University of Strathclyde Glasgow

# 40

# FORTY TURBULENT YEARS

## How the Fraser Economic Commentary recorded the evolution of the modern Scottish economy

FRASER OF ALLANDER INSTITUTE

**Alf Young**
Visiting Professor,
International Public Policy Institute,
University of Strathclyde

# Table of Contents



Alf Young, Visiting Professor,
International Public Policy Institute, University of Strathclyde

# PREFACE

WHEN the University of Strathclyde's Fraser of Allander Institute, together with its Economic Commentary, was first launched in 1975, its arrival was made possible by substantial philanthropic support from a charitable foundation that bore the Fraser family name. The Fraser Foundation (now the Hugh Fraser Foundation) continues to dispense support to deserving causes to this day.

It represents the lasting public legacy of one of post-war Scotland's major men of commerce. Hugh Fraser - Lord Fraser of Allander - created the House of Fraser department store empire, incorporating as its flagship emporium the up-market Harrods in London's Knightsbridge. And through his commercial holding company, Scottish & Universal Investments or SUITs, Fraser controlled many other diverse Scottish businesses from knitwear production to whisky distilling.

In 1964, after a titanic takeover battle with Roy Thomson, the Canadian-born owner, since the 1950s, of the Scotsman newspaper and the commercial Scottish Television franchise, the soon-to-be-enobled Fraser, through SUITs, took control of Outram, publisher of The Glasgow Herald and a stable of local Scottish newspapers. But two years later the new press baron was dead, struck down by a heart attack at the age of 63.

Control of Fraser's commercial empire passed to his son, who disclaimed his father's peerage and became Sir Hugh Fraser. The younger Fraser embraced his father's philanthropic instincts and it was under his aegis that backing for the Fraser of Allander Institute (FAI) and its Economic Commentary was forthcoming in 1975.

However Sir Hugh's corporate inheritance progressively overwhelmed him. By the end of the 1970s, SUITs was in the hands of Tiny Rowland's Lonrho. Control of House of Fraser eluded Rowland, however. Government saw to that. The store chain, including Harrods, was bought by the Al-Fayed brothers in 1985. Two years later Sir Hugh Fraser died of lung cancer. He was just 50 years old.

The turbulent business careers of the Fraser of Allander Institute's original benefactors mirror the tempestuous currents that have continued to flow through the Scottish economy and that the FAI and its Economic Commentary were set up to record and analyse.

By 1975 that economy was being buffeted by two conflicting sets of forces. Older industries, in which an earlier Scotland had excelled, were under increasing competitive strain. Shipbuilding, for instance, was in deepening jeopardy. On Clydeside, the Upper Clyde Shipbuilders experiment had, by the beginning of that decade, led to the UCS work-in. Now state control, on a UK-wide scale, of all major shipbuilding, loomed.

Yet 1975 was also the year the first oil from under the North Sea was being brought ashore. Rig construction sites were popping up all round Scotland's coastline. A new state-sponsored development agency covering all Scotland south of the highland fault was launched. The Scottish Development Agency mirrored another initiative, ten years earlier. The Highlands and Islands Development Board (HDB) had been charged with injecting a fresh dynamic into the economic prospects for Scotland's dispersed northern and island communities.

The SDA and the HIDB were designed to build on earlier attempts by successive governments to kick-start post-war regeneration and development. Between 1947 and 1966 five new towns were designated across central Scotland, amalgams of new housing for those escaping the old industrial slums and factories fit to house modern industrial enterprises like NCR, Ferranti, Honeywell, Burroughs and IBM, many of them riding a boom in US investment into war-torn Europe.

By 1975 some earlier iterations of such state-sponsored interventionism were already in trouble. Attempts by the two Wilson governments a decade before to bring volume car assembly to Linwood and aluminum smelting to Invergordon were already unravelling. By the start of the 1980s both would be gone.

Both coal-mining and steel production across the UK had been nationalised decades before shipbuilding. But it would not be long before tensions between the unions in both industries and the Thatcher government first elected in 1979 would lead to outright industrial conflict, a return to private ownership and a long lingering death of almost all their remaining productive capacity.

The post-war investment boom from America in more modern electro-mechanical industries was, in part, brokered by a remarkably-inclusive body, the Scottish Council for Development and Industry. SCDI brought industrialists and financiers, trade unionists, politicians and local councillors together in a shared sense of purpose as to how to rebuild Scotland's economy.

From the mid-seventies onwards, successive UK governments and their development agencies sought to build on that earlier success by trying to lure investment in the emerging digital technologies into Scotland. They came, not just from the US, but, increasingly from the Far East too. There were some big hits. But the longevity of many of these inward investments proved much shorter than their predecessors in the 1940s and 50s.

That sense of running to stand still was compounded by the loss, through acquisition, of many indigenous quoted Scottish companies. And by the modest achievements of successive government sponsored initiatives to foster more of an appetite among Scots themselves for entrepreneurship and creating new generations of Scottish businesses.

The great crash of 2008/09 led to Scotland's two oldest banks, Bank of Scotland and Royal Bank of Scotland, taking massive injections of UK taxpayer support to survive. Seeing three centuries of relative commercial success shredded in a matter of months has shocked most Scots to the core. Watching a volatile global oil price tumble below $30 a barrel, with all that means for jobs and investment in the North Sea, compounds current gloom in the sector.

For forty years the Fraser of Allander Economic Commentary has charted what impact these conflicting tides are having on the resilience of the Scottish economy and the prosperity of Scotland's people. It's been my privilege to review what's been said by FAI economists about that unfolding story between 1975 and 2015. That story in full is now available in an online university archive.

What I found was captured in three long pieces I wrote over the past year, all of which first appeared in the three 2015 editions of the Commentary itself (Vol. 38, No.3 to Vol. 39, No. 2). They are gathered together here in a single volume. It concludes with a short postscript, considering the kind of opportunities and challenges the Scottish economy may face over the next forty years.

# **Part 1:** 1975 – 1990: Inflation, intervention and the battle for corporate independence

The recent economic history of Scotland, its performance and place within the UK and international economy can be traced through the pages of the Fraser of Allander Economic Commentary. Created in 1975 by a private bequest from Sir Hugh Fraser, a prominent Scottish businessman, the Fraser of Allander Institute has provided a continuous commentary on the economic and related policy issues facing Scotland over the period. In this the fortieth anniversary of the Fraser of Allander Institute, this is the first of three articles which charts Scotland's transformation from an economy significantly based on manufacturing (and mining) to one that saw rapid deindustrialisation (in terms of output), the discovery of oil and the rapid transformation of its business base with the impact of both merger and acquisition (M&A) activity as well as the varied impacts of successive governments' industrial and regional policies.

When the Fraser of Allander Economic Commentary first appeared, in quarterly installments, in July 1975, the Scottish economy it set out to analyse was very different, in texture and tone, from the one it continues to appraise, now in its fortieth consecutive year. Then UK inflation was going through the roof. From May to November of 1975 the then-benchmark RPI measure of UK price inflation was consistently running at an annualised rate of 25% or above. Indeed inflation stayed in double digits for much of that decade and on into the early Thatcher years. At the start of this anniversary year, with the now-core CPI inflation measure reaching an all-time low of 0.3%, the fear stalking policy makers is not of hyper-inflation and the kind of wage-price spiral that led to the "winter of discontent" in late 1978, but of the kind of deflationary spiral that has gripped Japan for much of the past quarter century and currently stalks the Eurozone.

Nowadays the performance of Scotland's labour market broadly mirrors that of the UK as a whole. Ministers in Edinburgh vie with London, when the monthly jobs figures come out, to lay claim to any marginal out-performance they can find. In the 1970s the differentials were starkly negative. Thanks to its heavy exposure to traditional manufacturing capacity, by then in serious decline, Scotland's unemployment rate typically outstripped the UK rate by a very large margin. The very first Fraser Commentary noted that "the unemployment percentage in Scotland fell from an average of more than twice the UK rate in 1964 to a ratio of 1.7 in 1973." It then noted that "by November 1974 the Scotland/GB rate had fallen to 1.48, the

Alf Young, Visiting Professor,
International Public Policy Institute, University of Strathclyde

lowest figure recorded since 1954." Had there not been massive net out-migration from Scotland in the fifties and sixties, one wonders how much bigger these adverse Scotland/ UK unemployment ratios might have been in that period. Between 1951and 1971, net out-migration from Scotland totalled 606,500.

One feature of the Scottish economy has been a constant thread though the past forty years. Oil. Less than a month after the second Fraser Commentary appeared, on 3 November 1975, Her Majesty the Queen pressed a gold-plated button in Dyce, sending the first crude from BP's Forties field from its landfall at Cruden Bay, by pipeline, to Grangemouth. Now, with the recent slump in the global oil price and Shell announcing plans to dismantle another iconic North Sea system, Brent, which lent its name to a global benchmark crude, all the talk is of the beginning of the end for the North Sea, if drastic fiscal action isn't taken. The story from there to here has provided a continuous stream of material for debate, from whose oil it is anyway to the capacity of indigenous Scottish businesses to capitalise on the opportunities exploiting hydrocarbon reservoirs off our shores presented.

Throughout, the fluctuating price of oil has been an ever-present and challenging reality. In 1973, in protest at the United States arming Israel in the Yom Kippur war, Arab states first imposed a supply embargo and then started hiking the global price of oil. By March 1974 the barrel price had quadrupled, from $3 to nearly $12. There was a stock market crash as recession bit. In the UK these problems were exacerbated by what came to be known as the Barber boom. In his 1972 Budget, Edward Heath's chancellor Anthony Barber delivered a tax-cutting package designed to ensure the Heath government's re-election. He certainly stimulated an intense burst of growth. But the electorate, in February 1974, returned a minority Labour government led by Harold Wilson. That very first Fraser commentary was blunt in its assessment of the Barber boom and its likely consequences.

"The UK has been almost alone amongst industrialised countries in continuing to expand domestic demand, maintaining this expansion by means of heavy external borrowing," (Vol. 1, No. 1) it argued. "A comparatively lower rate of unemployment has been achieved at the cost of an alarming and accelerating rate of inflation and deteriorating price competitiveness. However while the necessary readjustment of the domestic economy has been postponed, it cannot be avoided."

