[REDACTED]

From:	**[REDACTED]**
Sent:	22 June 2022 16:43
To:	Permanent Secretary
Cc:	DG Economy; Director of Economic Development; **[REDACTED]; [REDACTED]** [REDACTED] Aitken R (Reuben); **[REDACTED]** Rooney M (Maureen); **[REDACTED]**
Subject:	Permanent Secretary - AO Review - Stocktake - Lochaber Smelter
Attachments:	PermSec Stocktake_Lochaber_Briefing v0.5.docx; 220627 - GFG Lochaber - Permanent Secretary Stocktake Session (1).pptx; Permanent Secretary - AO Review - Stocktake - Lochaber Smelter - Business Case Review Paper - 20 June 2022.docx

Permanent Secretary,
Cc DG Economy
Director of Economic Development
Colleagues

In respect of the planned stocktake of Scottish Government's Lochaber smelter intervention, I attach a briefing pack to support discussion at the pre-meet on 27 June:

- A Business Case Review providing the historic background to the Scottish Government's guarantee
- A briefing on the current and future situation in respect of Scottish Government's Lochaber intervention
- A slide pack to support discussion on the current and future situation

I hope this is of use in support of the pre-meet. I would be happy to address any queries in advance.

Kind regards,

[REDACTED]

[REDACTED]| [REDACTED]- Industrial Sectors and Projects
Manufacturing & Industries Division | The Scottish Government
3rd Floor, 5 Atlantic Quay, 150 Broomielaw, Glasgow, G2 8LU
[REDACTED]

Permanent Secretary – AO Review – Stocktake – Lochaber Guarantee – Summary Business Case Review Paper

Business Response and Insights Unit (BRIU), DED 20 June 2022

Context

[REDACTED]

This paper summarises key information from a review of the original submission to Ministers from the AO (DG Economy), and related documents on the financial guarantee provided to the GFG Alliance (Liberty House and SIMEC) in relation to the Lochaber aluminium complex. The purpose of the paper is to set out the strategic rationale for making the financial intervention and subsequent changes or updates that relate to the original case for intervention.

The documentation that has been reviewed is:

a) Rio Tinto's Lochaber Strategic Review: Government Guarantee – AO submission to Ministers seeking approval – 16 November 2016
b) Rio Tinto's Lochaber Strategic Review: Government Guarantee – AO submission to Permanent Secretary seeking PAO approval – 21 November 2016
c) Project Golf II – EY final report – December 2016
d) Lochaber Submission of New Business Plan for Investment – AO Submission – December 2020

Background

In January 2016 Rio Tinto announced a strategic review of the company's operations in Lochaber, comprising:

- the aluminium smelter,
- the hydro-electric power stations located in Fort William and in Kinlochleven,
- extensive estate lands located to east of Fort William (c. 115,000 hectares).

Following this review, Rio Tinto sought bids for the purchase of its assets in Scotland, which raised concern for the operation's future given any potential closure would result in the loss of around 160 direct FTE jobs (**[REDACTED]**) and several hundreds more in the Lochaber area and through the supply chain. The smelter and hydro-electric power stations are located in Fort William. The loss of any manufacturing jobs in this location was therefore considered to have a disproportionately negative effect on the economy of the region.

The sale was offered in two alternative lots: (i) *as a whole* – smelter complex, both hydro stations and estate lands or (ii) a *'power-only'* option which would segregate the power stations from the aluminium operation. **[REDACTED]**. Rio Tinto stated at the time that the smelter would continue operating for the **[REDACTED]** as this was deemed essential to manage the water moving through the reservoirs and hydro power station at Lochaber.

Officials' discussions with Rio Tinto and shortlisted bidders at the time indicated that power-only bids were likely to be more competitive (higher) than bids for the whole operation due to economic factors making it challenging to keep the smelter operational. For example, due to a limited ability to export power to the national grid at the time, the smelter was the main user of the power from the hydro which gave the smelter a stable and low-cost power source. **[REDACTED]**. **[REDACTED]**, a scenario the bidders were well aware of.

These factors led to the conclusion that without Scottish Ministers' intervention, a power-only sale was the most likely outcome of the bidding process; in that event, Rio Tinto would begin a transition process by which the smelter would be wound down as grid capacity for power exports increased.

Scottish Ministers' Intervention

In order to prevent the fragmentation of the Lochaber complex, Scottish Ministers offered its support, to all viable bidders, in order to protect operations in the Fort William area (particularly in relation to the smelter).

Only one of the bids received, that of the GFG Alliance, contained firm plans to operate the smelter over the long-term and develop additional higher value downstream manufacturing. Consequently, in December 2016, Ministers supported the GFG Alliance in its purchase of the Lochaber site comprising an aluminium smelter at Fort William, an adjacent hydro power station and extensive estate lands from Rio Tinto Alcan. The GFG Alliance were already operating in Scotland through the purchase of the steel plants at Motherwell (Dalzell) and Clydebridge in 2016.

Guarantee

The arrangement is captured in the form of a guarantee between Scottish Ministers and Liberty House Group (part of the GFG Alliance) whereby the Scottish Government stands behind the power purchase obligations of the smelter in the event that the business cannot fulfil its obligations to pay for contracted power from the associated hydro power station (owned by sister company Simec) over a 25 year period. This contingent liability required the approval of the Scottish Parliament Finance Committee (which was obtained in November 2016).

