

The Political Economy of Brexit

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Abstract

Brexit is already a fact – the UK shall notify to the withdrawal of their country from all the structures of the EU. The decision of the British voters has a major impact both on the UK, so the development in Europe. However, not only impact decisions, but also the causes of Brexit are many and on both sides of the English Channel. Demarcation of political economy isn't clear-cut – there is a dividing line between politics and economics concept. In the decision of the British played their role to many factors, which can be classified into motto – let's take back control. The analysis of the costs and benefits of Brexit should serve to facilitate the understanding of the further development of the two actors - the UK and the EU. Here I will focus mainly on the economic aspects.

Keywords: *Brexit; causes of Brexit; effects for the UK and EU economic, institutional, political*

JEL Classification: *E6; F4; F5; P0*

1. Introduction

The announcement of the referendum by David Cameron turned out to be the opening of Pandora's Box. I do not know whether it was just a surprise or a shock from the result of voting, though so tight. The decision of British voters has far-reaching consequences for more than half a billion EU citizens. What were the reasons for the voters' decision and the consequences of their choice? Is the British voter postmodern? It wants its own identity, defining itself against continental Europe against the EU and its bureaucratic apparatus, but wants its, which other than anywhere else. Britain is something else...

The following article tries to analyse Brexit's input-output using political economy.

2. Political Economy as a Theoretical Framework for Reflections on the Brexit

The discipline of political economy is nothing new under the sun - for the first time this term was used in 1615 by Antoine de Monchrétien. Political economy nowadays examined the relationship between economic theory and practised policy, or the effects of practical political decision (Strange, 1988, p. 19). For political economy, it is crucial to understand how economic, social and political phenomena affect the decisions of people and institutions (Germain, 2014, p. 6). In general, political economy applies the economic methodology to the human decision-making, explains social conduct through the apparatus of the economic instruments. But not only – is the political economy tracking the impact of political decisions on the breadth of the social and economic spectrum, including psychological responses.

Brexit is connected very closely with the European Union's development, with the future of both the EU and UK. European political economy spread broad framework ranging from European integration theory, public choice, comparative politics and policy-making approaches (Talani, 2014, p. 7). The political economy of Brexit is generated by Britain's traditional isolationism, by Britain's non-euro membership while possessing the offshore financial centre (Thompson, 2017, p. 434). The critical political economy on UK side is growing out of fear of a divergent development of views on integration between the mainstream in the UK and the EU. The deepening of the integration steps, the building of a strong institutional apparatus, taking over many powers of national governments, is becoming the new constitutionality of Europe (Gifford, 2016, pp. 780-781) against which the British are opposed and that leads to creation strong Euroscepticism as a base of distinctive British critical political economy.

These definitions of political economy are important for understanding the results of the referendum in the UK in June 2016 about their staying/leaving the European Union.

3. Causes of Brexit

The reasons for the UK voters' decision to leave the EU may vary. I will try to outline the most prominent for the British, although for other Europeans it may not be an adequate decision so important. But they should not ignore the specifics of every nation in the individual EU countries. It is not the goal of examining the differences in elections in the UK, although they have a great deal of value. I'm considering Brexit as a whole.

3.1 The Identity Problem of the British in the Context of European Integration

The British public has always been wary of the European continent. Some vigilance of the English towards Europe can be traced back to the 16th century, when institutional changes such as the previous accumulation of capital (Smith, 1776), the religious reform of Henry VIII take place within the Kingdom of England, and the real colonisation of Ireland 1541. Its resources largely generated Super-power's growth of England, hence the detachment from the European mainland. Especially England people have always felt like reformers in the British community - thanks to Protestantism as a state religion since the first half of the 16th century, thanks to the industrial revolution and the maritime success of the Francis Drake of the Elizabethan times, so no one else needed their development. It seems that in Britain this feeling is inherited from generation to generation up to now.

At first, the British did not want to participate in the European integration process at all, only after finding the economic disadvantage of being out in the 1960s, they rethought their attitude. After two unsuccessful attempts to join the EC, they eventually joined in 1973, but two years later the first referendum on British participation in the European integration community took place. The results of this referendum confirmed the original decision and the British decided to stay in the European Community. But "UK never fully embraced the European project" (Geoghegan, 2016, p. 3).

