TRANSITION COSTS IN SECESSIONS

Presented to the International Conference on Economics of Constitutional Change
Dalmahoy Marriott Hotel
September 19-20, 2013

Robert Young
Department of Political Science
University of Western Ontario
young@uwo.ca

©Not for citation without permission.
Introduction

During the short term, without the long view of history, secession is best understood as a process rather than an event. This process is the transition to independence. The transition of a territory in a larger union to become an independent, sovereign state can entail costs that are very substantial. These transition costs are the topic of this paper.

Some economic analysis focuses squarely on the costs and benefits of achieving sovereignty, in both the short and the long term. Another body of economic work tends to ignore transition costs altogether. The latter work can be interesting, but it can also be misleading in practice, and so here we are most interested in the former type of analysis.

This paper explores the magnitude of the short-term costs of achieving sovereignty, to show why the transition is very crucial to the calculation of the net benefit of independence. Then we explore the various types of transition costs, especially as they were analyzed in the debate about Quebec sovereignty in 1995. We then explore the sources of transition costs, and it is argued that the largest portion of the costs is not fixed (inevitable) but rather is variable, depending importantly on the degree of cooperation between the seceding state and the continuing state. This leads to modeling secession as a two-player game, and it is clear that non-cooperation can be a rational strategy in the process of secession. Next, the case of Scotland is shown to echo some aspects of the general analysis of secession costs. Then a short section analyzes how transition costs can be minimized, and another discusses some possible benefits of the transition. A conclusion sums up.

The economic literature on secession
In the debate over Quebec secession, some nationalist economists traced a familiar argument about the advantages of independence. They took the view that a cohesive, flexible Quebec society, with a loyal business class, would benefit from state policies tailored to its particular needs, and would fare better economically than it did as a part of the Canadian federation, where adjustment is slow, government is ponderous, and policies, because they necessarily reflect an inter-regional compromise, are never exactly suited to Quebec’s conditions (Latouche, 1992; Proulx, 1991)

Such views arise in part from models that focus on heterogeneity of preferences and the costs of public goods provision, as in pioneering work by Buchanan and Faith (1987) and Casella and Feinstein (1992). A very influential paper in this tradition attempted to show that “under free trade and global markets even relatively small cultural, linguistic or ethnic groups can benefit from forming small, homogeneous political jurisdictions” (Alesina, Spolaore and Wacziarg, 2000: 1276 [abstract]; see also Alesina and Spolaore, 1997). These authors develop a model relating production, trade, growth, and the number and size of countries; as well it incorporates a variable for the “costs of heterogeneity,” which is an important driver in the model. They proceed to show that smaller countries have benefitted more from being open to trade than larger ones. And they conclude (1294): “an implication of this paper is that as the process of economic ‘globalization’ will progress, political separatism will continue to be alive and well. The concept of relatively large and centralized nation-states is and will be more and more threatened by regional separatism from below, and the growth of supranational institutions from above, in a world of ‘global markets.’”

This may be true - but not because of the authors’ argument. They only perform comparative statics, completely neglecting the process of becoming a small, independent country.
Indeed, the authors warn explicitly about making the kind of statement that they did in their own Abstract: a full accounting of secession “should involve an explicit modeling of adjustment costs and potentially complex transitional dynamics” (1283), which they cannot handle. Their model assumes smooth adjustment as its parameters change, but admittedly this is unrealistic: “in practice, border changes and secessions or unifications are costly and lengthy processes” (1285). The paper is highly incomplete, yet it is part of an influential tradition.¹

Other analysts are interested in the costs and benefits of secession. Some propose very general frameworks, where calculations are not restricted to material costs and benefits (Bartkus, 1999). More commonly, economists focus on the real economy, and are interested in the effects of secession on investment, production, employment, trade, and so on. Bookman (1992) explores economic issues and the impetus to secede, as well as the factors that contribute to the economic viability of the independent state. She also deals at length with the “period of redefinition” - our ‘transition’ - and explores some of the internal and external issues that need to be settled (117-44). As she notes, “there is very little information on the actual process of disassociation” (117). And yet the transition is crucial in determining the long-term outcome of the secession. As I wrote about the Quebec-Canada case, after surveying all the extant economic studies, legal studies, and political scenarios, “the economic costs and benefits of secession would depend mainly on how the process took place” (Young, 1995: 125).