The funds required by the GFG Alliance to acquire the aforementioned assets from Rio Tinto (c. £330m) and to invest in downstream production (£70m) were raised against the hydro's revenue streams guaranteed by Scottish Ministers. The GFG Alliance sold the guarantee revenue stream to bond holders via Greensill Capital for**[REDACTED]** Greensill Capital no longer holds the debt which was guaranteed by Scottish Ministers; it was securitised and sold to institutional investors (the 'bondholders').

The guarantee provides for timely payment of fixed amounts of income due quarterly under a power purchase agreement (PPA) between the smelter and Simec Lochaber Hydropower Ltd. In return the Scottish Government is paid a fee quarterly, currently at **[REDACTED]** (larger payments of **[REDACTED]** were due in the early years of the guarantee and reduce over its lifetime as the perceived risk reduces). The guarantee does not require the Scottish Government to buy electricity but to pay the bondholders if Liberty does not pay.

Strategic Rationale

The strategic case in 2016 reflected that, without Scottish Government intervention to support the sale of the whole business, the smelter would have likely begun transition towards closure **[REDACTED]**

The Lochaber complex is considered a key part of Scotland's industrial capability and a major employer in the West Highlands (Annex B). Fort William is the last aluminium smelter in the UK with over 90 years' worth of experience of aluminium-production. At the time of the intervention it was estimated that staff at the smelter accounted for around 20% of Lochaber's manufacturing employment (in FTE terms), making it a critical regional asset as well as a national strategic industrial asset.

The objectives for providing the Lochaber guarantee were to:

- prevent the fragmentation of the Lochaber complex;
- to secure the smelter's long-term future viability and to realise further industrial and employment opportunities on site; and
- preserve the skills and capability necessary to produce aluminium in Scotland.

Specifically, it was envisaged that the guarantee would have the potential to:

- secure around 160 direct jobs;
- stimulate new capital investment in the Lochaber complex **[REDACTED]** and
- fund construction of a new manufacturing plant for automotive parts creating over 200 direct jobs.

Economic Rationale

The economic case identified the following options:

1. **Do nothing:** The do nothing option was that the previous owners (Rio Tinto) accept a power-only sale of the business and continue to run the smelter for a period to wind down its operations. **[REDACTED]**. This was the counterfactual option against which to assess the proposed intervention.

2. **Scottish Ministers provide guarantee**: Scottish Ministers offer support to any bidders looking to purchase the whole business to prevent fragmentation of the Lochaber complex. The provision of the guarantee involved the Scottish Government standing behind the power purchase obligations of the smelter in the event that the business cannot fulfil its obligations to pay for contracted power from the associated hydro power station (owned by sister company Simec) over a 25 year period. No initial outlay by Scottish Ministers was required as this is considered a contingent liability.

The economic case for intervention was based on analysis which showed that provision of the guarantee would:

- provide long-term stable energy for the smelter (via a 25-year contract for renewable power);
- provide revenue certainty to the hydro asset owner;
- reduce the risk of stranded power arising from early closure of the smelter; and
- underpin a strong funding package (ie debt raising) to avoid a power-only solution and enable fresh investment.

Also by standing behind the smelter's payment obligations in this way it was accepted that SG insulated SIMEC from the default risk of the smelter therefore enhancing its capital-raising potential. Furthermore, SG's credit worthiness allowed funding to be raised on more favourable terms than would otherwise be the case.

Predicted economic benefits

Liberty House / SIMEC's plans for Lochaber were initially focused on maintaining the aluminium smelter and building and operating a complementary on-site alloy wheels factory to serve the UK car industry. When fully operational the integrated facility (smelter and new alloy wheels factory) was expected to:

- create an additional **[REDACTED]** FTE jobs on site and a further **[REDACTED]** indirect and induced jobs;

generate additional GVA of **[REDACTED]** and**[REDACTED]**during the two-year construction phase, create **[REDACTED]**direct jobs per annum with an associated GVA of**[REDACTED]**

According to SG's commercial advisor EY's estimates at the time, the plans had the potential over 25 years to generate total additional GVA of**[REDACTED]** in real terms, comprising:

[REDACTED]

Compared with a realistic counterfactual which would see the smelter **[REDACTED]**the plans of Liberty / SIMEC were expected to create additional net GVA of**[REDACTED]**

Revised 2020 business plan (further details in commercial rationale section)

Deloitte's assessment of the revised business plan in 2020 highlighted the following predicted economic benefits:

[REDACTED]Creates**[REDACTED]**new jobs; and**[REDACTED]**Total additional net GVA of**[REDACTED]**

Value for money

Commercial advisors EY considered the benefit to the public sector in supporting the transaction and provided commentary on the assessment of value for money based on Grant Thornton's (Liberty's own external consultants) "Initial feasibility assessment". EY commented across three elements of the transaction:

- the quantity of debt raised;
  [REDACTED]
- the pricing of the finance;
  - **[REDACTED]**.

- the economic output benefit following the intervention and how this compared with the potential exposure for supporting the transaction;
  - EY expected the proposal to generate positive benefits over costs under a range of scenarios.

Updated Wider Economic Benefits – June 2022 (OCEA)

[REDACTED]Annex E presents a more detailed overview on the wider economic context, however information on the level of full-time equivalent (FTE) jobs at the industrial asset at Lochaber can be used to estimate the economic contribution (in terms of the number of jobs) that it currently makes to the local and national economy both directly and indirectly, through supply chain and re-spending of wages effects.

