ECONOMIC *Perspective*

THE IMPACT OF THE EURO ON THE SCOTTISH LABOUR MARKET - SOME POSSIBLE SCENARIOS*

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INTRODUCTION

The introduction of the EURO on 1 January 1999 could have profound implications for the UK Labour Market in general and the Scottish Labour Market in particular. The precise ways in which the EURO may impact on the Scottish Labour Market will depend on a number of inter-related factors, inter alia:

- Whether or not Sterling does eventually join the EURO system;
- The extent to which Economic Convergence (see below) is achieved within each of the EU Member States;
- The impact of Convergence (if achieved) on specifically labour market aspects (eg labour mobility, wage and non-wage costs etc);
- The effect of the EURO in making price and wage differences between member states more transparent; and
- The implications of other European policies (eg The Social Charter and Minimum Wage Legislation) on the Scottish Labour Market.

1. Whether or not Sterling joins the EURO?

This is the primary question to address. The delay in Sterling joining the EURO System, and indeed, the possibility that the currency may never join, creates uncertainty within financial markets. A key gain from joining, is a downward drift in UK interest rates to levels comparable with those in the rest of Europe (see Table 1). This undoubtedly would be a gain because lower interest rates within a low-inflation environment, will be growth-inducing and will stimulate investment and therefore employment. Of course, much of the British reluctance to commit to the EURO is based on the notion that Economic Convergence (Lower Public Sector Deficit Levels, Lower Unemployment levels etc) has to be achieved, or nearly achieved, before Britain finally commits itself to the EURO.

We should be clear on possible directions of causation. It is not the EURO alone that will achieve convergence. Rather it will be as a consequence of more general macroeconomic factors – the so-called Economic Fundamentals – which will help to achieve Convergence. In this connection, the debate about the EURO can be considered as **"Much Ado About Nothing"**. The exchange rate is after all just one of a number of price variables which influences the competitiveness of countries. Abolition of exchange rates within Europe certainly reduces transaction costs associated with trading, which should in time be trade-creating.

For the UK economy, and also for the Scottish Economy, perhaps one of the justifiable reasons for caution is the heavy investment and trade which the UK enjoys with the US, the Japanese and other non-European economies eg Latin America, the Commonwealth etc. This is manifested by the high degree of inward investment which the UK Economy (and the Scottish economy in particular) exhibits vis-à-vis these non-EU partners. It could be argued that such inward investment has been attracted into the UK by an almost **"Beggar My Neighbour Policy"**. Namely, Japanese, Far Eastern and US companies have been more inclined to invest in UK plant, because of the relatively high recent rates of economic growth within the UK, alongside a labour market environment which compared with European competitors has been more flexible and less constrained by high non-wage costs (eg social security provisions) – the so called **Safe Haven** argument.

The question is whether such willingness on the part of these non-EU investors would be affected at all if Sterling joined the EURO. The honest answer is we do not know!

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Providing the EURO does not bring with it some of the structural (Non-Convergence) weaknesses exhibited by our European neighbours, it should make no difference to their willingness to invest in the UK. Instead of the Americans, Japanese or Koreans exchanging their respective currencies for Sterling, they will exchange them for EUROS. They will continue to incur a transaction cost in this regard which they would have incurred against Sterling anyway.

Therefore, on balance, whether Sterling joins the EURO is not the fundamental question. What matters more is whether the Gains to Trade to be derived from enhanced European growth, and trading opportunities are offset by the losses to the UK economy from reduced non-European trade and investment. Certainly, all the forecasts suggest that UK interest rates will continue to fall within a European context and this may be a substantial gain from EURO membership. This will have to be borne out in any calculus of overall gains and losses.

2. Is Economic Convergence being achieved within Europe?

This is a more difficult question to answer than we might imagine.

