

RESPONDENT: Paul Sheerin, CEO, Scottish Engineering (20)

QUESTION

MACRO/FISCAL

In your opinion, what will be the shape and form of the recovery and what will be the implications for the future growth and structure of the economy?

Our recent survey of members in the engineering and manufacturing sector provides ample evidence of the stark implications of the coronavirus crisis on our industry in terms of business sentiment and all key measures of commercial activity. It is entirely consistent with the findings of recent business surveys across this and other business sectors.

- 77% of respondents reported that their organisation's view is that the impact of Covid-19 will still be felt by businesses in 12 months' time.
- 80% of companies said that they will likely shrink employee numbers in the next six months.
- 72% forecast that reluctantly they will have to reduce training and apprenticeship plans to ensure business survival.
- 73% of businesses are forecasting that orders will be down and 70% are forecasting a decrease in output volume.

These figures illustrate that we are experiencing the most significant downturn in living memory with serious implications for employment and economic growth. Scottish engineering and manufacturing businesses deliver world class products and services and there is confidence amongst many in the sector that they will ultimately come through this crisis stronger and leaner. However, as we contemplate some sort of return to normal business in Scotland and the wider UK massive uncertainty remains regarding the roadmap to get there, the robustness of the international supply chains in which we operate, and levels of demand for our products and services in the UK and overseas.

A reasonable expectation would be that it will take at least 2 years to see some semblance of broad recovery across the engineering/manufacturing sector. The underlying situation at sub-sectoral level is, however, much more complex. All sectors have been impacted to some extent, but some more or less than others. For example pharma / meditech, those who have adapted to produce PPE, food and drink, utilities, and defence have largely continued to operate

albeit at reduced levels of output and have already adapted to the working methods required to reduce risk as far as possible in line with Government and HSE advice.

Other sectors, however, have been much more seriously impacted at both the national and global level and recovery may take several years. In some industrial sectors such as aerospace, oil and gas, and automotive there are serious concerns that they will struggle to recover to pre COVID-19 levels of production and employment for the foreseeable future. For these businesses the spectre of mass redundancies and plant closures looms large.

Industry support measures The Job Retention Scheme and other initiatives at UK and Scottish level have been critical in delivering “life support” to industry, protecting jobs, productive capacity and long-term economic growth. As an industry we appreciate the unprecedented and exceptional measures that have been taken which we believe compare very favourably with international competitors, and we welcome the extension until October of the Furlough scheme, but are concerned that any early cut-off date for new applications would adversely affect those sectors where the timing of impact is delayed but no less serious.

These measures are of course time limited and it is clear from the scale of the shock that many sectors of industry will require ongoing support beyond the period that they are available. The key questions that Government and industry must work together to resolve are around how that support will be structured and targeted to create the greatest long-term benefits for the economy, whilst protecting the interests of the taxpayer. As an industry association we know from first-hand experience that many of the businesses most at risk as a result of the pandemic would be entirely stable and viable in the course of normal business activity, with the prospect of making a significant long-term contribution to our economy and the global challenges we face over the coming years. These are the businesses on whom we must now focus our attention. They should have the fundamental requirements for recovery already in place in terms of leadership strength, the quality of operations and products and determination to survive, but in many cases even these will not be sufficient to ensure survival through the period of unprecedented disruption that

we find our ourselves in. Where established market funding mechanisms such as equity, bank loans or commercial lending have been exhausted then there is a rationale for Government intervention as a last resort. We are supportive of the creation of a government backed long term investment facility or funding body to support businesses via loans on this basis. Such lending would be open to applications from all sectors and would be targeted appropriately at those firms which can demonstrate a path to recovery and long-term growth.

As a last resort,there may also be circumstances in area of national strategic interest where equity based intervention is more appropriate. There has been much discussion in business, media and political circles about a focus on new emerging sectors such as renewables and life sciences and we would welcome such, but we are also concerned that those more traditional and mainstream industries which create the largest part of wealth and employment in our sector also receive support as required to ensure that they can manage through this crisis, adapt to global market trends and make a long term contribution to our economy. Other key areas for consideration would include the potential to target support onto addressing some of the structural issues in Scottish and UK industry including productivity, sustainability, and skills. It is not yet clear that the pandemic per se will have a significant impact on long term globalised trading patterns. Our sense is that international trade will recover rapidly, and we expect that Scotland, as an open economy will continue to be home to many with many firms operating at the heart of UK and international supply chains.

