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UK in or out of the EU: The economic considerations

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SPECIAL REPORT

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Ahead of the 23 June referendum on whether the United Kingdom should leave the European Union, much attention is being focused on whether the UK would be economically better off in or out of the bloc. Whereas there seems to be general agreement that the UK economy would be hurt – albeit to varying degrees of magnitude – in the immediate aftermath of a vote to leave the EU, there are markedly differing views as to how it would fare over the long term. In this report, IHS looks at the main issues that are likely to determine how the UK economy would fare outside the EU, while we also look at the implications of a UK exit for EU countries.

Key findings

- The United Kingdom will hold a referendum on membership of the European Union on 23 June. Although IHS believes that the most likely outcome is a vote to stay in the EU, we assign a 35–40% chance that the UK could vote to leave.
- Should the UK vote to leave the EU, there would be a two-year timeframe from when the decision to leave was made and the exit actually taking place. One issue that would have a significant influence on how the UK economy fared over this period is how amicable/constructive/successful the UK's negotiations were with the EU.
- On balance, we believe that there would be a significant hit to UK GDP growth prospects over the second half of 2016, in 2017, and most likely 2018 in the event of a vote to leave the EU. Among other factors, a vote to leave the EU would most likely result in a major hit to business confidence due to the heightened uncertainty, leading to reduced investment and employment plans. Sterling would be likely to fall sharply, leading to a substantial rise in consumer price inflation, thereby eroding consumers' purchasing power. This would damage consumer spending alongside likely reduced employment plans and a negative impact on consumer confidence.
- There are several factors that would have an important influence on how the UK would fare economically outside the EU over the longer term that are very hard to predict in advance. These most notably relate to developments regarding potential UK trade agreements with the EU and other regions, the UK's access to the European Single Market, how effective deregulation is in the UK, the UK's immigration policy, and how the City of London fares. Indeed, the widely varying estimates in published studies of how the UK economy would be affected in both the short term and further ahead reflect the differing assumptions that have been made in these studies.
- In this report, we set out a "soft" exit scenario under which the UK would be likely to fare best outside the EU and could potentially thrive. We also set out a "hard" exit scenario under which the UK would be likely to struggle markedly over the short and longer term. In reality, what would happen to the UK after leaving the EU would undoubtedly lie somewhere between these two scenarios.
- Any assessment of the economic implications of a departure of the UK from the EU on the remainder of the bloc needs to take into account the fact that political and economic consequences are closely interrelated in this matter, implying second- and third-round effects that are very hard to quantify in net terms. What seems certain, however, is that the opening of such a Pandora's box would render any quick agreement between the EU and the UK on new trade regulations extremely unlikely. This would ensure a lengthy period of high uncertainty about counter-party risk that would significantly dampen international trade and investment activity within Europe for at least two years and probably longer.
- Negotiations about a new UK-EU trade regime would not only be hampered by feelings of resentment on the side of EU member countries but critically also by the (correct) perception that any move to allow the UK to maintain most of the benefits of the EU without bearing any of the costs would undermine the EU's raison d'être and induce copycat behaviour.
- The long-term economic consequences for the EU may paradoxically be modestly positive if the political process in the wake of a UK exit were to eventually lead to a more homogeneous EU membership, greater clarity about the wider benefits of being part of the EU, and enhanced willingness to support common EU institutions and abide by self-set rules.

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Political backdrop

Cameron's deal with the EU

On 20 February, UK prime minister David Cameron called a referendum on the United Kingdom's membership of the European Union and confirmed that the poll would take place on 23 June. Following prolonged negotiations at an EU Summit in Brussels, Cameron and other EU leaders struck a deal on reforming the UK's role within the bloc. The agreement was delayed by intra-EU disputes on particularly contentious issues such as reduced welfare payouts for EU citizens working in the UK, which was initially opposed by many Eastern and Central European countries including Poland and the Czech Republic. In addition, Belgium, France, Germany, and other EU member states were concerned about financial market regulation and how the UK's role is defined outside the Eurozone. Another sticking point was the UK's envisaged exemption from the contractually stipulated "ever-closer union", as member states such as Belgium feared this could lead other member states to make similar requests. Political support was highest for the overall goal to cut red tape and improve competition within the European Single Market.