Britain has always been a little bit aside because fears of national identity disruption in the melting pot of European integration have been felt very strongly. After all, the splendid isolation as a concept of the foreign policy of Prime Minister Benjamin Disraeli has been in place since the middle of the 19th century. The accent on strict sovereignty in many aspects of economic, not only security, development has led to the negotiation of many exceptions within European integration. In a nutshell, I will only highlight the most opting regimes - the exception from the Schengen system, initially the exception from the Charter of Social Rights of Workers and, above all, the opting clause on EMU membership. The last was the

objection to the possible extensive interpretation of the Charter of Fundamental Rights when the Lisbon Treaty was approved. Of course, the most visible is the so-called British rebate, which was agreed by Margaret Thatcher in Fontainebleau in 1984, and which would be used by other net payers in the budget, but has always been used only by Britain. And even under the rule of the most pro-European British Prime Minister Tony Blair. For his first government, Gordon Brown, as Treasury Minister, set five conditions, the criteria for the potential accession of the UK to the EMU, all formulated to benefit the UK economy. This was an example of a rational approach to European integration, not just its principle - solidarity. But it is purely an economic approach, not a political one. And it resonates with British interests. "The UK has never been at ease with either its membership of the European Union or the broader idea of European Integration" (Phinnemore, 2016).

3. 2 Impacts of the Global Financial Crisis on the British Economy

The global financial crisis of 2008-2010 has hit hard the British financial sector, and the whole economy and the Bank of England's responded to the crisis by expansionist politics – compared to the ECB in these days. London City, as one of the world's financial centres connected with others, has seen a significant fall. However, the London financial sector represents euro's off-shore centre in Europe, maybe the most important European financial trade. Although the UK is not a member of the EMU, the Euro-zone crisis has undoubtedly impacted on domestic politics and has seen its rise in Euroscepticism (Gifford, 2016, p. 779).

When the financial crisis grew in the Euro-zone crisis, and the economic practices of the southern EU countries were revealed, the British understood this development as the crisis of the whole integration project. The main reason was the non-systemic steps taken by Germany and France, including ECB to save the southern banking sector at the expense of their taxpayers, which is unimaginable for the British. Therefore "the 2008 financial crash and the euro-zone crises put a time-bomb under sustainability of Britain's membership of the EU" (Thompson, 2017, p. 446). The British obviously did not want to pay the bills for the other, because after all David Cameron refused to sign a Fiscal pact commitment fiscal responsibility within the whole EU, not just the EMU at the beginning of the year 2012. Overall, the pressure on narrower monetary and fiscal integration, which has emerged as a result of the crisis, is unacceptable for the British. The development of monetary and, in fact, fiscal consolidation of national policies leading to economic harmonisation and, consequently, to the gradual federalisation of Europe is utterly unimaginable for the British.

The problem has also been the inability to mobilise other non-euro states into the alliance against the German-French tandem towards European integration towards a fiscal union. Of the non-member countries of the EMU, only two countries were the strong negotiating partners within the EU, namely Denmark with the same opting regime as UK, and Sweden. Other EU Member States outside the EMU come from the new member states and are thus significantly weaker negotiating partners. If more than four countries joined the EMU by the start of the crisis, the euro area now includes 19 EU countries out of a total of 28. This has reduced the bargaining position of Britain. After all, another issue between the EU and the UK was a proposal to introduce a financial transaction tax that would hurt the City of London, which Cameron averted but weakened the UK's position within the EU as opposed to Germany, France. The logical response could be to return the check to Britain.

3. 3 Growing Immigration to the UK, whether Work or Social

Immigration to the UK area from other EU's countries, initially mainly from new member states, or later from South Europe, i. e. from economies affected by financial crises – it is the

next logical cause of the decision to leave the EU. These are other very important factors deciding the British people about their future in the EU - a feeling of nonconformity, social tension, and the arguments of the nationalists that the foreigners are taking their jobs. The paradox is that in this period the British economy, in any case, not worried about unemployment, on the contrary, the lack of certain professions.

It is true that Britain under the leadership of Tony Blair opened its labour market immediately to the new member countries of the EU in 2004 with the connection of so-called Big-Bang Enlargement of the EU - as one of the three states of the EU. Within the "Blair's" Labour party began to deepen the trench misunderstanding, since the traditional members were expecting more protection of their interests (the government's first priority should be its citizens) contrary to the modernist most of the party professing cosmopolitanism, and the benefits of globalization (Parker, 2017, pp. 479-480). As regards migrants from the southern EU countries, this was mainly due to the collapse of their economies as a result of the global financial crisis of 2008-2010, which has grown in the southern EU countries in the Euro-zone crisis. This, of course, has reinforced the belief of the vast majority of the British that a single currency and a common monetary policy are pointless and harmful. The so-called the European migration crisis, culminating in 2015-2016, only raised the problems. Almost all migrants at that time dreamed of the two final destinations of their emigration - Germany and Britain. The UK has a relatively accommodating migration system from Commonwealth countries, leading to a steady stream of migration from this part of the world. Mass immigration from other countries has led to the doubts of the British about whether greater regulation or liberalism is so typical of the New Labour Party governments.