The importance of the transition to independence

From a strictly economic point of view, the desirability of secession depends on whether a regional economy can achieve better economic performance as a sovereign state than it is

¹ For a listing of papers along these lines, see Spolaore (2008). Interestingly, this contribution features a model which has resources devoted to conflict between the seceding and continuing states, which could be extended to the imposition of transition costs.
currently managing as part of a larger union. Once the transition is finished, and a new equilibrium has been reached, performance will depend on many factors, such as the degree of integration that is maintained with the continuing state, relations with other countries within international trade regimes, inflows of foreign investment, labour-force productivity, innovation, and so on. But there is a prior consideration - how costly will be the transition to sovereignty? This question is crucial, because the costs of transition can more than offset the long-term benefits of independence.

Let us assume that a seceding region has a growth rate of 2% per year, but that as a sovereign country it could achieve a growth rate 1% higher. If the transition period were three years, and if the new country’s GDP were 3% lower for those years until 3% annual growth began, then it would return to where it would have been as a region in a little over nine years. As shown in Figure 1, all the lost output would be made up in a little over 16 years. For many inhabitants (always ignoring any non-material benefits of sovereignty) this could be a rational choice. ((FIGURE 1 ABOUT HERE))

In contrast, assume that the growth rate as a region is 2% and that 2.5% could be attained as an independent country. Assume too that the transition period were four years, and that GDP dropped by 5% for this period. In this case, as Figure 2 depicts, it would take about 30 years for GDP to reach the regional level, and a much longer period of time - 50 years - to recover all the lost output. ((FIGURE 2 ABOUT HERE))

Secessionists would have to have a very low discount rate to accept independence under these assumptions, or else they would have to place a high value on non-material benefits. Messy transitions can be crippling (Schroeder, 1992).
The composition of transition costs

There are three main components of transition costs. These are transaction costs, fiscal costs, and the effects of uncertainty. Transaction costs include the resources devoted to disentangling the two states, which bear on both the continuing state and the seceding state, and also the costs of creating the institutions of the new sovereign country. Transaction costs can be substantial. In cases of peaceful secession, the two parties generally deal with a relatively short list of items, and they negotiate expeditiously (Young, 1994a, 1994b). But, as will be discussed below, negotiations can be difficult. In the Czech-Slovak case, for instance, the disposition of cultural properties and secret-police files were not very tractable. Then there are the costs of transferring programs, revenue sources, public servants, and pensions. Dividing the armed forces and its assets is costly, but is always a high priority. The new state must devote resources to international treaty negotiations and foreign representation. It must also build a range of institutions from scratch, and the cost of this varies with the extent of prior institutional development in the seceding region. No advanced industrial capitalist state has ever undergone such a breakup, but transaction costs obviously could be very large. In the Quebec case, where the provincial government had a very large array of responsibilities, Fortin estimated the cost of reorganizing the Quebec state to be only $600million - about .38% of GDP (Fortin, 1992). But not all transaction costs show up as measurable losses of GDP. There are also considerable costs to individuals and firms of learning about and accommodating themselves to the new arrangements. One Canadian economist estimated the cost of “institutional restructuring” as “large” for both Quebec and Canada, meaning over 1% of GDP (Grady, 1991, Table 37). Restructuring can take a few years to complete.
Fiscal costs are the costs of higher taxes to provide the services that are currently provided in the seceding region by the central government. In the Canada-Quebec case, much economic analysis of the transition focused on government finances, rather than on the economy per se. The Economic Council of Canada conducted a sanguine assessment of four alternative constitutional futures, including sovereignty-association (1991). It found that the elimination of transfers would mean that the total tax burden on Quebecers would increase by about 3.3% of GDP (84-5). John McCallum (1992: 39-42) argued that the deficit of a sovereign Quebec would lie in the $10billion to $22billion range (6.3% to 13.9% of GDP) and that drastic cuts in spending would be essential. But of course such estimates depend on how the national debt is apportioned, and this is a matter for negotiation.

