Business decision-making in conditions of constitutional and political uncertainty in the UK and Scotland: Evidence from business final report

Professor Brad MacKay, University of Edinburgh Business School, August 2014
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1.0 Executive summary

This report presents the findings from 75 semi-structured interviews into the future of the UK and Scotland with senior business leaders in medium and large companies in six industries of strategic importance to Scotland. They include electronics and technology, energy, engineering and industrial manufacturing, financial services, food and drink, and life sciences.

Evidence from independent, politically-neutral studies of business leader’s attitudes towards Scottish independence is relatively consistent. Uncertainty over the currency (with a strong preference for Sterling), EU membership (with a strong preference for remaining in the EU), regulation (with a strong preference for having a common regulatory framework with the rUK), taxation (with a preference for competitive taxation, consistency with the rUK and stability) and the general trading environment, poses a significant challenge to business. The perceived risks associated with such uncertainties expressed by business leaders are highly specific and directly concern business activity. An average of half of business leaders’ surveyed cannot identify any opportunities that independence would present for their businesses. Of those able to identify opportunities, they are less specific or unspecific and tend to relate more to the economics and politics of the debate. Only a small minority can identify an opportunity for business investment and growth.

A majority of business leaders indicate that the potential costs and risks of independence to business outweigh the perceived benefits and opportunities that might occur. Unsurprisingly, PLC companies headquartered in Scotland appear to be more affected than companies headquartered outside of Scotland. Companies supplying to the MoD also report that independence could pose a challenge to their business. A significant number of medium and large companies have the majority of their trade in the rUK (typically 90% rUK, and 10% in Scotland), and appear far more affected than companies whose trade is mainly in Scotland, or is diversified globally. Medium sized, privately owned companies appear more willing to absorb downside risk than PLCs, the latter of who are also concerned about shareholder value. Medium sized, foreign-owned companies trading predominantly in a global market indicate they are less affected by the constitutional debate than PLCs trading primarily in the rUK. Business leaders of smaller medium-sized, private companies exporting globally, and smaller firms whose trade (both customers and suppliers) is predominantly in Scotland are the most likely to emphasise the opportunities presented by the possibility of Scottish independence.

Business attitudes towards Scottish independence are clearly influenced by a combination of where the business is domiciled, customer location, headquarter jurisdiction and ownership structure. This report also reviews two other surveys of business attitudes towards Scottish independence. In all three studies reviewed here, approximately 10% of business leaders indicate they may move business activity out of Scotland in the event of a yes outcome.
2.0 Introduction

On September 18th, 2014, Scots will vote on whether to secede from, or to remain part of the United Kingdom. It is a Union that Scotland has shared since 1707. As the referendum date nears, the debate over whether Scotland would be better off as an independent nation, or as part of the Union has intensified.\(^1\) One of the single most important determinants of any country’s future economic prosperity is business competitiveness and growth. Understanding the implications of the referendum debate outcome for business decision-making can therefore be an important guide to the economic consequences of the vote, and its implications for Scotland’s fiscal position, and wealth creating potential.

The uncertainties posed by the referendum on Scottish independence have the potential to influence any number of business decisions, such as whether to invest, re-invest, expand, withdraw, locate or relocate business activity within or out-with Scotland. There have been several studies whose aim has been to explore business attitudes towards independence, and business decision-making in conditions of constitutional and political uncertainty in Scotland and the United Kingdom. From these studies we are able to develop a broad typology that helps to give an indication of how businesses in different sectors might behave under different constitutional scenarios.

2.1 Project aims

This project involved undertaking 75 interviews with senior business leaders in medium and large companies from across a range of strategically important industries and sectors operating in Scotland. The aim of the project was to explore business decision-making in conditions of constitutional and political uncertainty in Scotland and the United Kingdom, and to develop a number of alternative scenarios around the different possible outcomes from the Scottish independence vote. For instance, a Scottish vote for independence suggests uncertainties around changes in fiscal and monetary policies, regulation of industries, what currency might be adopted, participation in international economic and political agreements and so on. Equally, a vote for the Union could also bring with it other uncertainties including the UK’s future participation in the European Union, what further powers might be devolved to Scotland, or chronic uncertainty brought about by the prospect of future votes on Scottish independence. Such uncertainties have implications for businesses operating in Scotland, including whether to invest and expand capacity, withdraw from the market, locate operations elsewhere in the UK, Europe or the world, amongst others. Such implications may also vary depending on individual businesses, or between industries and sectors.

This project was designed to address a pressing need to conduct independent, objective and systematic research into what key uncertainties are of most concern to business leaders and how they are affecting business decisions, the decisions that business leaders are likely to take under different independence vote outcomes. This research agenda was aimed at generating evidence that helps business decision-makers, policymaking officials and the public to assess and predict the

implications of a Scottish independence referendum for business decision-making. By identifying the key types of uncertainty that are of concern to business leaders, developing a decision-making typology of the possible decisions that business leaders might take against the backdrop of constitutional and political uncertainty in the UK and Scotland, and developing alternative scenarios around possible independence vote outcomes, this research study also seeks to provide business decision-makers, policymaking officials and the public with decision-making tools that can improve and support decision-making in such circumstances. Such conceptual tools are useful for informing the wider public debate on the implications of a Scottish independence vote for business decision-making by bringing research evidence to bear on this critically important issue.