3. 4 EU Budget and British Contributions

The main motto for opponents of European integration was how much the UK contributes to the EU's common budget. Simply put - many. Britain is the second most powerful EU economy, so its contributions to the common budget are very high. Not only did Boris Johnson or Nigel Farage use the numbers in the pre-referendum campaign to prove how "Brussels" slashes Britain and how much money the UK must send to the common budget. Those numbers were not deliberately true but exaggerated. In spite of many warnings by other members of the government or parliament that this was manipulation, Boris Johnson insisted on it and paid off, for the British obviously believed it. Real numbers are as follows (European Union [online], 2018): British contribution to the EU budget total in 2016: 12.760 billion Euros, or 0.55% of UK GNP; EU spending in the UK total: EUR 7,052 billion, i. e. 0.3% UK GNP, the net costs of membership for the UK amounted to 5,708 billion Euros, it means 0.246% of UK GNP. In contrast, UK public expenditure is more than five times bigger than the EU budget, more precisely 42% of GNP (European Commission [online], 2014). A lot of commotion for nothing? Not quite - if you exaggerate false figures in your favour, and if you claim that this money could be used immediately in problem areas such as health care, then you are guaranteed success. Voters are looking for easy solutions.

Setting the budget for the next period after 2020 is a challenge. How many members of the EU? What about the UK as the second largest contributor? The EU asks for higher payments to the budget due to Brexit, as the failure of the UK contribution could jeopardise the funding of many integration projects. Member States' responses are diverse - ranging from refusing to increase compulsory levies for approval by poorer countries. Eight of the new Member States (excluding the Baltic States and the Mediterranean island countries) are more likely to increase their contributions. However, there is still a variant that, after Britain's departure from the EU, the UK government will continue to contribute to the EU budget if it wants to keep its firms on the EU's internal market.

4. Effects of Brexit

The impacts of the British decision to leave are hardly quantifiable, as the UK exit scenario is not known. I'm afraid that even Theresa May does not know exactly what to do with the EU because the mood in the UK is changing. And also, estimates of Brexit's impact on the British economy are being developed, and the cost numbers are very unfavourable, which neither voters, nor the government, nor a general idea.

It is necessary to consider the effects both towards the UK and the EU. I will only focus on the economic impacts.

4. 1. *Input-Output Analysis of Brexit for the UK*

The decision of the British voters to leave the EU at a close ratio of 51.9% against 48.1% for their continued existence has far-reaching consequences not only for the whole of Britain and its individual historical countries but of course also for the EU. Statistics are a treacherous methodology - out of five British territories voted for leave two, while Scotland 62 %, Northern Ireland 55.8 %, and Gibraltar 95.9 % of the votes to remain (Phinnemore, 2016; Geoghegan, 2017). The consequences are and will be far-reaching and yet not fully predictable.

4.1.1 *Access to the Internal Market*

Britain only represents partial changes in its participation in the EU internal market, in the sense of excluding those lucrative as financial and legal services, else automotive industry that the UK would manage itself. But the current regime of trade in industrial production would like to leave it in the internal market regime. The European Commission has a different opinion, supported by the supreme representatives of the EU Member States – it couldn't be just about picking cherries from the cake, new relations must be set fairly for both sides - the EU and the UK. The EU has taken a position „no negotiation without notification“, and intends to act on the internal market as a whole. If Theresa May will insist on her, there is a risk of Britain losing all four freedoms of the internal market, which could be a considerable loss for the British economy. While it is true that British exports to the EU have declined, they are still around 45%. For objectivity, it has to be acknowledged that Britain has diversified its exports outside the EU since 2000, not just a referendum. But so are the EU markets vital for Britain. Conversely, the EU needs an extensive and advanced UK market. This is an additive relationship that is beneficial to both parties and serves as an incentive for further development.

4. 1. 2 *Labour Markets*

Britain has opened up its labour market to new countries in 2004 not because it feels solidarity but because it had - and still has a great structural disproportion in the labour market. British economies have been sharply developing since Margaret Thatcher, involved in globalisation, lacking many professions, including those highly qualified, such as physicians, nurses, or perhaps their expansion in the financial sector or new technologies.

In addition to the specific professions of a country with a high standard of living and low unemployment, Britain has a shortage of unskilled labour willing to do subordinate, inferior work. Over the past twenty years, the British economy has been able to absorb an incredible amount of foreign workers who have contributed not only to their own development but also to the growth and stability of the British economy, and have often filled places that have not been among the British. It is, therefore, interesting and even less understandable why the in-

work workers have played such an important role in the left campaign, although immigration and labour migration are likely to emerge. The agricultural sector has a special position in labour migration, since it only employs a small percentage of the British population, while the largest share belongs to workers from other EU countries. It is very little paid work that the British do not want to receive. This work is often carried out by students or residents of the eastern EU countries who are willing to go for significantly lower wages. Interestingly, the anti-European campaign objected that migrants take the British job, but not that they are pushing wages down, below the minimum wage...

