European integration and Brexit

In these days the possibility of a Brexit has become very concrete. Discuss how the reintroduction of a tariff between the UK and EU would impact the UK’s external trade on the basis of IMF figures on trade reported below (Figure 1). In a second step, discuss whether any theory of EU integration discussed in class could explain the ‘exit’ outcome.

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Author: Raphaël CARON
CPR number: xxxxx-xxxx
Study programme: BSc in International Business and Politics, 2nd semester
Copenhagen Business School
Examiner: Manuele Citi
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On 23rd June, the British people will vote to decide whether they want to leave the European Union or not. Although the possibility of the UK leaving the European Union (a scenario called “Brexit”) seemed rather improbable a few months ago, it appears that it could be the result of the referendum. If Brexit happens, it will have major consequences for both the United Kingdom and the European Union. On the one hand, the United Kingdom trades a lot with its partners in the European Union, especially thanks to the development of the European integration since 1973 (when the UK became a member of the Union). That trade, which is very important for the British economy, will certainly be affected in the case of a Brexit. But will it be detrimental to the UK? On the other hand, with regards to theory, Brexit would be a yet unseen event, which the European integration theorists haven’t even imagined before. Still, can we understand Brexit through the description of the European Union provided by these theories? To answer these questions, I will first present the nature of the United Kingdom’s trade before showing the main issues that Brexit would bring up, both for trade between the UK and the EU and between the UK and third-party countries. Afterwards, I will discuss whether any integration theory can explain Brexit, even partly, since no theory can explain the phenomenon completely.

1. The United Kingdom’s external trade

The UK has been experiencing an important trade deficit in the recent years. In April 2016, the total trade deficit was at a level of 3.3 billion £. Total exports represented 44.9 billion £, whereas total imports accounted for 48.2 billion £ (Office for National Statistics, 2016, 3). Having a trade deficit reflects a decrease in domestic currency demand, which also pushes down its exchange rate and thereby increases the cost of imports (Grahame Bamford & Grant, 2000, 77). That precarious situation of the British trade balance puts the country in a difficult posture, as the Brexit scenario looms. If the UK leaves the European Union, its trade balance and its economy could be highly affected, since the UK is part of the European Customs Union (EUCU). A customs union is a more integrated form of free trade area (FTA). A FTA is an agreement where the members of the union accept that no tariffs should be levied on goods and services which are sold abroad. In addition to that, a customs union requires a common external tariff to be set for the imports of goods and services coming from outside the union. I will start discussing the potential effects of a Brexit on the UK’s trade balance by pointing out the advantages that the EU provides to British trade within the EU. These advantages would, in the case of a Brexit, be lost. I will then look at the potential benefits triggered by a Brexit for the UK’s external trade with the rest of the world, showing eventually that these are quite illusory.
The UK’s external trade and the European Union Customs Union

Without any doubt, the member states (MS) of the EUCU are essential trading partners of the United Kingdom. Indeed, among the 20 countries to which the UK exported the most goods in 2014, 9 were part of the EUCU. In the same way, among the 20 countries from which the UK imported the most goods, 10 were member states of the EUCU (International Monetary Fund, 2016). That pre-eminence of trade between the United Kingdom and the EUCU is boosted by the customs union. In fact, since the customs union tears down monetary or non-monetary tariffs within the union (European Commission), the price of imported goods from another country of the union is pushed down. That has two consequences: an increase in the exports in the foreign country, and a decrease in the domestic price of the good, as a result of increased competition. This happens in every country: consequently, all the countries of the union trade more. That effect is called trade creation and needs free trade to be observed.

Furthermore, the European Union’s Single European Market (SEM) integration process launched in 1985 has clearly made the specialisation process of the European countries easier through the “four freedoms” (of movement for goods and services, capital, labour and information). That is, the united countries can start producing only the good or the service that they produce in the most efficient way. That shift increases the overall productivity of the specialising countries, allowing them to produce more and trade even more (Springford & Tilford, 2014, 3). For example, it is a remarkable fact that the UK exports mainly financial and business services, a sector in which the British economy has a comparative advantage. As a matter of fact, in April 2016, the exports surplus in financial services in the first quarter of 2016 had a value of 10.5 billion £, which represents around 50% of all British services exports surplus during the same period (Office for National Statistics, 2016, 23). The EUCU, which originated the SEM, should therefore definitely be considered as the main power behind the intensified trade connections between the UK and its European partners. Leaving the union would halt that trend.

