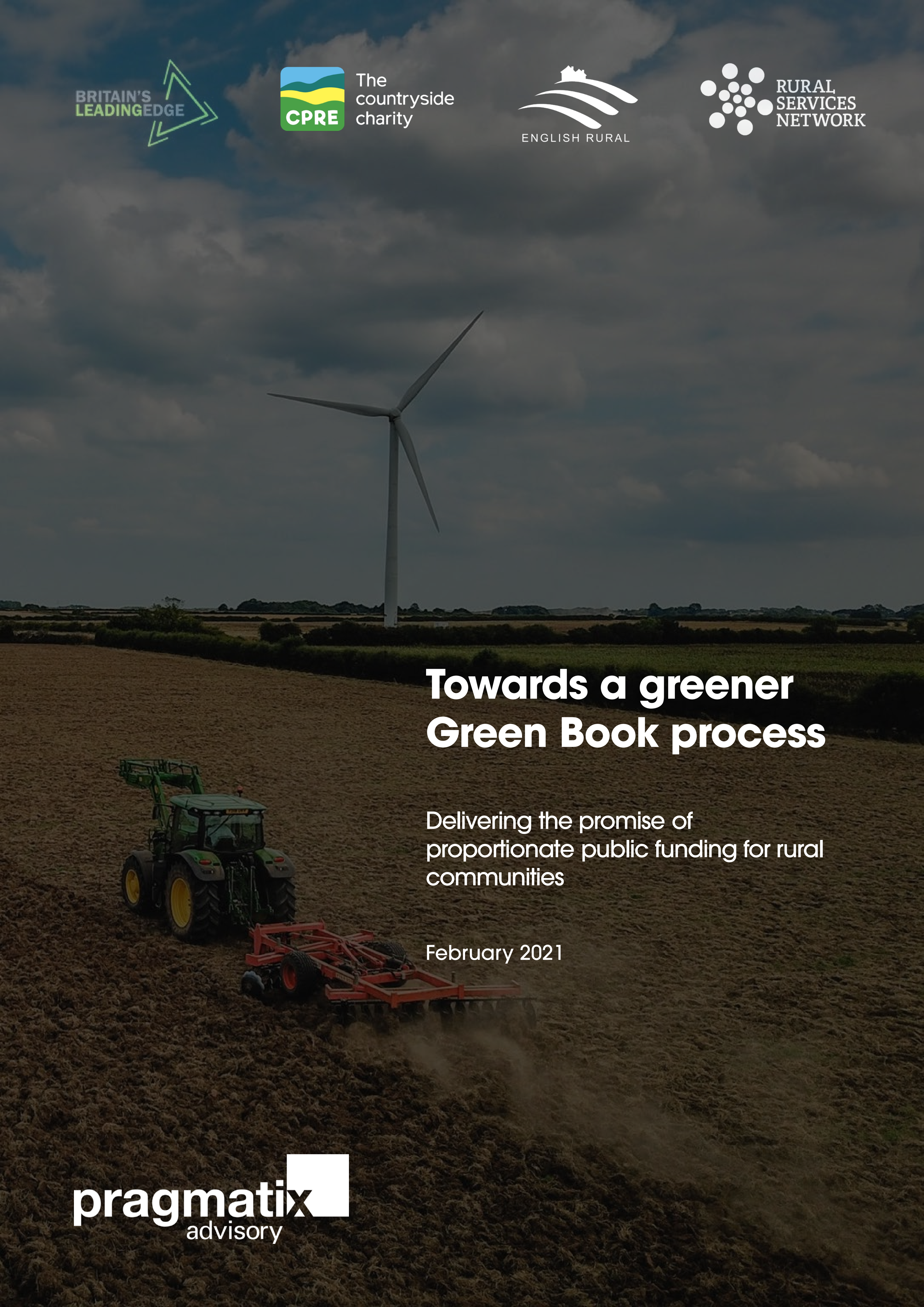

BRITAIN'S LEADINGEDGE

CPRE The countryside charity

ENGLISH RURAL

RURAL SERVICES NETWORK

# Towards a greener Green Book process

## Delivering the promise of proportionate public funding for rural communities

February 2021

pragmatix advisory

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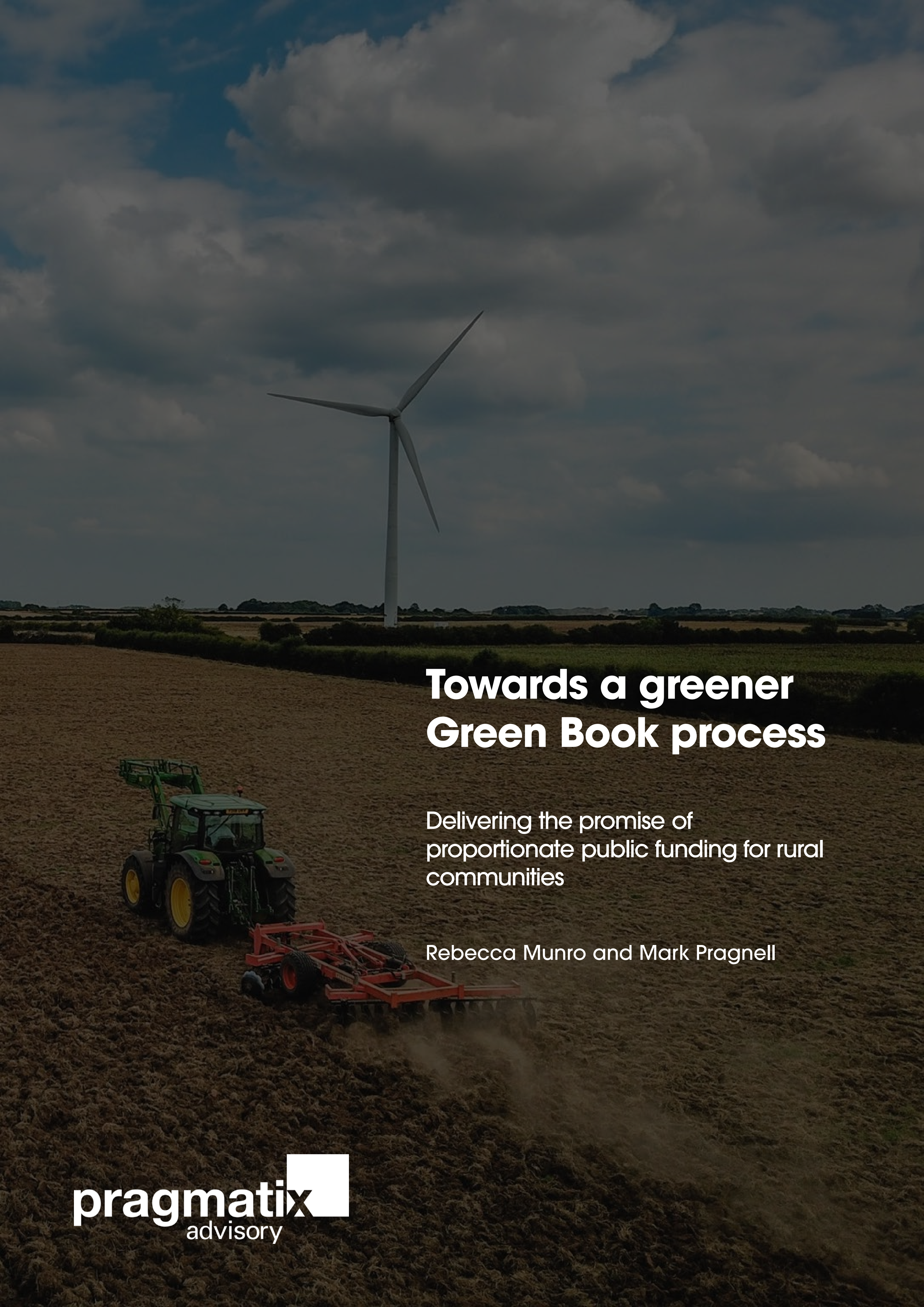

# Towards a greener Green Book process

Delivering the promise of proportionate public funding for rural communities

Rebecca Munro and Mark Pragnell

pragmatix advisory

# Level up

**The rural challenge**

Rural areas face a triple whammy

## Higher costs

(rural areas lack economies of scale)
Average number of pupils per school

**424**
in a major conurbation

**138**
in a village

## Lower funding

Local authority capital expenditure per person

**£434**
in urban and less rural areas

**£301**
in rural areas without a major city

## Greater need

Median full-time wage per hour

**£15.91**
in mainly urban English local authorities

**£13.69**
in mainly rural English local authorities

The way in which government allocates spending spatially is placing rural communities at a disadvantage - and failing to unlock the opportunities they can offer to the nation as part of a digitised, decarbonised and decentralised modern economy.

## The Green Book review is a missed opportunity

The Treasury's recent review of the Green Book was an opportunity to deliver a mechanism for proportionate funding as part of the commitment to levelling up and closing gaps between regions. But it has not been seized.

**3.5%**

The Green Book should recommend 'sparsity-normalised costs' in funding appraisals to redress the rural imbalance. Other options to improve the government funding process include a review of the overall discount rate used, and to consider the potential for a new lower rural-specific rate.

**£4bn**
Levelling Up Fund

## Reducing rural disadvantage

The government's 'levelling up agenda' should encourage tangible progress in reducing rural disadvantage. Success must be measured in a way that reflects the inherent differences between country and city lives, and will require more granular public spending data at the local level.

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Sources: Department for Education; Ministry of Housing, Communities & Local Government; Office for National Statistics; Pragmatix Advisory

# Contents

# Introduction and summary

**Pragmatix Advisory has been commissioned by Rural Services Network in association with Britain's Leading Edge, CPRE and English Rural to undertake a review of HM Treasury's *Green Book* appraisal guidance, with a view to formulating recommendations to make its application fit for purpose in rural areas and meet the government's levelling up agenda.**

## The rural challenge

The challenge of levelling up disadvantaged communities is one which is as much, if not more, about differences within regions as between regions. The gaps between rural and urban can be more acute than those between north and south.

There has been increased focus in recent years on the economic gap between northern England and the southern regions, including the extent to which there are differences in levels of government expenditure. Since the 2019 general election, the so-called 'Red Wall' constituencies which flipped from Labour to Conservative have provided both political and journalistic loci for the 'levelling up agenda'. But, the 'north-south divide' trope fails to capture the complexities of England's socio-economic disparities and inequalities.

Rural areas face the triple whammy of higher costs, lower funding and greater need. Lack of economies of scale mean delivery of services in rural areas will likely cost more than in urban locations. But despite this, public sector spending per head is higher in regions with a greater share of the population living in urban areas. This urban-centric bias has a particularly acute impact on the rural regions with no major cities that make up Britain's Leading Edge.

The way in which government allocates spending spatially is placing rural communities at a disadvantage - and failing to unlock the opportunities they can offer to the nation as part of a digitised, decarbonised and decentralised modern economy.

