University of Economics, Prague

International Business – Central European Business Realities

United Kingdom's Economy after Brexit with Emphasis on the Financial Industry

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Declaration

United Kingdom's economy after Brexit, with enthuses on the financial industries and sectors

I hereby declare that I am the sole author of the thesis entitled "United Kingdom's Economy after Brexit with Emphases on the Financial Industries and sectors". I duly marked out all quotations. The used literature and sources are stated in the attached list of references.

In Prague on .... Signature

Valentyn Pivnyk

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Abstract

My thesis covers the Brexit topic and focuses on the economic and financial consequences side of the effects which follow in leaving the union. The United Kingdom is the first country ever to try and leave the European Union, after many years as member of the Organisation, the U.K. enjoyed the benefits of operating in a single market, free travel, rules and regulations which benefit not only the political side but also the citizens and businesses of those countries.

The untold truth of Brexit followed with government uncertainties and relations have damaged the reputation of the UK's stronghold as an economic giant. An analysis of the political situation shows that the UK government are losing the Brexit fight, as the draft agreement seen some key political figures resign from top Brexit posts caused the Pound Sterling to fall even further to that of the June 2016 vote, this has been the biggest fall against the euro and the dollar.

London as a financial industry giant will take the toll of a no Brexit deal as many financial operations will look to move to mainland Europe where they will seek the comfortability of operating in the community. My thesis further explains the Brexit process, such the triggering of article 50, the key Brexit facts about soft and hard Brexit procedures, but also other options including the cancelation of Brexit altogether and stay with the union, this scenario gives the best options for stability and economic prospects.

Looking at the economic and financial side of the UK I had to research the Balance of Payments of the UK to further analyse the effects of Brexit, the economic stability will fall and take some to recover as new trade deals begin negotiations and finally to finish my analysis I taken a country (Ukraine) as the one which can replace the UK in the European union and looked at key facts of how integration will be beneficial for the EU as a whole. It is certain that the UK's exit no matter how strong in agreement will damage the economy and the financial stability for several years to come, Brexit build on overestimations and false accusations of migration including other facts brought out by a few political figureheads caused disbelief within the union, it is a definite mistake which should be dealt

carefully and gracefully as a wrong move can cause crisis in the UK where the recovery will take tens of years to bring back stability.

Tématem mojí diplomové práce je Brexit a zaměřuje se zejména na ekonomické a finanční důsledky, které následují při opuštění Evropské unie. Spojené království je první zemí, která se kdy pokusila opustit Evropskou unii. Po mnoha letech členství v této organizaci se Spojené království těšilo z výhod jednotného trhu, volného cestování, pravidel a nařízení, které mají prospěch nejen politice, ale také občanům a podnikům těchto zemí. Nevyřčená pravda o Brexitu následovaná vládní nejistotou poškodily pověst Britské pevnosti jako hospodářského obra. Analýza politické situace ukazuje, že vláda Spojeného království prohrává bitvu, neboť v návrhu dohody došlo k tomu, že některé klíčové politické osobnosti resignovali z nejvyšších míst Brexitu, což způsobilo, že libra klesla ještě více než při hlasování v červnu 2016. Jedná se o největší pokles oproti euru a dolaru.

Londýn jako gigant v oblasti finančního průmyslu si vybere daň Brexitu, protože mnoho finančních operací se přesune na evropskou pevninu, kde se budou snažit o komfortní fungování v komunitě. Moje práce dále vysvětluje proces Brexitu, jako je spuštění článku 50, klíčová fakta o měkkých a tvrdých postupech Brexitu, ale i další možnosti včetně úplného zrušení Brexitu a setrvání v unii. Tento scénář poskytuje nejlepší hospodářské vyhlídky možnosti stability.

Při pohledu na ekonomickou a finanční stránku Spojeného království jsem musel zkoumat platební bilanci Spojeného království, abych dále analyzoval účinky Brexitu. Ekonomická stabilita klesne, aby se pomalu zotavila, jakmile začnou nová obchodní jednání a nakonec končím analýzu tím, že jsem vybral zemi (Ukrajina), která by mohla nahradit Spojené království v Evropské unii. Podíváme se na klíčová fakta o tom, jak bude integrace přínosná pro EU jako celek. Je jisté, že výstup Spojeného království bez ohledu na to, jak silná bude dohoda, bude poškozovat ekonomiku a finanční stabilitu po několik dalších let. Brexit vycházející z nadhodnocení a falešných obvinění z migrace včetně dalších skutečností, které vyneslo několik politických osobností, byla jednoznačně chyba, která by měla být pečlivě a racionálně řešena, protože nesprávný krok může způsobit krizi ve Velké Británii a návrat ke stabilitě by trval desítky let.

Důsledky Brexitu ovlivní obchod s výrobky a služby přinesou vyšší ceny do Spojeného království. Společnosti, které se rozhodnou opustit Velké Británii mohou zanechat tisíce nezaměstnaných. Brexit s sebou nepochybně přinese hospodářskou a finanční nestabilitou. Nejlepší způsob, jak může Velká Británie znovu získat svou sílu, je zrušení Brexitu, protože by se veškerá jednání mohla smést ze stolu. Také by se konalo druhé referendum. Nepravděpodobné, avšak další způsoby, jak udržet silnou ekonomiku, by bylo vyjednávání obchodů s jinými zeměmi, jako jsou USA nebo Commonwealth, kde by se Velká Británie obešla bez EU.