Looking at Cameron's deal, one of the central questions is whether he achieved enough to actually make an impact. Many critics see the agreement as a weak political compromise, which is partly true if comparing the outcome to Cameron's initial demands presented in November 2015. Nevertheless, many EU leaders moved substantially from their original positions, largely because none of the EU member states wants the UK to leave the bloc.

The timeline for the implementation of Cameron's EU deal varies from issue to issue. For instance, measures such as cutting child benefits for EU citizens working in the UK require a change of secondary EU law and will by nature have to be approved by the European Parliament. Although there is no guarantee of parliamentary support, it is very unlikely that the Parliament will block the European Council's decision. Cameron's demand for the UK to be formally excluded from an ever-closer union refers to the EU's primary law and will be incorporated into EU treaties. However, treaty change will not happen before the referendum and is unlikely in the coming two years.

In the UK, a debate has started over the legality of Cameron's deal and some Eurosceptics claim that the arrangement could be overturned by EU judiciary. A majority of legal experts, however, confirmed that the Council's decision was legally binding.

UK domestic politics will be dominated by "in" and "out" campaigns

In the coming months, Cameron will have to further engage in political dialogue at the EU level while also facing significant domestic pressure. In this context, the biggest challenge will be to build a convincing case to persuade the UK electorate to support his call to remain a member of the EU, as well as appeasing Eurosceptics within his centre-right Conservative Party and across the wider political spectrum. According to recent opinion polls, UK voters are currently split rather evenly over the UK's relationship with the EU. However, some polls indicate growing support for the "leave" campaign, which has been strengthened recently by endorsement from cabinet members such as Secretary of State for Justice Michael Gove and prominent Conservative politicians such as London mayor Boris Johnson. There are several "in" and "out" groups campaigning for their causes. On the Eurosceptic side, there are two groups: "Vote Leave", which is backed by some well-known business leaders; and "GO" (Grassroots Out), which is supported by anti-EU United Kingdom Independence Party (UKIP) leader Nigel Farage. On the pro-EU side, there is "Britain Stronger in Europe", which is led by Conservative peer and former Marks and Spencer boss Lord Stuart Rose. The Electoral Commission will grant official status to one campaign on either side, allowing each to spend up to GBP7 million.

Most UK businesses and large lobby groups such as the Confederation of British Industry (CBI) are strongly in favour of the EU and a recent poll indicated that four out of five business leaders would vote for the UK to remain in the bloc. However, there are also groups such as "Business for Britain" that endorse a UK exit. In addition, the British media will play a crucial role in the campaign as most news outlets will vociferously support one side or the other. At the political level, there are Eurosceptics across the spectrum. However, the centre-left Labour Party, the Liberal Democrats, and the Scottish National Party will all campaign for the UK to stay in the EU, leaving Cameron's ruling Conservatives as the most divided party.

Trade, geopolitical clout, regulatory burden, and security at core of debate

The pro-EU camp argues that the UK's economic stability will be guaranteed if it remains part of the world's largest integrated single market. In this context, it is also often claimed that trade benefits and positive impacts on the labour market and income brackets outweigh the UK's financial commitments vis-à-vis the EU. In addition, Europhiles believe that the UK's EU membership enhances national security while facilitating co-operation on fighting terrorism and other security challenges. Correspondingly, many fear that a UK exit would reduce the country's geopolitical clout. International allies such as the United States and many others have reiterated that a UK exit would pose a high risk; for instance, many political leaders voiced their concerns at the recent G20 meeting in Shanghai. With regards to the regulatory environment, the EU's supporters say that it is much better for the UK to be able to influence EU laws directly rather than being in a trade relationship that requires the UK to adapt to most EU rules anyway.

