PROBABLE EU-UK RELATIONSHIP AFTER BREXIT

PERSPECTIVES OF GERMANY, FRANCE, ITALY, SPAIN AND POLAND

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Executive Summary

This report seeks to answer the question of **how things will develop if, following the 23 June 2016 referendum, the United Kingdom of Great Britain and Northern Ireland leaves the European Union, in a move commonly referred to as Brexit**. The Polish Institute of International Affairs posits that such a scenario would have adverse consequences for both the European Union and the UK. But given that, just a month before the referendum, the possibility that voters will opt for withdrawal cannot be reasonably ruled out, it is only natural to explore how this outcome could impact the future of European integration.

Brexit will necessitate a new agreement between the European Union and the UK which would define a framework for their mutual relations. Possible options range from establishing a preferential trade zone to creating a single market area, including a scenario in which the UK would take part in the developing EU regulations in sectors covered by the agreement.

The eventual model of the relationship will reflect the pattern of economic and political interests of the UK, on the one hand, and, on the other, key EU Member States, namely Germany, France, Italy, Spain and Poland (hereinafter, the B5).[1] The arrangements preferred by the B5 will define the alliances within the EU with regard to the post-Brexit EU–UK relationship among the smaller Member States and their orientation toward the political views of the B5 coalitions.

Member States' preferences for any future agreement with the UK will be contingent on three factors: the scale and intensity of single-market ties to the United Kingdom involving the free movement of goods, services, capital and people; the convergence of views with the country on economic policy at the EU level; and, the vision of the future of EU integration.

The configuration of these factors within the B5 reveals the following:

Germany would give preference to an advanced model of a single market with a strong British voice on regulatory policies (the "Norway plus" model). But the German position also will seek to confine the UK's voice to economic matters and bar it from debates on the further deepening of integration.

France also would prefer a single market-based model, but one that leaves no room for the UK to influence regulatory policies. The optimal solution for France would be if the UK could belong to the European Economic Area (the "Norway" model), in which the country would have to comply with EU regulations but could not influence them. Paris will oppose any institutionalisation of political dialogue with the UK, especially if such bodies were to be vested with co-decision-making powers on the future of European integration.

Spain would support a model involving the UK's broad participation in the single market, with a preference also for the "Norway" model. The Spanish government is likely to stay neutral regarding British participation in the decision-making process, whether on the single market or integration policy. This reflects a similarity in the Spanish and British governments' approaches to certain economic issues, on the one hand, and, on the other, the traditional political alliance with France over the future of European integration. Spain's final position will be defined by a likely new government that will be formed only after the June elections.

Italy most probably would opt for the "Norway" model, too, because it involves wide access to the internal market but not to the decision-making process on economic policy and political integration. But Italy's approach will be flexible, and these issues may well be used as bargaining chips in an attempt to wrench concessions from other areas not necessarily linked to Brexit.

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[1] The B5 was defined according to the following criteria: population (voting rights in the Council of the EU) and GDP.

Poland would call for the current, strong economic integration ties with the UK within the single market to be continued, with a focus on the free movement of people. Also, given that Poland's vision of economic policy and European integration is similar to the UK's, the Polish government likely would tilt towards giving it some say on internal market regulations (the "Norway-plus" model) and institutionalising decision-making bodies in potential areas of political cooperation between the EU and UK.

As this presentation of these five Member States' preferences indicates, **the most likely model for the EU–UK relationship given Brexit would be one close to that of membership in the European Economic Area (EEA), i.e., the "Norway" model**. The United Kingdom would enjoy wide access to the EU's internal market but would not have a say on EU regulations with which it would have to comply.

It is also possible that a more advanced form of cooperation would be agreed whereby the UK retains influence on the EU's single-market regulations ("Norway plus"). The pattern of interests of the key Member States, including in their economic ties with the UK, suggests that Poland and Germany would be especially interested in the "plus" arrangement. The political rationale for this model is that while Norway has never been an EU Member State, the new status of the UK would reflect the reality that for several decades while it was an EU member, it contributed both to making and co-authoring EU regulatory policies.

At least two conditions have to be met before agreement can be reached on using the "Norway plus" model. First, the UK would have to accept all single market-related obligations, i.e., free movement of people and contributions to the EU budget. Second, a large intra-EU "Norway plus" coalition would have to be built that would be capable of persuading France and Italy to embrace deeper cooperation with the UK. **Poland and Germany could play a key role in building such a coalition**, since it is in their interest that the UK maintains its influence on the shape of the single market. **Such attempts, though, may be thwarted by France**, which is seeking to restrict London's say on regulatory policies as much as possible and benefit politically from the UK's "abdication" of its legacy of EU membership. France would be soliciting support for this line from Italy and Spain. Thus, negotiations on the new relationship may lead to **the emergence of a new pattern of influence exerted by individual Member States and EU institutions as part of European integration.**

Conclusions

An analysis of the preferences that the five key Member States have with regard to the EU's future relationship with the UK leads us to the following conclusions (also shown in Table 1; Table 2 presents details of economic ties).

Germany, given its strong economic links in foreign trade and investment, probably would seek to ease UK access to the single-market framework. Similar approaches to a number of economic issues may prod Berlin towards accepting joint institutionalised bodies dealing with regulatory policies of the single market. Yet, for Germany, reconciling its economic interest in securing close ties to the UK with the strategic aim of deepening the EU's political integration will be a challenge. Making good on the latter might require restricting the UK's influence on the direction of this process by limiting the creation of any joint decision-making bodies. Brexit may trigger a change in Germany's EU policy course with a shift in position towards abandoning the idea of widespread integration to focusing on deepening cooperation within the EU core. With such an approach, Germany would likely find political allies in France, Italy, the Netherlands and Belgium.[2]

France, with a record of intense trade exchange and joint investment, would also seek to put the relationship with the UK on the single-market basis without pressing for any British participation in decision-making, in view of the countries' differences on economic policy. It should be kept in mind that negotiations with the UK would be taking place in the shadow of the 2017 French presidential elections. The current government is very likely to be unwilling to grant too many privileges to a United Kingdom that has left the bloc to prevent strengthening National Front. To France, the best model would be the "Norway" model, involving British membership of the EEA in which the UK would be required to adjust to EU regulations without influencing their content. If, however, things move to a stage where joint decision-making institutions have been negotiated, France would seek to weaken as much as possible the British influence on the bloc's economic policy and further integration. France sees in the absence of British government from EU decision-making the chance to deepen eurozone integration, build on European social policy and reinforce its security policy.

Spain, in view of its strong positions in direct investment (FDI) in the UK, a services trade surplus, and close cooperation in the financial sector, it would be in favour of a high degree of economic integration with the United Kingdom. Thus, its preference would be for a model with a single market within the EEA framework. Keeping free movement of people would benefit Spain, given the growing scale of Spanish migration to the UK, but if need be, this question could also be regulated through a bilateral agreement, given the considerable numbers of Britons on the Iberian Peninsula. Even despite similar views on some economic questions, the Spanish government would rather stay neutral if a debate is held on including the UK in the process of EU decision-making concerning the internal market. Because of the long spell of non-governance in Madrid and, consequently, Spain's disengagement from debate on the future of EU integration, it is much more difficult to predict what attitude the country could take towards the institutionalisation of British influence on EU regulations. In fact, the Spanish position would be largely contingent on the outcome of the parliamentary election planned for just three days after the British referendum.

Italy also is likely to back the "Norway" model based on UK EEA membership. Although Italy is less exposed to the economic impact of Brexit than the rest of the B5, it has relatively strong trade volume in terms of capital and services with the UK. But given the country's cautious approach to market deregulation and desire to deepen political integration within the Union, it

[2] K. Borońska-Hryniewiecka, "The Dutch EU Presidency: Between Seeking Unity and Policy Effectiveness," *PISM Bulletin*, no. 3 (853), 12 January 2016, www.pism.pl/publications/bulletin/no-3-853.

should be expected to oppose giving the UK a say on economic policy and the direction of the EU's future evolution. Italy may try to exploit Brexit to force the idea of differentiated integration and increase the use of the community method, especially with respect to policies on employment and migration.

Poland, which in 2015 reported its first trade ssurplus in a long time (thanks in part to exports to the UK) and whose citizens form the largest immigrant group in the United Kingdom, will be seeking arrangements that give Britain a presence in the internal market and secure continued free movement of people. Because the Polish and British visions of market regulations and European integration are similar, the former will most probably support granting the latter say on EU economic policy. It might be expected that in case British influence on EU regulations is negotiated, their common interests within the single market and EU trade policy will trump their differences over the EU budget. Given that both countries remain outside the eurozone and are reluctant to deepen political integration, Poland will support a solution that would grant the UK at least consultative powers in EU policymaking. The similarity of their positions towards Russia might also cause Poland to promote the UK's quest for influence, especially in foreign policy, in order to counterbalance the more conciliatory approach towards Moscow taken by Germany, France and Italy.

Table 1. Arguments for keeping close EU–UK relations after Brexit based on the strength of economic ties and convergence of views on EU economic policy and the future of European integration

		Germany	France	Spain	Italy	Poland
Economic ties with the UK	Trade in goods*	[green]	[blue]	[blue]	[blue]	[green]
	Trade in services*	[green]	[green]	[green]	[green]	[green]
	Foreign direct investment (FDI*)	[green]	[green]	[green]	[green]	[blue]
	Migration*	[yellow]	[blue]	[blue]	[yellow]	[green]
Economic policy: convergence of views with the UK	Support for deregulation of the EU single market	[green]	[red]	[yellow]	[yellow]	[green]
	Support for liberal EU trade policy	[green]	[red]	[blue]	[blue]	[green]
	Support for scaling down intra-EU redistribution	[green]	[red]	[red]	[red]	[red]
Future of integration: convergence of views with the UK	Convergence of views on deepening political integration	[red]	[red]	[yellow]	[red]	[green]

Notes	
	Arguments for advanced cooperation between the EU and Great Britain after Brexit
[green]	Strong argument
[blue]	Medium-strong argument
[yellow]	Weak argument
[red]	Counter-argument
	* Detailed data in Table 2.

Source: Authors' compilation.

Table 2. The UK's economic ties with Germany, France, Spain, Italy and Poland

		Germany	France	Spain	Italy	Poland
Trade in goods*	UK's position among major trade partners, 2015	5	7**	6	6	6
	Trade in goods (exports and imports), % of GDP, 2015	4.21	2.34**	2.85	2.02	3.85
	Surplus, % of GDP, 2015	1.69	0.5**	0.52	0.73	1.72
Trade in services*	UK's position among major partners, 2014	2	2	1	4	2
	Trade in services (exports and imports), % of GDP, 2014	1.4	2.02	1.88	0.90	1.09
	Surplus, % of GDP, 2014	0.01	0.21	0.56	-0.06	0.05
FDI (foreign direct investment) *	UK's position among major FDI partners (two-way investments), 2014	4	4	2	4	10
	two-way FDI, % of GDP, 2014	6.93	7.16	10.65	3.16	1.49
	Surplus (FDI to UK to FDI from UK as % of GDP), 2014	2.67	1.62	0.76	-0.45	-1.13
Migration*	UK position in terms of mutual migration Ties, 2015	11	8	5	13	2
	Migration to and from the UK, % of population, 2015	0.53	0.52	0.87	0.36	1.91
	Surplus of migration to the UK, % of population, 2015	0.27	-0.06	-0.47	0.15	1.73

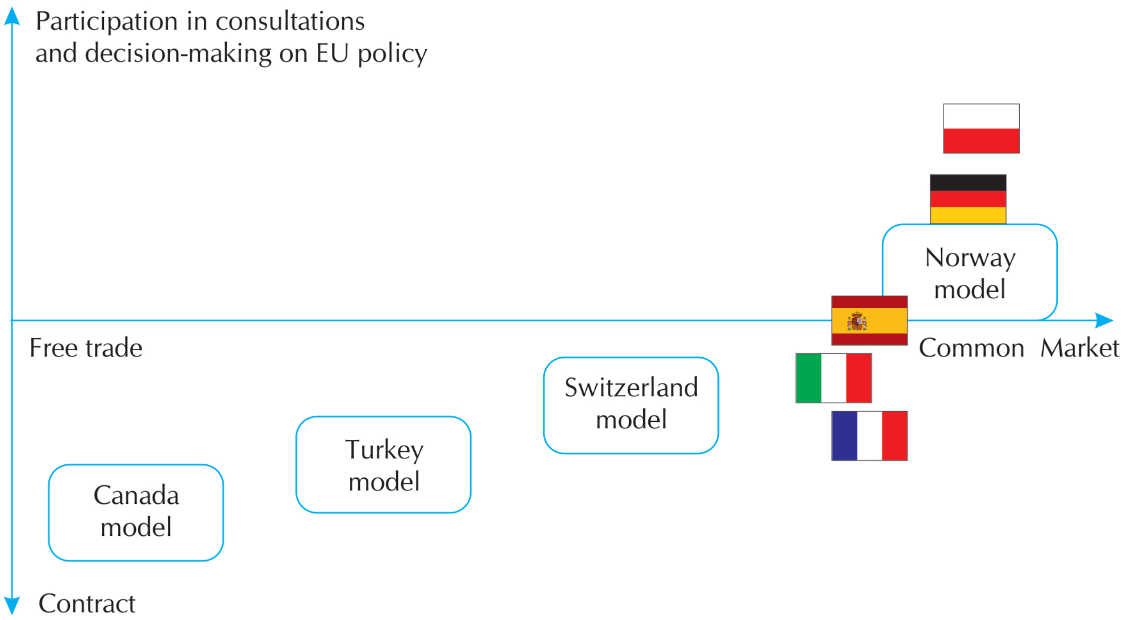
Notes:
* Data in the table, and particularly the UK's position in terms of major partners in areas of economic cooperation (1-5, 6-10, 11-20), form the basis for determining the Member States' likely preferences with respect to EU–UK relations after Brexit (see Table 1).
** Data for 2014.

Sources: OECD. Stat; United Nations Department of Economic and Social Affairs (2015). Trends in International Migrant Stock: Migrants by Destination and Origin (United Nations database, POP/DB/MIG/Stock/Rev.2015); United Nations, Department of Economic and Social Affairs, Population Division (2015). World Population Prospects: The 2015 Revision, DVD Edition; authors' computations.

The B5 preferences as laid out above point to the likelihood of an EU–UK relationship based on the "Norway" model, that is, membership of the European Economic Area. Even though each EU Member State has its own specific interests within the internal market and may be willing to press for the liberalisation of relations with the UK in particular sectors, it might be expected that all of them will be seeking as wide an agreement as possible to ensure that—in case a selected approach is taken—areas of special importance to a given Member State are not excluded.

When it comes to allowing the UK access to decision-making of internal market regulations and EU economic policy after Brexit, the B5 opinions will be divided. While Germany and Poland will likely give their support to arrangements in which London participates in developing EU regulations, France and Italy can be expected to block such arrangements, while Spain may remain neutral (although if required to take a definitive stance, it may be inclined to side with the latter).

Diagram 1. The B5 member states and their likely favoured models of EU-UK relations post-Brexit



Source: Authors' compilation.

The institutionalisation of consultative and/or decision-making bodies that would give the UK a say on any aspect of EU political integration post-Brexit looks like a fairly distant prospect. If, however, such negotiations proceed, Poland would be the only B5 country willing to lobby for London. The remaining Member States' eurozone membership status and vision of the EU's evolution are likely to define the major lines of division in this respect. Potentially, Poland could win allies in Hungary and the Czech Republic, both non-eurozone members with a sceptical view of EU political integration.

Even though the Member States would impose tough conditions, the final agreement on EU–UK relations after Brexit would also be influenced by a British government doing everything in its power to minimise the adverse consequences of withdrawal.

From the British standpoint, the optimal outcome would be to have as much access to the internal market as possible while keeping only the elements of political cooperation that suit British interests.[3] Among them, freedom to provide services, accounting for some 80% of the UK economy,[4] will be especially important, including financial services rendered under bank passporting rights (possible only within the EEA framework).

The Cameron government realises that complete access to the internal market would necessitate taking on many commitments and bearing certain costs arising from EU membership, i.e., keeping free movement of people and contributing to the EU budget. An alternative would obviously be a free trade-based model, but even in its most elaborate form it would offer narrower access to the single market compared to EU membership. In fact, each and every one of the presented models would deprive the UK of influence in EU decision-making and forming internal market regulations, which—Brexit notwithstanding—would continue to fundamentally affect British business.

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[3] "Alternatives to membership: possible models for the United Kingdom outside the European Union," Cabinet Office of the British Government, *Policy Paper*, 4 March 2016, www.gov.uk/government/publications/alternatives-to-membership-possible-models-for-the-united-kingdom-outside-the-european-union.

[4] The United Kingdom has a surplus in trade in services with the EU.

The juxtaposition of the British and B5 preferences indicates that the basic model will be one of EEA membership ("Norway" model). But, as Prime Minister Cameron himself has stated, following the path taken by Norway, which has no influence on internal EU market decision-making, will not suffice. If the British want to negotiate anything further, they will meet resistance from France and Italy, and if they also oppose continued free movement of people and contributions to the EU budget, Germany and Poland may join those blocking a preferential agreement. In such a tense atmosphere, EU leaders may pressure the UK to choose between the "Norway" model or reverting to bare membership of WTO.[5] In fact, it is the EU leaders, not Downing Street, who will hold the stronger collective hand because in the final economic analysis, it is the UK, not the EU, that will lose more from Brexit.[6] EU Member States also might not be willing to accord special treatment to the United Kingdom for political reasons, lest a precedent be set and others encouraged to follow suit.

Summing up, the uncertainty over the British referendum outcome seems to obscure another important unknown, namely the form of the relationship between the UK and the EU and its impact on the interests of individual Member States. This report only presents the likely post-Brexit preferences of the five major EU players, but the research methodology employed here may help establish the relevant positions of the remaining 22 states. Whether Brexit materialises or not, this methodology also may be used to study the preferences of Member States that might in the future be interested in redefining or altering their ties with the EU.

[5] Bare membership of WTO would represent the most pronounced breaking of economic ties with the EU and establishment of tariff barriers to trade, thus exposing UK businesses to a considerable disadvantage.

[6] The importance of the EU market for the UK is much greater than that of the British market for the EU. Almost 50% of British exports go to the EU, compared to around 10% in the other direction (Global Counsel, "BREXIT: Potential impact on the UK and EU," June 2015, www.global-counsel.co.uk/system/files/publications/Global_Counsel_Impact_of_Brexit_June_2015.pdf).

Introduction

On 23 June, UK citizens will vote in a national referendum to answer the question, "should the United Kingdom remain a member of the European Union or leave the European Union?" With just a month to go, it cannot be ruled out that a majority will choose Brexit.

Opinion polls indicate that the difference between the "remain" and "leave" camps is minute, percentage-wise,[7] and that it has fluctuated over the past six months.[8] Even after the February 2016 agreement with the EU on the "new settlement" for the United Kingdom in the EU, which satisfied the UK government and allowed Prime Minister Cameron to flaunt it as an unquestionable political success,[9] no major increase in support for the "remain" option followed.

Working to the disadvantage of those advocating "remain" is the cumulative effect of major challenges facing the European Union. The still unresolved refugee crisis,[10] the recent terrorist attacks in Europe, and the pestering Greek problem in the eurozone make it easier for Brexit supporters to portray the EU as a source of problems rather than a solution. They have also received a boost from the successes of integration opponents in other Member States. After the Dutch in a referendum rejected the Ukraine Association Agreement, arguments were made in Britain that European integration is being criticised elsewhere in the EU and that it is "the beginning of the end of the EU".[11] In addition, the UK's internal situation is more complicated. The disclosure in the "Panama Papers" of Prime Minister David Cameron's financial links to offshore funds in a known tax haven has dealt a major blow to his image and may influence the outcome of the referendum.[12]

Considering all of these factors, the European Union should be prepared for the prospect of having to build anew its relationship with the UK, this time as a non-member. **The aim of this report is to explore what this new relationship may look like and which form it will most likely take**. The pursuit of this analytical task has been rendered difficult by three major problems.