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Abbreviations

UK: United Kingdom
IA: Investment Association
CA: Current Account
IIP: International Investment Position
FA: Financial Account
GBP: great British Pound
USA: United States of America
FDI: Foreign Direct Investment
EC: European Community
CE: Council of Europe
FDI: Foreign Direct Investment
NGDP: Nominal Gross Domestic Product
EU: European Union
AUM: Assets Under Management
BOP: Balance of Payments
CA: Capital Account
PM: Prime Minister
BOE: Bank of England
CZK: Czech Koruna
EEC: European Economic Community
ECB: European Central Bank
IIP: International Investment Position
ONS: Office for National Statistics
MP: Member of Parliament

Introduction

I wish to express my enthusiasm in the topic of Brexit, therefore I aim to investigate the impact the withdrawal from the European Union will have on the British economy with particular interest into the financial industry and the catalyst of events to follow.

In a speech held January 2013, in a tactical gesture to the Conservative Party's Eurosceptic wing that secured continuing support for his leadership, the then UK Prime Minister David Cameron promised to hold an in-out referendum on the UK's membership to the European Union before the end of year 2017, on the assumption that he would go to win the 2015 General Election. This has indeed secured him a second term in charge and as promised, the necessary steps to a peoples' vote on the referendum were being put together. The European Union Referendum Act 2015 which set out guidelines for the referendum with the ultimate question to be should the United Kingdom remain or leave its membership to the EU (UK Parliament and Legislations, 2018) brought into law a non-binding referendum to be held on 23rd June 2016 (Jackson, 2016)

The government held a referendum whether the UK should terminate its membership to the European Union as promised by Mr Cameron, the leave/remain vote was 51.9 to 48.1 (Financial Times, 2016) The so-called Brexit vote has been dubbed by the media as the world's most complex divorce, due to the uncertainties behind it on the governmental level and the perceptions of the voting public, I will examine these statements further in the thesis paper, as there are infinite number of effects that can follow after the Brexit vote triggering a catalyst of events following the UK/EU divorce. The main issue would be to examine the UK after the vote and the state of its economy and financial industries, as we well know, London is the hub of main banking and financial industries, but also the metals exchange, I will examine the state of UKs economy the effects on the pound, gold and other sectors linked to the financial and economic sectors.

The monarchy could intervene with the government, Queen Elizabeth has overstepped protocol before and, although neutral, she could stop Brexit altogether. However, in 2011 she has reportedly told a colleague that the EU is heading in the wrong direction (Jackson, 2016), thus, giving us more uncertainties about the UK and its future. Held together by opinions of a misinformed public and a government which is uncertain of how to structure the UK's exit in such a way as not to damage relations and its economic status, the vote only further increased nationalism and gave hopes of national identity in an already tense situation between the UK and EU.

It is important to see some history of the UK and the EU before I further talk about how the Brexit vote came to what we have today, a misinformed public and a government full of uncertainties and misconceptions of the what leaving the EU can hold in a post Brexit Britain, as no country has ever tried to leave membership and in the current state of affairs we have countries awaiting to gain access to membership of this big economic establishment as for them it will bring economic stability and prosperity.

The main goals of my thesis will be to analyse the effects of the Brexit on the UK's economy and the financial industry, the reasons for this is the UK is a main hub for financial firms, banks and investment sectors but not only that, the metals and financial markets exchange also tend to have the UK as their bases.

Throughout this this paper I will seek to determine the effects that the Brexit vote had on UK's economy and its financial consequences, as the Brexit deal is still under planning and mis-agreements of governments, the work will carry on through the paper and will look at the different stages of the negations between the UK and the EU. To analyse the total effect on the United Kingdom post Brexit I will further look at financial and economic data pre and post vote and come to my own analysis of how Britain will be without Europe. I will analyse the short and long-term effects the Brexit had on UK's economy and financial industries, the type of Brexit Britain is heading for, the devaluation of the pound and if so, how can market correction be in place following planned departure.

1. Methodology

My thesis will explore the effects of Brexit on the economic and financial side of the story, there are a number of articles and books that have to be read, the methodology will be further adapted as this part of the work is still ongoing. I will have to research new data and findings which have just been published to develop assumptions and the scope of leave vote has yet to be known in detail. I have chosen to concentrate on main economies and financial industries that will be effected by Brexit, just the sheer scope and uncertainty of Brexit and governments have increased the workload, after further research these factors will be further concrete for me to make assumption and come to conclusions after which this will help me setup some kind of analysis and determining factors for me to able to compile a plan for suggestions for the future.

The focus of the work will be on the economic and financial consequences Brexit will have on the economy and the financial industries, as I cannot focus on all the areas that will be effected, I will link my research on main aspects that of UK economy, working in the financial industry myself I think and the fact that regulation is a much-debated topic with regards to Brexit, though there has been no convincing evidence to explain the economic consequences of EU regulation. Hence, I have chosen to focus on areas that arguably will have large economic impacts on the UK, and for where there are developed theories to predict such outcomes.

This is quite a difficult but very interesting work to write, and as a British national I would like to write about my experiences with Brexit some of which including the exchange rates with personal experience of the level GBP to CZK in 2015 being upwards of 35 to GBP and after the vote the pound plummeting against the most currencies, in November 2017 the current rate is well below 27CZK to the Pound. The governmental uncertainty can also be clearly visible when looking at currency markets.

