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Policy Unit

Chapman

PRIME MINISTER

The Policy Unit has now completed its work on the subject of jobs. We have visited Merseyside, Consett, Corby, the Scottish Development Agency area, London Docklands and the Highlands and Islands Development Area. The distillation of our thoughts in this paper may be of some assistance in Sunday's meeting and thereafter in discussions with Tom King.

The long-term solution to unemployment is the creation of an economy where markets function properly. Companies have to respond to demand, have to find it profitable to invest, need to draw on skilled people for design, marketing, production and management; and people need a relatively free labour market so that they can move around with ease.

Much of the work under way within Government will help in this task. The Youth Training Scheme and technical and vocational initiative should help in training people into jobs. The MSC initiative to make training more relevant should be pursued vigorously. The Budget has begun the process of removing bias in the tax system against employment and in favour of capital investment. The changes already undertaken in trade union law, and the modifications to the Employment Protection Act are helping create a freer labour market, but much more remains to be done, and Tom King's Inquiry into the next steps is vital. The competition policy initiative can also assist in encouraging new business and creating new opportunities.

Policies towards small companies, international trade and the lowering of administrative burdens also need carrying further, and are a vital part of any programme to make markets work. For example, there are too many local authority licensing regulations; tax is still too bureaucratic and complex for small employers; Wages Councils are troublesome; the Employment Protection Act has not been sufficiently neutered; and the small business measures need rationalising. Similarly, the housing market needs improvement so that more rented accommodation is available in areas of better job prospects.

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Job-Creation in the Regions

In our visits to some of the most intractable problem areas in the UK, we were looking to see if there were any common threads underlying both success and failure in generating new activity. We saw nothing that persuaded us that direct Government involvement, by offering large subsidies or inducements to companies, would work. Indeed, on Merseyside part of the problem was the inducement offered to firms like BL and Ford to set up plants in relatively hostile conditions which could not stand the test of time. Our investigation of Enterprise Zones did not encourage us to believe that they offered a great deal, and many features of the Urban Programme represent the worst kind of expensive tinkering. Whilst there was evidence of some success in the Scottish Development Agency's area of activity, this seemed to owe more to their persistence and their dedication in hammering home the message that their area was a good place for electronics companies to locate, than to their role as a kind of Scottish NEB.

The main lessons which emerged from our survey of local projects were:

1. The attitude of the local authority to the regeneration of the region is all-important. Where a sympathetic local authority was prepared to work with any other bodies and assistance that came from Government action - as in Corby - the results could be most impressive. Where the local authorities were hostile to the whole endeavour - as in London and on Merseyside - success could only be achieved by setting up an independent corporation able to cut through the red tape and the planning controls imposed by the unsympathetic local authorities. The first question to ask in any area where the Government wishes to intervene is how the local authority is going to respond. Where hostility is at all likely, the best way of achieving progress is the establishment of a Development Corporation with strong planning powers over a limited area.
2. Scattering subsidy and assistance over a very wide area without clear targets is a bad way of proceeding. Regional assistance for the whole of Merseyside has achieved little.

3. We found inadequate monitoring of the effectiveness of measures in creating jobs which might be self-sustaining. It is important that the jobs are not just subsidy-dependent, so we need to know how the companies fare in the longer run. Few of the organisations we visited did this thoroughly. There is also a complete lack of comparable statistics between the different programmes of Government attempting to address the same issue.

We therefore recommend:

- i. That subsidies for wide areas should be phased out. The current review of regional aid should be used to squeeze the sums of money involved still further, as it does not give a good return. Similarly, the current review of the Urban Programme should take a robust view of many features in it which are ineffective.
- ii. Departments should be required to show that adequate monitoring arrangements for the long-term viability of jobs are built into any scheme.
- iii. Each proposed scheme for a given local area should include an assessment of the attitude of the local authority.
- iv. The Treasury should be asked, in conjunction with the departments, to set up a proper cross-programme monitoring system capable of giving Ministers good information about the costs relative to the benefits on the range of schemes aiming to tackle similar problems. This should include the Job Subsidies - reviewed below.

B. Job Subsidies

The Government believes that any attempt to bring about real reductions in unemployment by offering permanent job subsidies will be self-defeating. This is correct. Our review of the costs and benefits of job subsidies is designed to help in controlling public spending on this large area, and to assist in winding down some of the more costly and unhelpful programmes of job subsidy that have been established by long user.

The theoretical problems with subsidising jobs are well known. The cost imposes additional burdens on the taxpayer, and tends to raise public borrowing. This can have an impact in reducing other kinds of private demand and in raising interest rates, which contracts other parts of the economy. Subsidy can also serve to undermine the attitudes needed in a successful economy to respond to the challenge of change in an enterprising way.

