

successful Scotland

The Smith Institute

The Smith Institute is an independent think tank that has been set up to look at issues which flow from the changing relationship between social values and economic imperatives.

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successful
Scotland

A series of four seminars held in Edinburgh between
March and June 2004

Edited by Tony Pilch



2004

THE SMITH INSTITUTE

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Preface

Wilf Stevenson, Director of the Smith Institute

The Smith Institute is an independent think tank, which has been set up to undertake research and education in issues that flow from the changing relationship between social values and economic imperatives. In recent years, the institute has centred its work on the policy implications arising from the interactions of equality, enterprise and equity.

The series of seminars transcribed in this monograph were held between March and June 2004. The recent history of economic growth and activity in Scotland has been patchy, and some commentators have argued that Scotland has lately lost some of the ground gained in the past 10 or 15 years. The Smith Institute decided to run these seminars in order to look at some of the issues affecting future prosperity in Scotland, in the light of the government's commitment to securing full employment and rising prosperity in every region and community of the country.

Over the course of the series, we tried to address a range of factors that will be critical to the future of Scotland's economy: the role of major multinational companies in the Scottish economy; the lessons that can be learned from the "Celtic tiger" economy of the Republic of Ireland; the role of universities in facilitating business development through innovation and knowledge transfer; and the barriers to widespread economic and social inclusion that must be overcome if Scotland's economic potential is to be realised.

Inevitably, in transforming a live event into print, some of the colour and texture of the original has been lost. We hope, however, that those who attended the seminar will recognise much of what is included, and that those who read it fresh will respond to the flow of good ideas that emerged during the series.

The Smith Institute gratefully acknowledges the support of the Royal Bank of Scotland towards this publication and the associated seminar series.

Seminar 1

Staying in Scotland

A seminar held in Edinburgh on 4 March 2004

Welcome

Wilf Stevenson, Director of the Smith Institute
Dr Lewis Moonie, MP for Kirkcaldy

Presentation

Sir Fred Goodwin, Group Chief Executive,
The Royal Bank of Scotland Group

Panel discussion

Chaired by Sarah Smith, Presenter, Channel 4 News

Welcome

Wilf Stevenson, Director of the Smith Institute

Good evening, ladies and gentlemen. Thank you very much for coming.

The Smith Institute has done work in Scotland before but it is always nice to be back. Today we are publishing a booklet which is a record of a speech given by the Chancellor of the Exchequer in May 2003 on Carnegie, and it is a contribution to the discussion about the role of entrepreneurship and the way in which the enterprise spirit – which of course started in Scotland before anywhere else – has taken root and flourished.

But we are also starting a series of four seminars, with the support of the Royal Bank of Scotland, at which we hope to pick out some of the things that will make Scotland even more successful in the future. We start tonight with the question of how Scotland should deal with its large companies: what conditions make them grow successfully and, in particular, what would keep them here.

After an introduction from Lewis Moonie, we are going to hear first from Fred Goodwin, who has very kindly agreed to give us some thoughts on the problems, or the opportunities, there are for major international companies in being headquartered in Scotland. He is going to raise some questions for us to pass to the panel, chaired by our Channel 4 Scotland correspondent, Sarah Smith.

Dr Lewis Moonie, MP for Kirkcaldy

Thanks, Wilf. It is a great pleasure to be able to give a few words of welcome to this seminar, and I am looking forward to it and its successors. There is nothing more important, for a country like ours, than fostering and encouraging wealth. Government can do so much, but that is only part of the answer. The rest of the answer lies with our entrepreneurs – with business in this country – and government needs to work with business to understand what their needs are. So thank you very much for coming, and I think we are going to have a most enjoyable seminar.

Presentation by

Sir Fred Goodwin, Group Chief Executive,
The Royal Bank of Scotland Group

Good evening, everyone. This is quite a difficult task in the sense that I have only got 10 minutes, not because of my diary commitments, but 10 minutes was the allocated slot for me to talk. Taken as a whole, this is clearly a thesis-length subject. Even taken in some of its individual components, these are thesis-length topics, so what I would like to do is not offer up a speech, but offer a few thoughts around some of the specific aspects of the blurb given out prior to this event.

The event is called "Staying in Scotland". On a positive note, for us at the Royal Bank, we are staying in Scotland. We are first and last a Scottish company and we have no intention but to stay in Scotland. But my eye was caught by the statement, the assertion that – if I might read it out – "there are several internationally renowned companies with global reach headquartered in Scotland, demonstrating that Scotland can provide a competitive economic environment".

I do not think it demonstrates that at all; or if it does demonstrate it, in the context of the Royal Bank of Scotland, it probably demonstrated that it was a competitive economic environment in 1727. Company headquarters do not come and go, fortunately, with the breeze. They do not come and go with economic circumstance from month to month or year to year or, in many instances, from decade to decade. The fact of the matter is that company headquarters move voluntarily extremely rarely.

I was kicking this around with some colleagues earlier on today, and we were trying to think of examples where companies have moved, certainly cross-border, voluntarily, and we struggled. We got to HSBC moving to London, but that may have been partially wrapped up in the Midland acquisition. There were other reasons, but the Midland acquisition was in there. We could not think of too many others. Boeing moved some of their business from Seattle to Chicago, but again that is not cross-border in the sense I am talking about.

History determines headquarters location

There are very few examples of companies moving their headquarters voluntarily, so the notion that the reason there are so many companies with global reach which exist in Scotland today is something to do with Scotland's current economic environment is

something I think I would disagree with. I think it is to do with history and the fact that these companies were here, and the ones that are still here are ones which have been characterised by success. As it happens, I do think Scotland is a competitive economic environment, so I am not actually challenging that notion about where we are today, but I do think it is disconnected from why headquarters come to be here.

I think looking at why headquarters come to be here takes us down quite an interesting path, and it is not a totally satisfactory path in many respects. What are headquarters? Is that the biggest building in the group? Is that where board meetings are held? Is that where the boardroom is? Is it where the registered office is? Is it where the brass plate is? Is it where the chief executive sits? Is it where the finance director sits? If you start to apply those criteria to a number of companies that you might consider to be Scottish headquartered you would come up with some quite interesting ticks in the boxes as to which of these attributes are actually in evidence in Scotland. So I think we do need to ask ourselves what we mean by "headquartered".

Also, as we start to talk about large companies in a global context, it is probably worth reminding ourselves that because of the size of Scotland you cannot be a global company and rely simply on the Scottish economy. I cannot think of any particular activities, except possibly kilt making, where you could actually be a global player and simply survive off the demand from within Scotland itself.

So again I think I would highlight the point that the Scottish economy is not so relevant to having the headquarters here. The vast majority of our business is outside and has been for a very, very long time. I certainly would not say we are not influenced by economic conditions in Scotland, but economic conditions in the United States have a far greater bearing on our business than economic conditions in Scotland: ditto conditions in England and in a variety of countries in Europe. I am not complaining, but it is just that in a global company large parts of your business tend to be other economies other than Scotland.

Going back also to where people are located, I think it is a reality these days that – despite video conferencing, internet, email and all the rest of it – if you are running a global company these days travel is a reality. You will spend more time away from your headquarters than at it, so I am not sure that the location of the headquarters really matters too much.

So, should we be building a strategy on having headquarters of global companies in

Scotland? My answer to that is no – not that it is not good to have headquarters of global companies in Scotland but, as I said, I think it is unlikely that companies will move to Scotland. Not because Scotland is not an attractive place, but, simply, history does not point to companies moving their headquarters across the border. If we want to grow or want to have more global company headquarters in Scotland we are going to have to grow those companies in Scotland, which seems to be quite an exciting and challenging opportunity.

That said, there are risks. As soon as you put your head above the parapet into the global marketplace, you are in the global marketplace. One of the old, pervading realities of the global marketplace is that it is highly competitive and consolidation appears to be an old, pervading theme. If you are in the global marketplace you tend to be a consolidator or a consolidatee. The more successful you are the more visible you are, and that gives you either the opportunity to buy someone or to be bought.

I think it is interesting, if slightly sad, that many of the great Scottish companies which had global reach and which were headquartered in Glasgow, Edinburgh and elsewhere have disappeared. This was not because they were bad companies; in fact in most circumstances they were very good companies – so good in fact that they were attractive to larger global players and they were acquired. That is maybe the reality of the global economy – you cannot be half in it. If you are going to be a global player you run the risk that the more successful you are, the more at risk you are, unless you can quickly get the critical mass and get into that category of consolidators rather than consolidatees.

An attractive place to work

So, where does that leave us? I think it leaves us in a good place, because in looking at what makes Scotland an attractive place for us to do business I keep coming back to one simple thing: people. It is the people that we can attract to our business in Scotland that make us viable. It is the quality of the people who work for us in our headquarters that makes us the company that we are. Those people are not all Scottish. We did not recruit them all from Scotland. We have been able to bring a great many people to Scotland.

I will come back to one part of the question: what could we, as a big company, ask for? Well, probably not too much more than we actually get at the moment, which is that Scotland remains an attractive place for people to come and live and work. If we could not get those people to come and work in Scotland we would have a problem, and it would be a very difficult problem to do anything about.

As we get into the area of what causes people to come to Scotland and what makes Scotland an attractive place to work, we have got the scenery and so on, but of course it is so much more than that. It is the existence of large companies, it is the existence of a vibrant economy, it is good education, health and transport.

But it is terribly important in thinking about Scotland that the needs of big companies are not, in many respects, different from the needs of small companies. The single biggest need that we have is that Scotland remains an attractive country for people to come and work, so that when we are looking for talent we can say, "Come and work for the Royal Bank of Scotland, and oh, by the way, you are coming to Edinburgh," and have that recognised as somewhere that is attractive to live. It is a very soft and delicate issue, but one which actually fills my mind more than almost any other when I think about sustaining our headquarters here in Scotland.

Panel discussion

Chaired by Sarah Smith, Presenter, Channel 4 News

Panel

Charles Berry, UK Executive Director, Scottish Power

Sandy Crombie, Chief Executive, Standard Life

John Laurie, Director of Group Financial Services, Scottish & Newcastle

David Sigsworth, Generation Director, Scottish & Southern Energy

Sarah Smith

Fred has got to leave us, so it falls to me to introduce to you the other panellists that we are going to be hearing from, who make up a pretty good advert for staying in Scotland and doing business in a successful Scotland. That was the fifth-largest bank in the world we were just hearing from, and we have four other international companies with the global reach that we have been talking about – who are all headquartered here in Scotland – here with us tonight.

We have John Laurie, who is the director of group financial services for Scottish & Newcastle – who extend far beyond Scotland and Newcastle, and their brands are the market leaders in seven different countries. We also have Charles Berry, who is the UK executive director of Scottish Power, which is supplying gas and electricity to Scotland, the UK and North America. Then we have Sandy Crombie, chief executive of Standard Life, based here in Edinburgh, and selling financial services in Europe, North America and into Asia; a pretty global reach. And we have David Sigsworth, generation director of Scottish & Southern Energy, one of the largest energy companies not just in Scotland but across all of the UK.

What I want to ask you first is: what is it that makes you stay in Scotland?

Staying in Scotland

John Laurie, Director of Group Financial Services, Scottish & Newcastle

I would echo a lot of what Fred said. We have been here since 1749. We have an excellent, comfortable base; it would be unlikely that we would find reason to go on any voluntary basis. I think the other thing I would pick up is the people. We have access to very good-quality management and staff here, and that is an important aspect of why we are here and why we would like to stay here. It is also, relatively speaking, a good cost base. It is a good place: a good, low-cost part of the UK. If the alternative were to be

London, which is obviously significantly more expensive, that would be a big factor for us.

So, it is heritage, people and cost that are probably the three factors which have brought us here and kept us here.

Charles Berry, UK Executive Director, Scottish Power

Let me give you a little bit of background on Scottish Power that will set in place the context for some of the questions or comments I will make.

We were born in June 1991. But I guess it would be fair to say that Scottish Power was quite a big baby, because it had been the former South of Scotland Electricity Board, and it was brought into the private sector. And we had a start of something like 2 million customers and 10,000 employees, although it was a baby in the private sector.

Since that time we have grown beyond Scotland into the rest of the UK, and then beyond the UK into North America, so that today something like 60% of our business is in North America, and within the UK just about half of it is in Scotland and half outside Scotland. So there are similarities to the things Fred talked about. We are a company that has most of its business outside Scotland. We have got something like 6 million customers, 14,000 employees, through the UK and North America. We are very proud to remain firmly headquartered in Glasgow.

Sarah Smith

Is it a problem having so much of your business outside Scotland but having headquarters here?

Charles Berry

No, no. It was possible for us to grow because the skills we have built and developed at home were better than the equivalents others had in the UK and in North America. So we were able to step up efficiency, and service improved as a result. So why are we still here? Well, we were born here. We were born here in 1991. We have reached beyond it but we have not forgotten our base, and the point about people is a very real one. We are able to recruit and retain the quality of people in Scotland that we need to be at the heart of our main company.

One other factor: image. I know you can often hear questions about what is the tartan factor, but for us it was a very real factor in being able to make a big acquisition in 1999

into the United States. We have learned since that those that had to approve it – the six state regulators, trade unions, the shareholders and state governors – did not just look at the image, they came over to visit us and test all these things. It was only when they found that the image was matched by reality that they actually said: “Okay, you are now fit to own and make that move.”

Sarah Smith

Standard Life, you have the same situation where much of your business is done outside Scotland but you are still staying here?

Sandy Crombie, Chief Executive, Standard Life

Yes, we were formed in 1825 – as we are all comparing ages. I have been there most of that time! Standard Life was working in Canada within nine years of its formation. It took us 12 years to get as far as London. This is a little bit about the attitude of the Scots at the time towards the English, perhaps. But I think it says that Scots have been entrepreneurial and had to go outside Scotland to seek a market that was bigger than the local market.

I echo all that has been said so far. It is about people. Edinburgh as a headquarters has provided ready access to talent, not just in our own particular disciplines but in all the associated disciplines: the legal disciplines, accountancy and so on. We have had a professional base that has supplied our need for talented individuals at all levels in the company. There is no permanent future for a company that is poorly led, so I think we need talented people all the way through an organisation. I have to exclude myself from that, in case you think I am just big-headed, but I think we have been well led and it will be a feature of all of these companies that if they have survived this long, they have been well led throughout.

Sarah Smith

David Sigsworth, we are hearing that it would take an enormous wrench to move a company's headquarters outside of where it belonged, but is it conceivable that conditions in Scotland could mean that a company like yours – or any of these – would not be staying in Scotland?

