

# THE ECONOMIC AND SOCIAL CONSEQUENCES OF BREXIT

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## Ladies and Gentlemen,

I have been invited as a former member of the European Commission, but I am speaking in personal capacity. Therefore I would like to start with a personal aspect.

This is my second visit to York. The first time I came to this city when I was a student in Manchester (1992). At that time, the big development in Manchester was the new tram system, which was built with financial support from the European Community.

The met in Manchester was a clear example of the added value of European Community membership of the UK. It helped modernize the city and its neighbourhood, and improved the quality of the environment and the quality of life.

I learned in 1992 in Manchester that Margaret Thatcher had not have too many ideas for the North of England, apart from closing coal mines. The European Community, on the other hand, promoted regional development, and funded projects like the tram system of Manchester.

However, this was also the time when the gap started to widen between British and continental visions regarding European integration.

(And I was witnessing that, since I arrived to Manchester just 3 days before Black Wednesday.)

## EU or EMU?

In the second half of the 1980s, the EU was prepared as a combination of a Single Market and a Monetary Union. However, those two were not equally supported in the UK.

The creation of the Single Market was supported by Margaret Thatcher and her party. But they did not welcome the idea of the single currency and also opposed Jacques Delors' effort to build a social dimension within the Single Market.

Having restructured the British economy and the welfare system, Thatcher was keen to weaken trade union power at home and did not like the idea of social dialogue at EU level.

Jacques Delors, EU Commission President at the time, strove to strengthen the social dimension of the single market, to make it acceptable for working people. He came to England to address the conference of the TUC in 1988, thus won over the British left, but the EU started to lose support among the British Conservatives.

Many in Britain never fully signed up to the continental concept of the **social market economy**, which is also enshrined in EU treaties.

However, British euro-scepticism was particularly energized by the creation of the euro as single currency. Even if the UK has an opt-out, and no one would want to force the UK to give up Sterling, the gulf between Britain and the continent has been widened by the launch of the monetary union.

As we know today, the original design of the single currency was flawed. It wanted to achieve monetary union without the slightest element of fiscal union, which is a bad idea.

John Major was right to negotiate an opt-out from the single currency, and Gordon Brown was also right to introduce the five tests and insist on keeping Sterling.

Today it is not so much the existence of the euro which fuels UK euro-scepticism but its **functioning and performance** (as I heard it from Michael Howard on television this morning).

The Eurozone crisis gave a lot of ammunition to UK Euroskeptics who wanted to prove: „the EU is not working“. It also boosted unwelcome migrant flows from the South to the UK and made it harder to reduce the level of immigration, and many Britons became disaffected when they saw how the community, or more precisely: the Eurozone finance ministers, treated its most unfortunate member, Greece, in the Summer of 2015.

People may ask if this really is the community Britain should belong to.

### Eastern enlargement and Westward migration

Today the main issue in the UK debates is not the euro but the “immigration”. And it is the case because the EU was enlarged towards the East.

The UK was a major advocate of Eastward EU enlargement in the second half of the 1990s.

Undoubtedly, Eastward enlargement gave a boost to capital mobility from the West to East, and **labour mobility from East to West**.

However, even if this was true, it is only about 3 per cent of the total EU workforce which works and lives in a country other than the country of birth. The share of foreign born employees is higher in the UK, but this country is not “swamped” but migrant workers.

These isolationist campaigns in the UK about mobile workers from new EU member states were never honest. First, they failed to point out that EU migrants have consistently remained a minority in the last 20 years as compared to non-EU immigrants to the UK.

They should have added that the first big waves of emigration from Poland, Romania and other countries would not repeat themselves, but after some point the number of new migrants from these countries would certainly decline (and it did).

Finally, the **manufactured image** of the EU migrant was that they would come as a burden on the host society, while the reality is that Poles and others are very active economically, they have higher employment rates than the UK workforce, and they are net contributors to the UK budget.

Contrary to what isolationist UK politicians and some tabloid media editors claim: the UK welfare system is not a magnet, and the UK is not among the EU countries with the highest share of EU migrants within their workforce. (Countries with higher share of EU migrants in the workforce include Luxembourg, Ireland, Cyprus, Belgium and Austria.)

With such gaps between the perception and the reality of EU migration, it cannot realistically be expected that the UK could extract big changes in the EU regulatory framework for the free movement of workers.

