy within the procurement process we endorse the *Barriers to Procurement Opportunity Research* when it recommended:

- Transparency of the PQQ process and feedback could be significantly improved as a priority.
- A simplified and 'fit for purpose' Register of Standard Pre Qualification Data, maintained and managed centrally to avoid duplication for all parties is essential.
- Engagement between SMEs and the public sector can work successfully, given strategic intention and political will. Models of good practice in this regard should be extended across Wales.
- Increased and enhanced training and professional qualification would improve overall procurement performance in the public sector.

Public procurement could be utilised more effectively to grow Wales third and private sectors. We recommend the Assembly Government consider how best it could utilise the recommendations within the Office of Government Commerce's report, *making equality count*, which illustrates how to achieve greater supply chain diversity.

The London 2012 Olympics have created the 'CompeteFor' website which encourages large public and private sector suppliers to diversify their British supply chain. We would encourage Value Wales to consider what lessons it could learn

from the success of this initiative to increase the number of companies in Wales supplying the Welsh public sector.

### Deregulation- an ignored advantage

The level of regulation remains a key concern of Welsh businesses, with many businesses struggling to cope with the relentless pace of new measures. For business, and small firms in particular, this translates into time and money spent on complying with government imposed requirements rather than wealth creation. Business is not anti-regulation but we are opposed to unnecessary, ill-conceived and poorly implemented regulation. In a recent National Audit Office survey, complying with regulation was ranked second in a list of business concerns, behind 'attracting and retaining customers'.

#### Case study: cumulative impact of regulation

There are a number of legislative and regulatory proposals being pursued by the Assembly Government which will impact on some or all parts of the construction sector in Wales. These include:

- The provisions of the Waste Measure to widen landfill bans and charge for site waste management plans.
- Ambitious zero carbon development standards
- Wales-specific building regulations
- Mandatory fire sprinklers for new housing

The Assembly Government has increasing powers yet it never uses these powers to deregulate. Since the Assembly's creation in 1999 there has never been a strategic approach to monitoring the impact of Assembly regulation or to reduce its impact. The Assembly Government must take a more systematic approach to improving the regulatory framework for business in Wales. Early actions include: appointing a deputy minister with responsibility for deregulation, introduce an 'administrative burdens reduction programme' that would reduce the impact of Assembly Government regulations, reform and strengthen regulatory impact assessments, and introduce regulatory budgets. This process should be co-ordinated by the Director-General of Public Services who should act as 'executive sponsor', reporting periodically to the Minister for Public Services.

A deputy minister responsible for deregulation should be tasked with establishing an effective approach to deregulation. His/her job should be to introduce an 'administrative burdens reduction programme' with the aim of reducing the regulatory burden by 25% within four years. A similar programme, introduced in England in 2007, is estimated to have saved UK businesses £1.9bn per annum. In Wales our approach must include urgently tackling the cumulative impact of Assembly regulations on the private sector. Whilst regulatory impact assessments are developed for individual regulations, the



cumulative impact of these measures on key sectors is not assessed.

The Assembly Government must carry out robust regulatory impact assessments that enable policymakers to assess the need for and impact of new regulation on the private sector. Current Welsh RIAs are largely tame and ineffective versions of the assessments carried out in Whitehall. RIAs can and should be an effective tool to determine the appropriate policy response- which should only require regulation as a last resort.

The failure of government departments to begin the RIA process at the earliest stages in the policy making process is seen as the system's biggest structural flaw. The CBI, UK government and successive National Audit Office reports have highlighted this fundamental failure in departmental approaches to RIAs. It is an error the Assembly Government is also making. The National Audit Office (NAO) stated 'RIAs are ineffective if started late... and were often seen by officials as a bureaucratic task rather than being integral to the process of policy-making.' The May 2007 UK government reforms have changed this, requiring RIAs from the earliest stages in the policy formulation stage. The Assembly Government must follow this lead.

We believe consideration should be given to requiring some form of RIA for all significant Welsh Assembly Government policy proposals- not just Assembly Measures and subordinate legislation.

Given recent economic events, wider regulatory budgets for Welsh Assembly Government departments- covering all activity impacting on business in Wales- so that proposed regulation is better prioritised, targeted, costs minimised and the benefits maximised; should be considered with a new sense of urgency. Reduced regulation could deliver huge benefits to businesses across Wales and be implemented at very little cost to the Welsh Assembly Government.