David Sigsworth, Generation Director, Scottish & Southern Energy

We have had to make that choice. Five years ago we had the same sort of roots as Charles Berry talked about at privatisation. When we merged with Southern Electric five years ago

we had that choice to make, and very firmly the two boards that came together decided to come to Scotland. In terms of us ever considering leaving Scotland, the people that we have, we believe, are some of the best. We moved many of our senior executives from the South of England to come and work in Perth, and I would not say there was anyone who regrets that move.

Sarah Smith

It is clear from what we are hearing that we should not be too focused on the headquarters – it is the quality of the staff that is in them. I would quite like to hear what is more important: the Scottish staff that you are able to recruit here locally, or the ability of Scotland to attract staff internationally to come and want to work in the Scottish headquarters?

Charles Berry

Up until now it has been the local talent, because for some years we found it difficult to actually bring people into Scotland to set up home. I think that is changing now, as you see more and more of the most capable people looking for challenging jobs and placing a much greater emphasis on work/life balance. There is a lot more attention to the circumstances in which people live, to the countryside etc. I think there is a big attribute that we have got there. So, the most important thing up until now has been recruitment of local talent, but I think the features that we have got will increasingly play a part in recruitment from outside Scotland.

Making Scotland more attractive

Sarah Smith

What can Scotland do to make itself more attractive?

Sandy Crombie

In taking our asset management capability from being a function into being a business we did have to bring talent from elsewhere, and there is no doubt at all that Edinburgh has a brand and that brand is important. It is seen, these days particularly, as a great place to live and work. It is seen as a place where you could come and, if for some reason you have to leave the current employer, there is a community of other businesses where you can go without necessarily having to upheave your family yet again. So I think we should all be conscious that Edinburgh is attractive and we have got to keep it that way. We have got to maintain the brand: it is Scotland and the brand is Edinburgh. It is a great place to live and work.

David Sigsworth

I think we have talked a lot about what I would call the executive element of companies and the job opportunities there. But if we look at the craft and technical opportunities, there is a big vacuum that exists – in the UK generally, but particularly in Scotland – for engineers and craftsmen. We also find that the attractiveness of some of the other sectors means that, although there is a will in the universities and in schools to try and bring those people through, we still have not managed to create the right environment to recruit them and to show them how they could succeed in our companies. I think it is well recognised that the solution still is not fully in place.

Sarah Smith

Are there special problems with being headquartered in Scotland, which imply special help for Scottish companies?

John Laurie

Other businesses are largely English-speaking focused; we are not, or much less so. I think one thing that we are conscious of as an issue in luring people to come and work here is a lack of a school which will teach in foreign languages; to teach in French, to teach in German, etc. If we are creating an international environment, that is a necessary feature. Bright people come here, their children come too, and their children need to be catered for and do not always come at an age when they can be expected to learn in English.

Sarah Smith

Presumably, if they were choosing between London, Paris and New York, all of that would be on offer to them?

Sandy Crombie

It is quite an important factor, and quite an important drawback to us in recruiting people to come here.

Charles Berry

If I may, I would just like to pick up on one of the things that Fred challenged, and that is the notion that the measure of growing the number of headquarters in Scotland is the right one. I think maybe the thing we should concentrate on is: how do you grow companies in Scotland? If they are big and successful they will each eventually become international, and I think there is some stuff we can do that will be helpful to grow companies more quickly in Scotland.

In the 1980s I had a chance to live in Boston in Massachusetts, and there were some things that I found quite special. If you look there you will see local government and bodies very keen on promoting economic development and growth. Growing companies is what it is all about. You see big, strong universities creating talent and ideas, and you also see a financial sector that is very committed to funding and fuelling that growth. There was a lot of venture capital in those days and these things did not just exist in silos, they were catalysed and interacting all the time. I lived just off route 128 in Boston and as you drove up and down that you saw all these huge high-tech companies that had grown from nothing very, very quickly.

Now, if I just look at Scotland, have we got a powerful financial sector? Well, yes, we have. Have we got universities that have all the talent and all the rest of it? Yes, we have. And have we got the potential for local government, Scottish Enterprise and all the rest of it that could do what I saw in Massachusetts? Yes, we have. I certainly see no reason why the equivalent experience could not be cultivated here. That will then create successful, growing companies, and the strongest of those will end up not just headquartered here, but international.

What should government do?

Sarah Smith

So, what do you actually want to see the government doing?

Charles Berry

Well, if I pick a good example, renewables, which is a live example in front of us now. The dominant country in wind power is Denmark, because many years ago they set up and fuelled the companies that build turbines. The next wave of this is going to be marine energy: the devices that generate energy from waves and through sub-sea devices. Scotland is beautifully positioned for that. So what is wrong with trying to grasp the opportunity through trying to fund and cultivate the R&D transfer into business supported by the financial community, with the universities doing their bit? There would be others too where we could plant a seed right, because we have got all the fundamentals.

David Sigsworth

One of the issues, though, that we have to question is why in Scotland, as compared to other parts of the UK, we have far lower levels of business start-up. I do not believe it is a criticism of the entrepreneurial ability, but for some reason or another we have a far lower rate of business start-up, and is that to do with the culture or attitude to risk?

If we can solve that it unlocks a lot of the opportunity to do what Charles is saying.

Sarah Smith

Is it up to government to create an environment to do that, or to create an environment to make it easier for companies to grow or stay in Scotland?

Sandy Crombie

Maybe in some places, but I think the companies themselves are often growing things that are not necessarily recognised as start-ups. If we take Standard Life, six years ago it started Standard Life Bank. It is now within the top 15 mortgage providers in the UK; within five years it will be in the top 10. But it takes time to develop that. You have got to have a stable environment, the right sort of nurturing environment. That particular start-up made its first profit in year six; it will provide a decent accounting return on capital in year 10, and will provide a return on capital measured from inception in year 15. You have got to be patient to make these businesses grow and develop, and you need the right type of environment.

But as well as the Standard Life Bank, we have also started an investment company and a healthcare company, and they are all going very nicely. There is a lot of activity and these are all very successful businesses in their own right, but they are not really recognised because they are all deemed to be part of Standard Life.

Sarah Smith

Now, we have got many just as distinguished and experienced faces in the audience as we have sat on the panel here. So let me open it up and see if anybody has got any questions or points they want to make – either individually to any of our guests, if you say who you want to talk to, or that we can just throw out for discussion.

Sir Angus Grossart, Chairman and Managing Director, Noble Grossart

Although the focus on enterprise is important, we must not let this focus hijack the public sector; and this assumption that it is all about small start-ups, which are of course important, fails to recognise that the real economic momentum tends to come from the larger companies. And a very important thing about large companies is that they are enormous forces which can provide real benefits in terms of skills, training and mentoring. How can we get more of that? Often, the government focuses on small companies through economic development schemes, which can often help, but are spread very thinly on the ground. The seeds grow slowly and you very often finish off also watering

the weeds. My view is that we need to engage large companies in providing the sort of leadership and skills development that will lead to success.

Sarah Smith

Would anyone like to pick up on that?

Thinking global

Sandy Crombie

Just in a way, perhaps obliquely: I do not think you can build world-class companies on anything other than world-class capabilities, and what is important for this economy in my view is to try to attract and foster a collection of world-class capabilities.

We have it in pockets in asset management. Asset management is quite an interesting business. It crosses boundaries very easily, and in the UK environment we are up against the best in the world. There are many local, smaller businesses but the really big business is being done by the really big, global-standard players and to compete with them you have to be global-standard. We have many law firms in Edinburgh and we have many accountancy firms, but I confess that often when we are looking for the most specialised legal support or the most specialised accountancy support we go to a firm based outside Scotland for it.

I think we would have an even more successful Edinburgh if we could be sure that we had world-class capabilities in more disciplines and that they were more regularly used by the local companies. World-class businesses are built, in my view, on world-class capabilities. Anything other than world-class will eventually get overtaken by businesses crossing boundaries.

Sarah Smith

John, you have a business which does cross boundaries already. Do you have a similar experience? Do you have to farm work outside Scotland?

John Laurie

Inevitably so. It is partly because of the language thing, but also there are specialisms which are not available here; and I think, so far as we can, we would always prefer to use local services, but increasingly there is great limitation on that because they are just not available.

Sarah Smith

Is that just a feature of the global marketplace, that specialities will become concentrated specialists and we cannot expect Scotland to cover all of the ground, or is there a problem finding the things in Scotland that you should be able to?

John Laurie

The problem is there. I think it is something we have to work on, and again there is no way you can try to achieve that across a big, wide spectrum, but in sectors we would hope to encourage that.

Sarah Smith

And is that something that companies like those represented here can play their part in doing?

John Laurie

I am sure it is. We have to be seen as the first targets and encourage people where we can.

Sarah Smith

Is it possible to do that?

Charles Berry

Yes, I think it is.

May I just nip back to Sandy's point about all of it being built on world-class capabilities? I think that is critical, no matter whether it is a small company, a big company or whatever. You have got to constantly benchmark: how well am I doing relative to best practice and where is there scope for improvement?

But to Angus's point about small company start-ups and not forgetting the big companies, I think that is also critical to bear in mind, because it is both of them. There are opportunities to be grasped by new start-ups, because that is basically what Massachusetts did; but big companies employ vast numbers of people, create big spend in the economy; so we need both. So I would stand by what I said about small company cultivation, but for big companies I think it is possible to support their development through education, through health and just making sure the infrastructure is right.

David Sigsworth

Could I just come in here? I think that particularly in the technology field, a lot of the things that we believe we could be world-class at developing and benefiting from are there in our universities in Scotland; that is one of the silos. You then have the companies that will want to somehow pick up and capitalise on those ideas, and we actually now in Scotland have got the intermediate technology institutes that are just being formed that can make that process work.

I think there is another blockage, though, that is still to be recognised, and that is that many of those start-up companies, which will be driven by venture-capital private equity investment, often find that there is a blockage to get products to maturity. Even if they can take the ideas that come out of the universities and build the technology, they then need a big balance sheet behind them to break through and produce a mature manufactured technology for sale. I feel that often at that stage there is an overvaluation of the intellectual property that those small start-ups have actually created. The big balance sheets are not prepared to pay over the odds to get into a joint relationship to pursue success. So I think bringing the start-ups alongside the money that may be available in the bigger companies is still an equation that we have got to work on and be able to solve more effectively.

Devolution

Colin Currie

There is a kind of elephant in our living room in this discussion, and that is big government. Scotland has got an awful lot of government per head compared to Yorkshire, which has the same population. So from the point of view of growing and nurturing good business, big business, international business, is this a benefit? Can it help? What advice would you give it, or should we ignore the elephant in the living room?

Sarah Smith

Advocates of devolution would have argued before we got the parliament that it would have helped Scottish businesses, alongside other aspects of Scottish life. Has that been your experience? Is more government helping you?

John Laurie

I think certainly the Scottish Executive have tried to recognise where their strengths are and help and capitalise on them, but it is clear that in some sectors that is not being seen as very effective.

Charles Berry

I actually do not think it is the size that counts, it's what happens. What I see happening and developing in Scotland now is actually quite encouraging, because there is a regular dialogue from the top and centre of the Scottish Executive with the big companies that we have been talking about here in Scotland. It is happening regularly, and the messages that have come out of that from big business have been: please concentrate on education, on health and getting the infrastructure right, and then stand back. If you look at some of the policy initiatives and comments that are coming out, they are now consistent with that.

If you look at the example that I gave earlier of marine energy, there is a body now set up in Scotland called FREDS – it stands for the Forum for Renewable Energy Development in Scotland, and its aim is to get job creation and growth through the whole renewables thing; and Scotland has many features of wind and wave that are going to make it opportunistic, and that is working. It is the catalyst for putting the spotlight on marine energy and making sure we are doing that sort of thing well. So I am much more optimistic on what I see happening. I see listening and interaction with big industry, I see us taking account of what is said, and I see, before, our getting established to do this sort of catalyst thing that we have talked about.

Sarah Smith

The Scottish Executive – a help or hindrance?

John Laurie

It is a bit neutral. There is a very small part of our business that is in Scotland. We are a worldwide business with a very small business base here. We would just like them to leave us alone and let us get on with it, honestly – and to encourage education (to come back to educating people and developing people), improve the education system and improve higher education. And in that area, yes, we look to them to help in that area. But we can look after ourselves, thank you very much.

Magnus Linklater

On the whole the reputation of devolution, particularly as seen outside Scotland, has not been very encouraging. The last few years have had more than their fair share of bad news stories. Has that affected in any way the reputation of Scotland as a good environment in which to do business? Have you had any feedback from people you are trying to recruit from elsewhere, or people with whom you are doing business, that somehow doing

business in Scotland is not, with the current political climate, a hugely advantageous thing to do?

Sarah Smith

Has anybody had that experience?

John Laurie

I think that sort of development takes decades really to work its way through the system. Scotland has a good brand image; people like Scotland, it is a friendly society, and I think it would take a long, long time for people to diminish that in any way. So: so far I would say I do not see any evidence of that sort of change.

Sarah Smith

Can it happen, though? We are looking at very old, established companies represented here, and the Royal Bank of Scotland who for hundreds of years have been building the reputation of Scottish prudence and good business sense. And then you look at a country that cannot keep the costs of its own parliament under control. It doesn't look like a good business environment, does it, when things spiral out of control to that extent?

Sandy Crombie

It is certainly not my experience that this has affected the brand that is Edinburgh, or that is Scotland, either positively or negatively. It just has not had an impact.

Charles Berry

When you talk about the Scottish parliament and all the coverage and that, I would just ask how much of that is covered outside Scotland?

Sarah Smith

I think that is one of the few stories that do get out from outside Scotland.

We have a question at the back.

Sandy Crombie

While the microphone is travelling, can I just add one point on Scotland, the brand? When I am interviewing senior people, particularly from England, to come they ask about four things: health, education and transport being the first three. Then they ask the question that always surprises me: "Will my kids be beaten up in the pub for having a posh accent?"

I find it bizarre but am frequently asked. There is an element of concern that Scotland is anti-England and some of that manifests itself in strange ways – football events or rugby events, or whatever, but I have to say that none of them have ever regretted coming here. But I really am surprised at how frequently I am asked the question.

Sarah Smith

There was a survey a few months ago saying 60% of British companies thought that Scotland was anti-English and it was a bad environment for English people to do business in.

Bill Speirs, General Secretary, Scottish Trade Union Congress

I have found it intriguing that since devolution the number of trade union centres around the world that have intensified their contact with the Scottish TUC has grown so rapidly. In Lombardy, the Basques in particular are very interested in the way in which political devolution and the role of the trade union movement can be helpful in getting peaceful constitutional change. Last week I got a communication from the All China Federation of Trade Unions saying that they wanted to send a delegation over and could we also send one there to talk about how the trade union movement interfaces in economic development. So, there may actually be a bit more attention being paid to devolution than sometimes we think.