First, given pan-European consensus that the best option is that the British stay in the EU, none of the governments currently in office has taken a stand on the possible future relations between the EU and the UK after Brexit. No Member State would see more gains than losses from it.[13] The general expectation is instead that economic problems will arise because of obstructions to trade, new capital flows and sudden movement of many people. Major political consequences would also follow and the EU's position vis-à-vis other global partners would be seriously

[7] According to an opinion poll conducted in mid-May by YouGov, 44% of the British want to remain, 40% want to leave, and 15% remain undecided. In a study conducted at the same time by ICM, the results were 43% for staying in, 47% for leaving, and 10% undecided. See: M. Goodwin, "Don't trust received wisdom on UK's EU referendum vote," Chatham House, www.chathamhouse.org/expert/comment/don-t-trust-received-wisdom-uk-eu-referendum-vote?utm_source=Chatham%20House%20Newsletter&utm_medium=email&utm_campaign=6968890_Newsletter%20-%2008.04.2016&utm_content=EU-CTA&dm_i=1TYB,45D8A,I53760,F2XB6,1.

[8] For a roundup of public opinion surveys since September 2015, see: *Financial Times*, https://ig.ft.com/sites/brexit-polling.

[9] K. Borońska-Hryniewiecka, "A Win-Win Situation? What to Make of the EU-UK Deal," *PISM Strategic File*, no. 3 (84), February 2016, www.pism.pl/Publications/PISM-Strategic-Files/PISM-Strategic-File-no-3-84.

[10] While the recent Turkey–EU agreement has decreased in the short term the number of refugees crossing to the EU, the bloc still lacks systemic arrangements to reform its asylum policy and protect its external borders, and it also lacks a mechanism to relocate refugees already residing in the Community. In addition to that, the agreement is questioned by international lawyers and it remains unclear how long it will be in force.

[11] A Twitter message by Geert Wilders, the Dutch far-right leader, released immediately after publication of the referendum's initial results.

[12] N. Nougayrede, "The Brexit nightmare is becoming reality. The remain camp is in denial," *The Guardian*, 9 April 2016, www.theguardian.com/commentisfree/2016/apr/09/brexit-nightmare-remain-camp-denial-cameron-panama-papers.

[13] Global Counsel, "BREXIT: Potential impact on the UK and EU," June 2015, www.global-counsel.co.uk/system/files/publications/Global_Counsel_Impact_of_Brexit_June_2015.pdf.

weakened. Britain has huge military potential and voting right in the UN Security Council, so the country's absence from common security policy projects would surely be felt.[14] The British withdrawal also would lead to significant internal complications within the EU. Member States would be forced to revise the EU budget,[15] unleashing fights between net payers and beneficiary countries. The European Union would very likely enter a period of political turbulence, with the emergence of new coalitions of shared interests and new blocking minorities or even, perhaps, successive exits. The risks associated with Brexit are so high that Member States refrain from making public their post-referendum preferences, even if some of these states may perceive some chance of pushing their interests through in an EU without the UK.

The divided British government also cannot choose a particular model to pursue at this stage, and in recent months its focus has been on presenting the considerable economic costs and political problems Brexit may trigger.[16] Economists estimate that withdrawal would slow the UK's economic growth to 1% in 2017 and push up inflation to 2%.[17] The competitiveness of the British economy would take a hit, too, with public debt gradually increasing.[18] There is also a real risk that, after Brexit, EU-friendly Scotland would seek another independence referendum, which could end in a break-up of the United Kingdom.

Second, the future of EU-UK relations is anything but settled. The EU is not obliged to sign a new trade agreement—or any other agreement for that matter—with the UK while negotiating that country's withdrawal from the bloc. Under EU law, the process for a member to exit may last as long as two years, and even longer if the European Council consents.[19] But it is not clear whether, and if so, to what extent the exit agreement would specify the terms of the future EU–UK relationship. This is because Article 50 of the Treaty on European Union (TEU) only deals with an agreement setting out arrangements for a Member State's withdrawal and that it should, it reads, take into account "the framework for its future relationship" with the Union. The fuzzy wording of this provision permits a variety of scenarios, not only for an exit procedure but also for a future EU–UK relationship.

Third, while a withdrawal agreement under Art. 50 TEU may be reached by a qualified majority vote in the EU Council, a new agreement on the UK regaining access to the single market will require ratification by all Member States—and may possibly be subject to consent through referendums.[20] It is thus fair to expect that a long-term negotiating process will have to be set in motion. The UK itself should take an interest in an arrangement in which the withdrawal agreement does not contain too many details about its future relationship with the EU because under Art. 50 TEU it will not be allowed to participate in debate and decision-making by the European Council and the Council of the EU on the terms of the withdrawal. In other words, it is in

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14 *Ibidem*.

15 The UK is currently the second-largest net payer after Germany.

16 "HM Treasury analysis: the long-term economic impact of EU membership and the alternatives," 18 April 2016, www.gov.uk/government/publications/hm-treasury-analysis-the-long-term-economic-impact-of-eu-membership-and-the-alternatives.

17 "One in three chance Britain will leave the EU, warns Morgan Stanley," *The Telegraph*, 12 May 2016, www.telegraph.co.uk/finance/economics/11974221/One-in-three-chance-Britain-will-leave-the-EU-warns-Morgan-Stanley.html.

18 See, for example: "Why Britain Is Better Off Losing the 'Brexit' Debate on Migrants," *Bloomberg*, 12 January 2016, www.bloomberg.com/news/articles/2016-01-12/why-britain-is-better-off-losing-the-brexit-debate-on-limiting-migrants; "The Economic Consequences of Brexit: A Taxing Decision," www.oecd.org/economy/the-economic-consequences-of-brexit-a-taxing-decision.htm.

19 Art. 50 TEU.

20 "Mixed" agreements dealing with areas where competences are shared by Member States and the EU (i.e., the single market) are subject to ratification by national parliaments.

the interest of the UK to negotiate the terms of withdrawal and—either in parallel or subsequently, under a separate procedure—to open talks with the EU on a new model for mutual relations.[21]

Based on these constraints, the analysis in this report involves the following assumptions.

(i) The potential models for the future UK–EU relationship will be defined by two variables: the current depth of economic relations and of political cooperation. As far as the former is concerned, less-advanced forms than the current membership status can be considered, including a preferential trade area, free-trade area, customs union or the single market.[22] With regard to the latter variable, it should be differentiated between a formula of a static contract—one in which a third-party country might influence relations with the EU at the time of negotiating an agreement and loses any influence on EU decisions once the agreement is reached—and a formula for contributing to and controlling the EU's decision-making process to an extent covered by the agreement, usually by means of creating joint decision-making bodies. These two variables, that is, the form of economic integration and form of political relations, are correlated—the more advanced the economic form, the higher the probability of political institutionalisation.

(ii) The new UK-EU relationship will be determined through tough negotiations, contingent on the interplay of the economic and political interests of the Member States, most notably key countries Germany, France, Italy, Spain and Poland. It is around their interests that coalitions of smaller EU states will be built.

(iii) With the largest Member States exerting decisive influence on the negotiations, defining those countries' post-Brexit interests and preferences is of key importance. In this analysis we assume that individual Member States' positions will be influenced by the following factors (see Tables 1 and 2):

1. Intensity of Economic Links with the UK

The extent of these links can be established when considering the main aspects of the single market, namely trade in goods and services, capital flows and the movement of people. The Member States registering high levels of trade in goods and services with the UK (exports and imports), linked with that country via direct investment (FDI) or migration, will be interested in maintaining the state of play (see Table 2). If things change and barriers emerge, adverse consequences may follow for the labour market, company profits and price levels—and they will be more pronounced, the more intense and complex economic relations with the UK are. Far from being confined to competing, these relations also include collaboration within global production and technology chains. The costs if they are weakened would be high for all parties concerned. The pressure to keep existing arrangements will be stronger still where surpluses are registered in key areas of cooperation with the UK. Those Member States that run a trade surplus with Britain and/or have more investments or more migrants than the other way around, will be particularly exposed to the costs of major change, and as such they have a distinct interest in upholding the present terms of cooperation.

Also, a more assertive course in negotiations of the future EU–UK relationship may be demanded by Member States without any major economic ties to the UK. Such cases, though, look few and far between: after all, the United Kingdom is Europe's second-largest economy in

[21] Lawyers argue that the two agreements could be negotiated in parallel, one dealing with the withdrawal and the other with the future EU–UK relationship. See: "House of Lords European Union Committee, 11th Report of Session 2015-16, The Process of withdrawing from the European Union, 4 May 2016," www.gov.uk/government/publications/the-process-for-withdrawing-from-the-european-union.

[22] Cameron has often argued that Britain's interests lie in membership of a fully integrated single market, not a political union. Consequently, following the recent negotiations with Brussels and the February 2016 agreement, the country won an opt-out from the "ever closer union" provision.

terms of GDP and a top player in most sectors of economic cooperation. Still, Member States that run high trade deficits may perceive the removal of British competitors as a chance to strengthen the interests of their own companies.

2. Position on EU Economic Policy

Three detailed questions need to be discussed here:

Position on deregulation of the single market. The British approach remains unchanged: the less regulation and control exercised by governments and EU institutions, the better for the EU economy. This way of thinking reflects the traditionally liberal British attitude to economics and also the fact that in recent years the country has deregulated its labour market and cut social spending. In the EU, this "Anglo-American" approach has its supporters, who often have been able with the UK to enforce their own interests, but there are also opponents taking a more interventionist and state-oriented path and regarding far-reaching market regulation as a necessary element of economic policy.

The openness of the European Union in trade with third countries. The UK has always opted for only minimal restrictions in this field, in view of its traditional links with Commonwealth countries. This approach has both its backers and protectionist-inclined opponents in the EU.

Position on transfers and redistribution policies in the EU, particularly common agricultural policy and structural policies. The British approach has been one of considerable restraint, mostly because of the required contributions to the EU budget and also because of market distortions caused by common policies. The stance taken by the UK government often has inspired the views of a number of Member States, especially net payers to the EU budget.

3. Position on Political Integration

The British position on European integration has for years been marked by restraint in delegating authority to Community institutions and a preference for the inter-governmental model of decision-making. Consequently, the UK's membership of the European Union involves various kinds of derogations (opt-outs) from Community policies. The country is not part of the eurozone or Schengen, and it benefits from the "British rebate" and from opt-out in justice and home affairs. The EU has of late been increasingly split over these issues. Some Member States share the British scepticism of further deepening of integration and would prefer the idea of selective, *à la carte* integration. Others seek the speedy creation of a political union by means of differentiated integration, with internal financial transfers and common security policy.

Given the differences in the Member States' positions towards the UK, the following hypotheses on a new relationship can be formulated:

H1: EU Member States with strong economic links to the UK will seek to protect these links, drawing on the most advanced form of economic integration, the single market.

H2: EU Member States whose economic relations with the UK are not of strategic importance will be much more indifferent to this issue and more willing to accept less complex structures, such as a free-trade area.

H3: EU Member States sharing the British stance on economic policy will opt for keeping as many policy areas as possible where the UK government will be able to influence the single market and the economic policy of the European Union. These Member States may try to establish new institutions suiting their political preferences in this respect.

H4: EU Member States that prefer stronger regulation of the market and state intervention will seek to limit as much as possible the UK's influence on EU economic policy, which translates into opposing any institutionalisation of British influence on EU regulations.

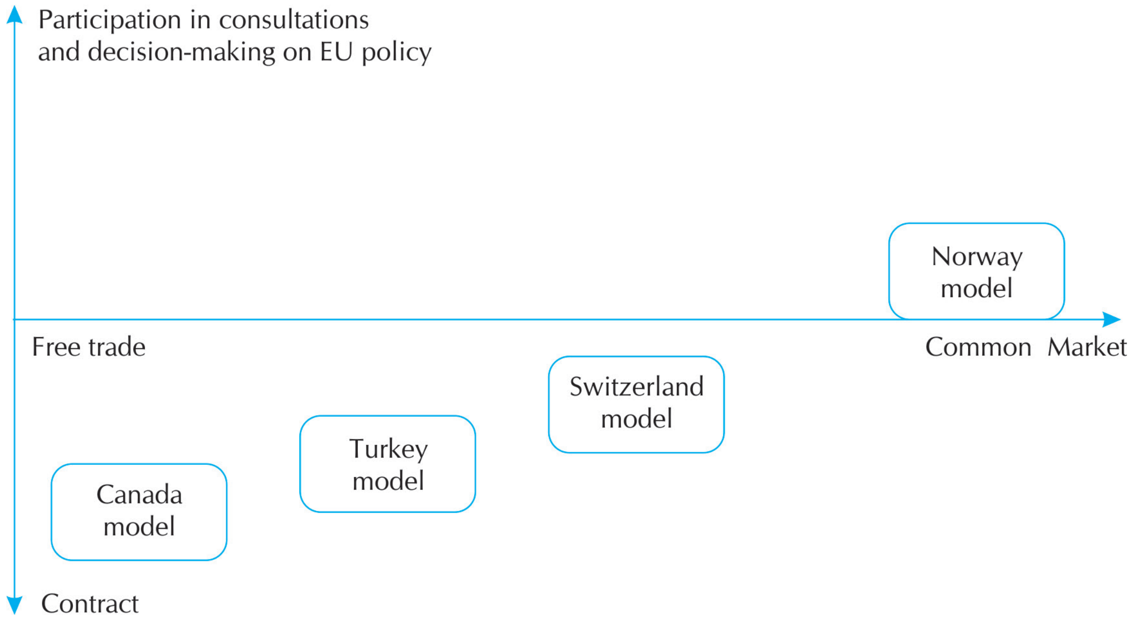
H5: EU Member States wary of deepening political integration will opt for continuation of the UK's influence on the course of political developments in the EU, most notably through joint consultative and decision-making institutions.

H6: EU Member States seeking deeper political integration of the EU will try to limit the room for the UK to slow down this process. They will oppose the institutionalisation of British influence on the political decision-making process in the EU.

1. EU-Third Country Relations: Current Models

When negotiating a new relationship with the UK after Brexit, the EU would not be completely in unchartered territory. Over the past few decades, the bloc has concluded many agreements with third countries that were based on a combination of criteria concerning the depth of economic integration and intensity of political integration. This agreement will no doubt provide points of reference for both the United Kingdom and the EU Member States in case there is a vote to leave, a circumstance that warrants a brief presentation.[23]

Diagram 2. The European Union's relationships with third countries



Source: Authors' compilation.

1.1. Norway Model

The EU's relations with Norway are determined by that country's presence in the single market, based on its membership of the European Economic Area, which includes all 28 EU Member States plus Norway, Iceland and Liechtenstein. EEA membership requires complying with EU regulations and respecting its four freedoms, i.e., free movement of goods, services, capital, and people.

Norway is obliged to observe EU competition and state-aid rules and comply with EU law in many horizontal policies involving consumer protection, company law, environmental protection, social policy, statistics, etc. The EEA agreement provides for equal rights for and obligations on EEA citizens and companies on the single market, including the right to take up employment and obtain social benefits. According to Eurostat, as much as 6% of Norway's

[23] See also: J.C. Piris, "If the UK votes to leave: The seven alternatives to EU membership," *Policy Brief*, Centre for European Reform, 12 January 2016, www.cer.org.uk/publications/archive/policy-brief/2016/if-uk-votes-leave-seven-alternatives-eu-membership; Global Counsel, *op. cit.*; Oxford Economics, "Assessing the Economic Implications of Brexit," 22 March 2016; "Alternatives to membership...," *op. cit.*

population in 2014—more than the UK's– were citizens of EU Member States.[24] Along with the EU states, Norway makes a considerable contribution to the EU budget, thus co-financing, among other things, research and educational programmes and the agencies with which it works.[25]

Norway's access to the EU market, however, is constrained by a number of exceptions, e.g., in agriculture and fisheries and by tariffs and quotas on some product groups. Norway is not part of the customs union, which means that while no customs duties are imposed on Norwegian merchandise covered by the EEA agreement, the Norwegian companies must prove that the products they export and their components originated in the EEA or that they comply with EU rules. Norway's customs procedures and tariffs in trade with third countries have not been brought into line with those of the EU, nor is Norway party to trade agreements between the European Union and third countries. It has the autonomous right to negotiate such deals on its own, but in practice, so far these have been negotiated within the framework of the European Free Trade Area (EFTA), which in addition to Norway includes Switzerland, Iceland and Liechtenstein.

Norway collaborates with the EU in other, non-economic areas, too. It is a member of the Schengen zone,[26] allowing it to participate in EU Council debates but without voting rights, although it has a limited right to voting within Frontex, the EU border agency. Through a bilateral agreement with the EU it also cooperates with law enforcement agencies Europol and Eurojust.[27]

A major feature of the EEA agreement is that the common rules must be constantly updated to keep pace with the evolution of EU law and, therefore, Norway has to take care to ensure that its domestic regulations within the scope of the single market are in line with the EU's. This means that the Norwegian parliament transposes a large chunk of EU regulations into national law. Yet, Norway does not have representation on EU decision-making bodies, such as the Commission, Council or European Parliament, and its influence on EU policies and regulations is fairly limited. Where such influence is exerted is mostly through the European Commission's working groups, at the early stages of the legislative process. Norway also has envoys on the EEA's Joint Committee who exchange opinions with EU representatives and where decisions on extending EU legislation to the EEA are taken by consensus.

And finally, Norwegian experts can pass their opinions on proposed single market regulations to EU institutions via the EEA's Consultative Committee, which includes members of the European Economic and Social Committee. The Consultative Committee seeks to strengthen contacts between public partners of the parties to the agreement and it provides data on the EEA's economic and social aspects.

The strategic body under the EEA agreement is the EEA Council, comprising foreign ministers from EU and EFTA-EEA member states. It provides political impulse for further collaboration and guidelines for the Joint Committee. This relative depth of political cooperation between the EU and Norway is compatible with their shared interests in the field of security, as reflected, for example, in the unified policy towards Russia and in NATO membership.

1.2. Switzerland Model

This model is based on an array of bilateral Swiss-EU agreements regulating the country's access to the single market without membership of EEA. Over the past two decades, Switzerland

[24] "Alternatives to membership...," *op. cit*.

[25] www.eu-norway.org/eu/Financial-contribution/#.VzW8ROTGAWA.

[26] Norway has been a member of the Schengen zone since 2001.

[27] The European Police Office (Europol) is the EU's law enforcement agency tasked with increasing the security level in Europe through assistance to Member States and partners' law enforcement authorities.

has negotiated more than a hundred such deals in individual sectors.[28] Economically, this is a mixed system, with elements of a free-trade area and a single market.

It is in trade in goods that Switzerland enjoys the widest access to the EU market, although there are many exceptions related to agriculture. In services, its access is limited with respect to professional services, such as accounting, auditing and legal services, which has the effect of restricting exports in these segments.[29] Switzerland is barred from access to the EU's financial services market as it is not covered by the so-called "passporting" procedure, which minimises legal barriers to entry by financial entities, forcing Swiss banks to set up subsidiaries in EU countries.[30]

Switzerland respected the principle of free movement of people for quite a long time.[31] Only in 2014 was EU citizens' access to the local labour market questioned, following a referendum in which more than half of the Swiss (50.3%) voted to impose annual quotas for those not holding Swiss citizenship. The EU retorted by curbing Swiss access to educational programmes, such as Erasmus, and to research financing. Faced with the EU's firm refusal to renegotiate the agreement on free movement of people, the Swiss government found itself in a political and legal impasse and is still conducting consultations with the European Commission on this issue.[32] The consequences of this dispute may affect other areas of cooperation.

