

What kind of divorce: a clean, hard Brexit or a messy, confrontational Brexifast?

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Prime Minister Theresa May is attending her final European Union (EU) Summit before the Article 50 negotiations are triggered, almost nine months after the referendum vote. The perceived wisdom is that the proceeding by which United Kingdom (UK) will leave the EU will take at least the two years specified in the EU Treaties, with some arguing that this period might have to be extended (which would need to be decided unanimously by the EU27), given the sheer difficulty and scope of issues that will need to be resolved. However, such an extension seems rather unlikely in light of the required unanimity, unless it is a purely technical provision to allow for the ratification of a deal already reached or to conclude on some of the finer details.

The imminent negotiations will focus on the withdrawal process, only taking account of the framework for the leaving country's future relationship with the Union. They are not intended, nor is it possible within this timeframe, to pre-negotiate a future trade and investment deal. Such a deal will take a number of years to conclude and the negotiations can only start in earnest after the UK has left the EU. But for many, there is at least hope that some kind of transitional deal can be found to bridge the time between withdrawal and the future deal.

Towards a trade deal?

What is clear is that the long-term deal will not be a soft Brexit – i.e. the UK remaining within the single market and/or the customs union. The red lines of the UK government, in particular concerning the freedom of movement of people and the role of European law and the European Court of Justice, made it impossible to strike a deal modelled after EFTA/EEA membership. In the end, it was the UK government that reached this conclusion, making it clear that it will be a hard Brexit, or, as dubbed by Theresa May, a clean Brexit.

So now there is clarity about the UK's position on the single market and the customs union, and, by implication, an indication of what the long-term desired outcome is from the UK perspective: a comprehensive deal that minimises the impact on the trade and investment flows between the UK and the EU while at the same time enabling Great Britain to be selective regarding in-migration and strike trade deals with the rest of the world.

It remains to be seen how likely such a trade deal will be. Any such deal would have to meet the interests of the EU27, as well as satisfy the European Parliament, which will probably react unfavourably to any mercantilist behaviour, for example with regard to corporate tax. But before both sides can even enter these negotiations there will have to be a successful conclusion of the withdrawal agreement.

First things first

With respect to the withdrawal, London's expectations and demands are still highly unclear. The UK government's White Paper said little about this crucial first step in the process. The overall indications are contradictory: while the government has repeatedly noted the need to avoid going over a cliff's edge, the White Paper also emphasises that no deal is better than a bad deal. The Article 50 notification could give an indication of what the direction of travel is going to be: will there be a sign of willingness to compromise or unreasonable demands that cannot be met by the 27?

There will be a number of tricky issues in the Article 50 negotiations, including, for example, the question of UK benefits for EU citizens. A big hurdle will be the legacy payments the EU is going to demand from the UK. While estimates vary, it will certainly be a significant amount. This is anathema to the Brexiteers in the British government and will certainly prompt a reaction in the Eurosceptic tabloid press. So far, at best, this payment has been portrayed in the British debate as the price the UK will have to pay for continued market access. But given the sequencing of the negotiations, this is unlikely to remain a convincing argument. In addition, the conclusion of the House of Lords Committee that there is no obligation for the UK to pay will most likely result in a hardening line on any divorce payments.

From a negotiation perspective, reaching a withdrawal deal without any payment is highly unlikely. After all, the EU will not simply scrap its demands in the face of UK opposition. But without a withdrawal deal, there is little chance of transition arrangements or a long-term trade deal. This will add fuel to the arguments of those in the UK who believe that a quick exit will be better in any case: if you can't reach a long-term deal, better to strive out on your own now to be able to conclude trade deals with other countries.

In addition, there might be a domestic reason why Brexfast is desirable. The Scottish government is adamantly opposed to a hard Brexit and an independence referendum could happen as early as autumn 2018. Leaving the EU before such a referendum might make it harder for the Scots to vote to leave the United Kingdom into a more uncertain waiting stage for EU membership.

Consequences of a breakdown

There is thus a significant risk that there will be a breakdown in the withdrawal negotiations, driven by UK domestic political considerations. This would economically be highly detrimental for Great Britain, with companies bearing the brunt of the immediate consequences, and with significant litigation in both UK and EU Courts. There could be global financial turbulences as a result and the UK's credibility as signatory to international treaties would also be undermined, jeopardising its ability to reach trade deals with third countries.

There would also be a significant cost to the EU. Uncertainty, including legal uncertainty, would affect the workings of the EU. In addition, an immediate cessation of UK budgetary payments would create financial difficulties, which would also necessitate budget negotiations. But a messy Brexfast would also have a positive effect: it would pull the EU27 closer together and provide an example to avoid for Europe's populists.

While there are domestic UK reasons which will potentially increase the risk of a breakdown in the withdrawal negotiations, the big remaining question is what Theresa May is willing to do to avoid going over this cliff. There might well be a real appreciation of the costs such a step could entail. But given the UK government's focus on keeping the Conservative Party together and winning the next election, domestic politics might override economic reasoning. At the very least, we need to start contingency planning for how to deal with the real possibility of a messy Brexfast.

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