## The not-so-Green Book

The Treasury's recent review of the *Green Book* appraisal and evaluation rules was an opportunity to address the treatment of sparsely populated areas and deliver a mechanism for proportionate funding as part of the commitment to levelling up and closing gaps between regions. But it has not been seized.

There is little wrong with *Green Book* itself – even before the revisions announced alongside the Chancellor's November 2020 spending review. It is a well-developed and thoroughly tested manual for the application of cost benefit analysis to public sector decision-making. But the revised guidance still does not address the rural challenge, and specific mechanisms need to be incorporated if the potential for rural disadvantage is to be reduced.

While there are no perfect solutions to achieve the desired outcome of ensuring that *Green Book* assessments support levelling up, there are a range of practical options that could be adopted to take account of the higher costs and weaker growth prospects in the areas most in need of levelling up. Options for improvement to the *Green Book* include:

(i) Use of 'sparsity-normalised costs' in appraisals to ensure rural communities have equal chance of securing funds for projects with like-for-like outcomes as their urban counterparts; and

(ii) Develop the new *Transformation, Systems and Dynamic Change* appendix to recognise the potential impact of transformational schemes in rural areas and to give meaningful guidance on how to appraise them.

In addition, the differential needs of rural communities could be at least partly accommodated by review and revision of the *Green Book* discount rate. Regular review of the discount rate value would permit adjustment to better reflect expected growth in per capita consumption over time; use of a new lower rural-specific discount rate could account for weaker growth prospects, partly the legacy of poor public funding, in rural communities.

Nonetheless, the greater challenge to proportionate treatment of rural communities comes from how the appraisal guidance is implemented by government departments. The Treasury is clear that the *Green Book* must sit within a broader and strategic policy development and decision-making framework, and this point is reinforced in the 2020 review. But, in practice, the outcomes for rural areas demonstrate that this is not happening effectively – and the recent revisions to the guidance do not to change this.

New guidance, either within the *Green Book* or as a separate document, is needed on how different policy interventions should be considered together to form an effective and efficient portfolio that meets the needs of varied locations and communities.

## Levelling up

The imperative now is to ensure that the criteria for the success of the government's 'levelling up agenda' are specified in a way that makes visible and encourages progress in reducing rural disadvantage. Levelling up must relate to revenue spending core allocations and not just to capital spend if its objectives are to be met.

To measure and drive progress on levelling up, spend data on public services and growth enhancing Infrastructure must be published consistently at a sufficiently granular level. Publishing data at the level of the nine English regions hides disparities within those regions and makes It Impossible to track whether growth enhancing spending Is reaching the places that most need levelling up.

**Any framework developed to allocate national funds for levelling up should assess local needs at a minimum for each of England's 101 'Level 3' areas in the *Nomenclature of Territorial Units for Statistics*, which is broadly unitary authorities, small counties and groups of contiguous lower tier authorities in larger counties. This should be specified In Green Book guidance on place-based analysis.**

It remains unclear on what metrics the success of levelling up will be measured, but whatever are chosen need to properly reflect the nature of rural disadvantage and account for the inherent differences between country and city lives.

With the allocation of the Levelling Up Fund set to be the outcome of a bidding war between different local areas, rural authorities are disadvantaged by their lack of resource and capacity to complete their applications to Whitehall. Expert resources need to be made available for rural authorities to produce businesses cases and advocate for their priorities.

December 2020

# The rural challenge

**The challenge of levelling up disadvantaged communities is one which is as much, if not more, about differences within regions as between regions. The gaps between rural and urban can be more acute than those between north and south.**

There has been increased focus in recent years on the economic gap between northern England and the southern regions, including the extent to which there are differences in levels of government expenditure. Since the 2019 general election, the so-called 'Red Wall' constituencies which flipped from Labour to Conservative have provided both political and journalistic loci for the 'levelling up agenda'. But, the 'north-south divide' trope fails to capture the complexities of England's socio-economic disparities and inequalities.

This section highlights the urban-rural divide. Rural areas receive government funds at a lower per capita rate than elsewhere. But, it costs more to deliver the same service or same capital project in a rural area than it does elsewhere. And, rural areas have some of the greatest need for government expenditure.

## 2.1 Rural funding

Although official statistics do not permit a comprehensive evaluation, the available evidence points clearly to rural areas receiving government funds at a lower per capita rate than elsewhere.

The Office for National Statistics calculate and publish estimates of the amount of government spend in each English region – for those expenditure items for which a geographical location is identifiable and meaningful.[1] The latest data, for 2018/19, demonstrate an unambiguous relationship: government per capita spend in a region increases with the proportion of residents living in urban communities (defined as population living in settlements of 10,000 or more). This favouring of urban over rural is visible across not only investment but also all categories of current activity (although for some categories of spend the relationship is not statistically significant). (See Exhibit 2-1.)

[1] HM Treasury, *Country and regional analysis'*, Office for National Statistics, 2019

**Exhibit 2-1: Regionally identifiable government expenditure for the English regions, £ thousands per capita, 2018-19**

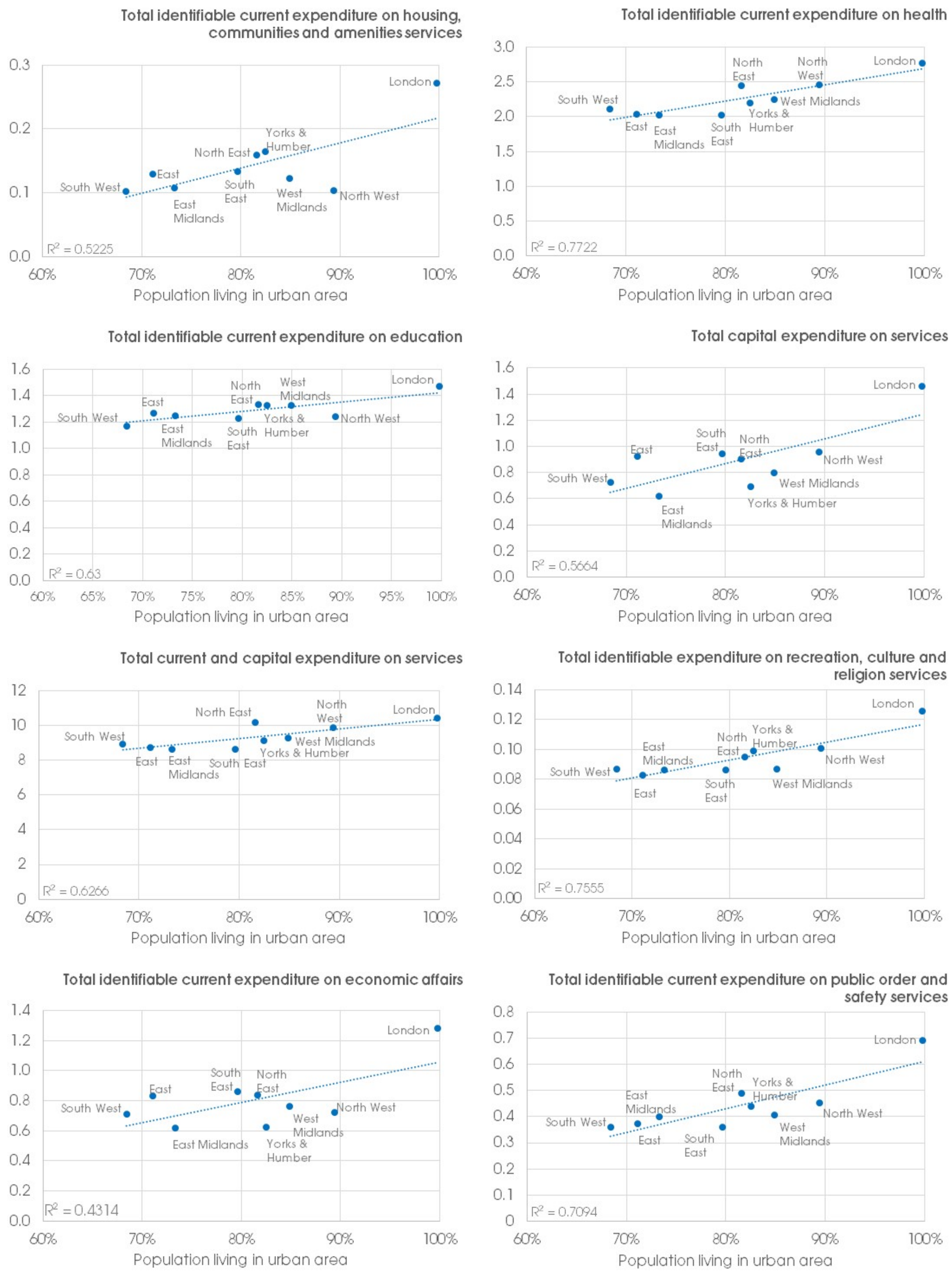
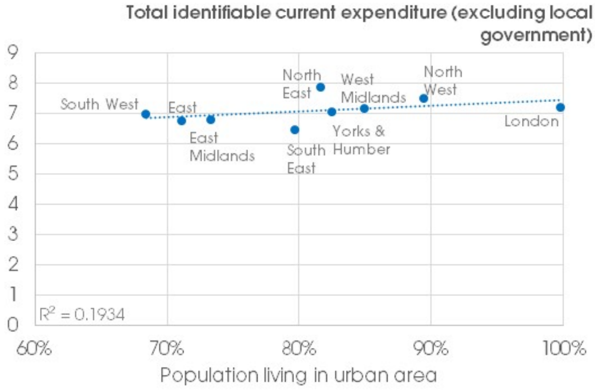
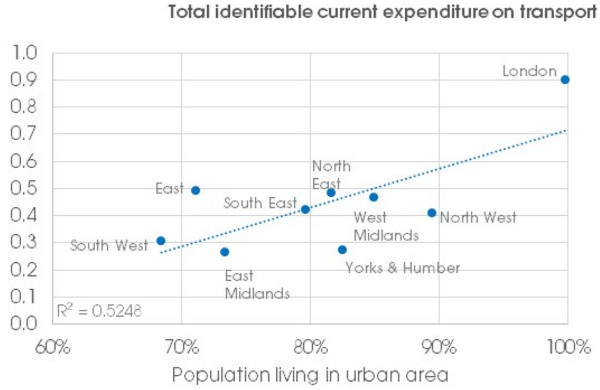


**Exhibit 2-1 (continued): Regionally identifiable government expenditure for the English regions, £ thousands per capita, 2018-19**