How right they were. Within months of being elected the minority Labour government had gone back to the voters, to be voted in again with a wafer thin majority. Harold Wilson resigned unexpectedly in March 1976. Jim Callaghan replaced him as prime minister. By that November, Callaghan's chancellor, Denis Healey, had had to go to the International Monetary Fund, seeking a loan and submitting the UK's finances to IMF supervision. Distant echoes of the position facing the current Greek government; though its financial plans are now overseen by the 'troika' of the IMF, European Central Bank (ECB) and the European Commission.

There was a second significant surge in global oil prices at the end of the 1970s. When the Shah was ousted in Iran in 1979 and through into 1980, when the Iran-Iraq conflict started, OPEC pushed the global price higher still. In its October 1980 commentary, the Fraser of Allander Institute estimated that a 130% oil price hike would lead to an accumulated loss of output in the industrialised countries of around 5% by the end of 1981 and would add an additional 11% to consumer prices. It expected the United States and the United Kingdom to experience absolute falls in output. "Both in deeds and words, the leaders of the western countries have made it clear that, given an apparent choice between greater inflation and greater unemployment, they have chosen greater unemployment," (Vol. 6, No. 1) the commentary warned.

When Margaret Thatcher's first chancellor, Geoffrey Howe, unveiled his 1981 budget the following March, the Fraser authors found they had under-estimated just how uncompromising his approach would be. This was the mirror image of the Barber boom budget. Having pushed up VAT to 15% and added 10p to the cost of a gallon of petrol in his first budget in June 1979, Howe now froze personal tax thresholds and allowances and whacked a further 20p on the cost of a gallon of petrol. The April 1981 commentary called the measures "ill-advised and their claimed justification - the restoration of order to the public finances - highly questionable." (Vol. 6, No. 4)  Its authors were not alone.

A group of 364 academic economists across the UK wrote to The Times[1], claiming Howe's measures had "no basis in economic theory" and would threaten the UK's "social and political stability". Among them was Mervyn King, later destined to become Governor of the Bank of England. A fierce debate has raged ever since. Howe's supporters claim his approach did indeed tame inflation, leaving it at more subdued levels ever since. But the price that continues to be paid is, as the Fraser team foresaw, much higher average levels of joblessness in the UK economy than existed in the previous quarter century pre-1981.

Higher global oil prices had a significant impact on the UK's public finances. It has been argued that, without that offshore bounty, the Thatcher government might never have been able to finance the consequences, in terms of rising unemployment, of that controversial Howe budget in 1981. Revenues from UK oil and gas production grew steadily from 1980, peaking in 1984/5 and 1985/6. Then, having risen so high in the previous decade and a half, the oil price itself fell sharply again. Inevitably government revenues from oil and gas

[1] Including University of Strathclyde economists R. G. Brooks, Professor A. I. Clunies-Ross, K. Hancock, J. Sconller and P. Wanless – Philip Booth (Editor) Were 364 Economists All Wrong?, Institute for Economic Affairs, 2006

fell dramatically too. At 2009/10 prices, revenues peaked at £35bn in 1984/5. Two years later revenues had fallen in value by two-thirds. The November commentary in 1986 carried an article entitled 'The Oil Price Collapse: some effects on the Scottish economy' (Vol. 12, No. 2). It was written jointly by a member of the Fraser Institute's staff, Jim Walker, and the oil economist at The Royal Bank of Scotland. An 11.5% fall in world oil demand and a substantial rise in non-OPEC production had put pressure on the oil price. The dollar barrel price had virtually halved since the start of the year. The paper suggested that, while lower oil prices might be good for global growth, "Scotland would seem to be a clear loser in that group of oil exporting states and oil related industries which are feeling the immediate and adverse impact of the oil price collapse on output and employment."

The RBS oil economist who, with Walker, penned that warning was Alex Salmond. It was his only contribution to the Fraser Economic Commentary. Nearly thirty years later, having been Scotland's first minister for more than seven years, leading his country to an independence referendum, Salmond has now stepped out of government. As he did so the global oil price was again on the slide. Having virtually halved in just four months, Scotland is once more facing that challenge to output and jobs. Only this time the North Sea province is much more mature and the prospects for ongoing investment much more problematical. Oil has indeed been a continuous thread in forty years of Fraser commentaries.

When the first one appeared in 1975, the Scottish economy was already facing many, much-older, industrial challenges. Its coalfields, nationalised under the UK-wide National Coal Board in 1946, were struggling to stay competitive. Miners were fighting for wages that could keep pace with rampant price inflation. In 1972 they called their first official strike since 1926. A second followed at the start of 1974. On both occasions the Heath government's response was to declare a state of emergency and implement a three-day week. The lights went out. Electricity was strictly rationed. Faced with that second strike, Heath decided to go to the country to seek a fresh mandate. But the electorate returned a minority Labour government which promptly settled with the NUM (National Union of Mineworkers).

Fast forward to the 1980s and the explosive issue dividing miners and government turned from wages to pit closures. The incoming Thatcher administration backed down, in 1981, over plans to close 23 pits. But as we now know from her own biographer Charles Moore, one of the first things she did on taking office in 1979 was to tell her deputy Willie Whitelaw "The last Conservative government was destroyed by the miners' strike. We'll have another and we'll win." By 1981 the logistics and planning for ensuring that victory - stockpiling enough coal; mobilising police strength in coalfield areas - were not yet in place. By 1983 she had brought a Scot, Ian MacGregor, over from America to run the National Coal Board. He had privately put a massive pit closure programme back at the top of his agenda. A bitter, protracted battle with the miners, now led by Arthur Scargill, was almost inevitable. It lasted a year and left the NUM defeated, demoralised and divided. Thirty years on from that March 1985 denouement, the three remaining deep mines in the UK (none of them in Scotland) are due to shut over the next two years.

The long decline in shipbuilding in Scotland and the rest of the UK has followed a shallower trajectory. Arguably production of ships reached its peak across these islands in the first decade of the 20th century. Had it not been for two world wars marine engineering might have emulated coal's rapid endgame.  As it is ships are still being built on the Clyde, mainly for the Royal Navy. The latest, two massive aircraft carriers, are actually being assembled in huge modules at yards around the UK, then brought by barge to Rosyth on the Forth, for final assembly. When the Fraser commentary series began, there were still hopes of maintaining a viable merchant shipbuilding capacity in Scotland and across the rest of the UK.

On the Clyde, the Geddes-inspired restructuring of the late sixties foundered with the liquidation of Upper Clyde Shipbuilders in 1971, barely three years after five major shipbuilders on the upper river had amalgamated. The iconic work-in that followed, led by the late Jimmy Reid, served the workers in the yards more productively than Arthur Scargill's mortal combat with Margaret Thatcher a decade later. In 1977 what was left of UCS, together with the Scott Lithgow grouping on the Lower Clyde and numerous other yard groupings around Britain were merged into state-owned British Shipbuilders, headquartered in Newcastle. In the merchant yards the mismatch between order books and production capacity persisted. By the end of 1982, British Shipbuilders had closed half its yards.

New legislation by the Thatcher government the following year ensured the remaining yards would be privatised once more. On the Clyde, Govan Shipbuilders became part of the Norwegian-owned Kvaerner group and the naval shipbuilder Yarrow became part of GEC's Marconi division. Together they now constitute the naval ships arm of BAE Systems Maritime. On the Lower Clyde the small Ferguson yard survives (after a recent buy-out by the Scottish industrialist Jim McColl's Clyde Blowers Capital), building ferries for the Scottish government and hoping for orders from the offshore and renewables sectors.

It wasn't just the historic bedrock of Scottish industry, like coal and shipbuilding, that was facing tumultuous times during these first fifteen years of Fraser commentaries. Singer, the American corporation that then dominated world sewing machine manufacture, first came to Clydebank in the mid-1880s. It built a production complex so vast it had its own distinctive clock tower and dedicated railway halt. By 1980 it was closing its gates for the last time. Tractor manufacturer Massey-Ferguson came to Kilmarnock in 1948, but departed in 1978. British Aluminium opened a large smelter at Invergordon on the Cromarty Firth in 1971, only to close it at Christmas 1981. Diverse industries across Scotland, with life cycles a long as a century and as short as a decade, all falling like ninepins by the end of the 1970s.

There were others. The giant car plant at Linwood. The pulp mill in Lochaber. The BMC/ Leyland truck and tractor plant at Bathgate. The strip steel mill at Ravenscraig. All now gone. Some forever enshrined in the Proclaimers' plaintive lament Letter from America. Only Ravenscraig kept producing into the 1990s, finally closing in 1992. In a commentary piece in 1982, reflecting on why such plants had been sanctioned and financially supported by the state in the first place, David Simpson was blunt "Their establishment and location was dictated by political, and not by economic, considerations. Since, in the modern world, change is continuing, closure of such uneconomic plants was only a matter of time" (Vol. 7, No. 3).

Post-war regional policy was certainly deployed by governments, regardless of the party in power, to persuade companies to invest in some of the least economically dynamic parts of the country. The system of industrial development certificates, introduced by the Atlee Labour government in 1947, was used enthusiastically by the Macmillan Tory government in the early 1960s to persuade Lord Rootes, against his own instincts, to locate his Hillman Imp plant at Linwood, rather in the West Midlands. Harold Wilson, when prime minister, certainly lent on British Aluminium to build a new smelter at Invergordon.

But other major investment decisions can be traced more to heritage and personal connections. The American Singer Corporation brought its sewing machine plant to Clydeside because the executive charged with taking the decision was an emigrant from Clydebank. Alfred Yarrow, having outgrown his existing site, brought his burgeoning shipyard to Scotstoun in Glasgow from Poplar in London in 1906, having advertised around the UK for a new home for his yard. He even persuaded many of his existing workforce to make the move with him and built homes around the yard in Scotstoun to house them. And Thomas J Watson, the founding father of what came to be known as IBM, though born in America was from Scottish emigrant stock. His friendship with the then Secretary of State for Scotland, Hector McNeil, helped ensure IBM's first major European manufacturing plant came to Greenock in 1951. McNeil was Greenock's MP at the time.

In 1975, Labour, led by Harold Wilson, tried to reformulate the way government nurtured economic activity in Scotland by creating the Scottish Development Agency. The SDA was charged with furthering economic development; providing, maintaining or safeguarding employment; and promoting industrial efficiency and international competitiveness. It could invest directly in businesses (taking on the powers created for the National Enterprise Board in Scotland and paving the way for SDA's engagement in Scotland's nascent 'hi-tech' sector). SDA became Scotland's biggest industrial landlord and had widespread powers over derelict land clearance and urban renewal. It took over from the Scottish Council the task of luring more IBMs to Scotland's shores. In the jargon, inward investment. Its initial budget of £200m matched its wide-ranging powers.

