

NEJISTOTA KOLEM BREXITU A ROSTOUCÍ FINANČNÍ NAPĚTÍ V OBCHODU EU

EFFECT OF BREXIT UNCERTAINTY AND INCREASING FINANCIAL TENSION IN THE EU TRADES

SNEZHANA BIZYUKOVA

Abstract

The referendum on the UK membership in the EU was held on June 23, 2016. Then on March 29, 2017 Britain officially notified Brussels of its withdrawal from the European Union. The key points of the negotiations concerning the withdrawal of Britain from the EU are related to Britain's conditions for access to the European single market. Since important issues are currently unresolved and the status of London as a financial center is disputable, the effect of uncertainty has occurred. This one of factors causes financial tensions in the global financial market, which includes the European financial market. The next important factor increasing tensions in the European financial market is the expected significant reduction of the EU budget.

Keywords

financial market, financial institutions, global investors, uncertainty effect, financial tension

JEL Classification G190

Introduction

The referendum on the UK membership in the EU was held on June 23, 2016. The next morning, it was announced that 52% of citizens voted for withdrawal from the EU. Then on March 29, 2017 Britain officially notified Brussels of its withdrawal from the European Union. According

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to the rules stipulated in the article 50 of the of the Treaty of Lisbon, the state willing to leave the EU is eligible to do so after the two years period as of the date the official notification was issued.¹ Thus, Britain is to leave the EU on March 29, 2019.

The key points of the negotiations concerning the withdrawal of Britain from the EU are related to Britain's conditions for access to the European single market that is the most important question for London as for the world's largest financial center. The main issues relate to the possibility of free access to the European capital market, ensuring the unimpeded movement of capital; liberalization of securities' transactions; the free opening of bank accounts in any EU country; the right of establishment of companies in different EU countries; providing of financial services in the euro and the national currencies of countries outside the euro area.

Since these important issues are currently unresolved and the status of London as a financial center is disputable, the effect of uncertainty has occurred. Therefore, global investors are to create the adaptation model of behavior under the new conditions. This factor causes financial tensions in the global financial market, which includes the European financial market.

The next important factor increasing tensions in the European financial market is the expected significant reduction of the EU budget, which means that financial institutions of the EU countries will incur additional costs, as well as it can provoke a struggle between the EU members for a seven-year expenditure plan.

The Brexit Uncertainty Effect

The term "uncertainty" on the level of relations between business entities, often means that they do not have a clear view and understandable expectations about the prospects of economic development. Hence the

¹ The official website of the European Parliament, Article 50 TEU: Withdrawal of a Member State from the EU

problem of creating of an adaptation model of behavior in the new conditions is arising.

The current events confirm that in the short term period in Britain is more exposed to significant destructive influence of the effects of Brexit's uncertainty on the state of the currency and financial market than in the EU. This is fortified by the sharp drop in the pound sterling rate in the first months after the referendum, not only in relation to the US dollar, but also to the euro. In anticipation of changes in the conditions of financial regulation in Britain, a number of financial companies and banks are now declaring about their relocation to the countries of continental Europe. Financiers also support the preservation of the country in the European bloc, having fears that London may lose the status of an international financial center. In the case of Brexit, global banks, such as HSBC, Citi and Deutsche Bank, are ready to transfer part of the operations and personnel from London to another locations in Europe and Asia.²

The implications of Brexit for global investors

The consequences of Brexit have already been felt by 71% of the 254 global investors polled by EY.³ Many of them recorded a decline in profits or a reduction of demand, many were forced to increase prices. 14% of the interviewed investors plan to transfer part of the business to another country during the next three years in case of exit of the UK from the European market. It is worth noting that the most preferred places in Europe are Germany (54%), the Netherlands (33%) and France (8%).⁴

² The Russian Information Agency Ria Novosti, the article "Price of Brexit: in Britain were calculated three scenarios in case of UK withdrawal from the EU" 22 June 2016

³ Ernst & Young, the report from the official website of Ernst & Young "Strong global investment appetite into Europe despite geopolitical instability London", 31 January 2017

⁴ Ernst & Young, the report from the official website of Ernst & Young "Strong global investment appetite into Europe despite geopolitical instability London", 31 January 2017

The most significant consequences of Brexit will have one of the largest investors in the economy of the UK and the EU - the United States. Many firms view the United Kingdom as a kind of a door that opens access to free trade with 28 EU countries. Brexit will jeopardize all these benefits and force the American business to seek for the center of European operations in another place of the continent.