So far as having headquarters in Scotland, obviously from where I am coming from it is nice to have the headquarters of Scottish & Newcastle in Scotland; it would be nice if we had lots of people manufacturing the beer in Scotland as well. In as far as having headquarters here is good, what can the organised workers of Scotland do to be helpful?

John Laurie

Let me pick up first on the decision to close Fentonbridge brewery, to which you refer. That is a business decision; it is our least economical brewery, and it is something which we simply have to do to maintain our profitability. As far as what the organised workers can do, they should do their best, work as well as they can, and provide a good service to their employer. I do not think there is a political line which I could find where they could be encouraged to help; but just be a good workforce.

Sarah Smith

Does the labour force need to give you anything to help you stay in Scotland?

David Sigsworth

I think, certainly, over the past five years in Scottish & Southern Energy we have had a great relationship with our trade unions and with our staff. The change that has been required to maintain and be able to keep abreast of developments in our sector has been embraced and it is part of the company's success.

The role of the unions

Sarah Smith

Are you looking for anything from the workforce or the unions?

Sandy Crombie

I do not think I want to answer that question ...

Sarah Smith

I don't know if many of Bill's members work for you.

Sandy Crombie

We may come at it from a different way. In a whole range of ways, we are all in competition and our people are in competition. There are people elsewhere in the world who are very able and very hungry, and it is very popular these days to outsource certain things to India, for example. If the job can be done at half the price and every other competitor in our market is doing that, it is very hard to say we can ignore that.

Sarah Smith

Even the might of the STUC cannot change the fact that the economics sometimes do not add up, and wage differentials between Scotland and India.

Charles Berry

True, that is a live one now. Maybe I can give you a specific example of where our company has developed because of huge support and input from the trade union movement. As I mentioned earlier, when we made a big deal in 1999, we bought an American utility – it served five states – and, as I said, the governor was interested, the regulators were interested, the trade unions were very interested. They contacted and visited our trade union colleagues, full-time officers and members, here in Scotland to say: "What are these guys like; they say this, but is it true?" They got a very positive, supportive response and that enabled us to take that huge step, which is now 60% of our business outside Scotland. That is it in action.

To answer your point: going forward, in my opinion, what the trade union movement can do – and it is doing it – is work in partnership with employers in developing world-class skills. Just to give you a measure, that is not easy: I mentioned when we were privatised in 1991 we had 10,000 employees in Scotland; we now have around half that number, but that is part of building a big group that is much bigger and much broader. That is not easy to do and it is only accomplished by working together in partnership, so I think the answer to the question is: keep doing what we are doing.

Sarah Smith

Well, unless anyone is desperate to get in, I will come to the fact that it is a beautiful, warm evening, the best advert we could probably have for attracting staff to Scotland or persuading people to stay here. Looks like it's time for a drink.

Seminar 2

Becoming a tartan tiger

A seminar held in Edinburgh on 4 March 2004

Welcome

Wilf Stevenson, Director of the Smith Institute

Presentation

Wendy Alexander MSP, Author of *Chasing the Tartan Tiger: Lessons from a Celtic Cousin?*

Response

Alf Young, Public Policy Editor, *The Herald*

Discussion

Welcome

Wilf Stevenson, Director of the Smith Institute

Good evening, ladies and gentlemen. This is the second in our series about “successful Scotland”. The first one was about “staying on”: what are the conditions under which big companies want to be part of the Scottish economy, stay here and headquarter themselves? This evening, we are going to concentrate on what it is that will get the Scottish economy thriving. We have already published a pamphlet on this, which Wendy will introduce. But as part of the budget papers, the Treasury have published a paper about devolving decision making, which picks up a number of the themes that Wendy is going to talk about – not least the evidence showing that there are worrying signs that Scotland is not punching its weight and that it needs to raise its game.

Presentation by

Wendy Alexander MSP, Author of *Chasing the Tartan Tiger: Lessons from a Celtic Cousin?*

My task today is to talk about the role of government in promoting enterprise. I want to use the first five minutes to try and unpick the Irish analogy, but then I want to move on and talk about where I think Scotland is now and the role of the Scottish government as we move into the second term.

Ireland is a good place to start, because for so much of the last decade an oft-asked question in Scotland was: "How do we become a tartan tiger that matches the Celtic tiger?" I think we have begun to have a pretty sophisticated debate, which acknowledges that Ireland and Scotland are fundamentally different. Ireland was a story of take-off by a rural, largely agricultural nation that had been left behind economically in the 20th century. In contrast, Scotland, rather than looking for a take-off, is really looking for a turnaround.

Scotland has been an urban, industrial society for a very long time – one which was at the peak of its relative performance at the start of the 20th century, followed by a pretty slow relative decline since the start of the 20th century, and has subsequently recovered, relative to the UK, in gross domestic product per head in the last 40 years. So the challenge for Scotland is not a take-off but a turnaround.

In 1985, Ireland languished at two-thirds of the European average GDP per head. It has now moved to a position where it is around 120% of the European average GDP per head, although nearer the European average if gross national product per head is the measure. Scotland, as part of the UK, has broadly performed around the European average throughout the last 40 years. So when you are looking at contemporary Ireland and contemporary Scotland, the relevant question is really: "What are the Irish doing today to boost further success, and what should Scotland be doing *today?*"

Government is vitally important in this process. The right question is: how do we achieve a degree of strategic intent about Scotland's prospects, comparable to the Irish approach to their challenges two decades ago? Government matters, because the Irish success was not inevitable. If you look at the small nations that joined the European Union in the 1970s and 1980s, there was Ireland, who went from two-thirds of the European average GDP per head to exceeding it. There was Portugal, that struggled up towards parity, and

there was Greece, that stayed stuck at two-thirds of European average GDP per capita.

Three Irish lessons

So, while Ireland's success is a story of catch-up, there are potentially some lessons from this nation that did not simply converge, but actually exceeded the European average. By examining this Irish experience we can begin to identify lessons: let me just cite three of them.

The first is about self-confidence. If you had held a competition in the 1960s about melancholy, Scotland's predisposition for Celtic melancholy would have been competing with that of the Irish. I think there is a lesson for Scotland there about the effect of the Scottish whinge and the Scottish cringe. In short, how Scotland sees Scotland is a significant handicap. Scotland possesses more valuable assets, attributes and capabilities than perhaps she is aware of. So, the first lesson is that there is something around self-belief and its relationship to economic prosperity.

Second is strategic intent. How and why did the Irish catch up when the others did not? Arguably, they collectively came to understand that they had to put the economy first. They first tried to adopt such an approach in 1958 by moving towards a more open economic policy. It did not achieve its promise until post-1987, when forward-looking industrial policies and education policies were complemented by a policy of fiscal retrenchment. The implication for contemporary Scotland of putting the economy first means that we need to be clearer about the capabilities we have, and the extent to which the introduction of greater competition and contestability in the Scottish economy matters.

The third Irish lesson is that as a pretty small nation they realised that they needed to build a consensus. They essentially took economics out of the political arena. That is something that I do not think rings true in a British context, but if you look at the small nations and regions, the building of a degree of consensus that neutralises political argument around the economy is something that we have to be willing to consider. Crucially, the Irish also took the economy out of the constitutional quagmire, which I think we also need to do in Scotland.

So with these three lessons, let me move on to what the Irish story tells us about the role of government. In shorthand, for almost 40 years – from independence in 1922 through until 1958 – the Irish pursued the wrong economic strategy: domestic protection. Their

relative economic failure in those decades cautions us about the risks of having a wrong-headed strategic framework. Scotland likewise cannot afford to have the wrong strategic framework. You can afford tactical errors – indeed, they are inevitable – but you cannot afford to have the wrong strategic direction. In that sense, I think that in Scotland we have changed direction more fundamentally than people perhaps realise.

We could have been forgiven in Scotland for spending the first term worrying about establishing the parliament, the return of democratic legitimacy and the success of our new institutions. And this is in fact what the Irish did for many years post-independence. In the early decades of the Irish nation, their economic strategy was dictated more by the political imperatives of establishing a state that was democratic but distant from Britain.

If you look at what happened in the first term of the Scottish parliament, there were significant shifts away from what had characterised Scottish industrial policy in the early 1990s. If you go back to 1996, the Conservatives were pursuing a low-cost, low-wages strategy, of which the archetypical example was Chungwa at Belshill. This involved bringing an outdated technology to a piece of ground where you offer special incentives, even when you know the investors are unlikely to develop significant local linkages and many may not even stay, medium term. That was the high-water mark of the “low road” low-wage, low-skill strategy towards Scotland’s economic development.

From low road to high road

The strategy changed fundamentally in the first term of the parliament, abandoning the earlier “low road” strategy for a “high road” strategy based on high wages, high skills and high technology. One signal was bringing enterprise and lifelong learning together in one department – the first place in the world to do so. We also created Careers Scotland, because we understood that lifelong learning is what tomorrow’s success will be about. We put support into modern apprenticeships and into the further-education sector. We changed the financial incentives for industrial support, so they were no longer based on cost per job but began to reflect the quality of investment being undertaken. We began to tackle the missing links on transport infrastructure that were holding us back. There was a whole new approach to the role of universities in promoting innovation – for example, through the co-investment fund, the proof of concept fund, and the new intermediate technology institutes.

Another signal of this new high-road strategy was GlobalScot. The forerunner of the fresh talent initiative, it recognised that there was no point in Scotland historically having

exported more people per head of population than any other country in Europe unless she actually sought to more effectively harness the Scottish diaspora to support economic activity at home.

Now, all of these things did not just happen. If we had kept doing what we were doing in 1996, Scotland would have still have been pursuing a low-road, low-cost, low-wage economic development strategy. Of course, the election of a Labour government in the UK was the essential prerequisite for both constitutional and economic change, but the existence of the parliament has facilitated the development of particularly Scottish solutions to Scottish challenges. There was a significant change of economic direction in Scotland, complementing Labour's economic leadership in the UK during the first four years of the parliament. All this occurred alongside the recovery of Scottish democracy. It occurred against the backdrop of stability that had been created in the UK.

Where are we now?

So, where are we now, early in the second term of the Scottish parliament?

Yes, there has been real progress, but real challenges also remain. There is significant evidence of insufficient contestability and efficiency in the provision of Scottish public services. A recent paper to the parliament's finance committee by the water industry commissioner quantified the gap in efficiency between privatised water companies in England and Scottish Water as £250 million a year.

Shortly there will be a new framework for planning policy. There is significant evidence highlighting the economic cost of development constraints. The communities committee of the parliament will consider a report on planning reform, based on the deliberations of an expert group that had only two out of 15 members from the private sectors. Last year's planning audit in Scotland reveals that only four out of the last 12 structure plans were processed on time by the Scottish Executive. If you take the major developments west of Edinburgh that were considered in less than three months, you have a less than impressive 9.2%. But if you want to build a conservatory on your house, then you have a 90% chance of it being considered within two months.

One of the knock-on consequences of such delays in major applications is the impact on new housing supply in Scotland. We had a discouraging debate in parliament where parties on all sides characterised the problem with affordable housing in Scotland almost entirely in terms of insufficient finance for socially rented housing. But socially rented

housing now accounts for only around 15% of the new build for people wanting to move into a home. Likewise in the areas of transport and digital technologies, the pace and speed with which we pursue the structural reform agenda as laid out at Lisbon by the EU is likely to be what determines Scotland's competitive success over the next decade. There is no *prima facie* reason why Scotland should be bringing up the rear around structural reform. We should be out ahead.

When you look at the progress of structural reform across Europe, and at individual countries, progress in implementing reform – as measured by the Lisbon scorecard published by the Centre for European Reform – the Scandinavian countries now top the list for structural reform. They provide a set of models of ambitious social democracies that could be hugely congenial to the Scots. If one of the insights of the Irish experience is the need for consensus, then Scandinavian social democracies may offer a possible model for a devolved Scotland. These nations exhibit a commitment to harnessing competitive forces in the public and private sectors, alongside a commitment to social justice, which together deliver the sort of dividends that I think Scotland seeks but has perhaps not yet grasped fully.

Response

Alf Young, Public Policy Editor, *The Herald*

I sympathise hugely with the initial thrust of the argument, but you cannot make meaningful comparisons across countries with such different histories, heritages, although they are Celtic cousins. Ireland was, for much of the 20th century, essentially an agrarian economy. Scotland was not; Scotland was an industrial economy. They were quite different in character. Today they are quite different in terms of the demography. Walk along the street in Limerick and the average age is about 20. Walk around parts of Scotland and the average age is getting way up to my territory. They were and are quite different countries, quite different cultures, quite different societies.

So, I think you can only push those arguments so far, but I want to come on to where that takes us to in terms of looking at the Scottish experience. It is right to say that there is no Irish or other magic bullet out there and that the Scottish solution has to be indeed a Scottish solution.

But in terms of where we are and where we are going, again I agree with some of the analysis. For example, I have argued for a very long time that the Chungwa experience was in many ways the low point of the inward investment phase of our policy making. It was madness, frankly, to throw the millions that we threw at that plant to bring in an 80-year-old technology that we had invented in the first place.

But where I begin to have some problems is: while it is right to say that the Irish/Scottish dichotomy is a real one, and that the history and heritage and traditions are very different and the experience is very different, I equally worry that the high road/low road dichotomy is also a dangerous one. I cannot conceive of an economy where the dominant portion of activity in that economy is accounted for simply by higher-order activity; I think you would be pushed to find an economy where more than 10% of the labour force was actually working in higher-order activity anywhere on the planet, and that includes the United States. So the idea that we will find an economic destiny where we are all living from our brainpower and that none of us are doing anything so servile that it could be copied in Bangalore or Shanghai is actually, I think, a fraud.

Yes, let's try to develop high-level skills and base businesses on them, but there will still be a large tail in that economy which is pretty basic. There will still be shops; there will still be hotels; there will still be great swathes of economic activity that require lower

orders of skill, although even within the lower-level skills activities there is still tremendous variety in terms of skills and service levels. We all know from our own personal experience that a hotel receptionist in Japan or in the States compared to the average hotel receptionist of just 10 years ago in the United Kingdom was a revelation, and I think there are still great swathes of industry where that is still the case.

A complex road

So, the economic future for Scotland, when we call it a high road future, is a complicated high road. It is a high road that is about a quality of service in an increasingly service-dominated economy. I also think that despite pitching for a high road approach that emphasises skills, there are significant areas of our current economy where we are actually losing those activities in quite big order.