Eurosceptics on the other side would prefer to claim back sovereignty through an EU exit and hope for autonomy from EU regulatory burden. They also argue that the UK would be a safer place outside the EU as it would be able to address border management and matters of national security in a more effective way. In this context, the "leave" campaigners also say that the UK would be able to control migration if it were to leave the EU. In addition, the "leave" proponents state that a UK exit would allow the country to establish itself as a strong regional and international power with a special status that would actually attract investment rather than divert it. They see big advantages if the UK were free to just opt into some trade arrangements with the EU while negotiating beneficial trade deals with other countries around the globe.

UK exit would be likely to increase government instability

Given that Cameron has allowed members of his party to speak out for either side, it is likely that the UK's domestic politics will be dominated by heated debates on the EU over the coming months, leading to elevated government instability. It is unlikely that the Conservative majority government will break up during the current administrative term. However, the intra-party divisions over Europe will deepen longstanding fault lines and a victory for the "leave" campaign would heighten the risk of Cameron stepping down as prime minister.

In addition, the UK would possibly face a constitutional crisis in a few years' time as a UK exit from the EU would increase the risk of another independence poll in Scotland in the UK government's post-2020 administrative term. A UK exit would also be likely to create several regulatory and political difficulties for Northern Ireland with regards to current arrangements with the Republic of Ireland and EU funds supporting the peace process in the region.

UK exit would further deepen current divisions in the EU

With regards to the EU, the UK referendum comes at a time of high instability as European leaders are struggling to adopt a common approach to the refugee crisis, resulting in uncertainty over the future of the Schengen Agreement. The EU also faces challenges with regards to the ongoing financial and social problems in countries including Greece and elevated geopolitical risks threatening internal cohesion of the bloc. Conflicts at the fringes of Europe, including the military confrontation in Eastern Ukraine and the war in Syria and Iraq, add to the overall pressure on EU leaders.

If the UK were to vote to leave the EU, the bloc's internal cohesion would most likely further deteriorate in the one-year outlook and this would weaken the EU's geopolitical and military clout. Additionally, right-wing parties such as the National Front (Front National: FN) in France would use the UK exit to boost their anti-EU and nationalist causes.

Economic implications of UK exit from the EU

Backdrop

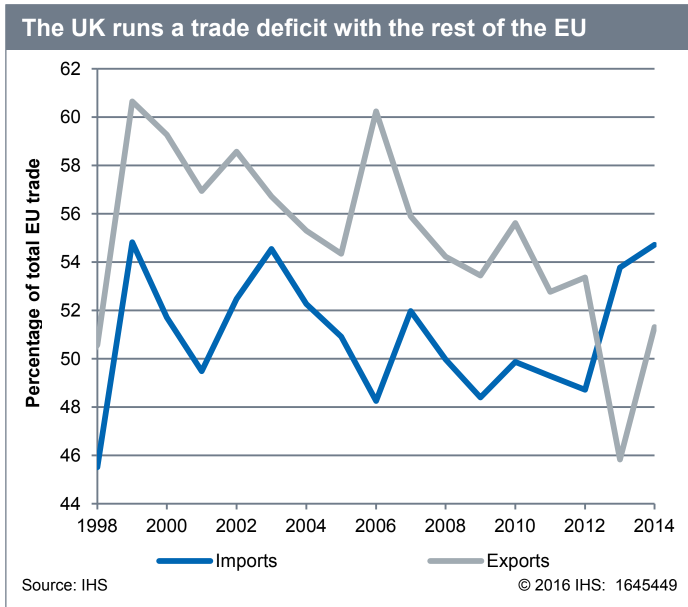
Any attempts to come up with meaningful measurements of the likely impact of a UK exit from the EU on the UK economy are fraught with problems. There are a number of factors that will have an important influence that are very difficult to predict in advance. Indeed, the widely varying estimates in published studies of how the UK economy would be affected in both the short term and further ahead reflect the differing assumptions that have been made in these

