

ECONOMIC PERSPECTIVE 1

Scotland v Wales in the Inward Investment Game: Wales' Triple Crown?

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Introduction

Overseas direct investment in the UK economy is of substantial and growing importance. Overseas direct investment in Britain had a net book value of over £106bn in 1990, having grown from a total of under £18bn in 1978 (Business Monitor, 1991). Foreign owned enterprises operating in the British economy provide an estimated 13% of all manufacturing employment, 19% of net output and just over 20% of net capital expenditure (Invest in Britain Bureau, 1991). Between 1951 and 1990 over 35% of total US and Japanese investment in the European Community was sited within the UK. In 1990 a total of 350 projects were announced by foreign owned companies in the UK, with over 60,000 associated long term jobs.

At a national level the success of the UK in attracting high levels of new foreign inward investment may be explained by a number of market and cost related variables. Access to the wider EC is important, but the UK itself is also a major market. The UK generally has lower relative unit labour costs than many of its EC neighbours. The UK has a relatively low profit tax rate and no controls on profit repatriation. Added to this can be generous incentives for foreign investors to locate in specified development areas.

At a regional level there is keen competition to attract internationally mobile capital investment projects. During the 1980's both Wales and Scotland were amongst the keenest competitors.

In comparing performance, Young (1989) concluded that whilst Wales had edged ahead in terms of numbers of inward investors (and associated jobs) being attracted, Scotland was leading in terms of the quality of investment. This paper re-examines the performance situation in the light of more recent data and empirical investigations.

Foreign manufacturing industry in UK regions

Employment within foreign owned (and indigenous) manufacturing industry in the UK fell sharply in the early 1980's, before recovering slightly towards the end of the decade. In 1981, almost 860,000 people were employed in foreign manufacturing in the UK. By 1989 this figure

had fallen to just over 724,000 people, a drop of over 15%. Within these aggregates some regions fared rather worse than others. Table 1 gives a regional breakdown of these employment changes in foreign manufacturing. Northern Ireland, the South East and North West were particularly badly hit, with the Northern region being the only significant gainer in terms of the number of jobs in foreign owned manufacturing companies. However, the Welsh share of UK foreign owned manufacturing company employment rose from 5.3% to 6.3% whilst the Scottish share increased from 9.5% to 10.6%.

Both Wales and Scotland saw their shares of aggregate foreign owned manufacturing output increase between 1981 and 1989. However, with respect to shares of net capital expenditure the experience of Wales and Scotland diverge. In 1981 net capital expenditure by foreign owned manufacturers in Wales was £121m (8.6% of the UK total). By 1989 this figure had grown to £433m (11% of the UK total) or £9542/person employed. Corresponding figures for Scotland are £231m in 1981 (16.5% of the UK total), and £484m in 1989 (12.5% of the UK total) or £6320/person employed.

Attracting new foreign investment - Wales and Scotland compared.

Whilst data from the Census of Production illustrates changes in the stock of foreign manufacturing investment in Wales and Scotland, it can say very little about the success of the two areas in attracting new foreign inward investment. A large proportion of foreign projects are notified via the regional agencies to the Invest in Britain Bureau of the DTI. The IBB publishes data on new projects (including expansions, acquisitions and joint ventures) going to regions of the UK, and associated planned employment connected with projects. The difficulties of utilising this data set are noted elsewhere (Hill and Munday, 1992a, 1992b). The IBB data does however provide a guide to the relative success of Wales and Scotland in attracting new foreign inward investment.

Table 2 utilises IBB data from 1979-1990. The Table shows Welsh and Scottish shares of UK reported new foreign projects and associated planned new employment. Scotland is larger than Wales and can therefore be expected to attract higher shares of new investment. To

compensate for this, regional shares of new jobs/projects are divided by respective shares of employment to derive an index of comparative success. The data is grouped for tri-annual periods to remove the effects of annual fluctuations.

Table 1 The level and distribution of foreign manufacturing employment in UK regions, 1981 and 1989

Region	Employment (thousands)		Percent change
	1981	1989	
Northern	42.4	46.8	+10.4
Yorks/Humber	49.9	51.4	+ 3.0
East Midlands	41.3	39.7	- 3.8
East Anglia	36.5	36.1	- 1.1
South East	310.7	221.4	-28.7
South West	42.8	37.1	-13.3
West Midlands	68.0	69.4	+ 2.1
North West	115.0	86.7	-26.4
Wales	45.4	45.4	0
Scotland	81.5	76.6	- 6.0
N.Ireland	24.8	13.6	-45.2
UK	858.1	724.1	-15.6

Source: PA1002 Census of Production (various).

Table 2 New foreign projects and planned new jobs in Scotland and Wales 1979-1990.