Resilience and security of supply We also believe, however, that the experience of the pandemic demonstrates clearly that the threat of disruption to international supply chains, albeit temporary in nature, is very real and has a high impact. At the same time we have been reminded in these tragic circumstances of the strategic importance of retaining a flexible and diverse manufacturing/engineering capacity within the Scottish economy, capable of meeting at least a substantive part of the range of goods and services required to preserve our way of life, our health and security .

This is an issue which will need leadership, commitment and co-ordination between public and private sectors to make sure that Scotland and the UK can mitigate the risk of being exposed to global shortages at a critical time. We were very impressed by the efforts of the manufacturing and engineering sectors to fill those gaps over recent weeks in areas such as PPE, ventilators, medicines and food but we also believe that there is a strong strategic rationale for ensuring that we have standing capability to meet these requirements and other vital products. Given the fiscal impacts of the crisis over the coming years, we also believe that there is a strong case for a greater focus in Government and industry on ensuring that as much of our public and private procurement, for example on major infrastructure projects, can be sourced domestically. When considered alongside the need to support the transition of carbon intensive industry towards more sustainable long-term business models there would appear to be significant opportunities for Scottish industry.

The experience of offshore renewables demonstrates the potential of such but also that there is much work to be done. Domestic versus foreign ownership Foreign ownership of capital and assets is a natural outcome of being an open internationally focused economy which attracts global companies to do business here. We note that many of our most successful manufacturing facilities in Scotland are an integral part of international groups.

Taxation We understand the sheer scale of the fiscal implications of the pandemic crisis and the potential consequences thereof. We would argue strongly, however, that taxation levels for business, including Corporate taxes and other levies in Scotland and the wider UK must be maintained at competitive rates with other major competitor economies to ensure that we can maintain and grow viable and internationally competitive domestic industries which are able to attract international capital and investment. This will be particularly true in the recovery phase over coming months and years where taxation policy must be sensitive to the economic fragility that will characterise many industrial sectors.

	<p>Regulation Effective regulation is key to ensuring appropriate standards of operational performance, governance and quality of outputs across manufacturing and engineering. The key issue is to ensure that such regulations do not unduly disadvantage Scottish business versus overseas competitors, deterring production and investment in Scotland in favour of offshore locations with lower regulatory “hurdles”. Brexit Brexit, and the continuing uncertainty over future trading arrangements were already creating an economic drag on Scottish manufacturing and engineering investment prior to the lockdown, especially for businesses at the heart of cross European supply chains and those who rely on EU labour markets.</p> <p>The UK has now left the EU and it is vital that future trading arrangements with EU and our other key trading partners are clarified as soon as possible and have minimum impact on international supply chains to avoid the “double whammy” of pandemic recovery and trading uncertainty.</p>
<p><u>MICRO/ENTERPRISE</u></p> <p>In your opinion, what are the medium to long-term consequences of the lockdown on businesses, including loss of employees, debt overhang, loss of markets, reduced investment and unemployment?</p>	<p>Sectors where the consequences are likely to be particularly severe. The oil and gas sector, and its associated supply chain are at particular risk given energy price volatility related to the pandemic crisis and global changes in environmental policy.</p> <p>Our Aerospace industry is also facing significant challenges given the impact of the crisis on air-travel.</p> <p>These sectors make a vital contribution to employment and wealth in Scotland and will demand careful support as we transition towards zero carbon targets. The skills and capabilities in our oil and gas supply chains are world class and support customers globally. There are also significant transferable skills in the sector in relation to renewable energy eg offshore wind. The industry should be supported, not penalised as it makes the long term transition to serving new greener energy markets.</p>

Likewise, our Aerospace sector is world class and is playing a significant role in developing new lower emission technologies. Support for these industries will be vital in maintaining high skilled, high value jobs in Scotland.