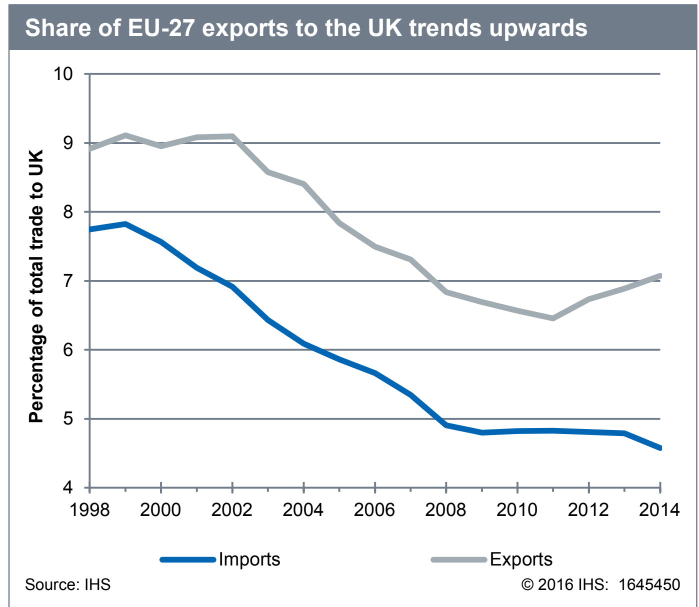
studies. The plain fact is that nobody knows how developments would pan out should the UK vote to leave the EU. The most meaningful approach is to focus on the factors that would most influence how the UK economy would perform and to highlight the issues.

UK economy in two years after exit vote

There would be a two-year period from the UK voting to leave the EU and the exit actually taking place. As a result, one issue that would have a significant influence on how the UK economy would fare over the second half of 2016 and in 2017 and 2018 is how amicable/constructive/successful the UK's negotiations were with the EU during this period. Negotiations on trade agreements with other countries/regions would also be important, but the key factor would be how matters developed with the EU.

Essentially, the prospective negative impact from a "leave" vote on UK economic activity during the two years from June 2016 would most likely be compounded if it quickly became clear that negotiations with the EU over the UK exit were messy and antagonistic, particularly relating to new trade agreements and access to the European Single Market. Alternatively, constructive and meaningful progress on the UK's post-exit relationship with the EU would be likely to increasingly dilute some of the concerns and uncertainties for the UK economy and would probably limit the fallout from a "leave" decision.





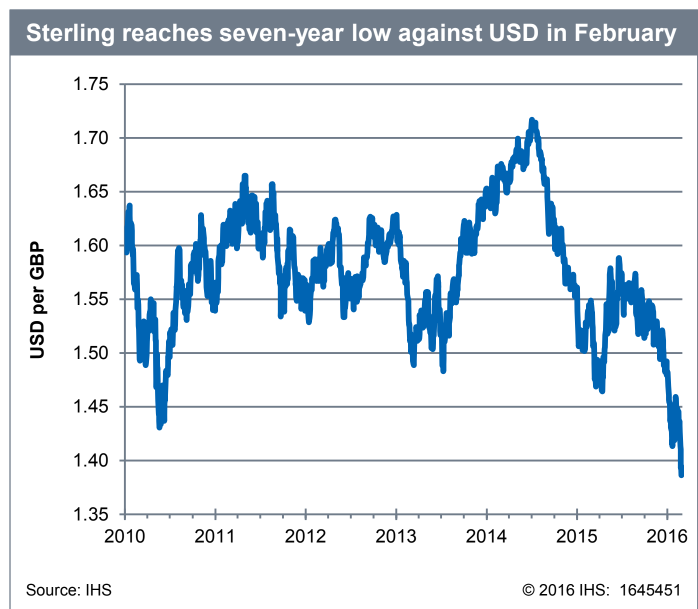
Even the most ardent supporter of a UK exit would be likely to admit that the UK economy would suffer in the near term from a decision to leave the EU. However, they would argue that this would be short-term pain for long-term gain. More commercially, it is widely argued by the pro-exit camp that the large EU trade surplus with the UK, which is considerably greater than the UK's surplus with the EU in financial services, provides clear incentives for all involved to avoid any disruption to the current free trade between the EU and the UK. However, not all EU members enjoy large trade surpluses, and political factors could encourage at least some member states to be difficult negotiators, at least initially. In contrast, supporters of the UK staying in the EU argue that the economy would not only suffer major near-term pain, but would also be worse off over the long term.