The October 1974 general election had sent eleven SNP MPs to Westminster, most from Tory-held constituencies, on the slogan: It's Scotland's Oil. Labour's creation of the SDA was widely seen as a political ploy by Wilson and his Scottish Secretary Willie Ross to blunt that nationalist charge. Labour had, of course, created a template for the SDA a decade earlier, in 1965, when it launched the Highlands & Islands Development Board, with a radical mandate to revitalise the economy of the fragile North of Scotland. But while the HIDB drew strength from the less partisan nature of politics above the highland fault line, the advent of the SDA breached the old cross-party consensus on regional policy that had flourished in the fifties and sixties. The SDA became something of a political and ideological football.

It wasn't that conservatives, even those led by Margaret Thatcher from 1979, were consistently hostile to state intervention when markets looked like doing things they'd rather they didn't. At the start of the 1970s, when an insolvent Rolls Royce went into receivership, Ted Health nationalised it to secure its future. The next Tory to enter Downing Street as prime minister faced a similar challenge. With a similar result. When the Glasgow-based engineers, the Weir Group, chaired by Viscount Weir, got into serious financial difficulties in 1981, the SDA was prevailed upon to participate in a rescue package.

And in the same year, when the Royal Bank of Scotland board was minded to accept a takeover bid by the London-based Standard Chartered Bank, only to find itself on the receiving end of a much-higher hostile bid from the Hong Kong and Shanghai Banking Corporation, Mrs Thatcher's Scottish ministers went public on their hostility to both bids and helped ensure the Monopolies and Mergers Commission threw both of them out. As a memorandum from Professors McGilvray and Simpson to the MMC in the July 1981 edition of the commentary put it: "In terms of market capitalisation, the Royal Bank is the second largest company with its head office in Scotland. It is not putting it too strongly to say that if the Royal Bank goes, it will the beginning of the end of the indigenous private sector in Scotland, with all which that implies for the regeneration of Scottish industry." (Vol. 7, No. 1).

One of the dominating features of that whole decade was the wave of takeovers of major private sector players in the Scottish economy by rival businesses. Having fended off a takeover bid from Tiny Rowland's Lonrho in 1981, thanks to another MMC veto, the department store chain House of Fraser was sold to the Al Fayed family in 1985. Harrods is now owned by the Qatari royal family. The rest of the chain, having passed through Icelandic hands, is now in Chinese ownership. In 1983 South African-based Charter acquired mining equipment maker Anderson Strathclyde, based in Motherwell. Britoil, which started life in 1975 as the state-owned British National Oil Corporation, was privatised in two stages by the Thatcher government, first in 1982, then in 1985. Just three years after that floatation of the fourth biggest oil and gas producer in the North Sea was completed, it was acquired by BP. In 1986 the Glasgow-based thread maker Coats Paton was taken over by David Alliance's Viyella group.

The messiest of the 1980s takeover wave engulfing Scotland's private sector hit the whisky sector. In 1984 the Irish brewer Guinness launched a surprise takeover bid for the Perth-based whisky distiller Arthur Bell. Having swallowed Bells, it then downed the much-bigger Distillers Company, home to a whole family of well-known brands of Scotch. Distillers accepted the embrace of the Ernest Saunders-led Guinness, rather than succumb to the mercies of the Argyll Group supermarket chain, led by the upstart Jimmy Gulliver. The outcome split the Scottish business establishment. The then governor of the Bank of Scotland Sir Tom Risk and a leading Edinburgh lawyer Sir Charles Fraser had agreed to serve with Saunders on the enlarged United Distillers group board. But when promises made to them weren't kept, the flak began to fly. Saunders and three others were subsequently charged with fraudulently manipulating the Guinness share price to win the battle for Distillers. Saunders served ten months of a thirty month sentence in an open prison.

The fear expressed by McGilvray and Simpson over the fate of the Royal Bank, that its loss of independence would spell "the beginning of the end of the indigenous private sector in Scotland" was widely shared at the time. There was sustained debate, even in boardroom and professional circles, about what kind of protectionist measures might stem the tide and retain more headquarters control in Scotland. Could some kind of tartan ring-fence, enforced by the competition authorities, be erected? But as we will see, in later stages of this three-part story, that trend was not reversed. Indeed it spread to areas like finance and professional services. And the Scottish bank that was saved from itself in 1981, RBS, ended up going on a massive takeover spree of its own that plunged it into a near-death experience.

The Thatcher government's comparative pragmatism over intervening directly in markets, as it did over the possible collapse of the Weir Group and the Royal Bank's corporate independence did not extend to buying in to its Labour predecessor's vision of the role of the fledgling SDA. At the start of 1980 more restrictive guidelines were issued on when the Agency could invest directly in businesses and in what form – and dropping its Labour-inspired aim to extend trade union representation in Scottish industry. The following year the business of attracting more foreign direct investment into Scotland was hived off to a new joint SDA/Scottish Office agency Locate In Scotland. In the latter half of the decade, the SDA was told to sell off its large industrial property portfolio and leave more of the task of housing Scotland's industries to the commercial property sector. In between there was a select committee inquiry and various National Audit Office and HM Treasury trawls to keep the SDA on its toes.

The vast Glasgow Eastern Area Renewal project (GEAR), coordinated by the Agency – at the Government's direction - and launched the year after the SDA was up and running, was allowed, under the Tories, to complete its ten-year journey. However the fact that it has taken a project of the scale of last year's Commonwealth Games to revisit the physical regeneration of much of that same area of Glasgow's East End speaks volumes about how difficult it is to renew economic vitality in physically run-down inner city areas. The creation of Locate in Scotland had a positive impact on the flow of inward investment to Scotland, notably the steady stream of electronics ventures coming to swell the residents of Scotland's 'Silicon Glen'. Some, of course, had been coming long before that. There was a wave in the 1940s and 1950s. Ferranti, IBM, Burroughs, Honeywell, NCR. Motorola brought its first chip plant to East Kilbride in the 1960s. National Semiconductor brought another to Greenock in the 1970s.

But the wave of plants that opened in the 1980s, mainly in Scotland's New Towns, many assembling the hardware for the first generations of desk top computers, seemed to herald a new industrial dawn. Sadly, thanks the speed of innovation in the technology and the emergence of even lower-cost locations to do such work, notably in Eastern Europe and the Far East, it was to prove a transient boom.

Attempts were made to attract other emerging technologies. In 1985, to much fanfare, Damon Biotech was supposed to be coming to Livingston, with $40m of investor backing, to build the biggest monoclonal antibody plant in the world. It did not happen. Risk is, of course, unavoidable for any national development agency, seeking to replace outmoded industries with tomorrow's growth businesses. But, by the late eighties, it was becoming clearer that the Thatcher government had never quite forgiven the SDA for being Labour's initiative. Its death knell was sounded in 1988 when a Tory supporting businessman Bill Hughes came up with a new model - a network of enterprise agencies with strong business representation that would not only reignite Scotland's entrepreneurial spirit but take over responsibility for skills training too. How Scottish Enterprise came to be, forms part two of this series.

And how did the state of the Scottish economy look as the first fifteen years of the Fraser commentaries drew to a close? I'll leave the last word to Dr John Hall TSB Scotland's Treasury Economist. In his economic briefing in the last issue of 1989 (Vol. 15, No. 2) he writes "Companies, already faced with a burgeoning financial deficit and a squeeze on profits and liquidity, may then be forced into a period of intense labour shedding, thus tipping the economy towards recession. The intensity of pressures in the labour market have once again raised the spectre of stagflation, albeit of a milder form than previously experienced and in the context of a far more benign international environment: slugflation may be a more appropriate term" (Vol. 15, No. 2). Slugflation? It's a period of sluggish growth and rising inflation. An Age of Diminished Expectations perhaps, to borrow the title of one of Paul Krugman's books.

# **Part 2**: 1991 – 2000: From recession to democratic renewal via privatisation and fading silicon dreams

For the UK as a whole, the recession foreseen by Dr John Hall, TSB Scotland's Treasury Economist, at the end of part one of this series, duly arrived. The Lawson boom of the late eighties had pushed inflation close to 10%. As chancellor, Nigel Lawson had tried to persuade Margaret Thatcher to take sterling into the European Exchange Rate Mechanism (ERM). All he managed was an informal shadowing, by value, of the Deutschmark. With the UK economy embarked on an unsustainable credit boom, interest rates hitting 15% and an inflationary wage spiral in full swing, it was left to Lawson's successor as chancellor, John Major, to persuade an increasingly-beleaguered prime minister to formally join the ERM, in October 1990,  However a day - or rather, days - of reckoning still beckoned. Thatcher herself was ousted by her own party within weeks, with Major taking her place. The ERM experiment lasted less than two years, sterling crashing out under speculative pressure, on Black Wednesday, September 16, 1992. With commendable Scottish understatement, the then-chancellor, Norman Lamont, confessed it had been a "difficult day".

In the first Fraser of Allander Economic commentary of 1991, editor Jim Love noted "As late as November the Government was still denying there would be a recession, despite the mounting evidence to the contrary. The GDP figures for the third quarter of 1990 and provisional figures for the fourth quarter removed any lingering doubt." (Vol. 16, No. 3). In previous recessions, the Scottish economy had taken its full share - sometimes more - of the resultant pain. And this time one of the last remaining mainstays of Scottish heavy industry, the Ravenscraig steel works in North Lanarkshire, was already under threat. In May 1990 British Steel had announced its intention to close the hot strip mill at the plant in the first half of 1991. By the end of 1991 it went on to tell horrified Scottish ministers the rest of the complex, including its giant furnaces, would close too, in January 1992. Yet despite what was happening to Scotland's biggest steel plant, Jim Love questioned whether this recession would hit Scotland as hard as the rest of the UK. While recent evidence did not "inspire much optimism", there were reasons for believing any falls in output north of the border were “unlikely to be of the scale experienced in the UK as a whole”. Lower levels of borrowings by Scottish consumers left them more immune to high interest rates. Scotland had some export-intensive industries, like the burgeoning electronics sector in Silicon Glen, which were still enjoying growth in overseas demand. And the North Sea was going through a mini-boom in the wake of the first Gulf War.