The following are the main Convergence Criteria which EU Member States are working towards:

- The achievement of price stability;
- The sustainability of the government financial provision (Budget Deficits at no greater than 3% of the GDP) – (Public Debt Ratio should not exceed 60% of GDP);
- The durability of convergence among Member States as reflected in long-term interest rate levels. This means a downward harmonisation of interest rates towards the level of the most successful Member States;
- Member currencies should observe the normal fluctuation margins provided for by the ERM for at least 2 years without devaluing against the currency of any other Member State.

EU statistics appearing in Table 2 indicate that with the exception of the Budget Deficit in some countries, a high degree of convergence has been achieved particularly in relation to price inflation and interest rates. When we come to unemployment levels, however, there is significant disparity with the UK in an especially strong position at approximately 4.7%, whilst countries such as Spain stand at 15%. However, by January 2000 the average European Union level of unemployment was 9.9% which certainly represents a declining trend from the level of January 1999 (10.6%).

It is common knowledge that the UK Government has indicated a **"wait and see"** approach to Euro membership. This is based on 2 main aspects. Firstly, a settled or sustained period of convergence and; secondly an increased preparedness of the UK economy for the effects of a European-wide (and ECB co-ordinated) monetary policy with continually declining interest rates. The latter is as difficult to be certain about as the former even although the recent performance of the UK economy in terms of the **"virtuous circle"** of high economic growth accompanied by low inflation would indicate a higher level of preparedness of the UK economy than ever before. The **Stability and Growth Pact** of Member States which lies at the very core of this objective, at least as far as the UK government is concerned must be achieved simultaneously with falling budget deficits. It is on the latter aspect that the UK's position seems to be more solidly-based. In this connection David Smith (1999) in a recent article makes a valid point when he says ... "Paradoxically the economic argument for EMU may be won only if Britain's economy is seen to be doing less well than it is now ...the public's response to a decision to join EURO would be .. **If it ain't broke why fix it? ...**"

Further confusion and uncertainty has recently been added to the dilemma faced by the UK government from the findings of a recently published IMF paper which suggests that Sterling is significantly overvalued against the EURO perhaps by as much as 20%. Prior to joining the EURO, Sterling would have to be devalued to that extent giving an entry rate at 81 pence to the EURO, compared with the current rate of 63 pence to the EURO. Of course, since the EURO's launch in 1999 Sterling has appreciated sharply, as has the US dollar. The dilemma for the UK government is whether it would be willing to suffer the inflationary effect of such a substantial currency devaluation on EURO entry. Or should the currency remain outside the EURO even if this means that Sterling remains high?

UK (and Scottish) exporters are normally unhappy when Sterling is overvalued as this makes their export markets less competitive. Ironically, and this complicates the picture even more, recent trends suggest that perhaps UK exporters are beginning to live with the strong pound. This was certainly the view expressed in the Bank of England's November 1999 Inflation Report which indicated that the fall in the UK's export of goods and services experienced in 1998 (largely attributable to the decline in exports to East Asia,) - was reversed at least in the second and third quarters of 1999. The combined total of export growth (including those to the US and EU countries) was 2.1% during that period. Surveys by both the CBI and the British Chambers of Commerce indicated that the growth in world demand experienced during 1999 more than offset the potential negative effects of Sterling's high value on UK exports.

Moreover the early performance of the EURO since its launch in January of last year, if it persists, might indicate a less powerful currency than Member States had anticipated. Whilst it is premature to speak of a Euro-currency crisis, a possible threat to the prospect of continually falling interest rates would arise from a falling EURO. If this were to persist, it may in fact be necessary to raise Euro interest rates, thereby throwing away one of the long sought after gains of EMU. On this score alone, the UK Government's reticence to commit itself to the EURO, whilst undoubtedly irksome to EU neighbours is probably the wise and cautious approach.

There is a fundamental cause and effect issue at the heart of this debate. Will Economic Convergence among Member States be speeded up by the creation of the EURO-zone? On one level the answer is affirmative, to the extent that the single currency will be growth and trade-inducing which should boost employment in Member States. This, in turn, should (providing the political will prevails) contribute to falling Public Sector Deficits in Member States. However, such prospects also depend on a future strong EURO in order to avoid increasing interest rates, which would be detrimental to growth. Therefore, it is difficult to avoid the conclusion, which seems to be that reached by the UK Government, that what matters most is the political and economic conviction to see the convergence process through to the end, with or without the EURO.