As at June 2022, the workforce (headcount) of the three entities forming the overall industrial asset at Lochaber (the smelter, hydro and estates) stood at **[REDACTED]**. In full-time equivalent (FTE) terms, this was **[REDACTED]** FTE jobs. Analysis undertaken by OCEA using the latest Scottish Government Input-Output model of the economy, estimates that these jobs support around an additional **[REDACTED]**full time equivalent Scottish jobs in the wider economy, this includes supply chain and re-spending of wages effects. GVA impacts **[REDACTED]**

In considering what the net impact of the investment has been, we need to consider the counterfactual. However, we cannot be definite about what would have happened to the number of jobs and GVA supported by the industrial asset at Lochaber had the Scottish Government (SG) not intervened. It is likely that some or all jobs would have been absorbed

into other parts of the economy, so that in the medium to long-term, the impact on employment would not be significant on the Scottish economy as a whole. However, that is not to say that there would have not have been impacts at the local level.

The extent to which jobs could have been absorbed depends upon a number of factors including the level of capacity in the local and national labour market; the extent to which the skills of the workers at Lochaber are transferable to other businesses/sectors in the local and national economy and the associated wage levels; and the extent to which the Lochaber workers are willing to travel for work. These issues are explored further below (with further detail on the local Highland economy, national labour market and aluminium sector provided in Annex E):

- Highland's labour market is very self-contained with 92% of people who work in the local authority area (LAA) also living there. This is a high proportion when compared with most other LAAs in Scotland but is not surprising given the relatively large area covered by the LAA. Information from the business suggests that only**[REDACTED]**workers live in excess of 20 miles of the site. This suggests that workers may not be willing to travel far outwith the immediate area or wider LAA for alternative work. This indicates that, had jobs been lost, employment and spending impacts would have be felt within the immediate local area.

- Compared to the national average, the Highland local authority area (LAA) is characterised by a slightly lower employment rate and earnings (although the unemployment rate is slightly lower than the national average). This suggests that the local area may have had slightly less scope than other areas to absorb any job losses, had the SG not intervened.

- Like most of Scotland, Highland's labour market is dominated by services. Just 5% of employee jobs in Highland are in manufacturing, lower than in Scotland as a whole (7%). Looking at employment by occupation, a slightly higher proportion of jobs in Highland are "process, plant and machine operatives" (7% compared to 5% in Scotland as a whole) and "skilled trades" (11% compared to 9% in Scotland as a whole) - the occupations categories that account for the vast majority of jobs at the Lochaber asset. This suggests that while there may have been limited opportunities within manufacturing in the LAA, similarly skilled alternative work may have been available in the area.

Commercial Rationale

The commercial case for intervention was underpinned by the Market Economy Investor Principle and informed by the subsequent development of a credible business plan by Liberty for investment in downstream manufacturing.

Business plan

The smelter was loss making and as a standalone business was deemed not viable in the medium term. The Lochaber guarantee transaction was underpinned by a business plan which showed that, after £70m+ of investment in an Alloy Wheels Factory (a key undertaking of the 2016 agreement), both the Hydro and Smelter would be profitable.

The original GFG business plan approved by Ministers centred on investment in a new alloy wheels factory to be built alongside the aluminium smelter. This investment was expected to add considerable value to the base aluminium, preserve all existing employment at the smelter, create several hundred additional direct and indirect jobs, and importantly deliver a sustainable/profitable smelter. The substantial economic benefit to Scotland predicted

through additional GVA arising from increased employment and induced spending provided the core rationale for the guarantee and underpinned approval by the Finance Committee.

As a result of the downturn in automotive market following Brexit, GFG abandoned its plans **[REDACTED]**

[REDACTED]

In late 2020, GFG updated their business plan and committed to:

- **[REDACTED]**Construction of an aluminium recycling and billet casting facility **[REDACTED]**

[REDACTED]In endorsing the recommendation to approve the revised business plan, the Accountable Officer for the Lochaber Guarantee, DG Economy, noted ***[REDACTED] [REDACTED]***

<u>MEIP and State Aid</u>

Advisors EY considered whether the project demonstrated an adequate return on investment and whether in similar circumstances, a private shareholder, having regard to the foreseeability of obtaining a return would have invested in the project.

EY noted that Liberty/SIMEC committed to providing **[REDACTED]**into the project and the estimated Internal Rate of Return for both the hydro and smelter was commensurate with the nature of the assets and was in line with market expectations.

In terms of State Aid, EY considered four tests:

1. Whether the borrower is a firm in difficulty
2. The extent that the guarantee can be properly measured
3. The guarantee does not cover more than 80% of the outstanding loan or financial obligation
4. Whether the price paid for the guarantee is market oriented

Based on EY's analysis, they concluded that the overall transaction was based on commercial principles and an appropriate market-oriented fee was being charged by SG for the guarantee.

EY were asked to confirm that the market economy investor principle had been met on a commercial basis and concluded in their Project Golf analysis:

"*In summary, subject to the final legal and security documentation reflecting the points above and providing the protections expected in a commercial transaction, it is our view that the transaction elements are proposed on a commercial basis for the guarantee."*

[REDACTED]

<u>Financial Rationale</u>

The financial case for intervention was considered in depth as part of officials and external advisors' due diligence in 2016, and this concluded that the intervention would be affordable over the period of the investment.

Detailed briefing was provided to the Cabinet Secretary for Finance and the Constitution at the time in which he was appraised of the overall scale of financial risk posed by the guarantee, including SG's reduced ability to offer other guarantees if this were approved.

Scottish Ministers' exposure and recent performance

There has been no investment by SG of public funds into the operation of the Lochaber smelter complex. Instead SG provided a financial guarantee in respect of a power purchase arrangement between the smelter and hydro. The guarantee in respect of payments to bondholders enabled GFG to raise credit to purchase the assets, maintain jobs and commit to future downstream development.