Love’s contrarian prediction proved a shrewd one. For the UK as a whole the 1990/91 recession proved shallower than those of the mid-1970s and early 1980s. Overall, output contracted by 2.4% over five quarters and took twice that time to recover that loss in full. Yet, despite Ravenscraig’s fate, the Scottish economy barely contracted at all. Another manufacturing sector, that cluster of modern electronic assembly plants, collectively known as Silicon Glen, was booming. Between the first quarter of 1991 and the first quarter of 1998 its collective output tripled. In part that was down to growing capacity, as more American, Japanese and other overseas corporations were persuaded to invest in Scotland.

But Silicon Glen’s competitiveness in these new digital export markets was also helped by the sharp depreciation of sterling that followed the UK’s abrupt departure from the ERM. The Fraser commentary had sensed that prospect too. “One of the expected effects of ERM entry is to remove the ‘easy option’ of maintaining competitiveness by devaluation, and the government sees this as a means of imposing discipline on firms to keep costs - especially wage costs - down,” wrote its editor at the end of 1990. “Entering the ERM at a fairly high rate and at a time of rising unit labour costs was bound to put a great deal of pressure on manufacturing industry, particularly those sectors geared towards exports which are crucial to providing an outlet for UK-produced goods at a time of faltering domestic demand. In the long-run the entry mid-point level of DM2.95 may prove unsustainable.” (Vol. 16, No. 2).

While Scotland’s economy, as a whole, emerged relatively unscathed from the early 1990s recession, its two biggest banks were not so fortunate. Injudicious lending at both the Royal Bank of Scotland and Bank of Scotland undermined profitability. Bank of Scotland had recorded pre-tax profits £194m in 1990. These fell sharply to £134m the following year before recovering marginally to £141m in 1992. In 1993 they fell again to £125m. Its larger rival, RBS initially took a much more serious hit. Profits of £262m at the start of the decade fell 78% to £58m in 1991 and collapsed a further 64% to just £21m in 1992. By 1993 RBS profits had rebounded to £265m. The Fraser commentary was alert to the dangers. “Fuelled by poor lending decisions and consequent bad debts, the banks have an urgent need to cut costs if they are to restore profitability. The bad debts, although severe, do not appear to threaten the existence of the companies at present but they must inevitably raise questions about how banking is organised in the UK.” (Vol. 18, No. 2).

Indeed RBS was already well embarked on an internal revolution in how it did business. George Mathewson, an expatriate engineer by training who had been running the Scottish Development Agency since 1981, had joined the Royal in October 1987 as director of strategy and development. By 1992, surrounded by a hand-picked group of former SDA colleagues he had taken with him, Mathewson was the Royal's chief executive, implementing Project Columbus to root out the banking "dead wood" he thought was clogging the Royal's decision making. Over at Bank of Scotland another unconventional banker, Peter Burt, who had started his business life in the computer industry, was taking over the leadership role. By the end of the decade these two men would lock horns over which of their banks would acquire the English clearer NatWest. The first seeds of what would eventually become the biggest banking crisis in UK banking history were already being sown.

The SDA Mathewson left behind in 1987, to sort out RBS, was also approaching its political endgame. As we saw in Part 1, in 1988 Bill Hughes, a Scottish businessman with the ear of Margaret Thatcher, had proposed a much more balkanised model of economic development for Scotland, integrating skills training, stressing enterprise and innovation, and giving business people a much more powerful, localised voice in how the state helps grow an economy. Scottish Enterprise (SE), with its network of local enterprise companies (LECs), and its similarly configured northern counterpart, Highlands and Islands Enterprise (HIE), which replaced the even older Highlands and Islands Development Board, first opened their doors at the beginning of April 1991. The man recruited to head SE was an ex-patriate Scot from California's Silicon Valley, a human resources specialist called Crawford Beveridge.

In the pages of the Fraser commentary, the advent of SE was greeted with plenty of healthy scepticism, notably from Neil Hood, Professor of Business Policy at Strathclyde Business School. (Vol. 16, Nos. 2 and 3) Hood was also an insider who had been Director of Locate in Scotland from 1987-89 and then Director of Employment and Special Initiatives, SDA during the run up to its merger with the Training Agency in Scotland and the launch of SE. He was concerned that, while in principle the SE core had been given a strong strategic role by ministers, the way its relationship with its network of 13 business-led LECs developed in practice could leave it "strong and powerful" or "weak and impotent". That SE core, he argued, should continue to be recognised as "a national development agency in it own right". Were it to become either a channel through which more localised funding and support was negotiated, or simply a facilitator of the work of the LECs, any strategic benefits from the reforms would soon be "frittered away".

There were plenty of early tensions between the SE core and its LEC network. In another contribution to the commentary, Keith Hayton of Strathclyde's Centre for Planning considered the local development pressures resulting from British Steel's decision to close down its Ravenscraig site. Hayton cited one estimate of the funds needed by Lanarkshire Development Agency's chief executive. It came to £650m spread over ten years! SE's entire annual budget at the time was around £420m. "It is difficult to see funding on this scale being provided," he observed. "A more likely scenario is that money will be diverted from the other LECs' budgets. It may be that those LECs that have below average unemployment levels will be particularly at risk." (Vol. 16, No. 3). The more prosaic reality is that, more than twenty years after the event, much of the Ravenscraig site has yet to be redeveloped.

Even in its formative years, under Crawford Beveridge's leadership, Scottish Enterprise did manage to pursue some bold new national strategic goals. Swopping California for the west of Scotland, Beveridge quickly grew concerned about the relatively low rate of new business formation in his homeland, even compared with other parts of the UK. In 1993, at his instigation, SE launched its Business Birth Rate Strategy, designed to close that yawning enterprise gap. A whole suite of interventions were launched - from personal enterprise shows to new materials to support enterprise education in schools; new business network groups and funding forums; a higher education entrepreneurship programme and mentoring support. The strategy had a target of helping create 25,000 new start-ups by the end of 1999. However when the Fraser of Allander Institute was commissioned to review the Strategy's impact over those seven years, it estimated the number of additional start-ups achieved was just 2124. At a cost of some £20m a year, the strategy had eaten up some £140m. And over its life, Scotland's business birth rate had actually fallen from 30.4 per 10,000 of the adult population (using VAT registration data) in 1993 to just 27.5 by 1999.

The political rationale behind creating Scottish Enterprise's devolved, business-led structure was that it would deliver better Scottish solutions to distinctively Scottish problems. However even Conservative governments of the 1980s and early 1990s could not resist the lure of prestigious international projects that promised large numbers of skilled jobs. Health Care International, a £180m private hospital, built on derelict industrial land on the north bank of the River Clyde between Clydebank and Dalmuir, was the showpiece project of that type, when it opened in June 1994. The brainchild of two Boston-based doctors, Ray Levey and Angelo Eraklis, the 260-bed HCI offered advanced medical treatments to patients from southern Europe, North Africa and the Middle East. Costs would be met by their own health systems or out of their own pockets. The complex incorporated a four star hotel so that relatives could travel to Scotland to be with patients. The project had started under the old SDA which spent £7m clearing asbestos and other pollutants from the site. SE invested in the hospital, alongside its builder, John Laing, British Aerospace, an investment arm of Harvard University and a consortium of Dutch, French and UK banks (including Scotland's RBS).

Less than three months after its official opening, at least one of HCI's banks (IMG) was already very nervous. Only 400 of the promised 1800 jobs had been created. Patient numbers had fallen even more dramatically behind forecasts. Peak bed occupancy at that stage barely topped twenty. The Scottish Office and the Bank of England cracked the whip and support payments, from public sources and from the banking consortium, were accelerated. But to no avail. By November 1994 HCI had called in the receivers. In early 1995, the assets were acquired by the London-based Abu Dhabi Investment Company and the hospital relaunched with fresh investment and a plan to treat a steady stream of patients from the Emirate. But even this intervention, involving a son of Abu Dhabi's crown prince, did not resolve HCI's destiny. Increasingly it was used to treat urgent NHS cases from across the UK. In 2002 it was acquired outright by NHS Scotland to help address lengthening waiting times and is now the Golden Jubilee National Hospital, specialising in heart and lung treatments, but also carrying out a significant proportion on orthopaedic procedures for NHS patients from across Scotland.

What happened to HCI in the 1990s - a state-supported private health care initiative being turned on its head, through abject market failure, into much-needed additional capacity for Scotland's domestic state-provided health service - ran completely counter to what successive Conservative governments thought they were about at that time. Privatisation of state assets and utilities was one of the defining drivers of the Thatcher and Major years. British Telecom and British Gas were sold to the public in 1984 and 1986 respectively. British Airways and water supply, in England and Wales, were disposed of too. While the HCI hospital was being built it was still full steam ahead on privatisation. In 1991 the Scottish Bus Group was privatised. At the beginning of 1993, the process of breaking British Rail up started, replacing it with a track, signals and stations operator; a series of privatised regional train operating companies, including ScotRail; and three rolling stock leasing companies. The first of these three groups, Railtrack, was effectively renationalised after the Hatfield Rail Crash in 2000 and is now Network Rail.

In 1991 along with the rest of the UK electricity supply industry, shares in Scotland's electricity suppliers were offered to the public. However there was room for a specifically Scottish solution for those parts of the network operating north of Hardian's Wall. Both the South of Scotland Electricity Board (SSEB) and the North of Scotland Hydro-Electric Board were privatised as vertically-integrated businesses - Scottish Power and Scottish Hydro-Electric respectively - controlling everything from generation and transmission to distribution and supply in their designated areas. Only SSEB's nuclear assets were ring-fenced from the sale, later to be merged into British Energy and sold to the French utility EDF. In England and Wales the old Central Electricity Generating Board was broken up into four - a National Grid company, responsible for the entire high voltage transmission system south of the border and three electricity generators, National Power, Powergen and Nuclear Electric (later British Energy). In addition twelve regional electricity companies were created, responsible for distribution and supply in their areas.

Even before the privatisation process was complete, the commentary was noting (Vol. 15, No. 4 and Vol. 16, No. 1) that both Scottish companies had much to gain by exporting more of their excess power south and exploring new collaborative generating opportunities and commercial supply deals there too. As the post-privatisation environment matured, both Scottish companies exploited their integrated structure to acquire regional supply companies over the border and develop their generating capacity there too. Hydro-Electric, now SSE, after its 1998 merger with Southern Electric, remains a listed company, headquartered in Perth. Scottish Power was acquired by the Spanish group Iberdrola in 2007. Like all their main competitors, SSE and ScottishPower now supply gas as well as electricity. Today, of the six biggest players, two are German-owned, one French and one Spanish. Only SSE and British Gas (owned by Centrica) remain in UK ownership.