3. The implications of Economic Convergence for Labour Markets

The Amsterdam Treaty placed employment policy at the very heart of European economic policy. The Treaty embraced a legal basis for Community action to form "Guidelines for Employment" which in time should be specified to individual national plans. A "target-orientated" approach to employment will form the basis of community monitoring and periodic review. Among the many measures within the Treaty for reducing employment, four key priorities have been identified in order to reduce the obstacles to employment which currently exist within European labour markets, namely:

- A reduction in the social charges on low wages. Social charges (unemployment insurance, sickness benefit etc) account for 35% of the labour costs within the EU. In the US the figure is 22%, whilst in Japan it is 18%. There is also substantial variation within Europe, with some nations such as France and Spain at the top of the scale (38% and 36% respectively) and others such as the UK at the bottom end (26%)

- A second priority identified by the Commission is to reduce the amount of red tape and bureaucracy associated with setting up businesses. Compared with counterparts in America, the average UK or French business start-up takes longer, costs more, and is beset by numerous administrative procedures and hurdles, all of which mitigate against business activity.

  It is true that the UK has more than other EU nations, relaxed the level of bureaucracy associated with new business start-ups. It has also gone further in terms of its approach to recruitment and redundancy in an attempt to encourage greater flexibility within the workforce. This, of course, is a controversial issue. As public finances become tighter, which is one of the key targets of economic convergence, greater pressure will develop to extend this trend further;

- A key challenge for the European labour market, and one which may prove to be the most stubborn obstacle to real convergence is the requirement to encourage greater geographical mobility in the European workforce. Currently only 3% of Europeans live in an EU country other than that in which they were born. Within the contemporary labour market, employees will require to be flexible both in terms of what they work at and where they work. This will obviously entail a radical re-appraisal of EU systems of education, vocational training and life-long learning. Central to this should be the encouragement amongst UK students and others to participate in EU exchange schemes such as Socrates and Leonardo in which language skills are strongly emphasised. Of course, such enhanced labour mobility opportunities within a European context may be hindered by lack of progress on tax harmonisation and social security systems.

- The fourth key objective is support for Lifelong Learning involving yet higher participation levels in Higher and Further Education and at the same time re-skilling and retraining opportunities for a flexible workforce.

4. The EURO and greater wage and price transparency

A widely-held view is that the creation of the EURO will make wage and price differences within the EMU more transparent than was previously the case. As a consequence of this greater transparency, wage (and price) differences will have to more accurately reflect differences in productivity between Member States.

This is a challenge for policy-makers and not least for trade unionists. Member States within the EURO area where wages are below the EU average cannot expect wage levels to increase dramatically without the consequence of higher unemployment. This will only be achieved over time as a result of improved labour productivity to a level close or above the current EU average.

The Amsterdam Treaty laid much emphasis on the enhanced competitiveness of EU economies within a globalised marketplace. Productivity increases play a central part in this process. Between 1974 and 1997-98 the growth of labour productivity averaged at a stable rate of 2% year-on-year. This was above the equivalent for both the US and the Japanese economies (at 0.7% pa and 1.9% pa respectively). Despite this, a dominant aspect of EU economic performance over this period was its poor employment growth and level, again compared with US and Japanese.

By 1997-98, the extent of EU Non-Employment was severe (18 million), representing 10.7% of the total Civilian Labour Force. From the mid-1970s on there has in fact been a five-fold increase in the unemployment rate as well as a very low ratio of effectively employed persons with respect to the working-age population. This so-called Employment Rate reduced from 67% in 1961 to approximately 60% currently. This compares unfavourably with rates of 70+% in the US and Japan. This significant decline is not solely explained by the impact of unemployment (its inverse). Explanations have to be sought elsewhere.