1.1 Delimitations

My thesis covers a number of methodological approaches that diversify according to the nature of the subject in matter and at the different stages of my analysis to reach my final goal of answering the research topic of my studies on how Britain's departure from the European Union will affect its economy with the emphasis on the financial sectors. With regards to the methods of the research, I have chosen to rely upon estimates from professionals in the field, rather than collecting my own data through surveys or interviews. I am fully aware that I therefore have less control over the validity of the data and I will not be able to present a calculation that sets a number to the costs of Brexit, and the total toll on the economic spectrum. On the other hand, this approach I have chosen allows me to portray a broader perspective of the research topic in mind and to bring up different aspects of the consequences. I can depict the many uncertainties involved and thereby emphasise the impossibility of quantifying the economic costs with a number, and the full toll on the British financial and market situation.

1.2 Methods

As whole Brexit topic is quite wide and has many different elements in the means of the Brexit vote and the ongoing negotiations, there are many changes that happen daily not only in the political segments but also financially thus making it more difficult to concentrate on the whole anatomy of Brexit. I understand fully that the research for this is quite difficult and may be misleading on some spectrums, however, the method I have chosen to employ was formulisation as it exists on the idea of borrowing information found through other methods. I did not need to gather new data by means of interviews. Formalisation which is mainly concerned with behaviour and structure as it emphasises the analyses which can be measured. Hence, it was ideal for helping me to determine economic consequences of Britain's international relations with the EU and looks at trade agreements like the single market, and the open border policies with regard to trade, but also as mentioned the movement of labour.

The other methods which are more closely related to my topic of investigating are the methods of Stratification and Numeration which involve the use of numerical data to analyse the full extent of the British economy and the effects Brexit will bring to economical spectrum of my work. Using these methods will help to better emphasise my analysis of the thesis on the effects on the financial industry and the sectors of the British economy, this will also, help me to conclude the status after the march 2019 leave date in a far better way.

To write my thesis, my concentration on the research will be based on already published articles, books surrounding the subject matter such as ‘The economics of Brexit’ written by Philip B Whyman and Alina I. Petrescu, ‘The EU after Brexit’ written by Francis B. Jacobs and ‘Unleashing Demons’ written by the former director of politics and communication Craig Oliver and many other books which I have read for research and personal interests surrounding the subject matter, other works of interest include institutional research publications, with the aim to look at the political side of Brexit and their uncertainty and the Economic and Financial consequences of Brexit on the United Kingdom. I will also use news and media sources to carry out my studies of my research topic before writing my own conclusions of the effects of Brexit on the economy and financial sector.

1.2 Structure

The structure of my thesis will be looking at the Brexit negotiations throughout the timeline and different stages of the Brexit procedure the different part of my thesis cover the range of topics including the history of the European Union and the integration of the UK, I would cover some basis for the Brexit vote, UKs history in the EU, the economic analysis of the UK pre vote and post vote, the Exchange rate and financial markets pre vote and post. The effects on London and its industries, FDIs, the financial markets including the Banks and world commodity trading companies, some who have already announced to leave London and the UK to settle in another European country, The Czech Republic, Germany and Luxemburg as a main choice for some financial and other major firms operating in the UK currently. I will also cover the topic of the financial sector and the accounts of the UK including a thorough analysis of the economy. I will also look at one country to take the place of the UK in the EU.

1.4 Literature review

There are a number of works which have been published by different organisations and institutions that will be used for this thesis, books which have been recently published as mentioned above are good sources for information as well as institutional publications as the data they present is relevant to subject at hand. The following areas of interest with more topics to cover the Economic and Financial consequences of Brexit on the United Kingdom, I will thoroughly analyse the Brexit vote and the effect it had and the consequences which might arise for UK, The Great British Pound (GBP) has plummeted since the Brexit vote so an analysis of the economic and fiscal policies will be necessary, what has the weak pound to offer and how was the Bank of England (BoE) effected by its decline, the actions the top analysts are talking about and the plan for the future of the pound. The exchange rates are a big concern with a weak pound and a weaker economy maybe the UK is heading towards a big shock or a mass turnaround for the future. The effects on UK foreign investment. (will investors seek other opportunities or move from the UK. Short-term and long-term effects of Brexit on the economy and the Pound.

The Economic and Financial consequences of Brexit on the European Union, this part will look the effects the British decision had and what the outcomes may hold for the European Union and its remaining 27 members, the analysis of which will contain the different treaties and financial investments, UK FDIs, the exchange rate the economic factor of the EU without Great Britain. London as a global financial centre, it is well known that London has been at the heart of the financial industry and a home for many Banks, investment firms, trade markets, precious metals and other world leaders in financial markets, and the economics of the pound and its exchange rate against other leading currencies.

The main economies effected by the UKs decision to leave the EU: this part will analyse the trade partnerships the UK has with world economies and including Commonwealth countries, The European Union, the United States of America (USA), I will analyse the effect of Brexit on the UK and trade partnerships with the EU and how Other countries will be affected, maybe Brexit will bring more countries leaving partnerships or unions (Scottish independents, Irish independents) maybe Brexit will bring stronger relations with the US and how current US politics will bring UK and US closer. Answer a question of how US and UK relations might bring new partnerships and agreements that might bring better insights for post Brexit. And how Donald Trump as the USA president affecting trade and negotiations or Trumponomics as this may be referred as.

The goals will lead through the Thesis and some will of course be adapted for the work, the level of uncertainty of the government will definitely have key role for the work, the consequences on trade, financial outcomes of Brexit the GPB. Overall this will help the main topic of this work which will be to examine the effects of Brexit and come to conclusions which will inevitably lead to the evidence of Brexit and my own suggestions for post Brexit. I also will look at how close ties with the EU effected the UK for further trade with other nations leading to the main goal of my thesis which is to investigate the impact of Brexit on UK' economy with the emphasis of the financial industry.

