National Audit Office

REPORT BY THE
COMPTROLLER AND
AUDITOR GENERAL

HC 214
SESSION 2009–2010

30 MARCH 2010

Regenerating the English Regions: Regional Development Agencies' support to physical regeneration projects

Summary

1 Government support for physical regeneration can help to promote economic growth and to reverse economic, social and physical decline in areas where market forces will not do this alone. Regional Development Agencies (RDAs) are expected to help target and deliver regeneration effectively in their regions. The Agencies are sponsored by the Department for Business, Innovation and Skills (The Department). The eight RDAs outside London, which this report covers, have together spent approximately £5 billion on physical regeneration projects since 1999.

2 Physical regeneration is one of five tasks undertaken by the RDAs, alongside: promoting business efficiency, investment and competitiveness; promoting employment; enhancing development and application of skills; and contributing to sustainable development.

3 This report examines how well the RDAs support physical regeneration projects and, in particular, how well: priorities are determined; funds are targeted; projects are appraised for value for money; outcomes are evaluated; and lessons are learned. The report covers the eight Regional Development Agencies outside London. (In London, the London Development Agency is accountable to the Mayor of London and audited by the Audit Commission).

Key findings

On agreeing priorities and targeting investment

4 **Prioritising is challenging given the many conflicting pressures and objectives with which the RDAs are tasked.** RDAs are tasked with economic development within their regions, but must support a number of initiatives that have a spatial element, are primarily addressed at tackling deprivation, and which are funded by the Department for Communities and Local Government. These objectives may not always be readily compatible when deciding on potential investments.

5 **RDAs do not have direct influence over all central government funding in a region, making an integrated approach to maximising value for money more challenging.** For example, the North West region received £72 billion of public sector funding between 2006 and 2009 for economic development and regeneration. Of this, £45 billion falls explicitly within the scope of the Regional Economic Strategy (a document prepared by each RDA setting out the policies, aims and objectives for their respective regional economies over the next ten to 15 years), including the budgets of the RDA, the Learning and Skills Councils, Higher and Further Education, neighbourhood renewal, rural, transport and economy-related social protection budgets.

However, more than one third (£27 billion) of the funding is only partially within the remit of the Regional Economic Strategy, including spending on housing, environment protection, school and pre-school education, arts, and sport.

6 **The RDAs must work with a large number of local bodies and partnerships to plan investment.** In the case of the North East, the RDA needs to align the plans of 12 Local Authorities, four sub-regional partnerships, and three economic or urban regeneration companies that together spend several billions of pounds each year. Public agencies and private companies to whom we spoke most often identified the benefits of RDA involvement in physical regeneration as being: the additional capacity and expertise they brought; and their ability to bring together and broker agreement between other regional, sub-regional and local agencies.

7 **For every pound of RDA spending, an estimated additional £2.80 is secured from other bodies of which £1.51 is from the private sector.** While some of this spending may have occurred without the RDAs' involvement, their engagement can ensure that regionally important projects proceed with more speed and confidence than they otherwise might. The added value of the RDAs' strategic role and support to partners in delivering physical regeneration projects is an important benefit to the regions, but it is difficult to measure.

On the impact of physical regeneration

8 **Before 2009, RDAs reported to Parliament on the number of gross jobs they had created. The number of net additional jobs created by RDAs provides a more accurate reflection of their impact on the regional economy.** RDAs reported that between 2002 and 2007 from all activities they had helped to create or protect 413,000 gross jobs. Departmental guidance requires RDAs to report those jobs "directly attributable" to the contribution made by the RDA to the project, regardless of whether the jobs were additional or net to the regional economy. Attributing jobs that would have happened anyway or which have transferred from elsewhere within the region to the activity of the RDAs does not provide an accurate reflection of their impact on regional growth. An independent evaluation of RDA expenditure suggested the RDAs had helped to create 375,000 gross jobs from 2002 to 2007, but that only 178,000 jobs were additional. On this basis the public sector cost of each of the net jobs created so far would be £60,000. This will, of course, be sensitive to the final number of jobs generated and to future costs.

9 **RDAs are now expected to contribute to a Gross Value Added outcome measure, rather than report on progress against particular target outputs such as jobs created.** Many RDAs were slow to evaluate the impact of their work on Regional Gross Value Added. RDAs had to implement a three-year programme of work to ensure that they had evaluated on a consistent basis the impact of all their interventions by the end of 2008. By December 2007, RDAs had only evaluated 40 per cent of the projects, although some RDAs such as the East Midlands had done more. The Department appointed external consultants to provide additional capacity, so that by December 2008 nearly 70 per cent of the projects had been evaluated on a consistent basis.