2.2 Research methods

The research methods that this project applied were inductive, semi-structured, qualitative interviews designed to surface those uncertainties that are of most concern to business leaders and the extent to which uncertainties are likely to impact on business decision-making. Business leaders were asked a range of questions pertaining to what, if any, uncertainties the independence debate posed to their businesses, whether it presented opportunities or risks to their business operations or strategies, if it had any material impact on business decision-making, or whether it might under different constitutional scenarios, and if they had been contingency planning. The interviews were transcribed verbatim, and the data was then coded based on patterns that emerged naturally from the data. Given the sensitive nature of the subject matter, all interview participants and their companies remain strictly confidential.

2.3 Acknowledgements

This study is part of a wider programme of research into the Future of the UK and Scotland. Details can be found at http://www.futureukandscotland.ac.uk/ This research project was funded by the Economic and Social Research Council (ESRC), which is the UK’s largest organisation for funding authoritative, independent and high-quality research on economic and social issues. The ESRC is a non-departmental public body (NDPB) established by Royal Charter in 1965. It receives most of its funding through the Department for Business, Innovation and Skills (BIS). Further details can be found at http://www.esrc.ac.uk/ The project would not have been possible without the additional support of the University of Edinburgh Business School (UEBS). Details about UEBS can be found at http://www.business-school.ed.ac.uk/

I would like to express my gratitude to the Future of the UK and Scotland programme, the ESRC, and the UEBS for their generous support. I would also like to express my gratitude to my research assistant, Ms. Veselina Stoyanova, for all of her hard work. Most importantly, I want to thank the 75 participants in the study who agreed to be interviewed about such a sensitive, if critically important topic for business.

2.4 Report structure

After outlining the positions of the Scottish Government and the UK Government on independence in relation to business, this report presents the data from 75 interviews between November 2013 and June 2014 with senior business leaders in randomly selected medium (over 50 employees) and large (over 250 employees) companies. This report also draws on two other surveys of business
attitudes towards independence to place the findings in a wider context. In particular, it compares its findings with Bell and McGoldrick’s survey with the Scottish Chamber of Commerce (SCC) of 759 businesses, and Ivory and MacKay’s survey with the Federation of Small Business (FSB) of 1800 small businesses. It also refers to the Aberdeen and Grampian Chamber of Commerce (AGCC) survey of oil and gas companies led by Grant Allan.

3.0 Overview of the Scottish and UK Government Positions

3.1 The Scottish Government position

In a series of papers, the Scottish Government argues that Scotland has a highly skilled workforce, world-class businesses, an internationally recognised brand, a reputation for innovation, and substantial natural resources. It suggests that industrial manufacturing has suffered decades of neglect. The UK economy, it proffers, is dominated by London and the South East. Many of the policy levers for creating jobs and wealth in Scotland are reserved powers for Westminster. The Scottish Government states:

“Control of taxation, public spending limits, regulation of business and industry, and competition policy all rest in London. Successive devolved Scottish governments have had considerable success in reducing unemployment, increasing employment and promoting inward investment. But the fundamental economic decisions that affect Scotland are taken in Westminster, often by governments that have no popular mandate in Scotland, and in the interests of an economy and society with different priorities from Scotland.”

Independence, the Scottish Government maintains, will allow it to reduce Air Passenger Duty by 50 percent, business rates for small businesses, and corporate tax by three percentage points to counter the gravitational pull of London and the South-East. Compliance costs for business will be reduced through a simplified tax system, and, combined with greater control over immigration and capital investment in infrastructure, will improve productivity. Links between businesses, funding providers, public sector agencies and universities will be improved with a coherent strategy and shared priorities. A package of employment measures designed to enhance employee representation and female participation on company boards and to create cohesion and opportunity in the workplace will help to improve fairness and company performance. The economy will be rebalanced through policies to improve innovation and exports and re-industrialisation. They argue:

“An independent Scotland will have the opportunity to pursue policies designed to grow the economy and create jobs. With responsibility for the full range of policy levers, the government of

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6 Ibid.
an independent Scotland will be able to create a more supportive, competitive and dynamic business environment."\(^8\)

The Scottish Government views independence as an opportunity to transform the economy through policy choices that better reflect the priorities of Scottish households and businesses, and to create a fairer society.\(^9\)

### 3.0 The UK Government position

The UK Government argues in their *Scotland Analysis* papers that Scotland has flourished as part of the UK; it is one of its wealthiest parts. Scotland’s economy has outperformed many small independent European states. The UK, they maintain, is one of the most integrated single markets in the world, and Scottish businesses have become successful within that policy and regulatory context. Scotland’s strong sectors in defence, energy and financial services rely on the UK market where a majority of their trade is. As part of the UK, Scottish businesses have a market of 63 million people. An independent Scotland would have a population of 5.3 million. They argue that some 70% of Scottish exports go to the rest of the UK (rUK). In addition, goods, services and people can move freely throughout the UK. Furthermore, business and consumers benefit from the stability of the pound Sterling, shared institutions, regulations, infrastructure and a single labour market. Costs and investment in, for instance, energy, are shared by the UK as a whole. Moreover, costs for businesses and consumers are kept lower by the reputation of UK institutions and the scale of the UK. They argue:

“As it stands, the UK is a true domestic single market – with free movement of goods and services, capital and people. Businesses are able to trade freely across the whole of the UK; consumers benefit from a greater number and variety of goods and services at lower prices; and workers are able to access a greater number of jobs allowing them to maximise their skills and realise their range of aspirations. It is one market with no internal barriers to the flow of goods, capital and labour.”\(^10\)