Source: Office for National Statistics; HM Treasury

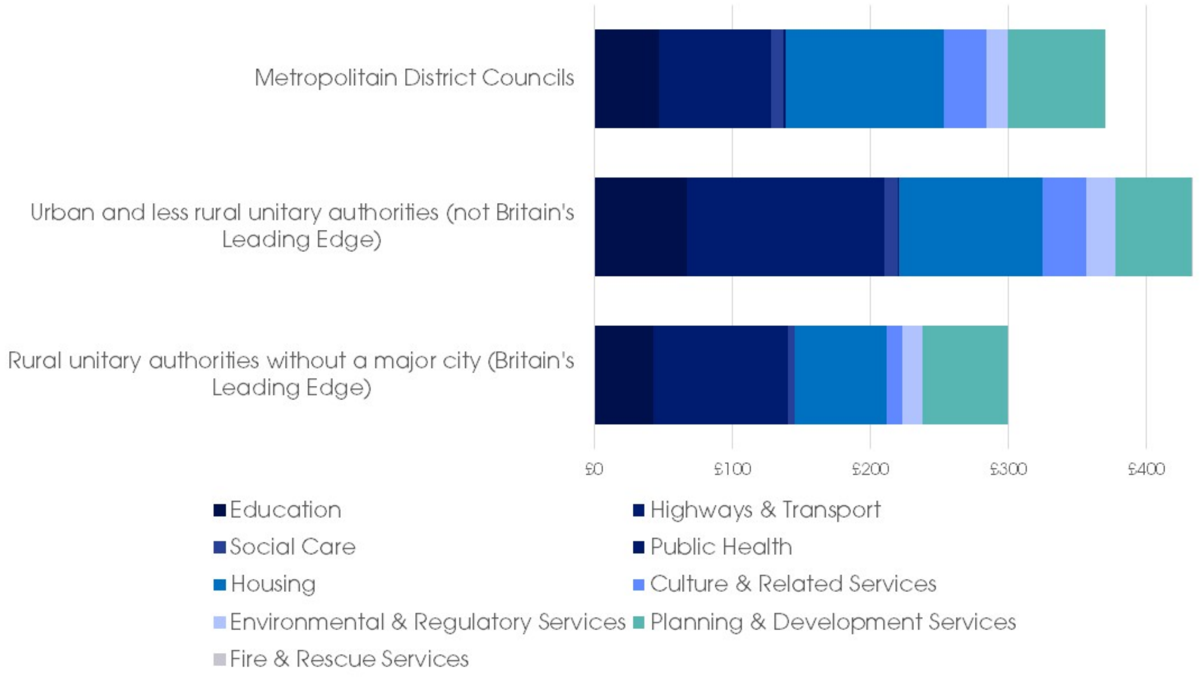
The Office for National Statistics does not publish consistent and comprehensive government expenditure data for geographies smaller than regions. As all regions have urban settlements, and most have rural communities too albeit in varying proportions, regional comparison can only go so far in helping understand or quantify any differences between sparsely and densely populated areas.

Local authority data show lower per capita spend in rural areas.[2] For example, capital expenditure by the most sparsely populated unitary authorities, who are members of Britain's Leading Edge, was an average of £301 per head in 2019-20 compared to £434 in their equivalents elsewhere. (See Exhibit 2-2.) The complexity of council finances and responsibilities and the paucity of available data make it difficult to compare like-with-like beyond the unitary authorities; detailed research in this area is overdue.

Evidence also points to national programmes funded and administered by central government delivering fewer outputs in rural areas than urban. For example, the rate at which new social and affordable homes were built in the most rural areas was 116 homes per 100,000 of population over 2016-17 to 2018-19 compared to 158 elsewhere. (See Exhibit 2-3.)

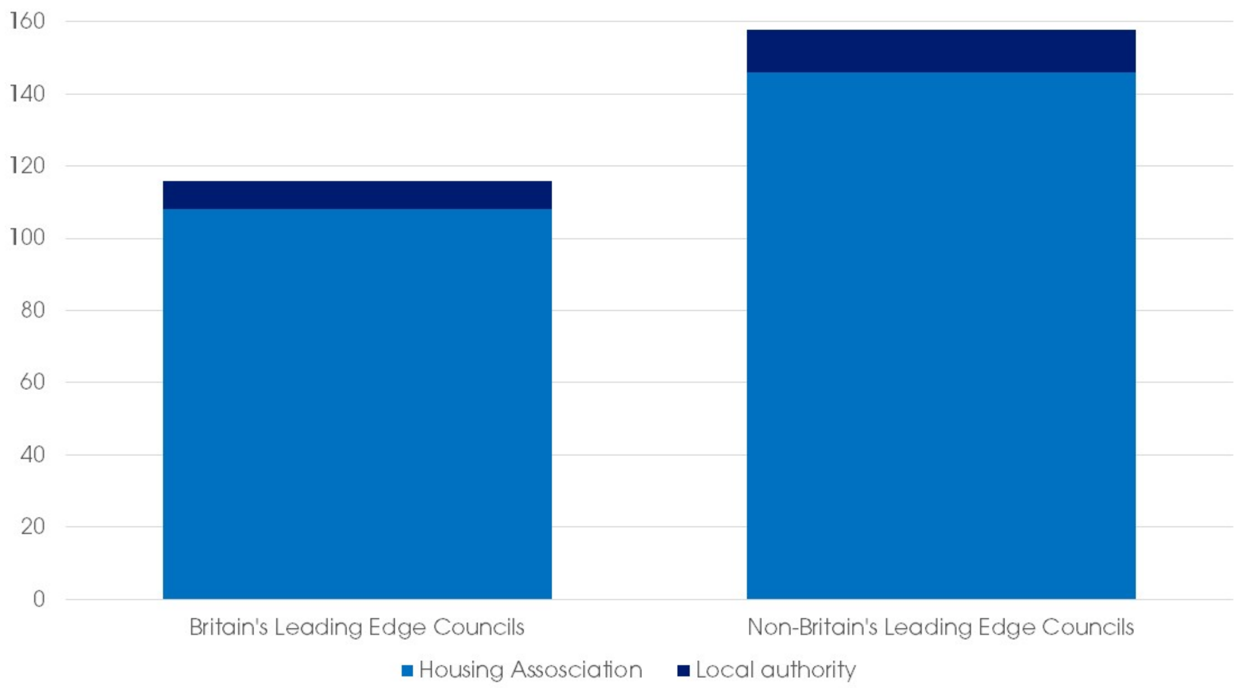
[2] Ministry of Housing, Communities and Local Government, *Local authority capital expenditure, receipts and financing*, Office for National Statistics, 2020

**Exhibit 2-2: Upper tier local authority capital expenditure, England 2019-20**




Source: Ministry of Housing, Communities & Local Government; Pragmatix Advisory

**Exhibit 2-3: New build dwelling completions for social or affordable tenure, England, 2016-17 to 2018-19**




Source: Ministry of Housing, Communities & Local Government

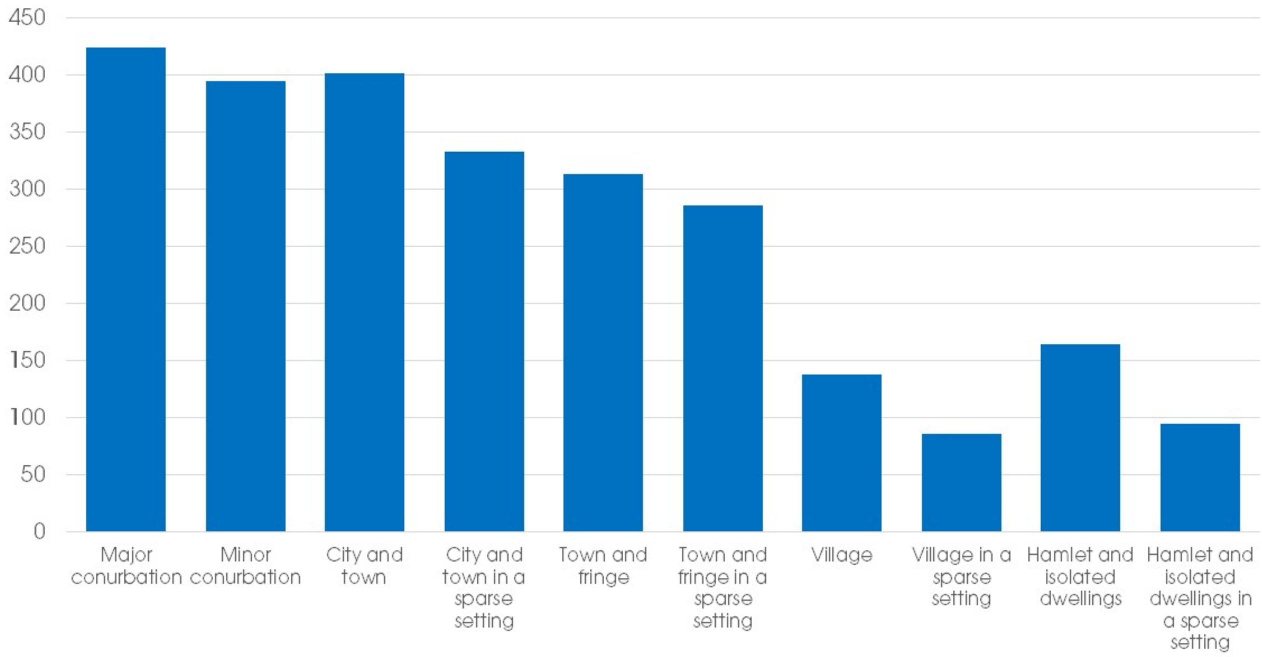
## 2.2 Rural costs

In general, it costs more to deliver the same service or same capital project in a rural area than it does elsewhere.

The unit cost of business activity in a given area will decrease as the population density of that location increases. Although some of the benefits of urban locations will be partly offset by congestion costs and higher wages, towns and cities provide for economies of scale and scope that rural areas cannot match. Moreover, rural areas are often most affected by a seasonal influx of visitors driving up demand for services, so analyses per resident population can understate the additional costs from hospitality.

The differences in economies of scale are evident, for example, in the average number of pupils serviced by one school. (See Exhibit 2-4.) Rural areas have more fixed costs per pupil due to lower numbers in each establishment.