The amounts guaranteed vary between £14 and 32 million per annum over 25 years, with the total day one undiscounted contingent exposure amounting to £586 million. In return SG will receive **[REDACTED]** in fees over the life of the guarantee **[REDACTED] [REDACTED] [REDACTED]** All guarantee fees due to Scottish Ministers are up-to-date.

Notwithstanding the ongoing global financing and other corporate issues faced by the Group, the local business remains operational and profitable and performed better than projected this year with **[REDACTED]**. Further positive operational developments include:

- Employment levels being retained and expanded;
- Significant progress being made on investment planning for the billet plant;
- A new **[REDACTED]** is in place providing a greater and more efficient capacity to export.

Management Rationale

The original Guarantee and Reimbursement Agreement (GRA) that provides the legal basis for the securities package included a series of undertakings in relation to financial monitoring such as the requirement to provide SG with evidence of:

- A Business Plan for the Alloy Wheels Plant;
- Planning consent for the Alloy Wheels Plant;
  [REDACTED]

Combined this was intended to provide for a robust and on-going evaluation of the activities of the two businesses and provide an early warning of any increased risk being faced by SG during the duration of the guarantee.

Current controls in respect of Lochaber relate to:

- The amended Guarantee and Reimbursement Agreement;
- A cycle of quarterly Guarantee Management Meetings (GMM) that provide a forum for update, review and challenge in respect of business performance and risk management;
- Regular engagement with corporate executives and local management;
- A quarterly review of business management and project development by **[REDACTED]**A series of securities over the smelter and hydro assets, estate lands and cross-company parent guarantees.

Shareholder Interest and Governance

In respect of SG's intervention at Lochaber, it differs significantly from other such interventions:

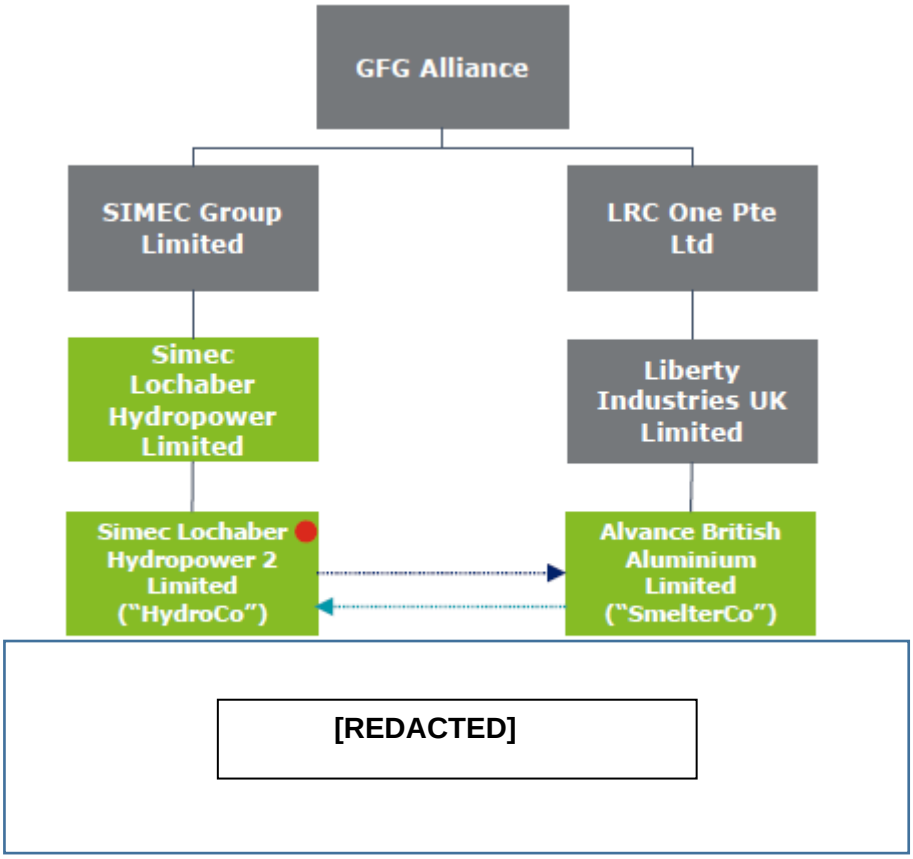
- SG does not own the Lochaber smelter and hydro assets which remain in the ownership of GFG alliance;
- While SG provides a guarantee for PPA payments to bondholders, it has no financial outlay or commitment while PPA payment are met (to date, all PPA payments have been met and there has been no call on SG's guarantee);
- SG has no role in the running of the business **[REDACTED]** and is not represented on any corporate board in respect of the management of the business but maintains close and frequent contact with corporate and local business leads.

Annex A sets out the Group Structure. Annex D sets out the timeline to the intervention.

Exit strategy plans for the public sector

SG's guarantee is irrevocable through to 2041. Given the different nature of the SG intervention in Lochaber when compared to other interventions, the exit plan reflects a move to a positive and stable corporate and local business situation. As such, an exit plan would see the business continue operating through the period of the guarantee, providing revenue to SG, investing in Scotland and divesting SG of any liability. **[REDACTED]**

Annex A – Group Structure



- GFG Alliance (GFG) is a collection of global businesses and investments owned by Sanjeev Gupta and his father, Parduman Gupta.
- GFG is structured into three core divisions:
  - Steel - Liberty Steel (Sanjeev Gupta);
  - Aluminium - ALVANCE Aluminium (Sanjeev Gupta); and
  - Energy - SIMEC Energy (Parduman Gupta)
- Estimated to be over 100 legal entities under Gupta control.
- Prior to the collapse of Greensill Capital, GFG was reported to have global revenues of c.$20bn and employ c. 35,000 people across 30 countries.
- In 2016, GFG purchased HydroCo (Simec Lochaber Hydropower2) and SmelterCo (Alvance British Aluminium), including various land assets in the Fort William area.
- An abridged global structure of the GFG Alliance is provided in the following pages.