The UK Government argues that if Scotland were to become independent, the UK would cooperate in areas of mutual interest, as it does with other independent states. There would not be a monetary union with a shared currency with Scotland. Scotland would have to support its own financial sector during crises. Scottish businesses and consumers would no longer benefit from the same borrowing rates available to the UK. Scottish firms might no longer be eligible for bidding on MoD contracts. Costs and investment in, particularly, energy, would no longer be spread across the UK as a whole, but borne by Scotland. Scotland would have to set up its own funding councils for universities. Trade might also be reduced by ‘border effects’ caused by trade barriers between the UK and Scotland.\(^11\) They state:

“The UK’s shared business framework helps drive growth and competitiveness across the UK, and is at the centre of Scotland’s success in creating businesses that can compete on the world stage. This

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\(^11\) HM Government. (June 2014). *United Kingdom, united future: Conclusions of the Scotland analysis programme*
UK-wide framework and guaranteed access to the whole of the UK’s domestic market, underpins FDI in Scotland.¹²

They conclude that Scottish business has the best of both worlds: they have the benefit of the size, stability and strength of the UK, and they are also supported by the focused and targeted efforts of the Scottish Government using devolved powers.

4.0 Evidence from business

The following section begins with an overview of the sample. While 75 interviews were conducted with senior business leaders, this report presents the evidence from 72 business leaders interviewed from six industries. Three participants were from other industries. The report goes on to present data on business attitudes towards the opportunities presented by the independence referendum outcome, the risks, and finally, on what contingency planning is taking place in businesses, and on whether the debate is having any material impact on business decision-making.

4.1 The sample

In-depth interviews were conducted in six, broadly defined, strategically important, and mobile, growth industries including energy, engineering and industrial manufacturing, electronics and technology, financial services, food and drink, and life sciences. Interviews were semi-structured, meaning that they were a conversation based on five questions relating to whether the referendum posed uncertainties, risks and/or opportunities, whether businesses were contingency planning, if the prospect of a referendum was having a material impact on business decisions, and whether it might under different constitutional scenarios (see Table 1 for industry profile).

<table>
<thead>
<tr>
<th>Table 1: Industry Profile</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>By Sector</strong></td>
</tr>
<tr>
<td>Electronics/Technology</td>
</tr>
<tr>
<td>Engineering/Industrial Manufacturing</td>
</tr>
<tr>
<td>Energy (incl. Hydro and Oil and Gas companies)</td>
</tr>
<tr>
<td>Financial Services (incl. life insurance, retail, wealth management)</td>
</tr>
<tr>
<td>Food and Drink</td>
</tr>
<tr>
<td>Life Science</td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
<tr>
<td><strong>Other</strong></td>
</tr>
</tbody>
</table>

Accurate and consistent statistics on the contribution that individual sectors make to the Scottish economy appear to be problematic to pin down precisely. Available statistics appear to be rough estimates and vary depending on the year and how they were calculated. Industries and sectors can also be categorised and defined in different ways. However, table 2 gives an overview of the estimated contribution in terms of annual turnover that the six industries incorporated in this study make to Scottish GDP, and how this compares to Scottish, UK and public sector spending more generally.

<table>
<thead>
<tr>
<th>Industry (included in the study)</th>
<th>Turnover (Estimated)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aerospace, Defence and Marine</td>
<td>£5 Billion</td>
</tr>
<tr>
<td>Electronics, Engineering and Technology (Manufacturing)</td>
<td>£15 Billion</td>
</tr>
<tr>
<td>Energy</td>
<td>£12 Billion</td>
</tr>
<tr>
<td>Financial Services</td>
<td>£7 Billion</td>
</tr>
<tr>
<td>Food &amp; Drink</td>
<td>£13 Billion</td>
</tr>
<tr>
<td>Life Sciences</td>
<td>£1.9 Billion</td>
</tr>
<tr>
<td>Government/Public Spending in Scotland</td>
<td>£130 Billion</td>
</tr>
</tbody>
</table>

While small businesses (0-49 employees) account for some 98.3% of the 343,105 private sector enterprises operating in Scotland as of March 2013, they make up 42.3% of private sector employment and generate 23.6% of private sector turnover. The 2,270 large businesses operating in Scotland, by contrast, only make up 0.7% of the total number of the 343,105 businesses operating in Scotland, but account for 45.3% of private sector employment, and crucially, generate 63.3% of private sector turnover (see figure 1 for business size, employment and turnover in Scotland). What happens with these businesses following the vote, therefore, is critical for Scotland’s economic prospects during any transition period.  

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As table 3 summarises, in the sample, just over half of the firms were large (250+ employees), while just under half of the firms were sampled were medium (50+ employees). Of the firms sampled, a little over half were registered in Scotland, while the rest were registered outside of Scotland.