We are sitting here in the middle of financial Edinburgh. Fund management is in some difficulty at the present time. First, we had the loss of the ownership of a lot of the mutual life offices. Now we are seeing a second phase of this restructuring and the loss of quite a lot of the fund management activity associated with those independent institutions.

So the high road approach is not easy – it is not even easy to hold on to some of our traditional strengths, like in the industry, a really indigenous business. If you talk to people in that sector in some of the bigger companies, in Diageo, there is a constant battle going on within these businesses to retain a lot of higher-order activity, not just here but even in London. Diageo now thinks on a European scale. People I know who run bits of the business here seem to spend their life shuttling off to Amsterdam or off to the Far East. There is an increasingly globalised focus in what they do. So, there are problems, even in traditional sectors like financial services and whisky, in maintaining that high-road approach to the future of the Scottish economy. I think that is a profound challenge to us, going forward.

So while I accept that the classic aspiration to be another Celtic Tiger is misconceived, in terms of thinking that you can “do an Ireland” in Scotland, I also think there are dangers in creating a new dichotomy of high road and low road, because we are currently experiencing difficulties holding on to bits of our high road. We will always, I suspect, have a low road, because every economy and every society does, and what matters there is improving the quality of the low road, retarmacking it with a rather better attitude to the customer than the one we have had historically.

Wilf Stevenson

You did not pick up on two things that Wendy was, I think, hoping that you might come back on. One was this very important question about whether there was enough competitiveness being engendered within the Scottish economy. The second is the question of the public sector, and how you are going to get productivity gains of the order we are talking about.

Alf Young

I accept the diagnosis of the public sector pretty well completely. I think there is a big issue about the lack of productivity. There are pretty basic problems about the public sector in Scotland – we do not even know how to measure productivity within the public sector. We do not have any real meaningful way of knowing whether it is efficient or inefficient, but it certainly is not competitive in the main. I think there are big issues there about breaking up old assumptions about traditional models of public service delivery.

One of my favourites is that our much-heralded support for free personal care for the elderly is actually having massive consequences for other elderly all over the system, because to pay for free personal care a lot of local authorities are now cutting daycare services, like home help services.

On competitiveness in the economy: my experience of competitiveness in Scotland is that you can increasingly exercise personal choice in ways that you could not do even five years ago, which is adding to our competitiveness. Even if there is not direct competitive pressure on the street in important sectors in Scotland, we as customers can do something about that in ways that we could never do before. I have just got my latest quote for my home insurance, and I suddenly realised that I am a pretty rotten customer because I do not look around. I just do not have the time. I think I have got more important things to do with my life than road-test what I am being charged for house insurance against what I might pay elsewhere. But I have made a resolution to myself that I will do something about it, so I will be testing that in the very near future.

Discussion

Dr Marian V Jones, Senior Lecturer/Researcher, University of Glasgow

Coming from the higher-education sector, I have realised that the students today do not seem to have the optimism that they had in the 1970s, and the low-cost labour approach appears to have a legacy. While we are educating more people, we are actually producing people that are not necessarily better thinkers and are certainly not enterprising or have much optimism about the future. This has partially been due to underfunding in higher education, which we are all aware of, but another thing you actually said was something to do with costing products. If we see our institutions as being a premium product, surely we should price them as premium products? I am wondering what people think about how they might reconcile the education for the masses with the idea that education is a premium product, and should be a premium product on the global stage that we are competing in?

Wendy Alexander MSP

Let me try and answer. I think education has to be a premium product for as many people as possible. In Ireland their equivalent organisation to Scottish Enterprise, the Irish Development Agency, has created a new slogan: "Knowledge is in our nature". Reading the *Irish Times* this week, I came across this interesting article about the OECD's report on the future of higher education in Ireland. It notes that in the 25- to 35-year-old age group in Ireland, 15 years ago only 20% of people went through higher education; now it has risen to 48% – that is strategic intent.

In Scotland I think we are probably somewhere short of that, around 40%, among that age group. I think education is a premium product, but it needs to be one that is accessible to everybody. While we all know that we need more plumbers, the number of people going through higher education also needs to remain high or rise.

Alf Young

Every society needs plumbers. When you open the papers there is often a story about a biotechnology PhD student who has given it up to be a plumber, or a young woman in the City of London proudly brandishing her spanner and saying, "I am a plumber, too". The bit that is missing is any kind of public esteem for what plumbers do. That is the piece that is still missing.

A few weeks ago our dishwasher broke down and a guy turned up on a Friday to fix it, after we waited about 10 days to get him. On a Friday I sit at home writing a column on a laptop for the *Sunday Herald*, and I came to the door and he said, "Tell me what's wrong with the dishwasher," and I kind of displayed the symptoms and he said, "The pump's malfunctioning." He ripped the thing apart and said, "Yeah, it's the pump. I've got one in the van." He went out, got it and fixed it, then he opened this box that he was carrying, which had a laptop inside it, and he did my guarantee and my bill on a laptop.

He asked what I was doing and I said I was writing a column for the *Sunday Herald*; I'm a journalist. And he said, "Ah, brainwork." To which I said, "You mean what you have been doing for the last 40 minutes isn't brainwork? You didn't diagnose what was wrong with my machine; you didn't fix it; you didn't do a bit of IT to do the bill?" So that is what I mean about having problems about high road and low road. This guy had fixed himself on the low road, but he is an absolutely vital function in a modern economy. If he doesn't diagnose and keep machinery going in a domestic environment, then we all fall apart. If we could get some degree of balance into the esteem that we have for these different roles, then we would maybe begin to get somewhere.

Drivers of growth

Brian Ashcroft, Director, Fraser of Allander Institute, University of Strathclyde

I think the issue in terms of high road and low road is how you interpret it. First of all, we are talking about the drivers of growth, and in a sense you have got to distinguish between tradables and nontradables because tradables are essentially the drivers of growth; so, that is the first thing. The second thing: my interpretation of high and low is not to do with high quality versus low quality. It is about essentially trying to have a quality approach as against a low-cost approach.

Of course a successful economy requires a vibrant service sector that is producing quality inputs for its tradable sector, and they need to be skilled; they need to market the products in an effective way. So, there is no real problem here. The problem that you illustrate is, I think, a correct one in that the market does not work very effectively in ensuring that plumbers get sufficiently high wages so that people want to be plumbers. So people rather foolishly go and do PhDs in biotechnology, which are maybe not of use to anybody, and do not go into plumbing. This is a real issue and I think it is also an issue that we have to recognise in Scotland.

Jeremy Peat, Chief Economist, Royal Bank of Scotland

Four quick points. First of all, I want to endorse what Brian was saying about tradable and nontradable, and I want to go further than that and to say that the basis of an efficient tradable sector is often efficiency in nontradable, and if you do not get that then you have not got the foundation for success. But the competition internationally comes from the tradable side, and that is where the pressure needs to be, but the foundation below has to work as well.

Within that context my second point is related back to Wendy's point about the public sector, because if we have an inefficient public sector then we are providing an impediment to ourselves across the whole economy. When I was in the Treasury in 1984 I was asked by the permanent secretary to write a paper on comparative public productivity, and I was given no instruction other than that I had to show that productivity in manufacturing was strong and growing; productivity in the service sector was higher; productivity in the public sector was higher than that in the private sector; and within the public sector, productivity in the civil service was higher than any other comparison. And being a civil servant I produced an excellent paper – which may have a lesson for productivity in itself!

Going back to my third point, on plumbing: actually, you will be interested to know, the market mechanism is working. I have just come from a joint meeting of the higher and further education funding councils and I have been informed that there is now excess demand for plumbing places across all further-education colleges. So the market mechanism does work.

Coming back to the beginning of Wendy's session, going back to the Celtic tiger experience, in which I think you gave three lessons from Ireland: I want to come back to your second and third lessons and just say, can we really claim that these are learned for Scotland? The first one is that they understood they had to put the economy first. Have we learned that? I don't think so. I do not think we are saying efficiency rules – let's get that right. I think we are still fudging it all over the place.

Secondly, you said you had to take economics out of the political arena, in Ireland, to be successful. Have we done that? No. We are still playing silly, messy games that are detracting from getting at the critical issues on structural reform, on supply-side efficiency, which is where the public sector can play a role in providing the environment within which the private sector, tradable or nontradable, can then be efficient. We are not doing that. I am

delighted that enterprise and lifelong learning were brought together. I think that it was right that transport be added to the portfolio, but I still do not understand why we do not have a committee on the economy in the Scottish parliament.

Samantha Barber, Chief Executive, Scottish Business in the Community

I wanted to pick up on a thread that quite a few people mentioned, and it was about service. I think one of the problems we still have in this country is we mix the word “service” for “servitude”. If we are going to talk about providing a high quality of service, whether it is in retail, whether it is in our tourism industry – industries which contribute highly to our economy – then we have to address this question of service. It is not just in the private sector, because it is also in the public sector and the service that we are receiving as customers of the public sector.

My concern is that within the public sector, those of us who are using the public sector are not regarded as customers. I think one of the interesting adverts that is currently on some of the billboards out there is the one for BUPA, where it actually says: “The patient will now see you, doctor.” I think it is a very clever advert on BUPA’s part. Anybody who is using the National Health Service at the moment will realise that they are not a customer.

Crisis or no crisis

Wendy Alexander MSP

I want to disagree with Alf’s basic dichotomy between the high road and the low road. The high road is not about what you do as an individual; rather, it is about the character of your economy, and *how* you do your job (whatever it might be), rather than *what* you do. Alf’s plumber who is highly skilled enough to use his laptop – that is an example of how he does his job, rather than what he does.

A big issue for Scotland is that we do not have a crisis as the stimulus for change. In contrast, Ireland had a fiscal crisis in 1987, which stimulated far-reaching change, and the question which we have all been asking, in different ways this evening, is what might stimulate further change in Scotland in the absence of crisis? One answer is: evidence.

For example, we now have increasing evidence about the cost of inefficiency, but one issue is: how do we make that evidence visible enough to demand action? Recently, in the finance committee, we asked Scottish Water how much bills have risen in Scotland for small companies, large companies and domestic consumers. For small companies in Scotland, bills have risen between 50% and 2,600%. This is because many have been

moved on to fixed charges. It is also about saying we cannot afford to burden the domestic customer, we cannot afford to burden big business, as they are vocal, so there is only small businesses left.

The evidence on housing supply, on planning, on water and associated development constraints – in all of these areas, important evidence suggests better regulation rather than extra spending could fix some of the delays which are retarding development.

So, my instinct is for evidence, rather than crisis, as the way to strengthen the growth focus.

Wilf Stevenson

You could play a part in this, couldn't you? Write a few leaders, even on Sundays?

Alf Young

I can't write any more than I am writing at the moment. Four big columns a week I think is pretty good productivity from one person.

There has been lots said that I do not disagree with. When Wendy said that we have not had a crisis – I'm not so sure. I am old enough to have lived through that big industrialisation sweep in the late 1970s and early 1980s, and I have sat outside lots of factories that were closing. I have been to Lynwood, I have been to Invergordon, I have been to Fort William, I have been to Bathgate; I have been to them all, microphone or notebook in hand. It felt awfully like a crisis to me at the time. There was a sense of crisis then, but of course we adopted a strategy which I think with hindsight was not a very intelligent strategy. We just tried to replace one set of low-priced jobs with another set of low-priced jobs, and they came and went pretty fast.

I do accept that we have got to move up the value chain, but it is not easy. It is not even easy to hold on to some of your existing high-value chain, as I have said, and in both financial services and whisky I think you are seeing signs of that. It is quite hard to get a handle on some of the new high-value chains, as the experience at Livingstone with the Alba Centre has demonstrated.

Equally, let's not make the mistake of thinking that the other argument about globalisation is all about cheap jobs going to Bangalore and cheap jobs going to China. It is not. General Electric's biggest research and development centre anywhere in the world is now in China.

India is producing more software master's degrees than any other country on the planet at the present time. We will soon, I suspect, be in a position where if you want a cost-efficient cataract operation, the answer is to go to India. Do a bit of tourism at the same time and it will cost you a lot less than it would in the private sector in the UK, and it will be done a lot quicker than the NHS would get round to doing it.

So, I think there are high roads in India, and emerging high roads in China too, that are going to be pretty competitive in a very short space of time. So it is a much more complex interaction of forces and choices.

I am not being disrespectful to Brian or Jeremy or Sam, but the point that I did not address about how today's generation of young Scots feel in our university context interests me, because I have one kid who has just gone through university and has just finished a planning degree. Wendy will be delighted to know that he never intends to be a planner. But he has learned quite a bit about the hospitality industry in the last year, because he has blagged his way into being a bar manager. He has run a bar and he is now working up in the West Highlands in a hotel, and learning a quite valuable and quite portable set of skills in a global sense. All of it done in an informal basis, through no education system whatsoever.

Professor Alice Brown, Public Services Ombudsman

Wendy, one of your basic arguments was that governments do matter. I think you would concede that they do not matter in setting international global monetary trends; where they matter is in how they respond to them. You then went on to make the argument that you needed strategic intent, so my question is: where does the strategic intent come from? The answer should be: the Scottish Executive. But if you are genuinely operating a more plural political system, then this is where Jeremy's idea of the economic committee comes in. Are we mature enough to go down that road of the kind of Scandinavian model? I would not call it consensus, because I think actually if you use the word "consensus" it gives the wrong message. You are talking about building alliances that allow you to make that strategic leap.

Jack Perry, Chief Executive, Scottish Enterprise

The high road/low road debate strikes me as a little bit sterile, because quite frankly we need both. We need the rocket scientists and we need the plumbers, and I do not see them as mutually exclusive. I think we ought to be able to come up with a system which recognises the value of both and celebrates the success of both.

Optimistic youth

In terms of the graduates – and this is an interesting subject – as someone who has recruited hundreds of graduates over the last 25 years, I disagree substantially with the remark that this generation are not optimistic. I think the graduates I have been hiring over the last few years out of Scottish universities are the brightest, most assertive, most confident that we have been producing.

What I think is depressing though is that they do not see Scotland as a lively, vibrant, growing economy and a place where they want to make their lives and careers very often. They are not staying, and that is why the creation of the economy as our number one priority is so desperately important. I would like my children to feel that this is a place that they want to be and want to grow and raise their own families in future.

So, I disagree with the premise that they are not optimistic and confident. They may not be optimistic and confident about what the future in Scotland holds for them.

Alf Young

I think Jack may well be right. We agree on the high road/low road issue, but on the question of the outlook of the younger generation, I suspect your sample was a pretty unusual one. In terms of the broad sweep of students, I think it is a more complex picture. I do not know whether I would find the same picture in other European environments with similar demographic and other challenges. I don't know; I am open-minded on that.