Growth forecasts would be markedly downgraded for 2016–18

Were the UK to vote to leave the EU, IHS would revise down its GDP growth forecasts markedly for the second half of 2016, 2017, and 2018. We currently forecast UK GDP growth at 2.1% in 2016, 2.5% in 2017, and 2.3% in 2018, on the assumption that the UK votes to stay in the EU. The size of the downgrade would be based on the quantification of two scenarios for a UK exit (amicable and contentious) presently under way using the Global Link Model, the results of which will be the subject of a second special report due in mid-April.

A vote to leave the EU would be likely to result in a major hit to business confidence owing to the heightened uncertainty, leading to reduced investment and employment plans.

Furthermore, foreign direct investment (FDI) and portfolio investment flows into the UK would probably suffer a major hit, which would make it much more of a problem to finance the UK's large current-account deficit and reinforce the downward pressure on sterling coming from market concerns. It is also very likely that the UK's financial market woes would be compounded by the credit rating agencies downgrading the UK's credit rating.



The strong likelihood that sterling would suffer substantial losses in the event of a vote to leave the EU is reinforced by the currency's sharp slide that occurred in the immediate aftermath of the announcement of the referendum on 20 February and following confirmation from popular London mayor Boris Johnson that he was in favour of leaving the EU. Although the general view is that the UK is most likely to vote to stay in the EU, the opinion polls are generally very close and Johnson's decision was seen as increasing the risk of a UK exit.

The expected sharp fall in sterling would be highly likely to lead to a substantial rise in consumer price inflation, thereby eroding consumers' purchasing power. This would damage consumer spending alongside likely reduced employment plans and a negative impact on consumer confidence. Weakened public finances would limit the government's scope to respond with fiscal stimulus.

Meanwhile, it is questionable how the Bank of England would respond. Would it raise interest rates from the current record-low level of 0.50% to try to limit the downward pressure on sterling and contain heightened inflationary pressures? Such a move would risk intensifying the downturn. Alternatively, would the Bank take interest rates lower (it recently said that interest rates could be taken lower if economic conditions warranted such a move) and reactivate quantitative easing in an attempt to limit the economic downturn?

UK economy outside EU over long term

It is particularly difficult to come to a definitive view as to how the UK economy would fare over the long term outside the EU. The various studies that have been carried out to date come to differing conclusions depending on what assumptions are made. Much would depend on the extent of the trade agreements that the UK reached after an EU exit – not only with the EU but also with other regions/countries. Other important factors include how much the UK would be affected by non-trade barriers when exporting to the EU, the amount of deregulation undertaken in the UK, what immigration policy was followed, and how the City of London's role as a dominant financial centre and how FDI into the UK were affected.

There are also questions as to whether UK economic dynamism would be seriously undermined – or alternatively unlocked – which is not easy to capture in any economic cost-benefit analysis of a UK exit. For example, supporters of an exit argue that UK productivity would benefit outside of the EU as substantially reduced regulation would facilitate an entrepreneurial culture by making it easier and cheaper to set up new, dynamic companies. In contrast, opponents of an exit argue that FDI into the UK would be adversely affected as the UK would be less attractive as a gateway into the EU, and that this would damage UK productivity by limiting access to foreign technology, skills, and working practices. Opponents of an exit also question just how extensive and effective the deregulation would be.

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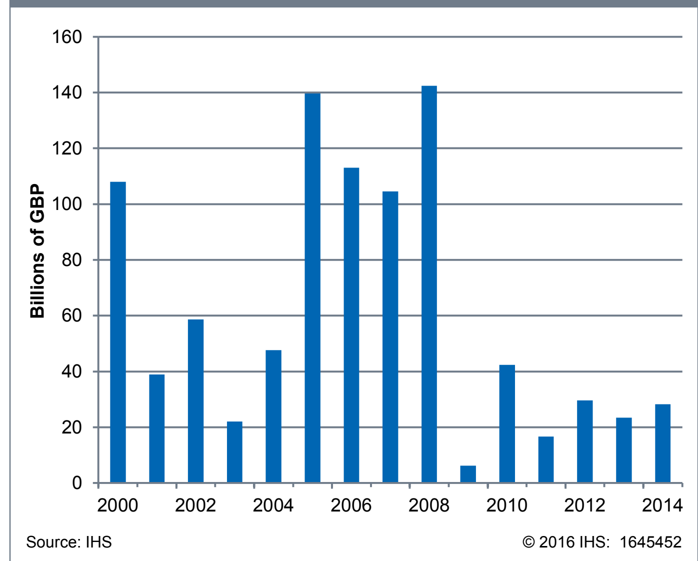
Most favourable outcome: A "soft" exit