As with Norway, Switzerland is not in the customs union, nor is it party to EU-third country trade agreements. It is in the Schengen zone, and works with Europol, but has no voting right in the institution's internal decision-making process. In exchange for access to the single market, the country pays a contribution to the EU budget, which, however, is much lower than Norway's.

Unlike in the Norway model, Switzerland's bilateral agreements with the EU are static in nature. Formally, the country is not required to make adjustments on an ongoing basis in response to changes in EU regulations.[33] Yet, the government has sought to do just that to prevent a situation in which the EU might block access to the single market. As in the case of Norway, Switzerland has no representation on EU institutions and has no voting rights in the Council of the EU. It only can influence its relationship with the EU through bilateral agreement negotiations. Once the negotiations are completed, Switzerland—unlike Norway—loses any opportunity to impact decisions taken by the EU with respect to the issue or area in question, even in the consultative dimension.

1.3. Turkey Model

Cooperation between Turkey and the EU involves a customs union in which Turkish manufactured goods and processed agricultural products have access to the EU market. Unprocessed products, services and access to public procurement are, however, excluded. In areas where Turkey has access to the single market, it must adjust its domestic regulations to EU law. Turkey and the EU have a common external tariff, but given the partners' asymmetry, it is the EU that lays down the rules. Turkey, while allowed to enter into trade agreements with third

[28] "Switzerland," European Commission, http://ec.europa.eu/trade/policy/countries-and-regions/countries/switzerland.

[29] "Alternatives to membership…," *op. cit*.

[30] *Ibidem*.

[31] In 2015, citizens of EU Member States accounted for more than 16% of Switzerland's population.

[32] Enforcement of the results of the referendum would not only contradict the bilateral agreement with the EU but also could pose a threat to a whole series of other agreements between Switzerland and the bloc because of the so-called "guillotine clause," which annuls all agreements once one is terminated.

[33] Consequently, it has been more and more difficult to effectively manage the considerable number of separate agreements and it is time-consuming to oversee their current status. On 22 May 2014, Switzerland and the EU opened negotiations on a framework agreement to solve problems resulting from the evolution of the EU's single market regulations and introduce mechanisms to settle disputes over the current web of bilateral treaties.

countries, is required to keep its external tariff in line with the EU tariff. When the EU signs a trade agreement with a third country, Turkey must offer the latter access to its market on identical terms and that third country is under no obligation to reciprocate.

Turkey has no say on decisions taken by the EU, has no representation in the latter's institutions and only to a small degree cooperates with the EU in foreign and security policy. Turkey is not in the Schengen zone and is not involved in law enforcement cooperation through Europol. The country's political and institutional links to the EU, though, are strengthened by its EU membership candidacy and accession negotiations, even if they are more than a decade old.

1.4. Canada Model

This model is defined by the freshly negotiated Comprehensive Economic and Trade Agreement (CETA), of which the main part is an extended free trade agreement covering manufactured goods, some agricultural products and certain services.[34] It includes, however, major limitations (such as export quotas in some sectors) and outright exclusions from preferential treatment (audio-visual services and air transportation, for example). As with most trade agreements, this one also involves country-of-origin rules: Canadian companies must prove that the proportion of non-third country raw materials and components in the price of the final product stands at the required level.

Basically, the Canada model does not go further than its trade-related provisions. Mutual recognition of professional qualifications is limited and the model does not include free movement of people[35] or freedom of investment in the banking sector. For obvious reasons, CETA does not include elements of political integration. This is primarily a contractual relationship and the relevant institutions only serve to implement the agreement.

The future EU-UK relationship will very likely land somewhere between the models described above, but because each reflects a specific situation and particular bilateral negotiations, it will not duplicate them word for word.

It is also probable that the negotiations will result in the emergence of a new model of a two party post-EU exit relationship in which in one extreme scenario would provide for a single market with a much stronger political component (i.e., allowed the UK more institutionalised participation in the EU decision-making process than in the Norway model), while another scenario would downgrade the EU-UK relationship to the level of WTO agreements.

[34] Canada's negotiations with the EU took seven years and were finalised in 2014, but the agreement has yet to come into force as it is awaiting ratification by the European Parliament.

[35] CETA requires adopting provisions on the temporary movement of service professionals.

2. Germany

The Bundesrepublik's approach to British participation in the mainstream of European integration reflects the various dilemmas of German European policy.

On the one hand, Germany sees its vital interests in the United Kingdom's staying in the mainstream. From the very beginning of the Communities, this reasoning was backed by economic considerations. The British market was high on the list of priorities for German industry, recovering after World War II, and the elites in both countries were firmly in favour of dismantling barriers to international trade. Great Britain was also of key importance for security, due to the country's military potential and the strengthening of transatlantic ties, and its membership of the European Communities helped Germany in balancing the influence of France, which in the first decades considered itself the integration leader and did not hesitate to push its interest vigorously. The British membership fitted in well with Konrad Adenauer's vision of a united Europe where broad integration, covering more and more countries, was expected to enable German unification in the long run. For these reasons, the Federal Republic of Germany strenuously supported the British government's early applications for membership of the European Communities, assuming a demanding role of an advocate working hard to persuade the enlargement-wary France. Great Britain's final accession in 1973 was in large measure a result of this patient approach by Germany.

But this is not to say that the United Kingdom's presence in the mainstream of integration has been free of dilemmas for Germany. After all, the country has sought a Europe that is not only "wider" but also "political," sailing towards federalism and quasi-state arrangements. These ideas were openly contested by the UK, which forced Germany to play a difficult game of guarding the cohesion of integration. In pursuing this goal, Germany resorted to the "open vanguard" method of accelerating cooperation among interested Member States and supporting successive enlargements.

The British withdrawal from the European Union would certainly deal a painful blow to Germany. Brexit's major—and likeliest—consequences would include economic problems, destabilisation of EU policies (e.g., budget financing), a strengthening of anti-European integration sentiments (also in Germany itself) and the risk of successive "exits." This is why UK Prime Minister David Cameron's "remain" campaign has been backed by German Chancellor Angela Merkel.[36] Even the Eurosceptic party Alternative for Germany (Alternative für Deutschland, AfD) sees in Brexit a threat for German interests.

If, however, Brexit does take place, the predictable German attitude towards European integration may start to wane. Berlin will face a dilemma of whether to wait for a "return" of the British to a broad EU or, perhaps, to take the path of an accelerated deepening of political integration and the building of *Kerneuropa*. Yet another option—marginal so far but advocated by a growing Eurosceptic community—would be to settle for a less-integrated Europe and push for Germany's own interests, being the strongest force on the continent. The final choice will be contingent on a variety of factors, but Berlin's preferences for the EU-UK relationship will carry significant weight. Hence, these major questions arise: how important for German interests are economic relations with the United Kingdom; how much do Germans need the British to reach their own goals within European economic policy; how popular in today's Germany is the idea of in-depth political integration, so fiercely rejected by Britons?

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[36] "Merkel wirbt für Verbleib Großbritanniens in der EU," *Zeit Online*, 12 February 2016, www.zeit.de/politik/2016-02/angela-merkel-david-cameron-brexit.

2.1. Economic Ties

2.1.1. Trade in Goods and Services

The United Kingdom is the third-largest export market for Germany, after the U.S. and France, and was worth close to €90 billion in 2015 (according to Germany's Federal Statistical Office data). Its weight is additionally emphasised by Germany's huge surplus of €51 billion (second only to its surplus in trade with the U.S.), which was achieved with 2015 imports running at just €38.3 billion.[37] It should be noted that the weight of the UK market has changed in recent years: as early as 2011, German exports were a "mere" €65.5 billion and imports (€44.8 billion) exceeded the present level, thus translating into a smaller German surplus.[38] This reveals an obvious regression on the part of the British.

The numbers largely reflect the respective structures of the two economies. The foundation of the German economy is provided by industry, exporting advanced high-quality merchandise (drawing on tested, mature technologies). The demand for these products is quite stable, avoiding dramatic fluctuations even in the worst of economic times. The industrial sector's share of German GDP stood at 22.3% in 2015—almost unchanged from the 1994 level of 23%—which compares with the EU's average, oscillating around 15–16% (15.3% in 2015). In the United Kingdom, the corresponding proportion is particularly low at just 9.4% of GDP,[39] which may explain the trade imbalance. In a breakdown by product group, the German surpluses are particularly high in vehicles, machines, chemicals, data processing equipment, electric products and optical equipment. In British exports to Germany, a relatively high proportion is accounted for by oil and natural gas.[40]

A much more balanced trade is seen in services, where the United Kingdom's relative position is much stronger than in industry, reflecting a powerful financial sector with its largest "powerhouse," the City of London. But following reforms in recent years and increasingly more vigorous operations by banks and insurance companies, Germany has more and more to offer in this field. In 2014, German service exports to the UK reached €20.6 billion, a considerable portion of the country's overall service exports to the whole of the EU (€106 billion). British service exports to Germany amounted to €20.2 billion, representing one-eighth of Germany's combined service imports from all EU Member States.[41] The two-way relations can thus be described as intensive.

[37] "Rangfolge der Handelspartner im Außenhandel der Bundesrepublik Deutschland," Statistisches Bundesamt, 2016, www.destatis.de/DE/ZahlenFakten/GesamtwirtschaftUmwelt/Aussenhandel/Handelspartner/Tabellen/RangfolgeHandelspartner.pdf?__blob=publicationFile.

[38] "Export, Import, Globalisierung 2011," Statistisches Bundesamt, 2012, www.destatis.de/DE/Publikationen/Thematisch/Aussenhandel/Gesamtentwicklung/AussenhandelWelthandel5510006127004.pdf?__blob=publicationFile.

[39] "Anteil der Industrie am BIP seit 20 Jahren nahezu konstant," Statistisches Bundesamt, Pressemitteilung Nr. 124, 8 April 2015, www.destatis.de/DE/PresseService/Presse/Pressemitteilungen/2015/04/PD15_124_811.html.

[40] "Großbritannien – Statistik – Umsatz – Einfuhr – Ausfuhr – Export – Import," Enterprise Europe Network, www.een-bayern.de/een/inhalte/Unser-Service-fuer-Sie/Auslandsmarkterschliessung/Laender/Europa/Grossbritannien/Export-Import-Statistik-Grossbritannien.jsp.

[41] "Außenhandel und Dienstleistungen der Bundesrepublik Deutschland mit dem Ausland," Statistisches Bundesamt, 2015, www.destatis.de/DE/Publikationen/Thematisch/Aussenhandel/Gesamtentwicklung/AussenhandelDienstleistungsverkehr.html.

Table 3. German trade with its main partners, 2015, € billions

Export			Import	
1.	U.S.	113.9	China	91.6
2.	France	103.0	Netherlands	88.0
3.	United Kingdom	89.3	France	67.0
4.	Netherlands	79.5	U.S.	59.3
5.	China	71.3	Italy	49.1
6.	Italy	58.1	Poland	44.5
7.	Austria	58.1	Switzerland	42.7
8.	Poland	52.1	Czech Republic	39.3
9.	Switzerland	49.2	United Kingdom	38.3
10.	Belgium	41.3	Austria	37.4
Trade turnover (exports + imports)			Balance (exports – imports)	
1.	U.S.	173.1	U.S.	+54.6
2.	France	170.1	United Kingdom	+51.0
3.	Netherlands	167.6	France	+36.0
4.	China	162.9	Austria	+20.7
5.	United Kingdom	127.6	United Arab Emirates	+13.7
6.	Italy	107.2	Spain	+12.3
7.	Poland	96.6	South Korea	+10.2
8.	Austria	95.4	Saudi Arabia	+9.1
9.	Switzerland	91.9	Italy	+9.0
10.	Belgium	78.2	Sweden	+8.9

Source: Statistisches Bundesamt.

2.1.2. Capital Links

Germany is among the world's biggest capital exporters, which is not surprising for a country with structural trade surpluses. Its foreign direct investment (FDI) in 2013 reached €1.233 trillion, of which half, or €665.9 billion, was in EU Member States. Within this group, the United Kingdom is the most important partner, absorbing more than €126 billion worth of German FDI. These investments came from over 2,200 companies with a combined workforce of 354,000 and total sales of €172.6 billion in the UK[42] (among them: Siemens, Bosch, BMW, VW, RWE, E.ON, Deutsche Telekom, Deutsche Post, Linde, and Heidelberg Zement[43]).

The German presence on the British market may soon become still more visible. Following the February 2016 announcement of plans to merge the London Stock Exchange (LSE) and Frankfurt-based Deutsche Börse AG, it looks like the project that had been mooted for almost two decades will finally come to fruition. The Germans are to take a 54.4% stake in the combined entity, worth an estimated $30.5 billion. In actual fact, this will be a tripartite alliance—German-British-Italian—remembering that a decade ago LSE took over the Milan-based Borsa Italiana. In addition to benefitting from the economies of scale, the new scheme is expected to put up more effective competition against Euronext, an alliance of Paris, Brussels, Amsterdam and Lisbon and owned by Intercontinental Exchange (ICE), the operator of the New York Stock Exchange.[44]

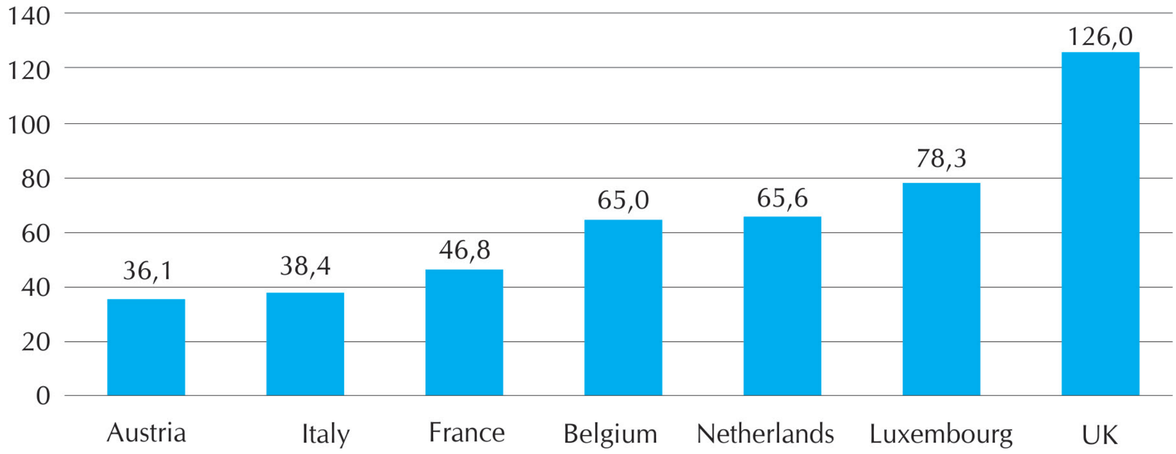
[42] "Bestandserhebung über Direktinvestitionen," Deutsche Bundesbank, April 2015, www.bundesbank.de/Redaktion/DE/Downloads/Veroeffentlichungen/Statistische_Sonderveroeffentlichungen/Statso_10/2015.pdf?__blob=publicationFile.

[43] According to the German Missions in the United Kingdom: www.uk.diplo.de/Vertretung/unitedkingdom/en/04/Economy/Bilateral-Economic-Relations.html.

[44] J. Detrixhe, "Deutsche Boerse Nears Merger with LSE as Brexit Vote Looms," Bloomberg, 26 February 2016, www.bloomberg.com/news/articles/2016-02-26/deutsche-boerse-moves-closer-to-merger-with-lse-as-brexit-looms.

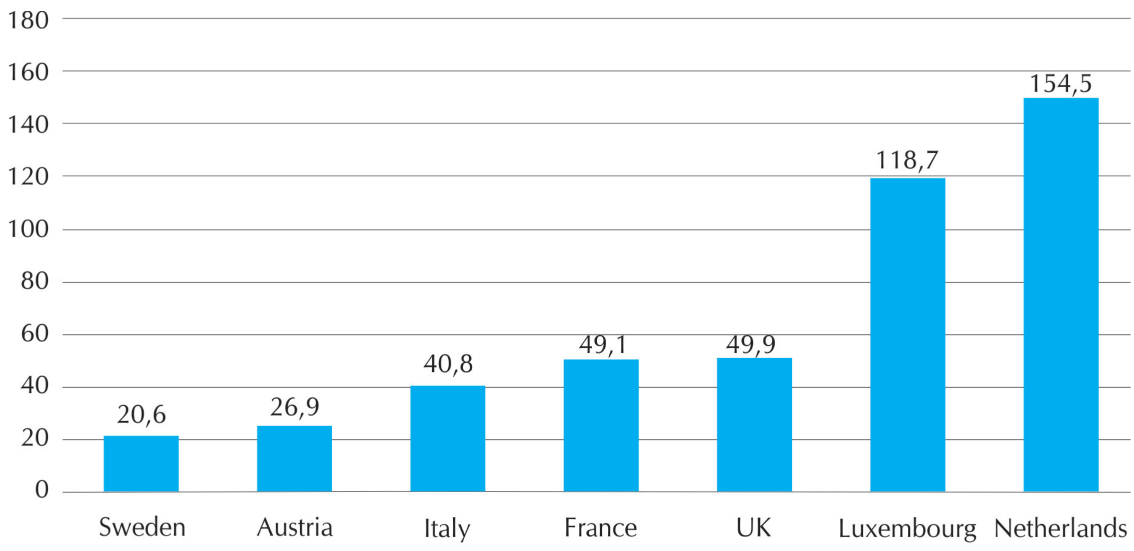
The British direct investments in Germany, even if quite considerable, are much lower. In 2013, the United Kingdom contributed almost €50 billion to Germany's inward FDI total stock of €650.8 billion (of which €504.5 billion came from EU Member States).[45] Among the biggest UK investors are petroleum companies BP and Shell, and also GKN, Terra Firma and Rolls Royce. The UK places third in German statistics, after Luxembourg and the Netherlands. But it should be kept in mind that the bulk of investments from the two last-mentioned countries come from companies whose parents are based in Germany.

Figure 1. German direct investment in EU member states in 2013, € billions



Source: Bundesbank.

Figure 2. Direct investment from EU member states in Germany in 2013, € billions



Source: Bundesbank.

[45] According to Deutsche Bundesbank.

2.1.3. Migration

The impact on Germany-UK economic relations by migration is much smaller than in trade and investments. According to United Nations statistics for 2013, there were 311,300 German-born residents in the United Kingdom, and 96,900 British-born residents in Germany.[46] Compared to both countries' total populations, these are very small proportions indeed. More German inhabitants were born in Turkey (1.5 million), Poland (1.14 million), Greece, Italy, Croatia or Iran.[47] The low importance of migration between Germany and the UK can be easily explained: there are no major pay differentials between them and over the past decades neither country has suffered any major crisis that might have prodded people to emigrate to the other.

Table 4. German students abroad in 2003 and 2012

	2003	2012
Austria	6151	32 192
Netherlands	6479	25 019
Switzerland	6716	14 352
United Kingdom	10 760	13 720
U.S.	8745	9819
France	6496	6400
China	1280	6271
Total	64 800	135 960

Source: Migrationsbericht des Bundesamtes für Migration und Flüchtlinge im Auftrag der Bundesregierung, Migrationsbericht 2014. Bundesministerium des Innern, January 2016, pp. 116–117.

The qualitative dimension of migration may prove more interesting than sheer numbers and may help explain why there are more Germans in Great Britain than Britons in Germany. From the German perspective, the United Kingdom—and particularly the financial sector, with the City of London—is a great magnet for professionals, researchers and students. According to data from the German academic exchange centre DAAD (*Deutscher Akademischer Austauschdienst*), out of a total of 17,886 German academics who in 2013 opted for research work abroad, many chose the U.S. (16.1%), with the United Kingdom coming second (6.2%).[48] The UK is also an important education destination: out of the 136,000 German students enrolled in foreign colleges/universities in 2012, 13,700 did so in Britain. This number may be lower than in the case of German students in Austria (more than 32,000), the Netherlands (25,000) and Switzerland (13,400),[49] but it is important to remember about the high costs of university education in the United Kingdom. The flows in the other direction are incomparably lower. In the 2014/2015 winter semester, a total of 1,163 British students took up studies in Germany, or just about a quarter of the numbers from Italy or Spain.[50] The key barrier is obviously language, but career prospects are not encouraging for the British, either. Opportunities for outsiders' promotion in corporate Germany are relatively limited.