What happened to the electricity sector through privatisation has left one competitive wrinkle, causing tensions to this day. National Grid still owns the high-voltage network south of the border. Under BETTA (the British Electricity Trading and Transmission Arrangements), it is also the system operator for the entire UK-wide high-voltage grid. In effect it regulates flows of electricity around the whole UK and the terms under which these flows take place. However National Grid is a major commercial player in that market, just like SSE and Spanish-owned Scottish Power, who still own and operate their own parts of the high-voltage wires in Scotland. So when it comes to moving away from fossil fuel generation towards greener forms of generation (most notably onshore wind) there is growing political tension.

Scotland wants to export as much green electricity south as it can. But its own baseload generating capacity is diminishing, now that Scottish Power is closing its massive coal-fired Longannet station next March. And no one, not even Scottish Power or SSE, seems interested in building new base-load capacity north of the border. The SNP-controlled devolved Scottish government has an embargo on any new nuclear generating capacity here too. And now the new majority Conservative government at Westminster is talking about cutting back on subsidies for renewable generators, like onshore wind farms. The future of BETTA, which the SNP, in its 2014 Scotland's Future white paper, said it would continue to support, were Scotland to vote yes to independence, looks like becoming a growing source of political friction between Edinburgh and London over the next few years.

While the final decade of the 20th century was marked, right across the UK, by a very significant re-drawing of the boundaries between what the state could best provide and what should be vested in market competition, it was also a time of significant political and constitutional upheaval, especially in Scotland. In 1994 the Major government legislated to abolish the two-tier structure of regions and districts across Scotland, introduced in the 1970s, and replace them with 32 unitary authorities. When the new Act came into force in 1995, the vast Strathclyde Region, centred on the City of Glasgow and the Clyde estuary, was no more. Water and sewerage services were taken away from local democratic control. However in the wake of a political campaign which included a 'water referendum' organised by Strathclyde Region, the Conservative government baulked at privatising these services the way it had in England and Wales. Instead three public water and sewerage authorities were created, covering the west, east and north of the country. In 2002 these would be merged into a single body, Scottish Water, created by an act of the new devolved Scottish parliament.

Against all the predicted odds, the Major government had retained power in the 1992 UK general election. That gave it a mandate to continue to pursue its wide-ranging programme of privatisation and advance the wholesale restructuring of the architecture of the British state. But as the next general election loomed, in 1997, there were growing signs that eighteen years of Tory rule were coming to an end. The choice facing voters was particularly acute in Scotland, where the Labour opposition, now under Tony Blair's leadership, was committed to holding another referendum on Scottish home rule and - if it proved to be the settled will of the Scottish people - the creation of a devolved Scottish parliament in Edinburgh for the first time since the Act of Union in 1707.

A month before the 1992 general election, the Scottish Office published, for the very first time, what its press release of the time rather prosaically called a “booklet” on Government Expenditure and Revenues in Scotland. “In reading this booklet, the people of Scotland will be able to judge for themselves the extent to which Scotland derives economic benefit from being a part of the United Kingdom,” explained Ian Lang, the Secretary of State for Scotland at the time. That first booklet showed total public expenditure per head in Scotland just over 12% higher than in the UK as a whole, and identifiable general government expenditure 19% higher than its UK equivalent and 24% higher than in England. On the revenue side, over the four main classes of revenue raised in Scotland - income tax, national insurance, VAT and local authority revenue - Scotland’s contribution was below its population share. “In short,” claimed Lang, “we contribute less than our population share to the UK Exchequer, and receive more from it.”

That analysis, now known universally by its acronym GERS, has appeared annually ever since. It has been refined. Since the start it has been the work of Scottish civil servants. It has proved contentious and sometimes inflammatory fuel for the ongoing political debate about Scotland’s constitutional future. A strong flavour of that controversy is evident in three linked pieces which appeared in the Fraser commentary in 1997 (Vol. 22, No. 3). The first is a comment on the SNP Budget for Scotland by the Institute’s Jim Stevens. The second is a riposte by Andrew Wilson, an economist, speaking for the SNP, later a list MSP for the party in the very first Scottish devolved parliament. The final piece is an analysis of the SNP budget, which formed part of the party’s manifesto for the 1997 UK general election, by Peter Wood, of the independent Scottish consultancy group Pieda. Intriguingly the pieces only appeared in the June edition of the commentary, six weeks after the votes cast on May 1st had been counted and Labour had swept to power with a 179-seat majority. The SNP had doubled its Scottish seats tally from three to six.

Stevens based some of his analysis on the latest GERS figures. He rejected the charge that, by doing so, he was accepting “Tory fiddled figures”. That was a “puerile slur on the professional integrity of government economists”. The SNP’s view of our fiscal prospects, Stevens concluded, was “ludicrously optimistic and fatally flawed”. Oil revenues would endure for a long time “but on a declining trend and would not be sufficient to ensure that we did not have to borrow more or tax more to enjoy the same level of public services that we would have enjoyed inside the Union.” If we are to opt for independence, he went on, “It will not be an easy ride and we should only do so with our eyes wide open. Suspect and inaccurate appraisals of our fiscal prospects are about as much use in the Scottish constitutional debate .... as a chocolate fireguard.”

Wilson's response, on behalf of the SNP, didn't pull any punches either. He opened by recalling that, in 1970, David Simpson and Kenneth Alexander had contributed essays to an OUP book, respectively for and against the economic case for Scottish independence. Simpson was the founder director of the FAI and Alexander, the founding professor of economics at Strathclyde. Alexander was, Wilson quipped, in "the grey corner" while Simpson occupied "the sunshine corner". Clearly the gloves were off. Scotland's inherited fiscal position on independence, Wilson argued, "is of less importance to the economics of independence than the dynamics. It is not the starting point but what happens through time that is of greater importance." If an independent government proved better for the Scottish economy than London government, delivering faster growth and releasing latent enterprise, then any initial fiscal deficit would quickly diminish. Stevens's contribution to the debate was "welcome". But it contained "unsustainable arguments couched in pejorative language.'

It was left to Peter Wood of Pieda to offer a view from outside the ring. "Few, if any, economists would dispute that Scotland would be economically viable as an independent country," he observed. "It is quite evident that Scotland's economy is larger, more prosperous and more soundly based than many existing independent states. However there is much less agreement as to whether an independent Scotland would be more or less prosperous than a Scotland which remained within the UK." He went on to point out that the budget the SNP proposed involved spending increases that, by 2001, would push Scotland's budget deficit to almost £7bn, or nearly 10% of GDP. "With some determined belt tightening in terms of reduced public spending and/or tax increases" an independent Scotland could reach the Maastricht criteria for joining European Monetary Union. Whether it might become another Celtic Tiger in the longer term was, Wood judged, "far less certain". And the idea that independence would deliver an instant public spending bonus he dismissed as "untenable".

The really striking thing about these exchanges, reading them again now in 2015, is how little has been resolved in this core economic argument about Scotland's constitutional future over the eighteen years since they took place. Next year the devolved Scottish parliament and government will complete its fourth full term. We have had a referendum on Scottish independence where the yes side lost by a margin of more than ten percentage points. We have had another UK general election in which the SNP swept the board in Scotland in unprecedented fashion. The Smith Commission proposals have led to another Scotland Bill, offering more devolved fiscal powers to Edinburgh, currently being debated at Westminster. But, in tone, texture and temper, the economic arguments for and against further constitutional change seem as entrenched and unresolved as ever they were. Even debates about the prospect of something short of outright independence - full fiscal autonomy within the existing Union - suffers from the same statistical trench warfare.

In the final years of the old century, constitutional preoccupations were more about whether Scotland would vote for the new devolved parliament Labour had promised and whether Scots would also vote to give that parliament modest powers over tax. Labour, led by Tony Blair, won its huge 1997 majority in part on a pledge of strict fiscal rectitude. Blair's chancellor, Gordon Brown, would stick, for their first two years in office, with the same tight spending plans already set by the outgoing Tory administration. Even Brown's Treasury predecessor, Ken Clarke, later admitted he didn't really think his party could have delivered on those legacy spending plans had they won. But Brown stuck with Clarke's hair shirt. In each of its first three years in office, New Labour generated increasingly large budget surpluses, thanks to that squeeze on public spending. Such budget surpluses had only happened in four other years since the mid-sixties. For the vast majority of the past half century, annual budget deficits have been the norm in the UK whoever was in power. Against that backdrop, it is no surprise that the modest fiscal powers vested in the new parliament in Edinburgh in 1999 - to vary the basic rate of income tax up or down by up to three pence in the pound - has withered unused on the fiscal vine ever since.

As the new millennium approached, did that tight squeeze on public spending have any significant impact on the real economy in terms of output and jobs? As we have seen, the 1990s had started with the Scottish economy narrowly escaping the recession that hit the rest of the UK. At the start of the decade unemployment, in both Scotland and the UK as a whole, had been on a downward trend for nearly three years. The Scottish jobless rate, while not as far adrift as it had been at the end of the 1970s, was still a full three percentage points higher than the UK equivalent. However that gap narrowed when the recession was felt more keenly south of the border. Scotland's unemployment rate even dipped below the UK rate in 1992/3 and stayed much the same until the middle of the decade. Then it began to drift higher again.

Two contrasting forces were at work. Scotland's push to attract more electronics assembly plants to its shores appeared, for much of the decade, to be paying dividends. Successive Fraser commentaries charted the way output from Scottish manufacturing plants caught up with equivalent UK output by late 1994, then to soar higher right through to the end of the decade. There's a chart on page 7 of the January 2000 edition (Vol. 25, No. 1) that captures that clear trend. However New Labour's squeeze on public spending was also having its impact, in sectors where the Scottish economy was already more dependent, in employment terms, than its southern counterpart. On top of that, there were already clear signs, despite that soaring manufacturing output, that the silicon dreams fostered in Scotland through the 1980s and 1990s might be beginning to fade.

Motorola had built a massive complex to assemble mobile phones at Bathgate  which opened in 1990 and employed more than 3000 people. By 2001 it was closing down and shipping the assembly work off to cheaper host economies in eastern Europe. In 1996 the Taiwanese group Chungwha arrived at Mossend in Lanarkshire promising even more jobs, 3300, assembling cathode ray tubes. But that was yesterday's technology. The advent of flat screens changed all that and Chungwha was gone in six years. The Korean group Hyundai agreed to come to Fife to fabricate silicon chips. A hugely expensive wafer fab was built, with lots of support from Scottish Enterprise and government. But Hyundai changed its mind. And with other established wafer fabs, like the Japanese group NEC's plant at Livingston, also closing, the Fife site never produced a single wafer. It has since been demolished.