I am a bit confused on Jeremy's appeal for an economic committee. Both he and Wendy are saying that one of the lessons from Ireland is to take economics out of the political arena, and yet your primary call seems to be: "Let's have an economics committee." How do these two things sit together? Trying to disengage would certainly give the economic issue priority, but also disengage it from the party political environment. How does that quite square? I'm not absolutely clear on that.

Wendy Alexander MSP

I do not think the parliament is the only starting point or the only end point. I think Ireland remains interesting because they changed what many people thought it meant to be Irish. Remember, they historically thought of themselves as "one of the most oppressed peoples". Our collective psychology in Scotland (if nothing else) has a lot in common with that earlier Irish world-view, and yet in 15 years they transformed what it meant to be Irish, and for the most part they have not relinquished their Irishness by changing.

In contrast, many people in Scotland think that they are somehow jeopardising their Scottishness if they line up behind change. I think it is partly generational. I think Ireland is interesting because they learned both to be Irish and to be comfortable with change. In Scotland we too need to learn to be Scottish and comfortable with change.

Wilf Stevenson

As Wendy said at the beginning, and it is right, one thing that politicians can do is set the tone. Thank you very much indeed for being such a lively and interesting audience.

Seminar 3

Innovation in Scotland

A seminar held in Edinburgh on 29 April 2004

Welcome

Wilf Stevenson, Director of the Smith Institute

Presentations

Roger McClure, Chief Executive, Scottish Higher Education
Funding Council

Charlie Woods, Senior Director of Knowledge Management,
Scottish Enterprise

Discussion

Welcome

Wilf Stevenson, Director of the Smith Institute

Thank you very much for coming. This is the third in our series looking at the elements which make a successful Scotland. We have been looking at the drivers of prosperity and growth in Scotland and seeing if, and how, they are distinguished from the rest of the United Kingdom as a whole and, by implication, whether different approaches are needed.

Today we are looking at many of the issues raised in the Lambert report, which was produced for the last budget and looked at the conditions under which the transfer of knowledge and expertise could happen between the higher-education community and the business community. The report came up with a series of observations and recommendations which are interesting in themselves, but it has become clear that there are substantial differences between Scotland and the UK in this area. So, with that as a background I am going to ask Roger to kick off and give us some thoughts.

Presentation by

Roger McClure, Chief Executive, Scottish Higher Education Funding Council

First of all, I would just like to say thank you very much to Wilf for giving us this opportunity to talk about things from the education side. It does not seem to matter what branch of administration or policy you are in, there is always nagging away at the back of your mind the refrain that is normally ascribed to Bill Clinton, which is: "It's the economy, stupid." While that is nagging away in the background, we now have in Scotland a partnership agreement between the coalition partners and government, which very explicitly puts the economy right at the top of the agenda.

When people talk about the economy these days it is not long before they talk about the knowledge economy, and indeed we have an economic strategy in Scotland which is called "Smart, Successful Scotland", so a major component of that is the knowledge base and how it is transferred.

Comparing Scotland with other European regions

I thought it might be useful to kick off with some highlights from a report that was recently published – you may all be familiar with it – which is the *European Competitiveness Index 2004*, by Robert Huggins Associates. It is the latest in a series of indices which that organisation produces. It is the first time that they have produced a regional index for Europe, and so all of the analysis is very detailed. There is a huge amount of figures centred around 91 regions of Europe, and Scotland is listed in here as one of those regions. I think that is an appropriate comparison. We often hear of Scotland being compared with England or the rest of the UK, but it is much more appropriate, I think, to think of Scotland as a region and compare it with comparable regions in Europe.

For Scotland, if you have not had a chance to look at it, the results are pretty mixed. On the competitiveness composite – that is, putting everything together – Scotland was 42nd out of 91 regions, so somewhere in the middle on the competitiveness index. Scotland is sixth of the UK regions. London comes out eighth overall, so that just gives you some kind of feeling for the range.

It fares rather better on the creativity composite index, where Scotland is 27th out of 91, and is fifth of the UK regions.

On economic performance, the basket of indicators places Scotland 32nd out of 91. But the one which is not such good news: on infrastructure and accessibility, Scotland comes out as 80th out of 91. You might think that is probably higher than it ought to be, but it is worth noting that on that particular ranking, London comes out as 65th out of 91 on that composite. Now, clearly there is a huge amount of stuff wrapped up in that single composite indicator and it needs a lot of disentangling.

The good news from all of this is that right at the top of most of these indicators are Scandinavian regions, and right at the top of the competitiveness indicator is a region in Finland. So, at least from Scotland's point of view, it would seem to indicate that geographical position and topography are not necessarily fatal characteristics when it comes to being a competitive region.

The economic role of tertiary education

So, what then about the role of tertiary education in supporting the Scottish economy? I think the first thing to say is there has been a long history of this. This is not new, and universities have been doing this for a very long time throughout the UK and in Scotland. But I think there is a significant point to be made, which is that the motivation for this, as prompted by successive governments, was that this should be seen as a means for the university sector to compensate for inadequate central grant. In other words: you have assets; you have intellectual property – go out and sell it.

Now, we know from the results that this, if that was the motivation, has not been particularly successful. It does not bring in significant income for institutions, except in a few isolated cases where you hit the jackpot.

It is also misguided in that, in seeing it as an income-generating activity, the incentive for institutions is to create barriers and to hang on to the property, to try and negotiate the highest value they possibly can for it. So, in terms of the sector supporting the economy, it has the impact of putting the brakes on any economic benefits. That is how things were.

I think it is important to stress that things have changed rather dramatically in the recent year or two. At the end of last year, University of Scotland held an annual conference. Bill Stevely, the convenor of Universities Scotland, was saying that the university sector fully recognised an economic role for the higher-education sector. You might think: well, no big deal; surely they ought to be doing that. But I can assure those of you who have not been associated with the university world over the last 10, 20, 30 years that if you went

back that far and asked a vice-chancellor what the university's role was in the economy, they would have just given you a very strange look and said: "That is nothing to do with us. We are engaged in higher activity that you wouldn't understand." The role in the economy was not recognised as being anything to do really with the main purposes of the university. That has changed, and I think that is terrifically significant.

Speaking for the funding council, for SHEFC, we certainly support that change and are doing all we can to encourage the sector to carry out that support for the economy. Why would we want to do that? You do not need to look any further than enlightened self-interest, because the name of the game has to be to grow national gross domestic product. We all want GDP to grow so that the standard of living can rise, that we can have better public services and so on. And from a bigger take, the education sector generally – the higher-education sector and the further-education sector in particular – can expect an increased income from their share of that increased prosperity.

Action to improve knowledge transfer

So, very quickly, let me just run through some of the things that we are doing. I am not sure that we have cracked it, but Scotland is distinctive in many things and I think in this area we are doing some different things and they seem to be bearing fruit. It is worth saying to start with that Scotland's institutions have been relatively successful already in the more usual measures of knowledge transfer.

We also know that there is a problem with business research and development, and although it has been improving over the last few years, it is remarkably low in the UK as a whole, and even lower in Scotland. But that is a major issue and needs to be addressed, and, as I am sure Charlie will explain, bold efforts are being made to address that.

The second thing I should mention is that you cannot have knowledge transfer unless you have got excellent knowledge to transfer. So a prime responsibility of the university sector and of the funding council, and indeed of the government, is to protect and enhance the competitiveness of the basic research effort itself – the knowledge base, if you like.

While Scotland has been doing extremely well through the research assessment exercise, we do have issues about the way things are moving in England as a result of the Higher Education Bill and the fact that, notably in the golden triangle – Oxford, Cambridge and London – and now, more recently, with the merger of the two big universities in

Manchester, there are real risks to protecting the competitiveness of our basic research, because of the purchasing power of those individual institutions with increased selectivity of research funding. It is not too fanciful to say that this kind of world-class research is a bit like the football transfer market. The big players, if they have those resources, can afford to buy the stars and nowadays can buy the teams that are supporting them as well, and you can lose a whole area of expertise, or a significant chunk of it, almost overnight. So this is serious and has to be addressed.

I am not going to go into all the details now but the funding council, working with the sector, has sponsored an initiative to see how we could change the landscape for basic research in Scotland, to defend its competitiveness and to enhance it. The approach we are working on, with the support of the research community, is not to focus all our resources in one or two institutions, but to see how we can pool resources between institutions on a kind of national basis across Scotland. I think that is one of Scotland's competitive advantages: that with its scale and very strong sense of identity, that kind of collaboration is much easier to mount in Scotland than it would be, I think, in England. We have high hopes that this kind of initiative will actually strengthen the research base very considerably. But it is not easy to deliver and will take some working on.

In addition, because the council thought this was so important, just over a year ago we established a knowledge transfer task force involving Scottish Enterprise, the executive, and so on, to make sure we had a good understanding of what the higher-education sector can do to really have an impact on the economy, and, if you've got scarce resources to invest, where is the best place to invest it. There is a risk that, for example, some parts of this activity which are much more visible than others, such as spin-outs, become too appealing to politicians, when in fact they are not really leading to sustainable economic growth. So we really need to do that analysis very carefully to make sure that we are better informed.

Again, drawing on the distinctiveness of Scotland, we realised in drawing up our plans for knowledge transfer that we had completely overlooked the role that the further-education sector might play in supporting the economy in this way. The recent Department of Trade & Industry report on innovation made the point very clearly that proximity is incredibly important, particularly when you are dealing with SMEs, and the smaller organisations which do not have the ability to interact so easily with big university departments and which probably in any case do not want cutting-edge research. They need more routine expertise and techniques.

So we are setting up a parallel task force in further education; a steering group has now been established and will meet very shortly and will be linked to the higher-education one. The vision there is that throughout the tertiary sector – mobilising both the further-education colleges and the higher-education sector – we should aim to produce a comprehensive support network for Scottish industry and the Scottish economy, particularly with its high proportion of small and medium-sized enterprises.

A further distinctive element of our approach has been the way we have funded all of this; and, again, in England the Higher Education Funding Council is just getting round to thinking about moving to the kinds of funding approaches which in Scotland we have had for some years.

The one thing I would particularly draw to your attention is the knowledge transfer grant, which is a grant to institutions to support knowledge transfer. That is the sum which we are in the course of doubling over two years, so that by 2005/06 it will be up to the order of £12 million a year, which in English money is about £120 million a year, and is larger at the moment than any sums that have been put in there.

More importantly, we have developed the allocation process for this to be supported by a set of metrics, which the universities are all now returning systematically and routinely in a series of strands of activity which have been identified with the help of the university sector. So we have got a much clearer fix on the kinds of activity that are being undertaken. Clearly, that, over time, will give us the opportunity to target our funding more effectively.

Not just money but people

I will just finish by saying that a key part of knowledge transfer which tends to be overlooked in these discussions is the transfer of people. However much money we put into the research effort (out of the £800 million-odd that SHEFC allocates, about £200 million goes into research), approaching £600 million goes into the teaching effort, and pretty well everybody who comes out of a university or out of a further-education college ends up in the workforce. If we really want to influence the economy, we should be thinking about what is the nature of the experience for all of these people, and what attitudes do they emerge from the institutions with? Is there anything we should be doing to examine that experience, and see whether in fact it could be adjusted and enhanced so as to make each of those graduates economically more effective? That is not to say that the economy is the only purpose of it, but it is a very important purpose.

We have just, in the council, begun to think about that, but in the meanwhile we are funding, for example, the Scottish Institute for Enterprise. We give core funding to it and Scottish Enterprise itself has agreed to put in project funding. All of the higher-education institutions in Scotland are part of that activity, which seeks to support entrepreneurship in student programmes.

The very last thing, so that I can seamlessly hand over to Charlie, is to say that in recent years we have begun to work – you might say not before time – much more closely with Scottish Enterprise and with the Highlands & Islands Enterprise. It is already being identified in England that the regional development agencies are going to have an increasing role in economic development and in the development of higher education. The equivalent in Scotland of course is Scottish Enterprise, and we have started to work much more closely together. I sit on the Scottish Enterprise board as an observer. Jack Perry sits on our boards, and in many respects we are working much more closely together. On that note, I suggest we pass straight over to Charlie.

Presentation by

Charlie Woods, Senior Director of Knowledge Management,
Scottish Enterprise

I would like to split my remarks into two: first of all some general reflections on the innovation process itself, and then some specific comments on the Scottish scene, which tie in very closely with what Roger has been saying.

Innovation as the pump of growth

As Roger says, the executive has made economic growth its top priority. The distinguished academic Paul Romer has referred to innovation being the pump of growth; and he used this analogy when he was analysing the role that scientific advance and competitive markets working in tandem played in promoting growth. He was quite clear in his analysis that it is this interrelationship which has been the critical factor in driving productivity in America, and lies behind the tenfold increase in real incomes in the US in the last 130 years or so.

He also looks at the nature of the process and comes to the conclusion that it is not linear – with basic research leading to applied research, leading to engineering and designing, leading to a product in the marketplace. It is much more confused, and often the practical problems of the marketplace can actually be the stimulus for innovation, which then science can refine and develop. A good example for that is the steam engine.

I think this all goes to emphasise the fact that the whole process of innovation is this combination of science, technology and understanding of markets, economics, taste and design all woven together into a process. I suppose it emphasises the fact that at the heart of what we are talking about here is an innovation system: a system that involves research, businesses, academics, business services, finance and government etc, and making that system work better is what we are all looking at. And it was very much the rationale behind the Lambert review that Wilf mentioned.

I don't know if many of you saw it, but *The Economist* this week carried out quite an interesting review of trends in business innovation and highlighted a number of things going on. I shall just refer to a couple of those. There is less big research and development being done by in-house teams, with more being contracted out to specialists in all parts of the world. The smaller companies have often been more nimble in their development of both invention and innovation, and it is interesting that this particular piece was

talking about the role that small innovation start-ups play in mediating between pharmaceutical companies and universities. It also mentioned the interaction between more sophisticated consumption patterns and increasing degrees of niching of products and services, and the implications of that for innovation.

Also, the fact that innovation is obviously not just about products, it is also about services and it is also about processes, but increasingly about the whole business model as well. The one conclusion I drew from it is that the system is becoming even more complex and the degree of collaboration and the strength of relationships that are built within the system are becoming even more important.

Just a quick word on the role of government in the system. It is critical. By its very nature the whole system is shot through with externalities, with benefits accruing to the wider community. Rachel Griffiths of the Institute for Fiscal Studies has estimated that the private returns to research and development investments are less than 14%, but the social returns are over 30%. As Roger has said, much of the spillover has actually come about because investment in innovation is about the development of human capital, and it is that flow of knowledge that is embodied within human beings which is absolutely critical. Again, things that make the connections and that lubricate the system in that regard are vital, and government has got a key role to play in trying to secure these important external benefits.