[46] "Trends in International Migrant Stock: Migrants by Destination and Origin," United Nations, Department of Economic and Social Affairs, 2013 (United Nations database, POP/DB/MIG/Stock/Rev.2013).

[47] *Ibidem*.

[48] "Migrationsbericht des Bundesamtes für Migration und Flüchtlinge im Auftrag der Bundesregierung, Migrationsbericht 2014," Bundesministerium des Innern, January 2016, p. 222, www.bamf.de/SharedDocs/Anlagen/DE/Publikationen/Migrationsberichte/migrationsbericht-2014.pdf?__blob=publicationFile.

[49] *Ibidem*, p. 116.

[50] *Ibidem*, p. 197.

2.2. Economic Policy Preferences

2.2.1. Regulatory Policy

At first sight, the German economic model may look like it is poles apart from the liberal approach to the economy prevailing in the United Kingdom. This view seems to be supported by Germans' strong sense of collectivism, the special role assigned to trade unions, and the traditionally big importance of social policy. It is no accident that such descriptions as the Rhineland model of capitalism, coordinated market economy (CME), or social market economy, associated with Germany, are contrasted with Anglo-American (or Anglo-Saxon) capitalism. And, indeed, the differences show up in the approaches to some areas of the single market. The Germans, for example, take a more sceptical view of the freedom to provide services and of financial market deregulation.

A more nuanced analysis, though, reveals a great deal of similarity. First, economic liberalism is deeply rooted in Germany, too, although it takes a specific form of so-called ordoliberalism, developed in the 1930s by the Freiburg School and later provided the theoretical background for Ludwig Erhard's reforms. German liberalism, while accepting that the free market offers the best possible mechanism for the coordination of economic decision-making, posits that its functioning requires order to guarantee competition and prevent the concentration of power. Even despite many subsequent departures from liberal thinking (such as the rise of corporatism), its role in shaping economic policy has remained substantial. This helps explain why—even in the early EEC of the 1960s—Germany was the leading proponent of enlargement to include the UK. Given the political domination of the statist-minded French, a liberal ally was seen as very much needed. That pattern changed little over the ensuing decades. The German-British cooperation towards keeping the primacy of the free market in the European Union—quite effective, even if not ostentatious—often forced more interventionist-friendly Member States to back down.

Over the past two decades, the United Kingdom and Germany came closer together with similar reforms of the labour market and social policy, founded on the "third-way" concept, which attempted to reconcile social-democratic thinking with the free market. Developed by the British sociologist Anthony Giddens,[51] the "third way" was embraced by Tony Blair and also by Gerhard Schröder, who in 2001–2005 pursued his famous liberal programme "Agenda 2010" and "Hartz IV" reforms. They sought to activate the unemployed by means of cutting down social transfers and deregulating the labour market, resulting in the creation of many low-paid jobs and flexible employment. That line was followed by the Merkel government, which largely helped to bring down the unemployed to the presently very low level (4.7%). The price of success, though, was growing income disparity,[52] a problem being addressed only recently with the introduction of statutory minimum hourly pay.

On the practical level, the many similarities between the British and German approaches to the labour market translated into both governments' support for cuts in benefits for immigrants from other EU Member States. When the United Kingdom took up the issue and won concessions in the EU forum, Germany showed understanding and perceived the move as a measure against abuse, seeking equal rights, not discrimination. Even previously the German government cited the September 2009 judgement of the European Court of Justice confirming Member States' right to curb social benefits of those employed on a temporary basis.[53] And recently, Labour Minister

[51] A. Giddens, *The Third Way: The Renewal of Social Democracy*, Polity Press, Malden 1999.

[52] M. Fratzscher, "Verteilungskampf: Warum Deutschland immer ungleicher wird," Hanser, München 2016.

[53] "Deutschland darf EU-Migranten Hartz IV verweigern,"*Der Tagesspiegel*, 15 September 2015, www.tagesspiegel.de/wirtschaft/urteil-des-eugh-deutschland-darf-eu-migranten-hartz-iv-verweigern/12321312.html.

Andrea Nahles has announced further restrictions in access to the German benefits system by employees from EU Member States.[54]

2.2.2. International Trade

Both Germany and the United Kingdom set great store in trade liberalisation and regard an open attitude towards the global economy as an opportunity, not a threat. The British position reflects, on the one hand, allegiance to liberal values and, on the other, the strong ties with the British Commonwealth. Trade with countries such as India or Australia, especially in the agricultural sector, was long a bone of contention in relations with France and others, provoking disputes about the orientation of Community trade policy.

The German position is informed by different factors. In the latter half of the 20th century, foreign trade was not only driving German GDP but also served as compensation of sort for truncated sovereignty and a means of building political influence in the world. Consequently, Germany, a middle-sized economy, became an exports leader, occupying top positions in international trade performance tables for years. This continues to be the case today. Even if Germany was overtaken by China and the U.S. on the largest exports list, its current account surplus of over €200 billion leaves no-one in doubt as to the vitality of the country's foreign sales. German ties with non-European markets are fairly strong, and far from weakening they have been all the time tightening. Significantly, the U.S. moved in 2015 to the top of the list of Germany's export markets, for the first time since the early 1960s.

If only for this particular reason, one should expect Germany to show interest in further trade liberalisation (particularly the adoption of TTIP) and in close cooperation with the United Kingdom on this front. But while German big business and even *Mittelstand* (medium-sized companies) are interested in the treaty with the U.S., there has been growing scepticism on the part of the public at large. The fears are largely about consumer safety and big corporations' influence on government—a sensitive issue that has gained notoriety in the aftermath of the financial crisis. Thus, while structural indicators and an analysis of interests might point to a community of British and German opinion on free trade, the growing political dispute over TTIP in Germany calls for a greater dose of caution in drawing unequivocal conclusions.

2.2.3. Redistribution in the EU

With their higher-than-average levels of per capita GDP, Germany and the United Kingdom are net payers to the EU budget. At first sight, their interests may look identical, which should translate into joint efforts to temper expectations from net beneficiaries, interested as they are in high transfers. But the two countries clearly differ in their political attitudes to this issue.

To the British, the budget contribution comes as the price of access to the EU market and—what is only natural within this perception—they seek to lower it as much as possible. Such was the logic behind the British rebate demands, which translated into a lower contribution than the budget arithmetic would dictate. The Germans, on the other hand, look at intra-EU redistribution—through the Common Agricultural Policy and regional and structural policies—as a necessary component of European solidarity and the price of progress on the integration front. The famous adage about the Helmut Kohl government's "chequebook policy" reflected just that—a method of political persuasion whereby partners' resistance at EU summits was overcome by promises of

[54] "Andrea Nahles: Sozialleistungen für EU-Ausländer stark beschränken," *Wirtschaftswoche*, 28 April 2016 r., www.wiwo.de/politik/deutschland/andrea-nahles-sozialleistungen-fuer-eu-auslaender-stark-beschraenken/13513630.html?utm_source=twitterfeed&utm_medium=twitter.

higher payouts from the common budget. That said, it was not above Germany to use the United Kingdom to push demands for budgetary discipline and lower transfers, something Germany itself could not afford politically. A certain symbiosis thus developed between the two countries with respect to the EU's transfers policy: the UK had a lower contribution to the EU budget while Germany could use the argument of its own contribution to the "unification of Europe."

The German scepticism over redistribution is more visible in another sphere of integration, namely fiscal policy. During the post-2008 financial crisis, vociferous calls were made for the eurozone to increase the scale of redistribution by issuing eurobonds or forgiving debts of countries worst hit by the crisis. Those Keynesian ideas were firmly opposed by the Germans, who pushed for a policy of austerity—in other words, to overcome the crisis by means of restrictive budget policy and supply-side reforms (e.g., labour market deregulation). Not being a member of the eurozone, the United Kingdom was not a party to these debates, but if in their course a "transfers union" had been taken up affecting non-eurozone members, the British would have likely sided with Germany's restrictive position.

2.3. Approach to Political Integration

Since the beginning of the integration processes, Germany's Europe policy pursued an ambitious goal of simultaneously seeking a political union and building a large Europe that admits successive countries into the club. That put Germany in the role of middleman between the French idea of exclusive integration, based on strong political institutions, and the approach taken by the British who would gladly limit integration to the single market and economic matters. The United Kingdom has never been interested in deepening integration, which found reflection in the country's distancing itself from the monetary union ideas or participation in the Schengen area.

The German response to this dilemma took the form of the "vanguard" method, under which an absence of consensus on further integration among all Member States would permit a smaller yet determined group to go one with enhanced cooperation. Such a "hard core" would have to be open-ended, to allow other Member States to join once they had met certain criteria. This condition, reconciling the impulses for deepening and widening integration, was presented, for example, in detail in 1994 by Wolfgang Schäuble and Karl Lammers, two Christian Democracy politicians who put forward the concept of a differentiated Union.[55]

As a consequence of the vanguard method, Germany now has a large Europe of 28 members and deepened integration. The country is a key member of the hard core, i.e., the eurozone, and it formulates proposals for more advanced integration platforms. Calls to reinvigorate the vanguard group have recently intensified in response to the eurozone crisis and the migration crisis,[56] one of the latest initiatives is the joint manifesto of German and French economy ministers (Sigmar Gabriel and Emmanuel Macron), who advocated forming a eurozone parliament and the position of a eurozone finance minister.[57] Given the rising problems with reaching agreement among the 28 Member States, the hard core method has been increasingly attractive. Importantly, Germany's relative power within a "small Europe," far from diminishing, would rather increase.

It must be emphasised, though, that this is not the only option in Germany's approach to integration. The key elements of European integration are questioned by AfD, which emerged in 2013 and rose over the next three years to become a political power with which to reckon. Its

[55] W. Schäuble, K. Lammers, "Überlegungen zur europäischen Politik," CDU-CSU, 1 September 1994.

[56] R. Herzinger, "Nur staatlich geeint kann Europa dem Terror standhalten," *Die Freie Welt* (blog), http://freie.welt.de/2016/03/28/nur-staatlich-geeint-kann-europa-dem-terror-standhalten.

[57] S. Gabriel, E. Macron, "Gemeinsame Erklaerung zur wirtschaftlichen Integration, Deutsch-Französischer Ministerrat am 31," March 2015, Berlin, www.bmwi.de/BMWi/Redaktion/PDF/C-D/deutsch-franzoesischer-ministerrat-gemeinsame-erklaerung-zur-wirtschaftlichen-integration,property=pdf,bereich=bmwi2012,sprache=de,rwb=true.pdf.

demands include dismantling the eurozone, reinforcing the role of national states, and confining integration to the single market. This brings AfD much closer to the British Conservatives, and the party is in favour of the UK's staying in the EU. Not inconceivably, AfD may be a harbinger of change in the course of Germany's Europe policy, and it may be that within several years calls for retreat from deep integration will no longer surprise anybody, but for now, AfD attracts the support of no more than a dozen or so percent of the electorate while the continuation of political integration is firmly backed by the establishment.

2.4. Preferred Model of the EU-UK Relationship after Brexit

If the United Kingdom does withdraw from the European Union, Germany will find itself in a tight spot, namely between the economic need to maintain close links with the former Member State and the temptation to grasp an opportunity to build a "small" political union.

The economic ties push Germany in the former direction. The UK market's great weight for German companies will prod the German government towards promoting the most advanced form of cooperation with the United Kingdom, i.e., the single market. The less advanced this form, the greater the risk of obstruction to trade and damage to the German economy. The risk is quite high anyway, given the probable fall of the pound's value against the euro post-Brexit (estimated at even 20%, according to Goldman Sachs). That would weaken the price competitiveness of German goods, bring down exports and lead to a reduction of the very high surplus.[58] The same applies to the argument of capital links. They are so strong that the Germany business community will seek to reduce uncertainty and go on with the existing terms for conducting business activity. This, however, means the necessity of keeping integration at the single-market level intact.

Keeping ties between the EU and the United Kingdom close is also in line with Germany's economic policy preferences. Among the big European Member States, Germany has embraced the most liberal approach to the functioning of the economy, and on many counts it can expect EU support. If Brexit indeed follows, Germany's voting power vis-à-vis more statist-minded Member States will weaken. A pro-deregulation coalition in an EU with the United Kingdom can be expected to gather 41% of the votes, but without that country, the proportion falls to 33% (with 35% needed to form a blocking minority). At the same time, Germany will have less room to manoeuvre when it opts to block more interventionist arrangements.[59] It may thus be interested in building as many institutionalised forms of EU-UK economic cooperation as possible.

But in terms of political integration, a certain weakening of ties with the United Kingdom will prove beneficial. The German interest in building a political union may lead the country to seek narrowing the room for the British government's influence upon in-depth integration. This tendency, a reverse of the country's economic policy preferences, may actually get the upper hand if the opportunity emerges for successful implementation of an EU federalist project, involving several of the most determined Member States.

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[58] J. Kollewe, "Brexit could slash sterling by 20%, warns Goldman Sachs," *The Guardian*, 4 February 2016, www.theguardian.com/business/2016/feb/04/brexit--slash-sterling-20-warns-goldman-sachs.

[59] Global Counsel, *op. cit*.

3. France

The United Kingdom's presence in the EU is very important for France for a number of reasons. To begin with, the UK is France's major ally in promoting EU actions in international relations. Both countries are permanent members of the UN Security Council, possess considerable military potential and have declared they will raise defence spending to at least 2% of GDP, factors which permit pursuing an interventionist international policy.

From France's perspective, the United Kingdom ensures a political balance of powers within the EU, neutralising the dominant position of Germany.[60] It should be remembered that France backed the UK accession to the EU in 1969 only in response to the growing economic weight of Germany after a long period of opposing British presence in the EU.[61] This argument is still relevant. In this light, the French misgivings are also related to the shape of the EU budget, which not only would shrink after Brexit but would leave France the second largest net payer (taking over the spot from the United Kingdom).

The French elites are also wary of the indirect consequences of Brexit, especially a surge in euroscepticism.[62] A British withdrawal from the EU would be a point of reference for the extreme right party National Front, which has as an aim to contest EU actions. Its leader, Marine Le Pen, has already declared that if she wins the 2017 presidential election, she would follow the British model in France's relationship with the EU while also demanding her country regain control of border management and fiscal and monetary policy.[63]

For those reasons, France is a firm supporter of "Bremain" (i.e., the UK staying in the Union). If Brexit wins out, however, an entirely new political situation will develop that might make France no longer support close ties between the United Kingdom and the European Union. Such calculations likely would result from economic links and preferences concerning EU economic policy and political integration.

3.1. Economic Ties

3.1.1. Trade in Goods and Services

According to data from the French office for customs duties and indirect taxes (Direction générale des douanes et droits indirects),[64] the United Kingdom is fifth among France's largest export markets, and eighth on its imports list. In 2015, the exports figure was €31.6 billion (7.1% of all French foreign sales), with imports from the UK running at €19.5 billion (3.9% of the country's total imports). These indicators are not particularly high, given the two countries' geographical proximity, the size of their economies and the longstanding tradition of cooperation.

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[60] "Audition de Mme Sylvie Bermann, Ambassadeur de France auprès du Royaume-Uni de Grande Bretagne et d'Irlande du Nord," Sénat, 3 February 2016, www.senat.fr.

[61] Th. Chopic, Ch. Lequesne (eds.), *BREXIT: What Fair Deal between UK and EU Member States?*, SciencesPo Centre des Recherches Internationals, October 2015.

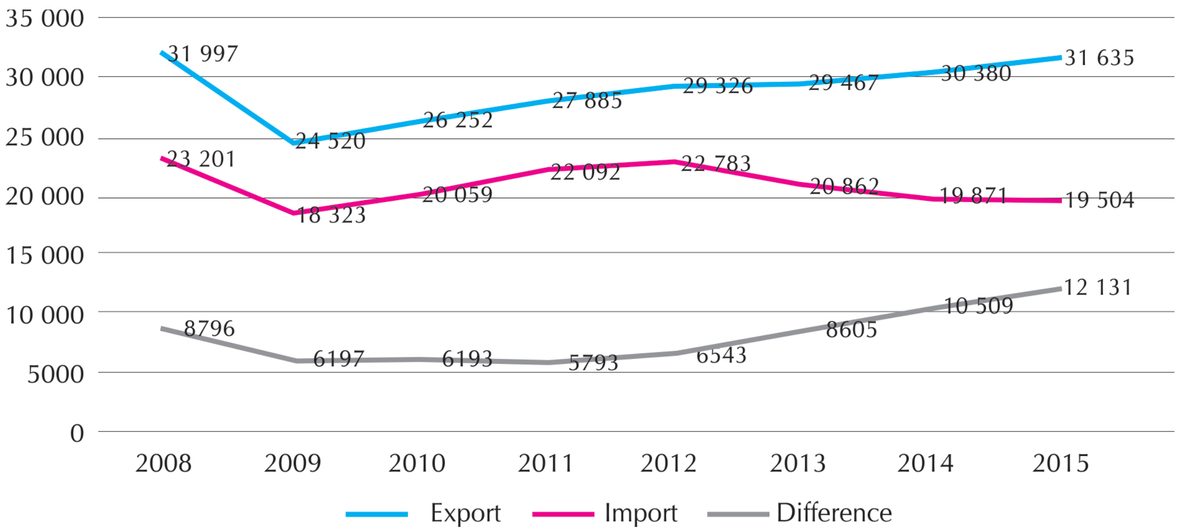
[62] Data from: "Progression du Front National: analyses et infographies," Nil Sanyas' blog, 22 March 2016, www.votrejournaliste.com/progression-du-front-national-analyses-et-infographies.

[63] A. Chassany, "National Front hopes Brexit vote will inspire Frexit campaign," *Financial Times*, 17 February 2016.

[64] "*Le Royaume-Uni, premier excédent bilatéral de la France*," Direction générale des douanes et droits indirects, September 2015, http://lekiosque.finances.gouv.fr/fichiers/etudes/tableaux/ee_60.pdf.

The pattern of trade exchange is more favourable for France and it runs its highest trade surplus with the UK, reaching €12.1 billion (0.55% GDP) in 2015, after an uninterrupted period of growth starting from 2011. This performance, resulting from a continuous rise in French sales coupled with a simultaneous decrease in purchases from the UK, is significant for France due to its overall trade deficit since 2014.[65] The trade exchange between the two economies are largely of an intra-industry nature and is focused on cars and car parts, pharmaceuticals, and aircraft and spacecraft.

Figure 3. Exports, imports and balance in France-UK trade in 2008–2015, € millions



Source: Authors' compilation based on data from the French office for customs duties and indirect taxes (Direction générale des douanes et droits indirects), April 2016.

3.1.2. Capital Links

The United Kingdom is a significant market for French investors, whose exposure there (according to OECD data) reached €102.3 billion in 2014, or 4.8% of French GDP,[66] mostly in the sectors of information and communications technology, retailing, motor industry, food and beverages, and financial services.[67] France was the third-largest foreign investor in the United Kingdom (after the U.S. and the Netherlands) and its share in the investment market has been steadily increasing since 2005. So, too, has been the number of new French investment projects in the United Kingdom: in 2014-2015, French entities launched 124 of them (6.2% of all projects), second only to the U.S. (564).[68] Importantly, the UK tops the EU in terms of the number of French subsidiaries (3,074) and in French workforce (359,000), and comes second (after Germany) in terms of turnover(€113.2 billion).[69] Among the French companies present in the United Kingdom

[65] "France Balance of Trade 1970–2016," *Trading Economics*, www.tradingeconomics.com/france/balance-of-trade.

