

POST-BREXIT BRITAIN: ITS RELATIONS WITH THE EU AND ITS FUTURE IN THE FRAMEWORK OF MULTILATERAL INSTITUTIONS¹

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In the next two years, the UK will be faced with a complicated geopolitical situation. The relations with its two key partners – the EU and the USA – will be changed. The USA, when dealing with European issues, will begin to rely on Germany rather than on the UK. It will be necessary to negotiate with the EU a new relationship model that will envisage that the UK should not participate in the decision-making process inside the European Union, and should have no internal influence there. Simultaneously, there will be a need for negotiations on new trade agreements with a number of countries that are not EU member states, because the UK, once it has withdrawn from the US, will automatically find itself outside of the international trade agreements concluded on behalf of the EU, including those in the framework of the WTO.

The uncertainty factors

The first uncertainty factor is the **future candidate for Prime Minister**: Boris Johnson, former Mayor of London, or Michael Gove, Secretary of State for Justice. Anyway, none of them possesses sufficient experience of working at multilateral international institutions, and both have only limited experience of dealing with the EU. The second uncertainty factor is **the timing of the negotiations on the withdrawal agreement** setting out the arrangements for the UK's withdrawal from the EU and the framework for its future relationship with the Union. These can be expected to take place no earlier than October 2016, or perhaps even later, if the new Prime Minister and the Cabinet ministers should need more time for elaborating the starting terms for negotiating their standpoint and thinking over the EU's proposals concerning the provisions of the withdrawal agreement. The third uncertainty factor is the actual **length of the negotiation process**. As stipulated in Article 50 of the Treaty on the European Union, the Treaty should cease to apply to the State that has notified the European Council of its intention to withdraw from the date of entry into force of the withdrawal agreement or, failing that, two years after the said notification. However, the European Council may decide to extend this period. So, the negotiations can be expected to round up by autumn 2018 or later. For 2017, presidential elections are scheduled to occur in Germany and France – two EU member states that used to be part of the EU 'axis', now depleted by the loss of the UK. The **viewpoints on the terms of future cooperation with the UK of the potential presidents-to-be of both Germany and France** represent yet another uncertainty factor.

The choice made by Scotland and Northern Ireland, who both backed staying in the EU (62% and 55.8% respectively), may actually shape the nation's future. This is one more uncertainty factor. If Brexit becomes reality, Scotland and Northern Ireland can then hold their own national referendums concerning their secession from the United Kingdom. The Eurosceptics

¹ This paper was originally published in *Online Monitoring of Russia's Economic Outlook* No.11(29).

will then get one small country (England + Wales), and consequently, a much lower potential for influencing international issues.

And finally, the new framework for the relationship with the Union is yet to be known. However, no matter what the outcome of the negotiations might be, the uncertainty that will be shaping the foreseeable future and the altered relationship with the EU will inevitably have an impact on the UK economy. If the free trade agreements under the Europe 2020 Strategy are actually realized, the country's GDP will plunge by 3%, and if the UK and the EU operate on the basis of WTO rules – by 5.5%. Alongside the GDP plunge, an unemployment surge to 7–8% can also be expected from its current rate of 5%.

The status in multilateral institutions

Group of Seven

The Group of Seven (G7), alongside NATO, will remain a major floor for the UK to shape its common viewpoints and decisions on a broad spectrum of issues, including economics, finance, development, security. When the UK withdraws from the EU, G7 will gain in importance even more, as it will become a bridge to the EU, while at the same time offering possibilities for influencing the world agenda. The their declarations made shortly after the referendum results were published, G7's ministers of finance and heads of central banks emphasized their solidarity with the UK and their preparedness to introduce the necessary measures designed to play down the excessive volatility of world markets.

The UK will stay in G7 even if, say, Scotland should decide to secede.

Group of Twenty

The position of the UK within G20 is not going to change in any significant way. The predicted plunge of its GDP will have no radical effect on the country's status, as it will remain the world's leading economy. The question as to the legitimacy of the UK's membership in G20 may be raised only in the event of the secession of Scotland and Northern Ireland. Nevertheless, tension can be expected between David Cameron, Angela Merkel and François Hollande at the forthcoming Hangzhou Summit. Germany's G20 presidency will not be free of tension, either. It can be assumed that later on, as the new relationship model for the EU and the UK takes shape, a new formal for consultations concerning G20 agenda will also be created during the period of Indonesia's presidency.

