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A Political Economy to Examine Brexit

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I Introduction

To many the British referendum on June 23, 2016, had shocked the world as the British voters had voted to leave the European Union (EU) with 52%. Certainly the British referendum was a political act, but it became very ideological as it symbolized also the ideological divide within the EU between leftist who are ready to embrace the illegal refugees at the cost of their own development, competitiveness and security, and the rightist who do not want to shoulder the burden of the illegal immigrants and prefer to take back their own power of decision making from the EU. In many ways, the Greece debt event in 2014 and the illegal immigrants in 2015 had battered the EU severely, as both drained not only the resources of EU thereby imposing huge burden on the part of the taxpayers, but the subsequent economic, social and security burden that may be become life-long.

When EU was formed and enlarged from the few stronger Western European members to incorporate many economically weaker EU members, it was wishful that the smaller and new EU members could gain strength from the stronger members. With the leftist behavior that capitalizes fraternity into a political ideology, it turned out that the weaker EU members remained weak and unprogressive, and the stronger EU members were being pulled to aid the accumulated economic burden of the weaker members. The Greece debt was the typical case where EU members were keen to come to the aid of Greece, knowing that the Greek economy could not make any progress.

Together with the decades-long socialist ideals of income redistribution and drive to equality through the imposition and practice of high taxation, high welfare spending and the cumulative fiscal deficit and national debt across many EU countries would only mean that the

EU as a whole is destined to remain weak, uncompetitive and capital would be driven to other more business-friendly destinations. The loss in economic competitiveness in EU would mean the gain in economic competitiveness elsewhere. However, there could be a redistribution of gain and loss within the EU members. The weak Euro would mean that the strong exporters among the EU members, typically Germany, would gain and their exports can remain competitive price-wise when compared to Japan and US products.

## II The British Calculations

As a member of the EU, the UK-EU relationship would occur on a mutual basis, as citizens and businesses would take advantage of each other. Although there are reports as to how much the UK government could save from exiting because the UK contribution to EU could be saved and so on, the truth is that there will not be any changes in the economic fundamental in the UK economy. Since the advantages in the UK-EU relationship are mutual, so are the disadvantages. As an independent territory, UK businesses can hire from overseas, including member of EU. Similarly, EU businesses can hire UK citizens. The arrangements should relate more to skill and professional needed rather than the immigration papers required. With Brexit, it probably would be true that visas are needed for travelers. That should be more of an administrative arrangement than changes in economic fundamentals.

One could complain that the British voters are 'selfish' and not prepared to help other EU members. But being one of the stronger members in EU, British voters would prefer not to be dragged into issues and problems of other EU members, and UK citizens had no choice but to shoulder the economic burden arising from other EU members. In the case of the illegal immigrants, it would be the case where Germany took on the immigrants, but once they are secured with the EU passport, they would further migrate to UK due to language advantage. Hence, the UK authority cannot stop the inflow of immigrants and the British taxpayers would have to shoulder the additional welfare spending, as the majority would not assimilate into the British society. The increase in the burden of the 'social cost' is obviously the first calculation when voters decided to exit from EU.

While the Labor Party in Britain opted to remain in EU, the majority of workers, especially the low skilled workers may not toll the party line. The new immigrants would sooner or later join the labor force, and many of these immigrants are not that highly skilled and the

supply of non-skilled workers should subsequently increase, thereby competing directly with the existing workers doing low-skilled jobs. A larger supply of low skilled workers in theory would lower the wage or the existing workers might become unemployed as the new supplies could be younger and more productive and efficient. Hence, the fear of increase in supply of labors from the new immigrants would definitely urge them to exit from EU. The British Labor Party has miscalculated the desires of its members. The increase in the supply of low-skilled workers should be the second calculation by the British voters.

A greater degree of economic flexibility should be the third calculation in Brexit. With an economically saturated EU, further expansion is unlikely to appear in the foreseeable future. The immediate burden of debt and immigrants that EU is facing would delay growth for a considerable period of time. Hence, economically associating with EU would not have much to gain. On the other hand, the UK economy has at least remained steady, if not strong. Thus, steering the UK's economic path independently from EU would allow greater flexibility in terms of resources deployment, industrial restructuring and engagement in the international economy through trade and foreign investment. The EU market is there, and the withdrawal of EU investment and other economic activities from Britain should be mutual. Indeed, economic activities between Britain and EU members would be calculated based on cost rather than political terms and measures. Although much has been politicized and propagandized, the actual economic cost and benefit may cancel out each other.