We accept that there may be a social and presentational case for offering temporary support for jobs that would in the long run turn out to be self-supporting; and there may be an additional case for making individuals more employable by giving them a morale-boosting period of relief from unemployment, which may be linked with the gaining of new skills and disciplines. The analysis set out in the tables in the Annex, and based on consultation with a range of Government departments administering subsidy programmes, have led us to these conclusions:

1. Measures to help individuals are generally cheaper and better than measures to help whole industries or companies.
2. Some aspects of regional policy and Enterprise Zones are very bad value for money.
3. Certain examples of subsidy to nationalised industries involve an unacceptably high cost-per-job.

We therefore recommend:

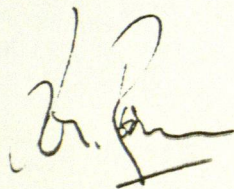
- i. As with our conclusions based on area reports, that the Government take a tough attitude towards the total cost of regional aid when coming to decisions following the review.
- ii. Nationalised industries' claim for subsidy - particularly when based on a job-protection or creation argument, should be analysed most sceptically, as it is likely to offer very bad value for money.
- iii. The Voluntary Projects Programme should be turned into a cheap benefit-plus scheme, which would enable participants to be taken off the unemployment register. More use should

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be made of VPP and the Job Splitting Scheme, as these offer the best value for money. More people could be used in a Clean-Up Britain campaign of benefit plus work geared to the renovation and restoration of our urban fabric.

- iv. When presenting the Government's policies, it should be made clear that there is no inconsistency of purpose between the general drive to create jobs by making markets work, and the measures being taken to alleviate particular distress or to help individuals get back into the employed world. Ministers could help publicise successes in places like Silicon Glen and Corby, where temporary subsidies have helped to create jobs that will be self-sustaining in the long run against the original odds of the region; they could help publicise those schemes in places like Sheffield, Bristol and London where the Community Programme and the VPP are giving individuals welcome temporary occupations and making a useful social contribution at the same time; and could draw attention to the excellent work of the Docklands UDC in London in completely transforming a whole area which had been left as a wasteland through the planning controls of hostile local authorities.

The attached Annex sets out some of the more detailed points to be considered in trying to compare the different schemes.



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JOB SUBSIDIES COSTS AND BENEFITS1. Costs

Three forms of subsidy appear to be particularly cheap: Agricultural Support, the Job-Splitting Scheme, and the Voluntary Projects Programme. These have gross Exchequer costs of £3,000 or less for each person "employed" each year.

Most other subsidies appear to have gross Exchequer costs of between £3,000 and £5,000 per person per year, though the measures to help individuals seem to be generally cheaper than the measures to help industries.

Three types of subsidy appear notably expensive: support for some nationalised industries, eg the merchant division of British Shipbuilders; Enterprise Zones; and some glamour projects, eg the A320 Airbus. These appear to have gross Exchequer costs of more than £5,000 per person per year. Indeed, the A320 costs a gross £9,000 for each person employed each year.

2. Incidental Benefits and Defects

Each measure may also have side effects which may help or hinder social or economic progress.

Our impression is that three of the measures - the Voluntary Projects Programme, the Young Workers' Scheme, and the Enterprise Allowance - are markedly superior in this respect. None of them distorts wages or investment decisions; the Voluntary Projects Programme brings considerable social benefits; the Young Workers' Scheme helps to price youngsters into jobs; and the Enterprise Allowance Scheme stimulates the creation of new businesses.

Most of the other measures appear to be neutral in their side-effects, either because they are harmless, or because defects are matched by offsetting advantages.

Two measures stand out for their undesirable side-effects: Agricultural Support and Regional Policy (in this case including Enterprise Zones). It may be argued that these bring social

gains, but only at the cost of sustaining high wages, misdirecting investment, and encouraging gold-plated projects, without any compensating economic benefits.

3. The Measures

In the following tables, we provide brief descriptions of the various job subsidies, together with estimates - where possible - of the costs per person and of the likely economic and social side effects.

The analysis of side effects is necessarily crude. Information is sparse, and the subject needs far more study.

The costs per person are approximate. To make the comparison feasible, we give gross sums, making no allowance for SB/UB savings (and adding a figure for SB/UB to the cost of the VPP, since the scheme does not disqualify people for benefit). In the case of subsidies to industry, we simply divide total costs by the number of jobs maintained: this will yield, if anything, too low a cost per job, since some of the employees would almost certainly be retained if subsidies were removed. (This strengthens our conclusion that industrial subsidy is bad value for money.)

