The future of Scottish money

The following article was written for EIR *by R. Craig Campbell, chief economist of the Scottish Council Development and Industry. It is written in a personal capacity and does not necessarily represent the views of the Council, which is an independent, non-governmental body, concerned with furthering economic development. The council is financed by voluntary contributions from industry, commerce, trade unions, and local authorities.*

Scotland has been in economic and monetary union (EMU) with its neighbor England since 1707. Yet it remains a distinct nation. Why, then, is there so much fuss over the United Kingdom entering economic and monetary union with our European neighbors? Scotland has retained several tangible aspects of nationhood—its own education system and a separate legal system. Less tangible but nonetheless real are a sense of fellow-feeling and cultural artifacts that are distinctly Scottish. Aiding and abetting the intangible qualities of identity is our money: We still have Scottish bank notes.

Three Scottish clearing banks issue notes under their own name. They have direct sterling equivalence and bear the imprint: "Promise to pay the bearer on demand—pounds sterling." Notes are in denominations from £1 to £100. Indeed only Scotland has £1 notes. In England it has been wholly replaced by coinage.

Because Scottish notes have only sterling denomination, the debate over EMU in Europe has special significance. If there is no sterling, our existing note issue must disappear. Therefore, its retention must be sought through a note issue denominated in another currency. The best candidate is the deutschemark. That is, Scottish banks should negotiate a new note issue which promises to "pay on demand" deutschemarks, not pounds.

This is not an idea wthout precedent. Prior to entering the United Kingdom's EMU, Scotland used a variety of currency. Like all small nations in earlier times, the currency of Scotland was made up in large part by the coinage of the countries with which it traded. For all practical puposes, the currency was the gold and silver content of coins, regardless of their country of origin.

Merks (surely from the same linguistic root as marks) appeared in 1579, having been authorized a year earlier. They were a replacement of an earlier set of coins called nobles. Because nobles were too easily forged, being made of base metal, merks were seen as a "hard currency" replacement probably inspired by the thaler (or dollar) of Bavaria, which was in circulation throughout Europe. Indeed, the two-merk piece was often called a "Thistle Dollar."

Merks were a hard currency. Between the original date of issue and 1705, the merk's value relative to sterling did not waver. By coincidence, the exchange rate was 3 merks=£1 sterling, i.e., not very different from the current deutschemark-sterling rate.

How could a new note issue be introduced? Without it, Scottish bank notes will wither away, along with sterling. A Scottish D-merk could come about if the Bundesbank was prepared to allow its existing copyright to be extended to the Scottish banks. The actual mechanism would be by Scottish banks making commercial deposits with German banks to the full value of the notes issued. Following this method requires no regulatory action: Money supply in both countries would be unaffected. While the Scottish banks' right to issue notes may require some extension to liberate it from sterling, there is no difference in principle from the existing note issue.

What are the prospects for EMU and the United Kingdom's participation? Mr. John Major's two proposals look like an attempt at avoiding full monetary union. Firstly he proposed competing currencies. Secondly he proposed a dual system of national currencies plus a "hard" ECU [European Currency Unit]. The latter proposal involved a super-ecu which would be constructed so as to never depreciate against the strongest national currency. On past performance such a super-ECU would be indistinguishable from the deutschemark. Indeed there seems little point in reinventing it.

The number of likely scenarios has been reduced by Mr. Karl Otto Pöhl's rejection of Mr. Major's formula in his London School of Economics speech of Nov. 9. Now that the dual currencies idea has been laid to rest, the United Kingdom has to face the decision of whether to be part of the "inner-core" of European Community member states who will operate a single currency, or whether to remain "semi-detached." It appears to have been Mrs. Margaret Thatcher's determination to stay in the latter group that precipitated the resignation of her deputy prime minister, Sir Geoffrey Howe.

Not being in the mainstream of monetary arrangements in Europe would be particularly dangerous for Scotland. Financial services are our biggest industry in employment terms, and there is special expertise in insurance products and investment management that should, under the right conditions, find ready markets throughout Europe. In those markets customers will want their financial services products to be dominated in a familiar currency in which they have confidence. In other trade too, a common currency has obvious advantages. About 60% of Scotland's manufactured exports are destined for other EC countries and the biggest single market for Scottish goods, after England, is Germany.

The note issue is part of the whole, but the use of the major European currency in Scotland (if necessary in addition to sterling) would help demonstrate our European credentials.

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Of course, EMU may not come about anyway. The widening of the Community by including more member states may distract attention and delay the process indefinitely. But the concern for money would still remain. The reason is the deepening of the Community by the Single Market measures. Ironically, it was Mrs. Thatcher's nominee, Lord Cockfield, who has been the principal architect of a situation in which changes of money cannnot be avoided.

The Single Market is not just giving us the prospect of free movement of people, goods, and services. Money will move freely also. And for those services whose end product is measured in money terms (savings, investments, life assurance, pensions), there will be increasing attention to their deutschemark value.

The deutschemark is bound to be the standard because people or companies who are obliged to hold cash, even for quite short periods, will want to hold the cash that is least likely to deteriorate in value. Given free movement of money, avoidance of risk will be achieved by trading in deutschemarks whenever possible.

The lesson for Scotland is clear. Our future is European because the consequences of not participating fully outweigh the difficulties of adjustment. Experience of the United Kingdom's EMU has shown that European EMU will not necessarily diminish Scotland's identity. To keep one component of that identity, our money, the Scottish banks should be allowed to issue deutschemark-denominated notes.

A neglected economy: V.P. Singh's legacy

by Susan Maitra and Ramtanu Maitra

The 11-month-old V.P. Singh government of India went out in a puff of smoke on Nov. 7. But it left behind a host of socio-political issues which may take years to resolve. In addition, the government's abject disregard of basic economic matters coupled with expensive populist measures, has helped to further set back the debt-ridden Indian economy.

When former Prime Minister V.P. Singh came to power last December, few were aware of his missionary zeal for social reforms. He had promised the Indian population that he would do his best to arrest the fast price rise of essential commodities, and many had been impressed by his handling of the finance portfolio during 1985-87 under the Rajiv Gandhi administration. At that time, he had worked to loosen the Gordian knot of controls and regulations which have made the Indian economy a high-priced one, suffering from low productivity, poor utilization of available technologies, massive waste, and over-bureaucratization.

Eleven months later, following an ignominious exit, V.P. Singh has little to show as his economic achievement. On the contrary, confusion and paralysis in making policy decisions heightened during this period. With the Eighth Five-Year Plan (1990-95) on the anvil, fights broke out between cabinet ministers and the Planning Commission, who saw in it an opportunity to chart out an alternative development path. Their conceptual outline of a decentralized plan with no firmly defined targets met the wrath of one and all, including that of the prime minister.

After months of being disgruntled and generating plenty of news leaks, the planners came up with a $180 billion five-year outlay with little notion where the money would come from. Being strong advocates of rural development and employment generation, they allotted 50% of outlays to the rural and agricultural sector and cut back on such crucial infrastructural sectors as power, coal, and railways. Now the planners are concerned that with little infrastructure available, the rural and agricultural sectors cannot absorb the 50% outlay.

While it is obvious that money is tight, and the government wasted no opportunity to tell people so, the V.P. Singh