A number of American corporations got involved in the fight to prevent the victory of the Brexit supporters. Among them, the British subsidiary of Ford, as well as the largest banks - Citigroup, Goldman Sachs, JP Morgan and Morgan Stanley. It is reported that each of them donated hundreds of thousands of dollars to support the campaign: «Britain Stronger in Europe». The results of the British American Business survey showed that 70% of its members are convinced: Brexit will damage their operations and future investments, writes The Washington Post.⁵

Strengthening Financial Tension: Reducing the EU Budget

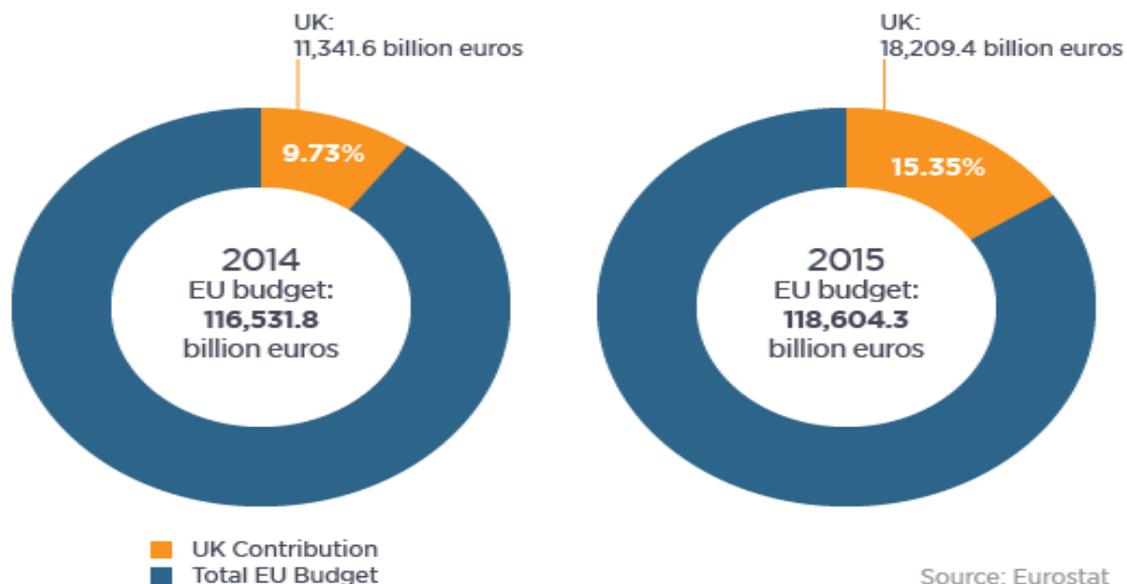
IMF scenarios that evaluate the impact of Brexit on the world economy forecast the increase of financial tensions in the world, first of all, in Europe and Great Britain, and a significant decline in investor and consumer confidence, especially in case of a unsystematic exit of Britain from the EU.⁶The result will be a weakening of economic growth rates, not only in the UK, but also in other countries EU.

Chart: UK contributions to EU budget

⁵ Ylan Q. Mui Article from the Washington post, “Brexit’ could send shock waves across U.S. and global economy”, 18 June 2016

⁶ The IMF official website, IMF Report “Cuts Global Growth Forecasts on Brexit, Warns of Risks to Outlook IMF News”, 19 July 2016

UK contributions to EU budget



Obviously that the financial institutions of the EU countries will incur additional costs for the formation of capital adequacy and maintenance of liquidity. After the UK will leave the EU, the EU budget will lose 15% of the money to subsidize countries that are their recipients.⁷ This can provoke a struggle between EU members over a seven-year expenditure plan from 2021, which will only increase financial tensions in the EU countries.

Conclusion

The current development of events confirms that in the short term period Britain will face a more significant destructive influence of the effects of Brexit's uncertainty on the state of the currency and financial market than in the EU. In anticipation of changes of the conditions of uncertainty in

⁷ ALICE FOSTER, The article from the U.K. newspaper Express "How important is Britain to the EU? What Brexit REALLY means for the EU budget?" 27 Mar 2017

Britain, a number of financial companies and banks are now declaring their relocation to the countries of continental Europe. The same applies to global investors who do not intend to lose access to the European market and incur losses. In the near future London will probably become not such an attractive location to access a single European market.

As Angel Gurría, Secretary-General of the Organization for Economic Cooperation and Development OECD, pointed out in an interview with The Washington Post, "Brexit will be bad for the United Kingdom, bad for Europe and for the whole world"⁸

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⁸ Ylan Q. Mui Article from the Washington post, "Brexit' could send shock waves across U.S. and global economy", 18 June 2016

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