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Brexit: UK's Savior or Downfall?

By Amelia Charles

Background

On June 23, 2016, the citizens of the United Kingdom voted on a referendum that would determine whether they stayed or left the European Union. In an extremely close vote, the choice to leave won by 51.9% to 48.1%. Since then, a chain of events left the UK in a delicate position moving forward.

On March 29, 2017, a little under a year after the vote, Prime Minister Theresa May submitted Article 50 to the EU. This article gave the UK and the EU until March 29, 2019, to negotiate an agreement.

On March 19, 2018, May and the EU agreed to a 21-month transition plan that was turned down by the UK Parliament in an overwhelming vote. That vote led to a vote of no-confidence in May’s abilities, which she survived.

On January 21 of this year, May submitted a revised transition plan to the British Parliament before meeting with EU leaders on February 7. Four days later, the UK signed a bilateral trade agreement with Switzerland in which no tariffs would be imposed if there is no-deal Brexit.

March 29, 2019 was the UK’s original due date for their departure from the EU. However, an extension was recently granted by EU leaders until October 31, 2019. Although, if the withdrawal agreement is sanctioned by both the UK and EU earlier than that date, the UK could leave sooner.

The Current Plan

The UK’s current plan is composed of two principal parts:

1. A binding withdrawal agreement between the UK and EU.
2. A non-binding set of guidelines to help with future negotiations.

Under this plan, the UK would remain within a customs union with the EU. This means that neither party would impose tariffs on each others’ imports but that they are both free to tax imports from other countries. In addition, the three million EU nationals currently working and living in the UK would be permitted to stay without work visas and vice versa for UK citizens in the EU. Finally, the UK would continue to abide by EU laws, but would no longer be allowed to vote on them.

Economic Consequences

When the referendum was first passed, many people tried to predict how the British economy would be impacted. According to several experts, the GDP was expected to decrease between .3 and .55% depending on what deal was struck with the EU.

Trade

FDI (Foreign Direct Investment) was also expected to fall. Before Brexit, the UK was attractive to investors...
because they could avoid tariffs when exporting to the rest of the EU. With the uncertainty regarding future trade agreements between the UK and the EU, investors were expected to go somewhere with more financial stability. In addition, without an open trade agreement, supply chains would become much more difficult to manage due to different costs and regulations for components. One study forecasted that the referendum would result in a reduction of FDI inflows by 22%. This in turn could lower real incomes by 3.4%. 

If a “hard Brexit” deal was made (no trade agreement), there would be an increase in the cost of exports that would hurt exporters. Companies would no longer be able to use the UK as an English-speaking entry into the European economy, which could result in 5,000 jobs being lost. Another expected result, an increase in the price of imports, would boost inflation and lower the standard of living for UK residents. Additionally, without a trade agreement, customs delays could lead to food shortages.

Currency

Another indicator of a country’s financial wealth is the strength of its currency. Almost immediately after the referendum was passed, the British pound dropped 14% against the US Dollar. While this makes it harder for UK citizens to travel outside of the country, it has resulted in an increase of tourists.

Potential Outcomes

The RAND Corporation funded extensive research concerning the economic implications for eight different trade scenarios involving the UK, EU, and the US after Brexit. RAND found that “the UK will be economically worse-off outside the EU under most plausible scenarios. The key question for the UK is how much worse-off it will be post-Brexit.” RAND also found that the greatest economic loss for the UK would be if it left the EU without a trade deal, in which case WTO (World Trade Organization) rules would apply.

Immigration Consequences

Migration

Brexit has also had a substantial impact on migration. Even before the referendum was passed, employment growth in the UK had slowed. Several factors have contributed to the slowing of immigrants, especially those from the EU. Legal and psychological factors have played a role in light of the uncertainty surrounding the UK’s future.

Migration is also tied to exchange rates. As the British Pound continues to get weaker, it is expected that migration will continue to fall as long as no trade agreement is reached. Any long-term changes to migration will depend on what trade agreement is reached and when. According to some forecasts, the net EU migration could fall by up to 91,000 annually under a liberal new migration system. Under a more restrictive migration system, the number would be even larger.
Economic Factors

Changes in migration are significant because they have a substantial impact on the economy. A reduction in net migration of 100,000 would result in a population decline of 0.15% and migrant share of the working age population by 0.20%. This would in turn result in a decrease in GDP by 0.3-0.55%.

The two biggest issues surrounding Brexit are the economy and migration. The referendum has had an effect across Europe, possibly influencing the decision by Angela Merkel, the current Chancellor of Germany, not to run for re-election.

Citizenship

Migration will also be relevant in a hard-Brexit scenario. As mentioned above, Brexit is likely to have a negative effect on FDI. In addition to supply chains becoming increasingly difficult to manage, companies would have more issues with intra-firm staff transfers. Right now, UK and EU citizens are allowed to stay as residents and employees in each others’ countries. Depending on the agreement reached on or before October 31, that could change.

Since Brexit, there has been a stark decrease of immigrants from the EU. Immigration from outside the EU decreased right after the referendum was passed but has since returned to its normal trend. This is demonstrated in Figure 2.

Geopolitical Consequences

Britain has had a complicated relationship with the surrounding countries, and Brexit has made those relationships even more delicate, especially those with countries that share a border. The United Kingdom includes England, Wales, Scotland, and Northern Ireland.

Scotland in the UK

During the Brexit vote, Scotland voted in favor of staying in the EU by 62% to 38%. Last May, Scotland’s First Minister said, “Once we get some clarity, which hopefully we will in autumn of this year, about the Brexit outcome and the future relationship between the U.K. and the EU, then I will consider again the question of the timing of an independence referendum.” As Figure 3 indicates, Scotland’s contributions are a considerable part of the UK GDP and population.

If Scotland left the UK, there would be many negative repercussions for both countries. England would lose control over important oil and natural gas supplies in Scotland and lose that country’s contributions to the UK GDP. If Scotland became independent, it would become a much wealthier country in terms of GDP per capita, although its debts would no longer be assumed by the entire UK.

Conclusion

If the United Kingdom officially left the European Union, in an act of cessation dubbed “Brexit,” repercussions would ripple across Europe. Many citizens in the UK are calling for a re-vote, as the majority of those who voted in favor of Brexit were older and in a population bracket that is shrinking. How the British economy, immigration, and geopolitical atmosphere are affected will depend on the type of Brexit agreement reached. Negotiations between the EU and Theresa May, as well as between Theresa May and her own parliament, are still underway.

Regardless of what type of agreement is reached, the uncertainty surrounding the future of the UK has already had negative consequences. The world is watching Theresa May and the British Parliament as they decide how to move forward with Brexit.

Will negotiations for a soft-Brexit go through, potentially diminishing negative trade repercussions?

Will the plea of many British citizens for a Brexit re-vote be heard?

Whatever the case, Prime Minister Theresa May and the government need to act quickly to alleviate the uncertainty currently shrouding the country and its fragile economy.

Notes


*On July 23, 2019, Theresa May was ousted from her position and Boris Johnson is now the new Prime Minister of the UK.

Figure 3

Scotland in the UK


% Scotland’s contribution to UK’s GDP

£130bn Scotland

£1.63 Trillion UK

8% Percentage of the UK population that lives in Scotland

5,327,700 Scotland

64.1 million, UK

8%