[66] "FDI positions by partner country BMD4," OECD. Stat, 10 May 2016, https://stats.oecd.org/Index.aspx?DataSetCode=FDI_POS_CTRY.

[67] "Foreign Direct Investment, 2014," Office for National Statistics, 3 December 2016, http://webarchive.nationalarchives.gov.uk.

[68] "UKTI Inward Investment Report 2014 to 2015," UK Trade&Investment, 17 June 2016, www.gov.uk/government/publications/ukti-inward-investment-report-2014-to-2015.

[69] "Implantations croisées d'entreprises France/Royaume-Uni," Ambassade de France au Royaume-Uni service economique regional, May 2015, www.tresor.economie.gouv.fr/File/412749.

are L'Oreal, Givenchy, Renault, Citroën, Électricité de France, Sodexo, and Capgemini.[70] The largest planned French investment project is the €24.4 billion construction of the Hinkley Point C nuclear power plant at Somerset by EDF Energy.[71] That firm already operates eight nuclear stations in the United Kingdom and in addition to Hinkley, Point C has plans to install new reactors to Sizewell C in Suffolk and Bradwell B in Essex.[72]

The weight of British investment in France is considerable, too, with a combined value of €64.6 billion in 2014.[73] In terms of new investment projects in that country, the United Kingdom occupied a high position, fourth in 2015 (after the U.S., Germany, and Italy), with an 8.4% share of the total, and came third in terms of newly employed workforce (2,833).[74] Two hundred companies with a British shareholding operated in France in 2014, giving employment to 200,000 people, among them, Elior (hotels), Castorama, Compass, Darty (electronic devices), and Camaïeu (textiles).[75]

When assessing mutual economic relations, links in the financial sector should also be taken into account. French banks, including the biggest, BNP Paribas, lend out considerable financial resources gathered from its UK counterparts, totalling €343 billion in 2013 (16.2% of French GDP).[76]In case of Brexit, Paris may seek to strengthen its position as a financial centre vis-à-vis London and Frankfurt, as cutting off the City from the European capital market could lead large financial institutions to move to Paris.[77]

3.1.3. Migration

Migration is quite evenly distributed between the two parties. In 2014, there were an estimated 300,000 French citizens in the United Kingdom, even if only 126,804 registered their stay in the country.[78] Young people (25–40 years of age) are the dominant group and the average duration of stay in the UK is 5.7 years.[79] The number of UK citizens in France registered as of 2015 was around 200,000,[80] but the actual figure is believed to be much higher due to nonregistration.[81] Importantly, more than 33% in this group were people of retirement age, reflecting an overall trend in British retiree migration to the south of Europe.

If Brexit happens, France would change control of its borders with the United Kingdom, which might trigger economic consequences related to ensuring the smooth movement of people and goods. The French government has declared that it would terminate the Le Touquet bilateral

70 *Ibidem*.

71 T. Macalister, "France agrees bailout for EDF to proceed with Hinkley Point C," *The Guardian*, 17 March 2016.

72 Based on: "EDF Energy Nuclear New Build," EDF Energy, 22 March 2016, www.edfenergy.com/energy/nuclear-new-build-projects.

73 "FDI positions by partner country BMD4," OECD. Stat, 10 May 2016, https://stats.oecd.org/Index.aspx?DataSetCode=FDI_POS_CTRY.

74 "The international development of French economy: 2015 Annual report. Foreign direct investments," *Business France*, March 2016, p. 25, http://invest.businessfrance.fr/wp-content/uploads/2016/03/2016_RA_BF_UK_V2.pdf.

75 "Investissements britanniques en France et en Languedoc-Roussillon,» Invest Sud de France, May 2015, www.investsuddefrance.com/uploads/paytodownload/2015-10/1444003200_0520866b89c77add0d2520ea25360c95.pdf.

76 Global Counsel, *op. cit*.

77 A. Hug (ed.), "Renegotiation, reform and referendum: does Britain have an EU future?," The Foreign Policy Centre, http://fpc.org.uk/fsblob/1616.pdf.

78 Based on: 22 March 2016, www.diplomatie.gouv.fr/fr/services-aux-citoyens/preparer-son-expatriation/dossiers-pays-de-l-expatriation/royaume-uni; on the other hand, the UN figure for French citizens staying in the United Kingdom in 2015 is over 150,000.

79 France Diplomatie, "Royaume-Uni," *op. cit*.

80 According to UN data, there were some 185,000 Britons staying in France in 2015.

81 M. Turck, "Les expatriés britanniques dans l'angoisse d'un 'Brexit'," *Le Monde*, 19 February 2016, British data at: www.statslife.org.uk, www.gov.uk (accessed 22 March 2016).

agreement,[82] governing this field, and that border checks would be conducted on the UK side, in Kent or Dover.[83] Border controls on the French side are troublesome, given the repeated attempts by migrants to break into the UK and the camps on the continental side, e.g., around Calais.[84] If France called off the Le Touquet agreement, the United Kingdom would have to process asylum applications from undocumented people and border controls would have to be conducted on the British side.[85] This post-Brexit risk would likely force both countries to revise the border-control arrangements.

3.2. Economic Policy Preferences

3.2.1. Regulatory Policy

France and the United Kingdom differ in their approaches to EU economic and competition policy. France is in favour of regulation while the United Kingdom favours deregulation.[86] Many factors impact this situation, but what counts most is the difference in economic models—statist views are dominant in France and free-market ones in the UK.

The two have often jousted in major debates on the development of the EU single market and competitiveness policy in particular. In 2004–2006, prior to the passage of the Bolkestein directive, aimed at introducing common standards for trade and investment in services, France led a coalition of opponents of deregulation while the United Kingdom argued for far-reaching liberalisation.[87] The UK has been the fiercest opponent of France's proposed tax on financial transactions, which will be adopted in June 2016 by 10 countries through the enhanced-cooperation mechanism.[88]

3.2.2. International Trade

France's attitude to liberalisation of foreign trade is less open than Britain's.[89] Even though much of the country's exports go to non-EU markets (40.8% in 2015, mostly to China and the United States, compared to 59.2%[90] to EU partners), France often chooses to pursue a protectionist policy. For example, during the negotiations on the EU's mandate for the TTIP agreement, France sought to limit the scope of trade liberalisation with the United States and won an audio-visual

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[82] The agreement regulates border controls and lets British officers operate on French territory and conduct border checks. Full text: "Treaty between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the French Republic concerning the implementation of frontier controls at the Sea Ports of Both countries on the Channel and North Sea," Le Touquet, 3 February 2003.

[83] A. Asthana, "François Hollande: Brexit would affect immigration," *The Guardian*, 3 March 2016.

[84] "The Implications of Brexit for Border Controls in Calais," Migration Watch UK, March 2016, www.migrationwatchuk.org/briefing-paper/376.

[85] *Ibidem*.

[86] A. Möller, T. Oliver (eds.), *The United Kingdom and the European Union: What would a "Brexit" mean for the EU and other States around the World?*, DGAP Analyses No. 16, September 2014.

[87] E. Grossman, C. Woll, "The French debate over the Bolkestein directive," *Comparative European Politics*, vol. 9, no. 3, 2011, pp. 344–366.

[88] E. Maurice, "EU financial transaction tax on life support," *EU Observer*, 5 December 2016, https://euobserver.com/economic/131435; "Financial Regulation Outlook, Revival of Europe's financial transactions tax," BBVA, February 2016, www.bbvaresearch.com/wp-content/uploads/2016/02/Financial-Regulation-Outlook_Feb_2016_Cap8.pdf.

[89] A. Möller, T. Oliver (eds.), *op. cit*.

[90] "Aperçu du commerce extérieur de la France," February 2016, http://lekiosque.finances.gouv.fr.

sector opt-out.[91] Currently, the French government opposes signing the treaty because it does not consent to the liberalisation of trade in agriculture and culture, or to access to public procurement.[92]

3.2.3. Redistribution in the EU

The French and British positions on the EU budget should be viewed in the context of particular areas. Generally, France is in favour of a high level of financing of EU redistribution mechanisms in preferred areas and is in favour of a large EU budget, a stance that collides with the British position. There have been regular French-British clashes during the negotiations of successive EU budgets, especially over Common Agricultural Policy (CAP). For instance, in the 2014–2020 budget term, France opted for the protection of EU farmers and the highest possible level of agricultural subsidies while the United Kingdom argued for the sharpest possible reduction of CAP financing.[93]

Yet, in some areas of the EU budget, there is room for French-British compromise. Given the problems of the French economy, the infrastructure investments under the "Juncker plan" are highly important for the country[94]—and the United Kingdom supports the plan as it is also a beneficiary of this kind of support.[95]

3.3. Approach to Political Integration[96]

From the very beginning of the EU integration process, France opted for a political dimension and pushed for the creation of political institutions and the deepening of integration. The British government, in principle, did not share that approach, which actually was one of the reasons why France blocked UK accession to the EU in the 1960s. This pattern has not significantly changed. The United Kingdom is still seen as the main opponent of in-depth integration, embracing a different vision, limited to the single market and the economy.[97] France, however, is in favour of eurozone political integration,[98] especially on fiscal and social policies and is for a eurozone "government" with a separate budget and a separate parliament.[99] From the French standpoint, a "multi-speed Europe" is already a fact and no country outside the eurozone should have the right to veto its development.

The French-British differences also pertain to the question of developing EU common security policy. While French policymakers fear that Brexit may weaken the EU's foreign policy in regions important to France, such as the southern neighbourhood, the Middle East and Africa,

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[91] G.X. Bender, "France's unexpected role on the way to a reasonable and balanced TTIP," The German Marshall Fund, June 2015.

[92] N. Vinocur, "François Hollande: 'No' to TTIP at this stage," *Politico*, 3 May 2016, www.politico.eu/article/francois-hollande-no-to-ttip-at-this-stage-matthias-fekl.

[93] H. Klavert, N. Keijzer, "A review of stakeholders' views on CAP reform," European Centre for Development Policy Management, November 2012.

[94] "Audition de M. Jean-Marc Ayrault, ministre des affaires étrangères et du développement international," Assemblée nationale, 1 March 2016, www.assemblee-nationale.fr.

[95] J. Fleming, "UK set to mop up Juncker Plan gains," *EurActiv*, 24 February 2015, www.euractiv.com; G. Gotev, "UK makes the biggest contribution to the Juncker Plan," *EurActiv*, 19 July 2015, www.euractiv.com.

[96] This analysis is based on official pronouncements by government representatives, Socialist Party MPs (notably at meetings of the Foreign Affairs Committee of the National Assembly and Senate and the National Assembly European Affairs Committee) and the Ministry of Foreign Affairs between January 2015 and March 2016.

[97] A. Robert, C. Barbière, "Irritated French politicians begin backing Brexit," *EurActiv (France)*, 10 March 2016, www.euractiv.com/section/uk-europe/news/irritated-french-politicians-back-brexit.

[98] "Audition de M. Jean-Marc Ayrault…," *op. cit*.

[99] "François Hollande: 'Ce qui nous menace, ce n'est pas l'excès d'Europe, mais son insuffisance'," *Le Journal de Dimanche*, 19 July 2015.

the British withdrawal from the bloc may prove conducive to France's ambitious integration plans in the security field. The United Kingdom is not interested in developing the Union's military capabilities, unlike the French government's position. Although both countries helped institutionalise the common security and defence policy (CSDP) in the 1990s, the UK has since refrained from supporting its enforcement, while preferring intergovernmental cooperation. One example of this was the signing of a bilateral agreement on military cooperation with France (Lancaster, 2010)[100], under which a joint expeditionary corps will begin operations in 2016. Brexit would make room for France to promote defence industry integration. Proposals to this effect were voiced by French authorities on the eve of the EU's December 2013 summit on CSDP.[101]

3.4. Preferred Model of the EU-UK Relationship after Brexit

When analysing economic ties, factors such as the relatively high level of trade exchange, the French trade surplus and mutual investment will likely lead France to support a single-market-based EU relationship with Britain.[102] This would include important issues for that country—trade, financial services, and the rights of French employees. As far as employee rights are concerned, France can wait for a favourable bilateral agreement to be concluded, given the equivalence in migration between the two countries.

Due to the differences in the British and French approaches to EU economic policy, though, and that French initiatives in this respect frequently were blocked by the United Kingdom, France might prefer a model of cooperation in which the UK has no voice in the EU's decision-making process (so, the EEA, or "Switzerland" model). France would then have a much greater chance of pushing arrangements it favours. Given France's widespread economic ties, the most favourable option would be the EEA, which would avoid lengthy negotiations on sector agreements while requiring the United Kingdom to automatically adjust to EU law.

France's refusal to allow British participation in the EU decision-making process is also derived from differences in their visions of political integration. An institutionalised British voice on even selected single-market issues could block French plans for further eurozone integration. However, it might be expected that France will be interested in collaboration with the United Kingdom in such areas as the defence sector on both the bilateral and EU levels.

[100] "Treaty between the United Kingdom of Great Britain and Northern Ireland and the French Republic for Defence and Security Co-operation," London, 2 November 2010.

[101] N. Dufour, "France's Intent at the December Defence Council: Opportunities for Poland," *PISM Bulletin*, no. 138 (591), 17 December 2013, www.pism.pl/publications/bulletin/no-138-591.

[102] D. Auroi, "Rapport d'information déposé par la commission des affaires européennes sur les négociations de l'Union européenne avec le Royaume Uni relatives à son maintien au sein de l'Union," Assemblée Nationale, 11 February 2016, www.ladocumentationfrancaise.fr/rapports-publics/164000114.

4. Spain

Spain would prefer the UK stay in the EU because Brexit might encourage separatist tendencies in Europe. If a subsequent referendum was held in Scotland on leaving the United Kingdom and remaining in the Union, similar moves could well be expected in Catalonia and in Basque Country. The Spanish government has not allowed referendums in these regions so far, claiming they are against the country's constitution. Of note is that a parliamentary election is going to be held in Spain at the end of June and the lead-up campaign offers an opportunity to discuss the subject in conjunction with the UK developments.

The United Kingdom's presence in the European Union is also of importance to Spain in the area of justice and home affairs, especially migration. As a country that manages a Schengen zone external border and is exposed to uncontrolled migration flows, Spain has taken interest in British logistical support provided to EU border agency Frontex.[103] Also, the Spanish government can use EU databases, including Europol's,[104] to check on suspected terrorists from the UK. Following the 2004 Madrid attack, Spain has promoted security cooperation within the EU and, for instance, jointly with the United Kingdom seeks to strengthen the system for the exchange of criminal records, including through the European Criminal Records Information System (ECRIS). Another important field in relations with the UK is enforcement of the European arrest warrant (i.e., simplified extradition procedure). According to British data for 2009–2013, many suspected terrorists with a connection to either ETA or Al Qaeda have been transferred to Spain, while 130 people were extradited from that country to Britain (out of a total of 507 from the entire EU).[105]

Spain's situation is also exceptional due to its political dispute with the United Kingdom over the status of Gibraltar. Brexit could be an opportunity for Spain to undertake talks on the subject at the EU level. Spain does not recognise the maritime border of Gibraltar, a British overseas territory, and for this reason has consequently been embroiled for over 300 years in recurring conflicts with the United Kingdom. In the past several years, the EU has been trying to mediate the dispute. Even though Gibraltar has special ties with the European Union, it does not participate in a number of important areas, including the customs union and CAP, Brexit would involve major economic losses for the territory, which has links to Spain and other EU Member States in the services, finance and tourism sectors.[106] Therefore, if Brexit takes place, the Spanish government may adopt a restrictive policy line towards Gibraltar in those sectors,[107] resulting in talks on Gibraltar's staying in the EU and a revision of its relations with Spain.

4.1. Economic Ties

4.1.1. Trade in Goods and Services

According to data for 2015 from the Spanish Ministry of Economy and Competitiveness,[108] the United Kingdom is the fourth-largest export market for that country (after France, Germany

[103] M. Drent, K. Homan, D. Zandee, "Civil-Military Capacities for European Security," Netherlands Institute of International Affairs Clingendael, 2013.

[104] T. Escritt, "Brexit would make UK counter-terrorism job harder: Europol," *Reuters*, 22 February 2016, www.reuters.com/article/us-britain-eu-europol-idUSKCN0VV1CR.

[105] "Spain-UK cooperation in fighting organised crime," Home Office, 27 February 2014, www.gov.uk/government/news/spain-uk-cooperation-in-fighting-organised-crime.

[106] F. Picardo, "'Brexit' would destroy Gibraltar," *Politico*, 1 June 2015.

[107] G. Keeley, A. Ellson, "Spain threatens action against Gibraltar if Britain leaves EU," *The Times*, 29 March 2016.

[108] "ICEX España Exportación e Inversiones," 25 April 2016, www.icex.es.

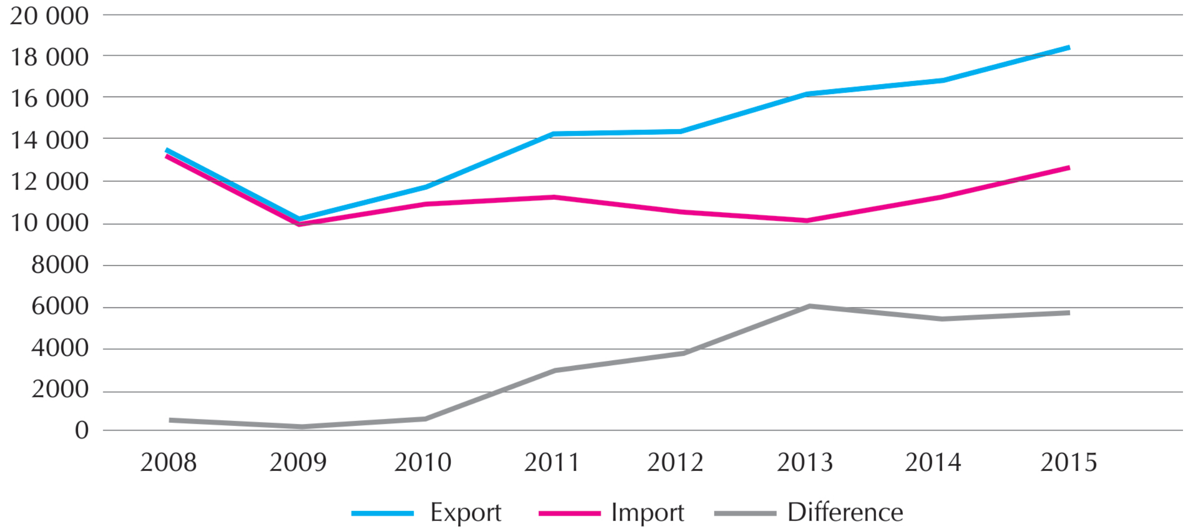
and Italy) and sixth on the imports list. Following a steady increase since 2009, Spanish sales to the UK reached €18.23 billion in 2015 (7.3% of the country's total exports), with imports running at €12.58 billion (4.6%).

Spain's surplus in trade with the UK has continued for more than a decade, which is important for a country registering an overall trade deficit.[109] Standing at €5.65 billion in 2015, this surplus has been growing since 2009, reflecting the post-financial crisis reforms that improved the cost efficiency of the Spanish economy.[110]

The top export sectors include transport vehicles (cars, lorries, buses, aircraft), consumer durables, food and pharmaceuticals. Spain is one of the largest arms exporters (aeronautics, shipbuilding, IT, electronics, missiles and space, auxiliary, armament, land vehicles) in the world, and in 2014 the United Kingdom moved to become its top export market in this sector, overtaking France, Saudi Arabia, Germany and Turkey.[111]

The main Spanish imports include vehicles, semi-manufactured products (e.g., chemicals and pharmaceuticals), consumer durables, food and beverages, energy and fuels. The country's balance of payments benefits from British tourist arrivals, which according to the Spanish statistical office equalled 15.7 million in 2015 (23% of all arrivals). Their spending amounted to €14.1 billion (20.9% of total tourist spending).[112]

Figure 4. Exports, imports and balance of Spanish-UK trade in 2008–2015, € millions



Source: Authors' compilation based on data from the Spanish Ministry of Economy and Competitiveness, April 2016.