**Exhibit 2-4: Average number of pupils per school by urban and rural classification, England, 2019/20**



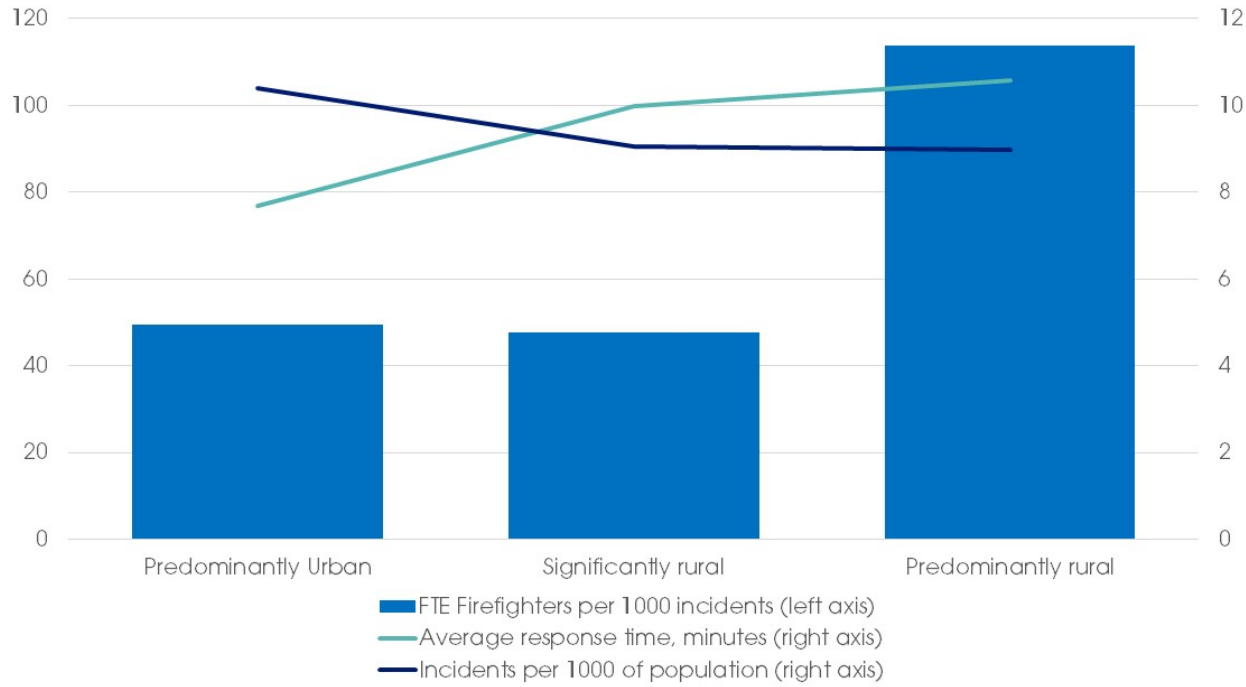

Source: Department for Education

Government should expect to spend more to achieve the same outcomes in a rural location than in an urban one.

Fire and rescue are another good example of the issue. Although urban areas place a higher demand on this emergency service, with 10.4 incidents per 1,000 of population, which is sixteen per cent more than 'predominantly rural' locations, the most sparsely populated areas require double the number of full-time equivalent firefighters per incident to provide cover. Indeed, even with this level of staffing, rural response times remain longer than urban ones. (See Exhibit 2-5.)

There is surprisingly little usable research into rural-urban differences in costs. Back in 2014, the then Department for Communities and Local Government and the Department for Environment, Food and Rural Affairs published a study that tried to identify local authority services where there was statistically significant evidence that unit costs of provision were influenced (positively or negatively) by density of population.[3] However, the analysis was unable to differentiate between the amount spent on services and the quality of resulting output.

**Exhibit 2-5: Metrics of fire service performance: full-time equivalent fire fighters per 1,000 incidents, 2020; number of incidents per 1,000 people, year ending June 2020; and average response times, 2018/19**




Source: UK Government Home Office

Even the most recent government announcements reinforce rural disadvantage. The *National Infrastructure Strategy* acknowledges the important role of connectivity in levelling up rural areas, but despite government plans, gaps will remain. The *Shared Rural Network* deal to provide 4G phone coverage to 95 per cent of the United Kingdom by 2025 will still leave five per cent of the country (almost certainly all rural) without faster mobile speeds at a time when cities will likely be serviced by 5G. The rollout of Gigabit-capable broadband has the aim of reaching 85 per cent of premises by 2025 – though previously the government target was 100 per cent of premises by the same deadline. Likewise, while the Spending Review and the National Infrastructure Strategy both refer to a £5 billion allocation for gigabit-capable broadband the detail shows just an allocation of £1.2 billion over the four years to 2024/25. With reliable and speedy internet now an essential service for many as demonstrated in the pandemic, the lack of provision in some rural areas will further widen the gap in productivity.

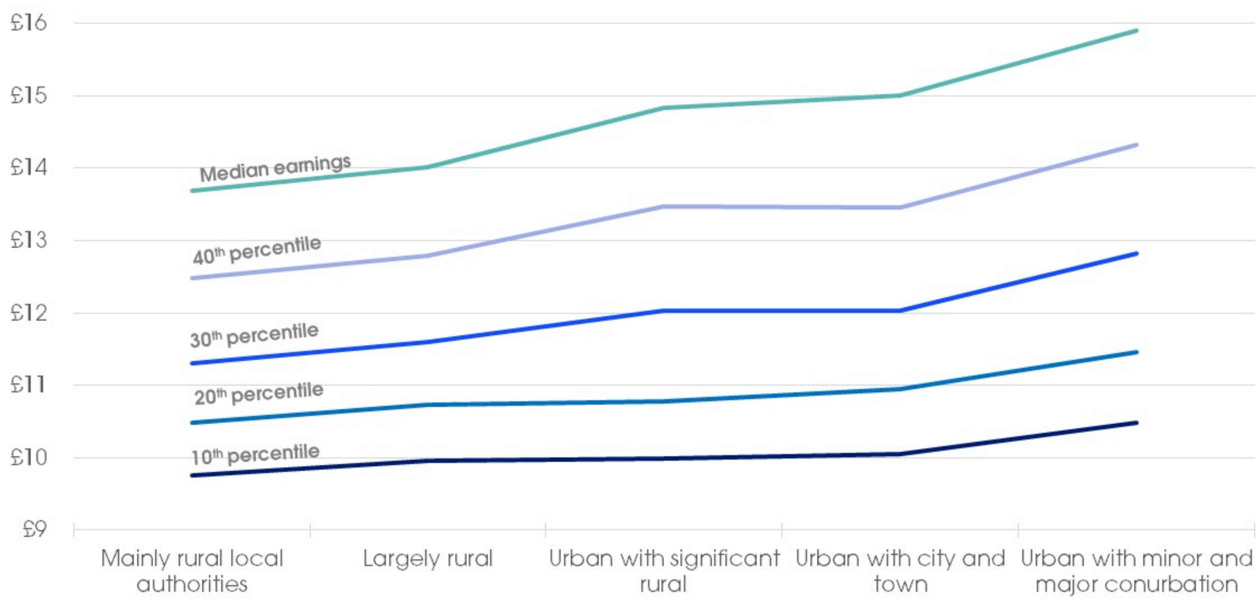
[3], LG Futures, *Research into Drivers of Service Costs in Rural Areas,* Department for Communities and Local Government and Department for Environment, Food and Rural Affairs, 2014

## 2.3 Rural need

Rural areas have some of the greatest need for government expenditure.

There are economic challenges, with relatively low levels of prosperity among those who live and work in rural communities. Wages and salaries paid by employers in these areas are, on average, lower than those paid in towns, cities and conurbations. This difference can be seen throughout the income distribution – including among those on the lowest incomes. (See Exhibit 2-6.)

**Exhibit 2-6: Hourly wage of full-time workers in England by rural and urban classification of local authority**

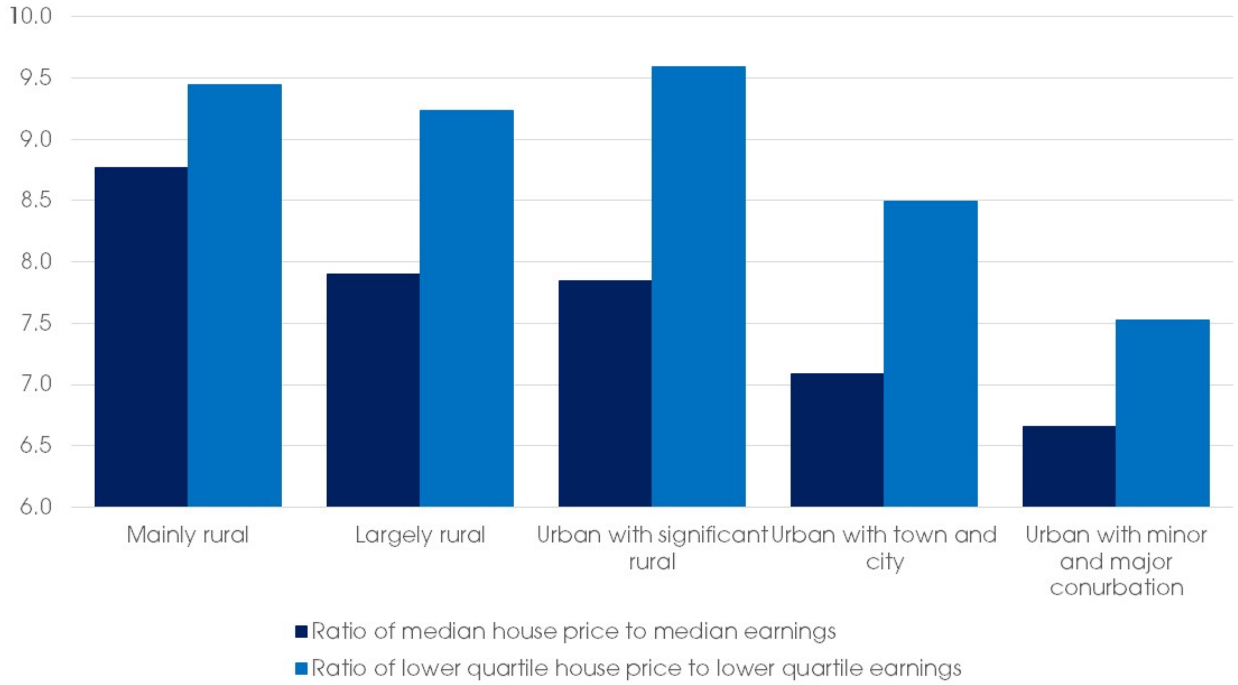



Source: Office for National Statistics

Lower wages mean market-rate house prices and private rental costs are unaffordable for many local people. Excluding London, the ratio of house prices to local wages is higher in rural or significantly rural areas of England than in urban locations. This is the case both for the 'typical' household and those on lower incomes. (See Exhibit 2-7.)