2 History of the European Union and United Kingdoms' integration

The United Kingdom (UK) a nation with European belief and values where the British foreign policy has always been dedicated to pursuit of freedom, equality and peace, ideals that was so nobly and eloquently perused by Sir Winston Churchill. In his 1946 speech at the university of Zurich addressed to the academic youth, the prime minister, after the shock of the second world war behind Europe stated "*There is a remedy which … would in a few years make all Europe … free and … happy. It is to re-create the European family, or as much of it as we can, and to provide it with a structure under which it can dwell in peace, in safety and in freedom. We must build a kind of United States of Europe*." (European Commision) Although the UK was not one of the founding member of the European Union (EU) it played a vital role in the development of the EU as we know it today. It is important to understand the history behind the establishment of the EU and how the UK became a member of the as known now the EU 28, The next chapters look at the historic formation of the EU, key historic dates and the UK's accession process.

2.1 How the European Union was established

With the need to rebuild after the atrocities of the war, Europe had to rebuild for a better, more integrated part of the world with economic wellbeing, freedoms and the mentality of a single mega nation where the view of many become one, thus in May 1948, The Hague Congress took place with more than a thousand delegates from 20 European nations came in favour of establishing a European assembly in which the UK took part in the negotiations for unification of nations.

This European ambition which was advocated by Churchill, has in tern lead to the establishment of the Council of Europe in 1949. (Council of Europe) as a separate organisation, however this is the first part of integration to the EU as no country can commit to being a EU member without joining the council beforehand. Following the successful negotiations, the then French minister of foreign affairs Robert Schouman proposed the

European Coal and Steel Community (EEC), the community was established in 1951, member countries including Belgium, France, Germany, Italy, Luxemburg and the Netherlands the full agreement came into force on the 23rd July 1952. Following the meeting in Messina in 1955 the six members agreed to extend the European integration to one economy as whole and in 1957 the European Economic Community was born with the European Atomic Energy Community (Europa)[1], the establishment of the EU were slowly forming however without the say of the British and it would be a few years before UK was under any consideration of joining any agreements.

During the Stockholm convention on the 4th January 1960 and at the incitement of the UK, the agreement came to terms to the establishment of the European Free Trade Association (EFTA) which compromised of "*European countries not as yet part of the EEC for which the UK applied for membership in 196"*. (the Guardian , 2016) However, UKs' chances of joining the EC were vetoed by the French government, this was a dispute as the UK was and is historically connected to the United States of America (USA), on the other hand the UK had great links between the USA and continental Europe, which will be seen in the decades to come, this come in greatly as the UK is a good trading platform between the two continents.

It wasn't until 1973 until the UK join the European community with Denmark and Ireland to form a now much larger much more reformed and managed community of countries. Following years of much needed negotiations and memberships the EC has singed the Schengen agreement which is aimed at removing borders within mainland Europe in the year 1990, some countries however have excluded themselves from the Schengen area such as the UK who decided to keep their sea borders with mainland Europe, and this might be an area of interest for the UK's government following the 2016 Brexit vote.

More significant events took place during the years 1991 and 1993. In 1991 the treaty of Maastricht was adopted by the council "The Maastricht European Council" on European

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[1] Europa. (n.d.). *Key dates in the history of European integration.* Retrieved 01 18, 2018, from europa.eu: http://europa.eu/abc/12lessons/key_dates_en.htm

Union. It placed the basis for common foreign and security policies, closer cooperation on justice and home affairs and the creation of an economic and monetary union, which included a single currency the Euro again some countries were exempt from changing to their homes currencies and have stayed with their monetary bases, the UK kept the Great British Pound (GBP). The multi-governmental cooperation in these fields added to the existing Community system thus creating the European Union (EU). "*The EEC is renamed the 'European Community'*" (EC) (Europa).
After more negotiations, Euro adaption and memberships of such eastern European countries such as the Czech Republic, Poland and lastly Romania and Croatia have developed the once small idea of inter-nation communication, trade and common law adaption has built the EU to a mighty 28-member state power house. Some of the top politics and economic leaders belong to the EU they decide the future of economic stability, trade negotiations and freedoms that its citizens have. The Euro is controlled by the European Central Bank (ECB) which some could argue is not so great for the less wealthy smaller nations as do control their own monetary policy however the ECB controls price levels floating around the 2% mark to avoid deflation.

On top of the price levels the ECB also controls the money supply the Euro zone has and the Interest rates of all 19 countries that share the common currency. Statistics show that the Euro didn't not fare well compared to the GBP during and after the economic crisis of 2008 and ongoing sovereign debt crisis might put the whole Euro system at risk as a battle for a fiscal union ongoing which is seeking to give power to EU to control national budgets. (Economics Onlne , n.d.)[2]

[2] Economics Onlne . (n.d.). *European Monetory Policy* . Retrieved 01 18, 2018, from econmicsonline:

2.2 The history of the United Kingdom's membership in the European Union

The June 23rd, 2016 was not the only referendum the UK has had, there were other plans to vote for a leave or remain ballot on the 7th June 1975, the majority voted Yes - 17,378,581 people (67.2 per cent) - to remain in Europe. (Nelsson, 2015)[3] Further comparison of the votes are not deemed necessary as the June 2016 vote is one under investigation in this paper.