WTO

The UK's withdrawal from the European Union will give rise to some serious reshuffling in the sphere of international trade. Among other things, this will affect the multilateral trade system established in the framework of the WTO, where the UK's place used to be defined by its membership in the EU.

According to WTO Director-General Roberto Azevêdo, the UK will enter a lengthy negotiation procedure involving all the 162 WTO member states, where its new status in the WTO will be redefined, and it will also have to revise its preferential trade agreements with other countries. The UK will lose its preferential access to the markets of 58 countries in the framework of 36 trade agreements, it will have to raise its tariffs for imports from those countries, while at the same time being faced with increased tariffs for its own exports¹. In fact, UK foreign trade will be revised in its entirety. One more

1 Brexit: the impact on the UK and the EU. <https://www.global-counsel.co.uk/analysis/special-report/brexit-impact-uk-and-eu>

issue for the United Kingdom will be its lack of a qualified corps of international trade negotiators, as all negotiations in the sphere of trade have been conducted, on behalf of the UK, by EU experts¹.

As far as rethinking of the terms of trade with the European Union is concerned, the UK will not have to negotiate separately with each of its member states. Evidently, a single UK-EU agreement will be signed².

Besides, the UK will experience some difficulties in the course of trade negotiations due to the shrinkage of its aggregate share in global trade, and also because its market will become less attractive for foreign investors and trade partners. The United Kingdom's share in world trade is estimated to be 4.3%, whereas that of the EU amounts to 15.4%³. Under these new conditions, the country will have to ease its approach to negotiations, and probably to make some concessions, including in the context of the forthcoming negotiations with Russia as a member of the WTO.

For Russia, the complex issues that the UK will have to deal with during the negotiations aimed at regulating the terms of trade in the framework of the WTO, are fraught with no significant risks. According to data released by the Russia's Federal Customs Service, the commodity turnover between Russia and the UK in January–March 2016 amounted to \$ 3.17bn, or 2.4% of the total volume of RF foreign trade. This index dropped on the same period of 2015, when the commodity turnover between the two countries was \$ 3.73bn⁴.

Thus, given the fact of the shrinking commodity turnover between Russia and the UK, as well as the existing restrictions on trade and investment, the Russian economy cannot be expected to suffer noticeably from any strong negative effects created by the UK's withdrawal from the EU and the revision of its trade relations with its major partners in trade in the framework of the WTO.

At the same time, as a result of the UK's withdrawal, Russia may hope for a more speedy coordination of its issues with the European union and for a certain easing of the standpoints of its member states concerning the relations between Russia and the EU, including in the sphere of trade policies.

International financial institutions

In the short-term perspective, in spite of its planned withdrawal from the EU, it is highly probable that the UK will retain its key roles in the leading international financial institutions⁵. Its withdrawal from the EU will give

1 WTO warns on tortuous Brexit trade talks. <http://www.ft.com/cms/s/0/745d0ea2-222d-11e6-9d4d-c11776a5124d.html#axzz4ClrMzPQw>

2 How will Brexit affect Britain's trade with Europe? <https://www.theguardian.com/business/2016/jun/26/how-will-brexit-affect-britains-trade-with-europe>

3 Brexit: the impact on the UK and the EU. <https://www.global-counsel.co.uk/analysis/special-report/brexit-impact-uk-and-eu>

4 Foreign trade of the Russian Federation, by main country, for January-April 2016 http://customs.ru/index2.php?option=com_content&view=article&id=23490&Itemid=1976

5 The UK's member quota and voting power in the IMF amount to 4.26% and 4.05% respectively (it holds 5th place among all its member countries) (<http://www.imf.org/external/np/sec/memdir/members.aspx>). The similar indices for the UK in the International Bank for Reconstruction and Development are 4.145 and 3.94% respectively (<http://siteresources.worldbank.org/BODINT/Resources/278027-1215524804501/IBRDCountryVotingTable.pdf>).