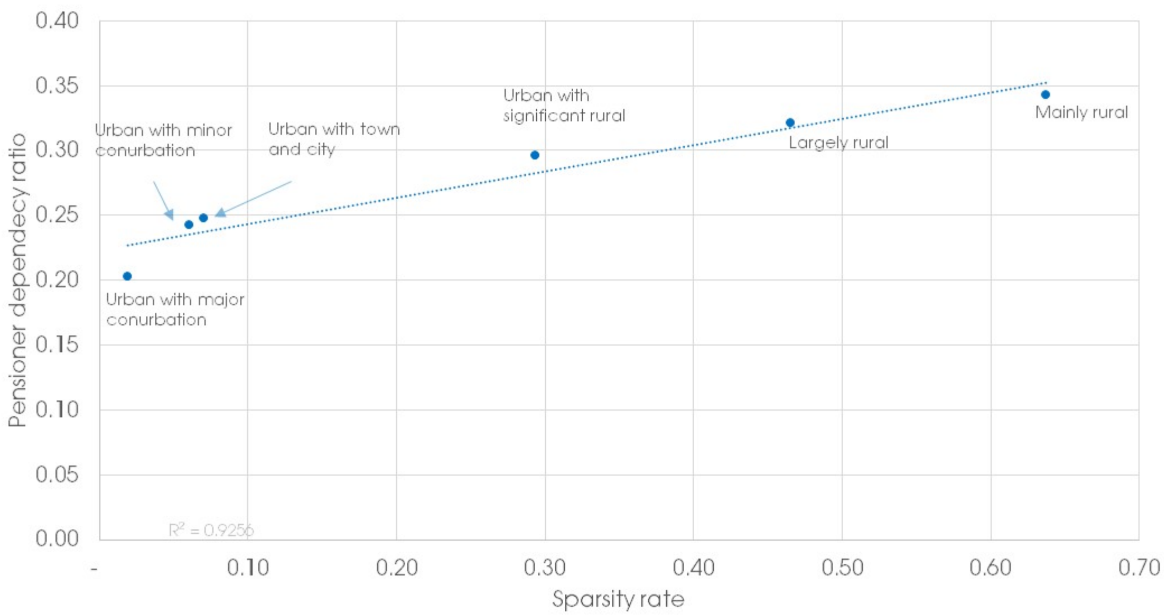
And, demographic challenges, like the aging population, are felt more acutely in rural areas – with more sparsely populated areas having higher proportions of the population at retirement age. (See Exhibit 2-8.)

**Exhibit 2-7: England (excluding London) house price to earnings ratio**




Source: Office for National Statistics

**Exhibit 2-8: The relationship between pensioner dependency and sparsity ratio, English local authorities grouped by urban and rural classification**



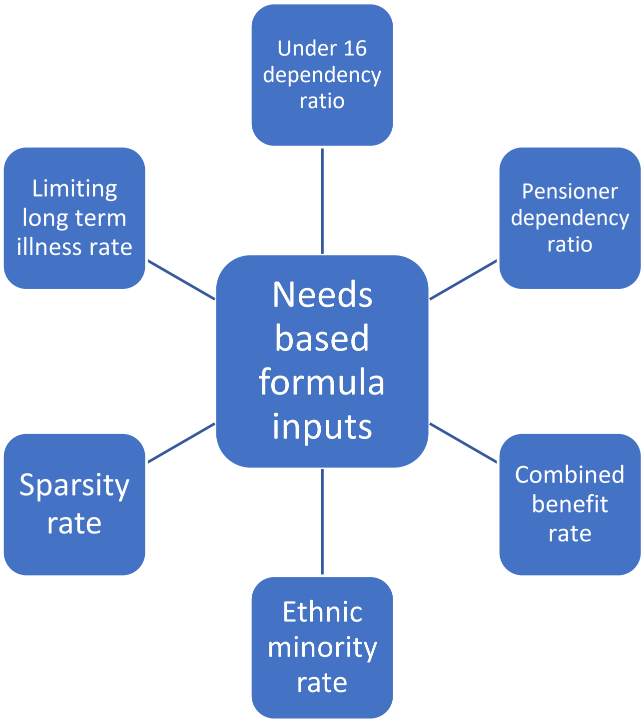

Note: sparsity rate is the number of people living outside settlements of 10,000 or more as a percentage of the whole population, and the pensioner dependency ratio is the resident population over statutory retirement age divided by the working age population.
Source: Office for National Statistics, 2011 Census

The higher costs and greater need in rural areas are explicitly acknowledged in the United Kingdom government's funding settlement for the devolved administration in Wales.

The Holtham Commission recognised that per capita government spending should be fifteen per cent greater in the principality than in England.[4] This assessed greater need was partly based on the larger proportion of the Welsh population living in sparsely inhabited areas. The equation used to calculate the spending premium was based on six factors – which included a 'sparsity rate', calculated as the number of people living outside settlements of 10,000 or more as a percentage of the whole population. (See Exhibit 2-9.)

The coronavirus pandemic has reinforced rural disadvantage – given these areas' share of jobs in badly-impacted sectors, such as tourism, retail and hospitality. (See Exhibit 2-10.)

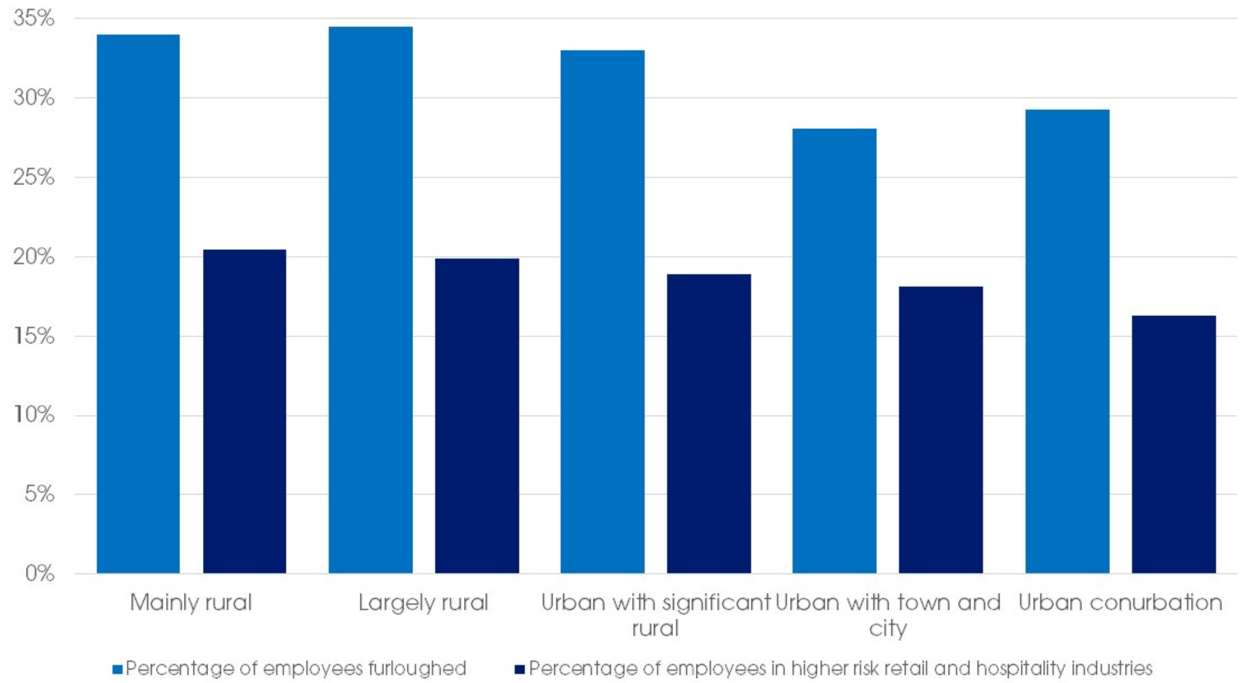
**Exhibit 2-9: Welsh funding settlement need-based formula inputs**




Source: Independent Commission on Funding & Finance for Wales

[4], G Holtham, *Fairness and accountability: a new funding settlement for Wales*, Y Comisiwn Annibynnol ar Ariannu a Chyllid I Gymru (Independent Commission on Funding & Finance for Wales), 2010, p.137

**Exhibit 2-10: Percentage of employees furloughed and employees in higher risk hospitality industries by rural or urban classification, England, August 2020**




Source: Office for National Statistics

# The not-so-Green Book

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The government’s recent review of the *Green Book* appraisal and evaluation rules is welcome. The Treasury has taken on board some of the criticisms levied at the previous incarnation of the guidance, and the 2020 edition has been updated to reflect this. But the inherent inequalities of public spending run deeper than a single guidance document. Levelling up must relate to revenue spending core allocations and not just to capital spend if its objectives are to be met.**

This section outlines the Treasury appraisal guidance, including recent revisions announced alongside the Chancellor’s November 2020 spending review, and its application to rural communities. It explains what still needs to be done to the *Green Book* and to the wider appraisal process to better ensure proportionate application to sparsely populated areas.

**Exhibit 3-1: HM Treasury guidance books**


Source: HM Treasury

## 3.1 The Green Book and the appraisal process

The *Green Book* is the key text in a rainbow-coloured library of Treasury documents issued as guidance to assist in the appraisal of potential public investment in projects, policies and programmes.

Focused on appraisal, the *Green Book* provides guidance on a key part of the 'ROAMEF' cycle of government policy development: rationale, objectives, appraisal, monitoring, evaluation and feedback.[5] Its guidance has broad applicability in the public sector, and applies to:

- policy and programme development
- all proposals concerning public spending
- legislative or regulatory proposals
- sale or use of existing government assets – including financial assets
- appraisal of a portfolio of programmes and projects
- structural changes in government organisations
- taxation and benefit proposals
- significant public procurement proposals
- major projects
- changes to the use of existing public assets and resources

The Treasury is clear that appraisal is multidimensional, and its 'five case model' demands that policies are developed taking full and proper account of strategic, economic, commercial, financial and managerial considerations. The importance of a rounded and strategic business case has been reinforced in the 2020 Treasury review of the *Green Book*. (See Exhibit 3-2.)

But the *Green Book* itself is concerned mostly with explaining how to assess the economic case through 'social cost benefit analysis'. It is used alongside supporting papers on managing public money, evaluation methods, management of risk and multi-criteria-analysis amongst others. These books in combination assist officials in their appraisal of proposals as well as providing guidance on monitoring and evaluation. It provides valuable direction not only to those in Whitehall but also for those submitting proposals to government.

The material included in the *Green Book* and its supplements are not a hard and fast rulebook for decision making. Their guidance describes best practice methods that encourage consistent appraisal across government departments, with the aim that the resulting evaluation is transparent, objective and evidence based.

