

Prosperity in an independent Scotland

Analysis from the *Legatum Prosperity Index*TM

Much has been made of Scotland's likeness to successful small, homogenous nations like New Zealand in the independence debate. Proponents of the potential of North Sea oil reserves even liken the future success of an independent Scotland to the proven success of Norway.

With New Zealand ranking 1st in the 2016 Prosperity Index, and Norway 2nd, could an independent Scotland really reach the very top of global prosperity?

The challenge is that the debate so far has been heavily focused on the economic side of independence. Yet prosperity is about far more than just wealth. New Zealand is not rich, rather its prosperity is the product of free markets, good governance, and strong society, supported by vital indicators like high levels of wellbeing and good life expectancy. Norway is not prosperous because it is rich, it is prosperous because it has used that wealth to deliver good lives for its citizens.

Using data from the global *Legatum Prosperity Index*TM and data from the first ever UK Prosperity Index, mapping prosperity across 389 local authority areas, we assess the opportunities and challenges for an independent Scotland beyond the simple economics. We find that the path to prosperity for Scotland is more likely successfully travelled as a part of the United Kingdom.

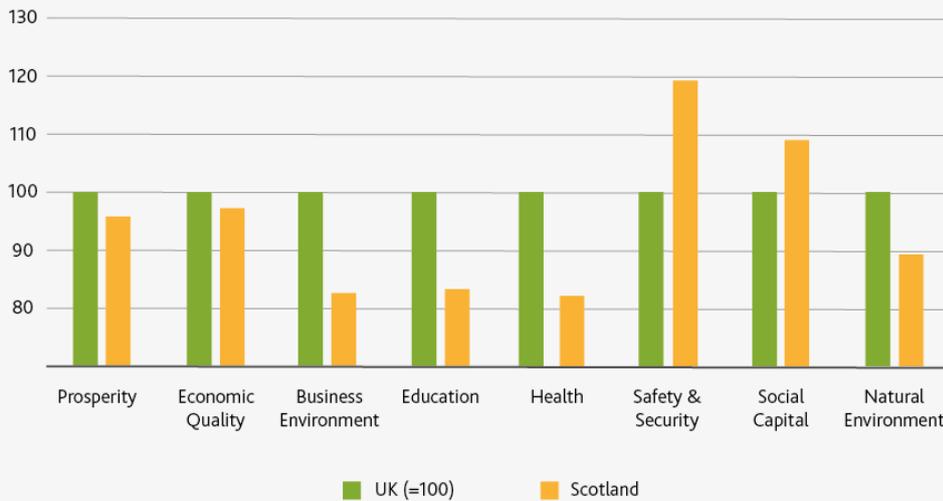
How does Scotland compare to the UK?

The UK ranked 10th in the 2016 Prosperity Index with a prosperity level of around 95% of that of top ranked New Zealand. There is, therefore, potential for Scotland to outperform the UK.

However, it is a long way off doing that. The UK Prosperity Index demonstrates that prosperity is not evenly shared



Measuring Scottish prosperity against the UK average



across the UK. While the two measures are not strictly comparable as they contain different variables, they are measuring the same principles of the journey from poverty to prosperity across the world, and within the UK.

Looking at the breakdown of prosperity across the UK through the lens of the UK Prosperity Index, averaged at a regional level, then Scotland ranks 10th out of the 12 English regions and devolved nations.

In short, Scotland is around 4% less prosperous than the UK average. While this may not seem a large gap to close, the distance is far more significant in key pillars of prosperity (see graph above).

Scotland has the edge in a number of areas. It is nearly 20% safer than the UK average, and its communities are nearly 10% stronger (measured through things like volunteering and perceptions of family and friendship support).

However, Scotland trails the UK average in the other five pillars of UK prosperity. These gaps are significant. Scotland is nearly 20% less prosperous than the UK average in vital areas such as business environment, education, and health. This presents Scotland with both economic and social obstacles to prosperity.

Broader challenges for economic prosperity

The economics of independence are well rehearsed, with key challenges posed by dwindling North Sea oil revenues, a population that is aging faster than the rest of the UK, the largest budget deficit in the OECD, and a significant debt burden.

Increasing productivity to offset the growth-slowing effects of high debt levels and ageing demographics is the ultimate answer to these challenges long-term. However,

the weaknesses in Scotland's wider prosperity make this an uphill battle.

With Scotland's two high productivity sectors – oil and financial services – declining, raising productivity depends on Scotland's environment for innovation. There is talk of tax cuts, but they would have to be significant to compete meaningfully with the low corporate tax environments found elsewhere, including the rest of the UK. They are also not the main driver of innovation, human capital is. Without a highly skilled workforce, innovative capacity is greatly reduced. Here, Scotland's comparatively low Health and Education sub-index performance compared to the UK average presents significant challenges for rising Scottish productivity.

