

PEACE DIVIDEND

Introduction

1. This paper attempts to assess the effects on the economy, and in particular on employment, in Northern Ireland of a permanent cessation of violence. It has three objectives:-

- to provide broad indications of employment changes for Ministerial speeches etc;
- to start contingency planning in DED on means to secure the expected benefits; and
- to consider wider impacts on the system.

The paper recognises that steps taken to secure the benefits (and cope with any adverse effects) could reinforce progress towards political stability.

2. The paper concentrates on likely major employment changes in broad terms and does not attempt to evaluate the many other less tangible benefits. It concludes that a cessation of

violence is likely to result in an increase in employment in the manufacturing sector as a result of higher levels of inward investment and trade; a net increase in employment in the private service sector as a result mainly of an expansion of tourism offset to some extent by a decline caused by reduced expenditure on security; a decrease in employment in the public sector, that is security related employment; and a smaller net increase in employment in the construction industry.

3. It is not possible to forecast the extent of these changes with any precision; the outcomes depend upon the form which any cessation of violence takes, including the speed of subsequent political progress, and the degree of confidence shown by investors, customers and tourists in the permanence of the new situation. With this in mind, this paper considers a number of scenarios based on alternative security and investment outcomes. These are described in the paper but, essentially, the two security scenarios are (i) a pro rata reduction in spending and employment levels to Scottish levels within five years and (ii) a more modest reduction in that period based on some NIO forecasts (see Annex 1). The two investment scenarios are generally based on either (i) achieving ROI levels of investment, trade and tourism within 5 years or (ii) the more modest gains described in the paper.

4. Annex 3 sets out a permutation of the employment gains and losses of these different scenarios within five years. Even on the most optimistic combination, not all of the employment gains could be achieved within five years and so the Annex also looks at longer run scenarios but on the full security impact basis only. It is unthinkable that, more than five years after a permanent cessation of violence, Northern Ireland would still need a significantly higher level of LOPS spending than, say, Scotland.

Manufacturing Employment

5. The current level of manufacturing employment is about 100,000. Increases in manufacturing employment are expected to result from:-
 - (a) higher levels of inward investment;
 - (b) enhanced trade opportunities; and
 - (c) reduced operating costs;
6. Inward Investment. In the five years to 31 March 1993, inward investment to Northern Ireland (both new and expansions of externally owned projects) averaged almost 3,000 job promises per annum with an average cost per job promoted of almost £20,000. While the permanent cessation of

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violence will undoubtedly lead to an increase in the level of inward investment, it is not possible to quantify the likely amount with any precision. Comparisons with the ROI suggest that, after adjusting for differences in the size of the two economies, the level of inward investment in the Republic is around 2½ times that of Northern Ireland. On the other hand a comparison with Scotland and other areas of the UK suggests no increase in inward investment after adjusting for size differences.

7. These two comparisons represent the outer limits of what might be achieved following a permanent cessation of violence. On the one hand, to expect inward investment in Northern Ireland to achieve the ROI levels (even after adjusting for size difference) following a cessation of violence is likely to be optimistic bearing in mind the tax advantages available to inward investors in the ROI. On the other hand, to assume that no increase in inward investment is achievable, especially during a "honeymoon period", is unrealistic and contingency plans need to be drawn up to maximise the gains. Two scenarios have therefore been considered. The first assumes a 50% increase in inward investment leading to an additional 1500 job promotions per annum; the second assumes a doubling of inward investment activity leading to a further 3000 job promotions per annum.
8. An assessment of the impact on manufacturing employment of

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these higher levels of inward investment depends on estimates of the relationship between job promotion and job creation, the rate of build up in employment and job duration. Historical analysis of job creation and duration rates show that each job promoted by IDB has led to around 6 man (or woman) years of employment. This suggests that over time an increase in job promotion of 1500/3000 per annum would lead directly to an increase in the stock of manufacturing jobs of around 9,000/18,000.