The core document sets out:

- how to generate options and undertake long-list appraisal
- how to undertake detailed social cost benefit analysis of a short-list of options
- the approach to valuation of costs and benefits

[5] HM Treasury, *The Green Book*, 2018, p.9

- how to present appraisal results
- the approach to monitoring and evaluation

**Exhibit 3-2 : The Treasury's 'five case model' of evaluation**

| | |
|---|---|
| **Strategic dimension** | **What is the case for change, including the rationale for intervention?** What is the current situation? What is to be done? What outcomes are expected? How do these fit with wider government policies and objectives? |
| **Economic dimension** | **What is the net value to society (the social value) of the intervention compared to continuing with Business As Usual?** What are the risks and their costs, and how are they best managed? Which option reflects the optimal net value to society? |
| **Commercial dimension** | **Can a realistic and credible commercial deal be struck?** Who will manage which risks? |
| **Financial dimension** | **What is the impact of the proposal on the public sector budget in terms of the total cost of both capital and revenue?** |
| **Management dimension** | **Are there realistic and robust delivery plans**? How can the proposal be delivered? |

Source: HM Treasury

The social cost benefit analysis, which is central to the *Green Book*, provides a consistent and coherent basis for evaluating the net benefit to society of a proposed policy, and for comparing alternative interventions. It is a 'marginal analysis' technique that is generally most appropriate where the broader environment (e.g. the price of goods and services in the economy) can be assumed to be unchanged by the intervention being evaluated. That said, it provides for:

- Identification and valuation of a wide range of costs and benefits for both the public sector and wider society
- Qualitative assessment and incorporation of non-monetisable costs and benefits
- Discounting of future values so that costs and benefits in different years can be compared consistently
- Assessment of the risks to the achievement of the costs and benefits, and consideration of the potential for 'optimism bias' in the preparation of the cost estimates

Two of these aspects warrant highlighting here.

First, the discounting regime specified in the *Green Book* is not based on financial metrics or the cost of capital as might be expected in a business's appraisal, but on a 'social time preference rate'. Set at 3.5 per cent per annum in real terms (albeit with some exceptions) since 2003, it has two components:

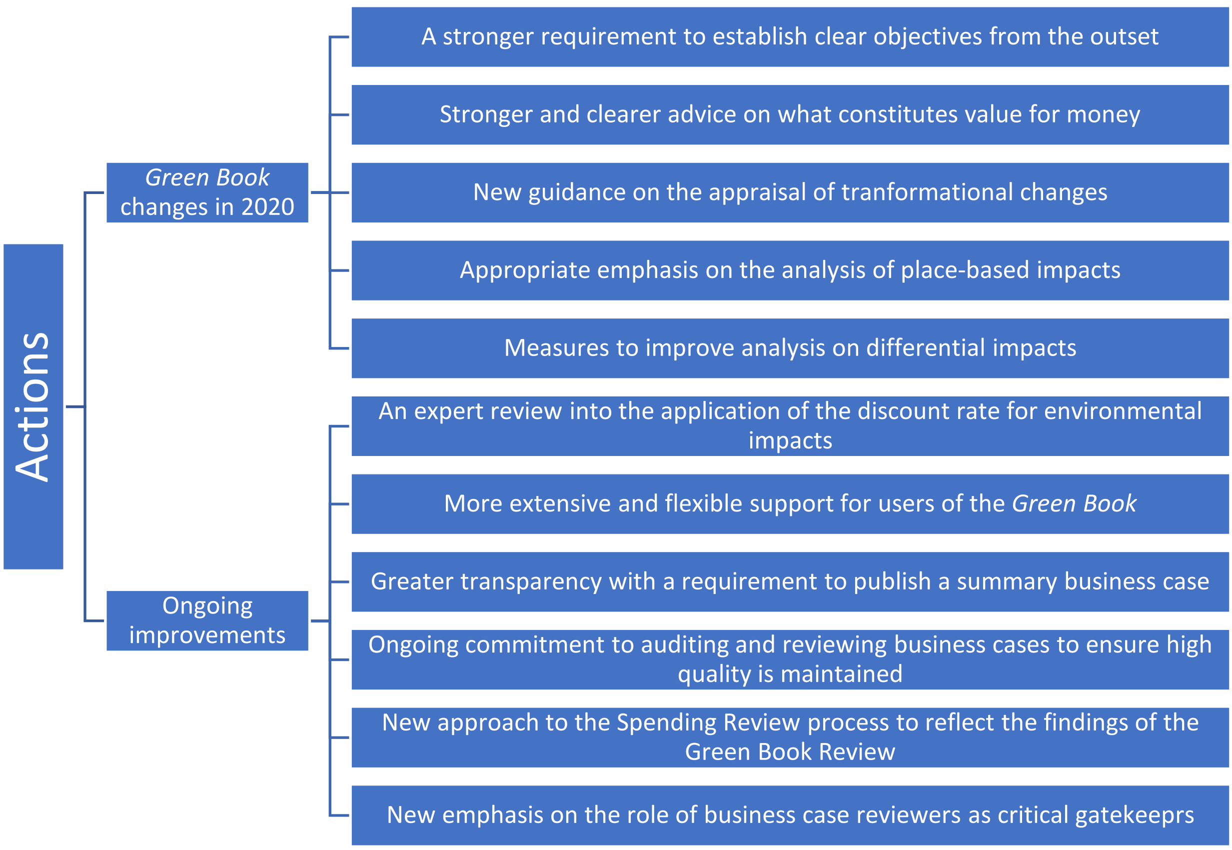
- 'Time preference' value accounting for 1.5 percentage points of the discount rate. This is the rate at which consumption and public spending are discounted over time, assuming no change in per capita consumption. It captures the preference for value now rather than later.

- 'Wealth effect' value of 1.0 percentage points. This reflects expected growth in per capita consumption over time, where future consumption will be higher relative to current consumption and is expected to have a lower utility.

Second, the *Green Book* gives guidance on the valuation of non-market costs and benefits, and on the inclusion of unmonetisable attributes. These include:

- Environmental and natural capital
- Land values
- Energy efficiency and impacts on climate change
- Life and health
- Travel time

**Exhibit 3-3: *Green Book* review response actions**




Source: HM Treasury

Following an announcement in the March 2020 Budget, HM Treasury has conducted a review of the *Green Book*, and numerous organisations and experts provided views. (See Appendix.) Treasury's response to the findings of the *Green Book* review provide a series of actions that will be taken to improve the guidance and attempt to make the appraisal and decision-making process more transparent.[6] (See Exhibit 3-3.)

## 3.2 Rural proofing policies

Alongside the *Green Book*, there is specific provision to ensure that the impact of policies on rural communities are considered. Published by the Department for Environment, Food and Rural Affairs, *Rural proofing* tells policy makers and analysists in government how to assess and take into account the impacts policies would have on rural areas.

The *Rural proofing* document contains guidance to be considered from the early stages of policy development through to policy evaluation and beyond.[7] Assessors are required to identify potential impacts on such things as access to services, living and working in a rural area, environmental impact, or distribution, equality, devolution and funding.

The four key questions it asks are:

1. What are the direct or indirect impacts of the policy on rural areas?
2. What is the scale of these impacts?
3. What actions can you take to tailor your policy to work best in rural areas?
4. What effect has your policy had on rural areas and how can it be adapted further?

While the focus is on ensuring that policies that are likely being developed for other environments are also effective in rural areas, the guidance does comment on funding and resources. It says: 'Policies do not need to deliver an equal level of resources for rural areas and urban areas but should be fair and equitable and demonstrate proportionality to rural areas'.[8]

Within the *Green Book* itself, place-based analysis is required for two categories of proposal:

- Proposals with an objective that is specific to a particular place or area or type of area
- Proposals which do not have geographical defined objectives, but which appear likely to have different implications either positive or negative for parts of the UK that decision makers will need to understand and may need to take into account[9]

[6] HM Treasury, *Green Book Review 2020: Findings and response*, 2020
[7] Department for Environment, Food and Rural Affairs, *Rural proofing: Practical guidance to assess impacts of policies on rural areas*, 2017
[8] *ibid*. p17
[9] HM Treasury, *The Green Book*, 2020, p.91

**Exhibit 3-4 : Rural proofing Checklist**

## Rural proofing checklist: actions to take

- ☐ Allow for higher rural unit delivery costs in funding formulae or allocations.
- ☐ Look at alternative means of providing and accessing the services in rural areas, e.g. through community involvement.
- ☐ Reduce the need to travel by using outreach, mobile services or localised delivery
- ☐ Consider better integration or improvement of transport links.
- ☐ Allow local delivery bodies flexibility to find the best local solution(s); avoid a "one-size-fits-all" approach.
- ☐ Use the rural networks and meeting points that exist, for example post offices, village halls, parish notice boards.
- ☐ Ensure the needs of smaller businesses are specifically addressed.
- ☐ Use small area based data to identify social, economic and environmental differences that need to be accounted for in the policy.
- ☐ Engage with rural stakeholders and their networks so you can gather evidence and test your proposals.

Source: Department for Environment, Food & Rural Affairs

The *Green Book*'s place-based analysis does not consider where previous funding has been allocated, which signals a failure to view proposals in a broader context. This reinforces the challenges facing rural areas in securing funding.

In a previous edition of the *Green Book*, from 2003, explicit advice was given on appraising the impacts of spending on different income groups; this detail has been removed from recent iterations.[10] Benefit to lower income households was given greater weight than the same monetary value of benefit to those with higher incomes. The use of such a weighting framework, dependent on income quintile, would have favoured at least some of those on lower incomes living in rural areas, although it would have been to the detriment of higher-earning residents.

### 3.3 Unfinished Green Book business

There is little wrong with *Green Book* itself – even before the revisions announced alongside the Chancellor's November 2020 spending review. It is a well-developed and

[10] HM Treasury, *The Green Book*, 2003, p.94

thoroughly tested manual for the application of cost benefit analysis to public sector decision-making.

There are, though, at least five technical areas where further revision or improvement would be welcome from the rural perspective. These issues potentially disadvantage the appraisal of rural interventions.

First, the relative impact of a given monetised value of benefit to rural communities could be explicitly included in the guidance. The argument here is that £1 of benefit in a rural community should have a higher-than-average weight in the *Green Book* to reflect typically lower incomes locally. Indeed, this would be consistent with the approach in the 2003 edition. Some caution does, though, need to be applied when prioritising the welfare and utility of one group over another.

Second, the discount rate is unchanged since before the global financial crisis. The Treasury has published a range of research into the appropriate value of the social time preference rate, and this is not the place to revisit or challenge it in detail.[11] Some experts believe that the 3.5 per cent per annum rate was set too high; others say too low. But, either way, one might not expect that the value be the same before and after the last recession — as the longer-term growth trajectory for the economy, which determines the wealth component of the value, now appears weaker than pre-2008 expectations. It would be more reasonable to expect a lower discount rate. The 2020 update to the *Green Book* again leaves the discount rate unaltered. With costs typically higher on a like-for-like basis than in urban areas, a higher discount rate makes it harder for rural projects to achieve a positive net present social value.

**It would strengthen the *Green Book*'s appraisal guidance if Treasury committed to regularly reviewing the discount rate and adjusting it when required to better reflect expected growth in per capita consumption over time.**

Third, the largely one-size-fits-all approach to the discount rate is not suitable for the assessment of all proposals. This is recognised for development assistance expenditure and risks to health and life; meanwhile, a review has now been announced in relation to the treatment of environmental impacts.[12] There are arguments for the **use of a new lower rural-specific discount rate**. Such a targeted reduced percentage would reflect:

(i) lower historical and expected rates of growth in per capita consumption, which themselves are partly the legacy of historical low rates of public investment there; and

(ii) higher inherent unit costs of delivering services or capital projects in sparsely populated areas – although this may be better addressed through adjustments to costs directly.