The third set of transition costs, and the most important one, is caused by uncertainty. When conditions are changing fundamentally, economic actors have less confidence in their expectations about the future. Perceived risk increases. This applies to individuals deciding where to live, firms deciding where to invest and to place orders, creditors deciding where to make loans, and all other economic activity. The Economic Council focused on financial markets and argued that borrowers would pay extra during the transition to sovereignty-association, because lenders would worry about (1) political risk, or uncertainty about future public policies, (2) default risk, because of uncertainty about the creditworthiness of both the continuing and the seceding state, and (3) currency risk, arising from uncertainly about future exchange rates (1991: 85-6). A rise of 100 basis points in rates would cause a decrease of 1.5% in GDP, estimated the Council. But the effects of uncertainty are much wider, involving migration, savings propensities, firms’ decisions about sources of inputs and market outlets, and investment decisions.

Estimating uncertainty costs is difficult, as the Canada-Quebec case shows. McCallum
and Green (1991: 69) assumed that unemployment would be higher in Quebec by between 1.0% and 2.0% over a five-year period, which would imply GDP drops of between 1.5% and 3%. Out-migration would depress the tax base. An interest-rate premium on government debt of between .8% and 1.6% would mean a loss of between 1.2% and 2.4% of Quebec’s GDP, using the Economic Council’s estimates (60). Another study, by the Royal Bank of Canada, focused on the investment climate. It assumed a 15% decline in investment over the two years following a secession, with investment then growing at 2.5% per year: real GDP would be 17.8% less than it would have been and the unemployment rate would be in the range of 10-15% rather than 7-11% (Royal Bank, 1992: Table 6). Finally, Patrick Grady made the most comprehensive estimate of the short-run costs to Quebec, and estimated the total to be at least 7.4% of its GDP, with the corresponding figure for Canada being 1.9% (1991: 160). Of course, such estimates rest on many assumptions, and they can be contested as extreme (Fortin, 1991). Other estimates were less pessimistic (Quebec, 1991). Predicting high costs can also be dismissed as fear-mongering, designed to discourage voters from choosing the Yes side. But the fact remains, as the Royal Bank economists stated (1992: 23) that “the things that cannot be measured accurately in the current debate are the things that will have the most important influence on the economic consequences of disunity.”

Those ‘things’ depend on the politics of the transition. It is useful here to distinguish between ‘fixed’ and ‘variable’ transition costs. There is some fixed floor of transition costs - resources devoted to negotiation and state restructuring and learning, along with some uncertainty-induced losses, even when negotiations proceed quickly and smoothly. But most costs are variable. They depend on the politics of the separation, on whether and how the two sides reach agreement about managing the secession and the post-independence issues.
Transaction costs would swell were there no cooperation about transferring public servants and pensions and programs. The sharing of information is crucial here. The fiscal costs depend importantly on how the debt and assets are divided, and sharp disagreements about this are probable. Most important, uncertainty is a function of the level of conflict, the gravity of the issues left unresolved, and the time that passes without a clear settlement of issues like citizenship, the debt, the currency, and trade relations, to name only a few. Politics determines the size of transition costs.

Games of secession

Cooperation is essential to reduce the costs of secession to both the continuing and the seceding state. As the Economic Council put it (1991: 88), “the costs of any political change, no matter how radical, can be significantly reduced if that change takes place in an orderly way, with the participants exhibiting fiscal and financial responsibility, as well as mutual respect.” There are strong incentives for cooperation in secessions. However, there are also barriers to cooperation.