Some key historic dates of the UK and the EU would be right from the beginning of the application proses where in 1963 French President Charles de Gaulle vetoes British entry into EEC[4] (Barber, 2007) and again in 1969 where the French president vetoed a second British application. (UK Parliament, n.d.)[5]

As mentioned in the previous chapter the UK didn't adapt to the Euro and kept the sovereign state GBP meaning it kept its monetary policy and banking systems, it also kept its border his was an attempt to easy immigration and to keep the independency of migration flow. The migration analysis and a full financial analysis will be written more in the depth in the following chapters of the paper, as an in-depth and detailed analysis is needed for the financial section of this work where the full comparability and outcomes will be analysed following financial and macroeconomic models.

One of the claims is that the UK is sending too much of its capital to the EU and figure argued was stated that it was over £350 million, however the actual figure is nowhere as

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[3] Nelsson, R. (2015, 06 05). *Archive: how the Guardian reported the 1975 EEC referendum*. Retrieved 01 16, 18, from The Guardian online: https://www.theguardian.com/politics/from-the-archive-

[4] Barber, T. (2007, 12 12). *Financial Times*. Retrieved 01 17, 2018, from ft.com: https://www.ft.com/content/91c025da-a967-11dc-aa8b-0000779fd2ac

[5] UK Parliament. (n.d.). *Key Dates: UK Parliament and teh EU* . Retrieved 01 18, 2018, from http://www.parliament.uk/about/living-heritage/evolutionofparliament/legislativescrutiny/parliament-and-europe/key-dates/

close, another analysis that will further appear is the argument of immigration levels to the UK from member and non-EU member states, as these are economic variables that have an impact on UK sovereignty and economic wellbeing full figures of taxes, foreign direct investments (FDI) will need to be taken into consideration. One thing that is clear that the two referendums held were no different to each other, but I would say it's different as the UK adapted to new laws and beliefs it has fully integrated to what Europe is known for today, a tough task lies ahead of the governments both the EU and UK as countries generally want to join the all member states to achieve economic well-being and European beliefs and no member as of yet exited or has planned to take such a step. Uncertainty is still a very talked about subject even after the two years from the referendum.

2.3 Article 50

I deem it necessary to understand the steps that the UK has to take after the 2016 vote and the triggering of Article 50 was one major initiative the UK had to take in-order to peruse its exit from the EU. As stated thus far the EU began its debut in 1957 as the European Economic Community (EEC), created to foster economic interdependence among members in the aftermath of World War II. Following the expansion of 1973, the EU was formally created by adaptation of the Maastricht Treaty held in 1992, by 1995 the bloc had expanded to 15 members covering Western Europe. From the years 2004 to 2007, the EU had its largest expansion recorded, which took on 12 new members and included former Communist states like the Czech Republic.

With a point of view to enhance democratic legitimacy, efficiency and improved coherence for actions of the EU the Lisbon treaty was created, signed by all 27-member states in December 2007 it came into effect in December 2009. The treaty is divided into two parts: The Treaty on European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU). It has a total of 358 articles in total which outlines the regulations and coherence all member states adhere to (the lisbon treaty , 2007). Article 50 of the Lisbon

Treaty outlines the provisions under which a country can leave the EU. Below is the text from article 50 taken from the Lisbon treaty website.

1. Any Member State may decide to withdraw from the Union in accordance with its own constitutional requirements.
2. A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.
3. The Treaties shall cease to apply to the State in question from the date of entry into force of the withdrawal agreement or, failing that, two years after the notification referred to in paragraph 2, unless the European Council, in agreement with the Member State concerned, unanimously decides to extend this period.
4. For the purposes of paragraphs 2 and 3, the member of the European Council or of the Council representing the withdrawing Member State shall not participate in the discussions of the European Council or Council or in decisions concerning it.

   A qualified majority shall be defined in accordance with Article 238(3)(b) of the Treaty on the Functioning of the European Union.
5. If a State which has withdrawn from the Union asks to re-join, its request shall be subject to the procedure referred to in Article 49.

(EEPA, n.d.) EEPA Europe External Policy Advisors

Article 50 should be delivered by Mrs May the current prime minister of the UK will see that Britain leaves the European Union in March 2019 with or without a deal, however this has been under scrutiny with many politicians and economic figureheads suggesting that the economy of UK will crumble if the two cannot come to agreements and even suggesting that article 50 to be delayed, and many asking for a second vote on the referendum. The financial times stated in an article written by a former UK deputy prime minister that extending the "*March 2019 deadline would be the best alternative to a no deal Brexit*", (Clegg, 2018). A number of protests organised by the remain campaign have also been held to show support for a UK with Europe, however this unclear whether the government will have any say in the close future to the March 2019 deadline. The indecisiveness of the prime minister has doubt her as Theresa Maybe by the economist online (The Economist, 2017) and the indecisiveness follows to this day, as a British expat with some of my income coming from the UK I am currently living and working in the Czech Republic, I have noticed a significant change in the lifestyle now, to what it was a few years, before the vote, when the pound was stronger and the economy was on the rise, this has changed, as the pound has fallen drastically, with noticeable change. I will study these effects further in my thesis with economic and financial backings, I will also write some of my experiences which I have had going through Brexit whilst living away from Britain.