Employers have warned before the referendum that shrinking from the free movement of people in the internal market will mean a substantial labour shortage for the British economy. These were Brexit's negatives for the British economy; it is upright to mention the pros.

4. 1. 3 Payments to the Common Budget

The most strikingly perceived effect of the Brexit will be the absence of contributory obligations in the common EU budget. Given the position of Britain as a clean contributor, it will certainly be very pleasant. Certainly, even in Britain, you can find signboards with the announcement that this project has been co-financed by the EU, but they are far less than in other countries. As has been mentioned above, Britain is more contributing to a common bill than it can draw from it. Therefore, the abolition of this duty is certainly the supposed goal of Brexit.

4. 1. 4 Less Bureaucracy

An absolutely indisputable benefit, even for the EU's supporters, must be the abolition of the "Brussels bureaucracy" dictate. And with that, Britain has always had great problems, especially as a country without a written constitution. Although I do not want to question this position, only two things are on the brink: this bureaucracy also helped to create greater transparency for the British, because that "Brussels" is made up of representatives of the member countries; growing institutionalization is also evident to international organizations outside the EU, so the UK will not be able to do it anyway.

4.2. Input-Output Analysis of Brexit for the EU

There is no doubt that the exit of such a strong economy from the Community will damage the whole of the Union's economy. I am afraid that the negative side of the EU outweighs both economic performance and policy-making.

4. 2. 1 Internal Market

The left of the British economy and its firms will weaken the performance of the EU's internal market, as London as a financial centre is likely to become the external financial market. This, of course, will increase the cost of trading on the financial markets. Yes, there are certain hopes for a hard Brexit that some of the corporate firms move at least partially to Frankfurt but cannot rely on it. The liberalisation of financial services is closely linked to the movement of capital - it cannot be assumed that there would be any restriction on the part of the EU at a time of virtually free capital flows in a global dimension.

Absolutely limiting the movement of people, as this was one of the demands of Brexit supporters. In this case, the cards are in the hands of the British - they are afraid of their citizens of continental Europe, the British somehow assume that nothing will change for their citizens in the EU.

The issue of the freedom of movement of goods is probably the least problematic since trade liberalisation has been an international trend since 1947. Despite the British thought, whether they want EU customs union or rather trade under WTO rules. However, the loss of the 64 million potential consumer markets is a big and unpleasant change.

4. 2. 2. Labour Market

The European Union does not even focus on the labour migration agreement as a guarantee of the rights of workers already living and working in Britain. Theresa May promises to protect those who are already working in the UK but reserves the right to control newcomers. Negotiations on both sides are processing.

4. 2. 3 Budget Contributions

It is inconceivable that the departure of Britain will come to the EU as its second largest donor. It is already under discussion how to replace the UK postponement or how it will be addressed. The European Commission is pushing for the UK to contribute to the EU budget even after its eventual departure, at least within the agreed financial perspective in force in 2020. The British side seems to agree. The question, therefore, relates to the post-2020 period - reflections on another form of the budget are already under discussion.

4. 2. 4 Policy-Making Processes

Despite many British obstructions and bargaining for their exceptions, in the case of Britain leaving the EU, the European Union will lose a rational member who defends at least partially the full institutionalisation of European integration. It is true that when the British understood that they would not stop further institutionalisation, they focused on negotiating their demands, but in any case, they were an example for other potential opponents of closer integration.

In addition, the British are afraid of too strong a "Europe", meaning Continental Europe and particularly too strong Germany (Kučerová, 2015, p. 147), whose roles are rising alongside the growing problems of the European Union, especially the Euro-zone. The economic and political power of Germany has turned out for most of Britain in the face of both the Euro-zone crisis and the European migration crisis.

5. Conclusion

Brexit means a breakthrough in the development of European integration, is clearly a proof of a spill-back effect, the fatigue of integration. The asymmetry of information has proven to be significant for British voters - many for the UK leaving the EU admit that they did not have enough information and that they chose emotionally rather than pragmatically. The outcome of the referendum itself, the discussion of the new situation and the reflections on the future has serious implications for the development of the participating partners.

Economics policies always measure the costs and benefits of any decision. The political economy of European integration and critical political economy are trying to specify the input-output analysis.

In the discussions and reflections of both parties, possible scenarios for the further setting of mutual relations are discussed. But future models of Britain and the EU will be the subject of further research. One thing is clear - the withdrawal of Britain from the EU will lose both sides. The very close ratio of voting results is reflected in the sharp controversy of the British themselves - "UK cannot expect to abandon membership and simply walk straight into whatever new relationship it wishes to have the EU" (Phinnemore, 2016).

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