Table 3: Company Profile

<table>
<thead>
<tr>
<th>By Size</th>
<th>No.</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large</td>
<td>38</td>
<td>53</td>
</tr>
<tr>
<td>Medium (250-499)</td>
<td>34</td>
<td>47</td>
</tr>
<tr>
<td>Total</td>
<td>72</td>
<td>100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Ownership</th>
<th>No.</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scotland</td>
<td>41</td>
<td>57</td>
</tr>
<tr>
<td>rUK</td>
<td>15</td>
<td>21</td>
</tr>
<tr>
<td>Abroad</td>
<td>13</td>
<td>22</td>
</tr>
<tr>
<td>Total</td>
<td>72</td>
<td>100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Primary Trade/Customers</th>
<th>No.</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scotland</td>
<td>9</td>
<td>13</td>
</tr>
<tr>
<td>rUK</td>
<td>21</td>
<td>29</td>
</tr>
<tr>
<td>Global</td>
<td>42</td>
<td>58</td>
</tr>
<tr>
<td>Total</td>
<td>72</td>
<td>100</td>
</tr>
</tbody>
</table>

Only nine firms, or 13% of the sample, traded predominantly in Scotland, while the rest of the sample either had most of their trade in the rUK or globally (including the rUK). Finally, just under half of the firms sampled were public liability companies (PLC), while around a third was privately owned, and the remainder were either partnerships, or trade bodies. According to Scottish
Government figures, some 65% of employment is in enterprises whose ownership is Scottish, while 16.5% of private sector employment is in enterprises with ownership outside the UK, and the remaining 18.7% of employment is in enterprises with ownership in the rUK.14

4.2 Opportunities posed by the independence referendum

In the interview-based research across six industries, 29 business leaders (of 72) reported that they had yet to identify any obvious opportunities for their businesses, and a further 14 indicated the opportunities would be marginal or negligible. Of the 36 business leaders able to cite opportunities, only in eight cases (12%) were they able to cite potential opportunities specific to their business. Seven business leaders indicated that the opportunities presented by independence outweigh the risks, while 65 indicated that, at present, the risks outweigh the opportunities. Opportunities cited tended to relate to tailoring government policy to the specific needs of the Scottish economy, such as export support, rather than specific business opportunities. For instance, one business leader stated:

“I think there are opportunities for a Government with all powers to help with policies that support business, like research and development, perhaps start-up for other businesses, or new businesses that we might start. For example, in China if a new factory is opened, you can get 7-10 years free of corporation tax to allow a business to be established.” (EM/FS20)

And along similar lines, another stated:

“If they genuinely created a low tax and business-friendly environment, whether that’s corporate or personal tax, whether they reduced the amount of legislation which we believe is kind of red-tape and bureaucratic, perhaps around planning and certain compliance issues. You know, business would respond favourable to that; an environment where investment was supported and encouraged. All of these things create a kind of positive business environment. We are not hearing an awful lot of this.” (F&D68).

Other business leaders suggested that, while there might be business-related opportunities presented by the independence debate, they had yet to identify them:

“Intuitively there may be opportunities. I can’t see that there would be significant new opportunities that don’t currently exist today. There wouldn’t be a breakthrough in oil and gas production ...” (EN43).

For many of the business leaders, particularly of larger companies, who cited opportunities that might arise from the independence debate, they also pointed out that for them they would be marginal:

“I think the opportunities for us would be ... For us it’s going to be fairly limited. I think access to government is clearly easier in a smaller country... the question is, what does that access give you? For example, there is Scottish Development International, there is Scottish Enterprise, and they operate in certain overseas markets. To be honest, we tend to work more closely with UKTI out of London because of the breadth of their coverage ... in the UK at the minute, you could argue we get the best of both worlds – we can use Scottish Enterprise in certain cases, we can use UKTI in others, whoever’s got the stronger presence would be how we would think about it.” (EM49).

For almost half of the participants in the study, however, the prospect of independence presented no new identifiable opportunities, and many argued that the complexity and costs to their businesses would go up. As one executive in financial services argued:

“...there is nothing [about] becoming a separate country from the rest of the UK that offers any new markets, or new business opportunities [in our] current configuration ... we’re configured around the market and the institutions of the UK, obviously if you fundamentally change that by turning into two markets you’re absolutely challenging the basis of our success. You’re changing the basis on which [we] have developed and [are] succeeding and I can’t think of anything positive about that really. At the minute we are in the same jurisdiction as the [the rUK] ... we’re in the same market as sixty-three million customers and consumers. [If it’s a yes vote] we wouldn’t be, we’d be in a jurisdiction of five million ... and we’d have an additional regulator to pay for ... and [we’d] have to have different products for the two markets because they would have different tax systems ... I’m not sure of any sort of new markets that would open up just because we leave [the UK] ... we’re part of the UK, it’s one of the most internationalised for reaching jurisdictions in the world.” (FS18).

The business leaders most sanguine about the opportunities came from smaller medium-sized companies (50-90 employees) in all but one case (see Table 4: Identifiable opportunities from the independence referendum outcome). For the majority of these companies, their trade is primarily in Scotland, or global.
As a company executive states:

“I don’t see any risks at all, I only see opportunity. One of the things, as I’ve said already, is that virtually all of our business is overseas, so I’m not particularly concerned about damaging any UK existing business, not that I think there would be any, but it’s really not an issue. The opportunity that we have is to be able to get better Government support in all kinds of ways for exporting activity ... So being closer to policy makers and decision makers in a Scottish Government has actually helped us take the business forward. And in the future one of the things – it’s a lot of little things that sort of add up, so for example, this air passenger duty issue is something that is actually material for us...” (ET29).

The findings from interviews with senior business leaders in medium and large companies are largely consistent with findings from survey responses from FSB and SCC members. In 50% of the interviews, business leaders suggested there might be opportunities posed by the independence referendum outcome. This compares with 49% of SMEs in the FSB study, and 53% in the SCC study.

