BEIS0001140

Briefing note: Secretary of State CST meeting

Background

- On 29th September you wrote to the Chancellor with the BEIS Budget Bid (Annex A). In your letter you focused on:
    - funding for access to finance and business support;
    - a commitment to the 2.4% R&D target (baselining the AS16 uplift and announcing a trajectory of public investment for the next spending review);
    - lifting the rate of the large company R&D tax credit rate and consulting on the definition of allowable expenditure for R&D tax credits, and
    - increased funding for local areas to support local industrial strategies.
- In total you bid for: £2.45bn to improve access to finance for SMEs, £2bn to drive improvements in business productivity, and, in support of DCLG, for the allocation of £1bn of structural funds for local investment.
- You did not bid for a specific figure in relation to meeting the 2.4% R&D target, but it is estimated it will cost c£10bn in 2027/28 above the Autumn Statement baseline.
- Following your trilateral with the Prime Minister and Chancellor on the 17 October, the CST has asked you for a meeting to discuss the BEIS budget bid.
- HMT officials have indicated that the CST would like to focus the discussion on the BEIS budget pressures, and the potential to reprioritise BEIS budgets to fund these and any other budget bids. They have reiterated the CST's operating principle that Departments should be funding any new proposals from within their own budgets.
- Our line to HMT officials to date has been that we cannot fund the proposals from within BEIS budgets, and that we have provided the minimum viable options.
- HMT officials have informally given us their view of BEIS pressures and how these may be resolved from existing BEIS budgets. Further detail is included in the first part of this briefing.
- The second part of this briefing outlines your key asks from the budget letter, at this stage we have focused on the full asks, should you wish to discuss scaling the BEIS budget package, your officials can provide further advice on how we could reduce the size of the proposals.

BEIS0001140

Part 1: Existing BEIS budgets and pressures

- As your Budget letter to the Chancellor noted, we have been in discussion with HMT in recent months about a number of shared, inherited problems, which are placing pressure on the BEIS budget;

- We understand the Chief Secretary's view is that existing budgets should be reprioritised to fund new priorities and existing pressures, and that pressures are resolved alongside the Autumn Budget;

BEIS/HMT broadly agree on the issues to be addressed:

- Post Office Limited: £210m in 2018/19, with potential option of funding 80% in 2018/19 and 20% in 2019/20.

IRRELEVANT

HMT officials' advice to the CST recommends funding the pressures by:

- Repurposing R&D unallocated budgets (c£125m in 2018/19, 2019/20 to be confirmed)
    - BEIS view is that any proposal is a cut to R&D undermines the ambition set out by the CX at AS16 and by the Industrial Strategy.
    - A cut to R&D is a poor signal to send to industry, especially those seen as crucial for retaining internationally mobile businesses.

BEIS0001140

- Efficiencies each year from 2018/19 (c£30m per annum)
  - HMT view is we have said we can make 3% efficiency savings in our letter to CX on efficiency review in June.
  - However we made clear that some of these options would have an impact on BEIS objectives and wider Government policy (e.g. scaling back of some policy areas such as shale gas monitoring and support). We have not had a response from CX to this letter.

IRRELEVANT

Conclusion

- We recommend reaffirming our position that BEIS budgets are under significant pressure in future years and we require HMT funding to resolve these pressures as they are shared inherited problems which we as government need to resolve.
- If CST brings up the savings options in detail, we recommend:
  - Pushing back strongly on R&D and efficiency savings;
  - Offering to explore the Heat Networks, Oil and Gas Authority and Insolvency Service options, with the caveat that we would need to work up the details including the scale and timing.
- We can provide you with detailed lines to take on each saving suggested by HMT if you would find that useful.

BEIS0001140

Part 2: BEIS Budget Bid

Ideas

BEIS ask

- Government to commit to a 2.4% of GDP R&D target
- A commitment to baseline current innovation spending into the next SR and to increase spending so that 0.8% of the 2.4% target is public investment (an increase in spending of around £10bn a year by 2027).
- Increase R&D tax credits for small and large businesses
    - Large business rates should be increased from 11% to 20%
    - Enhancement rate in the SME scheme should be increased from 130% to around 200%

Supporting facts

- Direct public investment attracts rather than displaces private spend in R&D – additional c£1.40 for every £1
- Nearly £1 in £5 of private sector research is funded from overseas
- R&D spend in the UK is second bottom in the OECD
- R&D intensive business consistently cite the strength of our science and research base as a reason to locate in the UK

BEIS0001140

Business

BEIS ask

Support business to be more productive:

- 468m over five years to overhaul the current business support provision. This includes reform of Growth Hubs, £60m p/year support for high potential businesses, and a ‘Business Basics’ fund to pilot interventions to improve small business productivity in partnership with Be the Business.
- £928m over five years for a Business Investment Fund to allow us to secure high-value investment from key internationally mobile businesses.
- £345m over five years for a supply chain productivity programme to improve productivity through supporting training and enhanced business processes
- £247m over five years for an industrial energy efficiency fund to support energy-saving investments and reduce energy costs for important manufacturing industries

Access to finance:

- £2bn over three years for replacement of European Investment Funding to provide additional resources to the BBB to invest in equity and debt funds
- £450m of additional funding to the BBB for regional equity Intervention
- £195m over 15 years for the extension of the Enterprise Finance Guarantee to support the BBB to lend to viable SMEs who are unable to raise external finance

Supporting facts

- Poor management is estimated to account for about a quarter of the UKs productivity gap with the US
- Mayfield shows many firms are not adopting modern business practices (e.g. online accounts). Small businesses tend not to access external advice and they are often not part of peer networks.
- The UK has a historically thin market for patient capital for innovative firms, Damon Buffini has identified a £3-6bn gap in availability of patient capital in the UK before the withdrawal of European Investment Funds
- Pipeline of potential finding asks to the Business Investment Fund is now over £270m.

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Place

BEIS ask

In conjunction with DCLG:

- Honour the total amount of EU structural funds each of the four nations would have been allowed by the EU to commit between 2014 and the end of 2020.
- Decide how we deploy the guarantee to take advantage of the opportunity to make efficiencies in the administration of those funds and strengthen the role local institutions (such as LEPs and mayoral combined authorities) as a part of that process.
- Strengthen the governance of LEPs as primary local institutions including aligning geographies with Local Authorities and removing overlaps.
- Make LEPs responsible for developing their Local Industrial Strategy.

Supporting facts

- Regional disparity in rates of economic growth is starker in the UK than in other EU countries
- Only six UK cities have higher productivity levels than the average of over 300 European cities