### Legislation and globalisation

As the Assembly Government gains more legislative powers it is more important than ever to ensure the potential impact of new legislation is analysed and alternatives to legislation are actively pursued. Legislation, for any country with a global economy, should be a last resort, not a first response.

We recognise the Assembly Government's desire to lead on certain issues but government goals can often be achieved by working with the private sector-not against it. Wales has a small private sector, heavily exposed to the pressures of globalisation. As we emerge from a major recession, new legislation must not be an automatic response to a policy objective or political problem. Too often in Wales the decision for new legislation is taken before any work begins to determine the most effective means of achieving political objectives.

### Recommendations to the Assembly Government:

- **Make Wales the best place to do business:** The quality of a country's business environment directly impacts economic growth. The Assembly Government must work with all levels of government to make improving the business environment a key priority.
- **Twin cabinet ministers with Wales' anchor companies:** In order to secure a new kind of relationship with anchor companies, Welsh Assembly cabinet ministers should be twinned with anchor companies, leading on relationships with those industries and acting as an informed voice around the cabinet table.
- **Deliver twenty-first century infrastructure:** Modern, efficient infrastructure that provides access to global markets is an essential part of a competitive economy. The Assembly Government must analyse Wales' infrastructure needs and form partnerships with the private sector to deliver major improvements in the near future. This must involve increased capacity through infrastructure partnerships (every 10 year delay in delivering 21<sup>st</sup> century schools is another generation of pupils lost).
- **Presumption in favour of development:** Wales needs a forward-looking independent review of the planning system to ensure it effectively supports economic growth and the transition to a low-carbon economy. The planning system in Wales needs rebalancing and a presumption in favour of quality development is now needed.
- **Direct access to skills funding:** The Assembly Government must reform the training system to enable employers to directly drawdown skills funding and spend with the provider that best meets their needs.
- **Reform public procurement:** The Assembly Government needs to reform public sector procurement to more effectively support small companies in Wales and elsewhere.
- **Deregulation voice around the cabinet table:** The Assembly Government has largely ignored the deregulation agenda. This must change. We recommend the appointment of a Deputy Minister for Deregulation whose job would be to reduce the impact of Assembly Government regulation on the private and third sectors and conduct annual deregulation budgets.
- **Legislation- a last resort not a first response:** We recognise the Assembly Government's desire to lead but government goals can often be achieved by working with the private sector-not against it. Wales has a small private sector, heavily exposed to the pressures of globalisation. As a result, legislation should not be an automatic response to a policy objective or political problem.

## Refocus business support

In 2009 the Assembly Government spent £107 per capita on business support- £10 more than the North East of England Regional Development Agency and £77 per capita more than the South West Regional Development Agency. The Assembly Government has allocated £288m to economic development spend for 2010-11-some £140m more than was spent in 2001 by the WDA. This is down from a high of £388m in 2006-7. Since 2001, almost £2bn has been spent on economic development projects in Wales. However, this has not changed Wales' position as the lowest performing region in the UK- a position it has held since 1998. The Assembly Government has a valuable role to play in achieving things private companies cannot do alone- risk capital provided by Finance Wales and trade missions are two examples. The provision of other forms of business support needs to be radically reappraised.

Better use should be being made of status that West Wales & Valleys currently has over other areas. Alongside Cornwall, currently it has the ability to offer the highest levels of aid to investment of any UK region - we must utilise effectively that major competitive edge to our advantage in building infrastructure. Sadly, it seems quite likely that this area will qualify for a third round of European regional funding.

Basic business support initiatives, such as advice on starting a business, employing your first staff etc are valuable for first time entrepreneurs and therefore should be retained. However, the Assembly Government needs to review the method of delivery. We believe the private sector is in a better position to respond to the demands of business for this type of support. The Assembly Government should use this as an opportunity to grow professional services capacity in less prosperous parts of Wales by allowing the private and third sectors to deliver these services.

We question the macroeconomic benefit of other business advisory services. Under the current system it is almost impossible to judge the impact and cost effectiveness of business advisory services. If the Assembly Government does decide to continue to provide such services, there must be far more transparency and monitoring of outcomes - not activity.

The availability of capital is likely to remain an issue for small businesses in Wales; as a result the Assembly Government should continue to offer repayable financial assistance. We recognise too the valuable role of Finance Wales in providing risk capital – on broadly commercial terms - to Welsh companies where private equity firms are limited in their presence.

