

What should EU do?

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One of the things I have noticed about Brexit is the extent to which it appears to have promoted introspection amongst the relevant parties. Here in the UK, this is manifested in domestic politics, with a furious to-and-fro between those who get labelled as “Brexiters” and those labelled “Remainers”.

In the EU (and, indeed, elsewhere in Europe), Brexit is mercifully a rather less divisive topic. “It is what it is”, so to speak. However, that does not preclude some strongly held opinions on the subject.

In both cases (the UK and the EU), there tends to be a focus on the short-term and a rather partial view of what the benefits or costs of any decision might be. In economic terms, this is rather like considering a partial equilibrium solution to a problem rather than considering it in its totality.

Something missing from both sides has been an appreciation of the issues and domestic challenges facing the other. In this blog, I’d like to try and redress this balance a tiny bit.

The broad thrust of the EU position is straightforward. In spite of the protestations of some, it is not the nefarious action of some actor with state-like ambitions. Instead, there are two or three key factors to consider.

Firstly, Brexit isn’t *that* important to the EU. As individuals, all of us have a tendency to consider ourselves the centre of the known universe. For better or for worse, we assume that others are looking at us. Yet in actuality, we are unimportant to them. When I’m out-and-about, very few will give me a second glance. Why should they? What practical relevance do I have to their lives? The same is true of Brexit.

The whole of Europe is dealing with a pathogen that has turned our world upside down. We are simultaneously desperately trying to salvage what economic activity we can, whilst mitigating job losses

and trying to avoid excess deaths. So far, we've done a fairly poor job compared to East Asia.

Then, we must consider the relevant actors. For those internal to the EU itself (whether employed by the EU or directly committed to its institutions), there are existential issues at play. Irrespective of reality, it must not be the case that the UK is seen to have got "a better deal" out of leaving the EU. Otherwise, what would be the incentive to maintain the organisation?

The other set of actors are the nation states that actually have decision-making power. For these, there are a host of competing issues at play. Naturally, domestic political interests are always at the fore – just as they are for the UK.

As such, there is pressure to obtain short-term advantage in various areas that can be trumpeted. Likewise, there is pressure to appease domestic interests – whether that is the French fishing industry, the automotive sector, Spanish views on Gibraltar or anyone else. The UK faces exactly the same set of pressures, although they operate differently in every locale.

However, I believe that the EU should look to take a longer term perspective. For the UK (including many in government), Brexit has become a totemic political issue. As a result, UK domestic discussion of any future relationship tends to descend into argument and the country is entirely focussed on the present negotiations.

So it falls to the EU to think strategically about the future and to do so in a cold, sober manner that avoids the emotions that have become bound up in the subject. The first challenge is something that has become obvious over the course of negotiations: the renewed growth of mercantilism.

Naturally, this has been clear on the British side (albeit wrapped up in a label of sovereignty). Ultimately, however, it is precisely this that underlies the problematic arguments around industrial subsidies, state aid and any "level playing field".

However, it is also quite obvious amongst many EU member states. We see this in the refusal to grant generous terms around cumulation

(particularly in the automotive sector). We see it in the bizarrely high tariffs applied to agricultural products. We also see it in the desire to use equivalence as a political tool (rather than a less opaque and more generous system).

This is not in the interests of the EU. Economic theory and most of the evidence we see is clear on this point: freer trade benefits *both* parties^[1]. This applies to *all* of the EU's trading relations, of course – the UK is one of many.

However, the UK is an unusually large and proximate partner. Moreover, as a member state, it has typically been more sceptical of mercantilist instincts than many other member states. The loss of that voice bodes ill for all of us.

So what should we do? Whilst the UK continues to eat itself alive engaged in bitter argument, the EU will need to think strategically (if not necessarily publically). Brexit will entail an economic hit to all of us. How can the EU create a structure that facilitates a closer economic relationship and mitigates that hit? If not now (due to political reasons) then at least there needs to be an understanding of how we get there. How can we best work towards eradicating the barriers that are currently being put in place in order to benefit all of us?

^[1] There are notable exceptions to this, but it is difficult to see how they apply in the context of the current negotiations. High tariffs on agricultural products are certainly a net negative and evidence suggests that insofar as service sector activity covered by passporting is concentrated, there are some benefits to efficiency. Again, we are all worse off if we lose this. As for automotive, it is hardly an infant industry and we are probably all better off maximising the efficiency of the European sector (minimising barriers).