No.19

2016.2.22

To Be or Not to Be in the EU?
"Tough-on-the-EU"Cameron Going to Hold Referendum on June 23

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The EU summit which had attracted much attention as the occasion that would define the future of the UK ended finally at around half past 22:00 local time on February 19. After gaining concessions from both of the EU and the UK, it agreed "unanimously" (President Tusk) on a package of the EU reforms which is called "New Settlement". Hailing the deal, UK Prime Minister David Cameron formally declared to hold a referendum on 23 June to ask whether the UK should remain a member of the European Union or leave the European Union. Concurrently the Government started a full-fledged campaign domestically to persuade the British people to remain in the EU. Since the negotiations on the terms and conditions for the UK remaining in the EU came to a conclusion at any rate, the focus on the Brexit debate is now going to shift from the government negotiations with the EU to the domestic campaign battle on "Stay or Leave", the main theme of the referendum.

At a first glance, it seems that the UK won their assertions in the summit, but the real evaluations over the "Special Status conditions" will be proven by the coming full-scale domestic campaign and the actual voting result of the referendum. Already Jeremy Corbyn, leader of the British Labor Party and others have criticized the UK negotiations with the EU as the "behavior deviating from the substance of the Brexit discussions", and many of the British media show rather a cool response to the summit agreements, as is exemplified by the FT article that the agreements on the EU reforms were "Cameron's Pyrrhic victory" (unrewarding victory won with much loss). A majority response seems to be like that the EU concessions were not enough to urge the "Brexit backers" to change their mind, resulting in the no-win-no-loss situation and therefore there will be no positive influence on the avoidance of Brexit.

Chart 1 David Cameron's Four Pillars of Proposal on the EU Reforms

1. Economic governance	Protect the rights of non-euro members in promoting a single market
2. Competitiveness	Build a more competitive European Union with less regulations
3. National sovereignty	Release the UK from the process of "ever closer union"
4. Immigrant Policy	Allow restriction on welfare payments to the immigrants from the EU

Based on the letter to the EU President dated November 10, 2015

Originally the process of negotiations with the EU on the conditions for the UK started on November 10, 2015 when the British Prime Minister Cameron sent a letter of proposal to the EU President (Chart 1). When we focused on the result only, it seems that the four reforms that the UK had proposed were agreed almost as much as in the original shape of the proposals. But the UK was somewhat forced to compromise in two of the most important policies.

One is on the restrictions on the welfare to the immigrants, which faced a fierce opposition from Poland. The second one is on the protection of the rights of the non-euro member countries, to which France vehemently opposed. The UK wanted to maintain the welfare restrictions for about 13 years at the longest, but it is reported that by the strong opposition of the Eastern European countries the term was compromised to about 7 years. As for the protection of rights of non-euro countries, strengthening of some of their powers were agreed but the agreement fell short of giving veto powers for them.

To the market participants, the protection of rights of non-euro members or their use of veto rights to the financial regulations in the EU is a very important theme. It is because the problem boils down in essence to the quite difficult proposition of whether the British government should continue to be the governing body of the London international financial market or it should be transferred to the EU authorities. This is an absolutely important issue that decides the future of London as an international financial center. In that respect, it would have been a great shock to the Prime Minister that Mr. Boris Johnson, the popular Mayer of London and a close colleague of Mr. Cameron whom the Prime Minister himself once counted to be one of his successors announced his backing of Brexit. On his announcement, Mr. Johnson commented that it was a heart-wrenching decision, but it was a decision necessary to reduce the resources to be spent in the EU and to bring back the sovereignty to the UK.”

Because of a rebellion from inside his government, the Prime Minister had been faced with an unexpected bad situation right after he started a campaign for remaining in the EU, but it is partly because of his own bluff. In January this year, the Prime Minister made a decision that declares the cabinet members can be free to take their own positions at the coming referendum, virtually acknowledging that there have been “disagreements within the cabinet”. At least three Tory members of the cabinet are anticipated to express their support for the “Leave” group, which, together with the rebellion of Mr. Boris Johnson, has put the prime minister further in a difficult situation. In the meantime, the government is taking an adamant “all or nothing” stance, which means if the support votes for “Leave” resulted in a majority in the referendum, the UK would immediately exit from the EU without trying any renegotiations.

As there have been a heap of important issues for the financial market to digest in January and February this year, the development in the UK has attracted less attention of the market so far, but in the coming months, “Possibility of Brexit” will amplify the high volatility of the market as a fat tail.The EU system has maintained a status quo with its so-called “constructive ambiguity” working as its own characteristic for a long time. The UK referendum, however, is pressing the EU to cut off this ambiguity, but for the time being, market turmoil caused by a rise of uncertainty may become the toll for it.