The first has to do with the basic structure of the debate about secession. It is to the advantage of the proponents of independence to minimize the perceived costs of seceding: the lower the expected costs, the more likely it is that voters will choose the Yes option. Similarly, the proponents of the status quo have an interest in depicting the costs of independence as high, in order to dissuade people from voting Yes. This means that pre-commitment to certain arrangements is very unlikely. (Pre-negotiation is even less probable.) Moreover, were the Yes side to pledge that a certain outcome would occur, it could be dismissed as wishful thinking; were the No side to do the same thing, it could be dismissed as an initial bargaining position.
The second barrier to cooperation is polarization. This is when there is growing estrangement between two communities, and an increase in solidarity within each one. It is normal in the course of secessions for public opinion to consolidate behind the national leaders, and to congeal in opposition to the ‘other side.’ Polarization strongly marked the break-up of Czechoslovakia (Young, 1994b: 11-18). It is always present to some extent as campaigns become heated and emotions build (Young, 2004: 388-92). But it did not strongly mark the 1995 referendum debate in Quebec, not least because thrusts by sovereigntists to attack the rest of Canada would have contradicted the core promise that secession would be followed by a new economic and political ‘Partnership’ between the two units (Young, 1999: 27-8). Nevertheless, polarization makes compromise harder to achieve.

The third barrier concerns whether cooperation is always rational. This is a question that can be illuminated through simple game theory (Young, 1994c, 1998; see also Brams, 1994: 159-63). This tool is applicable to cases of secession negotiations because they involve two sides, have a range of possible outcomes, and involve threats about a highly uncertain future. Assume that a secession crisis involves two players, Unity and Autonomy, the latter of which has declared an intent to secede. The issue is that of currency arrangements, where there can be four possible outcomes:

- **CU:** a currency union with no representation for Autonomy on Unity’s central bank,
- **CUR:** a currency union where Autonomy does have representation in the central bank,
- **M:** monetization, where Autonomy simply uses Unity’s currency, and
- **SC:** Autonomy establishes a separate currency, or uses another currency.

In the first game, assume that the Autonomists’ preference function is CUR>CU>M>SC. For their part, the Unitans prefer M>CU>CUR>SC. These are quite realistic preferences in
various potential secessions. In the Quebec-Canada case, for instance, the sovereigntists had a credible threat (unexercised and undeclared) to use the US dollar. In any event, these preference orderings produce the well known game of Chicken, depicted in Figure 3. As ever, each player can cooperate or defect. (The figures in brackets refer to the values attached to each outcome by the players, with Autonomy's values on the right.)

In this game, neither player has a dominant strategy. In choosing to defect and achieve the outcome most favourable to it, each risks that the other will do the same, producing the undesirable outcome SC. So one's best strategy choice depends on the choice of the other, and also on the capacity to make threats. If Unity can threaten non-cooperation through declaring itself prepared to live with the SC outcome, and can do so with credibility, then it can force Autonomy to accept M because Autonomy prefers this to SC. Similarly, Unity may have to accept CUR if Autonomy refuses to compromise and appears ready to stick at SC at all costs. So the threat of moving to SC is crucial to attain one's preferred objectives. Note, though, that if each player knows the other's preferences, the same threat can produce a stable outcome at CU. For example, Unity can adopt a cooperative attitude, knowing that it could react to a defection towards CUR by Autonomy through moving towards SC. Autonomy can make the symmetrical calculation. With foresight and information, the players can achieve a compromise at CU.

If preferences are different, of course, the players are not engaged in the game of Chicken. Perhaps the Autonomists really do find the Monetization option intolerable, so they prefer a Separate Currency to it, and have the preference function CUR>CU>SC>M. Assume as well that opinion in Unity has also hardened, so its preferences are M>CU>SC>CUR. Figure 4 shows the resulting game of Prisoners' Dilemma.
In this game there are two stable results, CU and SC. If each actor pursues its first preference by adopting a non-cooperative attitude, SC is the result, and this is a stable outcome because neither side then has an incentive to shift towards cooperation. In order to attain the compromise result at CU, each player must credibly renounce the pursuit of its best alternative. However, each also has to demonstrate its preparedness to accept SC should the other defect; that is, to exercise a deterrent threat. For example, if Autonomy is conciliatory but Unity remains intransigent, the result would be M. Hence Autonomy would threaten to choose SC unless Unity shifts to cooperate - and this is a credible threat because with this preference ordering Autonomy would get a better result at SC than at M. Anticipating this train of events, the two players can find a compromise at CU. But this depends on the exercise of deterrent threats. Indeed, the language of threat is common in debates about secession.