3 The Brexit Negotiations

"Not partial membership of the European Union, associate membership the European Union, or anything that leaves us half-in, half-out." British Prime Minister Theresa May Speaking at Lancaster house in London, (Dallison, 2017)

As it is up Mrs. May and her army of politicians and advisors to negotiate an exit deal with the EU that's beneficiary for the UK. And with the uncertainties surrounding the fact that a deal is yet to be reached, it is becoming clearer that, Brexit has been built on the power of delusion and targeted misinformation, the fact that Mr. David Cameron has resigned from office soon after the results of the Brexit vote showed the politicians willingness to carry the burden of what was about to begin, therefore it is up to the new holder of such power to deliver.

As the deadline for a deal with the EU looms closer, the bargaining power of the UK weakens and so if the two parties cannot come to agreements, it looks more likely that a no deal, exit, is more likely, but what does that mean? Not only for the UK but also the EU and what does a no deal lead to. In this chapter I aim to examine the possibilities of Brexit and how these will affect the parties on the opposite sides of the negotiations. As there are many legally and economically binding agreements that have to agree to and, thus carefully examined by the governments, however the terms of Brexit can be defined by two variables, in a way a sort of divorce would, reach an agreement or to not reach an agreement, a soft Brexit where a deal is reached and agreements such as the customs union and single market are agreed to, on the other hand a hard Brexit, where no deal is reached and Britain's departure is that, no agreements are carried forward and Britain would not be bound by any EU treaties. In the next subchapters I shall look at the two scenarios of Brexit as this will help me further in my analysis and give a deeper understanding of the affairs surrounding the negotiations, though as no agreement has yet been reached, the current government have a number of months to deliver on promises.

The seriousness of the Brexit vote wasn't taken much into account by the British public nor the rest of the world, as no one could predict such a result (Jackson, 2016). However, in practice, the leave campaign made great gains by drawing attention to the dangers of immigration as a consequence of the UK's open border to the rest of the EU. Brexiteers known as the voters for the leave campaign also highlighted the democratic deficit of the EU institutions, advocated freedom from EU bureaucracy and regulation, championed UK freedom to negotiate trade deals on its own terms and pointed to financial savings to be made by leaving. This has brought forward a great increase of nationalism in the UK and the attention of far-right political parties who back a no deal Brexit.

The Remain campaign was singularly focused on the catastrophic economic losses that would follow a UK withdrawal. Remain campaigners also argued that the benefits of EU membership far outweighed any loss of sovereignty these benefits included the freedom of movement and the ability of the "*EU to regulate the excessive or unfair profiteering activities of global corporations"* (Jackson, 2016). With many uncertainties following the Brexit, questions arise weather article 50 will be delayed to a more stable time or when these uncertainties are much clearer and well planned by the current government and ministries of the United Kingdom.

Although UK's new prime minister said: "Brexit means Brexit" (Cowborn, 2016) and she will respect the will of the people, nowadays, six months after the UK voted YES to leave the EU and two months before the expiry of her self-imposed deadline to trigger Article 50, the new UK-EU economic and trade policy remains unclear.

At this stage, so many crucial questions for both, the British and the world financial system have not been answered yet. Is the UK only leaving the European Economic Area (EEA) while maintaining full "passporting" and regulatory "equivalence" that allow access rights to the Single Market? Or, on the other hand, will the UK abandon the EU Treaties and the Single Market becoming a "third country"? I will need to break down some key terms to give some context before moving forward and explaining the main possible scenarios:

Third Country: A country that is outside the coverage of the EU treaties, consequently is not bound by them. Once a third country in the views of the European Economic Area (EEA), the UK will not be able to stand to the Court of Justice of the European Union, having severe consequences to regulatory equivalence and passporting rights.

Passporting: As a member of the EEA that must abide to EU legislation, it allows the transfer of services without any need for extra authorisations from other EEA countries. These other Member States have limits to the amount of regulations they can impose to other members of the EEA, although these “passport rights” are yet to reach third country firms.

By becoming a third country, the UK loses priority to other EEA countries, to what the single market is concerned. As a third country, the businesses between the EEA and the UK see their passporting rights abolished, as well as other perks that cover the EU treaties and legislations such as the freedom of establishment and the freedom of services.

Equivalence: Recent regulations from the EU allowing non-EEA firms to get their services across to the EEA once provided their home country regulatory regime is “equivalent” to EU standards. Equivalence is both limited and may require additional conditions and reciprocity. This regime can also be withdrawn at any given time if the third country wanders from the EU standards it agreed to follow. As there are two possible ways the Brexit can be executed, having different effects for both the UK and the EU economy:

In first end of the spectrum we find the high access scenario (or often described as “soft” Brexit). In this scenario, the UK keeps regulatory equivalence to a variety of European legislation despite new agreements will be needed where provisions do not exist.

As for the low access scenario (otherwise known as “hard” Brexit) the UK becomes a third country towards the EU, with no regulatory equivalence, imposing constrains and restrictions to the EU-UK massive web of financial services.

There is still a relevant half way point between the two extremes. In this complicated middle point, where the UK becomes a third country that abides by laws and regulations where provisions are made to grant equivalence to third countries, giving UK based firms access to both EU clients and specific products and activities. Some provisions already or soon to be in place for financial services include: European Market Infrastructure Regulation, Markets in Financial Instruments Directive II (MiFID II), Solvency II (SII), Payment Services Directive II (PSD II), Alternative Investment Fund Managers Directive (AIFMD).