If greater labour market flexibility is achieved, the EU estimates that, in addition to the further likely increase in female participation, Employment Levels could again reach those levels witnessed in the early 1960s. It should, of course, be noted that the current (approximately) 60% Employment Rate actually corresponds to a rate of 55% in terms of full-time equivalent (FTE) as a result of the impact of part-time employment within the total.

The combined effects of Globalisation, the (permanent) impact of new technologies and the importance of the so-called knowledge-Economy within the EU context emphasises more than ever the importance of modern up-to-date training policies and programmes on the part of Member States. It has been estimated by EU economists that as much as 40% of the current total EU unemployed labour force can be referred to as cyclically unemployed (as opposed to structurally unemployed). These workers could, therefore, re-enter the active workforce with relatively little re-training, although there will undoubtedly be sector-specific bottlenecks preventing such a transition.

5. Implications of other EU Labour Market Policies (Social Charter and Minimum Wage Legislation)

Paqué (1997 P113) has argued........... "most elements of the Welfare State lead to an increase in labour costs, because collective bargains are unlikely to fully trade off wages for social benefits. Hence social harmonisation on a relatively high level is most likely to narrow the gap in wage costs between the centre of the Community and its periphery (Ireland, Scotland, Southern Italy, Portugal and Greece) and to widen unemployment rates......." He goes on to argue that this would lead to a perverse outcome, one in which the inter-regional structure of wages would become more "equal" but the structure of unemployment more "unequal". This, in turn, will require a reinforcement of Community financed regional policy (eg EU Structural Funds). Put crudely, the richer countries (and Regions) of Europe will have to pay for this greater harmonisation of social policy by funding a higher level of fiscal transfers to the poorer countries (and Regions) of the Community. This would apply to a far greater extent than in the past under mainstream regional aid programmes.

This will be the real test for the EU, namely whether individual Member States can arrive at a **"fiscal redistributionist"** consensus, when national and/or regional identify is strong in most Member States. Paqué (P115) makes the telling point that ... "Such a Fiscal Federalist system is likely to share the same fate..... it works as long as it is hardly needed – that is when income differentials are minimum and is simply swamped when income differentials become substantial"....

Comparisons of GDP per capita levels across EU Member States indicate that this may be a major obstacle to real progress in the harmonisation of policies in this sphere. Recent figures suggest that per capita income in the 2 richest EU countries Germany (pre-unification) and Denmark was more than 30% above the EU average. Per capita income within the three poorest EU countries Spain, Greece and Portugal was more than 40% (in Portugal's case 70%) below that average.

European labour markets are significantly varied on a number of different aspects. Such differences can be subsumed under the heading **Regulation.** Within the EU, the UK is the least regulated Member State and in recent years has become broadly comparable with the US and Japan.

Siebert (1997) has characterised these differences in the Regulatory environment under the following headings:

- Existence of minimum wage legislation
- Provision for extending collective wage agreements
- The existence of statutory works councils
- Strictness of dismissals laws (eg notice periods and severance pay rules)
- Restrictions on temporary work agencies
- Restrictions on working hours
- The existence of statutory paid vacations

For a range of EU Member States he conducted an analysis of the impact of the above regulatory differences using econometric analysis on a set of employment 'outputs', namely; labour force, self-employment, unemployment, employment growth, part-time and temporary work opportunities, GDP per capita, hourly compensation, growth in Earnings, and income distribution. Limited space prevents a full discussion of the findings, but what is clear is that the EU is divided into two camps – the **regulated** and the **de-regulated.** To focus on particular indicators, the author found that the more regulated a Member State, the slower is its growth in private sector employment, and the lower is the country's level of average earnings/income. Secondly, there is no empirical evidence to link the Regulation Index and Income Inequality. Thirdly, as regards unemployment inequality, the author found that unskilled relative unemployment has increased (especially during the 1980s) in the 4 countries examined (the UK, the USA, France and West Germany) and that there was no clear advantage ascribed to the more regulated Member States such as West Germany or France. The period covered in this study was up to the mid 1990s.