However, 50% of business leaders interviewed thought that independence would not bring any new business opportunities. This contrasts with 51% of FSB and 47% of SCC members surveyed.
While 13% of the senior business leaders interviewed in the ESRC study could identify a potential business opportunity presented by the independence referendum, in only about 5% of cases was it an opportunity that would lead to additional investment/growth. For example, an opportunity frequently cited, but with no explicit link to either firm growth or investment aside from adapting a marketing strategy, was closer identification with the ‘Scottish brand’. This compares to 1% of respondents who could identify an opportunity for business growth in the survey of FSB members, and 4% of the SCC members. Of the 60 interviews with senior business leaders in the ESRC study, 10% emphasised the opportunities over the risks posed by the independence referendum outcome, compared to 27% of FSB members surveyed.

4.3 Risks posed by the independence referendum outcome

Across the five industries in the ESRC study, business leaders reported that the fundamental challenge posed by the independence referendum is uncertainty over and above the normal business uncertainty that business leaders are used to dealing with, and have an understanding of. But the uncertainties also contain in them a number of key risks that independence could pose to business. The key uncertainties cited in order of magnitude included currency, regulation, taxes (both corporate and income taxes), recruitment and retention of employees, and EU membership. A possible in-out referendum on the UK’s membership of the EU and lingering uncertainty in the event of a no vote were also cited. Where independence presents direct risks to business is with the prospect of the higher costs, complexity, difficulties in accessing key markets, overseas representation and reduced

“The risk is that we’re cutting ourselves off from our largest partner, our largest trading partner. And I think that goes for 9 companies out of 10 in Scotland.” (F&D61)
competitiveness that could result from being in a separate Scottish jurisdiction and a much smaller market from that of the rUK.\textsuperscript{15} Other risks cited included brand reputation, group relief on taxes, pension costs, basic research funding for universities, IP legislation and border effects with cross-border trade. Or as one senior executive from a food and drink company notes:

“The big risk is how will we do business out-with Scotland. Because there is no indication of what currency will be used. The other main concern that I have is the tax regime, because if there is a different tax regime to what we have with the rest of the UK, then it makes it very difficult to go and do export documentation [compared to] if it was a similar regime to what there is between, say, the UK and an overseas market. So the administration to do that would be impossible, or incredibly difficult ... just now we can sell from Scotland to England no problem at all and be cause of the model that we have for exporting whiskey, we can cope with that no problem at all; it’s really the business between Scotland and England if they were two different entities and different tax regimes.” (F&D69)

And another business executive from an energy company stated:

“It’s perceived risk around stability. And I guess there’s a number of subsets of that, so one of them is fiscal...issues around currency... concerns around who the regulators will be, where they’ll be based, what the influence of Europe may or may not be on that... EU safety regulation... there’s questions about Scotland’s EU membership, our infrastructure will cross boundaries ... So there’s a whole host of issues but they all really come down to this question of stability or uncertainty around what these things might look like.” (EN44)

15 The Chicago economist Frank Knight differentiated between risk, which is quantifiable, and uncertainty, which is not, in his 1921 book Risk, Uncertainty, and Profit. Boston, MA: Hart, Schaffner & Marx; Houghton Mifflin Company.
Such risks were particularly salient for companies with HQ functions in Scotland, but substantial trade in the rUK:

“[We deal] with 50 currencies as it is, so you could say at one level it doesn’t make any difference, it’s just another currency. But at another level it’s an extra burden, and actually I don’t think it’s any one of these things in isolation, I think it’s actually almost a cumulative effect of some of these things that might in their own respect be quite modest, but just collectively start to create and add 1) cost to a business, and 2) does it make sense for us to still be headquartered here, particularly when we are not a domestically focused business per se, but more of one that is operating in a UK-wide context, or indeed a global context ... corporate borrowing costs are impacted by the explicit sovereign rating of the jurisdiction of which they’re headquartered.” (EM49).

And other executives, while expressing a similar sentiment about the uncertainties, also pointed to related risks about what influence an independent Scotland, as a small country, could be expected to have internationally:

“It’s more about the medium-to-long term risks to the business. It’s largely about our access to markets and our representation overseas. Our industry relies very heavily on the UK in Europe to provide as level a playing field as possible for us. You know, we have a major trademark in terms of Scotch whiskey as a category, and then the brands within that and the IPR protection of that definition is respected in the UK in Europe. And the risk associated with that are pretty serious, you know, how powerful a smaller independent country would be in defending the category...Understanding the access to capital and the cost of that is pretty fundamental [in a] smaller economy that will have more volatility around its economy, there probably would be a higher risk premium attached, and the ability to borrow funds or finance projects over the longer term might have higher cost ... if we become independent in Scotland, probably 95% plus of our sales would then take place in foreign territories and the benefits of operating in the country where you have 5% would have to be spectacularly advantageous to counter the potential risk of diseconomies arising in the 95%.” (F&D 68).

Some variation existed across business types. For example, companies with a global customer base, or the subsidiaries of global companies operating in Scotland had more mixed, and often moderate views about risks in contrast with companies with significant trade in the rUK. A minority of predominantly smaller companies with both customers and suppliers located primarily in Scotland, or exporting globally, were also less concerned about the risks posed by independence. As one business leader of a smaller, medium sized technology company executive stated:

“I think the simple answer to [risk] is no. Because sometimes I think the people who are raising the uncertainty issues, I’m not sure they get out enough, you know...we’re all in the EU transacting cross-
border... we’re dealing with a multitude of currencies, different nationalities. So for the life of me, if Scotland chooses independence, I don’t see necessarily why that is going to overcomplicate things. I just can’t see it.” (ET25)