Projects	Scotland		Wales			
	Proj (% UK)	Rel.Index	Proj (% UK)	Rel.Index		
Years						
1979-81	97	20.6	2.3	54	11.5	2.6
1982-84	151	21.7	2.4	90	12.9	3.0
1985-87	124	11.9	1.3	152	14.6	3.6
1988-90	133	12.9	1.5	166	16.0	3.7
New Jobs						
Years						
1979-81	12987	26.3	2.9	6172	12.5	2.9
1982-84	16154	30.4	3.3	6975	13.1	3.1
1985-87	10556	16.6	1.9	8834	13.9	3.4
1988-90	19779	23.1	2.7	12306	14.4	3.3

Source: Derived from information from the Invest in Britain Bureau data.

On the basis of the tri-annual series Scotland has performed less well in attracting projects during the latter half of the eighties. The Scottish relative performance with respect to new jobs is better, but again performance during the latter half of the eighties is not as good as during the earlier period. Wales, however, has experienced growth in both share of UK new jobs and projects throughout the period. This conclusion is

consolidated with reference to the relative indexes in Table 2, which are a guide to comparative performance. In terms of both the attraction of new jobs and projects Wales in relative terms has clearly performed better than Scotland.

The weaker performance of Scotland relative to Wales in the late eighties is also shown by a comparison of Locate in Scotland/Welsh Development International data found in Table 3. Between 1988-1990 Wales attracted 175 projects with associated planned employment (new and safeguarded jobs) of over 20,000, and associated planned investment of nearly £1.9bn. During the same period Scotland attracted 106 foreign projects, with associated planned employment of around 18,500 and associated planned capital investment of just over £1.1bn. Whilst the Welsh figures are inflated by the massive Ford investment at Bridgend of over £700m, it is still noted that Wales is approximately half the size of Scotland in employment terms.

Table 3 Scotland and Wales - foreign inward investment record 1988-90

Scotland			
Source	Projects	Planned jobs	Capital investment (£m)
N.America	60	10373	787.7
Japan/Asia	19	3726	240.1
Europe	27	4416	113.9
Total	106	18515	1141.7
Wales			
Source	Projects	Planned jobs	Capital investment (£m)
N.America	71	10169	1111.142
Japan/Asia	32	3269	282.074
Europe	72	7499	497.104
Total	175	20937	1890.320

Note: Welsh data refers to investment entering the regional economy during the calendar years 1988-90.

Source: Welsh Development International, Locate in Scotland.

Whilst recognising the improving relative Welsh performance, Young (1989) pointed to the growing Japanisation of Welsh inward investment, its concentration on consumer electronics and consequent doubts about autonomy, links with suppliers, dependency, the lack of higher management functions etc. These quality concerns over Welsh inward investment were reinforced by reference to the comparatively low net output and value added of Welsh employees in inward

investing firms in relation to their Scottish counterparts. Table 4 both updates and takes a longer term view of this information by examining various efficiency indicators for foreign manufacturing companies operating in both Wales and Scotland.

Both Net Output and Gross Value Added (per employee) in foreign manufacturing companies have been generally higher in Scotland than in Wales, although Table 4 shows some recent signs of convergence after some widening in the mid 1980's. Of equal note are the capital expenditure per employee figures with Wales consistently leading Scotland in terms of the capital intensity of employment since 1983.

Table 4 Foreign Manufacturing Firms in Wales and Scotland Capital Expenditure, Net Output and Gross Value Added.

	£/employee		1985 prices.			
	Cap.Exp.		Net Output		Gross Value Added	
	Wales	Scotland	Wales	Scotland	Wales	Scotland
1981	3367	3589	19559	20417	16187	17107
1983	2697	2422	25090	24577	20749	20426
1984	3623	2676	23961	28335	19597	23474
1985	4576	4007	23560	30069	18776	25324
1987	5081	2832	30488	34566	24298	29133
1988	6160	4969	32039	36330	25528	30744
1989	7834	5189	31519	32766	24999	26685

Source: PA1002 Census of Production, various.

Taken together the figures in Table 4 fail to present any consistent picture of the quality of inward investment in either Wales or Scotland, reflecting as they do both the diverse industrial structures of the respective regions and the overriding influence of cyclical changes in economic well-being across the UK throughout the 1980s. By the same token Table 4 lends no support for the hypothesis that whatever Scotland has lost in terms of relative numbers of inward investors has been compensated in terms of investment quality. Taken together Tables 1-4 indicate an improving relative performance in inward investment for Wales compared to Scotland in terms of the number of new projects from overseas, the number of new associated jobs and the level of capital expenditure engendered. Thus Wales may have fairly said to have scored a triple crown success over Scotland in these three areas at the same time as the Welsh team was having rather less success on the rugby field.

