National Institute Economic Review No. 227 February 2014
EMBARGOED until 13.00 hours Friday 7 February 2014

Economics of Scottish Independence

Issue no. 227 of the National Institute Economic Review is a Special Issue on the Economics of Scottish Independence, edited by Angus Armstrong (a.armstrong@niesr.ac.uk) and Monique Ebell (m.ebell@niesr.ac.uk).

We will be holding our first ever Scottish press conference for the Review on Friday 7 February at 11:30am in the Wellcome East Room at the Royal Society of Edinburgh.

At this briefing, we will present our latest forecasts for the UK based on our global macro-econometric model, NiGEM, used by many leading central banks and finance ministries around the world. The embargo for the forecast is 00.01 hours Friday 7 February 2014, so it will have passed before the conference.

In addition, this issue includes six papers covering a wide range of the key economic issues related to Scottish independence. Some of these papers are new, and others revised, yet this material is embargoed for 13.00 hours Friday 7 February when the conference has closed.

The papers cover government debt and spending; the choice of currency and financial stability; pensions and the impact of ageing; measuring Scotland’s economic output; and possible alternative models of governance.

Contributions are from the Centre for Public Policy for Regions (CPPR) at Glasgow University, University of Aberdeen, University of Stirling, University of Ottawa, the Institute for Fiscal Studies and NIESR.

See below of the titles of the six papers included in the Review. Three of the authors will be present to introduce and discuss their papers.

The proceedings will be as follows:

11.30 am Welcome, Dr Angus Armstrong, NIESR

11.35am UK Economic Forecast followed by Q&A, Simon Kirby, NIESR

12.00 pm “Economic and fiscal implications for Scotland of moving to independence,”
Dr Jo Armstrong, CPPR

“Scotland: Currency Options and Public Debt,”
Dr Monique Ebell, NIESR

“Funding pensions in Scotland: Would independence matter?”
Prof. David Bell, University of Stirling

13.00 pm Close

Several of the contributors to this special issue of the National Institute Economic Review on the Economics of Scottish Independence are funded by the ESRC’s Future

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of UK and Scotland Programme, which aims to explore the key issues in the Scottish independence debate and to deliver impartial information and analysis on these key issues to voters.

Angus Armstrong (NIESR), Michael Keating (University of Aberdeen) and David Bell (University of Stirling) are all ESRC Senior Scotland Fellows and senior researchers at the ESRC Scottish Centre on Constitutional Change. Katerina Lisenkova (NIESR) is a senior researcher at the Centre on Constitutional Change, while Malcolm Harvey (University of Aberdeen) is one of its junior scholars.

The articles are as follows:

**Economic and fiscal implications for Scotland of moving to independence**
by Jo Armstrong and John McLaren (CPPR, University of Glasgow)
Contact: [Jo.Armstrong@glasgow.ac.uk](mailto:Jo.Armstrong@glasgow.ac.uk)

The authors provide an overview of the economic position of Scotland as it approaches the referendum, and examines how its fiscal position might evolve over the coming years and decades. One important focus is on different measures of aggregate income, Gross Domestic Product versus Gross National Income, and their implications for assessing living standards and the tax base available to an independent Scotland. Another important distinction is real versus cash terms measures of aggregate income, which are especially important due to volatility in the oil price. The authors go on to assess the impact of competing forecasts on future oil production and revenues for an independent Scotland’s medium- and long-term fiscal position.

**Scotland: Currency Options and Public Debt**
by Angus Armstrong and Monique Ebell (NIESR and Centre for Macroeconomics)
Contact: [a.armstrong@niesr.ac.uk](mailto:a.armstrong@niesr.ac.uk) or [m.ebell@niesr.ac.uk](mailto:m.ebell@niesr.ac.uk)

This article examines the implications of the level of public debt that Scotland might expect to inherit at independence for its optimal currency choice. Armstrong and Ebell argue that at high levels of government debt, a monetary union with the UK would restrict Scotland’s capacity to adjust using fiscal policy which would limit its degrees of policy freedom to manoeuvre in adverse economic circumstances. An independent Scotland would always retain the sovereignty to change its currency and fiscal arrangements in the future. This makes agreeing and implementing fiscal constraints which bind in all circumstances difficult to achieve. It may also mean that investors question the commitment of the government to remain within the union when a significant economic shock hits.

**Funding pensions in Scotland: Would independence matter?**
by David Bell, David Comerford and David Eiser (University of Stirling)
Contact: [d.n.f.bell@stir.ac.uk](mailto:d.n.f.bell@stir.ac.uk)

This paper considers the costs to providing state and public sector pensions in an independent Scotland. They note that the lower cost of financing pensions in Scotland due to lower further life expectancy make providing pensions in Scotland less
expensive per retiree, but that higher dependency ratios[1] work against this when pension affordability is assessed in terms of the cost per working adult. They also examine the distributional implications in the case that government debt carries higher interest rates for an independent Scotland: Pensioners would benefit from the higher interest rates, but at the expense of higher taxes for younger cohorts of taxpayers due to higher costs of debt service.

Can an ageing Scotland afford independence?
by Katerina Lisenkova (NIESR) and Marcel Mérette (University of Ottawa)
Contact: mmerette@uottawa.ca

The authors address the question posed in the title using a dynamic multi-regional overlapping generations model spanning Scotland, the rest of the UK and the rest of the world which differentiates two cases: Under independence, Scotland would finance its pensions alone, while as part of the UK pensions would be funded jointly. Lisenkova and Mérette find that Scotland would be slightly worse off under independence, but that this difference is small compared to the effects of ageing on both economies.

Fiscal challenges and opportunities for an independent Scotland
by Rowena Crawford and Gemma Tetlow (Institute for Fiscal Studies)
Contact: bonnie_b@ifs.org.uk

The authors present a detailed national transfer accounts analysis of how Scotland’s fiscal position might evolve in the next 50 years if current policies were maintained. Crawford and Tetlow project that if Scotland targets a debt to GDP ratio of 60% by 2062-63, it would have a fiscal gap of between 1.5 and 5.9% of GDP, compared to a fiscal gap of 0.4% for the UK. They conclude that Scotland would either need to reign in its current spending levels, or increase taxes, in order to fund this gap.

The political economy of small European states; and lessons for Scotland
by Michael Keating and Malcolm Harvey (University of Aberdeen)
Contact: m.keating@abdn.ac.uk

This contribution provides some fundamental analysis on the different political models that an independent Scotland might choose. The authors distinguish between the market competition state, similar to Ireland or the Baltics, on the one hand, and the social investment state model favoured by the Nordic countries, as well as discussing corporatist models. This work begins to map out the alternative social and economic models which would be available to an independent Scotland. Keating and Harvey conclude with an examination of which of these models fits most closely to Scotland.

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Notes:
For full copies of these papers, please contact the NIESR Press Office: Brooke Hollingshead on 020 7654 1923 / b.hollingshead@niesr.ac.uk

To discuss the National Institute Economic Review or for interviews, please contact: Angus Armstrong 020 7654 1925/ a.armstrong@niesr.ac.uk

[1] The dependency ratio is the ratio between pensioners and the working population.
To discuss any of the articles or for interviews, please contact the respective researcher.

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