The Outlook and Appraisal in the final Fraser commentary of 2000 ( Vol. 25, No. 4) caught the mood. "The Scottish economy experienced a further contraction in output in the first quarter of the year. Growth was considerably weaker than in the UK." it noted. "The service sector exhibited no growth, while manufacturing output fell markedly..... the fall in electronics output appears to be a key reason for the overall weakness." Some in the Scottish media were already talking of another recession. The Fraser team disagreed. But with trouble in Silicon Glen, a stronger pound hitting exports and growth in public expenditure tightly constrained, the new century was starting on an uncertain note.

# **Part 3**: 2001 – 2015: The 'Nice' decade turns nasty; banking Armageddon; and the politics of austerity

At the end of Part 2 we noted that Scotland's hopes of replacing its old core industries of shipbuilding and steel with a renaissance based on microelectronics was already beginning to fade. The largely American and South East Asian-owned plants fabricating processing chips and assembling computers and mobile phones, having turned large parts of central Scotland into Silicon Glen, were either transferring production to lower-cost locations or failing to deliver promised investments at all. In the first Fraser commentary of 2001 Richard Marsh considered the consequences. "The development of an electronics sector within Scotland was intended to increase job security, opportunities and value added within the economy," he wrote. "The sector's downturn is therefore bad news for Scotland's growth. This then begs the questions what are the underlying forces causing the recent developments and do they spell the end for Silicon Glen?" (Vol. 26, No. 2). Marsh suggested exploiting established linkages and upgrading Scotland's skills base might help underpin a smaller, smarter electronics cluster. In 2002 total exports from Scotland of computer, electronic and optical goods were worth nearly £5.6bn. By the end of that decade Silicon Glen exports had halved and halved again, to just under £1.4bn.

While Scotland's ambition to punch above its weight in this new digital world was facing setbacks, a much more traditional sector of its economy was embarking on a period of unprecedented export-led expansion. In the decade from 2004, sales of Scotch whisky to some 200 markets around the world grew by 74%. Over the same period, sales of single malts surged by 159%. In the 1980s the sector had been convulsed by takeovers, notably by Guinness, of Fells, then Distillers. In the 1990s, as a result of over-production and too much Scotch being sold in bulk to overseas competitors, distillery capacity was being mothballed. Now Scotch vies to be Scotland's biggest single export by value. Right through to the present some mothballed distilleries are being reopened, some working distilleries are having their capacity expanded, new ones are being built, and others planned. Scotch whisky now accounts for a quarter of all UK food and drink exports. Annual visitor numbers to distilleries have topped a million and a half, boosting Scotland's tourist trade.

Oil was first discovered off Scotland's shores when the first Fraser commentary was still in gestation. North Sea production peaked at the end of the 1990s. In early 1998 the price of Brent benchmark oil was heading down towards just $10 a barrel. Ten years later the price peaked at over $140 a barrel. Within a year, thanks to the Great Recession brought on by the banking crisis of 2007/08, that oil price had fallen back below $40 again. It recovered again to just over $120 by 2011 and, as Grant Allan shows in a recent Fraser commentary (Vol.38, No.3) then fluctuated in a band of $100 to $120, until late 2014 when the price rapidly collapsed to below $50 again. Government tax revenues from offshore oil and gas production first peaked in the early 1980s, spiking again in 2008 and again in 2011 when oil prices were high. The falls since late last year mean tax revenues have all but evaporated. Since the North Sea has been historically a high-cost province, one now moving steadily into maturity, with development plans being curtailed and staff losing their jobs in significant numbers, the future looks more and more uncertain. Oil price volatility now threatens significant consequences for Aberdeen, Scotland's oil capital, and for a supply chain that stretches down into central Scotland and much further afield in the UK.

Volatility was also a major factor in the eclipse of Silicon Glen in the early 2000s. One of the underlying forces at work there was the speculative dot-com asset bubble which afflicted the American NASDAQ stock market index in the final years of the old century into the dawn of the new millennium. Its tech-heavy composite index, which stood around 100 when the Fraser commentary first launched in 1975, broke through 1000 in July 1995. Then, fuelled by what US Federal Reserve chairman Alan Greenspan, in a speech in December 1996, called "irrational exuberance", the index rocketed. Those betting that the emergence of the world-wide web would be far more transformational for the global economy than any previous industrial revolution, could not get enough of the new internet -based companies heading to NASDAQ, some with brazenly overblown IPOs. Its composite index peaked at an intra-day high of 5132 on March 10, 2000. The collapse that followed was even more precipitous. It plunged back near where it started, to a intra-day low of 1108, in September 2002. Amazon saw its stock slashed from $107 a share to just $7. It took the NASDAQ index another thirteen years, until April 2015, to recover and surpass that millennial pre-burst peak. Many of its beneficiaries did not survive the burst. Some, like Bernie Ebbers of WorldCom, went to jail for securities fraud and conspiracy. Ebbers is currently serving 25 years. For some who successfully rode out the rollercoaster, it's been a very different story. Amazon's stock is now touching $600 a share.

Another traumatic set of events on American soil, which erupted on an unsuspecting world while the hot air was still spilling out of the dot-com bubble, was to have geopolitical consequences that have also helped shape our collective destiny ever since. Of the four US domestic flights hijacked on the morning of September 11, 2001 by 19 al-Qaeda terrorists, two were flown into the twin towers of the World Trade Centre in New York's Lower Manhattan district, one was flown into the west side of the Pentagon in Washington and the fourth, after resistance by civilian passengers, crashed into a field near Shanksville, Pennsylvania. In all 2,996 people died. One early instinct was to try and quantify the impact of 9/11 on the global economy. Three months after the twin towers fell, that December's Fraser commentary described that impact as "difficult if not impossible to quantify". Scotland could expect reduced tourism demand, lower exports outside the UK, and a reduction in inward investment. The Commentary agreed with the view of the then chief economic advisor to the devolved Scottish government, Dr. Andrew Goudie, that Scotland's annual growth "will decelerate but should remain positive". The Fraser team cut its forecast for 2002 GDP growth from 1.4%, but only down to 1.2% (Vol. 26, No. 4).

US and British forces had started aerial bombardments of Taliban and al-Qaeda targets in Afghanistan within a month of the mass slaughter in New York. Special forces, on the ground in Afghanistan, had already overthrown Taliban rule by the time the December commentary appeared. The Allied invasion of Iraq in March 2003 and the subsequent overthrow of Saddam Hussein were to follow. While winning the war in Iraq and managing some sort of peace in Afghanistan were to dominate the strategic thinking of Western governments throughout the first decade of the 21st century, by 2011 we had the multi-state intervention in Libya in 2011 and, by 2014, the rise of ISIS in parts of Iraq and Syria, and the growing exodus of refugees now risking all to find a new life within the EU. Even Tony Blair now concedes "elements of truth" in the claim that the war in Iraq helped cause the rise of Islamic State. However myopia at the highest levels of western governments about the long-term consequences of the geopolitical choices made in the immediate aftermath of 9/11 is mirrored in some of the key choices made by central bankers during and after the dot-com bubble.

US Fed chairman Alan Greenspan had certainly warned of the consequences of irrational exuberance in financial markets back in 1996. But he and his colleagues were slow to do anything, by way of monetary policy, to take the steam out of the mounting market hysteria. Over the five years between July 1995 and March 2000, while the NASDAQ composite index was rising more than fivefold (from 1000 to 5132), the Fed changed its main interest rate eleven times. But to little effect. It stood at 5.75% in July 1995. It was just a notch higher, at 6%, in March 2000. When the tech bubble burst, and with the wider US economy showing signs of increasing fragility, Greenspan and the Fed's open market committee suddenly became much more proactive. They cut the federal funds rate eleven times in 2001 alone. All the way down from 6% to 1.75%. Four of those cuts (1.75 percentage points in total) came in the shocking wake of 9/11. There were two further cuts, one each in 2002 and 2003, taking the main interest rate all the way down to 1% where it stayed for a further year. With rates that low for that long, another asset bubble was already in the making.

This time it was housing. With borrowing now so affordable who across America could not aspire to own their own home? The sub-prime mortgage scandal, which was to become such a central factor in the banking meltdown later in the decade, was already beginning to take shape. Greenspan has always denied he and the Fed were to blame. “Those who argue you can incrementally increase interest rates to defuse bubbles ought to try it sometime,” he said in 2008. “I don’t know of a single example of when interest rate policy has been successful in suppressing gains in asset prices.” The former chief economist of the IMF, Kenneth Rogoff, disagreed. “If you cut interest rates when asset prices are in free fall, then when asset prices are rising while indebtedness is rising all over the country, you need to raise rates. He (Greenspan) actively chose not to do that.”

Greenspan was not the only central banker taking a distinctly relaxed view of the emerging economic and geopolitical threats of the period. In October 2003, Mervyn King, just three months into his term as Governor of the Bank of England, delivered an intriguing speech in Leicester. Since the end of the Second World War, he suggested, Britain had experienced a succession of stop-go, boom-bust cycles. However the ten years from the 2nd quarter of 1992 had been, he ventured, the nice decade. The UK had experienced a Non-Inflationary, Consistently Expansionary ten years. NICE, if you can get it. A decade in which growth was above trend (2.9% compared with the post-war average of 2.5%). Inflation, having been targeted from late 1992, had averaged 2.5%, the lowest for a generation. Unemployment had fallen from 10% to 3%, the lowest level for three decades. Output had risen in every single quarter. Living standards were rising as the terms of trade moved in Britain’s favour. The new governor put the success of the 1990s down to a number of things. One was the new monetary framework, introduced by the first Blair government in 1997, that gave the Bank of England independence and a clear inflation target. Another was “a sustainable fiscal consolidation that had turned a deficit of 8% in 1993 into a sustainable position for the public finances based on a set of clear rules for government debt”. King was referring to the striking consequences of Gordon Brown, as the new Labour chancellor, adopting the tough spending targets of his Conservative predecessor, Kenneth Clarke. Since 1965 there have only been seven years when UK governments have not had to resort to net borrowing to fund their spending promises in full. Two occurred between 1969 and 1971, the last year of Harold Wilson, the first of Ted Heath. Another two at the tail end of the Thatcher era in the late 1980s. And the other three were at the end of the 1990s, when the New Labour government walked into Downing Street for the first time and Brown immediately donned Clarke’s hair shirt.