9. The speed with which these jobs might be created would depend on the time-lag between promotion and creation. Based on historical data, the 'equilibrium' position of an additional 9,000/18,000 jobs would occur after ten years, around 40% achieved within the five years covered by this exercise. Other unknown factors in these calculations (apart from the terms of any cessation of violence, the political stability which follows and the reactions of investors to a declared permanent cessation of violence already mentioned) are the extent to which it will be possible to capitalise on political goodwill and capture foreign assistance/investment, and the nature of North/South institutions, eg. an all-Ireland inward investment authority and/or a Dublin/Belfast economic corridor.
10. On the basis of recent inward investment ratios, these additional jobs would represent an investment of

approximately £80-160 million per annum leading to additional jobs in construction (see paragraph 30) and, as a result of typical multiplier and linkage effects, a further 1,600-3,200 jobs (split approximately equally between manufacturing and the services sector) within 5 years, increasing ultimately to 4,000-8,000 jobs.

11. It is difficult to assess the likely impact on the ID Budget of the additional inward investment identified above. Assuming a lag of a year between additional job promotions and actual ID expenditure, there are unlikely to be any additional expenditure pressures on IDB within the first year. Thereafter these are likely to build up rapidly to between £25m and £50m per annum depending on which of the two inward investment scenarios outlined above is selected. Once this new flow of inward investment becomes part of the home industry group it is likely to make further demands on IDB expenditure but this situation is not likely to emerge in the short term. On the other hand, following a cessation of violence it is likely that the overall average cost per job of all inward investment in Northern Ireland will eventually fall, which over the longer term may act to offset some of the additional costs. No account has been taken of this potential saving.
12. Leaving aside the unknown factors referred to above, achievement of the extra job promotions assumed above will

require, at the very least, an expansion of IDB's inward investment sales and back-up teams and a revision of their PR/Communication programmes. This is likely to involve immediate additional expenditure of £2m per annum for the first 2-3 years falling to £1m per annum thereafter. To achieve the higher scenario will require a determined effort to capitalise on political goodwill during a honeymoon period and involve far more players than the IDB.

13. Trade. Comparisons with Scotland and the Republic indicate that manufacturing exports (on a per head of population basis) are, respectively, 30% and 40% higher than in Northern Ireland. While differences in propensity to export between different economies can be due to a range of factors it is likely that the violence here has had a dampening effect on export performance relative to our neighbours. A cessation of violence should improve export performance by increasing the attractiveness of Northern Ireland to export orientated inward investors and by removing obstacles to export growth for existing industry - such as the reluctance of potential buyers to visit Northern Ireland and concerns about delivery etc caused by the troubles. Peace would also provide a greater impetus to the development of cross-border trade and increase the scope for import substitution North and South of the border.
14. The effect on employment of an increase in exports is

probably, and to a large extent, already reflected in the total additional employment (13,000-26,000) estimated in the inward investment section above. Any additional employment as a result of greater exporting activity by existing industry, while likely to be of significance, is difficult to estimate with any accuracy and therefore any estimate must be highly speculative. Taking a conservative approach, if indigenous Northern Ireland firms were to increase their external sales by a modest 10% then this would lead to an increase (including linkage and multiplier effects) of around 5,000 jobs.

15. Reduced Operating Costs. Many of these are difficult to quantify and, on their own, are minor but could have a cumulative impact. They are:-

- (i) reduced security costs,
- (ii) fewer delays and disruptions, especially in transport,
- (iii) sharper insurance costs,
- (iv) improved energy networks.

16. No statistics on the additional security costs falling on industry as a result of terrorism are available. However, broad brush figures suggest that 1000/2000 people are engaged directly by manufacturing firms on security duties and it might be expected that half of these would be made redundant

ie 500/1,000. An end to extortion costs will be a further bonus though one which is not easily qualified.

17. Although unquantifiable, it can be assumed that security forces' check points and disruption caused by bombs and bomb scares add to industry's annual operating costs.
18. The insurance companies claim that premiums are higher in NI for reasons other than terrorism. Nevertheless, it might be expected that a cessation in terrorism will lead to a general easing in premiums to industry.
19. The electricity interconnector between NI and ROI has been out of action since 1974 following a terrorist explosion. Its restoration is estimated to cost £1m and will benefit electricity supply industry costs initially by £2/3m each year. Restoration would also open up the prospects for all-Ireland competition between NIE and ESB and access by ESB to mainland electricity (through the Scottish interconnector).