Because it is all about human capital, proximity is also important. As Roger mentioned, the role of places is definitely changing as technology changes. Technology brings people closer together in virtual space, and networks do work at very many different geographical levels, particularly in the academic community. But physical proximity is still an important part of the crucible in which innovation flourishes, and again that complex web of relationships is important. Increasingly you hear words like "habitat" and "ecosystems", from Silicon Valley to Singapore, to try and describe this sort of phenomena.

The last thing I would say about the process is that there are also self-reinforcing virtuous and vicious cycles involved, and when you look at the charts of GDP per head and investment in research and development in the Lambert report, you can see that the South East of the UK scores very highly and as a result attracts investment, graduates, human capital, and this in turn generates more powerful demand and the cycle renews itself. That is not to say when you are in a vicious circle you cannot break out of that, but it does take a determined effort.

The Scottish innovation scene

If I turn, finally, to some issues for Scotland and what we are doing here: the issue of demand is absolutely critical for Scotland, as Roger pointed out. University research and development, at around £500 million, is around 12.5% of the UK average. Business research and development is a similar figure in pounds, at around £500 million, but is about 4% of the UK's figure. Relative to GDP, Scotland is about middle of the UK regions. The position is improving: the share has risen from 2.9% in 1995 to the 4% that it reached early in the 2000s. But at 0.6% of GDP, it is well below the UK at 1.3%, the OECD countries at 1.6%, and, as Roger rightly said, Finland at 2.4% and Sweden at 3.3%; and these are the sorts of benchmarks we should be setting for ourselves.

We have seen, over the last 20 years, a number of initiatives developed in Scotland, with an increasing emphasis on trying to tackle this question of increasing business demand. What we do in Scotland is driven and guided by similar forces and principles that exist in other parts of the world, but I think, as Wilf said, we are developing our own distinctive portfolio of activities here that are set in a wider UK context. We obviously must not be complacent and we must try and learn from what is going on.

Let me just run through some of the major initiatives. I think the work that Scottish Enterprise and the Royal Society of Edinburgh led on in the mid-1990s was quite an important strategic initiative in terms of trying to raise this issue up the agenda, and, coming out of that, a whole raft of things have developed – the whole focus that we have put on specific industry clusters and the innovation systems within those clusters.

The Proof of Concept Fund provides assistance to researchers to develop research ideas into commercial concepts. Thirty million pounds has been spent on that over six years, with 120 projects funded so far, 40 completed and already 280 jobs coming out of that.

In addition, we have the link between Edinburgh and Stanford University – the five-year programme in computer language technology, with 10 partnerships coming out of that already.

Enterprise fellowships are implemented with the Royal Society of Edinburgh, with over 50 fellowships being provided for fellows within universities to develop business ideas. Those ideas have raised about £50 million of funding.

One of the big things on our agenda at the moment is for the intermediary technology institutes to act as a proxy for increased business research and development by commissioning and eventually commercialising market-focused research in the areas of energy, life sciences and techmedia.

So, there is a significant portfolio of activity developing in both the higher-education sector and in the economy more widely, and I would endorse Roger's point about the importance of the growing interrelationship between SHEFC and ourselves in that. I think that is very important. I think we are beginning to see some early impact, but this is a long-term game.

As to the future – many of you would have heard me say this before – there is no silver bullet. We do have to work on all dimensions of the system and recognise the systemic nature of what we are dealing with. We have also got to try and avoid being too prescriptive as well. We must try and be as joined up as we can be, in both innovative policy and in practice, and (if it is not a contradiction in terms) practise what I call strategic opportunism – where we set the broad direction and set the right environment (build a human capital base, etc) for supporting innovation, and, when you see a seedling that actually begins to germinate, then nurture the hell out of it and make the most of it.

Thank you very much.

Discussion

Lesley Riddoch, BBC Scotland

Just on this very interesting subject of competitiveness, is there anything that we are stunningly bad or good at? The creativity index was what we seem to be doing best at. What is that composed of?

Roger McClure

The creativity index tends to be composed of about eight or nine indicators. I have not had long to study this document. It has got so much in it, but it really needs a lot of disentangling before you come to very firm conclusions; but it is very, very interesting. In terms of Scotland's position in the UK, on the three main ones that I mentioned it was fairly consistent, but on infrastructure and accessibility Scotland was ninth out of 10 regions in the UK.

Rachel Squire, MP for Dunfermline West

You have been talking about where Scotland rates in terms of research and development, and mentioned the North West region as being number two in that success. One of the things I would say is: I remember some years ago going to Scottish Enterprise and trying to work with Scottish Enterprise and British Aerospace and others to develop the kind of effective partnership that I gathered had been developed in the North West, and I am interested in that. I am interested in what have you done, if anything, to try and get a certain sector of industry to put aside their daily competition in recognition that by forming an effective partnership, they can really come together in promoting innovation and taking industrial interests forward.

The second thing I would say is I very much welcome the further-education task force. You may be aware that in Dunfermline we have Lauder College, with its business learning centre, which has been very innovative in trying to reach out and connect all levels of the community and industry and form effective common partnerships.

Roger McClure

You mentioned Lauder College, and it is a very good example, and we need to have far more entrepreneurial colleges. Usually when people are thinking about the further-education sector they think of colleges being 70%, 80% or 90% dependent on grant from the funding council, because that is what a further-education college is like. Whereas a university has less than 50% of its grant from the funding council. But Lauder College has

less than 50% of its income from the funding council, because it has been so entrepreneurial and active in engaging with partners and generating income in that way.

So, that is a good example of what can be achieved, and the challenge now is to see how that kind of culture can be spread. Of course, there are always complicating factors, and people who are not doing this will say, "It is all very well for them because they have the opportunity, whereas where we are there is no opportunity at all."

On your point about expanding participation, I think there is a real difficulty there because, as I am sure you know, starting with higher education, Scotland already has a remarkably high participation rate in higher education – a rate that Tony Blair aspires to – but it comes with a cost, particularly when higher education for degree students typically takes four years.

Wilf Stevenson

Just to follow up, you point very dramatically to the lack of demand-led research. You said the intermediary technology institutes are going to be a substitute for that. Can you do it that way? Can you substitute what should be a business-driven decision?

Charlie Woods

It is trying to put in place a mechanism which has business members, is market driven by trends that are going on, and is taking place in the market. So it is not actually acting as a substitute, it is a catalyst to try and get more things going.

Maintaining the momentum

Unidentified delegate

This is really a question for Charlie. It is about how do we hold on to this in the longer term? I suppose the parallel I am thinking of, sitting here in the kind of new town, is the Industrial Revolution. Supposing we were sitting here in 1750, we would all be saying that Scotland is doing fantastically well in innovating; we invented the steam engine and all these things. Twenty years later, where has it all gone horribly wrong? The answer is: because the English look at all these things and say that we have got a market that is 10 times the size of yours and we can do it all much more cheaply and efficiently and so on.

So, it is: how in the longer run do you hold on to the next stage of this, and is the investment that you are talking about sufficient in a sense to maintain that long-term advantage, and what is the plan for that?

The second thing I think is that what it implies is that a lot of this is to do with finance and financial mechanisms. Again, if you go back to the Industrial Revolution, one of the reasons why capitalism is fantastically successful is not because they were more inventive in the 18th century than they were in medieval Europe, I think; it is actually that you had financial mechanisms in the 18th century which would gear this up in a way that medieval Europe could not.

My question, in a sense, there, is: does Scotland in any sense have powerful enough financial institutions to be able to drive that, or will the money always go to, in effect, the South East and the golden triangle, simply because in a crude sense the economies of scale are there? So how do we hang on to this in the medium to long term?

Charlie Woods

It is a very interesting question. A good question. Obviously, trying to grow companies of scale, from the seedlings that you are actually developing here, is what we are about; so we are increasing income and employment into the future. But you are also operating within a marketplace as well and talking about the role that ... certain large companies are using acquisitions of small seedling companies as a way of doing their research and development, and if those seedling companies are in Scotland, by the same token you do not want to stick a wall round Scotland saying "Go away", so you have to be part of that global marketplace.

I think that ties in with the financing as well, that by and large the financing for fairly large-scale development projects is by no means easy, but for a number of firms now the financing of the smaller scale (still involving quite large sums of money) is what is difficult, and hence the reason for the co-investment fund. This is a development on the previous venture capital initiatives that had taken place, which led eventually to the floating off of Scottish Equity Partners. They raised £100 million in their first fundraising, and that is available for investment in Scotland and elsewhere. The co-investment fund is £45 million for an agreed set of private-sector partners, who will match up to 50% of the investment that you are actually making in primarily technology-based start-up companies.

On the basis of the first 20 investments – and it has only been going for a few months – it seems to be playing quite an important part in the market. So that is trying to plug some of those gaps in the finance that exist in this system, and it seems to be encouraging.

No, at the end of the day the seedling companies that help grow and develop and nurture and all that, whether or not they stay in Scotland, that is all part of the development of the system. So other things, like our global companies programmes, will help them develop. It used to be the case that you could develop for a while in your home market and then branch out, but more often than not now a lot of start-ups are actually starting pretty much from day one in a global marketplace. As I say, no silver bullet, these are all parts of the system.

Roger McClure

I was just going to draw attention to the recent work by Richard Florida. If you remember, he talks about a “creative class” and so on, and asks if you believe in that as being one of the drivers. He then asks the question: “Where do they want to be and where do they want to live?” It seems to me that one thing that Scotland can do, and where it has some financial advantages, is to try and turn itself into a nation where creative people want to be, because of the quality of life and the way people approach activities and so on.

I think I mentioned earlier on – when I was talking about collaboration between universities and research, and Charlie was talking about businesses both competing and collaborating – everybody knows that universities compete like crazy, but they still do an awful lot of collaboration. I do think in Scotland that this is a competitive advantage which is inherent in this country. I have said on many occasions: in England, all the time that I was in funding councils in England, I never ever heard a vice-chancellor or a principal say, “I am doing this for my institution and I am doing it for England, or for London, or for the South West, or the North West.” But in Scotland you hear it time and time again, “my institution and Scotland”. I think that is real, and in such a competitive world you have to really exploit the natural advantages that you have.

Can I just make one other point? I misled you all entirely on the North West. So before anybody goes away from here and misquotes or gets into trouble – I was shooting slightly from the hip – the five regions of England that are above Scotland on the competitiveness index do not include the North West. I will just run quickly down the list. London was eighth, the South East was 12th, the Eastern region of the UK is 17th; and then running on down, the South West is 32nd, and just above Scotland is the West Midlands. I was remembering some of the other tables – there are so many in here – and the North West does particularly well on measures which are to do with research and development, and so on, in that area.

Turning the thinking around

Dr Ian Johnston CB, Principal, Glasgow Caledonian University

I would like to think the exact opposite of what we have been thinking and – I speak as a member of the Smith Institute – how it would run if you looked at some of the issues the other way round.

The first place I am going to start is with clusters, and if you look at Scotland and the English regions – particularly their regional economic strategies – you find almost every region is thinking that almost every major sector needs to be a cluster. It is complete nonsense, just complete and utter nonsense. Nine out of 10 have got biotech as a cluster, nine out of 10 have got advanced engineering as a cluster and the only one that is making a real success of advanced engineering – the West Midlands – has not got it as a cluster.

I was very struck by a presentation made in Edinburgh recently by the director responsible for new drug development with GlaxoSmithKline, and they were getting very worried about the increasing inefficiency of their investments. There is a lot of evidence that the more public investment goes into research, the less innovation comes out. They were finding the same with their private investment in research, in terms of new drugs developed. Basically, every 10 years it gets double the cost in real terms to get a new drug. In economic terms it was making their accountants rather edgy.

What they have done is to go back to small, autonomous, multidisciplinary teams and not actually to go for collaboration, except internally in small, multidisciplinary teams. They have increased their productivity in terms of new drugs between two and three times. So I do worry about the notion that we can institutionalise innovation, and I do worry quite a lot about the notion that the bigger the lump that you do it in, the more effective it will be.

I have got just one other place to go other than to remark – and I shouldn't, as a vice-chancellor – that large, ponderous universities are not terribly nimble, either. The other place to go is with the notion of collaboration and geographic proximity. The research indicates, first of all, that pro rata, industry is spending less now than it used to with universities.

I want to turn the sort of notions that we have been playing with on their head, and think maybe Scottish Enterprise should be encouraging us to call on investors from all over the

world and to go to invest in research institutes all over the world.

So, finally, I actually think instead of spending a lot of money on it, maybe we should just encourage people to visit successful schemes. Maybe we should be spending a lot of money from public institutions encouraging companies and university administrators to go to Scandinavia and see how it is done. We should be repeating that innovation is important again and again and again. I do agree with Roger that you will get from vice-chancellors: "We are doing this great research and it will be great for Scotland." You can tell from my English accent that I have not been here for long enough to be contaminated accent-wise, but I am contaminated by the success of the Smart, Successful Scotland policy. Everyone knows it. Everyone knows what it means; it really is very, very powerful as a message.

Kevin Cullen, Director of Research and Enterprise, University of Glasgow

A logical conclusion for the universities from what we have heard tonight is that we should be going to Scandinavia and targeting companies there as people to fund our research. Would that be a good thing?

Ian Doig, Public Finance Consultant

I am an independent consultant in public finance. My question is about the need to develop effective measures of performance and publicly funded projects. The public and the media tend to assume the way to measure it is by inputs. Therefore if you double the amount of input you should get double the amount of output, and it is not nearly as simple as that. So I wonder how effective our speakers have found the ability to measure performance selectively within the public sector. It does not follow that if you apply money equally, it will be equally successful.

Roger McClure

There is an enormous swathe of points raised there. I would just say in response to Ian that I think he is absolutely right that we should not assume that the conventional wisdom is always right.

On the question of proximity, I was careful to say that I was talking about small and medium-sized enterprises, and I think the evidence is right that for the big multinationals they operate in quite a different way. But Scotland's economy is predominantly SMEs, and therefore we have got to think about that.

On the critical mass argument and research, the pharmaceutical company is driven forcefully by a very powerful driver of the bottom line, but, at the same time, when you look at performance to date coming out of research universities, critical mass does seem to be a positive correlating factor. That evidence is hard to avoid, and if you have a chance to trawl through all of this, they are using the same kind of measures. So, it is not to say that you are wrong, but there is evidence for what is being done.

On the performance measures: this can get incredibly deep. The performance measures for the higher-education sector are very compelling – in terms of achieving the participation levels that government has sought, in terms of pushing up the quality of research as measured by an internationally calibrated, very detailed research assessment process involving international adjudicators and so on.