A specific conclusion regarding the Minimum Wage aspect was based on a correlation of minimum wage legislation and whether such legislation "bites" – i.e. the ratio of the minimum to manual worker wages in industry. The so-called **'minimum wage bite'** is least in such countries as Spain and the US at around 40% and strongest in Belgium, France and Portugal at approximately 70% (see Table 3).

The impact of the EURO (and more precisely EMU) to such trends is difficult to gauge. The need for structural reform of EU labour markets has already been mentioned (see also IMF 1998). Where the currency element will make a difference is to the extent that a single currency across the EU area will mean that Member States no longer have recourse to currency adjustments in order to smooth out market inflexibilities. Indeed, without the opportunity for currency adjustments, the need will be even greater for more flexible labour markets in order to allow countries to adjust to external shocks, particularly asymmetric shocks.

Of course, the structural bottlenecks which inflict the EU are multi-faceted – social benefit systems which yield poor incentives to work, tax systems which disincentivise workers, and as we have discerned above, excessive labour market regulation. A difficult task ahead will involve policies to decouple wage behaviour from local (i.e. national) labour market conditions. Recently, the EU has introduced labour market surveillance procedures designed to monitor annually national employment policies and to assess individual national performance in this regard. For example, particular attention will be given to the effects of such policies as the reduction in the working week in order to ensure that this is implemented flexibly and to prevent an increase in employers' labour costs. Leading EU trade unionists have recognised the pragmatism of such an approach, whilst recognising the limitation of existing knowledge on these effects especially in relation to a **Sector-by-Sector** analysis (Coldrick, 1997; see also OECD, 1997).

IMPACTS ON SCOTTISH LABOUR MARKET

The following section tries to draw out certain possible Gains and Losses which might accrue to the Scottish Labour Market in relation to the impact of the EURO, whether Sterling joins or not.

There are of course, certain distinguishing features of the Scottish Economy and Labour Market which a longer paper could highlight in greater depth. Suffice here to list some of these features as follows:

- There is a heavier dependence on the part of the Scottish economy compared with the rest of the UK to foreign inward investment. The sectoral and country breakdowns of such investments are of crucial importance as far as the impact of the EURO is concerned (see Hood in Peat and Boyle 1999).

  Scotland attracts a higher share of inward investment than its relative share of UK GDP might predict. Hood (P44) argues that over the period 1991-1997 this averaged between 15% and 20% of the UK's annual total (manufacturing and non-manufacturing combined).

  The Sectoral breakdown of such inward investment is also of relevance. Foreign companies are especially prominent in Food and Drink, Chemicals and Petroleum Products and Electrical and Electronic Products. Of course, as Hood points out, electronics has been the pre-eminent sector as far as manufacturing inward investment is concerned, with in excess of 200 different manufacturing companies employing 46,000 people (1 in 7 Scottish manufacturing employment) and 80% of output exported. A further 400 software and services companies employ 15,000 people in Scotland. In total, 64% of all employment in electronics manufacturing in Scotland is based in the subsidiaries of multi-national enterprises of which 51% are in US MNE's.

- There is a continuing concentration of Scottish exports among a small range of products or sectors. The 1999 Annual Report of the Scottish Council for Development and Industry (SCDI) indicated that 3 sectors – Whisky (11%), Electronics (58%) and Chemicals (9%) – accounted for more than 75% of Scotland's total exports during 1999. Since a large proportion of these sectors are controlled by overseas institutions (especially in Electronics), this leaves the Scottish economy and labour markets particularly vulnerable to investment policies in such companies. To the extent that a large proportion of these companies have origins outwith Europe (North America and Asia-Pacific – 28% and 10% of all foreign direct investment projects respectively in 1997) compared with 17% for Europe, suggests that the impact of Sterling's membership of the EURO will be hard to predict. The other side of this coin is the point that based on these figures the single currency, as such, cannot be expected to yield significant inward investment benefits from other EU countries given the dominance to date of non-EU inward projects.