The Defence sector is also key to skilled employment and wealth creation in Scotland, and the relative stability that it has displayed through the crisis underlines its importance in a diversified economy. This sector is concerned that when counting the cost of borrowing to support the economy during the crisis, if public spending on these defence projects is reduced or delayed then it will come at the cost of the stability to the overall economy that these projects are supplying

Scotland's distinct specialisms and capabilities:

Scotland has a diverse manufacturing base which provides significant economic strength and stability to the country, however, there are specific specialisms and capabilities where we have opportunities to build on a leading global position eg in renewable energy, energy storage, aerospace/space, life sciences.

The concept of critical mass is vital here in terms of building national and regional hubs, supported in partnership with Government and academia by shared centres of excellence in developing and applying leading edge manufacturing and engineering techniques.

Revenue Funding:

Revenue funding will be key short term as “life support” to keep businesses operational and protect employment. Medium to longer term, innovative debt and equity approaches will be more appropriate to support those businesses with the long term potential to create value in competitive global markets

Public and private sector interaction:

Our expectation is that public / private interaction will be mainly focused on those sectors which offer the potential for Scotland to develop and build upon its distinctive capabilities, as described above. We would argue, however, that conditions should not be placed which unduly restrict support to other industries which remain vital in maintaining skilled jobs and economic contribution.

National Infrastructure and Services:

National infrastructure is widely perceived as a disadvantage for engineering and manufacturing in Scotland, particularly in those areas outside the central belt and North East. Transport connectivity in many areas is a serious constraint on investment and expansion, and energy costs are typically considered to be a material disadvantage versus competitor nations, particularly for more energy intensive industries. These issues only exacerbate the difficulties we face in recovering from the lockdown, and require targeted investment

Support businesses to drive a strong economic recovery:

	<p>Government needs to introduce targeted fiscal measures such as tax credits in relevant R&D/Investment, support for apprenticeships, and retraining, investment in measure to improve productivity.</p> <p>International experience indicates that such measures can be highly effective in incentivising industry to move in the desired direction where market forces alone may not yet have responded to the extent required. At the same time it will be important to avoid further taxation, levies or other penal approaches which risk rendering Scottish industry uncompetitive and displacing production overseas.</p>
<p><u>LABOUR MARKET AND INEQUALITIES</u> In your opinion, what will the implications of the recovery be for different groups, unemployment and on the nature of work? How is the recovery likely to impact on socio-economic inequality as a whole?</p>	<p>As a result of the pandemic crisis, and despite the efforts of Government, unemployment levels in Scotland and the UK have already risen to highest levels seen in 20 years, and with job losses typically lagging economic decline by around 3 months, we can expect to see further significant losses in the short to medium terms. This impact on the labour market in terms of unemployment and skills mismatch could be long lasting, and disproportionately affect those in lower skilled jobs, women, young people and those with disabilities.</p> <p>There is evidence that unemployment is detrimental to health and well-being, and that the longer you are out of work the less likely you are to regain employment. Scotland must start planning for recovery now if we are to avoid long term damage to our economy and society, and this means joined up effort between Government, industry and further education and significant investment in training and support.</p> <p>Prior to the impact of coronavirus, and even above the potential damage of Brexit, the number one talking point in the engineering and manufacturing sector has been skills, and the impact of a historical lack of work-based learning and training places. In the last few years, the impact of our increasing age profile in engineering has been felt acutely, with companies citing lost opportunities as demand has outstripped capacity in particular engineering skillsets. The response has however been encouraging, with increasing uptake in Modern Apprentices, and momentum building in the excellent additions of Foundation and Graduate Apprentices. The coronavirus pandemic has underlined how</p>

critical these skills are to the development of a flexible manufacturing sector that is ready to meet the many global priorities at hand.