Private Service Sector Employment

20. Changes in private service sector employment are expected to result from:-
 - (a) an increase in employment in tourism; and
 - (b) a reduction in employment in the security industry.

21. Tourism. Tourist figures at the same levels as in ROI, which employs 80,000 in the industry, would imply over 1,000,000 additional visitors and an eventual increase in employment in the industry of over 20,000 (including multiplier effects). This would take (at least) five years to achieve because the infrastructure to accommodate additional visitors, involving investment of £200/275m, would require several years to put in place. The action needed to achieve these outcomes will include co-ordinating on a major investment programme in new accommodation, an upgrading of the existing accommodation base and a significant increase in the international promotion of Northern Ireland as a peaceful holiday destination, most likely as part of an all Ireland package.

22. A scenario is as follows:-

	Capex £m	Grant £m	Visitors 000s	Employees 000s
1993/94 (provisional)			1,260	10
1994/95			1,360	11
1995/96	57	17	1,560	14
1996/97	88	26	1,850	18
1997/98	93	28	2,150	24
1998/99	47	14	2,440	30

Note: Capex based on £15,000 per bed space: need for 3,800, 5,900 and 6,200 extra bed spaces in the last three years of the period; and an average NITB grant rate of 30%.

23. A more modest increase in tourists of 500,000 would yield 10,000 extra jobs (including multiplier effects) and involve expenditure of £70/75m in 1996/98.
24. Security Industry. No statistics are available but broad brush figures suggest that the security industry in NI employs around 10,000 (excluding those identified in para 16 as directly employed by manufacturing firms on security duties). This figure might be expected to fall by, say, 5,000 on a cessation of violence with a further loss of 2,000 due to multiplier and linkage effects. Many of these jobs are part-time and comparatively low paid, so the economic impact may not be severe. These estimates assume that many companies will retain security staff to combat ODC, not least because the costs of such security have been tolerated by balance sheets for many years.

Public Service Sector Employment.

25. Public expenditure per capita in Northern Ireland is higher than in the rest of the UK. Excluding social security and agriculture, identifiable general Government expenditure per head in Northern Ireland in 1991/92 was around 20% higher

than in Scotland, the next highest territorial area. Almost three-quarters of the difference was due to expenditure on law, order and protective services (LOPS) and this section considers that employment only.

26. Per capita expenditure on LOPS in Northern Ireland similar to that in Scotland would involve a reduction in expenditure locally of around two-thirds (ie over £500m). A pro-rata reduction in RUC and Prison Service Staff would lead to a loss of around 12,000 jobs. However, it is likely that a significant proportion of the reduction in security spending would be absorbed not by job losses but by reductions in hours worked and hence the reduction in employment is likely to be around 8,000. Multiplier effects could lead to further loss of around 2,400 jobs mainly in private services. As noted at the beginning of the paper, these job losses, like the job gains, would most likely be phased over a period of time but what that phasing would be is not possible to predict and would depend on events.
27. The NIO have produced alternative, more cautious figures (see Annex 1). These, they have emphasised, are highly speculative and should be treated with caution. A much smaller reduction security expenditure is suggested, at least in the short term (the figures are for the four years up to 1997/98), with a cut of 50% in police overtime, a loss of 1,000 (out of a total of 3,000) in the full-time RUC Reserve

jobs and a loss of all part-time RUC Reserve jobs (around 2,000).

28. The mothballing of a prison (with a loss of say a further 1,000 jobs) is also anticipated. The other main savings are reductions in compensation payments and the police building programme. The latter two are likely to impact mainly on construction jobs.

Construction Industry

29. A cessation of violence could have two impacts:-

- (a) an eventual diminution of work in repairing bomb damage;
- (b) an increase in work arising from an expansion of the tourism industry and a greater confidence in the industrial, commercial and domestic sectors.