[11] M Freeman, B Groom & M Spackman, *Social Discount Rates for Cost-Benefit Analysis: A Report for HM Treasury*, 2018
[12] HM Treasury, *Green Book Review 2020: Findings and response*, 2020, p.6

Fourth, the issue of higher unit costs in rural areas may be better addressed through adjustments in the social cost benefit appraisals to the cost numbers themselves. The **use of 'sparsity-normalised costs'** – i.e. costs that have been adjusted to reflect the impact of the local density of population – would ensure that the appraisal of rural schemes would be like-for-like with urban ones.

Fifth, the *Green Book* struggles to assess the value of 'transformative' projects, which are interventions that deliver step changes in outcomes rather than incremental ones. Some high-profile big transport infrastructure schemes are good examples, such as London's Crossrail and the Humber Bridge. These create completely new connections and travel opportunities. Their impacts are broader and deeper than can be captured by traditional static marginal analysis techniques; they have the potential to change the underlying macroeconomic and social assumptions of the appraisals.

Although less headline grabbing than big metropolitan infrastructure projects, interventions in sparsely populated areas can be more transformative for their communities. New transport links, like the Skye Bridge – or even the widening of country roads to permit heavy goods vehicles, can open completely new opportunities, markets and industries for otherwise practically-unconnected populations. The rollout of ultrafast broadband is a greater step change in digital connectivity for rural areas than urban. The creation of an industrial estate with new engineering jobs will provide greater economic diversification and boost incomes more in a farming/tourism-only village than in a mixed-economy city.

In the 2020 revision to the *Green Book*, a new appendix has been added to provide guidance on transformational projects – although it is largely concerned with their definition than the scope, nature or methodology of their appraisal. **The *Transformation, Systems and Dynamic Change* appendix needs to be fleshed out to recognise the potential impact of transformational schemes in rural areas and to give meaningful guidance on how to appraise them.**[13]

## 3.4 Re-greening the Green Book process

The broader institutional environment in which the *Green Book* is implemented systematically disadvantages rural communities – even after the revisions announced alongside the Chancellor's November 2020 spending review.

Regardless of the technical detail of the guidance, the greater challenge to proportionate treatment of rural communities comes from how the appraisal guidance is implemented by government departments and agencies, including LEPs. The Treasury is clear that the *Green Book* must sit within a broader and strategic policy development and decision-making framework, and this point is reinforced in the 2020 review. But, in practice, the outcomes for rural areas demonstrate that this is not happening effectively – and the recent revisions to the guidance do not to change this.

[1313] HM Treasury, *The Green Book*, 2020, p.127

While the document provides the basis for evaluating the social costs and benefits of individual initiatives, there is little to provide broader guidance to either civil servants or political decision-makers about how to effectively structure a portfolio of interventions, or how to make the trade-offs between overall welfare and that of specific groups or in specific locations.

In this context, the *Green Book* reinforces incrementalism and inertia. Without a robust strategic framework, politicians and officials might reasonably consider each decision incrementally and opt for those initiatives with the highest positive net present social value. This may make sense on case-by-case basis but, when considering the process as a whole, it can result in an unbalanced and distortive portfolio of interventions – and it will likely disadvantage rural communities.

In a direct comparison between like-for-like interventions in rural and urban areas, a social cost benefit analysis will typically favour the towns and cities – because of their economies of scale. So, without well-directed political discretion or a separate explicit mechanism for achieving proportionate spending in rural areas, it will not happen.

Although major revisions to the *Green Book* have been announced alongside the Chancellor's November 2020 spending review statement, more will be needed to put rural communities on a proportionate footing with their urban counterparts.

There needs to be clearer demarcation between the role of the social cost benefit analysis and the broader, strategic and political judgements. The *Green Book* 2020 update stresses the importance of appraisals taking into account many other factors before reaching the cost benefit step, however rural projects will likely still miss out at this stage. At the short-list step of the appraisal process, projects should be required to meet a threshold target rather than being prioritised. This would allow for policy makers to choose from a range of proposals which all meet cost benefit criteria, but which can then be judged on their ability to support other aims like the levelling up agenda.

**New clear guidance, either within the *Green Book* or as a separate document, is needed on how different policy interventions should be considered together to form an effective and efficient portfolio that meets the needs of varied locations and communities.** It should provide further detail on how appraisers should analyse the return to the national economy alongside the return to the regional and local authority balance, as well as the effectiveness in reducing geographical inequalities. It would allow for a portfolio appraisal of past funding awards, to better direct future spending more equitably.

# Levelling up

**The criteria for the success of 'levelling up' need to be specified in a way that makes visible and encourages progress in reducing rural disadvantage. In turn, these criteria need to be embodied in the broader *Green Book* appraisal process.**

The first tests for this will be the application of the government's new *National Infrastructure Strategy* and its recently announced £4 billion 'Levelling Up Fund'. (See Exhibit 4-1.)

This section considers how the criteria for assessing both individual projects and the portfolio of interventions funded through these new initiatives should be defined to avoid rural disadvantage.

**Exhibit 4-1: Chancellor's announcement of the Levelling Up Fund**

> *"Today I'm announcing a new Levelling Up Fund worth £4 billion. Any local area will be able to bid directly to fund local projects. The fund will be managed jointly between the Treasury, the Department for Transport and the Ministry of Housing, Communities and Local Government – taking a new, holistic, place-based approach to the needs of local areas. Projects must have real impact. They must be delivered within this Parliament. And they must command local support, including from their Member of Parliament.*
>
> *"This is about funding the infrastructure of everyday life: A new bypass. Upgraded railway stations. Less traffic. More libraries, museums, and galleries. Better high streets and town centres. This government is funding the things people want and places need. Addressing rural disadvantage will have to be central to any meaningful attempt to level up communities across the country. As the government develops the policy framework and makes funding available for its levelling up agenda, mechanisms need to be put in place to ensure proportionate support for rural communities."*
>
> **The Rt Hon Rishi Sunak MP, Chancellor of the Exchequer**

## 4.1 Geographical criteria

Any criteria for the success of the government's new policies must have a focus more granular than the nine regions of England – with levelling up assessed, addressed and monitored at a local level.

There is no explicit definition of levelling up given in the government's new *National Infrastructure Strategy* but details of key projects are grouped by region.[14] The document focuses on the creation of 'regional powerhouses' and making cities the 'engines of growth' – although there is a pledge to leave 'no community or business behind'. Meanwhile, the objective of the new cross-departmental Levelling Up Fund, worth £4 billion in England, is to "invest in local infrastructure that has a visible impact on people and their communities and will support economic recovery". It is stated that this is: "Open to all local areas with priority given to places in need, those facing particular challenges and areas that have received less government investment in recent years". On the face of it most rural areas meet the headline definitions. To be transparent, government needs to define these areas and the criteria for the decisions.

The balance of where these funds are deployed and where projects are progressed needs to be seen in greater detail than the regions. As the Institute for Fiscal Studies highlight, inequalities within regions are larger than inequalities between regions, and it is therefore necessary for government to tackle the issue at a more localised level.[15] This distinction is stark when comparing rural and urban areas within regions. And, like regions, the English counties often incorporate communities with a wide range of population densities. The differences between rural and urban are often only visible when comparing data at the level of lower tier local authorities.

**Any framework developed to allocate national funds for levelling up should assess local needs at a minimum for each of England's 101 'Level 3' areas** in the *Nomenclature of Territorial Units for Statistics*, which is broadly unitary authorities, small counties and groups of contiguous lower tier authorities in larger counties. Preferably this should occur at the level of lower tier authorities, or Local Administrative Units, 'LAU1s'.

Moving forward, greater geographical detail is needed in official statistics to monitor the socio-economic gaps between sparsely populated communities and the counterparts elsewhere, and the extent to which government interventions are addressing them. As a start, the **Office for National Statistics should work to expand the coverage of their *Country and regional public sector finances* report to include detail at 'Level 3' of the *Nomenclature of Territorial Units for Statistics***.

## 4.2 Metrics of success

It remains unclear on what metrics the success of levelling up will be measured, although productivity, employment and educational attainment are mentioned in the *Green Book* review response.[16] Whatever are chosen need to properly reflect the nature of rural disadvantage.

There are numerous candidates for metrics of locational disadvantage – and they have been written about extensively by others elsewhere. (See Exhibit 4-2 and Appendix

[14] HM Treasury, *National Infrastructure Strategy*, 2020, p.38
[15] A Davenport & B Zaranko, *Levelling up: Where and how?*, IFS Green Budget 2020: Chapter 7, Institute for Fiscal Studies, 2020, p.320
[16] HM Treasury, *Green Book Review 2020: Findings and response*, 2020, p.13

exhibit 2.) Likewise, there are competing views on what success might look like. For example, is it the closing of a gap between locations or is just the reduction of a gap?

Campaign thinktank Onward recently published the report, 'Measuring up for levelling up'[17], offering recommendations as to how government should measure levelling up. This includes producing geographical analysis of all budgets and fiscal events. The report also recommends government publishing an annual report focussing on what it sees as the three key tests:

1. Are the bottom fifth and bottom half of local authorities by earnings growing their earnings more quickly than they have in recent years?
2. Are the bottom fifth and bottom half of local authorities with the worst unemployment seeing unemployment rates falling and converging with the national average?
3. Are the bottom fifth and bottom half of local authorities with the lowest employment seeing employment rates rising and converging with the national average?

