Twitter Thread by Tony Yates



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The titbits I get fed about the debate over a hypothetical post indy monetary policy in Scotland make it seem like a lot of nonsense is being talked on the indy side.

One could say 'it is doable, with some institutional risks, to set up a new central bank and do independent inflation targeting, with credible political backing, and the reservoir of econ and cb expertise, and history of inflation targeting itself.'

However, SNP don't want to say this, as it - rightly - fears that people fear the risks of setting up a new currency. Even though IMO this is a perfectly sensible and doable option.

There's also the complication of EU membership. On the face of it, given what that would require, the trajectory would be, in this case, 1) period of independent inflation targeting, 2) ERM like period, 3) Euro membership.

Owning up to this is tricky, because there is presumably the worry that people won't want to vote indy because they are against the Euro, a feeling aggravated by the EZ crisis.

A pragmatic observation often made is that there are countries on the Euro accession path that are not transiting to joining and will probably never join, and this is tolerated by the EU.

Presumably this can't be used to front-foot an indy currency + EU 'rejoining' strategy because it's embarrassing and counterproductive in the Sco-EU bargain to point to an institution honoured in the breach.

This leaves/led to Sterlingisation being proposed/offered, which IMO would be highly suboptimal.

It is highy unlikely that RoUK would consent to Scottish control of any kind over a Sterling area. This would be to recreate the worst aspects of the EZ - a monetary union with, on the face of it, no fiscal union [the latter being the point of indy].

Scotland could try to bargain for this.

But it would be such a bad deal for the RoUK that I can't envisage the circumstances where this would be conceded, or where a new Sco govt would offer something that would be attractive enough to make it happen....

.... bearing in mind that, with the indyref won, it could easily turn tail and fall back on the independent mon policy model, which would anyway be better for itself, even as a road to EU-euro membership, rather than pay a price [presumably in fiscal independence] for £ control.

So £ really means not having your own monetary policy or currency, or central bank, and all the financial stability and government finance in extremis options they give you. Highly sub optimal.

Not sure I have properly done justice to the local debate, but this is how it seems to me.

Taking mon pol and fin stab considerations together, seems better to stay part of the union. But the costs of leaving are - provided crisis risks don't materialize - not of the same order of magnitude as the costs of leaving the UK single market [given the current UK-EU FTA].

There is also a sub-strain of the debate, infected with MMT like silliness, but maybe also a bit of Project Fear too.

The Project Fear bit is 'where is the money going to come from to set up the cb, finance its running costs, establish FX reserves' [perhaps this exists only in the minds of the MMT-like lot who want to motivate their response...

... and the MMT-like response is: new currency, one magically acquires FX reserves, central bank capital, whatever you want really.

To which my response is: Scotland would effectively, perhaps even mechanically, get a carve out of the BoE's balance sheet; and like the BoE it would, operating its own currency, finance its running costs from its own seigniorage.

It would also, in the grand bargain, get a per capita portion of FX reserves, govt debt, etc...

So, there is no magic central bank, forex reserves, financing solution... but also there is none needed.

My guess is that there are slight economies of scale in central bank size, so an indy Scotland would suffer slightly. A lot would depend on how the size of the financial sector evolved [which in turn feeds back to supervisory effort and competence, LOLR demands...].

But central bank financing and running ought not to be a significant part of the debate. From memory, there is a lot of variation in cb staff/general pop size, no good evidence at all on what is optimal, and BoE is relatively lean.

From an economists' perspective - political, spiritual, whatever stuff aside - where does this leave the costs and benefits of leaving?

Obvs a major negative: 1) mostly because of errecting trade barriers with RoUK, where lowering them again with EU won't make of for it; 2) losing the subsidy and risk-absorption that comes from membership of the UK fiscal union;

3) a small negative associated with taking what I think would be the inevitable option of setting up own currency, small contingent on avoiding govt financing/currency crisis in the early years, which should be doable if SNP are open, honest and follow existing playbook.

And this general negative not offset with any significant positive, because I think most of the stuff talked about subsidiarity and govt induced industrial transformation is bollocks [see also 'levelling up]].

Of course, if you value non pecuniary things enough, it may well still be rational to vote for independence, and especially with the current lot of mendacious idiots in power in the UK, it is not hard to empathize.

And this is also not addressing the following argument, which is: what is the risk that you will a) have another epidemic and b) be subjected to the malevolent incompetence of a UK govt?

From here, one would hope the Scots stay, and help minimize the chance of b) happening so that the chance of a) and b) is very small. But you can see that with the current epidemic in mind, Scots will feel they have an easy way to eliminate the risk of a) and b) for themselves.

As a postscript, and as others responding to this thread pointed out, the lessons of the Brexit campaign for how you should broach tricky economic arguments whose exploration is not advantageous to your goal are not that encouraging.

The lesson is: you have a disparate coalition to pull together behind your binary choice. Lie about whatever you need to and promise whatever you have to even if these promises are mutually inconsistent and have to be broken later.

The econ and finance arguments are hard for lay people to get their head round. You'll be able to find a credentialled economist who has signed up to the cause to say what you want anyway and create the necessary smoke behind which your lies and inconsistencies can hide.