Nevertheless, although trade is enhanced by a customs union and further integration processes, it does not need them. One question arises: to what extent has the European Union promoted trade between the United Kingdom and the other MS? In fact, countries naturally trade with their neighbours. As the MS of the European Union are the closest neighbours of the United Kingdom, one could argue that they would trade with each other even without the European Union. Three of the UK’s five most important commercial partners are Germany, France and the Netherlands, which are all countries very close to the UK (IMF, 2016). If the trade creation effect of the EU is low, then the loss of leaving the EU would also be rather limited. Also, the potential benefits of a Brexit related to British trade with the rest of the world seem attractive at first sight.
The UK’s external trade and the rest of the world

The main drawback of a customs union is the Common External Tariff (CET). In fact, members of a customs union have to apply the same tariffs on imports from countries which are not part of the union. If the tariffs are high, then the price of imports from the rest of the world might be excessive compared to the price of imports from another MS of the customs union, even though the latter isn’t the most competitive in that productive field. In other words, the CET could in that case prevent the UK from importing at the lowest price, which in a trade deficit perspective isn’t optimal. Paying a higher price to import goods and services because of the CET is called trade diversion. If it offsets trade creation, then the customs union is not attractive for the country (Springford & Tilford, 2014, 3). In fact, this is what the UK could also be suffering from. The trade potential of the flourishing economies of developing countries could be hindered by trade diversion from the rest of the world to within the EU, even though developing economies often produce at a lower price. Leaving the EU would in that sense be beneficial because it would reduce the price of imports. Moreover, the customs union sets some technical standards for the production and sale of goods and services within the EU. These technical standards can be very precise and demanding, to such an extent that it makes the British production less competitive. Therefore, they could become too expensive with regard to the rest of the world. Consequently, according to that point of view, the exports of the UK are limited because they are part of the European Union Customs Union.

However, considering that an important part of the British trade is diverted from the rest of the world to within the European Union because of the customs union is ignoring the nature of productions in the rest of the world and within the EU. Actually, what is produced in the EU cannot be substituted by the goods and services produced in the rest of the world, because their development states are not the same: high value-added products are produced in the EU while the rest of the world produce low (or at least lower) value-added products. In other words, the German cars that the United Kingdom imports can’t be replaced by Chinese ones. Whether the UK is part of the European Union or not doesn’t change a lot to the picture. The reintroduction of tariffs between the UK and the European Union would only increase the price of European imports for the UK and put the country’s trade balance in an even more complicated situation (Springford & Tilford, 2014, 3). In fact, the difference in European and extra-European productions is big enough to greatly reduce the trade diversion effect of the customs union.

Also, apart from being a customs union and even a single market (to a certain degree), the European Union has signed trade agreements with many countries of the world which enhance trade in a similar though less effective way than the EUCU. As a member state of the European Union, the United Kingdom can take advantage from the different agreements such as the European Economic Area (EEA, including Norway,
Iceland and Liechtenstein), various free trade areas with Mediterranean countries, Switzerland or Latin-American countries (European-American Chamber of Commerce, 2016). The goal is to allow the British production to specialise, thereby increasing output and trade, as discussed previously in this paper. Some more free trade agreements are even being negotiated in different parts of the world, including the Transatlantic Trade and Investment Partnership (TTIP) with the United States of America, which is one of the main British commercial partners (IMF, 2016). All these free trade areas appear to be clearly beneficial for the UK, as they are zones with limited tariffs but with no common external tariff, thereby enhancing trade. Yet, the UK is part of all these agreements as a part of the European Union. If the UK decides to leave the EU, it will have to re-establish those agreements, but with a limited bargaining power, as the United Kingdom would be in a much more powerless and isolated situation (Dhingra & Sampson, 2016, 1).

As we see, even though it is very difficult to evaluate the trade creation and trade diversion effects, the UK seems to have a lot to lose by leaving the EU. However, that scenario is now more than plausible before the vote on Brexit on 23rd June. It is the first time that such a vote takes place and that a country is that close to leaving the Union. Yet, had any theory on European integration foreseen that?