- To counter this, the EU, according to the SCDI Report increased its share of Scotland's total exports – 63% in 1999 (compared to 61% in 1998). The top 3 export markets for Scottish products during 1999 were: France (27%), Germany (18%) and North America (11%). Sterling's appreciation against the EURO during 1999 has according to the Report, produced a "plateau" effect in Scottish exports.

- Of crucial importance to the Scottish economy is the Financial and Business Services Sector (Banking, Insurance, Legal, Accounting etc) which accounts for approximately 19% of the total Scottish GDP and 250,000 in employment (Wood in Peat and Boyle op cit). Fund management and insurance are of particular significance with the former being the key centre outside London. Wood (ibid) also shows that Financial and Business Services account for approximately 10% of total employment within Scotland and together provided nearly 50% of all new jobs created in Scotland between 1985 and 1997.

  As far as the EURO is concerned, this sector can be expected to benefit from Sterling's membership. This is so because European wide Mergers and Acquisitions (M & A) activity during 1999 showed an upward trend. This is likely to continue in response to the lower transactions costs of the single currently in the financing of European-wide mergers. Edinburgh, as a major fund management centre, could be a major beneficiary of such trends.

In the light of this, the Scottish Labour Market would be affected in quite contradictory ways as a consequence of Sterling's membership of the EURO. Some of these effects would not be unique to the Scottish Economy but would be UK-wide. A key question for the Scottish Economy is whether the EU, (if the EURO-Zone is to succeed), can be expected to offset or compensate for some of the potential losses that may occur if there is a decline in Foreign Inward Investment into the UK and Scotland. The latter would particularly affect the Scottish Economy with its heavier reliance on Inward Investment.

The other side of this issue is that such Inward Investment would probably continue to take place anyway on its previous scale, given that the EURO would simply replace Sterling as the appropriate currency for trading purposes on the part of US and other investors. The key issue, therefore is whether the EURO will over the long run be more stable than Sterling (see Table 4).

CONCLUSIONS

This paper has attempted to consider some of the possible effects of the creation of the EURO on the Scottish Economy and Labour Market. Although tentative, it has highlighted some of the conflicting possible scenarios open to the Scottish Economy as a consequence of the EURO. It is impossible to be prescriptive as to the likely effects on the Scottish Labour Market since for every gain to be derived from membership of the EURO there appears to be a corresponding loss. Some particular sections of the Scottish Economy, for example electronics and computers given their heavy dependence on non-EU investment may be adversely affected by a decision to join the EURO. However, a clear conclusion of this paper is that it is not the EURO per se which matters in this debate, but whether or not the much-heralded gains of the EURO in terms of macro-economic convergence and more flexible labour and product markets will be realised. Moreover, there is a clear need for economists and policy-makers to carefully monitor such trends as the UK prepares for its referendum on the EURO in 2001 and possible membership in 2002/3. Additionally, focus should be directed to examining the potential effects on a Sector-by-Sector basis, since the precise configuration of these possible gains and losses may affect different sectors of the Scottish Economy differently.

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APPENDIX

TABLE I

Nominal long-term interest rates – Annual data

Dec.97 – Nov.98	%
EU 15	5,1
EUR-11	4,8
B	4,9
DK	5,1
D	4,7
EL	8,8
E	5,0
FR	4,8
IRL	4,9
I	5,0
L	4,8
NL	4,7
A	4,8
P	5,0
FIN	4,9
S	5,1
UK	6.2