109 "Spanish external sector and competitiveness: facts and figures," 19 November 2015, www.thespanisheconomy.com/stfls/tse/ficheros/2013/agosto/150220_Spanish_External_Sector_Facts_and_Figures.pdf.

110 "Implications of Brexit for Spain," AFI Research on Spain, February 2016.

111 For an overview of Spain's military industrial sector, military alliances and operations, see: "Military Industrial Cooperation Between Spain and Australia," Enrique VigueraAmbassador of Spain to the Commonwealth of Australia, 14 June 2015, www.exteriores.gob.es/Embajadas/CANBERRA/es/Embajada/Documents/010203%20Military%20Industrial%20Cooperation%20Between%20Spain%20and%20Australia.pdf.

112 "Statistics of Tourist Movements at Borders (FRONTUR), 2015," www.ine.es/jaxi/menu.do?type=pcaxis&path=%2Ft11%2Fp16028&file=inebase&L=1.

4.1.2. Capital Links

According to Banco de España data for 2014,[113] the United Kingdom was the largest market for Spanish foreign direct investment (17% of all Spanish FDI), totalling €75.6 billion. Around two-thirds of the figure was accounted for by investments in the financial and telecommunications sectors.[114] The top Spanish companies present in the UK include Banco Santander, Telefónica, Iberdrola, Inditex (Zara, Massimo Dutti), Mango, construction firms FCC and ACS, renewable energy companies led by Gamesa and Abengoa, and also Fagor, Ferrovial, Acerinox (aluminium), Abertis (franchising), Repsol (petroleum), Mapfre (insurance), and Meliá Hotels International.[115] In 2012, more than 300 Spanish companies were present on the British market.[116]

In Spain, the United Kingdom comes third in terms of inward foreign investment (after the Netherlands and Luxembourg), with €59.4 billion registered in 2014, or 12.4% of all FDI in Spain.[117] The largest British investment presence is in the sectors of tobacco, telecommunications and finance.[118] The top group of UK companies in Spain includes Alliance, Aviva, BP, Barclays, RBS, British American Tobacco, Cadbury Schweppes, Compass, Deloitte, Diageo, Fitness First, Halifax, Primark, Shell, and Vodafone. According to data for 2012, a total of 700 companies with British shareholding were active in that country.[119]

Spain also has strong ties with the UK in the financial sector. Notable shares in the British market are held by two Spanish banks—Santander with 10%[120] and TSB (owned by Spain's Sabadell) with 4.3%.[121] Moreover, Spain's largest foreign financial assets are located in the United Kingdom (17% of Spain's GDP), ahead of Latin America (12% of GDP) and the combined group of Germany, France and the Netherlands, which accounts for a mere 8% of GDP.[122] In addition to that, Spanish banks' biggest liabilities are to the UK (equalling some 30% of Spain's GDP).[123]

4.1.3. Migration

British migration to Spain is far ahead of the flow in the other direction. The actual number of British citizens permanently residing in Spain is hard to establish because many of them do not register. However, British consular statistics put the number at 800,000 (those staying in Spain on a permanent basis, or part of the year).[124] According to the Spanish statistical office, only

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[113] "Balanza de pagos y posición de inversión internacional de España," Banco de Espana, 2014, www.bde.es/bde/es/secciones/informes/Publicaciones_an/Balanza_de_Pagos.

[114] "Implications of Brexit for Spain," *op. cit*.

[115] "Flujos de inversión entre Reino Unido y España," ICEX, August 2012, www3.icex.es/icex/cma/contentTypes/common/records/mostrarDocumento/?doc=4003124.

[116] *Ibidem*.

[117] "Balanza de pagos y posición...," *op. cit.*

[118] "Implications of Brexit for Spain," *op. cit*.

[119] "Flujos de inversión entre Reino Unido y España," *op. cit*.

[120] "About Santander," 5 April 2016, www.wearesantander.co.uk/de/about-santander.

[121] M. Scuffham, J. Aguado, "Sabadell eyes more UK deals after $2.5 billion TSB takeover," *Reuters*, 20 March 2015, www.reuters.com/article/sabadell-tsb-idUSL6N0WM0TD20150320.

[122] "Country Report Spain 2015 Including an In-depth Review on the prevention and correction of macroeconomic imbalances," European Commission, 26 February 2015.

[123] *Ibidem*.

[124] Cf.: "Daniel Pruce, Deputy Head of Mission, Madrid, My first blog," 22 October 2013, Foreign & Commonwealth Office, http://blogs.fco.gov.uk/danielpruce/2013/10/22/my-first-blog.

282,000 Britons were registered in 2015,[125] with an average age of 52.8 years.[126] Those going to Spain are mostly long-term-stay migrants (more than four years) and senior citizens.[127]

Spain-to-Britain migration is smaller and of a different nature, largely economic in character and linked to the consequences of the economic crisis. For Spanish migrants, the United Kingdom is now a top-of-the-list destination,[128] and in 2013–2014, was the option taken by 17,000, mostly young people (those in the 24–44 age group).[129] According to the UK's statistical office data for 2014, Spanish citizens (45,600) were the third-largest national group (after Romanians and Poles) in terms of employee registrations in the UK, which, however, is not equivalent to permanent residence because the figure also includes seasonal workers and working students.[130] UN data for 2015 put the number of Spanish citizens staying in the United Kingdom at around 91,000.[131]

4.2. Economic Policy Preferences

4.2.1. Regulatory Policy

Even though Spain most frequently cooperates within the EU with the bloc's southern members, the characteristics of its economy means it shares the British position on some economic issues. This is relevant unless a coalition with the UK would work against its interests in eurozone membership.[132] Cooperation in the services sector is one case in point. The sector greatly contributes to both economies,[133] which translates at the EU level into both countries' support for its liberalisation and promotion of free competition. In the 2004–2006 debate on the Bolkenstein directive, Spain joined the UK-led coalition in calling for services deregulation (along with the Netherlands, Czech Republic, Slovakia and Poland).[134] Currently, even with many Member States dragging their feet on implementation of the directive (e.g., France and Germany),[135] Spain and the United Kingdom are pushing for further liberalisation. In 2012, the two signed a letter along with the Netherlands, Italy, Estonia, Latvia, Finland, Ireland, Czech Republic, Slovakia, Poland and Sweden that called for the European Commission to open up the services market in the EU.[136]

Yet, in some major areas of EU economic policy, Spain follows a different line than the UK. This holds, for example, in the tax on financial transactions—which contravenes British interests—

[125] The UN figure for British citizens in that year was around 309,000.

[126] "Avance de la Estadística del Padrón Continuo a 1 de enero de 2015," Instituto Nacional de Estadistica, s. 8, www.ine.es/prensa/np904.pdf.

[127] *Emigration from the UK*, Research Report, Home Office, 2012, pp. 17–22, www.gov.uk/government/uploads/system/uploads/attachment_data/file/116025/horr68-report.pdf.

[128] "Implications of Brexit for Spain," *op. cit.*

[129] "Estadística de Migraciones 2014," Instituto Nacional de Estadistica, www.ine.es/prensa/np917.pdf.

[130] "Statistical Bulletin Office for National Statistics. Migration Statistics Quarterly Report," November 2014, www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/internationalmigration/bulletins/migrationstatisticsquarterlyreport/2015-06-30.

[131] "International migrant stock 2015," United Nations Population Division, 10 May 2016, www.un.org/en/development/desa/population/migration/data/estimates2/estimates15.shtml.

[132] A. Möller, T. Oliver (ed.), *op. cit.*

[133] E. Fernández Corugedo, E. Pérez Ruiz, "The EU Services Directive: Gains from Further Liberalization," *IMF Working Papers*, July 2014, p. 6.

[134] K. Nicolaidis, S.K. Schmidt, "Mutual Recognition 'on Trial': The Long Road to Services Liberalization, *Journal of European Public Policy*, 2007, vol. 14, no. 5, pp. 726–727.

[135] "Services Directive causes further EU headaches," *EurActiv,* 21 January 2010, www.euractiv.com/section/social-europe-jobs/news/services-directive-causes-further-eu-headaches.

[136] "David Cameron and EU leaders call for growth plan in Europe: full letter," *The Telegraph*, 20 February 2012.

that is to be introduced within the scope of enhanced cooperation by Spain, France, Austria, Belgium, Germany, Greece, Italy, Portugal, Slovakia and Slovenia.[137]

4.2.2. International Trade

Due to the gradual improvement in its economic situation and because it is looking for new markets globally, Spain has to some extent similar views on EU trade liberalisation as the UK. For example, both countries' prime ministers supported TTIP in a joint statement from September 2015.[138] This results from the structure of Spanish exports and the country's emphasis on expanding trade globally. According to data for 2015 from Spain's Ministry of Economy and Competitiveness,[139] 53% of Spain's foreign sales went to EU markets and 47% to non-EU countries, including those in Asia and Africa.

4.2.3. Redistribution in the EU

In the period between accession to the EU and the bloc's 2004 enlargement, Spain counted among the poorer Member States and received large transfers of EU funds. Even though it is still a net beneficiary,[140] over the past decade receipts from the EU budget have decreased considerably. Still, Spain benefited from EU financial aid in the aftermath of the 2008 economic crisis and, therefore, its economy continues to rely on EU assistance. For this reason, the country supports boosting the EU's redistribution mechanisms and in European policy it usually joins coalitions of like-minded southern Member States. This puts Spain at the opposite end of the spectrum from the United Kingdom, a net payer demanding lower spending in the EU budget.[141] To give an example, in negotiations of successive EU budgets, Spain, together with France, demanded a high level of financing for Common Agricultural Policy, which is criticised by the UK. Along with France, Spain is among the biggest CAP beneficiaries, with as much as 50% of transfers from the EU budget to that country going to agriculture (as of 2013).[142]

4.3. Approach to Political Integration

Despite strong economic ties, Spain and the United Kingdom have different visions of European integration. Spain is a eurozone member, supports deeper integration of the fiscal union, while the United Kingdom is distancing itself from political integration.[143] Hard hit by the 2008 economic crisis, Spain—as does France—perceives deepening eurozone integration as a chance for increased EU investment in the eurozone's lower-income members.[144]

At the same time, though, while focused on its internal economic policy, Spain stays out of debates on the future of political integration.[145] On eurozone integration, the Spanish government

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[137] E. Maurice, "EU financial transaction tax on life support," *EUObserver*, 5 December 2016, http://euobserver.com; "Financial Regulation Outlook…," *op. cit.*

[138] D. Cameron, M. Rajoy, "Jobs and growth in Europe," Prime Minister's Office, 4 September 2015, www.gov.uk.

[139] "ICEX España Exportación e Inversiones," *op. cit.*

[140] "Spain in the EU," 27 April 2016, http://europa.eu/about-eu.

[141] W. Van Aken, "Voting in the Council of the European Union: Contested Decision-Making in the EU Council of Ministers (1995–2010)," SIEPS 2012:2, www.sieps.se/sites/default/files/2012_2rap_1.pdf.

[142] "Spain, country info," European Commission, 6 April 2016, http://europa.eu/about-eu/countries/member-countries/spain/index_en.htm.

[143] A. Möller, T. Oliver (eds.), *op. cit.*

[144] "Britain in the EU: Renegotiation Scorecard," ECFR, 2015, www.ecfr.eu/europeanpower/britain/renegotiation.

[145] A. Möller, T. Oliver (eds.), *op. cit.*

backs the position developed by France.[146] For example, during the EU-UK negotiations, Spain opposed vesting the United Kingdom with a veto right over eurozone functioning[147] and was also against the British-demand for strengthening Member States' national parliaments.

4.4. Preferred Model of the EU-UK Relationship after Brexit

Given the two countries' economic ties, high levels of mutual investment, and collaboration in finance and in armaments, the Spanish government will be interested in maintaining cooperation with the United Kingdom within the single market. On the migration front, the high number of Britons in Spain allows expectations that a mutually beneficial bilateral agreement might be signed.

It is not clear whether the Spanish government would like the United Kingdom to exert considerable influence on EU economic policy. A common stance on regulation of services and international trade would suggest a "yes" answer but, on the other hand, the agricultural sector's weight and dependence on EU funding seem to point in the other direction. There are grounds to expect that in this respect Spain will back the French position.

On political integration, where Spain has refrained from disclosing its position so far, similar dilemmas may be faced. Membership of the eurozone should make Spain an advocate of in-depth integration, but given the country's economic interests in its relations with the United Kingdom, the Spanish government will likely prefer to stay neutral for as long as possible. If an offer of in-depth eurozone political integration is presented by Germany and France, Spain should be expected to back it.

Bearing in mind these arguments, Spain will likely opt for a high level of economic integration with the United Kingdom, preferably within the single market framework. It is unclear, though, whether this will translate into a preference for close political cooperation and whether some form of institutionalising the EU-UK relationship would be desirable.

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[146] J. Lichfield, "Greece debt crisis: Hollande calls for a 'eurozone government' to further integrate member states—but what will it mean for Britain?," *The Independent*, 19 July 2015.

[147] "Britain in the EU...," *op. cit.*

5. Italy

According to Istituto Affari Internazionali, the costs of Brexit for Italy would be substantial, in view of the country's economic relations with the United Kingdom in trade and investments.[148] Brexit may also have adverse consequences for Italy in terms of transfers to the EU budget. If the UK, the second-largest net payer withdraws from the EU, Italy's contribution will have to increase by 10%, or some €1.4 billion a year.[149]

For Italy, there would be unfavourable political consequences, too, mostly from a weakening of EU stability. The government needs to take into account the growing domestic anti-EU mood of the public. Italy's own right-wing parties may use Brexit to ramp up pressure on the government to firmly resist the austerity policy imposed on the country by the European Commission in the aftermath of the debt crisis. In 2015, the increasingly popular opposition party, Five Star Movement, collected more than 100,000 signatures on a petition for a referendum on Italy's withdrawal from the eurozone. Italy is also concerned about a repeat of the EU referendum scenario in other Member States. In the opinion of Minister of Finance Pier Carlo Padoan,[150] similar sentiments may emerge in France. There are also fears that Italy's post-Brexit position in the EU might diminish as a result of the increased influence of Germany and France.

5.1. Economic Ties

5.1.1. Trade in Goods and Services

The United Kingdom is an important trading partner for Italy, especially as an export market. Italian foreign sales to that country in 2015, according to Eurostat, reached €22.5 billion, or 5.4% of total Italian exports, which is in line with the British economy's weight in the EU. Cars, car parts and pharmaceuticals topped the list of Italian export items. The level of imports from the UK is much lower, at €10.6 billion (some 2.9% of the country's total imports), with the same product groups leading the list as in the case of exports. Consequently, Italy ran a huge trade surplus with the UK in 2015, amounting to around €11.9 billion, following a period of steady growth since the eurozone's economic crisis.

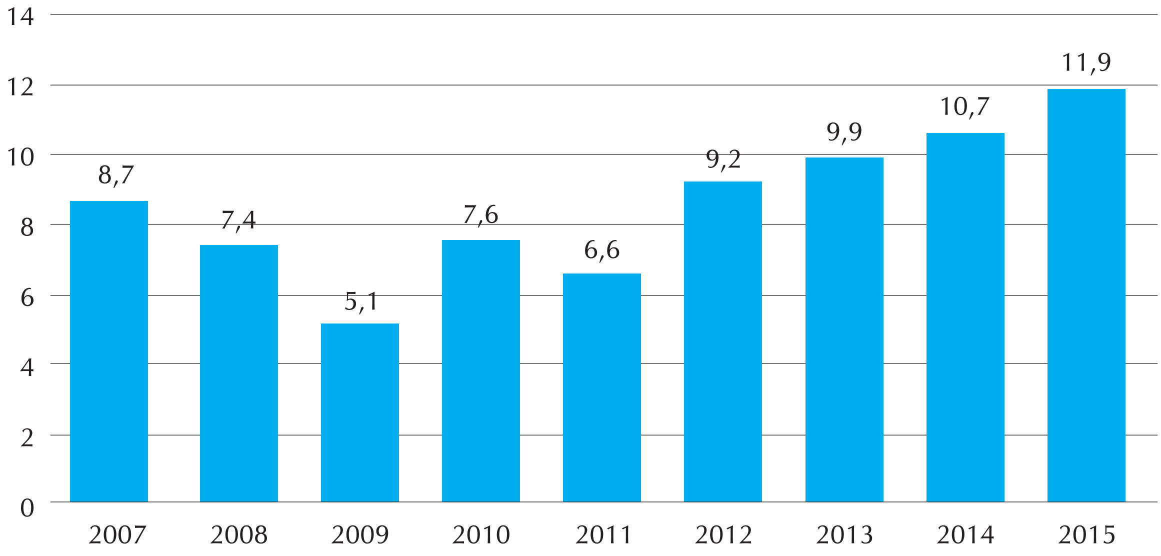
Table 5. Italy's top trade partners in 2015

Country	Position in exports	Exports volume (€ billion)		Country	Position in imports	Imports volume (€ billion)
Germany	1	51.0		Germany	1	56.8
France	2	42.5		France	2	32.1
U.S.	3	36.0		China	3	28.2
United Kingdom	4	22.5		Netherlands	4	20.7
Spain	5	19.9		Spain	5	18.4
Switzerland	6	19.2		Belgium	6	17.2
Belgium	7	14.6		Russia	7	14.3
Poland	8	10.9		U.S.	8	14.2
China	9	10.4		Switzerland	9	10.8
Turkey	10	10.0		United Kingdom	10	10.6

Source: Eurostat.

[148] R. Alcaro, "Italy and the renegotiation of the UK's EU membership," *IAI Working Papers*, November 2015.
[149] Authors' compilation based on the European Commission report, "EU Budget 2014, Financial Report."
[150] P. Wintour, R. Syal, "Brexit would damage EU and UK 'politically and economically'," The Guardian, 6 March 2016, www.theguardian.com/politics/2016/mar/06/brexit-damage-eu-uk-politically-economically-italian-minister-padoan.

Figure 5. Italy's trade surplus with the UK in 2007–2015, € billions



Source: Eurostat.

5.1.2. Capital Links

Doing business in the United Kingdom aids Italy in its cooperation with non-European partners and explains why the UK is the fourth-largest destination for Italian investment expansion (€23 billion, or 6% of Italy's total outward FDI stock, in 2014). The Italian Chamber of Commerce and Industry for the UK registered 695 Italian entities running investment projects in the United Kingdom.[151]

The largest presence of Italian capital in the UK is in the engineering sector, especially in renewable energy, (TerniEnergia, Falck Renewables, Conergy Group, Gala), aviation (Finmeccanica), automotive industry (Fiat Chrysler Automobiles UK) and digital technology (Aruba).[152] One major Italian investor in the United Kingdom is Investindustrial, whose shareholdings in the motor industry include a 37% stake in Aston Martin, which it acquired for £150 million.[153] On the other hand, Italian banks are almost absent from the British market (except for the minor presence of Intesa Sanpaolo and UniCredit).

UK investments in Italy are quite considerable: at €32 billion they represented some 9% of all British outward FDI in 2014. Some 26% of British capital in Italy was invested in industry and 56% in services (including 10% in financial services). The UK banking sector's presence in Italy is moderate compared to other EU Member States and is estimated at some 10% of Italy's GDP.[154]

[151] "Survey of Italian Investments in the UK: A Sector Analysis 14," The Italian Chamber of Commerce and Industry for the UK, 2014 www.italchamind.eu/ICC_Survey_eBook/index.html#p=1.

[152] *Ibidem.*

[153] *Ibidem*, p. 50.