The competitive edge

There is no shortage of speculation about why multinational enterprises choose a particular country or region as a location for manufacturing facilities. A

number of interview based surveys have sought to identify why both Wales and Scotland have been attractive locations for inward investors. What has generally been absent however is empirical research that directly identifies the key factors influencing the regional distribution of inward investment in the UK. In the US, the changing distribution of foreign direct investment has been more widely studied. Glickman and Woodward (1988), in a review of US research put forward a number of factors which have been empirically identified as key influences, including infrastructure availability, labour market variables, market access and capital incentives.

Hill and Munday (1991) investigated influences on the increasing Welsh level and share on inward investment in the UK. They concluded that the improving Welsh performance through the 1980s could be related to the declining Wales/UK earnings ratio over the period, as well as capital incentives and infrastructure spending. In particular a 1% decrease in the Wales/UK earnings ratio could be associated with a £41m increase in capital investment (1983 prices) into Wales or a 1.8 percentage point increase in the Welsh share of UK inward investment new jobs. This research implies that lower average earnings, higher levels of regional preferential assistance and higher levels of infrastructure spending explained the Welsh competitive edge through the late 1980's.

Later research (Hill and Munday, 1992b) used the same methodology to examine the distribution of inward investment across UK regions. This work found that two-thirds of the variation in regional shares of UK inward investment new jobs, and almost four-fifths of variation in shares of new inward investment projects could be explained by reference to financial incentives and infrastructure improvements, as measured by shares of UK Regional Preferential Assistance (RPA) and UK spending on new trunk roads and trunk road improvements. However, the same work failed to find a statistically significant association between regional shares of inward investment and relative regional earnings, across the UK.

Hence the current state of empirical research in the UK would look to cost minimisation and market access variables as an explanation of relative regional success in attracting inward investment. For example, both Wales and Scotland are eligible for Regional Preferential Assistance (available to both indigenous and inward investing firms). The regions' share of RPA can then be used as a broad measure of available assistance. Table 5 shows Welsh/Scottish experience in the 1980's in terms of shares of UK RPA. In the early years of the decade Scotland was averaging just over a third of all UK RPA- by the end of the decade this proportion had fallen to just over a quarter, whilst the Welsh share increased from a fifth to almost a quarter. By 1989/90 RPA per employee averaged £130 in Wales to just £72 in Scotland. In part, of course, the level and share of RPA reflects not only the intensity of assistance but also success in attracting

new projects.

Table 5 Average Shares of UK Regional Preferential Assistance

	Wales	%	Scotland
1981-3	20.4		34.2
1984-6	22.6		32.2
1987-9	24.0		26.0

Source: Regional Trends

We noted earlier that low relative wages has been a significant influence on Welsh success in attracting high levels of inward investment although the influence of relative earnings could not be confirmed across all UK regions. At the start of the 1980s average weekly earnings in Wales and Scotland were broadly similar, but by 1990 average female earnings were 4% less in Wales than Scotland, whilst average male earnings were 6% lower.

Finally, whilst market access is likely to be an influential but immeasurable factor for overseas firms investing in Britain in order to gain access to domestic and mainland European markets, substantial infrastructure improvements in Wales have certainly improved access in the recent past. For example, London is now within two and a half hours drive of Cardiff (and even quicker by rail), whilst long awaited Scottish access to the motorway network remains just that- long awaited.

Conclusions

There is no doubt that the success of Wales in attracting foreign inward investment has outshone that of Scotland in the past ten years. It is worth noting (as Table 2 above shows) that both regions have consistently attracted a disproportionately high (in relation to size) share of UK inward investment new jobs and projects. It is more difficult to specify the exact reasons for comparative Welsh performance, given the similarity of the regions in terms of industrial base, development agency activity and the availability of financial assistance. However, we can point to higher Welsh shares of UK financial assistance (reflecting both the level and intensity of aid), significant infrastructure improvements in Wales and levels of earnings that have fallen well behind Scottish (and UK) averages.

In the early to mid-eighties there were some signs that Scotland was managing to attract higher quality inward investments, particularly in high technology sectors (see for example Firm et al, 1988, Young, 1989 and Table 4 above). In particular Stephen Young pointed to quality concern over Japanese inward investment. Wales continues to attract a higher level (and share) of Japanese overseas direct investment. Recent evidence suggests that

whilst concerns about the underlying quality of this investment still exist, there are encouraging signs among some Japanese enterprises of a greater indirect impact in terms of employee training, school/industry liaison, product development, and local supply linkages (Morris et al, 1992).

Turning to the future it may well be that future competition for inward investing firms is on a European rather than a UK level. Indeed competition between Celtic regions may widen to include Eire, Brittany and Spain. More likely, given the importance of wage costs, the emerging nations of eastern Europe may turn out to have a distinct cost advantage in future, although they are some way off being able to match the level of infrastructure and financial support currently available in Wales and Scotland.

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