An abridged global structure of the Alliance is detailed below. The key UK operations sit in [REDACTED]

[REDACTED]

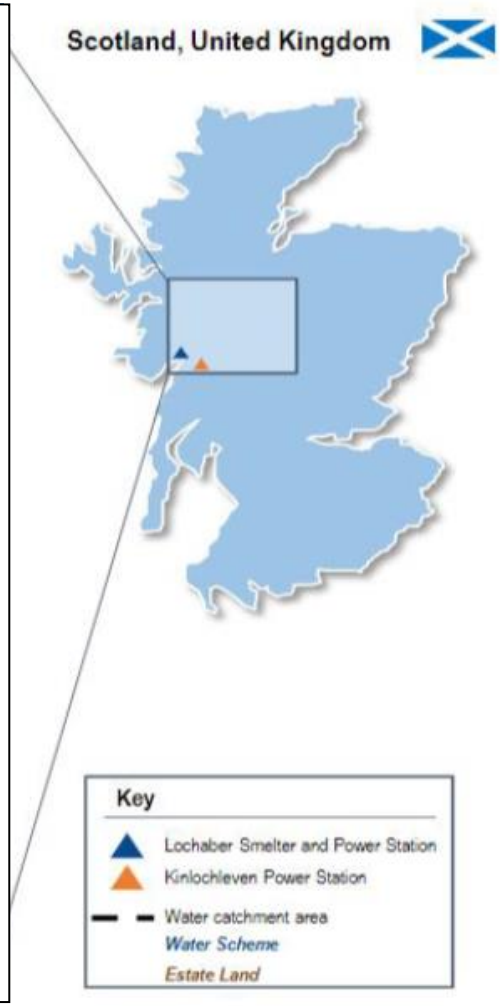
[REDACTED]

The structure below details the entities underneath [REDACTED]

[REDACTED]

Annex B – Map of Lochaber Assets

[REDACTED]



The Jahama Estate Land (part of the GFG Alliance) comprises the [REDACTED]

[REDACTED]

Annex C – Audit Scotland: 2020/21 audit of the Scottish Government Consolidated Accounts

The Auditor General included the following notes in relation to the Lochaber Aluminium Smelter:

- In December 2016, the Scottish Government issued a 25-year financial guarantee contract to SIMEC Lochaber Hydropower Limited. This contract guarantees the power purchase obligations of the Liberty Aluminium Lochaber Limited smelter if the business does not fulfil its obligations to pay for contracted power. The Scottish Government receives an annual fee in return for the guarantee.

- The annual exposure to the Scottish Government is between £14 million and £32 million, over the lifetime of the contract. At the start of the contract in December 2016, the total potential financial exposure to the Scottish Government was £586 million. To reduce the exposure of the contract, the Scottish Government created a security package which includes first line security over the hydro plant, the smelter and land which formed part of the original purchase of the smelter by the GFG Group.

- In March 2021, Greensill Capital (UK) Limited, a major provider of working capital to GFG Alliance, went into administration. This impacts on the Lochaber smelter as it is a subsidiary of Liberty Industries UK Limited, alongside Liberty Steel Limited, under GFG Alliance. The situation is further complicated as the hydro power station that supplies the smelter is owned by GFG Alliance through its other main group of companies, SIMEC.

- With the ongoing uncertainty regarding the financial stability of the GFG Alliance group, the Scottish Government reviewed the level of provision required with regards to their guarantee. The provision in the Consolidated Accounts increased from £37 million in 2019/20 to £161 million as at 31 March 2021. **I have concluded for 2020/21, the Scottish Government's approach to setting the level of provision against the potential exposure through the guarantee is reasonable.**

Annex D – Intervention Timeline

The timeline of key events between Rio Tinto's strategic review of the business and Scottish Ministers' intervention in late 2016:

January 2016	Rio Tinto announced its intention to undertake a review of its assets in Lochaber: • the aluminium smelter, • the hydro-electric power stations located in Fort William and in Kinlochleven, • extensive estate lands located to east of Fort William
April 2016	Rio Tinto issued a sale prospectus seeking bids for the purchase of its assets in Scotland.
January – September 2016	Discussion and consideration of options between Rio Tinto, the Scottish Government and Highlands & Islands Enterprise.
September 2016	SG offers "firm letter of intent to continue to assess" options for a power purchase agreement (PPA) or guarantee of a PPA to enable any bidder seeking a **[REDACTED]** Rio Tinto receive **[REDACTED]** bids with **[REDACTED]** the GFG Alliance containing firm plans to operate the smelter over the long term and develop higher value downstream manufacturing.
October 2016	Rio Tinto announced to its workforce that the Board had agreed to consider a sale of its Lochaber assets and exclusive discussions with a preferred bidder had begun.
November 2016	17th – 22nd: SG internal sign-off (AO, PAO, Ministers) of guarantee 22nd: Finance Committee approval obtained 23rd: Rio Tinto announce the sale to its investors

Annex E – Regional & Labour Market Profile and Analysis of Aluminium Industry Trends and Outlook

Highland Local Authority Profile

Population

Highland's population was 235,430 in 2020, 4.3 per cent of Scotland's population.