If you ask the question, “Has all that participation in the type of education helped the common weal as much as we hoped it would?” – I don’t know is the short answer, and I don’t think we have very good ways of measuring that. We have people like Richard Florida and others saying that when you look at successful economies and successful societies, there do seem to be compelling arguments that suggest that this is a strongly positive force. There was a recent survey that came out in England showing how one of the effects of higher education seems to be, for example, greater tolerance in society, and this has been measured by researchers. What price do you put on that?

We should not go away from here without acknowledging that the Scottish Executive actually has been very good on funding research in Scotland, and over the last few years it has continued to find money to put into basic research at a faster rate than has been the case in England. So I think that should be acknowledged.

Charlie Woods

I would hate it, Ian, if you went away from this thinking that what we are advocating is some sort of horrible, monolithic, institutionalised state planning machine or something like that. Quite the opposite: I was trying to get the point across that we are trying to pursue a mixed portfolio of activity which addresses different parts of the system and different sectors.

On the clustering point: I think part of the difficulty we have in Scotland is that it became almost a religious debate about whether or not you believed or did not believe in clusters. I think to a certain extent that is how the economy organises itself. If we look at our

research base, we see that both in terms of the quality and the quantity of researchers we have in the life sciences in Scotland, if we were not doing something to try and nurture that and get something out of that, we would probably need our heads examined. So perhaps that is one of the areas that you would look to put some focus on, but you would not put all your eggs in that basket. It is like any investment strategy: it does need to be a mixed portfolio. We have not really focused that much on advanced engineering, but that is another debate.

I guess, that mixed-portfolio point also ties in with the performance indicators point as well. One of the difficulties in all of this is you measure the inputs and, increasingly, we try and measure the more immediate outputs. But because of the nature of the system that you are working with, getting any really unambiguous attribution for what you are trying to achieve at the end of the day is very difficult. Now, that is not to say that you do not try and do it. Of course you try and do it, but you have got to try and push that output measurement down so that you get closer and closer and closer to the eventual outcome that you are eventually trying to get out of the system.

You also look at it from the other end as well, looking at how Scotland is performing against a benchmark set of countries and regions, so you try and look at it from a number of different perspectives and then try and take a judgment on it. But it is very hard to actually say: "I'll have 10 of those and two of those." But the essence of your question is right; you still must try and understand the impact, and when you are putting your mixed portfolio together you try and use that understanding to shape your portfolio. But it is a complex question.

Roger McClure

The performance indicators question is a very interesting one, and very often in the public sector it is very hard to find these precise measures, but we are going through an era where our political masters seem to think that unless you can come up with an absolutely specific number to measure some public policy outcome then you are failing. And of course in producing those numbers, as often as not, they drive managers into perverse behaviour, because the number is such a partial measure of what they are doing.

Wilf Stevenson

Time has beaten us. Thank you all very much.

Seminar 4

Opportunity for all

A seminar held in Edinburgh on 3 June 2004

Welcome

Lord Elder of Kirkcaldy, the Smith Institute

Presentations

Rt. Hon. Alistair Darling MP, Secretary of State for Scotland

Margaret Curran MSP, Minister for Communities, Scottish Executive

Discussion

Welcome

Lord Elder of Kirkcaldy, the Smith Institute

Good afternoon, ladies and gentlemen. Thank you for coming. This, as you know, is the fourth of a series of seminars that the Smith Institute have been running. The subject we are looking at today is social inclusion; we have got two of the most appropriate ministers – one from Westminster and one from Holyrood – that we could have. First, we have Alistair Darling, who is not only Secretary of State for Scotland, as well as the Secretary of State for Transport, but was also Secretary of State for Work & Pensions and so has covered this area as a minister in Westminster. We also have Margaret Curran, the communities minister, who is responsible for this area in Scotland.

Alistair, can I start by asking you to say a few words?

Presentation by

Rt. Hon. Alistair Darling MP, Secretary of State for Scotland

Thank you very much, Murray. I am grateful for the opportunity to speak to you today about an issue that is at the core of what I believe this government stands for, which is a just and fair society. I think it is also fitting that the John Smith Institute is involved in this. As Murray said, this is an area which John was very interested in, and when Gordon Brown was speaking at the John Smith memorial lecture almost 10 years ago he said that our task was to make opportunity real for millions denied life chances: the unskilled people denied hope in run-down areas, the marginalised and the insecure. That, I think, is what lies at the core of everything we have tried to do.

What I wanted to do was just briefly go through some of the things that we have done over the last few years. One of the points that we need to keep at the front of our minds is that of course social exclusion has a public price in terms of cost, but it also results in a terrible price for the individual and the families concerned. One of the first things we did in 1998 was to publish an annual poverty report. I remember being told by my colleagues that this was to be something that would come back to haunt us, and in some ways it is quite right that it does come back and haunt us, because it is a reminder that no matter how much has been done, there are still people who are excluded, still people who are living in poverty and still people who rightly expect our help.

It is worth remembering that just a few years ago, nearly one household in five of working age had no one in work, and there were nearly 3 million people living in poverty. I think we sometimes forget that, but actually it was not that long ago. Ten years ago in Scotland you could see visible evidence of that. All of us who were representatives of people, of whatever capacity, were conscious of the fact that we constantly came up against people who lived in a house where nobody worked and there was no experience of working.

We were also in the absurd situation where people could honestly say, "I can't afford to work," because the way the benefit system worked was that, in some cases, if you went into work you were worse off. The problem was that the welfare state was out of date, and what it did in many cases was done in a very out-of-date way.

A welfare revolution

Over the last few years we have brought about a quiet revolution in the role of the

welfare state, and I think in retrospect it will be seen as one of the biggest changes since the Beveridge reforms of the 1940s. What we did was to change the system from being a pretty basic form of insurance – and it was pretty basic in many cases – into something that provided people with choices and help, but above all a system where you could honestly say that it pays to work in every sense. Underpinning our approach – and this applies as much now as it did then – was our passionate belief in the vital importance of work. It is a work-first approach, and to that extent it was actually a radical departure from things that had happened in the past.

I remember being very struck by the fact that when I became Secretary for Social Security, eight out of 10 families where nobody worked lived in poverty, so it was pretty clear to me that the number one remedy was to provide work. If you provide work, you are well on the way to providing people with opportunity, because that is the best way of raising people's incomes. Work also gives people a stake in the community. If you've got work, you've got money. If you've got money and you've got a house, you've got a stake, and that is extremely important and gives a sense of belonging. That is one of the reasons why we removed a lot of the barriers to work, including changing the tax and benefits system in order to help people to get into work, and they could see the benefits of it.

The other thing that we did was to set up an organisation known as Jobcentre Plus, which some of you may have seen – you cannot miss it, because it is the most lurid green paint that we could have used. David Blunkett and I originally had joint responsibility for this, and for obvious reasons David said, "You choose the colour." easyJet had got away with orange, so we had to be stuck with the lime green.

But the serious point is that they are not the standard social security office with a grille. They are nicely turned out, they are a nice place to go to, and the reason for that is we needed to move away from a situation where we saw people who were unemployed or out of work as a sort of commodity that had to be handled in bulk and processed, to a place where you could sit down with people and say, "Okay, what do we need to do to help you get into work? What do we need to do to make sure you get what you are entitled to and help with training and so on?"

I think not only has the philosophy had to change, but the way in which you deliver the policy had to change as well. It was controversial at the time, but it did work. It is getting a lot of people into work. Of course, quality of work matters, but I do think that once you have got somebody into work and you have somebody on the first rung of the ladder,

then it is very important, because then there is the chance of getting people further up. I sometimes despaired in the past where people believed training courses were the only answer, and people would end up going on one training course after another, without experience of work. People never had to confront the grim reality, and I put it generally, of getting up in the morning, going to work and finishing at five o'clock.

The next stage

I think we have now reached a stage where we have got many people into work who were ready to work. But we are now in a position where there are many people who are out of work who will need rather more individual help and assistance than the system has hitherto given them. Don't misunderstand me: the New Deal has achieved a tremendous amount; I think it would be a tragedy if anyone came along and took it away, because you would go backwards. But we do need now to move to the next stage, of concentrating on those people who have not gone into the labour market for one reason or another.

I am struck by the fact that in this constituency, unemployment is pretty low – it has been 1% or 2%. But there are areas in the East End of Glasgow, for example, where unemployment is much higher – it is about 6% or 7%, and in some areas it is higher than that. You can see this in central London, where in Canary Wharf you have got very high levels of employment and there are labour shortages, but if you go into Hackney across the other side of the tracks, literally, you have got very, very high levels of unemployment.

So what I think we need to do now is move to the stage where we are providing far more individual help for people to help them get into work. I was saying to somebody earlier on that if you look at the people currently on incapacity benefit, yes, there are a lot of people who are on it who are sick and for one reason or another they will not be able to work. But an awful lot of the people on it are the generation who lost their jobs in the 1980s, ex-miners for example, who were conveniently shunted off unemployment on to incapacity benefit.

The question is: what do you do? I think it is essential that we move from the first phase of the New Deal, which I regard as being a way of getting a lot of people into work, into the next phase, which is getting people into work who have been excluded and who, if we are not careful, will remain so. We can do quite a lot as far as the national government is concerned. We do the benefits system, the Jobcentre Plus, and Margaret very shortly will be setting out some of the things that the Scottish Executive is doing.

The final point I want to make about this is: whereas I think you could have dealt with this problem a few years ago by setting up measures and help that were aimed at dealing with people in general, now we have got to focus much more on the individual who has got particular problems. That makes it very, very expensive in terms of resources and in terms of commitment, but, frankly, when you look at the rewards you can get, not just for the individuals but for the country as a whole, then I think that is something well worth doing.

So, with those preliminary thoughts, Murray, I hope that has given us something to get going on, and obviously when the time comes I shall be happy to listen to what people have to say, or to answer any questions that may come my way.

Lord Elder of Kirkcaldy

Thank you very much, Alistair; that was excellent. I will just ask Margaret to take us forward.

Presentation by

Margaret Curran MSP, Minister for Communities, Scottish Executive

I am gratified that the comments I am going to make run in parallel with what Alistair has been saying, because I do think that is very much how we see the agenda developing as well. The partnership with the United Kingdom government is obviously the central task and is something that is of critical importance to us. Also, interestingly enough, we see our partnership with business becoming more and more important to us, not just because of economic growth, which of course is our number one priority, but also, I think, because it helps us to address the social justice agenda in Scotland.

I suppose the starting point of all this is how we characterise the debate. I have been a politician for five years and I think I am learning all the frustrations of my more experienced colleagues here, because I get so frustrated at the way that the statistics are interpreted and how that is so easily translated into slogans. I think it actually does a disservice to the poverty analysis that we need to have.

We are told in Scotland that poverty is increasing. If you interpret the figures in one particular way, you can actually see why that would be substantiated, because while you have a government that is increasing national incomes – and I think British incomes rose by something like 19%, or some figure akin to that, over the past few years – then obviously the gap would apparently grow. But what that masks is that we are making strides in tackling poverty, and if you misunderstand that you underestimate and undersell the things we need to do to tackle poverty.

So what is important is that we get some of statistics and some of the facts around the poverty debate right. We have reduced the number of children in relative poverty by a quarter, and have halved the number of children in absolute poverty from one in three in 1997 to one in six in 2003. It is important that you understand the difference between relative and absolute poverty, because we still have to argue that part of our mission, if you like, is to change the conditions in which people live. It is not just to play a statistical game, it is actually to improve the quality of people's lives.

What we have to do is change how people live and change how people see themselves, and change how people actually develop their own aspirations and develop their own expectations for themselves. That is not the same as saying that you subscribe to a lifestyle analysis, because we know that work not only provides resources but actually

creates new opportunities and aspirations for people, and does allow people to live differently, and that is why it is so critically important.

We also know that it is not just about work. There is also a relationship with how people develop their opportunities within education, how they develop their housing standards, and how they develop their leisure and cultural opportunities. So we need to still get angry about poverty, as I think our generation of politicians still do – just as John Smith certainly did, and you can go further back than that to Keir Hardie – we still share that sense of vigour and anger in tackling poverty. It is because we still see people in the East End of Glasgow who not only do not have enough money, but also no aspirations in terms of their education. They have no aspirations or opportunities in terms of the cultural opportunities, and that is where you see teenage pregnancies going through the roof.

Of course there is a medical response to the problem of teenage pregnancies, but I would also say there was a social response to that. We have young girls in our communities whose aspiration in life is to get pregnant by the age of 15, and that is a challenge that we all face, and challenging poverty is part of the answer to that.

Abolishing poverty

The work of the Scottish Executive is absolutely essential. I think one of our most significant achievements is probably one that is least discussed. We are on the verge of abolishing poverty in Scotland – the verge is 2016, and that is a verge for a politician, I suppose – and have lifted 450,000 people out of poverty. When I was a community worker in the 1980s, in the bad old Thatcher days, the idea that we could abolish damp housing in Scotland or that we would introduce free central heating for pensioners in Scotland would have been an impossible dream.

So, that is my political point about how we characterise the debate about poverty. Those were absolutely the right things to do, but these things do not automatically appear in the poverty figures. We have got six councils now in our new wave of stock transfers coming through in Scotland, and that will do more to contribute to equality and tackling poverty in Scotland than a lot of minor projects that we have ever dreamed of.

But of course there is a lot more that still needs to be done. I would argue that we have made significant progress, but a lot more needs to be done. One of the most interesting dimensions to the work that I am doing is the emphasis on neighbourhood regeneration, and we have got big projects that are of great significance – Clyde Waterfront,

Ravenscraig, the extension to the M74, the second phase of Brayhead. And I think there is an emphasis on social inclusion, and we have to be very assertive about ensuring that those regeneration projects bring some advantage to the communities in which those projects are based. One of the great themes that we are developing – and I think we have to develop more in the economic sense of this – is that whole debate around community. What is community, and how do we develop people to take an interest and have a stake in their society?

There is a principle that underpins our work, which is that those who experience a problem really must have some say in its resolution. We have to recharacterise how we see the poor. Instead of being the problem, they are the solution, and I think that helps us understand how we transfer resources to those individuals and families, but also to those communities.

In addition, there is some interesting work we are developing around working with business on the employment front, and I think that helps us develop our relationship with Westminster, as we become closer to some of the Westminster agencies like Jobcentre Plus. There was a very interesting project that was developed in Springburn in Glasgow, where Tesco's dedicated to that community and guaranteed that they would take local people into their employment. Employment fell by 24%. There was evidence of reduced crime, including drug-related crime, in that community; and, through a training programme, new jobs were created for the local people.