30. NIO estimates (Annex 1) suggest annual capital expenditure reductions of £56m by 1997/98. The level of capital expenditure associated with an expected increase in inward investment has been estimated to be in the range of £80m-£160m per annum (see para 10). The additional capital expenditure associated with an expansion of tourism has been estimated for the three years 1995/96 to 1997/98 to be £57m.

£88m and £93m respectively (see para 22). This may be reduced and phased over a longer period if the tourism build-up is less pronounced. Estimates of the net impact on capital expenditure of the impacts referred to at para 28 with associated employment effects for the period 1994/95 to 1998/99 are outlined in Annex 2. They suggest that by 1998/99 there would be a net increase in construction jobs in the range 500 to 3,500. With linkage and multiplier effects these would increase to 700 and 4,300 respectively.

Cumulative Effects

31. Estimates of the likely employment effects of the changes identified in this paper, which might result from peace, are summarised in Annex 3. Over the short run (five years) four scenarios have been identified. These reflect the two security scenarios mentioned above - (a) the full security impact within five years and (b) the more cautious (and probably more realistic) approach outlined by NIO. For each of these two scenarios, two scenarios with respect to tourism, inward investment and exports have been considered. The more optimistic approach assumes a doubling of inward investment accompanied by a significant increase in exports, an expansion of tourism to current ROI levels and a 10% increase in external sales of indigenous manufacturing firms. The alternative, less optimistic, approach assumes growth of 50% for each of these. Overall the net employment effect

ranges from just 1,000 for the full security impact/modest increase in ID/tourism scenario to over 30,000 for the modest fall in security expenditure/large increase in ID/tourism scenario. Two long run scenarios have also been identified. These both reflect the full security impact but incorporate the alternative scenarios for ID/tourism benefits used in the short run. Both show that, compared with their short run equivalents, the positive employment effects increase in the longer term.

32. Previous studies have shown a 3:1 relationship between jobs created and falls in unemployment levels and it is likely that returning migrants (see below) and new entrants to the labour market will take up 60/70% of new employment generated. (NI has a 72% participation level compared with 78.5% in GB). Northern Ireland will therefore continue to have a very high level of unemployed and, particularly, long term unemployed ie unemployed for more than 1 year. Northern Ireland currently has 56,000 long term unemployed, predominantly Catholic males, pro rata, 18,000 more than it should have. Addressing this problem is likely to form a key part of reinforcing a permanent cessation of violence. SSG is considering an initiative in this area and its conclusions are important in ensuring that the stabilising benefits of an improving economic situation are shared by the most disadvantaged areas.

33. Like ROI, NI has, historically, suffered from net outward migration and, while levels of migration have generally reflected the buoyancy or otherwise of the labour market in GB, NI has seen peaks of outward migration at times of peak violence. Net outward migration statistics disguise large inward and outward migration figures. Amongst the outward migration figures are the 4,250 young people from Northern Ireland who enter higher education institutions in GB each year, only 16% of whom return on graduating.
34. A cessation of violence and the economic opportunities that would present, could be expected to result in a reduction in the numbers of outward migrants and an increase in inward migrants, including graduates. Many of these immigrants will have the qualities needed by existing companies, and may indeed possess entrepreneurial skills. While it is not possible to estimate the impact on unemployment levels of net inward migration it is reasonable to suppose that there will also be benefits in terms of the management of companies and levels of new business startups.
35. The major changes in employment patterns envisaged in the scenarios in this paper will require significant expenditure on retraining but no reliable estimate has been possible.

Opportunities

36. Implicit in all of these employment scenarios are potentially very large PE savings. The PE costs of the anticipated expansion of ID and tourism are at most around £80m per annum whereas the savings from a rundown in security are likely, taking the NIO estimate, to be £184m in the short-run rising to around £500m over the longer term.
37. There are, of course, a number of significant uncertainties relating to the PE implications of Peace:
- (a) the quantum and phasing of savings, in particular in the Law and Order programme.
 - (b) the quantum and phasing of direct costs on the Law and Order programme eg redundancy or severance payments.
 - (c) the extent to which Northern Ireland would be able to retain the savings within the Northern Ireland Block for reallocation to other purposes - HMT would argue that the Block in general and the Industrial Development and Employment programme in particular were over-provided; and that the level of Law and Order expenditure has been boosted by special additions to the NI Block.