Our sources for costs are as follows:

- for the nationalised industries, as current-year EFL divided by the number of employees in each;
- for Regional Policy, as in Cmnd. 9111, assuming that the jobs created last 10 years;
- for Enterprise Zones, as in the analysis recently published by Roger Tym & Partners;
- for Agriculture, as total current-year subsidy divided by the number of employees;
- for Special Employment Measures, as in figures provided by the Department of Employment.

TABLE 1. MEASURES TO HELP INDIVIDUALS

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	COMMUNITY PROGRAMME	VOLUNTARY PROJECTS PROGRAMME	YOUNG WORKERS' SCHEME	JOB-SPLITTING SCHEME	JOB-RELEASE SCHEME	ENTERPRISE ALLOWANCE SCHEME
Nature of the scheme	Subsidy for socially beneficial work for long-term jobless	Subsidy to voluntary agencies for socially beneficial work	Subsidy to under 18s for low-wage jobs	Subsidy to hire 2 part-time workers instead of 1 full-time	Subsidy for early retirement to let a new man do the job	Temporary subsidy for unemployed person setting up his his own business
No. of jobs p.a.	112,000	16,000 volunteers plus 945 supervisors	About 106,000	800 part-time	About 90,000	About 25,000
Cost p.a. to D/Emp	About £400m	About £6.5m	About £58m	About £600,000	About £250m	About £24m
Estimated deadweight	15%, or 17,000 jobs	Not applicable	About 80%	Official view is nil	5%	About 65%
Cost per person pa	About £4,500	About £3,000	Over £3,000	About £750	About £4,000 (full-time)	About £2,000
Wage distortions	Probably helps to sustain union rates	Probably none	None	May marginally increase part-time rates	Probably none	Probably none
Investment distortions	Probably none	Probably none	None	Probably none	Probably none	Probably none

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TABLE 1. (Cont.)

	COMMUNITY PROGRAMME	VOLUNTARY PROJECTS PROGRAMME	YOUNG WORKERS' SCHEME	JOB-SPLITTING SCHEME	JOB-RELEASE SCHEME	ENTERPRISE ALLOWANCE SCHEME
Economically beneficial effects in long-term	None	Probably none	Creates pressure for more realistic youth wages	May counter prejudices vs part-timers	Encourages early retirement	Considerable: creates new businesses
Social benefits	Renovation of buildings, care for old people etc	As for Community Programme	None	None	None	None

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TABLE 2. MEASURES TO HELP INDUSTRY

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	Regional Assistance	Support for Innovation	Small Firms' Support	Subsidies to Nat Industries	Subsidies to Agriculture
Nature of Scheme	Capital assistance towards qualifying industrial projects in Assisted Areas (AAs)	Grants towards industrial adoption of new technology and processes	Advice, Grants and Loan Guarantees to Small Firms	Loss funding and capital expenditure financing	Price support and production assistance
Cost to Exchequer (1983/84)	£474m	c. £250m	£30-50m	£2.5 billion	£1.2 billion via CAP, plus £0.8 billion in UK measure
No of jobs pa	c. 25,000 pa over 20 years <u>in the AAs</u>	Not known - not explicitly job creating	Not known	<u>600,000 employees</u> maintained in the subsidised industries	<u>750,000 employees</u> in the industry
Estimated deadweight	Very high - most jobs would have arisen anyway	Probably high - firms have to put in own funds, so most would have gone ahead anyway	Probably low	Some, but no estimate made	Probably very high
Cost per person	£3,500 pa before allowance for deadweight, very much higher afterwards (For Enterprise Zones, about £6,000)	Not known but probably very high	Not known	Average = <u>£4,000</u> Examples: British Steel £4,600 British Rail £4,800 NCB £5000 Merchant Shipbuilding £5,500 (NB A320 £9,000)	£2,700
Wage distortions	Some - not easily answerable	Not known but probably low	Probably low	Severe	Severe

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TABLE 2. (Cont.)

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	Regional Assistance	Support for Innovation	Small Firms' Support	Subsidies to Nat. Industries	Subsidies to Agriculture
Investment distortions	Considerable - not easily measurable	Probably considerable - encourages undue emphasis on production and/or R&D processes	Probably considerable	Severe	Severe
Economically beneficial effect in long-term	Probably none	May create long-term real jobs	May create long-term real jobs	In some cases, a rescue-operation for fundamentally viable industries	Probably none
Social benefits	Has probably dampened regional differences in unemployment rates, though these remain considerable	Probably none	Probably none	Dampens rate of decline in contracting industries. Should ease process of industrial structure change	May keep up population in rural areas

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