There are also areas where a government can achieve things that private companies cannot – trade missions and access to a global customer base may be examples of this. We urge the Assembly Government to work with and exploit to the utmost the resources of the UK government in doing this.

The Assembly Government also has a valuable role in stimulating different sectors to work together, for example,

universities and businesses. As our landmark report, 'Stronger Together' makes clear, effective collaboration between the sectors is best achieved by putting purchasing power into the hands of business. The early results following the introduction of innovation vouchers in England and Scotland are compelling evidence of this. We urge the Assembly Government to follow their example and introduce innovation vouchers in Wales.

## Grants

This is a challenging issue to be tackled. We have developed a culture of grant receipt in order to fund investment in Wales. We acknowledge the role of grants in making things happen that would otherwise not, and in lowering the ROI hurdle for new investment. However, the majority of our members recognise the distorting nature of such interventions and the temptation to use grants to support a business that is likely to ultimately fail, or to leave Wales at some stage. There is also a deadweight argument against providing grant support.

We therefore endorse the Assembly Government's plans to move towards an investment culture, where any Welsh Assembly Government financial assistance is repayable. Grant assistance- provided by local government and the Assembly- should be refocused on investment to support the transition to a low carbon economy in Wales.

## New Foreign Direct Investment

There is, however, one area where a move away from grant assistance for business investment would have serious consequences, and where the Assembly Government may wish to continue provision. Foreign Direct Investment (FDI) has made a huge contribution to the Welsh economy for decades. The fledgling Admiral business was an inward investment project and is now Wales' sole FTSE 100 company. There are currently over 500 foreign owned companies in Wales. There remains a worthwhile FDI market of which Wales can get its share but we need to get better at attracting it.

The Massey review made clear the flaws in our existing approach to FDI. The Assembly Government has significantly more resources at its disposal for supporting FDI activity than English regional development agencies but in 2008/9 Wales was the worst performing part of the UK. So we must not confuse Wales' recent lack of success in winning FDI with a drying up of the market. As the Massey review stated:

- FDI projects in Europe have risen for the last five years to over 3,700 per annum
- A total of 148, 000 jobs were created in 2008 by FDI investment into Europe
- New projects have outpaced expansions
- Mergers and acquisitions, including joint ventures have grown

To capture the global FDI market Wales must change its product offering and approach. Our old FDI offer was based on low wages, high grants and cheap land and is no longer tenable. As the Massey review of International Business Wales makes clear 'with the advent of globalization and the emergence of eastern Europe and other more cost effective options, this leading position has now been eroded.' The key to attracting future FDI is a new offer based on technology and knowledge not lowest labour costs and a reformed IBW.

#### An inward investment strategy must accept

- **FDI investment will have cycles.** We will therefore have to continue to reinvest in future investment projects by companies or see closures – and closures may happen anyway. This has to be accepted as part of the natural process, not seen as a failure.
- **We have to be much more selective as to the companies and projects we pursue.** Currently we chase anything and our offering is not well defined. We need to be much more focused and be prepared to turn down projects which do not match our focus.
- **We need to understand why we have been unsuccessful** in recent years and change our systems.
- **An excellent business environment is a necessary condition for attracting FDI today.** So focusing on improving our business environment and infrastructure will support new and existing FDI efforts.
- **But this is not sufficient - we will have to offer financial inducements** – grants – and these will not be repayable. If we want to play the game we have to play by the rules that the other players are using. A great business environment, if we succeed in creating one, will not be enough.

If the Assembly Government decides it does not want to continue to attract FDI, and it wishes to move away from grant aiding investment projects, then there will be consequences for our existing stock of FDI companies. Many of today's 'anchor companies' are here as a result of past successful efforts. Many of these are subsidiaries of global companies that do consider grant assistance when deciding on future investment. Over time therefore, and for some companies in the short term, we will see disinvestment (closure) by a significant number of our existing stock of FDI companies.