Labour Market Jan 2021-Dec 2021

	Highland	Scotland	UK	Rank of 32 LAs
Claimant count rate (April 2022)	2.6%	3.5%	4%	11th lowest
Unemployment rate (16+)	3.4%	3.9%	4.4%	10th lowest

Employment by Occupation (Jan 2021-Dec 2021)

	Highland (Numbers)	Highland (%)	Scotland (%)	Great Britain (%)
Soc 2010 Major Group 1-3	48,600	43.9	48.2	49.7
1 Managers, Directors And Senior Officials	8,500	7.7	8.7	10.5
2 Professional Occupations	23,900	21.5	23.8	23.7
3 Associate Professional & Technical	16,300	14.7	15.5	15.3
Soc 2010 Major Group 4-5	21,400	19.3	18.9	19.0
4 Administrative & Secretarial	8,900	8.0	9.9	10.2
5 Skilled Trades Occupations	12,500	11.3	9.0	8.8
Soc 2010 Major Group 6-7	23,300	21.1	17.7	16.2
6 Caring, Leisure And Other Service Occupations	11,700	10.6	9.3	9.2
7 Sales And Customer Service Occs	11,700	10.5	8.4	6.9
Soc 2010 Major Group 8-9	17,400	15.7	15.2	15.1
8 Process Plant & Machine Operatives	7,300	6.6	5.2	5.5
9 Elementary Occupations	10,100	9.2	9.9	9.6

	Highland (Numbers)	Highland (%)	Scotland (%)	Great Britain (%)
Source: ONS Annual Population Survey. Notes: Numbers and % are for those of 16+. % is a proportion of all persons in employment				

Employee Jobs by Sector (2020)

Human Health And Social Work Activities accounted for 19.2 per cent of total employment in Highland in 2020 (16.6 per cent in Scotland), Wholesale and Retail trade accounted for 15.4 per cent (13.9 per cent in Scotland) while manufacturing accounted for 5 per cent (7 per cent in Scotland).

	Inverclyde (Employee Jobs)	Highland (%)	Scotland (%)	Great Britain (%)
Mining And Quarrying	500	0.5	1.2	0.2
Manufacturing	5,000	4.8	7.2	7.9
Electricity, Gas, Steam And Air Conditioning Supply	1,000	1.0	0.9	0.5
Water Supply; Sewerage, Waste Management And Remediation Activities	2,000	1.9	0.7	0.7
Construction	7,000	6.7	5.1	4.8
Wholesale And Retail Trade; Repair Of Motor Vehicles And Motorcycles	16,000	15.4	13.9	14.9
Transportation And Storage	5,000	4.8	4.5	5.1
Accommodation And Food Service Activities	12,000	11.5	7.2	7.2
Information And Communication	2,500	2.4	3.7	4.5
Financial And Insurance Activities	800	0.8	3.3	3.5
Real Estate Activities	1,500	1.4	1.5	1.8
Professional, Scientific And Technical Activities	6,000	5.8	7.1	8.7

	Inverclyde (Employee Jobs)	Highland (%)	Scotland (%)	Great Britain (%)
Administrative And Support Service Activities	5,000	4.8	8.0	8.8
Public Administration And Defence; Compulsory Social Security	6,000	5.8	6.5	4.6
Education	9,000	8.7	8.4	9.0
Human Health And Social Work Activities	20,000	19.2	16.6	13.6
Arts, Entertainment And Recreation	3,000	2.9	2.3	2.2

Source: ONS Business Register and Employment Survey.

Notes: % is a proportion of total employee jobs excluding farm-based agriculture. Employee jobs excludes self-employed, government-supported trainees and HM Forces. Data excludes farm-based agriculture

Earnings[1]

Median weekly full-time earnings for employees who live in Highland were 1.7 per cent lower than the Scottish average in April 2021 (£611 in Highland compared to £622 in Scotland as a whole).

The percentage of all employees (18+) who work in Highland with hourly pay below the Living Wage, at 14.4 per cent in 2021, was below the figure for Scotland as a whole, at 19.4 per cent.

Qualifications

In 2021, 28.8 per cent of people (16-64) in Highland held a degree level qualification, below the average across Scotland of 36.1 per cent. In 2020, the year most recent data is available for, the proportion of people (16-64) with low or no qualifications at SCQF level 4 or below (SCQF Level 4 refers to qualifications at, or equivalent to, National 4), at 7.1 per cent in Highland, was below the figure for Scotland as a whole, at 9.7 per cent.

GVA

Gross value added (GVA) data is produced for NUTS 3 regions. Highland contains part or all of three NUTS 3 regions. GVA in the region 'Inverness, Nairn, Moray, Badenoch and

[1] The Living Wage, as defined by the Living Wage Foundation, is £9.90 outside London. This is different to the UK Government's National Living Wage of £8.91.

Strathspey' was £5,173 million in 2020, 3.6 per cent of the Scottish total. GVA per head was £25,257, lower than the average across Scotland (£26,752). Secondly, GVA in the region 'Caithness and Sutherland and Ross and Cromarty' was £2,068 million in 2020, 1.4 per cent of the Scottish total. GVA per head was £22,112, also lower than the average across Scotland. Thirdly, GVA in the region 'Lochaber, Skye and Lochalsh, Arran and Cumbrae and Argyll and Bute' was £2,345 million in 2020, 1.6 per cent of the Scottish total. GVA per head was £23,855, also lower than the average across Scotland.