As we know, the coronavirus not only has been a devastating health crisis but is also rapidly becoming an economic crisis as well. Engineering companies are openly talking about strategies for survival, and unfortunately our history has shown that those strategies often impact training budgets first. A twin edged impact could be that some inevitable company closures could temporarily add skilled labour to the market, masking the underlying aging impact of skills losses, and the concern is if we don't react, we will store up a bigger problem when our economy rebalances in whatever the new normal looks like.

Industry leadership has a part to play in that, and we will certainly take a sharp message to our sector to hold their commitment to work based learning to protect the future of our engineering industry. However, the Scottish Government will particularly be concerned at the impact this economic crisis will have on younger people's employment prospects and we would welcome the opportunity to contribute to the consideration of actions to address this. In particular, any special funding considered for this issue should prioritise work-based learning programmes, with incentives to encourage employers to hold or increase their commitment to these. This approach can benefit our Further Education and Higher Education sectors as well through the three apprenticeship programmes, whilst ensuring that precious spend will deliver the actual positive impact intended. We believe that it is critical to review the outcomes of investments made to address this issue during the financial crisis to enable an honest view on what worked and what did not.

Additional investment in HE and FE should be aligned with the critical skills needs of employers and the future economic vision for Scotland. For example

	<ul style="list-style-type: none"> • Apprenticeships delivered in conjunction with industry addressing key challenges and opportunities including digital, automation, artificial intelligence and the transition to a net zero carbon economy. There would be a focused effort to increase diversity and inclusivity in the workforce. • Industry designed training that will enable workers or those unemployed to transition rapidly from declining occupations to these growth areas. <p>It is also notable that apprenticeships can provide real opportunities for individuals from deprived backgrounds to enter structured work and gain valuable qualifications. Almost a quarter of participants in apprenticeship schemes are from deprived backgrounds according to the Scottish Index of Multiple Deprivation 2020.</p> <p>The pandemic crisis could promote the uptake of new models of learning focused around online and distance learning techniques. These approaches could also be combined with more traditional workplace experience and classroom based learning in apprenticeships.</p>
<p><u>WELLBEING, INCLUSIVE GROWTH AND NET ZERO</u> In your opinion, how can the wellbeing of the people of Scotland flourish and how can a wellbeing economy approach be embedded to bring distinct benefits to Scotland?</p>	<p><u>SKIPPED QUESTION</u></p>
<p><u>GOVERNMENT, POLICY AND DELIVERY</u> In your opinion, how will the crisis change the role and</p>	<p>Scottish Engineering see a key action on that list is for government guidance to manufacturers across the UK to re-align and stay aligned. We understand and agree with the Scottish Government’s focus on public health and have only praise for the leadership which has been consistent and clear in ways that others have not. However, the potential for damage to the manufacturing sector is too great if Scotland earns a tag that it is closed for business whilst the rest of</p>

<p>relationships between the UKG/SG/Las, business and other institutions?</p>	<p>the UK is not, and we would argue that both the public health priority and guidance alignment can be jointly achieved without detriment to each other.</p> <p>Since the start of this crisis, we estimate that 70% of manufacturers have remained open in Scotland, and in our most recent survey we now see over 90% operating at some level. That these operations have been achieved whilst Scotland has seen a decline in Covid-19 cases, and especially the all-important R-number, underlines our belief that few industries are better placed to safely operate in these times due to high average area per person workplaces, and a risk assessment led approach to operating having been embedded for many years.</p> <p>Our expectation is that Covid-19 will ebb and flow before vaccine or treatment options emerge, and so a supportive, coordinated, and matched message to manufacturers from both Scottish and UK Governments is essential to minimise damage.</p>
<p><u>LESSONS/DATA INSIGHTS</u></p> <p>Q. In your opinion, how do we ensure that we learn from the impact of the crisis and respond accordingly?</p>	<p><u>SKIPPED QUESTION</u></p>
<p>Please use this space for any other insights/comments:</p>	<p><u>SKIPPED QUESTION</u></p>
<p>Comments provided in response to this survey will be aggregated to produce broad themes and commentary from</p>	<p>Yes</p>

the business community, which will be shared with the Advisory Group and the Scottish Government.	
Please provide contact details	Paul Sheerin, CEO, Scottish Engineering