Source: Eurostat, November 1999

TABLE 2

euro-zone	EU15	B	DK	D	EL	E	FR	IRL	I	L	NL	A	P	FIN	S	UK
Harmonised indices of consumer prices																
euro-zone	EU15	B	DK	D	EL	E	FR	IRL	I	L	NL	A	P	FIN	S	UK
1.6	1.1	1.0	1.9	0.5	2.4	2.1	0.5	2.3	1.6	0.9	2.0	0.4	2.3	1.2	0.5	1.4
Harmonised unemployment rates																
euro-zone	EU15	B	DK	D	EL	E	FR	IRL	I	L	NL	A	P	FIN	S	UK
9.8	9.0	8.7	:	9.1	:	15.4	10.5	6.0	:	2.6	:	4.4	4.7	10.0	6.6	4.7
General government gross debt (total in % of GDP)																
euro-zone	EU15	B	DK	D	EL	E	FR	IRL	I	L	NL	A	P	FIN	S	UK
73.7	69.3	118.2	58.0	61.1	106.3	65.1	58.8	49.5	118.7	6.9	67.5	63.0	57.8	49.7	74.2	48.7
General government deficit (total in % of GDP)																
euro-zone	EU15	B	DK	D	EL	E	FR	IRL	I	L	NL	A	P	FIN	S	UK
-2.0	-1.5	-0.9	1.0	-2.0	-2.5	-1.7	-2.9	2.4	-2.7	2.5	-0.7	-2.2	-2.2	0.9	1.9	0.5

Source: Eurostat, November 1999

TABLE 3

Wage Regulating Framework

	Minimum wage (ratio to manual wages in industry, 1993)
Belgium	Yes (69%)
Denmark France	No Yes (73%)
Germany	No
Greece	Yes (57%)
Ireland	No
Italy	No
Netherlands	Yes (60%)
Portugal Spain	Yes (70%) Yes (40%)
Sweden	No
UK*	No – except for agriculture
Japan	Yes (53%)
USA	Yes (37%)

* This data obviously precedes the UK's recent adoption of the Minimum Wage.

Source: Adapted from Siebert (1997, p 230)

TABLE 4 THE EURO-POSSIBLE GAINS AND LOSSES

STERLING 'IN'	STERLING 'OUT'
<u>GAINS</u> (+) 1. <u>CONVERGENCE BENEFITS</u> (LOW INFLATION) (FALLING PUBLIC SECTOR DEFICIT) (CURRENCY STABILITY) (LOWER INTEREST RATES) 2. <u>FINANCIAL SECTOR BENEFITS</u> (SINGLE CAPITAL MARKET GAINS) (STRONG MERGERS& ACQUISITIONS EFFECTS – BENEFITS TO SCOTLAND)	<u>GAINS</u> (+) 1. <u>BENEFITS OF UK DE-REGULATION</u> (FLEXIBLE LABOUR MARKETS) (FALLING TAXES) (INCREASED BUSINESS START-UPS) 2. <u>USE OF CURRENCY AS POLICY INSTRUMENT</u> (INDEPENDENCE FROM EUROPE ON INTEREST RATES) (HIGH EXPORT COMPETITIVENESS) 3. <u>SAFE HAVEN BENEFITS</u> (HIGH LEVEL OF INWARD FOREIGN INVESTMENT TO UK ESPECIALLY FROM US AND OTHER NON-EU ECONOMIES) (LOW NON-WAGE COSTS VIS-À-VIS EU)
<u>LOSSES</u> (-) 1. <u>POSSIBILITY OF 'WEAK' EURO</u> (INTEREST RATES INCREASE) 2. <u>PUBLIC SECTOR DEFICITS INCREASE</u> (TO FINANCE INTER-REGIONAL TRANSFERS) 3. <u>INFLEXIBLE EU LABOUR MARKETS</u> (HIGH NON-WAGE COSTS) (LOW EMPLOYMENT GROWTH) (INCOME DISTRIBUTION EFFECTS) 4. <u>SECTORAL EFFECTS</u> (SCOTLAND, PARICULARLY VULNERABLE) 5. POSSIBLE STERLING DEVALUATION ON ENTRY (INFLATIONARY EFFECTS)	<u>LOSSES</u> (-) 1. <u>STRONG EURO-ZONE</u> (LOSS OF BENEFITS FROM STABLE EURO) (LOSS OF STRONG INTRA-EU TRADE GROWTH) 2. <u>STRONG EURO</u> (STERLING MARGINALISED – BECOMES EASY TARGET FOR SPECULATIVE ATTACKS)