Editorial

The Impact of Brexit on the UK and the EU

By Steven Blockmans and Michael Emerson

Brexit could have serious economic and political consequences for both the UK and the rest of the European Union. The way things play out will depend on whether the UK leaves in a spirit of partnership following a transitional period of flexible but orderly exit, or whether the split is acrimonious and messy, without properly tying up all the legal ends. If we assume that Brexit does become political reality, and that pragmatism prevails over ill feeling and resentment, we can envisage a more orderly exit. Under this scenario, economic and financial tensions could be limited if both parties tried to strike an amicable separation agreement. But broader political considerations, including the desire of the rest of the EU to prevent emulation of Brexit, might lead to a far more damaging outcome, not just for the United Kingdom.

Impact on the UK

Shortly after a vote to leave, the UK would probably trigger the voluntary withdrawal procedure foreseen in Article 50 of the EU Treaty. That would set the clock ticking to reach a separation agreement within two years, or the UK would revert to the default trade arrangement with the EU, based on WTO rules. Under this scenario, the EU would apply its external customs duties to UK goods and could introduce new non-tariff hurdles for goods (e.g. technical standards and measurements) and especially services (e.g. licences). The EU would be free to impose material restrictions on London’s ability to conduct euro transactions and euro-derivatives transactions, and thereby undermine the position of the City. UK citizens could also lose their automatic right to work in the rest of EU. The EU’s new external border would divide Northern Ireland from the rest of the island and thereby jeopardise the (fragile) peace agreement.

Even in the event of a more amicable separation, there would still be multiple adverse impacts on the UK, which are being thrashed out now on a daily basis in the UK media, and which it may suffice here simply to note.

As regards economic impacts there is an overwhelming majority of serious analyses from government, business organisations, think tanks and academia from within the UK, and the IMF and OECD from the outside, that converge on the following propositions:

- The UK’s trading relationship with the EU would not be as fully reproduced in the single market post-Brexit as it is under the status quo. None of the existing alternatives to EU membership (e.g. the Norwegian model of membership of the European Economic Area, the Swiss cheese model of multiple sectoral agreements, the enhanced free trade arrangement like that of Canada) is attractive for the UK.

- The UK’s trading relationship with the rest of the world would be subject to huge uncertainties beyond membership of the WTO. All of the EU’s existing preferential agreements would cease to apply, and it would be a long and messy process to reconstitute them on a bilateral basis. As for the EU’s ongoing negotiations for new trade deals, for example with the US, India and Japan, the UK would not benefit from a faster inside track on these bilaterally. President Obama and Hillary Clinton, his likely successor, have made it clear that the UK would be sent to the back of the queue for trade deals with the US.
The UK risks damaging all three of its economic ‘crown jewels’, namely the City in financial markets, other service sectors traded in the EU, and its prime location for foreign direct investment aimed at the EU market.

The UK is already witnessing early negative macroeconomic impacts, such as exchange rate depreciation, as a result of strategic uncertainty and dented business confidence.

While the precise economic impact is dependent on many factors, including the eventual trade arrangement between the UK and the EU, most economists agree that it would clearly be negative.

As regards the future of the UK itself, a prolonged period of political instability will follow a Leave vote. Politicians’ heads will roll, the split in the Conservative Party will deepen, and new general elections might be called. Brexit may also trigger a fresh referendum over Scottish independence, reinvigorate Welsh nationalism and even divide ‘Little England’ between its more pro-EU (London and Southeast England) and more Eurosceptic regions (the Midlands and the North).

From an international perspective, there is not a single voice among the UK’s friends in Europe, the Commonwealth, or the world at large that support the idea of Brexit. The EU has ‘multiplied’ the UK’s foreign and security policy interests in the world, and secession would be a ‘de-multiplier’.

Impact on the EU

It is highly unlikely that Brexit would lead to the collapse of the EU. The web of socio-economic ties between the remaining member states has been woven so intricately and deeply over the past six decades that Brexit would not unravel the fundamental post-World War II order in Europe.

But, unfortunately for the rest of the EU, Brexit would not be a zero-sum game. It would fan the flames of growing anti-EU sentiment in Europe and embolden nationalist, Eurosceptic movements, leading to a retreat from the search for EU-level solutions to tackling cross-border challenges. Brexit may trigger a new generation of nationalist leaders (most likely in France, Hungary and Poland) to copycat the blackmail tactics employed by David Cameron to obtain ‘specific status’ arrangements from the rest of the EU, for instance on refugee relocation schemes.

The need to prevent the UK’s exit from the EU from creating a precedent would likely lead to other member states (e.g. Germany, Italy, Spain, Belgium, Luxembourg) imposing tough terms for the separation agreement with the UK. Brexit would increase the predominant influence of Germany in the EU, which in turn could heighten tensions in countries suspicious of Berlin (including France, if Marine Le Pen were to win the presidential elections in 2017).