In energy, for example, service companies appeared less concerned with some risks than exploration and production companies in oil and gas and hydro companies. There was more variation in responses from business leaders in wealth management and servicing, particularly where clients were primarily global or Scottish based, than financial services more generally. Firms supplying to the MoD were also concerned about future procurement, as internal EU market rules do not apply to defence acquisitions (Article 296), which are exempted, and also the reputational importance of supplying to the MoD and the ‘British brand’ for exporting internationally. As one company executive of a defence related company argues:

“The thing that really does help us sell in export [markets] is endorsement by the UK MoD. Our armed forces are still regarded in the world defence market as a benchmark [for quality] ... if the [UK MoD] uses something it is thought to be good ... The lack of a [UK MoD] endorsement would be a real issue to us.” (ET27)

Firms with headquarters in Scotland and most of their trade in the rUK were universally concerned about being located in a separate jurisdiction from where the bulk of their customers are (see Table 4: Uncertainties/Risks posed by the independence referendum outcome).

Table 4: Risks posed by the independence ref. outcome

<table>
<thead>
<tr>
<th>Industry</th>
<th>FS</th>
<th>LS</th>
<th>E/T</th>
<th>E/M</th>
<th>E (0&amp;G)</th>
<th>F&amp;D</th>
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<tbody>
<tr>
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<td>2</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>Regulat. Changes</td>
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<td>3</td>
<td>1</td>
<td>1</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>Personal Taxes</td>
<td>10</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>4</td>
<td>8</td>
</tr>
<tr>
<td>Corporate Tax</td>
<td>8</td>
<td>–</td>
<td>2</td>
<td>4</td>
<td>5</td>
<td>–</td>
</tr>
<tr>
<td>EU</td>
<td>8</td>
<td>–</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>9</td>
</tr>
<tr>
<td>UK Services</td>
<td>15</td>
<td>–</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Recruit./Retent.</td>
<td>7</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>–</td>
</tr>
<tr>
<td>Comp/Client Reloc.</td>
<td>5</td>
<td>–</td>
<td>–</td>
<td>5</td>
<td>–</td>
<td>3</td>
</tr>
<tr>
<td>Reputation</td>
<td>5</td>
<td>1</td>
<td>3</td>
<td>3</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Investment/Financ.</td>
<td>–</td>
<td>4</td>
<td>3</td>
<td>4</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Pension/Coms</td>
<td>3</td>
<td>–</td>
<td>–</td>
<td>2</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>No vote/EU Referen.</td>
<td>1</td>
<td>–</td>
<td>1</td>
<td>2</td>
<td>1</td>
<td>–</td>
</tr>
<tr>
<td>rUK/Scot Collab.</td>
<td>–</td>
<td>2</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>3</td>
</tr>
<tr>
<td>Licen/ Lab. Laws</td>
<td>–</td>
<td>–</td>
<td>1</td>
<td>4</td>
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<td>IP</td>
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<td>1</td>
<td>1</td>
<td>–</td>
<td>2</td>
<td>3</td>
</tr>
</tbody>
</table>

For instance, as one executive in the food and drink industry argued:

“All our big customers are based in England. There is huge uncertainty about the currency. And we quite frankly do not want any boundaries to be created between our business and the vast majority of our customers who are based south of the border. So uncertainty with regard to the currency, trading, border/cross-border rules and regulations, will be a barrier for us in terms of our trading ability.” (F&D62).
The findings from the ESRC interview-based research are also largely commensurate with the large-scale surveys of FSB and SCC members (see Figure 3). Only a small minority of business leaders in the three studies reviewed here perceive there to be no risks with independence (5% ESRC, 13% FSB, 23% SCC), while a substantial majority suggest that there are (95% ESRC, 87% FSB, 77%). Extrapolating from the frequency by which the risks of independence are cited compared to the opportunities, it appears that the perceived risks outweigh any identifiable opportunities that independence might bring, at least in the transition period following independence (90% ESRC, 51% FSB) (see Figure 3: Uncertainties/Risks posed by the independence referendum outcome).

While the major risks posed by uncertainty around the currency, taxes, and the EU were largely consistent across the surveys, there was also some variation with other risks. Business leaders in the FSB survey, for example, were more focused on the practicalities of independence, such as cross-border invoicing and VAT payment, or postal and shipping charges, whereas the SCC survey also emphasized concerns over the transition period to independence and the general business environment.

### 4.4 Contingency planning and impact on decision-making

At the time of conducting the interviews, the degree of contingency planning taking place in firms varied markedly. It included: (1) none at all, (2) discussions, (3) monitoring risks, (4) analysis and tactical planning around specific

“At the end of the day, I will have to go with whatever is decided above my head. I don’t have any control over it so I don’t worry about it. And if we go Independent, I will have to deal with it. I’ll just feel that it won’t help my business, particularly the amount of export that I do, and I think you know the cost of my business will go up. And I want to become more competitive, and I want to create more jobs. And I want to get manufacturing back in Scotland and the UK in general.” (EMS9).
How might the referendum vote affect business decision-making?