#### Recommendations to the Assembly Government:

- **Focus on providing what the private sector cannot:** Assembly Government should continue providing services the private sector cannot. For example, trade missions and access to a global customer base. It should continue to collaborate with the UK and EU to maximise such opportunities for Welsh companies.
- **Reduce firm-level interventions:** Given the growing constraints on public funds and the pressure to focus on the above priorities, we recommend the Assembly Government significantly reduce the use of firm level interventions. If they do continue, there must be significantly greater transparency of spend and outcomes.
- **Move towards an investment culture:** We endorse the move towards an investment culture, where Assembly Government financial assistance is generally repayable.
- **Refocus FDI activity:** There remains a viable global foreign direct investment market. The Assembly Government needs a new approach to FDI that includes an understanding of why we have been unsuccessful in recent years and an action plan which is much more focused and selective. The action plan must accept that FDI investments often have cycles and FDI activity will need continued reinvestment.
- **Introduce innovation vouchers:** Wales needs a new approach to innovation. High-growth SMEs and large industries need greater support to innovate products and processes. Such activity should be supported through the creation of 'innovation vouchers' that would allow for demand-led collaboration between the private sector and universities.

## Summary of recommendations to the Assembly Government

### Recognise the need for radical change

**Recognise the challenge:** The Assembly Government's economic renewal programme must recognise the scale of the challenge facing the Welsh economy and that economic growth can only be achieved by growing the private sector-not the public sector.

### Growing the economy the number one priority

**Commit to growing the economy above all else:** The Assembly Government must make fixing the economy its top priority. It must recognise the link between growing a prosperous economy and our wider social justice ambitions.

### Choose most effective deliverer of public

#### services

**Grow third and private sector capacity:** The Assembly Government must commission a review of the Welsh public sector to identify areas where the commissioning of public services to the private and third sectors would increase efficiency and grow the economy while maintaining services standards.

### Radically improve the business environment

**Make Wales the best place to do business:** The quality of a country's business environment directly impacts economic growth. The Assembly Government must work with all levels of government to make improving the business environment a key priority.

**Twin cabinet ministers with Wales' anchor companies:** In order to secure a new kind of relationship with anchor companies, Welsh Assembly cabinet ministers should be twinned with anchor companies, leading on relationships with those industries and acting as an informed voice around the cabinet table.

**Deliver twenty-first century infrastructure:** Modern, efficient infrastructure that provides access to global markets is an essential part of a competitive economy. The Assembly Government must analyse Wales' infrastructure needs and form partnerships with the private sector to deliver a coherent infrastructure plan. This must involve increased capacity through infrastructure partnerships (every 10 year delay in delivering 21<sup>st</sup> century schools is another generation lost).

**A presumption in favour of development:** Wales needs a forward-looking independent review of the planning system to ensure it effectively supports economic growth and the transition to a low-carbon economy. The planning system in Wales needs rebalancing and a presumption in favour of quality development is now needed.

**Direct access to skills funding:** The Assembly Government must reform the training system to give employers parity with their competitors in England. Enabling employers to directly drawdown skills funding and spend with the best provider is urgently needed.

**Reform public procurement:** The Assembly Government needs to reform public sector procurement to allow more Welsh companies to bid for public sector contracts at a lower cost.

**A strategic approach to deregulation:** The Assembly Government has largely ignored the deregulation agenda. We recommend the appointment of a deputy minister with responsibility for deregulation, the introduction of an 'administrative burdens reduction programme', reform and strengthen regulatory impact assessments, and introduce regulatory budgets.

**Legislation- a last resort not a first response:** We recognise the Assembly Government's desire to lead but government goals can often be achieved by working with the private sector-not against it. Wales has a small private sector, heavily exposed to the pressures of globalisation. As a result, legislation should not be an automatic response to a policy objective or political problem.

### Refocus business support

**Focus on providing what the private sector cannot:** Assembly Government should continue providing services the private sector cannot. For example, trade missions and access to a global customer base. It should continue to collaborate with the UK and EU to maximise such opportunities for Welsh companies.

**Reduce firm-level interventions:** Given the growing constraints on public funds and the pressure to focus on the above priorities, we recommend the Assembly Government significantly reduce the use of firm level interventions. If they do continue, there must be significantly greater transparency of spend and outcomes.

**Move towards an investment culture:** We endorse the move towards an investment culture, where Assembly Government financial assistance is generally repayable.

**Refocus FDI activity:** There remains a viable global foreign direct investment market. The Assembly Government needs a new approach to FDI that includes an understanding of why we have been unsuccessful in recent years and an action plan which is much more focused and selective. The action plan must accept that FDI investments often have cycles and FDI activity will need continued reinvestment.

**Introduce innovation vouchers:** Wales needs a new approach to innovation. High-growth SMEs and large industries need greater support to innovate products and processes. Such activity should be supported through the creation of 'innovation vouchers' that would allow for demand-led collaboration between the private sector and universities.

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