The Brexit divorce bill will be paid by the UK into, "*EU's budget for the 2019 and 2020 a total of between 40bn to 45bn euros as published by the financial times December 2017"*, (Brunsden, 2017) the article also shows that some terms of were reached in case of the payment and citizens living in the countries, not all the effects of these negotiations were in fact present and as of yet no deal is reached, I deem it necessary to look at the examples of Brexit being proposed and will look for the differences between a no deal and a soft Brexit, however, there may also a number of other options to take and which might involve a second referendum, a vote of no confidence on the prime minister or to take a timely option and to postpone march 2019 exit date, a second referendum although very doubtful of this happening is now backed by campaigns and as recent polls show people are leaning towards a remain vote, also, the leave voters are changing minds as the worse of Brexit is still to come.

A poll of 20000 people carried out by Survation was the biggest public survey on Brexit of its sort since the referendum, using the methods that helped the few pollsters who predicted a hung parliament at last year's general election correctly (Payne, 2018). The poll found that in another referendum on Brexit, 54% of people would vote for the UK to stay in the EU, while 46% of people would vote to stick with the 2016 decision to depart (Payne, 2018). As the voters are now swinging towards remain the idea of Brexit of hitting hard not only the economy but also business and financial institutions the wellbeing of the UK hangs in the balance of the politicians and the deal making abilities.

3.1 Soft Brexit

A soft Brexit, a term used to define that UK's relation to the EU would be quite close and the main objective of a soft Brexit would be, to keep its close ties, minimise disruption to any trade, supply chains a as to business in general between the two, this option will also reduce the cost to Brexit as it would be derived from EU's regulations and standards. In practice a soft Brexit means staying within both the EU's single market (like Norway) and its customs union (like Turkey). Soft Brexiteers are willing to be bound by EU rules and tariffs of the bloc even though Britain will lose any say in making them. They also accept the inevitable consequence that it will be hard, even impossible, for Britain to do any trade deals with third countries (J.P., 2018) The soft Brexit approached is preferred by the stay voters as it would mean in some ways that the connection will be there. However, as the fear of having no deal so is the fear of not having a say in the rules and regulation the UK would have to adhere to.

3.2 No deal Brexit

A no deal Brexit or as otherwise called "Hard Brexit" proposes to reject the idea of close alignment with the EU as the goals of a hard Brexit is to escape the burdensome EU tariffs and its regulations, so as to be able to draw up rules and customs arrangements of Britain's own choosing, which would be beneficial for the UK. In practice a hard Brexit means leaving both the single market and the customs union. Hard Brexiteers believe that staying in either would turn Britain into a "vassal state" of the EU. They are willing to accept the short-term disruption and potentially high costs of breaking free from Brussels, because they believe that the long-term gains from better regulation and the striking of free-trade deals all round the world will offset the potential loses. (J.P., 2018). Some key elements of hard Brexit, are that it would also give Britain more control over its borders and immigration levels, It could however cause more economic damage to both the UK and the EU but supporters think this would be worth it for the country to be able to then draw up its independent trade agreements, (Finnis, 2018) as they deem it to be potentially more profitable and beneficial in the long run for the economy and British lifestyle. The Prime Minister has said that she intends to “take back control” over the country’s borders and laws which aligns with a hard Brexit. But she has also agreed to a transitional period which would see the UK still bound by certain rules and regulations (Finnis, 2018).

As the politicians are fighting for a hard Brexit many warnings are coming under their way. A warning from Ross McEwan the chief executive of the Royal bank of Scotland (RBS) warned that a no deal Brexit could tip the UK economy into recession, in his statement to the BBC a "bad Brexit" could result in "zero or negative" economic growth which would hit RBS's share price. He also said the bank was becoming careful about lending to certain sectors of the economy - particularly retail and construction. RBS is still 64% owned by the taxpayer following its bailout 10 years ago. Mr McEwan said: “*We are assuming 1-1.5% growth for next year but if we get a bad Brexit then that could be zero or negative and that would affect our profitability and our share price*.” (Jack, 2018). We are nearing the final months of the negotiations and the effects can be seen since beginning, having a weak pound and many uncertainties surrounding the full effects of Brexit, hence my aim for my thesis paper, would be to research these effects and come to my own conclusions, these will be written in more detail further in the research study.

3.2 The other side of Brexit

Rather can concentrating on the option shown, I would also like to look at the other sides of the story, and therefore have a much more of an overview of what is exactly is happening and the option that may be considered, so this chapter would look at the options such as; the postponement of Brexit’s march 2019 deadline and therefore extend article 50, other options for postponing or extending the Brexit deadline could be a second referendum in the UK, or imposing a vote of no confidence as the government ability to deliver a fair Brexit hangs with no agreement yet reached the deadline is just month away.

A vote of no confidence in the prime minister (PM) is as that it requires a politicians vote to trigger their disapproval in the current pm for them to be removed from power, Under current rules, 15% of Conservative MPs must write to the chairman of the 1922 Committee, Sir Graham Brady, to call a vote of no confidence, that means 48 out of 316 Tory MPs need to back the motion, with the committee then deciding whether or not to hold a vote. Motions of no confidence can also be triggered by the opposition, but they usually have little chance of succeeding (Sky News, 2018). However, even after the resignation of top politicians which include foreign secretary Boris Johnson and Brexit secretary David Davis which prompted the talks of a vote of no confidence, I believe that a vote of no confidence would not gather enough members of parliament (MPs) signatures for this to happen, a vote also did not occur during the Tory conference between September 30 to October 3rd 2018, it would not happen any time before the Brexit deadline, and is such event did occur it would have a significant impact on the British economy if Brexit went ahead afterwards.