Deprivation

According to the Scottish Index of Multiple Deprivation 2020, 9.6 per cent of Highland's 312 datazones were found in the 20 per cent most deprived datazones in Scotland.

Business performance

In 2020, the business start-up rate, at 37 per 10,000 resident adults in Highland, was below the rate for Scotland as a whole, at 39. In 2019, business expenditure on R&D per head in Highland, at £90, was below the figure for Scotland, at £258.

Small businesses

In 2021, small enterprises accounted for 49 per cent of employment in Highland, compared to 37 per cent in Scotland as a whole.

Commuter Flows

92% of people who work in the Highlands also live in the local authority area, suggesting the area is among the most self-contained labour markets in Scotland. However, the vast geography covered by the local authority area should be taken into account when interpreting these figures.

Local Authority Area (LAA)	Number of People Working in the LAA	% of those working in the LAA that live in the LAA	% of those working in the LAA that live out-with the LAA
Aberdeen City	174,100	66.5%	33.5%
Aberdeenshire	103,800	79.5%	20.5%
Argyll and Bute*	29,400	83.7%	16.3%
City of Edinburgh	366,600	70.5%	29.5%
Dundee City	80,100	71.6%	28.4%
Glasgow City	469,200	57.8%	42.2%
Highland	116,200	92.0%	8.0%
Moray*	40,000	92.5%	7.5%
Perth and Kinross	73,400	81.4%	18.6%

Source: Annual Population Survey (Jan-Dec 2021)

* indicates low sample size

Scotland's Labour Market

- Scotland's unemployment rate stood at 3.2% in the period February – April 2022, down 0.5 percentage points since December 2019 - February 2020 (pre-pandemic) and down 0.6 percentage points over the quarter. This is the joint lowest unemployment rate in the series. Scotland's unemployment rate was below the UK rate of 3.8%.

- The employment rate in Scotland was 75.5%, up 0.2 percentage points since December 2019 - February 2020 (pre-pandemic) and up 1.0 percentage point over the quarter. Scotland's employment rate was slightly below the UK rate of 75.6%.

- Early HMRC estimates indicate that the number of payrolled employees in Scotland in May 2022 was 1.6% (37,000) higher than in February 2020 (pre-pandemic). This compares with the UK where the number of payrolled employees has increased by 2.2% over the same period.

- Early HMRC estimates indicate that median monthly pay for payrolled employees was 11.1% higher compared with February 2020 (pre-pandemic). This is lower than the growth in median monthly pay for the UK over the same period (11.7%).

- The COVID-19 pandemic has led to an unprecedented impact on our society, economy and labour market, while the impact of Brexit has added to pre-existing challenges, exacerbating the issues around labour and skills shortages.

- There are significant workforce recruitment and retention issues affecting a number of sectors and regions of the economy, and the sectors worst affected include Haulage, Construction, Tourism, Hospitality and Food & Drink.

- The latest RBS Report on Jobs shows supply of permanent staff falling at the fastest rate on record in May and temporary staff availability also declining. Recruiters attributed the latest fall to workforce shrinkage (particularly a drop in European workers) and skills shortages.

- The latest RBS Report on Jobs also shows job vacancies for permanent staff increasing for the 16th consecutive month in May with temporary vacancies increasing for the 20th month in a row.

UK Aluminium Industry – Recent Trends and Outlook (source BEIS industry intelligence)

- The UK aluminium sector has seen strong demand from packaging and industrial goods.

- UK aluminium producers supplying the auto & construction supply chain are facing challenges in meeting demand, which has increased due to limited supplies from EU aluminium mills operating at full capacity given reduced extrusion and flat rolled products from China due to EU anti-dumping measures.

- The UK aluminium sector has seen steep consumer price rises as a result of the Ukraine conflict on top of inflation through tightness driven by the Covid bounce back.

- Some UK aluminium companies are reporting cashflow problems due to high costs.

PERMANENT SECRETARY STOCKTAKE – GFG LOCHABER

Headlines

- As a result of SG's intervention, the smelter complex is operating profitably and has resulted in the creation of 40 new jobs, increasing direct employment in the complex to 200 jobs
- No public funds have been invested in the Lochaber businesses while SG has received **[REDACTED]** in guarantee fees since 2016
- SG provides a guarantee of payments to bondholders (financial institutions) in respect of a Power Purchase Agreement (PPA) between the smelter and hydro-scheme
- **[REDACTED]**The Guarantee and Reimbursement Agreement includes a suite of remedies and securities in SG's favour in the event of a default by GFG**[REDACTED]**There has been no call on the guarantee and all fees due to SG and bondholders have been paid

Background

1. In 2016 Rio Tinto announced its intention to sell its Lochaber assets: the aluminium smelter, the hydro-electric power stations located in Fort William and in [1]Kinlochleven and extensive estate lands located to east of Fort William.

2. Scottish Government intervened in order to preserve the last remaining aluminium smelter in the UK, preserve jobs and establish a commitment to significant economic growth in the region.

3. GFG Alliance (GFG) was the **[REDACTED]** to seek to retain both the hydro and smelter assets as operational entities and thereby preserve the capacity for aluminium production. GFG's businesses, Alvance British Aluminium and Simec Lochaber Hydropower Ltd, operate the smelter and hydro scheme respectively.

4. The Lochaber guarantee was signed in December 2016 following Finance Committee approval in November 2016.

5. Under the guarantee, GFG is **[REDACTED]**The investment is focussed on an aluminium recycling and billet plant that will increase jobs and total output.