Nevertheless, David Cameron did achieve gains in his February deal, which requires a material sacrifice from people coming from Central European countries. Those countries accepted this compromise primarily because they are grateful for the earlier UK position supporting EU enlargement.

The geopolitical importance of the UK being active in Europe was also appreciated by all.

But they would not accept an interpretation that the UK in general “suffers” from immigration from Eastern Europe.

### Managing mobility better

Mobility in the EU is a great asset, but it could have been **better managed** in the UK. For example, more rigorous enforcement of the minimum wage could have helped to avoid that low-paid foreigners undercut local workers.

It could have been ensured that British workers receive better training before and during their employment, and that no job gets advertised just abroad without giving a fair chance to the local community.

More support should have been provided from national and EU funds to municipalities where there is a greater need for public services due to immigration.

All these actions could have been carried out without changing EU rules. In fact they should have been carried out without waiting for the EU to give such advice.

Due to the absence of timely action there are indeed legitimate concerns about the short-term impact of immigration on specific groups of the workforce and municipalities.

The EU itself is also working on updating and upgrading its mobility rules by preparing a document on Fair Mobility. The timing of that was apparently chosen in order to best take into account the needs of the UK, as long as it remains member of the Union.

A lot has already been done to improve the quality of mobility by fostering the cooperation of public employment services among member states, using Eu-

European funds to weaken the push factors of migration and reduce the risk of “brain drain” (or over-qualification) among EU migrants.

Instead of setting one country against the other, the EU can demonstrate its added value if its leaders can embed the question of mobility in a broader assessment of building human capital and managing the single market.

### Live and let live

Even if it is true that labour migration could have been better managed in the UK, it is wrong to see the entire theme of EU membership through the lense of migration related controversies. EU labour mobility should not be used as a trigger for Brexit.

By voting for or against Brexit on 23 June 2016, the UK will decide much more than just its own relationship with the European Union. It is also about what needs to change in the EU in order to function better.

The EU has to function well and be comfortable for all bigger as well as smaller member states.

Therefore, this debate is also about Europe’s overall architecture and political economy.

From this perspective, one needs to recognize that the UK’s membership of the EU is already somewhat special. It’s like a **semi-detached house**. It follows the blueprint of “live and let live”.

The UK has an opt-out from the single currency, it has a handsome rebate from the EU budget, it is not part of the Schengen zone, and it applies the Working Time Directive with a good deal of flexibility.

But this special status can be read in different ways. Some would say that since in the past it has always been possible to find a *modus vivendi* we should be positive now too. If there is a will, there is a way.

Others would say the UK has already exploited its ambivalence for special treatment to the limit so perhaps there should be an end to this à la carte approach. Enough is enough.

Some red lines have already been drawn regarding the free movement of labour in the EU. There is always room for fine-tuning of existing rules and providing resources to those who have to bear greater burdens than others. However, those who want to introduce general restrictions (e.g. quotas) or create different legal categories out of EU workers on the basis of nationality are challenging the very foundations of the Union.

Of course, the EU does give other Europeans the freedom to work in the UK, but it also gives the same freedom to move to British workers, pensioners, companies and investors.

What’s more, and this is crucial, the EU provides the framework within which the UK together with other countries can search for and find effective answers to the growing migration crises but also climate change or foreign policy challenges.

### Brexit and economic performance

The position of the economics profession regarding Brexit is clear and unambiguous. One out of ten economists may say the opposite, but the great majority of economists say the UK would be worse off outside the EU.

To sideline this as scaremongering is irresponsible. Without engaging in medium- or long-term predictions, the fundamental reasons for this negative opinion have to be understood.

**Brexit creates uncertainty.** Uncertainty is the enemy of investment. Falling investment would produce an economic recession and the only question is whether it would be a J-curve, or an L-shape economic development.

England, and in particular the North of England was where the industrial revolution started in Europe in the late 18<sup>th</sup> century. But today there are many international investors operating in the UK which chose their location because the UK is inside the EU.

Uncertainty about the UK's relations with the EU, and in particular about future trade arrangements would trigger downsizing or relocation among them. A period of adjustment, especially if coupled with much weaker Sterling, could bring down unemployment again, but nobody knows how long this would last, and how serious streamlining of the public sector would accompany the restructuring of the private economy.

Needless to say, uncertainty is not only economic but to some extent political and constitutional as well. What will happen to Scotland? What will happen to Northern Ireland and its border with the Republic? What will happen to Gibraltar? Could this become an example of a butterfly effect?