II. Explanations of Brexit through European integration theories

The scenario of Brexit has become increasingly probable in the last months. However, not a single theory on European integration had foreseen that. In fact, Brexit would actually be the start of a disintegration of the EU. Still, we can link the possibility of Brexit with the different theoretical conceptions of the European Union, since the functioning of the European Union is one of the main reasons why the British people could vote to leave the EU. Therefore, I will try to explain the plausible ‘exit’ vote through liberal intergovernmentalism, supranationalism and constructivism. Each time, we’ll see that Brexit is actually never fully explained using a single theory.

Brexit and liberal intergovernmentalism

Liberal intergovernmentalism is a European integration theory developed by Andrew Moravcsik in the 1990s. Derived from classical intergovernmentalism, this theory considers the member states of the European Union as the only self-interested actors in international negotiations, thereby dismissing all other actors such as business lobbies or non-governmental organisations from any sort of influential role. As a result, the development of the European Union is the product of intergovernmental bargaining, where the most powerful states shape the Union in the way they want it to be (University of Portsmouth, 2013). In fact, liberal
Intergovernmentalism is very close to realist theories in international relations. Albeit that theory doesn’t include any possibility of disintegration, we can assume from its conception of the development of the European Union that Brexit could be illustrating the fact that the UK is considering leaving the EU because it suits best its own economic interests. In that configuration, the EU’s functioning is assumed to prevent the UK to exploit the full potential of its economy, because it doesn’t have enough power to defend its interests against its major partners in the Union, such as Germany or France.

However, the conditions under which Brexit has become plausible contradict the explanation of Brexit through liberal intergovernmentalism. In fact, as we have seen before in that paper, leaving the EU would not be beneficial to the country’s economy, as it is very uncertain that trade diversion to the European Union Customs Union is more harmful to the country than trade creation within it. Also, liberal intergovernmentalism assumes that the European Union creates interconnections between the European economies. Reducing them by leaving the EU would be damaging. And in fact, that is why the actors of the financial services sector in the City of London are so hostile to Brexit: in April 2015, 73% of the “City folk” wanted to vote against leaving the EU while only 12% wanted to vote in favour of Brexit (Centre for the Study of Financial Innovation, 2015, 3). Besides, the UK is definitely not one of the weakest links of the European Union, and its bargaining power in the intergovernmental negotiations is important. Actually, in February 2016, David Cameron succeeded in bargaining some specific conditions for his country to stay in the European Union (Guardian, 2016). Although it might not be enough for the British people to change their mind, the fact that the EU sacrificed some equality among the member states to try keeping the UK within the European Union is not negligible.

Liberal intergovernmentalism does not explain well why Brexit is so close from happening, as the UK plays a big part in the European Union and because the economic benefits of leaving the Union don’t seem sufficient for the UK to take such a big decision. Perhaps leaving the European Union is not economically beneficial to the UK, but have the European institutions still taken too much of political power from the British Parliament?

**Brexit and supranationalism**

Derived from neofunctionalism, supranationalism appeared in the 1990s as another European integration theory. It states that when the European member states find an agreement at European intergovernmental negotiations, they create new institutions and delegate them decisional power in specific policy areas (Stone Sweet & Sandholtz, 1997, 303). The delegation of decisional power to supranational institutions will tend to create pressure from the productive sectors of the different MS of the EU for which the transfer of power has helped cross-border business. In fact, the European institutions help productive sectors to trade and thereby to produce more by integrating the different European markets into a single one. However, as the
power of the European institutions is limited in the beginning, the integration becomes also somewhat insufficient. Therefore, European MS will tend to delegate more power to the supranational institutions in order for them to further a European integration which is beneficial to the countries' trade and output (Stone Sweet & Sandholtz, 1997, 306). From that theory's perspective, it means that all power tends to get delegated to the supranational institutions as transnational trade increases. That means that national sovereignty is reduced, as more and more policy areas competences are given away by national governments. One could argue that that loss of sovereignty is the reason why Brexit could today happen, as the British people want their national parliament to keep control over the laws that are enacted and applied in their country (Gifford, 2009).

However, a loss of sovereignty can’t fully explain Brexit. In fact, the UK is one of the countries which has the most opt-outs and therefore conceded the least parts of its sovereign power to supranational institutions. The UK is neither part of the Eurozone and its regulations on budget deficit and debt, corresponding to the third part of Economic and Monetary Union (EMU) development process (European Union Law, 2006), nor of the Schengen area (Schengen Visa Info, 2016). That makes the UK one of the least integrated states in the European Union. The UK is not at all in the same situation as for example Greece, on which the EU imposed many important mandatory structural economic reforms in exchange of a credit bailout in August 2015 (BBC, 2015). Yet, although Greece lost a lot of sovereign power in that agreement, a majority of Greeks want to stay in the European Union and even in the Eurozone (Greek Reporter, 2015). That makes the explanation of Brexit through a loss of sovereignty contradicting.