6. The Scottish Government guarantee provides for timely payment of fixed amounts of income due quarterly under a power purchase agreement (PPA) between at the smelter and the hydro scheme. The guarantee is characterised as follows:
    - The total original exposure (undiscounted) over 25 years was £586 million.
    - The amounts guaranteed vary between £14 and 32 million per annum over 25-years.
    - The net present value of the remaining Purchase Power Agreement revenue stream over the remaining 20 years is c. £284 million.

[1] The Kinlochleven hydro was sold by GFG and no longer forms part of the guarantee or securities

7. The SG Guarantee was granted directly to Greensill Capital (UK) Limited under the Customer Agreement. Greensill no longer holds the debt which was guaranteed by Scottish Ministers as it was securitised and sold to institutional investors (the 'bondholders').

8. The Lochaber guarantee does not require the Scottish Government to buy electricity but to pay the bondholders if GFG does not pay.

   In a scenario where the smelter ceases production of aluminium, Alvance British Aluminium could still continue to take the power contracted and on-sell it via the wholesale market.**[REDACTED]**
   In a scenario where the smelter ceases production of aluminium**[REDACTED]**

Guarantee Fees

9. GFG is due to pay the Scottish Government **[REDACTED]** in guarantee fees over the life of the guarantee with the largest payments due in the early years.

10. Between December 2016 and May 2022, the Scottish Government has received c **[REDACTED]** in guarantee fees from GFG.

11. All guarantee fees due to Scottish Ministers are up-to-date.

Current Situation – Corporate GFG

Refinancing

12. Since the collapse of Greensill Capital in March 2021, GFG has been undertaking a global restructuring and refinancing of the Group. **[REDACTED]**

*SG **[REDACTED]***

13. Since the collapse of Greensill Capital as the main financier to the GFG, SG has taken forward **[REDACTED]**

    In the event of an insolvency situation, Ministers **[REDACTED]**
SG has also considered the **[REDACTED]**
[REDACTED] *– Longstop Date* ***[REDACTED]***

[REDACTED]
[REDACTED]
14. At the Longstop Date**[REDACTED]**.

15. **[REDACTED]**.

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
16. **[REDACTED]**.

Current Situation – Alvance British Aluminium, Fort William

17. Overall, the business is profitable and performed better than projected this year with **[REDACTED]** Employment has been retained and expanded to support the planned development.

    [REDACTED] that will increase the capacity and efficiency of the export of power from the hydro-scheme to the grid. This adds value overall to the Fort William assets and enhances their resilience**[REDACTED]**
18. Local management has progressed plans and contracts for the development phase of the billet plant**[REDACTED]**.

19. The management of the estates**[REDACTED]**business providing greater consistency. A revised estates strategy is planned while discussions are commencing in respect of a significant land transaction to community ownership.

20. The business retains a core position in the local community in addition to the economy; it provides support for ancillary and support businesses as well as a contribution to broader activities including supporting delivery of the education curriculum in conjunction with local schools.

21. SG's intervention has retained the business, the commitment to **[REDACTED] [REDACTED]**, in addition, the cultural and social heritage of the smelter and hydro.

Risks

22. There remain a number of risks associated with both the corporate and local business entities:
    - SG's **[REDACTED] [REDACTED]**
        - **[REDACTED]**Ongoing investigations, SFO and FRC

[REDACTED]

Intervention Management and Control Measures

23. SG's intervention at Lochaber differs significantly from other such interventions:
    - SG does not own the Lochaber smelter and hydro assets which remain in the ownership of GFG Alliance;
    - While SG provides a guarantee for PPA payments to bondholders, it has no financial outlay or commitment **[REDACTED]**to date, all PPA payments have been met and there has been no call on SG's guarantee); **[REDACTED]**SG is not on nor represented on any corporate board in respect of the management of the business but maintains close and frequent contact with corporate and local business leads

24. We have a dedicated team in the Manufacturing & Industries Division that actively monitors SG's exposure, the financial health of the Scottish businesses and the GFG Alliance globally. The SG team is assisted in this work by consultancy input from Deloitte (commercial), **[REDACTED]** and **[REDACTED]**.

25. The usual rhythm of monitoring activity around the Lochaber guarantee is as follows:
    - *Weekly:* Internal meetings within M&I Division and regular engagement with SG external advisors who monitor **[REDACTED]** for the Scottish businesses
    - *Fortnightly:* The SG team has a regular check-in meeting with local senior management of the Lochaber site; Deloitte also meets with GFG Alliance head-office staff to discuss the Group's global financing position (e.g. refinancing discussions)
    - *Monthly:* Regular Ministerial catch-up with Ivan McKee as lead Minister
    - *Quarterly:* Guarantee Management Meeting – this is the main set-piece quarterly monitoring point to review a substantive information pack on operating and financial performance **[REDACTED]**

Future Outlook

On taking ownership of the businesses, GFG was**[REDACTED]** million investment in an alloy wheels plant. However, given a downturn in the automotive market due to Brexit, it abandoned those plans**[REDACTED]**

- **[REDACTED]** included a GFG **[REDACTED]**investment package to secure the smelter complex as a GREENALUMINIUM hub: **[REDACTED]**Construction of an aluminium recycling and billet casting facility

[REDACTED]
[REDACTED]
The business has made significant advancement of its plans for the construction of the billet plant and has **[REDACTED]**
[REDACTED]
[REDACTED]

[REDACTED]

26. **[REDACTED]**.

27. **[REDACTED]**