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2/10

Dear Andrew

E(A) tomorrow: Regional policy

We had at one stage thought of circulating our own paper for EA, on regional support, but decided against — namely on technical grounds, given the trilateral tomorrow, etc.

The Chancellor & Chief Secretary will, however, be arguing to points in the attached draft paper tomorrow (and Mr Tebbit knows they will). I gather Bob Young in the policy unit has been fully briefed, and

may be letting you have a note.
But you might find it useful also
to see the attached draft - which, as I
say, we decided not to distribute.

Yours ever

Daniel.

DRAFT

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E(A)(84)

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MINISTERIAL STEERING GROUP ON ECONOMIC STRATEGY
SUB-COMMITTEE ON ECONOMIC AFFAIRS

THE NEW STRUCTURE FOR REGIONAL INDUSTRIAL INCENTIVES
Memorandum by the Chancellor of the Exchequer

I support the general direction of the Secretary of State for Trade and Industry's proposals in E(A)(84)53. However, both the logic of his arguments, and the scale of the public expenditure savings needed to achieve the planning totals agreed in Cabinet, point to going further. The aim would be to establish a level of spend nearer what was expected when we agreed last year to savings of £150-200 million - ie expenditure of around £300 million a year. (The attached table compares the various packages with the 1987-88 PES baseline expenditure and the latest forecasts of spend.)

2. First, I propose that the inner tier of the assisted areas map should be set at ten per cent rather than fifteen per cent. The size of the inner tier has the most significant impact on costs: the extra five per cent adds about £60 million to the annual costs of the scheme. We cannot achieve the required savings with a fifteen per cent inner tier.

3. Secondly, while I do not wish to oppose modest new schemes to encourage innovation and new firm formation in the assisted areas from 1987/88 onwards, any additional costs must be contained within the overall level of spend proposed for regional selective

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assistance. The proposal in paragraph 23 of E(A)(84)53 would reduce the net savings by about £20 million.

4. Thirdly, it is crucial that whatever new arrangements we introduce for regional assistance enable us to prevent actual expenditure from escalating out of control well above forecast levels. One suggestion for achieving this would be an annual limit on financial commitments for regional development grant and regional selective assistance taken together; accompanied by changes in the administration of these schemes to improve control over the annual expenditure. I propose that officials should urgently explore the possibilities so that a practical form of control can be adopted.

5. Finally, I am extremely concerned about the difficulty of getting European Commission clearance of a map, as proposed in E(A)(84)53, which exceeds 35 per cent, and includes Plymouth, the whole of Manchester and new assisted areas which are "islands". As I understand it, the Commission are very likely indeed to take exception to each of these singly, and in combination they are a recipe for rejection. We cannot afford that and the consequent delay in public expenditure savings.

Conclusion

6. I support the general direction of E(A)(84)53, but recommend the following amendments to the proposals in it:

- a. an inner tier of 10 per cent rather than 15 per cent;
- b. expenditure of £20 million for 1987/88 on schemes for innovation and new firm formation should be contained within the overall spend proposed for regional selective assistance, rather than reducing the net savings from regional policy changes;
- c. officials should identify a practical way of controlling regional expenditure;
- d. to avoid rejection by the Commission and delay in achieving savings, we should ensure that the total map coverage does not exceed 35 per cent and minimise the number of areas which the Commission is likely to resist.

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1987/88 EXPENDITURE ESTIMATES: REGIONAL DEVELOPMENT GRANT AND
REGIONAL SELECTIVE ASSISTANCE

	Expenditure	Saving on PES baseline (£489m)	Saving on latest forecast (£679m)
	£m	£m	£m
Map option A (15% + 20%)			
10% capital grant	350	139	329
15% capital grant (proposed in E(A)(84)53)	377	112	302
20% capital grant	409	80	270
Map Option B (10% + 25%)			
10% capital grant	297	192	382
15% capital grant (proposed in this paper)	316	173	363
20% capital grant	339	150	340
Map Option C (10% + 15%)			
10% capital grant	284	205	395
15% capital grant	303	186	376
20% capital grant	326	163	353

Note: these figures assume that any expenditure on new measures to encourage innovation and new firm formation in the assisted areas is absorbed within total expenditure for regional selective assistance. The proposals in E(A)(84)53 would add about £20 million to each expenditure total.