King did not deny there had been some “unexpected twists and turns of the world economy … especially in the latter half of (his nice) decade”. However, he argued, “those shocks tended to average out over time rather than cumulate in either an upward or downward spiral. In other words the economic surprises alternated between good one year and bad the next rather than adding up to ‘one damn thing after another’. In that sense, Lady Luck smiled on us.” Would the next ten years be as nice? was King’s rhetorical teaser. The new governor judged that “unlikely”. However he insisted that realistic conclusion was not “a case for pessimism, rather the opposite”. He judged the macroeconomic framework in the UK “sound and proven”. From such a “new-found position of macroeconomic stability” there was now an opportunity “to boost productivity, education and enterprise in order to generate the resources needed to raise living standards”.

The Bank of England’s governor was not alone in detecting more benign economic times. In February 2004, in a speech in Washington, the man who two years later would succeed Greenspan as chairman of the US Federal Reserve was saying something very similar. Ben Bernanke noted that the previous twenty years had seen a sharp decline in macroeconomic volatility in the US. Variability of quarterly real output growth was down by a half since the mid-1980s. Variability in inflation down by two thirds. Bernanke called it the Great Moderation. He cited three reasons for it. Structural changes in the economy, including much wider use of information technology, which improved the economy’s capacity to absorb shocks. Improved macroeconomic policies, notably control of monetary policy moving from politicians to central bankers. And that magic ingredient - Lady Luck - again. However these improved policies were still fallible. And all that luck was about to run out.

Before we discover why luck did run out, we should consider what impact changes in the way Scotland would now be governed were having on the evolution of the Scottish economy. The first devolved Scottish government came into being in 1999, a Labour/Liberal Democrat coalition led by First Minister Donald Dewar. It June 2000 it produced what it called “a step change in economic policy making in Scotland”. Its Framework for Economic Development was 92 pages of principles and priorities, enabling and outcome objectives, even a vision. It was “to raise the quality of life of the Scottish people through increasing economic opportunities for all on a socially and environmentally sustainable basis”. Words that would still not seem out of place in political debate on economic ambitions today. That they still seem so familiar fifteen years on suggests delivery is an altogether tougher nut to crack that trading visions. The Framework called for “the enhancement of productivity”. So did the current UK chancellor George Osborne in his most recent budget. In one commentary piece in June 2005, after the Scottish government launched a refresh of its Framework document, Peter Wood asked heretically “Is the growth of the Scottish economy the first priority for public spending in Scotland?” (Vol. 30, No. 1).

That first devolved coalition inherited the enterprise agencies, Scottish Enterprise (SE) and Highlands and Islands Enterprise (HIE), created in the Bill Hughes-inspired reforms of 1991. They are still with us today. Their inward investment arm Locate in Scotland was, in 2001, turned into Scottish Development International, charged with both attracting overseas investment to Scotland and encouraging Scottish companies to export more. The skills work previously carried out by Careers Scotland was folded into SE and HIE only to be hived off again in a new agency Skills Development Scotland in 2006. The year before SE and HIE were stripped of their networks of local enterprise companies (LECs). The Business Gateway Network was hived off to local authorities. Three self-standing Intermediate Technology Institutes (ITIs) were set up by SE in 2004 to find and develop innovative technology in the fields of techmedia, life sciences and energy, with a budget of £450m over ten years. The ITIs were absorbed back into SE in 2009, having spent £231m but with very modest returns to show for it.

A “bold” initiative, SE’s current chief executive Lena Wilson told MSPs in 2013, had fallen victim to an economy that had not turned out as the agency had thought. Both SE and HIE have survived the change of control of the devolved Scottish government, to a minority SNP administration in 2007 and then an outright SNP majority in 2011. Their budgets have reduced in real terms over a number of years and perhaps their influence too. Both Alex Salmond and his successor as first minister, Nicola Sturgeon, have chosen to appoint their own Council of Economic Advisers whom they meet twice a year. The core of both SE and HIE’s activity now is to run a system of account managed businesses, some 2500 in total, which are assessed as having real growth potential. But that, they are at pains to argue, does not preclude them doing a lot of support work with other businesses that are not account managed. One enduring mystery is why, given the failure of the ITI initiative, there is not more independent scrutiny of what the account management system is actually achieving.

The first decade of the new millennium did not quite match the 1980s in the range and scale of Scottish companies facing corporate takeover. Acquisition activity was, however, on the rise again. In 2002 the Mersey-based Peel Group acquired Clydeport. The following year the American newspaper group, Gannett, acquired the Glasgow-based Herald and Times from STV-owner SMG. In 2005 Scottish Radio Holdings was sold to Emap. In 2007 the Spanish group Iberdrola acquired ScottishPower. And in 2008 the French, largely state-owned, electricity generator, EDF, acquired British Energy, including its Torness and Hunterston B nuclear stations. From the late 1990s onwards almost all of Scotland’s mutual life insurance and pensions groups surrendered control to bigger English or continental based players. Only Standard Life, which demutualised in 2006, bucked the trend by seeking a full market listing in its own right.

However, as we noted briefly in Part 2 of this series, the takeovers that were to dominate both the Scottish and UK economies as the new century began were the attempts by Scotland's two oldest banks, Bank of Scotland and Royal Bank of Scotland (RBS), to turn predator not prey, in the takeover game. Bank of Scotland was first to act, spurred on by Standard Life's surprise decision in 1996 to sell its one-third share in the Bank, acquired a decade earlier from Barclays. BoS, having celebrated its 300th birthday the year before, suddenly discovered a sense of vulnerability. Once Standard Life was persuaded to dispose of its stake piecemeal in the market, the Bank's Governor Sir Bruce Pattullo and chief executive Peter Burt set out to find a merger partner among the bigger UK building societies, then abandoning their traditional mutual status. That trawl proved fruitless. After Pattullo retired, Burt persuaded his board on a much bolder strategy. The Bank should launch a hostile bid for NatWest, twice the size of BoS but the poorest performer among the big four English clearers.

At first Burt tried to persuade his opposite number at RBS, Sir George Mathewson, to mount a joint bid. That would bring much more financial firepower to bear and, if successful, would allow them to split the spoils between them. However it quickly became clear both Scottish banks would want the same parts of NatWest. The talks foundered. Then in September 1999 the intended prey announced an agreed deal to buy the giant insurer Legal & General for £10.7bn. If that deal went through, the price tag on an enlarged NatWest would be way beyond what the smaller Bank of Scotland could afford. It was decision time. Would it bid or walk away? The Bank's acting chairman Sir Jack Shaw broke the news of its hostile bid in a dawn phone call to NatWest's chairman Sir David Rowland on Friday September 24 1999. The timing was exquisite. Most other senior bankers, including RBS's Mathewson, were already in America for the annual meetings of the IMF and the World Bank.

Burt won lots of plaudits for the logic of the Bank's bid. It certainly killed off NatWest's deal with Legal & General. However, as is usually the case in hostile offers, pressure was on from the City to discover how much more BoS would be prepared to pay. It did raise its terms once but, with NatWest's share price rising faster than its own, closure was proving elusive. The Bank improved its terms. However the relative share prices of predator and prey pointed to the City expecting even more. Meanwhile, with Mathewson quickly back in the UK, RBS was planning its own counter-bid for NatWest. That came on the 29th November, with the Spanish bank BSHC (now Santander), then a shareholder in RBS, willing to provide some of the cash. It was made clear that RBS's then chairman Lord Younger would retire to be replaced by Mathewson. His deputy Fred Goodwin would mastermind the integration of NatWest and succeed Mathewson as chief executive to drive the combined bank forward. On the 11th of February 2000 RBS's offer was accepted by NatWest.

A shell-shocked Bank of Scotland was forced to confront its own vulnerabilities once more. Tentative merger talks with National Australia Bank and Abbey National followed. Then, little more than a year after NatWest slipped through its fingers, Bank of Scotland agreed to merge with the biggest mortgage lender in the UK, Halifax. While the headquarters of the combined bank - Halifax Bank of Scotland or HBOS - would be in Edinburgh, most of the main jobs - chairman, chief executive, finance director, head of retail and head of insurance - went to Halifax men. Burt stayed on briefly as executive deputy chairman, then retired. He had vastly more banking experience than the Halifax five had among them. Not that the Bank's Scottish rival, RBS, was any different in that regard. Mathewson had been first an engineer, then venture capitalist and had run the SDA before he joined RBS. And his successor, lawyer-turned-accountant Goodwin's first banking job was as chief executive of Clydesdale Bank for three years.

That didn't stop any of them from trying to build market scale in the sector that was really booming on both sides of the Atlantic, thanks to cheap money and all that central bankers' talk of a new era of macroeconomic stability. That sector was housing and the wider property market. Buoyed by capturing NatWest, Goodwin embarked on what began to look like a growth at any cost strategy. RBS kept buying more banks, many of them in the US as bolt-ons to its own existing Citizens Financial, a Rhode Island-based savings and loans bank with a big exposure to housing finance. That process led, in 2004, to paying an eye-watering $11bn for Charter One banking group, a launch pad into the American mid west. In Ireland, where another property bubble was rapidly inflating, Goodwin urged Ulster Bank, operational right across the island of Ireland and acquired as one of the NatWest spoils, to maximise its loan book. Between 2000 and 2007, Ulster Bank grew its total assets (effectively its loan book) six-fold to €55bn! Goodwin also bought a newer mortgage bank, First Active, because he wanted the man who created it to run Ulster Bank as well. A major strand of Goodwin's ambition for RBS was to turn it into a globally significant investment bank. Another of the NatWest spoils, Greenwich Capital in Connecticut, became one of the biggest players in the underwriting in securitised packages of mortgages, many of them sub-prime, traded on as investment opportunities.

HBOS was also going flat-out to exploit the growing housing bubble. Remember Howard, the singing bank clerk who starred on the bank's TV adverts? He reportedly bought an £800,000 second home with one of the bank's mortgages. I once asked Andy Hornby, the former ASDA executive who was HBOS chief executive James Crosby's right-hand man whether he ever worried the housing bubble was getting out of hand. "It's a simple question of supply and demand," he replied. "Demand for housing vastly outstrips supply. There's absolutely no evidence that's coming to an end." Corporate banking in HBOS was the really distinctive strand Bank of Scotland brought to the merger. BoS corporate bankers had always fancied themselves as more entrepreneurial in the way they did business. Little wonder then that as commercial property deals boomed, they grabbed more than their share and, in the process, became more and more exposed to the fate of bricks and mortar in the longer term.