One further consideration has to do with whether secession involves one-shot or repeated games. This is germane to arguments often advanced by secessionists that post-independence cooperation is inevitable. In either Chicken or Prisoners' Dilemma, a credible threat is essential to achieve compromise, and also to avoid being left with the sucker's payoff. But, as is well known, the surest way to have a current threat be credible is to have made similar ones in the past, and to have executed them. If games are to be repeated, therefore, a rational player may accept the short-term losses caused by carrying out a threat in order to establish credibility in a future game where the stakes are greater. Moreover, it seems that the best way to ensure cooperation over the long term is to adopt the meta-strategy (governing many games) of being cooperative, but threatening non-cooperation should the other player defect, and carrying out that threat if necessary: this is playing 'Tit-for-Tat' (see Axelrod 1984). Now cases of secession always
involve repeat play. Despite the frequent use of the analogy, a secession is not a "divorce", because no one is "leaving": immutable geography makes it inevitable that games between the two actors will continue, whatever the constitutional framework. But from this observation one cannot draw the conclusion that cooperation also is inevitable. Indeed, the threat of non-cooperation and the practice of retaliatory non-cooperation in the short term could be seen as the strategy most likely to produce mutually beneficial compromises in the long run.

Echoes in the Scotland debate

Much of the foregoing analysis is reflected in the currents of the debate about Scottish independence. The Yes side argues that Scotland would become sovereign, and that the full range of powers could be devoted to attaining Scotland’s objectives: “the paradox we face is that despite all of these strengths, we are not as successful as we should be. The one-size fits all policies implemented by the Westminster based UK Government are not generating the growth or delivering the social cohesion that Scotland should be enjoying” (Scottish Government, 2013d: 26). Further, with respect to the gaps in growth rates between Scotland and smaller European states and the UK, “it is the view of the Scottish Government that this growth gap is due to the fact that, in a competitive globalised economy, targeted policies designed to capture the unique strengths and address the relative weaknesses of an economy are vital. The current constitution arrangements do not allow economic policies to be tailored to the challenges faced in Scotland. This puts Scotland at a disadvantage and is also evident in the divergence in performance of the economies of other regions within the UK in relation to London and the South East” (28). As the government’s advisors put it, “the issue is not that Scotland is necessarily burdened with poor policies but that the centralization of economic policy levers means that specific policies -
particularly in key areas - cannot be tailored to the specific structure, opportunities and challenges of the Scottish economy” (Scottish Government, 2013c: 24).

The pro-independence forces downplay the transition costs. They provide little information about transaction costs. Indeed, the Scottish Government foresees “a smooth and cooperative transition” (2013a: 10). The various negotiations would take place after the referendum of 2014; as well, Scotland would be preparing a written constitution, along with a “constitutional platform” enabling the transfer of sovereignty from the UK to Scotland, which would occur before the Scottish election of May 2016. Even before the referendum, the government favours discussions with the UK government, information exchanges, and the development of approaches to the items to be negotiated (13).

But transaction costs have been described in great detail by HM Government, with clear predictions. For example, the UK is a signatory to almost 14,000 treaties: an independent Scotland would have to deal with these (United Kingdom, 2013a: 35). Domestically, 140 UK government organizations perform functions that cover Scotland, along with public corporations and advisory bodies: an independent Scotland may need to “create up to four times as many Scottish public organizations as currently exist” (59). The UK government has stressed the high cost of establishing new organizations (GBP15 million for a new policy department), and estimated that setting up a new tax regime could cost GBP562 million (2013b: 48, 51). The Scottish government contends that economic and competition regulation could become simplified and cheaper (2013b).

The fiscal costs obviously depend on the apportionment of the debt (and North Sea oil resources), which have drawn few feints from either side.

Uncertainty is evident. A sounding of business leaders found “a clear message that
unpredictable change and volatility are unwelcome, and potentially detrimental to the stability of the economy” (SCDI, 2013: 18). The consequence of the structure of the debate has caused considerable frustration. “The quality of debate on all sides has been particularly polarised, lacking in real insights beyond the realm of political interests, and has ill-served those players in the economy needing to understand in more detail the advantages and disadvantages of proposals for change and for the status quo” (20).