“But this isn’t a complex or complicated debate for us. It’s really very straightforward. We have 3 categories of stakeholder whose interest we need to bear in mind: our customers, our shareholders, and our employees. And we’re a PLC ... so our shareholders’ interests are obviously of paramount importance. So it’s, does the economic environment in which we operate, does it support the continued sustainability of the business and the future prosperity of those three groups. And if it doesn’t, what do we do about it. It’s not a political debate for us. It isn’t complicated. But it’s trying to take the politics out of it that’s the difficult thing. If you take any of those three stakeholder groups, employees for example, it’s very difficult to, in their minds, to differentiate between the political statement and the statement protecting stakeholders’ interests. So it’s quite difficult....But in terms of understanding what the right thing to do is, that’s not difficult at all. That’s not difficult. We’ve got to protect the interests of those three groups.” (FS6)

For instance, of those business leaders who were dismissive of the risks, they either argued that managing uncertainty was a part of business life, or that it was too uncertain to contingency plan. One business leader, for example, suggested that uncertainty might give his company an advantage over more established rivals:

“None [contingency planning] at all, as I say, I can only see positives if Scotland were to gain its independence. And I think a lot of the debate up here around issues going across the border are just overheated nonsense frankly ... I think the whole question about does the uncertainty cause issues for the business totally misses the point that businesses are all about managing uncertainty. If everything was certain the only companies that would survive would be the giant behemoths. It’s the smaller companies like ours that actually seek out uncertainty because that the way you can get a jump on established competitors.” (ET29)

While others argued it was simply too uncertain to plan. As a business executive summarised:

“We’ve just really had high level discussions, but it’s very difficult to go and make any contingency plans because we don’t know what the framework is, and until you get the framework, then you can start making some plans.” (F&D69)

While 64 of 72 business leaders interviewed indicated that it was business-as-usual (see Table 5: Contingency planning and impact on decision-making and strategy), there was also a range of contingency planning taking place at the time of the interviews.

Contingency planning in the majority of businesses at the time of conducting the interviews was informal:

“[Our contingency planning is] very informal. There has been no contingency plan, though I’m being asked more and more, what would you do if Scotland were to go independent... we could be based anywhere.” (FS14).
A number of businesses were also doing ‘what if’ scenario planning:

“There are not contingency plans … It’s more what if this could happen … it’s trying to think about it from different stakeholders – from our owners, from our employees, from our clients and from the regulator.” (FS4).

And for other, primarily foreign owned subsidiaries of global companies, business leaders indicated that they were relying on business continuity plans:

“We have contingency plans for our business in terms of if there was any dislocation of our business here … and we have the ability to switch this business here to any of our centres across the world.” (FS5)

Eight business executives, however, also indicated that they were delaying investment decisions. As one business executive, reflecting several other interview responses, stated:

“I’m delaying decisions, I’m delaying big spends. I have to now. I have to now because the vulnerability we have to currency, because we’re an exporter, could leave us very exposed. So I’m trying to build reserves at the moment so I can work out what to do. I can’t risk leaving ourselves close to the edge, I can’t risk it. We have no idea what the regulatory atmosphere, well, we know it’s likely going to be more social welfare, so we know taxes are going to have to go up … “ (FD64).

In the sample, ten business leaders indicated that they either had, or were “buying the option of restructuring the business” (EN37) to move some of their business activity out of Scotland, generally by registering companies in the rUK. But others suggested that such options already existed because they had operations throughout the UK:

“I suppose, arguably, the fact that we’ve already got a clear established growing operation in England, and a fairly solid, stable operation in Scotland, you know, that probably gives us options, because we’re already established.” (ET21)
And another stated:

“You know, our Scottish roots are so strong and we’re very committed to our Scottish base and our Scottish workforce…we also have an office in London and we can change responsibilities between various offices…we have the ability to do that…we [could] continue to operate in the way we do [now], we’d just have a different registration, [which] is a possibility” (FS1).

And in a similar vein, another business executive suggested that they’d taken decisions to structure their business to give them flexibility in where they located it:

“And when [the question was asked] ‘what are you going to do if Scotland ends up as an independent country’ [by our investors], well we have structured our business in such a way that we can up sticks and move. We know everything that we need and so we have an outlined contingency plan if we need to shift … if circumstances were appropriate then we could move” (EN45).

Other business leaders indicated that they’d taken decisions to diversify any risk by setting up operations outside the UK entirely:

“You know, I can’t afford to move the business, nor would I want to … but if there are problems by way of labour migration or customers not wanting to necessarily trade as easily, or suddenly I’m a Scottish supplier and not a UK supplier, then I’m building a supply chain, a near-shore supply chain as a contingency.” (EM57)

Of the 72 business leader interviews for the ESRC study reviewed here, approximately 75% suggested that the referendum outcome, if a ‘yes’ vote, would have an impact on strategy/operations (this compares with 67% of FSB and 49% of SCC members). But what that might be was less certain. Around 10% indicated that they’d deferred some investment until after the referendum (compared to 18% of FSB members).

Interestingly, in a recent survey of oil and gas companies, 45% of firms suggested that investment plans were being reviewed or deferred until the referendum outcome is known, while 38% of companies, many of whom operate globally, indicated it would make little difference to the sector (contrasted with 18%, primarily small companies that thought it would be a positive development for the sector, and 12% primarily medium sized companies that thought it would be negative)16 (see Figure 4: Independence debate impact on decision-making).

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In other surveys of business attitudes towards independence, some business leaders indicated positive changes of strategy and/or operations, including adapting marketing to identify more with the Scottish brand, adjusting operations to adapt to changes in the business environment, or focusing on the Scottish side of the businesses. In each of the surveys, a very small minority indicated investing or expanding the business. In 13% of interviews in the ESRC sample, however, business leaders implied that they had, or were developing contingency plans, or they’d invested in ‘the option to restructure’, depending on what materialised following a ‘yes’ vote (compared to 10% of FSB and 10% of SCC members surveyed). The option to restructure generally referred to migrating/relocating economic activity out of Scotland.