Since in recent years **UK economic performance** (growth of GDP and fall in unemployment) has been better than in the Eurozone, some draw the conclusion that economic regulation in the EU should converge further towards the UK model. For Downing Street, this was also among the negotiating chips.

Those, however, who connect Eurozone turmoil with the superiority of the British business model are mistaken. It is not because of microeconomic structures but a greater macroeconomic independence and elbow-room that helped the UK grow faster.

Comparing the record UK current account deficit to the German surplus gives a better idea about relative competitiveness.

It is not only for Southern European countries, but also for the UK to take inspiration from the well-springs of German competitiveness: the so-called *Mittelstand*, dual vocational training, and the social dialogue. The idea of "cutting red tape" in order to enhance economic performance is certainly too categorical, and too often misleading.

At EU level, the campaign to keep legislation within reasonable limits already serves the purpose of "smart regulation".

### Brexit and social policy

The impact of Brexit on economic performance could be temporary, but its impact on social policy could be long lasting.

The areas **most threatened by Brexit** are employment and social policy, regional development, and education, especially higher education and research. Some say universities would be “crippled” by cutting off EU funding and it would be a loss for Britain and a loss for Europe too.

Employment legislation is indeed the area where most Brexit advocates consider the EU activity and interference excessive and burdensome. It is telling that some of the most vocal Brexit advocates are those who hold or held the **labour and welfare related portfolios** in the Conservative led governments of the recent years.

Recent debates in EU fora may give a clue about the underlying intentions. In 2011 the European Commission proposed a Financial Transaction Tax in Europe and the UK opposed. The Commission proposed a regulation of bankers’ bonuses and the UK challenged that too.

When the Commission put forward the concept for an EU wide Youth Guarantee to eliminate long-term unemployment among young people the UK government was among the most reluctant ones and refused to use the phrase itself, despite a more positive opinion from the House of Lords.

The UK could have used the European Social Fund to help municipalities facing migration pressures but did not.

The UK could have used the European Globalisation Adjustment Fund when major producers were downsizing, but the government decided against.

The UK could have used the European Fund for the Most Deprived to boost the capacity of the food banks, which became so widespread after the Conservative welfare reforms, but it did not in order to avoid that the more caring side of the EU becomes visible in Britain.

The UK has been the country where **pillars of Social Europe**, like the Working Time Directive and Health and Safety rules as well as equality legislation are most often challenged, together with the rights of mobile workers.

One may say it is just the tabloid press, but the current campaign shows how easily the false coverage from the tabloid press can be recycled into political debates.

Perhaps not everything from EU social policy would be thrown out at once after Brexit, but the direction of change would be obvious.

It is true that some of the existing social legislation was made or could have been made by Britain itself. But the EU maintains the same standards for all member states, which is a benefit to the UK economy, helping to maintain a level playing field across Europe.

The UK is counted among the most unequal societies in Europe, especially what concerns the concentration of wealth by the top one per cent, and quit-

ting the EU would further weaken the positions of the more vulnerable groups of society.

### Better EU, better Britain

A better functioning EU is primarily a question of **repairing the single currency** and deal with divergence and imbalances within the Eurozone.

Playing a more active role in the macroeconomic debate the UK could help the Eurozone making progress and finding solutions.

The UK can, and should, make a point about greater transparency and accountability in EU institutions, and it could easily boost its representation among EU staff.

On the other hand, by marginalizing itself, or even exiting the EU, the UK would lose these channels of influence on decision-making in Brussels and Strasbourg.

Make no mistake about it: **Brexit is a way for the UK to marginalize itself.** It is an act to take a back seat instead of a front seat, let alone the driving seat.

No doubt, it is the right of the British people to have a referendum about EU membership. At the same time, it is for British politicians to explain what the real balance of costs and benefits of the EU is for the UK.

On the other hand, it is for the EU as a whole to ensure that the British, together with all other member states, continue to see membership as a win-win game.

People on the continent cherish your history and culture. But nobody believes that Britain should take inspiration from Henry VIII or Robinson Crusoe, when the question is about your relations with the continent in the 21<sup>st</sup> century.

It is not separation or isolation, but close cooperation with your neighbours that makes you richer, safer and freer.

Co-operation often requires compromise with other countries, but it is the only way to move forward.

**United we stand, divided we fall.**