The most favourable outcome for the UK outside of the EU would be what IHS terms a "soft" exit. Under this scenario, the UK would conduct amicable and constructive negotiations with the EU resulting not only in full trade agreements but also full UK access to the European Single Market. This would reflect belief that now that the UK had left the EU, it was in everyone's interests to make the best of the situation. Meanwhile, the UK would rebuild bilateral trade agreements with those countries that hold such an arrangement with the EU (as the UK would not be a party to these agreements once it left the EU). The UK would also move ahead with new bilateral trade agreements, such as with China, the United States, and probably former Commonwealth countries. Meanwhile, the UK would make efficient, meaningful progress on deregulation that was good for business.



With the UK achieving full access to EU markets and deregulation occurring in the UK, FDI would be increasingly attracted into the country. Portfolio investment would also be attracted into the UK as the economy would look increasingly well placed.

Meanwhile, the City of London would retain its position as the pre-eminent European financial centre. It would need to address two specific areas: third-party passporting and the sale of investment products from UK providers into the EU. The former relates to the many branches of non-EU banks that have been established in London to allow them access to the EU; this would need a new exemption specifically to be granted by the EU. For the latter, UK-based firms would have to comply with all relevant EU financial regulation.

On the migration front, the UK would attract highly skilled workers, perhaps through the adoption of a points system as used by Australia. A reduction in the number of less skilled workers coming into the country would have an upward impact on UK earnings. This would also put upward pressure on prices through increases in unit labour costs, hurting the UK's external competitiveness.

Most pessimistic outcome: A "hard" exit

Under a "hard" exit scenario, the UK would struggle to make progress on trade talks both with the EU and with other countries/regions, and would also find itself excluded from, or having limited access to, the European Single Market. This could very well be the consequence of governing politicians in EU countries being determined not to make things easy for the UK because of the risk that other countries/political groups could be tempted to push for an exit from the EU.

Meanwhile, the UK would make slow progress in reaching trade agreements with other countries. This could be the consequence of the UK looking to conduct negotiations on several fronts at the same time. Indeed, there are reports that the UK would have to negotiate (presumably from scratch) no less than 53 separate bilateral trade deals to replace what is currently covered by EU trade deals – an enormous task for even the most well-resourced/efficient country. There is also the possibility that other countries would be in no great rush to come to trade agreements with the UK. For example, the United States would probably be far more interested in reaching a trade agreement with the EU, which would still present a much larger internal market, than with the UK.

Tying in with this view, a report by the Cabinet Office released at the end of February claimed that the UK would face a "decade of uncertainty" in the event of an EU exit due to the time it would take to renegotiate new trading relationships not only with the EU but also with countries with which the EU already has trade deals. The UK has not independently concluded such agreements since the 1970s. Additionally, the Federation of German Industries (Bundesverband der Deutschen Industrie: BDI) – admittedly a strong advocate of the UK staying in the EU –

argued in an interview with Bloomberg that there would be “no amicable divorce” and that “a vote to leave in the June 23 referendum would spark a ‘tooth-and-nail fight’ between the UK and its erstwhile partners to secure bilateral advantages in the separation”. The BDI further argued that “there’s no default European free-trade status in the waiting” and that resolving post-exit legal issues including trade treaties, taxation, and regulatory matters might take 5 to 10 years, “embroiling companies in thousands of contract revisions”.

