

FINANCE COMMITTEE CALL FOR EVIDENCE

DRAFT BUDGET FOR 2013-14

SUBMISSION FROM SCOTTISH PROPERTY FEDERATION

1. The Scottish Property Federation (SPF) is pleased to provide comments for the Finance Committee's scrutiny of the Scottish Government's draft budget for 2013-14. We are happy for our comments to be made public.

2. The Scottish Property Federation is a voice for the property industry in Scotland. We include among our members; property investors and developers, landlords of commercial and residential property, and professional property consultants and advisers. We have some 130 corporate members.

General Comments and economic background

3. We continue to see challenging economic conditions, particularly in credit availability and business demand. The property industry now is producing perhaps a third of its former contribution to the economy. Sales of commercial property are about a third of their former value while new orders for commercial property are also around a third of their former total value.

4. Data from the Registers of Scotland records some £414mn of commercial property sales in the last quarter (April to June 2012) and some 682 commercial property transactions. These figures are an improvement on the previous quarter which showed £355mn of sales and just 592 transactions. Over the last 12 months the Registers of Scotland have recorded just under £1.8bn of commercial property sales compared to the high of £6.3bn sold during 2006-07. These figures will of course come to have serious consequences for the prospects of Scottish Government revenue from the impending Land and Buildings Transactions Tax (to replace Stamp Duty Land Tax).

5. Many businesses remain seriously over leveraged and debt finance is now extremely difficult to secure. Traditional sources of finance from the banks are also becoming increasingly regulated from both international and UK authorities. The Financial Services Authority (FSA) has recently introduced new Regulations that will apply to the lending of UK Banks on income related property (commercial property). This will increase the risk weighting applied to the sector and particularly for many loans in secondary market locations (which will include disadvantaged areas by definition). Clearly this will make much needed investment and development more difficult to attract in a number of areas on top of the existing strategic desire of major lenders to reduce their exposure to real estate.

6. The longer term prospects for the economy suggest little change in the current position for a number of years. Low or no growth is now an accepted expectation among a number of economic commentators and the Bank of England itself reduced its forecasts of economic growth in recent weeks. None of these factors contribute to building investor confidence.

7. Construction industry data relating to the Scottish economy clearly pinpoints the absence of development and construction orders in particular as a cause of continued low economic performance. Consequently the SPF believes that the Scottish Parliament should encourage Scottish Ministers to redouble their efforts to kick-start the development sector in order to support the economy. In our view this must be a strategic priority over this and subsequent budgets.

8. In terms of strategic priorities the Scottish Government has a number of options. Scottish Ministers will be aware of frankly shocking statistics collated by *Homes for Scotland* that demonstrate we are now seeing fewer houses being built than at any time since 1926. This is a reflection of the extent of the impact of the current recession on the house-building industry. And clearly the continued depression in the sector will store social problems for the future (through lack of delivery of affordable housing) as well as continue to weigh down the present economy.

9. Likewise in the commercial property sector the development crisis is if anything even worse. Overall commercial development has been limited in the past few years as evidenced by the drop in new construction orders. The risk-averse culture now in force means there has been little speculative development (with Edinburgh Council's Atria office development being an exception) and both Edinburgh and Glasgow are now facing a shortage of Grade A office space in the next few years. This will put the central belt cities at a disadvantage as occupiers requiring large modern floorplates find a lack of available space. Aberdeen itself has high commercial property demand and it is important that this demand for business accommodation is supported by Ministers if we are to continue to enjoy a world beating energy services industry in the north east.

10. It is worth reflecting that sometimes the Scottish Government should reduce its regulatory or taxation demands in order to encourage sustainable economic growth. For example, the decision to hugely increase empty property rates liabilities adds significant risks to commercial development, meaning that unless a developer is able to pre-let or sell a development they are unlikely to build speculatively.

11. In addition further regulations are expected on raising energy efficiency through building standards in 2013, despite evidence to suggest that further improvements are becoming increasingly difficult to achieve without significant costs. We are also concerned at the prospect of binding demands for retrofitting

commercial and possibly residential properties. This may depress values and add uncertainty and risk for both house-buyers and commercial investors at a time when we cannot afford to discourage property market activity. Added to this is the prospect of significantly increased planning fees. The SPF has long said that reasonable planning fee increases could be accepted if coupled with a tangible improvement in the delivery of the planning service. However, the Scottish Government must reconsider its singling out of the retail and leisure sectors for increases that, according to our members, will actually result in higher fees for like-sized stores in Scotland compared to England.

To what extent do you consider Scottish Government spending decisions align with its overarching Purpose of increasing sustainable economic growth and how should commitment to this objective be reflected in the draft budget 2013-14?

12. In one sense Scottish Government spending decisions that have a consequence for the property industry will inevitably feed through to the wider economy and hence sustainable economic growth. More particularly the spending decisions of the government in relation to capital investment, infrastructure, housing investment and regeneration will impact on sustainable economic growth.

The Scottish Government states in its economic strategy that “The actions of the public sector are co-ordinated to maximise their economic impact.” What progress has been made in harnessing the public sector to support sustainable economic growth and how should this be reflected in the draft budget 2013-14?