The UK also plays major roles in the other organizations of the World Bank Group. The country comes fifth by its voting power in the International Finance Corporation (IFC) (<http://siteresources.worldbank.org/BODINT/Resources/278027-1215524804501/IFCCountryVotingTable.pdf>) and the Multilateral Investment Guarantee Agency (MIGA) (<http://siteresources.worldbank.org/BODINT/Resources/278027-1215524804501/MIGACountryVotingTable.pdf>), and

rise to a short-lived recession produced by the resulting economic shock, as well as an economic growth slowdown in the medium-term perspective. However, although the voting shares and quotas in some international financial institutions depend of the actual economic status of each member state, the parameters of UK participation will, most probably, remain unchanged in the nearest future. This will be possible due to the absence of automatically applied mechanisms for recalculating the quotas and votes, as well as to the strength and sustainability of the highly developed UK economy, which is resilient to negative external shocks, and so makes it possible for the country to fulfill its obligations assumed in the framework of those institutions.

Nevertheless, over the medium- and long-term periods, the UK's status in these institutions may weaken. Firstly, as its share in world GDP shrinks, the pressure from the other members of those institutions will increase (for example, in the framework of the next general redistribution of IMF quotas), as the member countries are striving for a more fair distribution of quotas and voting powers that will reflect the existing economic realities. Secondly, if in the future the UK should be faced with the implementation of an adverse scenario like the withdrawal of Scotland or Northern Ireland, it is very likely that its member's quotas and voting powers will be redistributed in favor of the new sovereign member countries. Thirdly, this course of events will also have an adverse effect on the UK's role in those international financial institutions where the membership is based on the principle of equality, and not on quotas, including the Financial Stability Oversight Council, the Bank for International Settlements and the Basel Committee on Banking Supervision, as the influence of representatives of the Bank of England, HM Treasury and UK financial supervisory bodies there will also weaken.

The less prominent roles of the UK in international financial institutions will have a negative effect not only on the country itself, but also on the stability of these institutions and the sustainability of the international financial system as a whole. The necessity to find a replacement for the resources currently invested by the UK may result in a shrinkage of the volume of operations carried on by these institutions, and trigger a new round in the country's struggle for influence over their activity.

NATO

Although, post-Brexit, it will be difficult for the UK to fulfill its obligation, as a NATO member country, to allocate 2% of its GDP to defense¹, NATO will gain even more in importance (and probably also in strength) in the framework of relations between the UK, the EU and the USA. NATO will remain the only organization uniting almost all the relevant member states of the EU and the USA. The purpose of NATO's Warsaw Summit (to take place 8–9 July 2016) is to demonstrate unity of the Alliance to the entire world, and in particular to Russia. Brexit will not change the UK's choice of NATO as a major multi-

third in the International Development Association (IDAC) (<http://siteresources.worldbank.org/BODINT/Resources/278027-1215524804501/IDACountryVotingTable.pdf>).

Besides, the UK holds big stakes in regional development banks, including the Asian Development Bank (ADB), the African Development Bank (AfDB), the Inter-American Development Bank (IADB), the Asian Infrastructure Development Bank (being among the top twenty shareholders in each of them), as well as in the EBRD (sharing second place with Germany, France, Italy and Japan) (<http://www.ebrd.com/shareholders-and-board-of-governors.html>).

¹ UK Chancellor of the Exchequer George Osborne promised a cut on defense expenditures, given the ministry's calculations demonstrating that two years after the country's withdrawal from the EU its GDP will decline by 3.6%, and the pound sterling will weaken by 12%.

lateral defense institution. Moreover, the UK will make efforts to strengthen the practical aspects of its special relationship with the USA, including in the framework of NATO. As for the USA, it will promote Germany as one of its key partners, because the opportunities for the UK to influence the standpoints of the EU will be significantly reduced, once it finds itself outside of its framework.

United Nations Security Council

The UK will, most probably, retain its place in the Security Council, even in the event of Scotland and Northern Ireland's secession. No doubt, this may give rise to the issue of legitimacy of the former's membership in the UN Security Council, as the membership rights belong to the United Kingdom. However, there was already a precedent in the UN Security Council's history, when Russia became the legal successor of the USSR, while the USSR is still listed in Article 23 of the UNO Charter as one of its fifteen permanent members. The probability of the UNO Charter being amended is very low, although the discussion of its reform has been underway for a long time, and in November 2015, the EU considered, as its long-term goal, the possibility of it becoming a member of the UN Security Council in place of the UK and France. ●