5.0 Conclusions

Evidence from independent, politically-neutral studies of business leader’s attitudes towards Scottish independence is relatively consistent. Uncertainty over the currency (with a strong preference for Sterling), EU membership (with a strong preference for remaining in the EU), regulation (with a strong preference for having a common regulatory framework with the rUK), taxation (with a preference for competitive taxation, consistency with the rUK and stability) and the general trading environment, poses a significant challenge to business. The perceived risks associated with such uncertainties expressed by business leaders are highly specific and directly concern business activity. An average of half of business leaders’ surveyed cannot identify any opportunities that independence would present for their businesses. Of those able to identify opportunities, they are less specific or unspecific and tend to relate more to the economics and politics of the debate. Only a small minority can identify an opportunity for business investment and growth.

A majority of business leaders indicate that the potential costs and risks of independence to business outweigh the perceived benefits and opportunities that might occur. Unsurprisingly, PLC companies headquartered in Scotland appear to be more affected than companies headquartered outside of Scotland. Companies supplying to the MoD also report that independence could pose a challenge to
their business. A significant number of medium and large companies have the majority of their trade in the rUK (typically 90% rUK, and 10% in Scotland), and appear far more affected than companies whose trade is mainly in Scotland, or is diversified globally. Medium sized, privately owned companies appear more willing to absorb downside risk than PLCs, the latter of who are also concerned about shareholder value. Medium sized, foreign-owned companies trading predominantly in a global market indicate they are less affected by the constitutional debate than PLCs trading primarily in the rUK. Business leaders of smaller medium-sized, private companies exporting globally, and smaller firms whose trade (both customers and suppliers) is predominantly in Scotland are the most likely to emphasise the opportunities presented by the possibility of Scottish independence.

Business attitudes towards Scottish independence are clearly influenced by a combination of where the business is domiciled, customer location, headquarter jurisdiction and ownership structure. In all three studies reviewed here, approximately 10% of business leaders indicate they may move business activity out of Scotland depending on what materialises in the event of a ‘yes’ outcome.

For the ESRC study reported on here, the implications of the findings for, particularly larger businesses, are that the referendum outcome could influence significantly the decisions taken by firms on whether to invest, divest, expand, withdraw, locate or relocate business activity. This is particularly the case for the 100 large firms that constitute the ‘competitive core’ of business in Scotland, which are the backbone of the Scottish economy. The decisions that these firms take following the referendum vote, particularly if it is a ‘yes’, will depend, not on the outcome of the negotiations, but on their direction of travel. If it looks like a currency union is unlikely, for instance, or that independence will create any trading barriers between Scotland and its biggest market, England, it is likely that several headquarters of the larger PLC companies from across the industries sampled here, will be moved out of Scotland. The prospect of independence poses a particular challenge for the majority of businesses in Scotland because of idiosyncrasies around the nature of the Scottish economy; the Scottish economy is highly integrated with, and dependent on the wider rUK economy. If, of course, the sort of wide-ranging partnership that the Scottish Government is advocating with the rUK was to materialise, some of the drop in private sector economic output that we can expect from a ‘yes’ vote might be mitigated. Of course, a ‘no’ vote also brings with it uncertainty, particularly over what further powers might be devolved to Scotland (and whether such powers might create divergence between Scotland and the rUK in terms of tax policy and the fiscal regime), whether such powers might be devolved at all, and the possibility of a UK in/out referendum on the EU depending on the outcome from the 2015 general election.

While it is certain that there will be costs in any transition towards a new constitutional arrangement, it is uncertain what those costs might be, or how long it might take to recoup them. Some academic work suggests that there are three components to transition costs: they include the fiscal costs of setting up new institutions, the costs of disentangling the two states, and the effects of uncertainty. While the broad range of what the costs of setting up new institutions can be estimated, the costs of disentangling the two states are relatively uncertain. Most importantly, however, are the effects of uncertainty. This report helps to surface what some of those effects might be.

There are three main parameters to the effects of uncertainty, which include how much economic output is lost in the transition to independence, the length of time uncertainty effects are prolonged, and the rate of growth that can be achieved following any transition period. An example developed by Professor Robert Young of the University of Western Ontario in Canada helps to illustrate the point. A seceding region that has a growth rate of 2 percent a year, for instance, but could achieve a growth rate of 3 percent a year as an independent country, but experiences a 3
percent drop in GDP over a transition period of 3 years before a growth rate of 3 percent can be achieved would take 12 years to return to where it would have been as a region, and almost 21 years before all the lost output could be recovered. If the seceding region could only achieve a growth rate of .5 percent higher as an independent country, and it experienced a 5 percent drop in GDP over a transition period of 4 years, it would take about 30 years to return to where it would have been as a region, and around 50 years to recover all of its lost output. How much economic output is lost, how long the transition period from a seceding state to an independent state would take (including how long it would take to conclude all of the negotiations), and how much growth could be achieved afterwards, then, is a significant uncertainty that has wide-ranging implications for Scotland’s prospects.

In conclusion, business leaders point out that the companies having success in Scotland today have achieved it within the market, policy and regulatory context of the UK. If independence changes this, the foundations on which they have built their success also changes.

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The Future of the UK and Scotland Programme

The Future of the UK and Scotland programme is funded by the Economic and Social Research Council (ESRC). Its aim is to bring authoritative and independent social science research to the debate about Scotland’s constitutional future and its implications for the rest of the UK for those people looking for information that stands apart from the politics of the referendum.

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