Germany and its ‘coalition partners’ would nevertheless try to take a lead in putting the house together again with renewed integration initiatives to counter the reputational damage of UK secession. Rhetorical resolve would be immediately forthcoming, but implementation would be delayed as both Germany and France will be caught up in their own election timetables in 2017.

How might Brexit impact on EU policies? There are three likely areas of change: the euro system, the immigration/border management nexus and, more broadly, foreign and security policy.

After Brexit, the eurozone would have more power to drive economic and financial policy in the EU, regardless of the views of the remaining euro-outs. France, Germany and Italy all say they want to make the euro system more robust on the fiscal side, but behind this simple statement the disagreements are profound, with Italy wanting eurobonds, Germany blocking anything that smacks of a transfer union, and France making speeches about the need for an EU ‘finance minister’.

Without the UK, the EU budget would have to do without the approximately €5 billion of net UK contributions (19% of total net contributions to the EU budget in 2014). Also, the weight of the ‘economically liberal’ block in the EU (whose current core members include the UK, the Netherlands, Sweden, Denmark, and Estonia) would decline. While pundits have suggested that a post-Brexit EU would probably become more protectionist, there has been a growing consensus across the Union in favour of liberalising internal markets in goods, services and labour. Progress towards a Capital Markets Union would also continue, although at a slower pace and in a different direction from that favoured by the City of London. Some major US banks have already declared that they might relocate to the Continent.

On the immigration front there is much to be done. Objectively speaking, one can say that the EU needs a quasi-federal border control and asylum mechanism. While such momentous moves are unlikely in the foreseeable future, the need for more common action will remain, and even increase as African migratory pressures build up into something even bigger than the current movements from the wider Middle East. The ability of the EU-27 to tackle cross-border organised crime and international terrorism would be reduced, unless appropriate coordination and cooperation mechanisms are established with the UK.

The broad foreign and security front would perhaps be the least difficult route through which to progress. It is undeniable that Brexit would have a major negative impact on the EU’s global standing and soft power status, its capabilities to play a greater role on global security issues, and its negotiations with the US to arrive at a Transatlantic Trade and Investment Partnership before Obama’s end of term. On the other hand, EU decision-making without the ‘ unruly’ UK would become simpler and lead to more Common Foreign and Security Policy (CFSP). Indeed, without the UK, there would be less opposition to the establishment of permanent structured cooperation in the area of defence, with more pooling and sharing of capabilities, more cooperation on defence planning and the creation of a single military headquarters in Brussels.

Concluding remarks

Brexit would not only be bad for the UK, it would generally be bad for the European Union. Both parties could waste years negotiating a new relationship. At a time when the post-WWII world order is under strain and the market economy is increasingly threatened by protectionism, it is abundantly clear that the EU needs to face the big global issues more resolutely. But if the ‘Remain’ vote prevails in the UK referendum on June 23rd, the EU could gain strength internally through further liberalisation of the single market, and externally as a robust pillar of a liberal order in an increasingly hazardous and chaotic world

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Remarks by High Representative/Vice-President Federica Mogherini upon arrival at the Foreign Affairs Council
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Statement by the Spokesperson on suspension of Mejlis activities of the Crimean Tatars
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European Commission proposes visa-free travel for citizens of Ukraine
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Statement by the Spokesperson on today’s decision of the “Supreme Court” of Crimea to ban Mejlis activities
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Joint Statement by the High Representative/Vice-President Federica Mogherini, Vice-President Maroš Šefčovič, Commissioner Johannes Hahn and Commissioner Neven Mimica on the 30th anniversary of the Chornobyl disaster
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Russian Council on Foreign Relations holds the second meeting of European Union and Russian experts in Berlin
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Ein neuer integrierte EU-Politik für den Arktischen Raum adoptiert
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Anzeige von High Representative/Vize-Präsidentin Federica Mogherini beim Vorstellung der integrierten EU-Politik für den Arktischen Raum
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Algeria

La Haute représentante Federica Mogherini a expliqué dans une réponse à une question parlementaire – mise en ligne le 31 mars 2016 – les détails du processus de révision décidé conjointement avec l'Algérie dont un des éléments est que les deux parties « définiront les modalités et les objectifs de l'exercice commun d'évaluation »
08 April 2016. Link

L'Algérie pourrait être un des partenaires majeurs les plus importants de l'Union européenne (UE) dans son action de lutte contre la pollution en mer Méditerranée et de la préservation de sa ressource halieutique, a déclaré, jeudi à Alger, le commissaire européen à l'Environnement, aux Affaires maritimes et à la Pêche, Karmenu Vella
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Visite en Algérie de M. Christian Danielsson, Directeur Général à la Commission européenne
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Egypt

European Union and partners promote Egypt Gas Connection
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Facility for Refugees in Turkey: Commission delivers an additional €110 million under the implementation of EU-Turkey agreement
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