It should be acknowledged that proponents of a UK exit argue that this is scaremongering and dismiss the notion that it could take so long to negotiate trade agreements, particularly when there are various other models/relationships on which they could be based. Yet trade negotiations have always taken place at a snail’s pace and even if the UK were to push for prompt conclusions, one could not guarantee similar urgency among all the trading partners. Proponents of a UK exit also point out that for those countries with which the UK did not reach a new trade agreement, the UK would revert to “most favoured nation” status, so there would not be crippling tariff increases.

With the UK having limited access to the European Single Market and struggling for trade agreements, there would be significantly lower levels of new FDI. This may well be displaced to other EU countries, most likely including Ireland. Meanwhile, deregulation in the UK would prove limited, constrained by the fact that the UK would still effectively have to adopt many European standards to sell products and services in the EU.

In this “hard” exit scenario, the City of London’s position would be compromised and it would lose appreciable business to Frankfurt and Paris. The role of non-EU bank branches and investment managers and hedge funds that wish to sell into the EU would face clear threats, and many of these could need to relocate at least partially to an EU location. Furthermore, Eurozone regulators could make it more costly and awkward for banks located and regulated in the UK when dealing in euro-based products and instruments. However, it should be noted that the City would still have many in-built competitive advantages such as volume of business; existing financial linkages; a large, experienced, and trained financial workforce; and the English language. In 2014, financial and insurance services contributed GBP126.9 billion in gross value added (GVA) to the UK economy, 8.0% of the UK’s total GVA. London accounted for 50.5% of the total financial and insurance sector GVA in the UK in 2012.

Finally under this scenario, the UK’s migration policy would result in a lack of incoming workers needed for lesser-skilled jobs, and the resultant reduced workforce would limit potential UK growth.

Conclusion on long-term economic consequences for UK

In reality, what would happen to the UK after an EU exit would undoubtedly lie somewhere between the two scenarios set out above. One general conclusion that emerges from the studies that have been carried out is that the greater and more comprehensive the trade agreements that the UK comes to after an exit – both with the EU and with other regions/countries – the better (or less badly) the UK would be likely to fare after leaving the bloc.

However, even here there are uncertainties. One concern, for example, is that by engaging in more trade agreements with countries/regions outside the EU, UK companies could be increasingly exposed to competition in their domestic market from very low-cost companies. If this did happen, a key question would be how UK companies responded and if it helped UK economic dynamism by encouraging innovation. If UK companies failed to respond, there would be a risk that it could lead to some manufacturing sectors suffering a serious hollowing out. This would threaten to outweigh any wider benefits to the UK economy arising from cheaper imported goods.

UK exit implications for EU countries

A tectonic shift in the political architecture of Europe

An assessment of the economic impact of a UK exit on the remainder of the EU is complicated by the intertwining of political and economic implications, especially in the current climate of an already frail situation due to the inadequate and split European response to the migrant crisis.

The more the national views of EU members diverge with respect to what the EU should represent and what degree of inter-country harmonisation and solidarity is desired, the more difficult any negotiations with the UK about post-exit relations would become. In addition, an EU preoccupied with how to get the migrant crisis under control – including how to prevent a complete collapse of Schengen rules and damage to the Common Market from re-erected internal borders – is unlikely to reach any quick agreement with the UK about a new trade regime, leading to an extended period of major uncertainty that would dampen trade flows and investment in the whole EU for at least several quarters and more likely two years. This would be down to both political disagreements among EU members and also to the sheer strain on administrative resources (in the European Commission as well as at the level of national governments) in such exceptional circumstances.

This generally unfavourable political background would be exacerbated by the fact that most people in other EU countries would not like to see the UK leave the EU – be it simply for financial reasons (the UK being one of the few net contributors to EU budgets) or because such a market-oriented voice would be sorely missed, carrying the risk of an even more bureaucratic and/or politicised European administration in Brussels. A recent survey conducted by Lord Ashcroft Polls among 28,000 voters in the EU-28 revealed that only 10% of people in the other 27 EU countries would welcome a UK departure, with 60% preferring the UK to remain a member and 30% being indifferent.