[154] To compare, British capital in the banking sector in Germany amounts to 19% of GDP while in France it is 25% of GDP. Global Counsel, *op. cit.*

5.1.3. Migration

UK-Italy migration links are fairly moderate (see Table 2), but the recent period saw an increase in economic migration to the United Kingdom, especially of young Italians entering the labour market.[155] Persistent high unemployment among young people[156] has been the main driver of migration to the UK, especially after Italy was forced to pursue austerity. This translated into a worsening of domestic labour market conditions—which include growing market segmentation, i.e., a split into trade union-protected, well-paid stable jobs in large companies and unstable, lower-paid positions at smaller firms (with diminishing chances for moving from the "worse" labour market segment to the "better" one). Many young people are also drawn to the UK by the promising career prospects offered by British universities as well as their prestige, resulting in a total of 13,700 Italians studying in the United Kingdom. Overall, some 152,000 Italian citizens were in the UK in 2015, representing around 10% of all Italians staying in the EU.[157]

The number of Britons staying in Italy approached 65,000 in 2015,[158] or some 6% of all British migrants in the EU. Italy's moderate popularity reflects the protracted procedures involved in obtaining permanent stay permits—with the resulting temporary limitations in access to public services, including healthcare[159]—and also higher costs of living compared to, for example, Spain and Portugal.

5.2. Economic Policy Preferences

5.2.1. Regulatory Policy

In the aftermath of the financial crisis, the Matteo Renzi government embarked on gradually changing the country's economic profile and increasing its competitive edge through such measures as restricting the influence of trade unions and adopting a reform package to reduce administrative burdens.[160] Consequently, Italy also has moved in a pro-market direction in its EU-oriented policy , where it supports deregulation in some areas of the single market, [161] a goal sought by the United Kingdom.[162] Thus, the countries' foreign ministers have jointly expressed support for increased competitiveness in the EU and for it to be achieved by fully exploiting the potential of the single market in services and digital goods.[163] Another shared goal is creating a capital markets union, which would facilitate access to financing for Italian small businesses.[164]

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[155] N. Squires, "Young Italians abandon la dolce vita to move to Britain," *The Telegraph*, 8 October 2014; J. McKenna, "Italians help fuel surge in UK immigration," *Thelocal.it*, 27 August 2015, www.thelocal.it/20150827/italians-help-fuel-surge-in-uk-immigration.

[156] The overall unemployment rates in the United Kingdom and in Italy in 2015 were 5.4%, and 12.4%, respectively; youth unemployment was 14.6% and 40.3%, respectively.

[157] "Trends in International Migrant Stock: Migrant by Destination and Origin (data base POP/DB/MIG/Stock/Rev.2015)," United Nations Department of Economic and Social Affairs, Population Division, December 2015.

[158] *Ibidem*.

[159] "British expats fall victim to NHS clampdown," *TheLocal.es*, 17 April 2015 (updated 21 April 2015), www.thelocal.es/20150417/british-expats-fall-victim-to-nhs-clampdown.

[160] A. Mingardi, "Renzi's Messy Metamorphosis," *Politico*, 16 February 2016, www.politico.eu/article/matteo-renzi-messy-metamorphosis-italy; M. Fana, D. Guarascio, V. Cirillo, "Labour Market Reforms in Italy: Evaluating the Effects of the Jobs Act," *ISIGrowth Working Paper*, December 2015.

[161] "A Shared European Policy Strategy for Growth, Jobs, and Stability," Ministero dell'Economia e delle Finance, February 2016.

[162] Scaling down regulatory burdens on business was one of Cameron's four main demands in negotiations on EU reform.

[163] Ph. Hammond, P. Gentiloni, "Britain and Italy stand together on EU reform," *The Telegraph*, 14 December 2015.

[164] R. Alcaro, "Italy and the renegotiation of the UK's EU membership," *IAI Working Papers*, November 2015.

But these changes have yet to reach critical mass. Italy is still closer to the statist model, with far-reaching market regulation and bureaucratic control. According to the Heritage Foundation, Italy ranked only 86th in the world in terms of economic freedom in 2015.

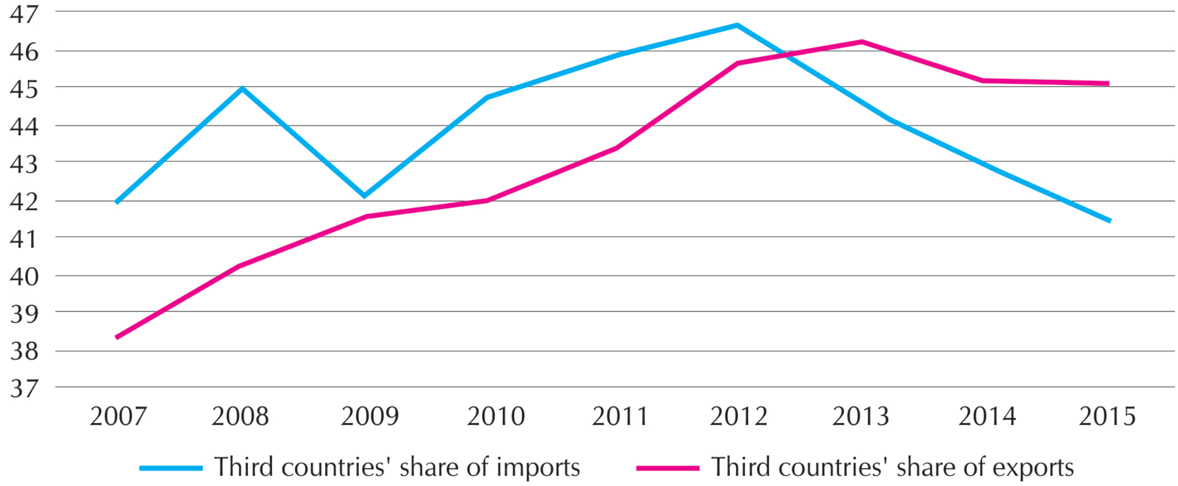
5.2.2. International Trade

Markets outside the EU are important for Italy, with their share of the country's total merchandise sales to third countries exceeding 45% at present, after rising by some 5 p.p. over 2008–2015. On the other hand, imports from non-EU markets have been on the decline since 2012, and their share in 2015 was 41.5%.

Italy sets much store in EU trade policy and, especially, the TTIP negotiations. The United States—the third-largest export market for the country and 8th on the list of imports—is described as the most important strategic partner in Italy's export promotion plan.[165] The country's positive approach to trade liberalisation was seen during the economic crisis when it introduced a similar number of market protection measures (31) as the United Kingdom (30) and lower than Germany (43),[166] thus demonstrating a position on international trade that is close to the British approach.

But Italy is not above supporting protectionist methods in selected trade areas where it suits its interests. This was reflected in the demands posed by previous governments with respect to competition rules on international trade,[167] demonstrating that Italy is ready to influence EU policy towards restricting imports that the country sees as infringing competition.

Figure 6. Third countries' shares of trade with Italy, 2007–2015, in %



Source: Authors' compilation based on Eurostat data.

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[165] "Piano per la promozione straordinaria dell'export," Ministero dello Sviluppo Economico, March 2015, www.sviluppoeconomico.gov.it/images/stories/commercio_internazionale/piano_straordinario_made_italy/piano_promozione_straordinaria.pdf.

[166] S. Durusoy, E. Sica, Z. Beyhan, "Economic Crisis and Protectionism Policies: The Case of the EU Countries," *International Journal of Humanities and Social Science*, vol. 5, no. 6 (1), 2015.

[167] "EU Future Trade Policy, Position Paper by the Italian Government," September 2010, http://trade.ec.europa.eu/doclib/docs/2010/september/tradoc_146648.pdf.

5.2.3. Redistribution in the EU

Italy differs from the UK in its attitude to the EU budget. Even though both countries were net payers during the 2012-1013 negotiations on the next financial framework, Italian support for cuts in spending was not as firm as the United Kingdom's. Italy also gives backing to strong cohesion policy—involving redistributive mechanisms almost by definition—which comes as a result of huge development disparities among Italian regions (in some of the southern ones, e.g., Calabria, per-capita GDP does not exceed 60% of the EU average). For this reason, despite being a net payer, Italy has sympathised with the Friends of Cohesion group, which gathers Member States with poorly developed regions that are net beneficiaries from the EU budget.[168]

Given the weight of agriculture in the country's southern regions, Italy supports a strong Common Agricultural Policy. In 2012, jointly with France and Spain, it endorsed a position calling for maintaining the level of the EU's CAP expenditure, but with greater flexibility in spending and a slower pace of convergence between the Member States in direct payments to farmers.[169]

Apart from the EU budget, the redistributive element is also important for Italy with respect to eurozone integration. According to Rome, the monetary union should draw on the so-called "fiscal capacity" designed to stimulate new investment in stagnated Member State economies and provide a kind of insurance against the risk of country-specific, or asymmetric, economic shocks. There are two reasons for this position. First, it is in line with the Italian vision of European integration. Second, the growing economic problems, including high levels of public debt and youth unemployment, prod the country to seek relieving national budget problems through EU-level arrangements.

National interest also underpins the Renzi government's promotion of redistributive mechanisms in sector-specific policies. For example, with its banking sector facing the threat of insolvency, Italy calls for a speedier formation of the common deposit guarantee fund and an institution to assume financial institutions' bad debts. The latter idea, however, has met with opposition from other Member States. Similarly, with its domestic labour market in dire straits (high youth unemployment), Italy seeks common eurozone-level unemployment insurance and a fund to counter joblessness.[170]

5.3. Approach to Political Integration

Italy has traditionally favoured a deepening of political integration within the EU. This hardly comes as a surprise: the idea of a federalist Union was shared by the Italian founding fathers of the European Community and was reflected in the 1980s "Spinelli plan." Being in the vanguard of integration, Italians have also shown a relative openness towards transferring national competences to the EU level and strengthening supranational institutions.

Italy's support for a stronger Union is expressed in a number of ways. In economy and finance, the Italian government calls for deep reform of the eurozone towards a fiscal and banking

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[168] M. Kölling, C. Serrano, "The Negotiation of the Multiannual Financial Framework: Budgeting Europe 2020 or Business as Usual?," Real Instituto Elcano, 19 October 2012, http://www.realinstitutoelcano.org/wps/portal/web/rielcano_en/contenido?WCM_GLOBAL_CONTEXT=/elcano/elcano_in/zonas_in/europe/ari68-2012_mff_negotiation_europe2020.

[169] "Italy, France and Spain join forces on the CAP," ARC2020, 23 October 2012, www.arc2020.eu/2012/10/italy-france-and-spain-join-forces-on-the-eu-agricultural-budget.

[170] *Ibidem*; "A Shared European Policy...," *op. cit.*

union and for the creation of a eurozone parliament[171] and finance ministry.[172] Italy also supports the idea that a portion of taxation should fall under EU competence or be further harmonised. This was reflected in the country's attitude towards the proposal for an EU financial transactions tax, which was promoted by the then-Italian Prime Minister Mario Monti, who argued—jointly with Chancellor Merkel[173]—that it should cover the whole EU, including Member States outside the eurozone.[174] Italy also sees further harmonisation of other taxes (VAT, CIT) as a necessary prerequisite for a capital markets union.

In other areas, the list of priorities is topped by reform of EU policy on migration and asylum, where Italy also backs supranational solutions achieved by the Community method. The country proposes the establishment of European Border and Cost Guards and an EU system of refugee allocation, both of which could be co-financed by EU bond issues (Euro-obligations).[175] Faced with opposition from some Member States to such arrangements, Italy is showing interest in differentiated integration through which it could engage with a limited group of Member States towards resolving EU problems within the framework of enhanced cooperation. Italian Foreign Minister Paolo Gentiloni spoke in this vein at a February 2016 special meeting of Ministers of Foreign Affairs of the EU founding Member States.[176]

But Italy's pro-integration profile is superposed by its immediate interests necessitated by its tough economic situation, which in the short term may impact the country's attitude towards political integration. This is, for example, the case with the European Semester, where the Renzi government favours the relaxation of fiscal policy coordination, thus running into conflict with the European Commission and Germany.[177] In this case, paradoxically, support for Italy in its disputes with EU institutions may come from the United Kingdom, an advocate of greater flexibility in the way the EU tackles economic problems.[178]

Yet, despite this occasional convergence of views, the European visions of Italy and the United Kingdom bear more differences than similarities. Consequently, there are more reasons to expect Italy to press against the United Kingdom's continued influence on the direction of EU political integration.

5.4. Preferred model of the EU-UK relationship after Brexit

Given Italy's fairly strong economic ties with the United Kingdom, it will likely opt for a relationship model guaranteeing the United Kingdom a strong foothold in the single market, and especially benefits from capital movements. But Italy will oppose granting the United Kingdom a right to influence the economic policy and direction of integration in the EU. This translates into a preference for the model of the European Economic Area, in which the United Kingdom would

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[171] J. Politi, "Italy's Pier Carlo Padoan calls for 'political union', to save euro," *Financial Times*, 26 July 2015, www.ft.com/intl/cms/s/0/2c57fb62-3205-11e5-8873-775ba7c2ea3d.html#axzz46HexDeRW.

[172] P. Wintour, R. Syal, *op. cit.*

[173] While the Renzi government is in more conflict with Germany compared to previous governments, it still takes a pro-integration stance (e.g., by backing the completion of the capital markets union and strengthening eurozone economic governance), which is close to the French position.

[174] V. Pop, "Monti and Merkel: Financial tax must cover whole EU," *EUObserver*, 12 January 2012, https://euobserver.com/economic/114847.

[175] "A Shared European Policy...," *op. cit.*

[176] T. Palmeri, "Ministers of core Europe plan EU's future," *Politico*, 8 February 2016, www.politico.eu/article/ministers-core-europe-plan-eu-future-rome-meeting-founding-members-integration.

[177] B. Romano, "After Juncker rebuke, sharp tensions with EU burst out in the open," *ItalyEurope24*, 16 January 2016, www.italy24.ilsole24ore.com/art/public-finance/2016-01-15/renzi-juncker-183735.php?uuid=ACrbY2AC.

[178] Ph. Hammond, P. Gentiloni, *op. cit.*

be a fully-fledged member of the single market, respecting the freedom of movement of people and contributing to the EU budget but without a say in EU regulatory policies.

Italy's preferences about political integration are also likely to lead the country to be prone to limit the United Kingdom's influence on EU decision-making. This largely reflects the pro-integration approach embraced by Italy, which may only strengthen if a proposal is made for differentiated integration. This pro-integration approach may trump Italy's perception of the United Kingdom as an important partner in balancing the political weight of the Germany-French tandem, which could be seen in Italian policy so far.

6. Poland

The United Kingdom has always been counted among Poland's important political allies in the EU. It was one of the most vocal advocates of the EU's eastern enlargement[179] and the first Member State to open its labour market to citizens of the 2004 new entrants. In addition to that, following the 2015 parliamentary election in Poland, both governments share a cautious approach to deeper political integration of the European Union, thus counterbalancing the vision of Germany and France. Polish Minister of Foreign Affairs Witold Waszczykowski, in his inaugural address on 26 January 2016, put the United Kingdom in first place among Poland's major European partners with a shared perception of European issues. The political cooperation of the two Member States is also facilitated by the circumstance that their ruling parties are members of the same political group in the European Parliament—European Conservatives and Reformists.

The United Kingdom's presence in the EU is also important for Poland in view of their similar positions on eastern policy and particularly towards the Russia-Ukraine conflict. Both the UK and Poland oppose normalising relations with Moscow until the Russian government meets all peace agreement commitments and withdraws from Ukraine. Poland, therefore, fears that Brexit might weaken EU determination to keep the sanctions on Russia.

Poland also benefits economically from the United Kingdom's presence in the EU, running a trade surplus with that country, which is also one of the main destinations for Polish migration. And finally, in the financial dimension, Poland is the largest beneficiary of transfers from the EU budget, where the United Kingdom is among the top net payers.

6.1. Economic ties

6.1.1. Trade in Goods and Services

The United Kingdom is the second-largest export market for Polish goods, absorbing 6.8% of total Polish sales in 2015 and worth €12.1 billion. The biggest product groups in Polish exports are cars, car parts and equipment, as well as consumer durables. Imports from the UK amounted to €5.1 billion (2.7% of Poland's total imports), with motor industry products and pharmaceuticals leading the list of top product groups.

Table 5. Poland's top trade partners in 2015

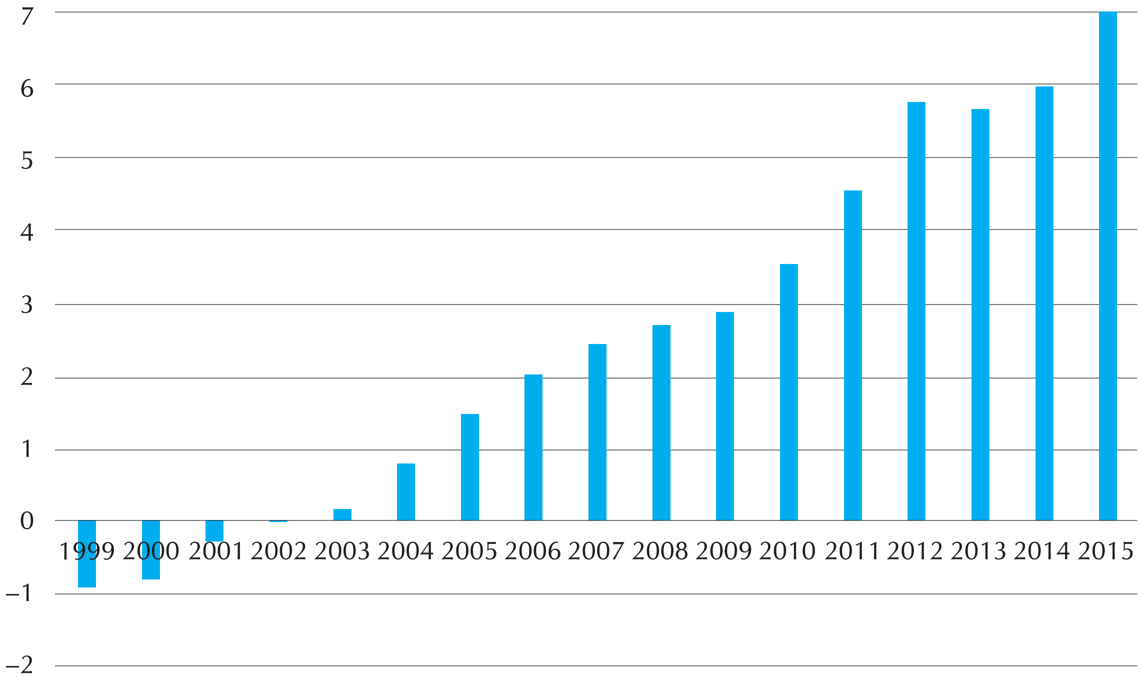
Country	Position in exports	Exports volume (€ billions)		Country	Position in imports	Imports volume (€ billions)
Germany	1	48.5		Germany	1	48.4
United Kingdom	2	12.1		China	2	13.1
Czech Republic	3	11.8		Russia	3	12.6
France	4	9.9		Netherlands	4	10.2
Italy	5	8.5		Italy	5	9.1
Netherlands	6	7.9		France	6	7.2
Russia	7	5.1		Czech Republic	7	6.8
Sweden	8	4.9		Belgium	8	5.8
Hungary	9	4.7		United Kingdom	9	5.1
Spain	10	4.7		Slovakia	10	4.6

Source: Eurostat.

[179] Paradoxically, the UK negotiated a rebate in its EU budget contribution to structural policy concerning new Member States.

Poland's trade surplus in goods with the United Kingdom is at €7 billion and has been steadily on the rise, which is important for a country that runs a trade deficit with the rest of the world.[180]

Figure 7. Trade surplus in goods with the United Kingdom, 1999–2015, € billions



Source: Eurostat.

