Spatial Economics Research Centre

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Regional Growth Fund (Round II)

The government's has announced the next round of projects receiving £950m from the Regional Growth Fund. We are told that this will directly create 37,000 jobs with a further 164,000 created indirectly ('in the supply chain').

As with round 1, with the details provided (severely curtailed by confidentiality requirements) it is impossible to provide any analysis of whether it will achieve this on the basis of the list of schemes agreed. Writing in 2005, SERC affiliate Colin Wren reviewed the available evidence on the impact of Regional Selective Assistance (a competitive scheme for allocating money to firms in depressed areas). The estimated cost per job ranged from £8,00 £21,000 (in 1995 prices). If the RGF of £950 million delivers 201,000 *additional* jobs that suggests a cost per job ‘created’ by the government of just ov £4,700 (the same calculation for round 1 suggested 3,500 per job). In short, if these numbers played out, this would be a pretty effective intervention relative to existing schemes.

There are a number of reasons to think that these figures may be optimistic. First, with incomplete monitoring it is highly likely some of the 'leveraged' private sector funds ('£5 for every £1 of public money') would have been spent anyhow. To the extent that monitoring is imperfect, the RGF will only create additional jobs if it is being given to organisations that are credit constrained. Research that I have done with colleagues at the CEP suggests th this may only be true for smaller firms. We suspect this is because larger firms are better able to game the system (so monitoring is not as good) and a less likely to be genuinely credit constrained.

All of this suggests monitoring will be important for delivering additionality. Here, if I understood Nick Clegg correctly, the RGF is doing something different from the RSA. Specifically, when defending the amounts of money distributed so far he suggested that organisations that *know* they have the money coming have started activities. With RSA, my understanding was that usually firms need to receive the money first to demonstrate that public money is crucial to the project going ahead. This might suggest that additionality will be less for the RGF.

A separate issue is whether RGF will be more efficient than the Regional Development Agencies. Of course, it is impossible to tell at this stage. The R uses a different (competitive) mechanism for deciding on projects. This may lead to better decision making (or it may not). I would expect RGF to be more efficient per pound spent simply because it is spending less money. Civil servants may not be able to perfectly rank projects, but I don't believe th their selection is completely random, so the fact that the fund is smaller means it should achieve higher returns.

A final note of caution on the employment numbers - if all of government truly believed these numbers you might expect to see a lot more spending on RGF (unless they think that the smaller size of the scheme drives the high returns - as discussed above).

What about growth? Here I think there are further reasons to be cautious. In our work on RSA, we were able to find a causal effect of government mon in increasing employment and investment, but not productivity. In addition, assisted firms are on average less productive, so RSA expands employmer in less productive firms. This is still a 'growth' effect to the extent that these workers would have been unemployed (and we find some evidence, for RS that this might have been the case). But increasing the employment share of less productive firms may not be a good long run strategy for driving grow

Indeed, if growth is the absolute priority then you begin to wonder whether the government might be better off dropping the 'R' from the Regional Grow Fund. The economics of that are difficult. On the minus side it might be more difficult to find projects in the 'south' where employment generation is genuinely additional. Offsetting this is the fact that a Growth Fund would expect to be generating those jobs at relatively more productive firms. Of course, while the economics might be difficult, the politics of such a change are far trickier.

Posted by Prof Henry G. Overman on Monday, October 31, 2011

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