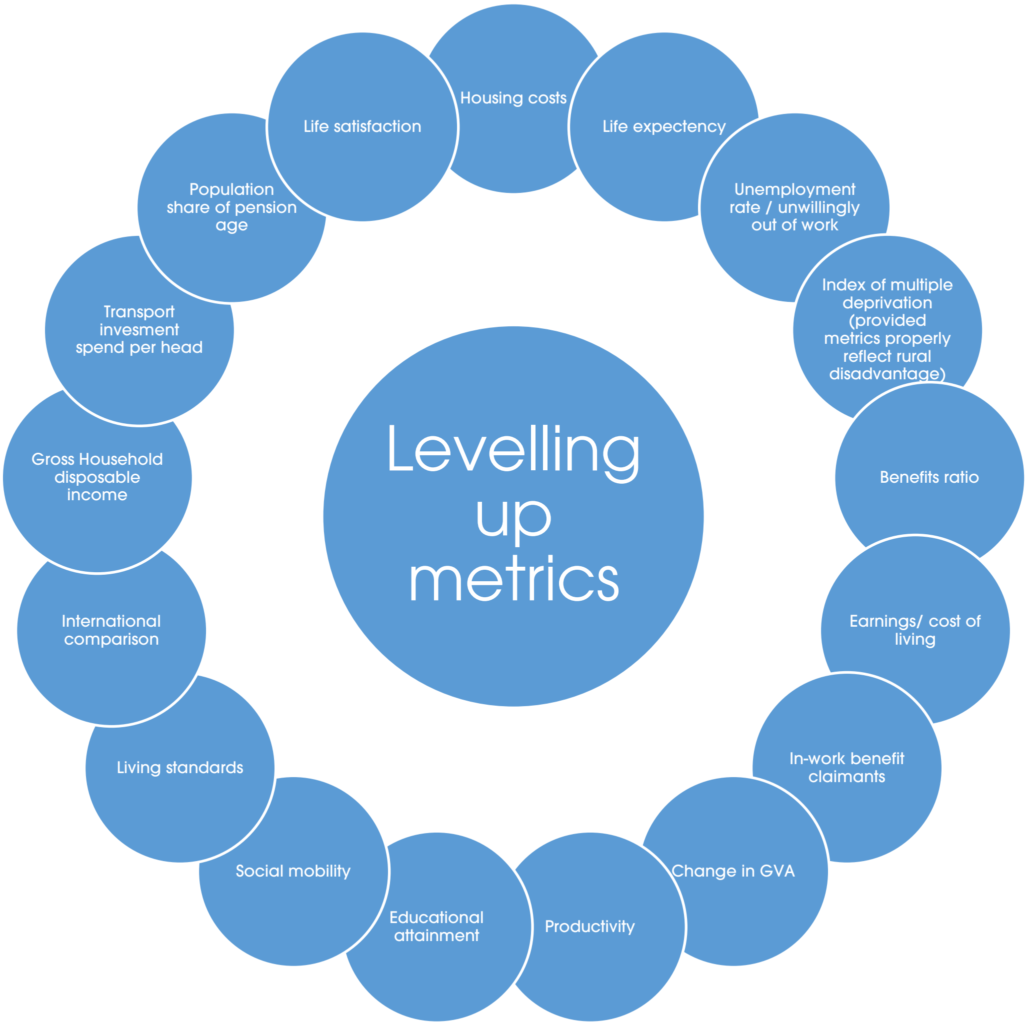
There isn't an inherently rural perspective on these issues – except that any choice and interpretation of local socio-economc data needs to account for the special characteristics of sparsely populated areas. These include recognition of:

- **Second home, commuter and retiree wealth, incomes and employment.** Average measurements of prosperity in a rural community can often hide two different stories, especially in areas within a reasonable commuting time of a major city. While many with wealth or high income city jobs who are able to 'escape to the country' push up average prosperity, those who depend on local jobs have different prospects and living standards.

- **Seasonal, casual and part-time working patterns.** Rural jobs are more likely to be on the basis of irregular hours and without continous employment. A simple comparison of 'full time equivalent' data with urban areas does not capture the difference in security and continuity.

[17] N O'Brien MP, 'Measuring up for levelling up', Onward, 2020

**Exhibit 4-2: Factors to measure the success of 'levelling up'**




Source: Pragmatix Advisory

## 4.3 Practical capacity

With the allocation of the Levelling Up Fund set to be the outcome of a bidding war between different local areas, rural authorities are disadvantaged by their lack of resource and capacity to complete their applications to Whitehall.

While the likes of the metro mayors are able to establish large strategy departments and commission Big-Four consultancies to write business cases for their proposed investments, rural councils cannot. Although the increasing number of pages in the *Green Book* and its associated documents represent a genuine effort by government to make the appraisal process fairer and broader, it is also a barrier to entry for those without the resources to engage with it. The Treasury has promised further online training and support for potential users – but **expert resources need to be made available for rural authorities to produce businesses cases and advocate for their priorities**.

# Appendix

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**Appendix exhibit 1: Review of *Green Book* critiques**

| | Comments |
|---|---|
| ***Re-writing the Green Book for levelling up,*** **Centre for Cities, September 2020** | **Issues**<br>• Criticism that benefit cost ratios skew public investment towards prosperous areas misplaced. BCRs actually biased towards transport investment outside Greater South East because they measure estimates of the benefits of value of time saved by transport investment using national average wages – this biases the BCRs *away* from the Greater South East as it has above-average wages.<br>• Lack of strategic direction at the national and local level frequently hamstring the arguments made for new investment.<br>• Green Book used to create shortlist, policy decisions decide the projects<br><br>**Recommendations**<br>• Levelling up' requires simplification of Green Book cost/ benefit appraisal methodology<br>• Simpler cost-benefit models<br>• A standard toolbox of models defined by central government<br>• A public database of BCR appraisals for evaluation of models and proposals held by central government<br>• More analysis should be done by in-house local government economists rather than outsourced<br>• Need for national 'levelling up' strategy<br>• Clear system for allocating public investment within England |
| ***The Green Book: Central Government Guidance on Appraisal and Evaluation,*** **Dr. Martin Hurst, Taylor & Francis Online, April 2019** | **Issues**<br>• Valuable document if appropriately used. Concerns with policy appraisal and evaluation less about Green Book itself but more the way guidance is applied<br>• Limited coverage of portfolio analysis<br>• Excessive reliance on normal distribution analysis<br>• Limited coverage of social impact<br>• Over-emphasis on monetization<br>• Tendency toward a reliance on carbon-copy techniques<br>• Hard for projects to go forward without positive NPV, choice between positive projects comes down to politics not policy<br>• Can lead to excessive costs<br>• Works for medium-sized 'carbon copy' projects but bigger projects face greater challenges. |
| ***Plan to 'rip up' treasury Green Book is an opportunity,*** **Grant Thornton, February 2020** | **Issues**<br>• Often areas with stronger economies come out more favourably, harder to make investment case in areas that need it most.<br><br>**Recommendations**<br>• Appraisal needs to go beyond economic benefits, sustainable growth should analyse prosperity, dynamism and opportunity, inclusion and equality, health, wellbeing and happiness, community, trust and belonging, resilience and sustainability<br>• Benefits case rather than economic case should contain analysis of each factor.<br>• Need to change behavior of those appraising proposals, and final decision makers. |

| | |
|---|---|
| *In Defense of the Green Book,* Simon Groom, March 2020 | **Strengths**<br>• Green Book is a flexible framework for facilitating analysis and decision-making, with potential to hold decision makers to account.<br>• Benefits flowing to poorer members of society receive higher weighting in NPV calculation.<br>• Green Book includes social cost-benefit analysis, and requirement for differential impacts on different groups of people or parts of the UK.<br>• Green Book not responsible for public investment in better off areas, it has been policy choice of successive governments<br><br>**Recommendations**<br>• Though it exists, the option of 'distributional weights' is rarely used. Could be used as mechanism for influencing investment decisions in pursuit of regional policy objectives. |
| *Levelling up: making investment appraisal for purpose,* North West Business Leadership Team, March 2020 | **Issues**<br>• Long-term trend of underinvestment in places, more productive regions receive more transport investment per head.<br>• Risk aversion leads to backing projects where prospect of return more self-evident, easier to bring in private sector investment in prosperous areas, decision makers based in London and have greater awareness of need for projects there<br>• System of appraisal processes contributes to skews in investment<br>• Green Book is a toolkit too often confused with decision-making guide<br>• Rebalancing Toolkit is an attempt to rectify this with regard to strategic rebalancing considerations - fails to do so<br>• The Strategic Case element of appraisal is often under-developed and generally undervalued<br>• Overreliance on benefit-cost ratios in decision-making<br>• The benefit-cost ratio, even when accurate, is blind to geographical considerations because it sums all national gains and losses into one figure<br>• Lack of transparency around infrastructure appraisal process.<br>• Complex Investment Appraisal processes without adequate support, expertise to use Green Book to develop value for money and compliant proposals is often lacking, particularly in areas with limited track record.<br><br>**Recommendations**<br>• Introduce a clear strategic framework for assessing projects into the Green Book.<br>• Clear framework as to how these aims will be achieved and what success might look like, along with metrics which can be used to evidence it<br>• Formally incorporating (with changes) the Government's Rebalancing Toolkit<br>• A review of discount rates and time horizons.<br>• Commitment to transparency<br>• Programme of capacity building to support business case development |

| | |
|---|---|
| ***Levelling up and revising the Green Book, Where next?*** **ARUP,** **June 2020** | **Strengths**<br>• Consistency of approach<br>• Balanced approach of different objectives (with a few exceptions)<br>• Flexible framework<br>• Consistency of values across the country<br><br>**Recommendations**<br>• Supporting local objectives<br>• Decisions on spend such as transport and housing should be taken at local level<br>• Enabling levelling up (requires a clear definition of 'levelling up')<br>• Better accounting of distributional impacts<br>• Improve appraisal of transformational schemes<br>• Improved appraisal methods<br>• Better capturing of the impacts of climate change<br>• Greater transparency of decision making<br>• Better use of economic evaluation and the *Magenta Book* |

**Appendix exhibit 2: Review of levelling up critiques**

| | Areas to measure | Metrics of levelling up |
|---|---|---|
| A Davenport & B Zaranko, *Levelling up: Where and how?*, IFS Green Budget 2020: Chapter 7, Institute for Fiscal Studies, 2020 | • Lower level than regional<br>• Large towns and some cities outside of London and the South East<br>• Former industrial regions<br>• Coastal towns and regions<br>• Isolated rural areas | • Regional GDP per capita<br>• Earnings<br>• Wealth<br>• Health<br>• Educational attainment<br>• Social mobility<br>• Living standards (net income after housing costs)<br>• Incapacity benefits<br>• Economic fallout from covid<br>• Impact of Brexit<br>• International comparison<br>• Capital spending per person<br>• Transport investment spending per person<br>• Expenditure on R&D<br>• Location of FTE civil servants |
| N O'Brien MP, *Measuring up for levelling up*, Onward, 2020 | • Local authorities<br>• Large cities vs the rest<br>• Inner cities and outer city regions<br>• Parliamentary constituencies<br>• Rural urban classification of Middle Layer Super Output areas | • Regional share of GB population and GDP<br>• Population share of pension age<br>• Working age population with degree level qualifications/ progression to higher education<br>• Wellbeing<br>• Housing costs<br>• Employment and unemployment rates<br>• Earnings by gender<br>• Gross domestic household income<br>• Earnings growth |
| Centre for Cities, *Measuring levelling up*, 2020 | • Cities, urban areas, large towns | • 'Business environment index' (number of start-ups, business stock, share of jobs in the private sector, productivity per worker, number of patent applications)<br>• 'Employment opportunity index' (employment rate, claimant count rate, average weekly workplace wages) |

| | | |
|---|---|---|
| | | • Relationship between skills and business environment index<br>• Relationship between business environment index and employment opportunity index<br>• Relationship between business environment, employment opportunities and housing affordability |
| **Frontier Economics, *Levelling up – getting it done*, 2020** | • Deprivation deciles<br>• Regions<br>• Local level | • Life expectancy<br>• Gross value added<br>• Gross household disposable income<br>• Life satisfaction score |

## Authors

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