Securing social progress for Scotland

An independent Scotland would benefit from inheriting the UK's strong performance in areas like governance and freedom, backed by its own strong civil society that outpaces the rest of the UK. These structural foundations of prosperity prove important in lifting countries to the top of the rankings. However, we see globally that these are foundations that must be built on if a nation is to flourish. Among the top ranks of the Index, this comes in the form of social progress.

Scotland's problem is that if the economic challenges are significant, which they are, the social ones are arguably more severe.

Scotland has a significant deficit compared to the rest of the UK in health and education. These are devolved areas, so performance is already in the hands of the Scottish Government. Independence is therefore unlikely in itself to alter the outcomes.

Looking at the UK Prosperity Index data illuminates some

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of these outcomes. Within the range of life expectancy in the UK, the Scottish average is around 60% of the UK average. Scottish life expectancy is similar to that in the US or Albania. Truancy rates are over twice as high, cancer mortality is 17% higher, and cardio-vascular mortality a staggering 31% higher than in the rest of the UK.

It is already clear that these are not only issues in themselves, but issues that affect an independent Scotland's economic potential also. Scotland's path towards greater prosperity requires it to tackle the deep and rooted health and educational inequalities when compared to the rest of the UK. Independence is unlikely to make this any easier.

The myth of the oil dividend

Much of the potential success of Scottish independence is hung on the share of North Sea oil revenue that Scotland would receive in a divorce with the UK. The argument runs that if Scotland received its territorial share (90%) then it would thrive as an independent nation.

Ignoring the challenge of weak production and low oil prices, it is worth noting that the global Prosperity Index does not find a positive relationship between oil revenue and prosperity.

Scotland should be wary of relying on its natural resources to bring it prosperity. The evidence is not in its favour. There is statistically no relationship between prosperity and resource rents as a % GDP, regardless of how you cut the data. There is no relationship globally, in the top 50, nor the top 20. Once oil rents become a significant part of GDP (over 10%), a nation is likely to be underperforming on prosperity. There is not an automatic prosperity dividend to be had, regardless of whether Scotland secured 9% or 90% of North Sea revenue. It is not the oil in itself that fuels prosperity, but what is consciously done with the wealth it brings.

Comparing independence to Brexit

Setting aside arguments of sovereignty, there is little statistically to demonstrate that Scottish independence is readily comparable to the UK leaving the EU.

Firstly, the UK is significantly more prosperous than the union from which it is exiting. The UK is the fifth most prosperous nation in the EU, and critically, it can boast the best business environment and the third best

education system in the EU. Globally, the UK ranks 10th compared to the EU's median rank of 30th. Secondly, the UK is more prosperous than the union from which it is exiting in every sub-index of prosperity. In exiting and gaining independence, the UK is theoretically well placed on prosperity to compete effectively against its EU neighbours.

Scotland would not be exiting a union in which it is a more prosperous partner. Scotland's exit from the UK would be more akin to Estonia or the Czech Republic (both of whom enjoy roughly 96% of EU average prosperity) exiting the EU than Britain. Critically, Scotland's comparative disadvantage to the remaining parts of the UK would come in areas critical to success as an independent nation, including the business environment and human capital.

Divorce in a global context

While the two indices are not strictly comparable, we have done some provisional analysis on how the UK (minus Scotland) and an independent Scotland would fare globally on prosperity at the point of divorce.

Based on the UK Prosperity Index, Scotland enjoys roughly 96% of UK average prosperity. Projected onto the global Prosperity Index at a sub-index level and summed to give a 'global' prosperity score, Scotland would rank 18th globally between the US and France. The remaining parts of the UK would together rank 7th, between Australia and the Netherlands. In both Business Environment and Education, Scotland would rank outside the global top 30, and in Health, Scotland would sit in the bottom half of the world.

This obviously does not reflect whatever path towards prosperity may be taken by both the UK after Brexit, and an independent Scotland after its divorce with the UK. It is a reflection of where Scotland would be now if taken out of the UK. These assumptions do not account for the loss of the subsidy through the Barnett formula, which is likely to further exacerbate both economic and social pressures.

What this briefing does demonstrate is that Scotland has challenges to prosperity whether it is a part of the UK or not. However, its international starting point would be significantly further away from Norway or New Zealand than if it were to stay as a part of the United Kingdom. The path to prosperity for Scots is likely better walked in a single, stronger, Union.

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