This means that many EU members might resent the UK if it were to vote to leave, strengthening their determination to make life difficult for the UK in a post-exit environment. Thus it seems politically unimaginable that the UK would be granted the same access to the Common Market as before, only without payments to Brussels. This would not only be motivated by feelings of resentment, but, even more importantly, by the sheer fear on the part of EU officials and Europe-minded national governments of copycat moves by other member states. This concern is fully justified as the existence of an option to reap the benefits of the Common Market without bearing any of the administrative and regulatory costs would effectively destroy the EU's raison d'être.

Economic implications of UK exit for the EU

A UK exit would naturally encourage the growing nationalist movements in other EU countries to "reclaim" national sovereignty. Apart from ignoring the political lesson of the Second World War that co-operation and permeable borders are vital for peace on the European continent, such a renationalisation would also have negative economic ramifications. In the almost 60 years since the Treaty of Rome, countless steps towards common rules and regulations applied within a growing geographic area have lifted economies of scale, and the effective removal of borders for trade in the Schengen Area has reduced transaction costs and raised productivity.

Within the Eurozone, the added advantage of the removal of currency risk has lifted overall growth potential further – while undeniably also creating new distributional problems across countries.

Developments likely to be negative in 2016–18

A departure of the UK from the EU would put much of that economic progress at risk. Initially, during the two years foreseen by Article 50 of the Lisbon Treaty for negotiation of the terms of an exit from the EU, the massive increase in uncertainty – not only in the UK itself but also in the remainder of the EU – would weigh down on activity. This uncertainty would pertain both to the terms of separation and the potential boost to separatist leanings in other EU member countries. This increased counter-party risk would stifle business activity with respect to external trade and investment.

As the possibility of a UK exit has been in the political arena for years already, its shock value would clearly be smaller than it had been in 2008 upon the unexpected collapse of US investment bank Lehman Brothers. Nevertheless, in both cases a large loss in trust in international business partners is at play, dampening economic activity. Although the consequences of such fundamental behavioural shifts are hard to quantify, annual GDP growth in the (remaining) EU in the two years following a UK exit would surely be hurt by more than one- or two-tenths of a percentage point. The order of magnitude would rather lie in the vicinity of a full percentage point per year.

Long-term economic consequences

In the long run, the economic consequences of a UK exit from the EU would depend heavily on the future composition of the bloc. On balance, they should be modestly positive. Paradoxically, the more countries that were to follow the UK out, the more homogeneous the remaining EU would become. For, it is reasonable to assume that in most cases those countries with the greatest motivation to leave are those that have the greatest problem with pooling sovereignty at a European level. France is arguably an exception to this rule, but in doubt this country would be likely to decide to stay in the EU. Therefore, in as much as the remaining members can agree on more far-reaching devolution of national political powers to the European level than is the case right now, the scope of gains in potential growth due to lower transaction costs, common rules, and smaller risks is widened. In addition, non-European trading partners would in doubt rather want to do business with such a bloc than with individual countries that are no longer part of that bloc, simply because of the larger market.

Indeed, another paradoxical corollary of a more homogeneous EU would be that reduced friction between EU members and potentially even a less unwieldy bureaucracy in Brussels (as fewer countries have to be "cared for") would remove some of the reasons why the UK and perhaps a few other countries are currently motivated to leave the EU in the first place. A more nimble EU, while preserving the advantages of a level playing field in an economic area with the same rules and regulations, would restore some of the attractiveness lost during the past decade or so.

Finally, a UK exit and the observation of what followed economically for the UK in its aftermath would focus the minds of all remaining EU countries as to the economic value of EU membership – even when the disadvantages such as curtailed national sovereignty and greater demands on international solidarity are taken into account. As a result, the current strengthening of centrifugal forces in Europe may well lose momentum and even reverse a few years from now.

How quickly perceptions can change is exemplified by the Greek situation in the current migrant crisis. Having for a long time viewed Germany as an enemy keen to throw Greece out of the Eurozone (or even the EU) over the debt crisis, Greece is now experiencing solidarity from Germany as a result of Chancellor Angela Merkel's insistence on creating a truly European solution (in this case including support from Turkey) instead of erecting new borders within the EU.

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