In Glasgow alone there are 90,000 people on incapacity benefit. If we could begin to do something with a small amount of those people, just imagine what we would do not just for those individuals, but also what we would do for those communities. We now have the conundrum where Glasgow has huge job vacancies and has a skills shortage, and here we have 90,000 people on incapacity benefit, and Alistair has explained how many of those people actually ended up there.

But there is another dimension of this, which is much more about the social inclusion agenda, particularly the homelessness agenda. We are told – and, I think, properly – that in Scotland we have the most progressive legislation on homelessness in Western Europe, because we have taken the very brave step of tackling the root causes of homelessness. We understand that homelessness is more than a housing problem. We have had to make sure that health services play their part, and social work services play their part, and begin to tackle that problem.

But we need to go much further than that, because what that legislation has done so far is support people in that experience. But it is not comfortable for us just to support people in their disadvantage; we want to give them routes out of their disadvantage, and we want to transform their lives and thereby transform the lives of their communities.

Therefore, I think, the next phase of that is the link to employment, because that is the only way that you can turn around people's lives. We can give them better housing, we can give them better rights, we can make sure they get to a GP and we can make sure they get a better social work service. But the only way that they get long-term sustainable change is through employment, and that is why we need to link up with Westminster, and that is why I think we need to do more work with business.

I have been trying to develop our work with business more recently, and businesses are absolutely in agreement that it is in their best interest to have a stable society. So there is a whole agenda there for us to meet the big challenges we face in terms of people who have been homeless, who have been using drugs, and people who have been outside the job market.

Closing the opportunity gap

Finally, one of the things I would like to talk about is our work on closing the opportunity gap, because we still have huge problems in Scotland. We need to cut the rates of heart disease. We need to close the life expectancy gap and we need to improve some of our poorest-performing schools. I think we need to expose some of the inconsistencies that have been tolerated perhaps a bit too much in Scotland. We need to make sure that all the spending that we have is geared to actually tackling the poverty agenda, because we know, and we all agree, that it helps the economic growth agenda.

One of the distressing things I have seen is – we have got a huge debate going on about health in Scotland, and one of the things that distresses me most about that is, despite all that we know about the gross inequalities in health that exist in Scotland, we have a health debate that is only talking about where are the hospitals going to be and how much are we paying the doctors. We should be arguing about how that money is getting used to tackle health inequalities. In Glasgow, the executive has spent £700 million on health, but we are not actually using that money in a way that helps us tackle health inequality.

I have to say – and I know we are not meant to be too political, Murray – but I have to say that the ultra-left are most complicit in that debate, because the very people you would be expecting to say “Give this to the poorest people” are the very people who are saying, “Put it all in buildings”. Now, somewhere along the line, if we are serious about this debate we have to come to terms with some of the tensions that are involved in this.

So, I think we face a number of challenges. I will be the first to defend the UK government’s record and the executive’s record. I think we are doing absolutely the right things, and I think we have taken the brave steps about going to the root causes and recognising that we are in this for the long term. There are no quick turnarounds when you are tackling poverty. So we are determined to do that, but there are still big huge issues facing us. I think that is about regenerating our communities. I think that is about working in partnership with those communities. I think it is about recognising that we need a partnership with business and we need a partnership with Westminster. But, fundamentally, we must make sure that poverty remains at the centre of our debate, because if you do not begin to tackle poverty, you do not get the economic growth that most of us would all be committed to.

Discussion

Sarah Chisnell, GPC International

We keep talking about partnerships with business, and I remember in 1997 when Blair gained office we talked about the relationship between government, communities and business. But what – and this is to both of you, but particularly to Margaret – what do you think that means in real terms, over and above the training and skills agenda that obviously we all accept as part and parcel of our role?

Ian Doig, Public Finance Consultant

I was very impressed by both speeches. I was particularly interested in what Mr Darling was saying, and I agree almost completely with what he said. The only thing that struck me as strange was when he said that the jobs should be in the private sector. I wonder whether that needs to be thought about. My wife and I are just back from a week's holiday in Hungary in Eastern Europe and we were amazed at the number of public-sector jobs there that have been stripped out of the economy here. Things like guides in museums, railway porters – when did you last see a railway porter in this country? – community policemen, etc. So instead of spending a lot of money on social security and getting no return for it, I would urge growth in the public sector that would generate some real jobs.

Margaret Curran MSP

For me, partnership obviously implies much more than supplying training schemes for us. In terms of the poverty agenda, I think we need to get into a much more systematic relationship and I think there are a few other dimensions to it. One is rethinking enterprise and what we understand enterprise to be; what we understand entrepreneurial contributions to be and where we find them. That is about redefining economic interest, and there is a whole debate about that, and we really need to sharpen up some of our thinking around that in Scotland.

I am not saying we have abandoned all socialist pretensions and it is all privatisation from now on. I don't mean that. I think there is a different way of doing business and we can learn from that. And it is a culture that delivers, rather than a culture that largely reflects, the producer interest. I think that is where we need to get into this debate, and I think that is what is interesting about some of the debates on housing that I am having.

Sustainable employment

Rt. Hon. Alistair Darling MP

I think I could answer both questions together and take you back to the late 1970s, when the then Labour government and then the Thatcher government did make some tentative attempts to deal with the growing problem of unemployment. There was a lot of youth unemployment, and that is why you got schemes like the youth training scheme, which actually gave job creation a very bad name. I mentioned earlier my concern with moving from scheme to scheme to scheme and so on, but it was also in terms of the nature of the job.

If you are genuine about getting people into work, you have got to get people into sustainable jobs. In other words, they have to be employed in something where the employer actually wants them. I do not complain about whether we give the employer some help to take people on initially, but unless the job is actually sustainable, frankly, these people are going to be back out of the door at the first opportunity. Most of those jobs, whether you like it or not, are going to be in the private sector. I do not mind for one minute employing people in the public sector provided there is a job to be done, but what I think would be a mistake to do would be to get ourselves into a situation where we created jobs which we do not really need.

It comes back to the point that you were making, and what is encouraging is, when we started our employment programmes, a lot of firms faced with labour shortages realised that this New Deal was actually quite good for them. It was getting people into work who traditionally were excluded from it, like single parents or people with disabilities, which is traditionally a very difficult area. But I think we should keep at the front of our minds that it is our objective to get people into jobs because the employer actually wants to keep them and there is a reason for them being there. If you have got that, you have every chance that that person can then go further up the ladder and into the labour market. Obviously, in some of the areas that Margaret was talking about, you do need to look at interim steps, but job creation is something I have grave reservations about because job creation does not seem to me to be sustainable.

Stephen Maxwell, Associate Director, Scottish Council for Voluntary Organisations

As Margaret said, statistics can be misleading and misused, but one of the fairly well-established statistics, which I don't think is contested, is that income inequality in both Scotland and the UK as a whole is higher today than it was in the mid-1990s, and that the UK is second only to Greece among members of the European Union in having the

greatest income inequality. If figures were available for wealth, then the gap between the top and bottom would almost certainly be shown to be even greater. Can you say something about whether you think the reduction of income and wealth inequality has any part to play in reducing poverty and social exclusion?

Jeremy Peat, Chief Economist, Royal Bank of Scotland

What I wanted to pick up on was the point that Alistair Darling was making about the different problem that is now facing the UK and the Scottish administration in dealing with different groups of people. I recall the Scottish Office initiatives back in the 1980s dealing with Westerhailes and Castlemilk.

While I totally endorse what both speakers were saying about the need to look for the private-sector interrelationship and to look for real jobs, I think the difficulty is that the actual intensity of making them ready for those types of employment is huge. But also, we have to make sure that that challenge is not renewed by the next generation, which means the greatest priority is ensuring that those coming through the educational system at this stage are not going to be the next problem group. Dealing with the problem once it has emerged is hugely difficult, and when it gets more and more deep-seated – as I have discovered in dealing with some of the Prince's Trust cases – it is hugely resource-intensive and very difficult. That looks to me to be the prime challenge that we face.

Inequality versus poverty

Margaret Curran MSP

I will start with Stephen's point. If you had asked me 20 years ago what was my political ambition in terms of tackling poverty, I would have said there should be absolute equality of wealth between people.

Having spent the next 15-odd years watching us get wiped out at election after election, you wonder what is happening. Part of the answer to that has been – and I really do think this has been what the UK government has done expertly well – that in order to actually make sure that we get resources to those who are the most marginalised in society, you actually have to ensure that the middle, if you like, actually have a stake in that society as well. What we did, wrongly, in the 1970s was pitch those two groups against each other. What we have to do is create a new contract in Britain, and it is essentially a contract that says we can lift the incomes of the majority of people. We can provide services and create an economic climate where people can have prosperity and the

economy can flourish, while at the same time we can divert resources to assisting those that are the most disadvantaged.

So part of the answer is not purely an economic one. That is why I think our policy of having devolution that allows us to operate more in the interests of disadvantaged people is absolutely the right one. It is not just about income poverty, it is about the connectiveness of all the issues, marrying social policies with economic policy.

Rt. Hon. Alistair Darling MP

I am going to start with Stephen Maxwell's point. I know that a number of you here are academics and others work for organisations who do a great deal of work; and I do not wish to be rude or offensive, but one of the things that I remember of my four years in social security work and pensions was that there are three great things that always came up at academic seminars.

One is the sacred nature of the contributory principle, which I could never understand, as by its very nature it rewarded people who could contribute and if you did not contribute you actually did not get very much out of the system, which is why we have turned that on its head, almost. But I know that was a heresy, and probably still is in certain quarters.

The second was the work-first approach, which a number of people just thought was wrong, and the third area was the definition of poverty, which is a debate which still carries on. What the government actually measures – and this is for both of us, north and south of the border – are three elements.

One is relative poverty, because I think relative poverty is important, though it cannot be the only thing you measure. Another one is absolute poverty, and absolute poverty is actually what hurts. One of our objectives and one of the things we have done is lifted the number of people – both children and pensioners; a large number of people – out of absolute poverty by putting money into their pockets. It is redistribution if you like, but it works.

And the other thing that is important is persistent poverty. You will remember, again at the risk of being political, in the 1980s there used to be a fad for Tory MPs to spend a week living on benefit. Now I suspect anyone here could probably live for a week on a low income, but the problem is when it is week after week after week after week, then it is a different story altogether.

In relation to relative poverty, one of the reasons that the relative poverty gap has widened is because in the last seven or eight years the economy has grown dramatically. People are earning more, and because of that you get a gap between people at the top and the people at the bottom. If you are cynical there are two remedies. One is to have another recession – you can say that 10 years ago one of John Major's great achievements was actually to narrow the income gaps by having a recession. The other of course is the classic recipe of increased taxation and increased benefits. I have a problem with that, because firstly there is a problem with incentives, and, for the reasons I said earlier, simply increasing benefits may do something to help somebody but it is not a long-term solution to it.

But I make the point generally because I think all of us in this room – or most of us in this room, I am sure – are concerned that we eradicate poverty, because of all the problems that come with it. And all I would say to you is that I think it is a mistake to become focused on one measure, although I know it is a measure that a lot of people write about, because there are actually a basket of things that you need to look at and look at. I know people have been critical of the tax credit schemes that we have introduced because it goes against some people's orthodoxy, but I think the idea that you give more to people who need money most is something that is welcome.

Niall Scott, Commercial Litigation Unit, McGrigor Donald

The point that I really want to put is that Scotland is a tiny, tiny country. It seems to me that one of the advantages that this brings is the ability to cover the range of problems in the country quite easily, and to identify people who really can help to make a difference with certain programmes. I wonder whether the executive is interested in taking that theme further forward, and identifying people in business who have got an obvious interest in progressing some of the huge range of the problems that we have discussed tonight, and working primarily with those people as a kind of bridgehead in tackling the problem. Would Margaret perhaps like to comment on the executive's willingness to approach the issue in that way?

The US influence

Unidentified delegate

To Alistair: you have said that a lot of the welfare ideas of the government came from the USA, particularly in tackling persistent poverty. Although it is not your patch, I wonder if you might like to make a comment about the suggestion that Scottish Enterprise should lose its regeneration function.

For Margaret: you were talking about the need to target resources and you used examples from health and education. I wonder if you might like to enlighten us as to whether you are making any progress in evaluating how well those resources are being used and delivered.

Rt. Hon. Alistair Darling MP

We as politicians have many weaknesses, and it is a great pleasure to have an opportunity to abuse others – and it shows that we do not have to go out and cause trouble on the streets; we can do it in other ways. You are right: I have said that the work-first approach owes far more to American welfare-to-work policies than it does in Europe, because in some countries in Europe there is a reluctance to adopt that approach. There is still the view that what you need to do is to increase benefit income and then things will look after themselves, but the evidence is that that does not work.

I think the big difference in the States is that firstly, welfare is confined to a very small section of the population. What I think you need is a comprehensive approach that helps individuals, but it is also one that has got to be tied with economic growth and sustainability.

In relation to the regeneration point: one of the things that I have learned in the 12 months that I have been Secretary of State for Scotland is that there are various people who jealously guard the demarcation between what the Scottish Executive does and what the government in Westminster does, and there are even more people who write about these things who are ready to seize on anything you say. What I would say about it is that there is no doubt a debate to be had as to who should be responsible for regeneration.

Margaret Curran MSP

There are two aspects, I think, to what you have asked. One is just the hard slog in terms of where is the money going and what is the money achieving, and that is actually a very, very significant job. We are now undertaking a spending review and one of the themes of that spending review will be closing the opportunity gap. We have also got a cabinet delivery group which will be much more focused at looking at spend and trying to track the outcomes of that spend.

That is one part of it, but we need to stop talking about poverty and do something, and be much more prepared to roll up our sleeves and say, "That means you spend money on that, and you cannot spend it on that." That is what redistribution means; it means

perhaps we cannot provide a hospital at the bottom of everybody's street, because we are actually spending more in trying to tackle health inequality

Some of the things I was trying to say, about some of the work that we do with employers, is about working with employers and homeless people. We have got a whole group of homeless people that are in the system who are ready to make the next step on, in terms of their life, but they will not just walk into a job. They actually need sustained support in that job, and I think we could do quite an interesting piece of work with employers on that. The next stage of that is to talk to employers. I think the executive could be interested in developing those kind of discussions and those kind of arrangements, because I do think we could have a decisive impact with some key groups.

Lord Elder of Kirkcaldy

We have had a remarkably full discussion. I would just like, first of all, to thank the Royal Bank of Scotland, who have been responsible for supporting the Smith Institute in this series of seminars; and, secondly, I would very much like to thank the two main contributors.