The political noise was greatest in the financial market, as the media had portrait the incident as if it was another crisis. The stock market has often been portrait as an investment market, but the true color is that it is a speculative market where speculators looked for opportunities in both the bull and bear markets in order to do the trading. The Brexit provided a golden opportunity for 'investors' who would speculate on the movements of stocks, currencies and other financial derivatives. While speculations took place in the financial markets, the rest of the world remained unaffected, and the 'dust' of the British referendum would settle down after one or two weeks of turbulence in the financial market. This was exactly what had happened, and that the stock and currency markets returned to normal after a while. Thus, the 'negative' impact on the stocks was probably a miscalculation, as there has always been a lack of distinction between investors and speculators. Given that there is no change in the economic fundamentals

in the UK economy, the Brexit served as a shock to the financial market, increasing its short term volatility.

### III The Next General Election

All major political parties shall worry about the next election, and the Conservative Party in Britain is no different. With the referendum on Brexit, especially when the Labor Party is also supported for Britain to remain in EU, the Conservative Party is likely to win the next general election. Since the leaders of both the Conservative Party and the Labor Party opted to remain, and if the majority of the voters chose to remain, it would give the Conservative Party the lead in the next election. If the voters chose to exit, the Labor Party would lose out completely in the next election.

The British Prime Minister, David Cameron, made a majestic move after the British referendum to exit and decided to resign from the post, since he himself supported the remain vote. By allowing the new Prime Minister, Teresa May, to be in charge of the exit process, the UK economy can have a fresh start in its economic relationship with the EU as well as the world economy. Unless the UK economy before the next election shows a weaker performance than before the exit, the Conservative Party would have a strong political support in the next election. Hence, was the Brexit referendum an instrument in preparation for the next general election in Britain? It certainly is as whatever the outcome of the referendum should be more favorable to the Conservative Party than to the Labor Party. As such, Prime Minister Teresa May would have a relative long period in handling the UK economy.

### IV Return of the Rightists?

“Enough is enough” is probably the message of the Brexit, as the EU policies have long been too lenient towards welfare, redistribution and fraternity to the extent of penalizing the tax payers, eroding economic competitiveness and thwarted potential growth. In short, there are too many pro-socialist policies that have taxed the EU economy considerably. With Brexit, the EU will probably be dominated by French and Germany, which are still keen in adopting pro-socialist policies. The question is whether other EU members would have the “Brexit urge” and proposed policies that could unwind the existing socialist path. Instead of providing endless aid

to others at the expense of their own growth and expansion, would it be better for individual EU countries to strengthen their own domestic economies in the first instance?

By using the “social cost vs private cost” paradigm, the simple questions include how far individual EU countries can aid the debt problems in Greece, while Greece itself is not that prepared to unwind their policies? Similarly, how extensive EU countries can absorb immigrants from the war-torn and conflict-prone countries in the Middle East and North Africa? In both cases, the ultimate question is how much ‘social cost’ EU countries can shoulder from problems of neighboring countries? There is always a ‘principle – agent’ problem in political decisions when it comes to aid and assistance. Political leaders (the agent) decided and capitalized on the policies, but the spending and security issues that arise from their policies would be shouldered by the taxpayers and the general public (the principle). Hence, it would be easy for German Chancellor Angela Merkel to opt for an open arm policy on the refugees as that could give her political capital, but it would be the German taxpayers who would have to bear the prolonged welfare spending on these refugees, and it would be the general public whom would feel insecure should terrorist attacks occur in their homeland.

Fraternity should not be included into an ideology. Helping others is a human virtue, but helping others by getting oneself hurt requires an entirely different consideration. The Brexit suggests that there should be an end to all these pro-socialist policies, but rather there is a need to return to rightist policies that aim to promote a country’s own economic strength, improve its own economic competitiveness, and re-energizing its industries. It is true that the ideological divide within EU members has been dominated by the leftist leaders, but new scenarios can emerge in Germany and France in the next elections as the pro-socialist policies among many EU members are not seen to have provided feasible solution to debts, immigrants, growth and competitiveness.

## V Conclusion

The impact of Brexit is not only confined to the political scene in Britain, or in its relationship with EU. It has world-wide implications because it served as a ‘wake up’ call to the international community that some prolonged pro-socialist economic policies are getting out of control, or that both the EU and the world community have been suffering from shouldering the vast ‘social cost’ burden which could have been exploited by the weaker neighboring countries.

The Brexit implies that economies should look after their own domestic problems and not pass their 'dirty linen' to a neighboring country. The neoclassical economic theory of improving one's domestic economic strength is still the best answer for regional and international growth and development. Voters should not be side-tracked by political decisions, which often produce unintended and unfavorable economic consequences. The 'principle – agent' theory should be kept in mind when voters are judging on the decisions of their political leaders.