Assuming that Brexit is mainly caused by an excessive transfer of sovereignty to the EU seems like a fallacy, since more integrated countries are not considering leaving the Union. Explaining Brexit through supranationalist theories therefore doesn’t fit well. We need to look at what the European Union represents for the UK to try to understand the reasons of a potential Brexit.

**Brexit and constructivism**

In international relations, constructivism is a meta-theory developed in the 1990s which assumes that all the interests of states are socially constructed. That means that many non-material factors such as history, behaviour or culture play a very important role in shaping the interests of and the relations between states (Hurd, 2008, 300-301). In the case of the UK, it means that even though the material benefits of being a member of the European Union seem consequent, some other non-material factors interfere and make membership less valuable for the UK. These factors can for example be historical. Many people in the UK have always felt their country as being a distinct part of Europe, different from Continental Europe in many ways (History Today, 2015). Although it is very uncertain that this feeling is justified, it does have a negative
influence on the conception of what the European Union is in itself and in relation to the UK. Furthermore, cultural factors also come into play. The cultural and linguistic affinity between the UK and the United States are also tempting the Brits to cooperate with the Americans, even though it is not necessarily the most materially beneficial. That refers to the nature of what Winston Churchill called “The Special Relationship” in 1946 (Freedman, 2006).

The constructivist conception of the UK’s role in European integration seems to be the most accurate of all the different theoretical conceptions. In fact, Brexit is difficult to explain in terms of interests or sovereignty, as liberal intergovernmentalists or supranationalists would do. Some other socially constructed factors have to come into consideration, and these are quite well accounted for by constructivists. When we look at the recent events in the European Union, some of them may have altered the social representation of what the EU is for the British people and thereby their attitude towards it. The refugee crisis which started in 2015 and the many incidents linked with them may have distorted the views of the UK’s citizens on the EU. In fact, the European Union has been denounced for not addressing efficiently enough the refugee crisis by giving access to too many migrants in many countries, including the United Kingdom (Grant, 2016, 2). Whether this feeling relies on any evidence is not important: it is the feeling that shapes the representation of the EU, not its veracity. On top of that, the recent terrorist attacks in Paris and Brussels in 2015 and 2016 have intensified the debate about whether open borders within the EU are helping terrorists in their attacks (Huffington Post, 2016). This definitely doesn’t promote the European integration, which tends to erase all kinds of borders between nations.

Conclusion

All in all, even though it is difficult to evaluate how much trade the European Union has created and diverted, it seems like the United Kingdom’s trade with its European partners will drop if Brexit. Meanwhile, it’s very doubtful that Brexit will boost commercial relations with countries outside of the European Union Customs Union. Therefore, the UK has a lot to lose, but not necessarily something to win from an economic perspective. That means that it is difficult to assume that Brexit suits the economic interests of the United Kingdom. That makes the liberal intergovernmentalist explanation of Brexit quite irrelevant. In the same way, while supranationalists could state that Brexit is linked to an excessive transfer of British sovereignty to the European institutions, that explanation ignores the fact that the UK is not one of the most integrated countries in the European Union. Constructivism seems to be the theory which explains Brexit most accurately, as the socially constructed representations of the European Union play a big role in promoting
Brexit, especially during the refugee crisis and the gloomy economic climate that we are experiencing right now.

Nevertheless, using European integration theories seems insufficient to explain Brexit, because the reasons of Brexit are not so much linked with European integration. In fact, the functioning of the European Union might be the most important motive behind Brexit being so close from happening, since the way the European Union is shaped doesn’t benefit all social classes within a country in the same way. One could argue that the European Union is specifically beneficial to a certain elite in the UK, because the single market allows for instance immigration from other EU countries, which makes employment more insecure for UK citizens from lower classes. Therefore, the European Union might be the new arena of a British class fight because it exacerbates socio-economic inequalities. Brexit might thereby be the symbol of a popular dissatisfaction against the establishment. In that case, the analysis of Brexit becomes much more complex and has to rely on the analysis of both the political as well as the socio-economic configuration of the United Kingdom in itself and not only with regard to the European Union.
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