10 Using the measure of jobs created by RDAs to estimate generated Gross Value Added, there is evidence that physical regeneration projects have helped to generate growth. Up until 2008, physical regeneration projects subject to independent evaluation were estimated to have generated Gross Value Added of £3.30 for every £1 spent. Many of these projects will not realise their full benefits for many years, and independent evaluation suggests a potential return over their full lives of £8 for every pound spent. Evaluation also shows that RDA intervention involving more direct support to business represents a better return both in the short term (£7.30 per pound spent) and long-term (£11.60 per pound spent). Physical regeneration projects generate other social, economic and environmental benefits that are more difficult to measure, such as building investor confidence and tackling squalor and deprivation.

On supporting the projects with the greatest returns

11 While independent evaluation shows that, overall, physical regeneration projects have added to regional growth, there is a considerable range in the success of individual projects both within individual agencies and between types of intervention. The RDAs are unable to demonstrate that they have consistently chosen the right projects to maximise economic growth and value for money because of:

- weaknesses in the quality of project appraisals, including over-optimism about the potential benefits of projects, a lack of clarity about the appropriateness of public sector intervention, and deficiencies in technical and financial analyses;
- the failure of most agencies to use robust and consistent internal evaluation of past projects to develop benchmarks against which to measure the value for money of particular proposals brought forward for support; and
- the skewing of RDA expenditure to the last few months of the year, which creates risks to adequate oversight and control.

Prioritising regeneration activities during the current economic difficulties

12 During the current economic difficulties, approximately 15 per cent of physical regeneration projects involving the private sector have stalled or slowed because developers have been unable to obtain finance or because of uncertainty over future yields. For many projects, developers have sought a reduction in quality or an increase in density, and the RDAs are providing additional public funding. The pattern of reduced demand has not, however, been universal. For example, there has been an increase in demand for start-up premises in the East of England from those people recently made redundant and wishing to start their own businesses.

13 RDAs face a challenge in flexing their plans to respond to the current economic difficulties without losing the capacity to deliver the potential longer-term benefits of physical regeneration for their economies. RDAs have reviewed their corporate plans in the light of the current economic difficulties, and also in response to a reduction of £300 million in their funding allocation for 2010-11 in response to changed government spending priorities.

14 RDAs are concentrating their funding on projects that they consider have the greatest chance of generating jobs in the short term, and have brought forward for start in 2009-10 some £100 million of projects previously planned for 2010-11. The RDAs told us that their current capital allocations provide for a limited number of new, large-scale physical regeneration schemes, but that they will mostly be concentrating on re-profiling and managing those projects that have already been approved. We will be reporting later this year on how effectively each of the RDAs has reprioritised in response to the current economic difficulties and budgetary pressures.

Conclusion on value for money

15 An independent estimation of regional economic wealth generated as a result of jobs created by the RDAs' support to physical regeneration shows benefits of £3.30 per £1 of actual costs incurred. On this basis, it is reasonable to conclude that the RDAs' activities have been beneficial overall.

16 However, we are unable to conclude that the regional wealth benefits actually generated were as much as they could and should have been, and are therefore value for money. Weaknesses which, in many cases, undermined the RDAs' ability to make decisions and set priorities to maximise regional economic wealth do not support such a positive conclusion. These weaknesses included poor project economic analysis and appraisal, pervasive optimism bias, and weak evaluation. In particular, most RDAs were unaware, until 2009, of the types of projects which yielded the best and most enduring benefits.

Recommendations

17 To provide additional assurance on value for money, the RDAs need to: further improve their forecasting; develop appropriate benchmarks to inform future decisions and make these decisions on the basis of appropriate comparisons of correctly assessed costs and benefits; and use evaluation to learn lessons and help identify the type and spread of projects that contribute most to their objective of increasing regional economic growth.

Regional Development Agencies should:

a wherever possible adopt an approach so that projects and programmes with the highest benefits are identified collectively by the region, and partners are then commissioned to deliver them;

b build the technical capacity and expertise required to improve the financial and economic analysis of their appraisals;

c make sure appraisals include adequate risk and sensitivity analysis;

d consistently apply factors to counter optimism bias to all appraisals of benefits following Treasury guidance;

e smooth expenditure throughout the year to reduce the risks associated with year-end expenditure; and

f use evaluation consistently to provide benchmarks against which to judge the likely benefits of future projects and help guide decision making about the projects to support.

The Department should:

g require Regional Development Agencies to ensure in any future reporting to Parliament on job creation that they include information on jobs that are additional; and

h require Regional Development Agencies to report on how they have ensured their interventions are designed to maximise regional growth, demonstrated through robust evaluation and appraisal processes.