But this is inevitable. Those opposed to independence have no interest in clarifying matters, even if they could. The publications of HM Government focus on the disadvantages of Scotland becoming independent, and on the costs of transition. There is particular uncertainty about border controls, negotiations with the EU, the debt, and military bases. The UK position is to make pessimistic predictions, warnings, and the occasional threat (2013a, b, c). The whole thrust of the ‘Scotland Analysis’ series is to demonstrate the advantages of union, and to point out costs that an independent Scotland would incur. There is no mention of costs to the rUK (for instance, the loss of seigneurage were Scotland to establish a separate currency or join the Euro), and common interests are mentioned only rarely (UK, 2013c: 66 on the joint benefits of a monetary union). Pre-negotiation, which could reduce uncertainty, is impossible when the UK government actually represents Scotland and its interests. There can be no “unpicking” of the union before a vote for independence (2013a: 42). After such a vote, Scots are warned repeatedly that in negotiations during the transition Westminster will act only in the interests of the rest of the UK: “in the event of a majority vote for independence, the UK government would engage in a process to bring it about. But that does not mean that representatives of the continuing UK would or could facilitate everything that the Scottish Government has said it hopes to achieve through independence or that the details of that process can be spelled out now. ... In any negotiations
following a vote for independence in the referendum, it would be the role of representatives of an independent Scottish state to seek the optimum arrangements for those who would live in it. Similarly, the role of the representatives of the UK would be to represent the interests of those who would remain in England, Wales and Northern Ireland” (2013a: 42).

On the Yes side, the strategy is to stress the long-term benefits of independence and to downplay the costs of transition. There is also the chance to stress that while the UK government might make dire predictions before the vote, after a Yes its self-interest will lead to cooperation, measures to smooth the transition, and joint management in areas of common interest. Dire predictions and threats are therefore bluffs. This is reminiscent of the Quebec campaign, where with great success the sovereigntist side used this argument to counter fear of economic disruption (Young, 1999: 39-59). As the premier of Quebec strikingly stated just before the October 30th referendum, “For heaven’s sake, it’s perfectly understandable that before the 30th all of these guys in Ottawa will say no, no, no, no. Well, after the 30th, they might say yes to a few things” (Montreal Gazette, 21 October 1995). In Scotland, the government’s advisors have put the argument more delicately: “much of the detail of any framework will be subject to negotiation with these partners post the referendum. In that respect, it is important to acknowledge that political considerations will play a role and may cloud pre-referendum comments and policy statements. However, these are likely to differ from the actual decisions taken post-referendum when agreement is likely to take place where there are common interests” (Scottish Government, 2013c: 16). The language of bluff and threat will likely escalate as the campaign heats up.

Reducing transition costs

Given their potential scale, it is useful to consider how transition costs might be reduced.
One obvious method is to pre-negotiate arrangements. This is favoured by the current Scottish government and its advisors, but as discussed above it cannot be contemplated by the government of the UK. Negotiations must await a decision. It is conceivable that there could be ‘back-channel’ discussions between the two sides. This might occur if the Yes side is leading when the referendum is near. But the No forces would run the risk of damaging leaks.

In other secessions, foreign powers have intervened. Generally speaking, outside actors fear the disruption that secessions create, and they have an interest in minimizing them (Buchheit, 1978). In peaceful secessions, they have imposed conditions to minimize transition costs (Young, 1994a: 786-7). In the Czech-Slovak case, for instance, in a face-to-face meeting in London, the leaders of the (then) European Economic Community made it quite clear to the prime ministers of the two component republics that post-secession economic integration between them could not fall below the framework prevailing in Western Europe (Young, 1994b: 49-52). In the case of Scotland, however, there is no such agent in the field. The EU cannot make pre-commitments or enforce conditions on the actors involved.

Another possibility is that the two sides could converge in their separate predictions, reaching tacit agreements. The Scottish government could commit to sterling in a monetary union, for example. There seems to be some parallel positions that the debt should be divided on a population basis. The extent to which Scotland’s maritime boundaries would encompass North Sea Oil is another area that has seen some tacit acceptance of the Scottish position by the UK (United Kingdom, 2013c: 54, note 6). These parallel agreements can be aided by non-partisan studies that can lay out a road map for the secession (Young, 1995; Murkens, Jones and Keating, 2002).