(d) the PE costs of responding to the consequences of Peace could vary, eg if inward investment became significantly cheaper.

(e) the timing/phasing of expenditure proposals.

38. DFP believes that a powerful combination of political and PE arguments could be deployed in the event of a permanent peace emerging:

(a) HMT would benefit from early and substantial savings in additional Army costs which are borne by the MOD and in security related costs being borne by other GB departments.

(b) the NI Block has "subsidised" the Law and Order programme and, as a consequence, other programmes are under-provided (an extension of the current debate with HMT on Needs Assessment and Year 3). However, DFP's Resource Needs Balance Study suggests it might be difficult to justify additions to the Industry/Trade and Employment programme on relative needs grounds alone.

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- (c) crucially, a Peace settlement would need to be underpinned by economic and social programmes which maximised the prospects for an enduring peace, eg by supporting private sector job creation and by addressing long term unemployment and community differentials.
39. Given the range and significance of the variables, DFP believes it would be unwise for Ministers to quote specific figures on money beyond saying that, if Peace broke out, the scope for reallocation could rise to something well in excess of £100m per year. Any such comment would need to be crafted carefully but, nonetheless, Ministers could convey a sense of confidence that the PE dimension of a Peace Dividend would be very substantial.
40. This paper identifies a range of possible applications including inward investment job creation, tourism infrastructure and employment, an expanded scheme for the long term unemployed etc. Ministers might ask officials to do further work on how various levels of Peace Dividend could be applied, but clearly the pattern of deployment would be affected by the quantum available as well as by how Ministers judged priorities at the material time.

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41. "Peace" would naturally have implications for the Secretary of State's public expenditure priorities, with the emphasis shifting from Defeating Terrorism to key economic and social objectives. Clearly Ministers would wish to review strategic priorities in that eventuality but, prima facie, the Strengthening the Economy and Targetting Social Need priorities would continue to be relevant.
42. Additional opportunities might arise from offers of assistance by the US Government (or other US interests) and the EU following a permanent cessation of violence.

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	1994/95	1995/96	1996/97	1997/98
	£000's	£000's	£000's	£000's
1. RUC overtime is cut y 50%	44,500	46,200	47,400	48,600
FTR is reduced by 1000	35,700	37,100	38,100	39,100
PTR disappears	5,700	5,900	6,100	6,300
2. No new terrorist related Criminal Damage	10,000	35,000	45,000	47,000
No new terrorist related Criminal Injuries	-	2,000	6,000	6,100
EP claims cease	1,500	2,000	2,000	2,000
One Prison is mothballed within 3 years	-	-	20,000	21,000
HIFSL shrinks	2,500	2,600	2,700	2,800
KPPS is abolished	3,900	4,100	4,200	4,300
Police building programme refocussed	6,100	6,400	6,600	6,800
TOTAL	109,900	141,300	178,100	184,000

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ANNEX 2

EMPLOYMENT EFFECTS OF CHANGES IN CAPITAL EXPENDITURE

	1994/95 (£m)	1995/96 (£m)	1996/97 (£m)	1997/98 (£m)	1998/99 (£m)
REDUCTIONS					
POLICE BUILDING PROGRAMME	- 6	- 6	- 7	- 7	- 7
CRIMINAL DAMAGE AND EP CLAIMS	- 11	-37	-47	-49	-49
INCREASES					
IDB ¹	-	40-80	80-160	80-160	80-160
TOURISM ²	-	0-57	29-88	44-93	0-47
NET CHANGE	- 17	-3 to 94	55 to 194	68 to 197	24 to 151
JOB GAINS/LOSSES	-340	-60 to 1880	1100 to 3880	1360 to 3940	480 to 3020

¹ Assume ^S inward investment promotion in range 1500 to 3000 per annum.

² Assumes extra tourist jobs in range 10,000 to 20,000