As the decade rolled on, investors were growing more and more restless about Fred Goodwin's seemingly insatiable appetite for serial deal making. They had noted that despite all the frenetic activity, Royal's share price, having peaked in 2002 around £21, had been becalmed for two years in the £15/£16 range. In 2005, under pressure from some on his own board, RBS's chief executive began publicly to dismiss any need for the bank to keep on making more acquisitions. But he was already preparing the next deal. A 5% stake in Bank of China. Then came the biggest deal of all - the hostile consortium bid Goodwin put together with Banco Santander and Belgian bank Fortis to snatch the Dutch banking group ABN Amro from under the nose of Barclays. The idea first captured Goodwin's imagination in 2005 and dominated his thinking for most of 2006 and 2007. The big prize for him was ABN Amro's American subsidiary LaSalle. But the Dutch bank sold it to Bank of America early in the proceedings. Quite how a generous, largely-cash bid for a bank with operations in 53 countries, operations that would then be split three ways among the consortium partners, made any sense in an environment where property risks were crystallising and banks in general were under growing pressure, is anyone's guess. But RBS shareholders voted for it and Scotland's new first minister Alex Salmond publicly led the home cheer-leading. Bear Stearns and Northern Rock were already going under as the Royal Bank of Scotland ABN Amro saga was reaching its catastrophic conclusion.

Within a year, with the credit squeeze tightening, interbank lending slowing to a trickle and yawning property black holes opening up in bank balance sheets, Armageddon loomed. In America Lehman Brothers filed for Chapter 11. In the UK, with the cash literally running out, HBOS was shepherded, with government and Bank of England encouragement, into the arms of Lloyds TSB, with the state the dominant minority shareholder in the combined group. RBS was also kept alive, just. But with the state as the dominant shareholder with more than 80% of the shares. The Fraser commentary spoke for many about how far the Scottish banks had fallen below the historic standards they had set themselves. "The scale of the losses on sub-prime and impairments facing the two principal Scottish banks, RBS and HBOS, are considerable and exceptional compared to other UK banks. The losses have pushed RBS and HBOS to the brink of bankruptcy. This outcome underlines the extent to which the lending behaviour of the two banks had ceased to be underpinned by the traditional risk management practices that had led Scottish banking and bankers to be perceived as prudent and even canny." On its worst-case scenario there would be a period of sustained recession. "Here the seizure of the financial system continues for an extended period, bank illiquidity persists, leading continues to be severely constrained, and confidence remains low. A greater contraction in household and investment demand follows, leading to negative growth for two consecutive years." (Vol. 32, No. 2).

Being an economic commentary, the Fraser tended to play down the political consequences of the great banking crash of 2008/09. The Labour government led by Gordon Brown garnered precious little credit from the electorate for saving the UK banking system from complete meltdown. In 2010 it lost the General Election and was replaced by a Conservative/Liberal Democrat coalition. In Scotland, having surrendered the control of Holyrood it had shared with the Liberal Democrats since 1999 to a SNP minority administration in 2007 that chose to govern alone, it lost the 2011 Holyrood election to a majority SNP government. Then in the 2015 General Election the Conservatives narrowly won outright control at Westminster, while in Scotland the SNP swept he board and left Labour and the Liberal Democrats in the same parlous state as the Tories north of the border with just one MP each. Somehow Labour had meekly allowed itself to be painted as the party of sustained fiscal irresponsibility, consistently borrowing too much and spending too much. Leaving Conservatives to “fix the roof when the sun is shining” or, in its latest iteration, “fixing the foundations” by sorting out the UK’s deficit once and for all. The actual numbers show a much more nuanced reality.

The numbers on public sector net borrowing as a percentage of GDP show, as we noted earlier, show the Blair/Brown years starting with three rare years of surpluses and two of minimal borrowing followed by six years of borrowing at similar levels to the Thatcher years. Only after the banks crashed and burned, requiring vast injections of liquidity by the state, did public borrowing spike higher. The Cameron/Clegg coalition promised a period of austerity that would sort the UK’s deficit by this year. It only actually managed the rate of reduction Alistair Darling was promising if Labour had been re-elected. The UK government books won’t be in surplus, we are now told, until the end of this parliament in 2020. A target that will only be met if George Osborne can find ways of modifying his plans for cutting tax credits for the working poor and still find the savings elsewhere. In Scotland our fiscal future has developed a whole other layer of complexity. The Calman-inspired Scotland Act will next year transfer a number of tax powers to Holyrood. And, in the wake of last year’s independence referendum, the Smith Commission process has added further tax and borrowing powers to that. Successive Fraser contributions have been contributing to this debate. For an early flavor try the debate involving Brian Ashcroft, Alex Christie, Kim Swales, Graeme Roy, Paul Hallwood and Ronald MacDonald in 2006 (Vol. 31, No. 1) and (Vol. 31, No. 2).

The recession that followed the banking meltdown of 2007/08 is increasingly being dubbed the Great Recession of modern times. Five years on the texture of the recovery we have experienced since continues to feel fragile. Indeed the outlook and appraisal in the latest Fraser Economic Commentary, just published, points to some worrying features of that recovery as it has evolved in Scotland, compared with the UK as a whole. While the pace of recovery appears to be slowing for both, it is weaker in Scotland than in the UK as a whole. In terms of GVA, the UK was 5.8% above its pre-recession peak by mid-2015, Scotland just 3% above. In terms of GDP per head - arguably a better measure of personal prosperity - Scots are still 0.3% below the pre-recession peak, while the equivalent UK average is 0.6% ahead. That, argues the economist Simon Wren-Lewis is “an absolutely terrible performance for a recovery”.

In financial services, a major driver of inward investment in Scotland since the decline of Silicon Glen, the picture is even less encouraging. As the latest Fraser outlook and appraisal shows, its GVA contribution had fallen 15.5% by 2012 from its 2007 peak. “There must now be a strong presupposition that the scale of the financial services sector might never return to the levels seen before the Great Recession” concludes Brian Ashcroft. After all what recovery we have seen has been achieved with an extended period of exceptional monetary easing. UK Bank Rate has been held at a rock-bottom 0.5% since March 2009. Six years, seven months and counting. Quantitative easing has totaled £375bn. Commodity prices are tumbling. The price of oil has more than halved since Scotland held its independence referendum, with significant impacts on the future of the North Sea. There is scant evidence of the promised restructuring of our economy away from consumption and excessive debt towards more exports, more manufacturing and increased saving and investment. With the latest closures in what’s left of the UK steel industry and the continuing haemorrhage of jobs from the oil industry, chancellor George Osborne’s ‘march of the makers’ seems to have stalled. Truly the shadow cast by the most dramatic event of the past fifteen years - that banking Armageddon - is a very long one. One that will continue to impact the Scottish economy for years to come.

Alf Young, Visiting Professor,
International Public Policy Institute, University of Strathclyde

# POSTSCRIPT

Having considered at some length, over this three-part series, the turbulent evolution of the Scottish economy over the first forty years of the Fraser of Allander Institute's Economic Commentary, one is tempted to ask: What next? What can we expect the journey of Scotland's economy to look like over the next forty years?

I am tempted to seek refuge in the almost-inevitable futility of any such exercise. Forecasts, especially economic forecasts, turn out, much more often than not, to be wide of the mark. I suggested, in the final two sentences of part three of this series that the shadow cast by the great banking crash of 2008 was proving to be "a very long one. One that will continue to impact the Scottish economy for years to come."

Since writing "Forty Turbulent Years", we've experienced further downward pressure on the price of oil and falls in global equity markets over the first two weeks of 2016 that are, on some measures, claimed to be the steepest since 1928 and the Great Depression. Even the current UK chancellor of the exchequer, George Osborne, having sounded quite bullish in his autumn statement to MPs in late November, went to Cardiff six weeks later to warn of "a dangerous cocktail of threats" facing the UK economy in 2016.

He pointed to growing problems in four of the five BRICS economies. China slowing rapidly and suffering steep stock market falls. Brazil, Russia and South Africa all with mounting problems. Only India behaving like all five were supposed to be performing when the BRICS acronym was first coined.

Continuing rock-bottom official interest rates here, in the eurozone and the US are also playing their part. There is even talk that the Federal Reserve in Washington might have jumped the gun in raising its official rate a notch. In Cardiff George Osborne acknowledged the risk of secular stagnation in economies were the monetary authorities keep interest rates at record lows for years to boost growth but risk creating fresh asset price bubbles in the process. Or raise interest rates to prevent such bubbles forming and trigger another economic slowdown.

He insists that's not the choice the UK has made. But, in the latest surveys, business confidence seems to be softening. Little more than a week after he spoke, Tata, the Indian owners of the last major steel works left anywhere in the UK, Port Talbot, announced more than a thousand more job losses, most of them at that plant. And here in Scotland the plummeting oil price is having a profound impact on the economy of Aberdeen and the north-east.

The non-oil Scottish economy barely grew at all in the second and third quarters of 2015. Throw in uncertainty about the outcome of the promised EU referendum and continued constitutional wrangling within these islands and, despite the UK chancellor's insistence that his plan is working, there is a lengthening list of risks facing our economy too.

What's to be done? Governments, in whatever constitutional form, are all the better for constructive non-partisan analysis and challenge on their fiscal and policy priorities. Here in Scotland the Fraser of Allander Institute is developing clear plans to play its part in that process. Back in 2003/04, under the auspices of FAI and with substantial support from a number of commercial sponsors, the 'Allander Series' was published. Distinguished international thinkers in their fields presented their findings at a series of eight seminars. One in particular - James Heckman's work on the significance of early years intervention in skills development - has had a profound impact on the formulation of policy since by successive Scottish governments.

The Allander Series, driven through to realisation by the then Labour MSP Wendy Alexander, seemed to me at the time to draw some of its inspiration from the big-tent policy-making in vogue in unconventional policy interventions in the years immediately after the Second World War. If today's risks and uncertainties persist, the day may not be far off when we have to relearn, yet again, just how these interventions managed to achieve what they did, at a time when so much needed to be done.

Alf Young, Visiting Professor,
International Public Policy Institute, University of Strathclyde

# FORTY TURBULENT YEARS

How the Fraser Economic Commentary recorded the evolution of the modern Scottish economy

FRASER OF ALLANDER INSTITUTE

**Author Details**

Alf Young
Visiting Professor,
International Public Policy Institute,
University of Strathclyde
alf.young@strath.ac.uk