The United Kingdom's importance as a trading partner for Poland is not confined to trade in goods. In trade in services, according to OECD data for 2014, the UK accounted for 6.5% of total Polish foreign sales and 7.8% of imports to Poland, that is, €2.3 billion and €2.15 billion, respectively, resulting in a small surplus of €190 million in that year. Since 2010, the balance of Polish-British trade in services oscillated around zero, and in 2012, a small deficit was registered.

6.1.2. Capital Links

In relations with the United Kingdom, Poland registers a net inflow of foreign direct investment. According to data for 2014 released by the National Bank of Poland (NBP), British FDI to Poland stood at €5.9 billion, putting the United Kingdom in 10th place on the list of the largest investors in Poland.[181] Poland's FDI position in terms of the United Kingdom amounted to a mere €807 million, which nevertheless represented 10.1% of overall Polish outbound FDI.

Polish investors' relatively high interest in the United Kingdom (compared to their interest in other countries) reflects the British business-friendly regulatory environment and wide access to non-European markets, facilitating cooperation with partners from outside the EU. An equally important consideration was the early opening of the British labour market, translating into increased demand for Polish goods and services. And third, companies investing in the United Kingdom

[180] Poland's overall trade surplus in 2015 amounted to around €3.5 billion, which is less than the trade surplus registered for that year with the United Kingdom.

[181] The figures may be affected by problems with properly establishing the origin of capital flowing through markets such as Cyprus and Luxembourg. In actual fact, the position occupied by the United Kingdom might turn out to be higher.

gain the opportunity to effectively build their brand image as a global enterprise. Investments in the UK were made by companies such as Integer (expanding its network of self-service parcel pick-up machines), Inglot, Fakro, Nowy Styl group, and also Can-Pack, REC Global, Comarch, Black Red White, Forte and Amika.[182] According to the British Polish Chamber of Commerce, over 40,000 Polish companies have been in operation in the United Kingdom since 2007.[183]

6.1.3. Migration

Poles are the largest group of migrants from EU Member States in the United Kingdom. According to United Nations statistics for 2015, there were some 703,000 Polish immigrants in the UK, accounting for nearly 2% of Poland's population.[184] They were pulled in by the high wages and relatively low unemployment on the British labour market, the low language barrier, and the early opening of labour-market access, which translated into the emergence of strong Polish-community structures.

Polish economic migration to the EU has pushed up the level of private remittances to Poland, which in 2013 were estimated at €902 million.[185] The United Kingdom is the second largest source (after Germany) of such remittances, accounting for 22% of all immigrant transfers received by Poland. A post-Brexit closure of borders and possible introduction of visa requirements could result in the return of some Polish emigrants, which might increase unemployment in the country and pressure on the national budget.[186]

Another increasing group of Poles in the UK are university students, largely motivated to go there by the quality of UK institutions of higher education and the associated opportunities for attractive employment.[187] OECD estimates the number of Polish students enrolled in UK universities in 2013 at 5,232.[188]

6.2. Economic Policy Preferences

6.2.1. Regulatory Policy

The Polish and British positions on EU economic policy are similar, with both parties perceiving the fairly deregulated single market as the EU's greatest quality. The Polish government

[182] D. Kazimierczak, "Kto i gdzie inwestuje," *Portal Promocji Eksportu*, 17 June 2015, https://uk.trade.gov.pl/pl/inwestycje/1667,kto-i-gdzie-inwestuje.html.

[183] "After 20 years of growth, Polish firms need the UK to go global," *Contact Online*, 2012, no. 6 (101), British Polish Chamber of Commerce, http://contact.bpcc.org.pl/issue06/articles/after-20-years-of-growth-polish-firms-need-the-uk-to-go-global.

[184] UN data on migration: www.un.org/en/development/desa/population/migration/data/estimates2/estimates15.shtml. It should be noted that, according to the British Office for National Statistics, in 2014 there were 853,000 Polish migrants in the UK. Nevertheless, for the purpose of data source consistency for all of the B5 countries, this report uses United Nations migration data as a point of reference.

[185] I. Chmielewska, "Transfery z tytułu pracy Polaków za granicą w świetle badań Narodowego Banku Polskiego," Narodowy Bank Polski, Warsaw, 2015.

[186] The return of Polish emigrants may also produce positive effects by helping to meet the growing domestic demand for labour (see, for example: K. Borońska-Hryniewiecka, "The Impact of Brexit on Economic Migrants in the UK: Implications for Poland and Its Citizens," *PISM Bulletin*, no. 24 (874), 23 March 2016, www.pism.pl/publications/bulletin/no-24-874.

[187] B. Sendrowicz, "Czy polscy studenci wrócą z Anglii do kraju?," *Gazeta Wyborcza*, 26 February 2015, http://wyborcza.biz/biznes/1,147753,17485148,Czy_polscy_studenci_wroca_z_Anglii_do_kraju_.html.

[188] "Enrolment of international students by origin," OECD database, https://stats.oecd.org/Index.aspx?DataSetCode=RFOREIGN#.

has often stressed the important role that the EU's internal market plays in the country's economic development and has sought to strengthen it, for example, by supporting the services directive, which provoked opposition from Member States advocating more regulation.[189]

The UK and Poland also converge in their support for flexible labour market policy.[190] Although after 2015 some measures were introduced in Poland to make the market more rigid (imposing a minimum pay rate, requiring national insurance payments under flexible contracts), the dominant trend in the period following the economic crisis has been one of continued labour-market deregulation, as reflected in three packages to deregulate professions,[191] and an additional injection of labour-market flexibility under the anti-crisis act.[192]

A further strengthening of the remaining three freedoms (capital, goods, services) is an important element of European economic policy for both Poland and the United Kingdom. For example, the Polish government points to the growth potential in services in the single market,[193] which is also of importance to the United Kingdom where services make up 80% of exports. Poland has a similar interest as the United Kingdom in creating a European digital single market, which was reflected in the signing along with other states of a joint letter to the European Commission calling for only minimal EU-wide regulation of digital platforms.[194] On the formation of a capital markets union, Poland largely takes a positive view of the deepening of financial market regulation—even despite reservations about a possible outflow of capital from the Warsaw Stock Exchange. This community of interests within the single market dimension may prod Poland to back models of the possible next EU-UK relationship in which the UK would retain its influence on single market regulations.

6.2.2. International Trade

The weight of non-EU markets in Polish trade is not as high as that of other EU states. In 2015, only 20% of Polish goods exports, worth € 37 billion, went to third countries. Those countries' share of imports to Poland was higher, standing at some 30% (€51.8 billion). The biggest non-EU trading partners are China and Russia, which supply Poland with electrical machinery and raw materials. The Polish government has plans to increase cooperation with non-European countries[195] and, consequently, it supports the TTIP agreement negotiated by the European Commission.[196] While the United States is not among Poland's top trading partners, the government position reflects the foreign policy importance of transatlantic relations in all their dimensions, including areas such as security and investment inflows from the U.S. (the fifth-

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[189] "Polskie 10 lat w Unii. Raport," Ministerstwo Spraw Zagranicznych, Warsaw, 2014, pp. 14, 15, 17, 45, and 46.

[190] OECD puts the index of employment protection in Poland at 2.23, which means that the Polish market is among the most flexible among the OECD's members. See: "Strictness of Employment Protection—individual and collective dismissals," OECD database; "2016 Index of Economic Freedom," Heritage Foundation, www.heritage.org/index/explore.

[191] "Act of 13 June 2013 amending legislation regulating the practice of certain professions"; "Act of 9 May 2014 facilitating access to the practice of certain regulated professions," Ministry of Justice, www.ms.gov.pl/pl/deregulacja-dostepu-do-zawodow.

[192] "Act easing the consequences of the economic crisis on employees and companies," *Dziennik Ustaw*, 2009, No 125, item 1035.

[193] "Inaugural address by Minister of Foreign Affairs Witold Waszczykowski," in: *Sprawozdanie Stenograficzne z 10. posiedzenia Sejmu Rzeczypospolitej Polskiej w dniu 29 stycznia 2016 r. (drugi dzień obrad)*, Warsaw, 2016, http://orka2.sejm.gov.pl/StenoInter8.nsf/0/6A4CD2F71231A36FC1257F4D003FECA4/$File/10_b_ksiazka_bis.pdf.

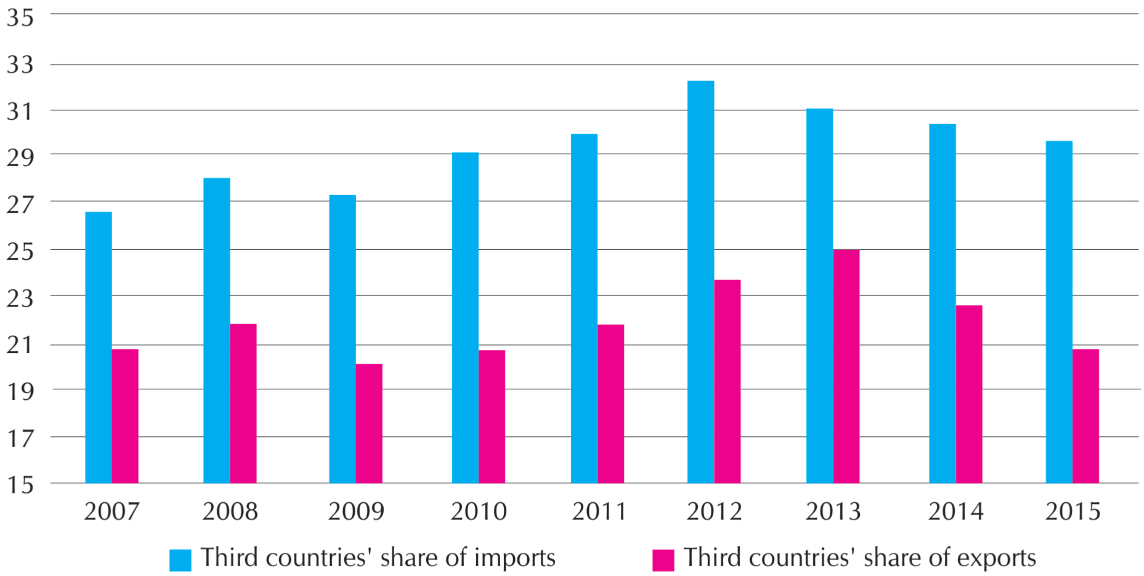
[194] "Joint Letter from the United Kingdom, the Czech Republic, Poland, Luxembourg, Finland, Sweden, Denmark, Estonia, Latvia, Lithuania and Bulgaria," Brussels, 4 April 2016.

[195] "Inaugural address by Minister of Foreign Affairs Witold Waszczykowski," *op. cit*.

[196] P. Sikora, K. Gałkowski, "The Polish Government's Standpoint on ISDS Inclusion in the Scope of TTIP," 2015, https://efilablog.org/2015/10/20/the-polish-governments-standpoint-on-isds-inclusion-in-the-scope-of-ttip.

largest investor in Poland).[197] Similarly, Poland has supported a lowering of non-tariff barriers in trade with Canada and an accelerated conclusion of negotiations on the EU's agreement with that country.[198]

Figure 8. Third countries' share of trade with Poland, 2007–2015, in %



Source: Eurostat.

6.2.3. Redistribution in the EU

Poland and the United Kingdom differ most in their attitudes to financial transfers in the EU. While the UK has pressed for the maximum possible reduction of the EU budget (and for keeping the British rebate), the Polish position is at the other end of the spectrum, seeking a common budget that is as large as possible and with no concessions for any Member State. The two countries also differ in their respective approaches to the EU budget's major items. For example, the Polish government is a supporter of a comprehensive cohesion policy. On the other hand, the United Kingdom argues that this policy, distorting market allocation, is costly and unnecessary, and that, consequently, it should be confined to the EU's lowest-income regions. On the agricultural market and CAP, the UK criticises the manner and level of financing, whereas Poland approves of this policy's shape and budget, notwithstanding the reservations it has about the pace at which direct payments to Polish farmers are converging to those in the "old" Europe. But it should be emphasised that the approaches to these policies are strictly determined by profit-and-loss considerations: cohesion policy and CAP involve huge transfers to Poland (e.g., a total of €17 billion in 2014), and negligible transfers to the United Kingdom.

Differences in approaches towards redistribution can also be seen in the British proposals to lower social benefits for EU immigrants, including in-work benefits and money paid for immigrant children living outside the UK.[199] Due to the large presence of Polish immigrants in the United

[197] E. Kaliszuk, "Transatlantic Trade and Investment Partnership: Polish Perspective," *The Journal of International Relations*, vol. 39, no. 1, 2015.

[198] "Poland-Canada consultations on CETA," Ministerstwo Spraw Zagranicznych, December 2015, www.msz.gov.pl/en/p/msz_en/news/poland_canada_consultations_on_ceta.

[199] "Brytyjski premier w Warszawie. Trwa spotkanie z premier Beatą Szydło," *PAP/IAR*, 5 February 2016, www.polskieradio.pl/5/3/Artykul/1578668,Brytyjski-premier-w-Warszawie-Trwa-spotkanie-z-premier-Beata-Szydlo.

Kingdom, the Polish government found these proposals hard to accept during negotiations on the new settlement for the United Kingdom in the EU.[200]

6.3. Approach to Political Integration

By sharing with the United Kingdom a similar vision of European integration and, consequently, similar interests within the Union, Poland would find itself at a political disadvantage in case of Brexit. The similarities between the countries' positions can be observed in several dimensions.

To begin with, over the last several years, Poland has become increasingly disillusioned with community institutions and has moved in favour of the British-preferred intergovernmentalism approach to EU decision-making. As a new Member State, Poland has been a supporter of the community method, where the Commission and European Parliament played the role of honest-brokers. Gradually however its position has been evolving due to certain disappointment with, *inter alia*, the supranational institutions' weakness in upholding the inclusive method of tackling the financial and the eurozone crises,[201] all the way to a perceptibly diminished trust in the EU's executive branch after the 2015 Polish parliamentary election.

The reason why the new Polish government favours the intergovernmental approach[202]—even though it holds the threat of marginalisation for Poland as a medium-sized Member State—is what it sees as an increasing exploitation of EU institutions by the biggest states for the pursuit of their own policy goals.[203] There have also been growing differences of opinion with the EC on key issues, such as the migrant crisis and EU asylum policy reform. Additionally, Poles are still poorly represented among the top administrative positions in EU institutions, especially the Commission, which translates into Poland's weak influence at the policy-development phase where the community method is applied.[204]

Next to promoting increased "national autonomy" in relations with Brussels institutions, both Poland and the United Kingdom are vocal about strengthening the democratic legitimacy of the EU's decision-making process by respecting the subsidiarity principle and reinforcing the role of national parliaments.[205]

As countries remaining outside of the monetary union,[206] Poland and the United Kingdom also share common interests in ensuring the open and inclusive character of eurozone governance based on close coordination with Member States that do not belong to the euro area. Consequently, during the renegotiations of terms of British membership of the EU, Poland backed the UK's demand for an additional consultation mechanism to protect non-eurozone members' interests in

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[200] K. Borońska-Hryniewiecka, "A Win-Win Situation? What to Make of the EU-UK Deal," PISM Strategic File, no. 3 (84), February 2016, www.pism.pl/Publikacje/PISM-Strategic-Files/PISM-Strategic-File-no-3-84.

[201] Poland then backed Commission President José Manuel Barroso and opposed French and German attempts to strengthen the inter-governmental method (e.g., by creating frameworks to counter the eurozone crisis such as the Euro Plus pact); "Poland supports Barroso's fight for 'Community method," *EurActiv*, 14 February 2011, www.euractiv.com/section/med-south/news/poland-supports-barroso-s-fight-for-community-method.

[202] "Inaugural address by Minister of Foreign Affairs Witold Waszczykowski," *op. cit*.

[203] P. Musiałek, "Małżeństwo z rozsądku. Unia Europejska według Jarosława Kaczyńskiego," Klub Jagielloński, 11 January 2016, http://jagiellonski24.pl/2016/01/11/malzenstwo-z-rozsadku-unia-europejska-wedlug-jaroslawa-kaczynskiego.

[204] "Mapa kierunków narodowych" (interview with Europe Minister Konrad Szymański), *Nasz Dziennik*, 17 December 2015.

[205] "Inaugural address by Minister of Foreign Affairs Witold Waszczykowski," *op. cit*.

[206] The United Kingdom has won a formal opt-out from eurozone membership, whereas Poland is treaty-bound to join the area under the terms of its accession to the EU.

eurozone economic decision-making.[207] Poland is also distancing itself, just as the United Kingdom is, from the idea of stronger economic governance at the EU level. For example, due to the specific features of its domestic banking sector (where only 34% of the assets are Polish-owned[208]), Poland has not joined the Banking Union in full,[209] nor did it give its backing to the idea of increased tax coordination (again, in line with the stance taken by the British). Consequently, Poland has remained outside the group of Member States launching a financial transactions tax under the enhanced-cooperation procedure.

Despite the two countries' similar views on regional security and similar proportions of budget spending going to defence[210], EU common security and defence policy is an area where the Polish and British approaches differ. The United Kingdom is invariably seeking to weaken this dimension of European integration, at the advantage of relying on NATO and inter-governmental cooperation ("coalitions of the willing"). Poland, on the other hand, has sought to strengthen the EU's defence policy since joining the bloc. In 2011, the Tusk government made it one of the priorities for the Polish EU presidency.[211] The UK was, at that time, the chief opponent of the Polish aims for strengthening the EU's capabilities to run military operations on its own and with a dedicated command structure. The Beata Szydło government will likely support further strengthening of the EU's defence dimension.[212]

6.4. Preferred Model of the EU-UK Relationship after Brexit

From the Polish point of view, the strong trade connections with the UK, complemented by the large number of Polish immigrants in that country, provide arguments for maintaining close economic ties within the framework of the single-market and ensuring the free movement of people. Any other, less-advanced form of economic integration will be harmful to Polish economic interests.

While the Polish and British positions differ significantly on EU redistribution, in the overall economic policy spectrum, a community of interests prevails. This can be seen particularly in both countries' views on the functioning of the single-market, approach to deregulation, and international trade. In the event of Brexit, this could translate into Polish support for a model of an EU-UK relationship in which the United Kingdom contributes to the decision-making process concerning the EU's internal market.

Both the Polish and the British governments distance themselves from deepening EU political integration and especially from the idea of establishing a political union. But Poland, as is the UK, is in favour of deepening sector-specific integration within the single-market and, therefore, can be expected to support an EU-UK relationship model that leaves a certain, at least consultative, British influence on the political process within the EU. Given the similarities in both countries' positions towards Russia, such influence would be particularly desirable from the standpoint of Poland's foreign policy by providing a counterbalance to the more conservative-minded EU core countries (Germany, France, Italy).

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[207] K. Borońska-Hryniewiecka, "A Win-Win Situation?...," *op. cit.*

[208] P. Hüttl, D. Schoenmaker, "Should the 'outs' join the Banking Union?," *Bruegel Policy Contribution*, February 2016.

[209] Poland signed the inter-institutional agreement on the single resolution mechanism but has yet to ratify it. The United Kingdom did not sign the document.

[210] Poland and the United Kingdom are among the small group of EU Member States that meet the minimum goal of 2% of the national budget going to defence spending.

[211] K. Miszczak, "Polska a wspólna polityka bezpieczeństwa i obrony Unii Europejskiej," in: M. Fiszer (ed.), *Dziesięć lat członkostwa Polski w Unii Europejskiej. Próba bilansu i nowe otwarcie*, ISP PAN, Warszawa 2015.

[212] "Inaugural address by Minister of Foreign Affairs Witold Waszczykowski," *op. cit.*; It should be emphasised, though, that the EU's current CSDP agenda does not provide for any ambitious, controversial political project, and that CSDP remains a marginalised instrument of security policy in Europe.

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