13. A major planning application will be scrutinized by an array of public sector agencies and authorities and on occasion directly by the Scottish Government itself. There are a number of reasons why this is the case, which is mainly due to the long term implications of development (commercial or residential) and the consequent implications for the local community. However, such regulation can also restrain and constrain the contribution of the property industry to the economy and SPF members believe that there is still considerable room for improved co-ordination and reduced regulatory demands (for example the costs of up-front appraisals that may run to £100,000s in some cases).

The Scottish Government states that the aim of its economic strategy “is not only to offer greater protection to the economy during periods of economic uncertainty, but to bring about a long-term, or structural, change in Scotland’s sustainable growth rate”. What spending decisions support such structural change in the long term and what spending priorities should be in the draft budget 2013-14?

14. The Scottish economy would benefit in the longer term through less dependence on the public sector to generate economic activity. Currently around 40% of Scottish GDP emanates from the public sector. This means that not only is the private sector (and government) struggling to cope with the demand of financially supporting this section of the economy, but the growing liabilities identified in the Scottish budget that are incurred through pensions from former public sector employees also means that the government is struggling to raise revenue to meet ever increasing liabilities.

15. We are not making comment on the size of the public sector in Scotland, which is in fact little different to many other parts of the UK. We merely point out that it is therefore surely a strategic necessity to expand the private sector side of the economy, in order to achieve sustainable economic growth and thus derive the revenues required to continue to meet the social aspirations of society at large.

16. The Scottish Government should therefore seek to use its spending power and covenant strength to support the growth of viable SMEs, accepting some risk into this process. It should also look to support our larger and more successful industries and centres of excellence (Aberdeen Energy services sector) through enhancements to our national infrastructure. It is also noticeable that direct support businesses through Scottish Enterprise and SDI appears to be reducing under the spending plans and we question whether this is an appropriate decision in the light of the continuing economic turndown.

In its Scottish Spending Review 2011 and Draft Budget 2012-13 the Scottish Government states that the Finance, Employment and Sustainable Growth portfolio “contributes towards ensuring that we achieve balanced economic growth that provides the most disadvantaged in society with the opportunity to prosper. Equity, whether it be social, regional or inter-generational or a combination of these factors, is also seen as a key driver of economic growth.” What progress has been made in achieving these objectives and what spending priorities should be in the draft budget 2013-14?

17. These objectives are by nature very long term and it is unlikely that in the space of a year we could expect to have seen much tangible change. However, in an era of reduced investment, economic activity and public sector spending constraints, we would question whether it will be possible to achieve ‘regional equity’ in terms of economic performance. Also, with increased competition for investment we believe the Scottish Government must not neglect support for stronger areas of the economy.

In its response to the Finance Committee’s report on the spending review 2011 the Scottish Government stated that “The National Performance Framework represents a common vision for the whole Scottish public sector and, as such,

is fully integrated with our spending plans.” How does the NPF impact on the spending decisions of the Scottish public sector and how should this impact be reflected in the draft budget 2013-14?

18. The SPF supports the policy of a central Purpose for the public sector in terms of delivering sustainable economic growth. The National Performance Framework sets a helpful focus on achieving this goal for public sector leaders and managers. However, inevitably much public sector spending is either delegated, in particular to local authorities, and is also earmarked for revenue as opposed to capital expenditure.

In its response to the Finance Committee’s report on the spending review 2011 the Scottish Government stated that its broader work was “focused on ensuring that our ambitions for a decisive shift to preventative spend are realised across all areas of service delivery.” What progress is the Scottish Government making in realising this objective and what spending priorities should be in the draft budget 2013-14?

19. We have no comments in this area. We do suspect however that evidence may be difficult to come by given the short period between the policy commitment and this current inquiry.

The Scottish Local Authorities Economic Development Group recently stated in evidence to the Finance Committee that “Quality, sustainable employment should be the outcome of all skills and employment measures.” What priorities should be in draft budget 2013-14 to realise this objective?

20. Publicly funded projects that can be brought forward to help the construction industry, in particular, to retain capacity. As we argued above it would also be helpful if the Scottish Government could avoid imposing further cost burdens on the development sector at a time when it is extremely difficult to make development appraisals stack up.

Small businesses represent 93% of the Scottish private sector and are more likely to employ people with low or no qualifications than large businesses. What spending priorities should be in the draft budget 2013-14 to support public-private partnership to improve the employability of and create sustainable employment opportunities for individuals experiencing high levels of multiple deprivation?

21. The Scottish Corporate Sector Statistics published in March this year highlighted the growth of SMEs *without employees*. These businesses tended to be in sectors dominated highly skilled individuals and therefore we wonder whether this question reflects a growing or declining analysis of the sector? The statistics also noted also that 35% of employment and 56% by turnover of the Scottish business community is owned by mostly larger organisations based outside of Scotland

(SMEs accounted for 53.6% of employment and 36% of turnover). There is therefore a polarity within the private sector between SMEs and larger organisations based outside of Scotland and at the least it would seem appropriate to focus on growing employment for unqualified people within both of these sectors.

22. The SPF would be pleased to explain its views further at the Committee's convenience.