In any event, Scotland and the rest of the UK already have taken great strides in
minimizing transition costs. The UK government has accepted in principle that Scotland can become independent. This is the critical factor that distinguishes peaceful secessions from those that are contested, at great cost. Further, the two sides have agreed to the “principles of good communication and mutual respect,” and to “work together constructively in the light of the outcome, whatever it is, in the best interests of the people of Scotland and of the rest of the United Kingdom” (United Kingdom and Scottish Government, 2012: para. 30). This by no means guarantees cooperation over the transition period, but it sets a standard by which conduct can be evaluated by the public.

Transition benefits

It is intriguing to address, finally, the question of whether there are benefits of the transition. This is a different proposition than assessing the benefits of sovereignty in itself, because the focus is only on the transition period. The primary transitional benefit arises from solidarity. A result of the cohering of the population around a new national project, solidarity is also generated in opposition to the other side. There may be psychic benefits from a sense of unity, but the concrete effect is found in greater support for government leaders, and in the willingness of people to make extraordinary efforts in the national cause. An example may suffice.

In the Czech-Slovak separation, there was an agreement to maintain a common currency, but the Czechs anticipated speculative pressure on the Slovak economy, and they began planning for this in the autumn of 1992 (Dedek et al., 1996: 126-42). It was decided that stamps would be affixed to banknotes to designate them as Czech. About 160 million stamps were printed. On the 4th of January, 1993, four days after the separation, stamping began, mainly at Komercni Bank
but also in some other institutions. Some 10,000 employees worked at this task, mainly on weekends and during the evening. The stamped money - some 65 billion koruna - was transported to 4,000 exchange points, an operation that involved 40,000 people. The exchanges of bills began on 4 February, and were finished for individual citizens by 7 February. The urgency of the situation and the size of the stakes can summon forth such efforts during the transition period.

Conclusion

The process of the transition to independence is vitally important in secessions. Events in the transition period can be very costly, because of transaction costs, fiscal costs and especially uncertainty. These can mount to very high levels, making secession an irrational choice from a cost-benefit viewpoint. Some transition costs are inescapable, but the largest potential components of them are variable; that is, they depend on the behaviour of the two parties that are negotiating or managing the secession. During the transition, it may be rational for each side to raise the costs through non-cooperation. Moreover the politics of the debate about independence are such that ex ante measures to reduce transition costs are unlikely. There are some ways that these costs can be reduced, in theory, but there are also barriers to doing so. Nevertheless, dispassionate scholarship and analysis can help citizens better understand the situation and make informed choices.
**Figure 1:** 3% drop in GDP for 3 years
3% GDP growth thereafter

- **Year 1**
- **Year 9**
- **Year 16**

**2% GDP growth**

**3% GDP growth after transition**
Figure 2: 5% drop in GDP for 4 years
2.5% GDP growth thereafter

- 2% GDP growth
- 2.5% GDP growth after transition
Figure 3: The Currency Negotiation as Chicken

<table>
<thead>
<tr>
<th>AUTONOMY</th>
<th>CO</th>
<th>DEF</th>
</tr>
</thead>
<tbody>
<tr>
<td>UNITY</td>
<td>CU</td>
<td>CUR</td>
</tr>
<tr>
<td></td>
<td>(3/3)</td>
<td>(2/4)</td>
</tr>
<tr>
<td>DEF</td>
<td>M</td>
<td>SC</td>
</tr>
<tr>
<td></td>
<td>(4/2)</td>
<td>(1/1)</td>
</tr>
</tbody>
</table>
Figure 4: The Currency Negotiation as Prisoners' Dilemma

<table>
<thead>
<tr>
<th>UNITY</th>
<th>CO</th>
<th>DEF</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>CU</td>
<td>CUR</td>
</tr>
<tr>
<td>(3/3)</td>
<td></td>
<td>(1/4)</td>
</tr>
<tr>
<td>DEF</td>
<td>M</td>
<td>SC</td>
</tr>
<tr>
<td>(4/1)</td>
<td></td>
<td>(2/2)</td>
</tr>
</tbody>
</table>
REFERENCES


London.