Another option that the UK would be looking at would be the postponement of article 50 and the Brexit deadline altogether, as published by the independent newspaper, European Council showing preparations for a delayed Brexit addressed. And have discussed to what will happen to the UK's seats in the European Parliament, which are set to be partly distributed between other member states at the body's next elections scheduled for the end of May (Stone, EU making preperations for possibility of Brexit being postponed, 2018).

under EU treaties if the UK is technically a member it would have to participate in EU elections which it has not been in preparation for such outcomes and are certain on the departure from the EU. The paper also states that "*In the event that the United Kingdom is still a member state of the union at the beginning of the 2019-2024 parliamentary term, the number of representatives in the European Parliament per member state taking up office shall be the one provided for in Article 3 of the European Council Decision 2013/312/EU1 until the withdrawal of the United Kingdom from the union becomes legally effective*," the European Council plan says. It continues, adding that the plan to redistribute the Members of European Parliament (MEPs) will come into force midway through the parliamentary term if and when Britain ultimately leaves the bloc (Stone, EU making preperations for possibility of Brexit being postponed, 2018).

If the two sides do fail to reach a final exit deal and the talks are not extended past the departure date or that Article 50 is not revoked, Britain would crash out of the European bloc without any transition period and go straight to trading on WTO terms, which could in fact consequentially start a massive economic crisis compounding on the on-going political implications. It is however more likely that no deal Brexit would occur as the governments cannot come to terms and such news would become clear at the later stages of the negotiations, on the other hand, these talks should happen in my view before the end year 2018 which would give 3 months for some agreement on the terms of extension. However, concentrating on the economic and financial implications, I will concentrate my studies on a no deal or a deal Brexit, as the implications of extension are extremely uncertain and a vote of no confidence highly unlikely, I will show these studies in the further chapters of my thesis, where I can give a broader view of the implication that is awaiting post Brexit.

With the budget vote the being an important talking point in way of Brexit the talks have begun to take hold once more, the budget has been delivered by chancellor Philip Hamond, in his statement he mentioned some key figures including that the 2018 growth forecast "*downgraded to 1.3% from 1.5% in March*", due to impact of bad Spring weather (BBC, 2018), however it is timely to say as the forecast for 2019 in time with the exit date raised "*from 1.3% to 1.6% and annual forecasts raised to 1.4%, 1.4%, 1.5% and 1.6% in 2020, 2021, 2022 and 2023 respectively*" (BBC, 2018), these figure presented are quite optimistic as I will further study the effects of Brexit will have.

Other figures to consider as stated by Mr Hamond are as follows; Public borrowing in 2018 to be £11.6bn lower than forecast in March, representing 1.2% of gross domestic product, (GDP) the total value of goods produced and services provided, Borrowing as a share of GDP to rise to 1.4% next year, Borrowing to total £31.8bn, £26.7bn. £23.8bn, £20.8bn and £19.8bn in next five years, Debt as share of GDP peaked at 85.2% in 2016-17, falling to 83.7% this year and to 74.1% by 2023-24 and 1.2% annual average growth in departmental spending promised (BBC, 2018). Back to the Brexit topic he also pledged an Extra £500m for the preparations for leaving the EU (BBC, 2018). In later news the Brexit secretary Dominic Raab has planned a deal to be made by November 21 2018 as the negotiations take place for gearing up once again, this has some effect on the pound, which has eased in recent weeks caused by jitters around the lack of a deal with the EU, it was trading a cent up against the dollar at $1.28 on oct 31 2018 (Allegretti, 2018), as I continue to examine the effects of Brexit, the pound or (GBP) is of great interest as the fluctuations surrounding it has changed its strategies closely related to the Brexit negotiations, the financial and the economic effects of Brexit are further examined in my thesis paper.

The leave campaign was criticised for their claims for most aspects of their marketing, especially the 350 million they claimed as payments to the EU and if Britain votes leave, this public money can be sent to the NHS as funding is desperately needed. As it was claimed by the then Foreign Secretary Boris Johnson, A campaign bus used by Vote Leave, including Mr Johnson himself, during the referendum campaign was emblazoned with the slogan: "We send the EU £350 million a week - let's fund our NHS instead" (BBC News, 2018). Another claim came conservative MEP Daniel Hannan who stated that "*Absolutely nobody is talking about threatening our place in the single market*" (Stone, INFACTS Brexit lies, 2017), these claims proved to be untrue as the true figures were much less, and the fact that if the Britain leaves the EU it would also essentially leave the single market.

In more recent news Lord Alan Sugar Speaking in the House of Lords, asks that if the rules that govern City businesses were in place for the EU referendum, Boris Johnson and Michael Gove would be prosecuted for claims made during the EU referendum campaign. They both deny any wrongdoing (BBC video, 2018). During the summer of 2018 Boris Johnson has resigned from his as the foreign secretary over disagrees with Mrs May's Brexit policies. (BBC, 2018). The claims arising will not have an impact on Brexit, as the governments are pushing for an all exit, however there is of yet no plan for a Brexit deal and talks are still ongoing with a great deal of indifference and a huge decrease of public trustworthiness, there is great pressure on the government to produce a deal where the economy of the UK not face recession or cause a financial crisis, as claimed there are also a number of financial institutions which plan a move of operations if there is a no deal Brexit.

The Brexit news continue to flow and with the dangers of a no deal Brexit starting to kick in more politicians have resigned in recent times due to the uncertainties of what is about to happen, in more recent resignations was the transport minister Jo Johnson "*who has warned that the UK faced a choice between "vassalage" under her proposed deal or the "chaos" of crashing out of the EU"* (Cochrane, 2018). This come after the Brexit secretary has admitted that the UK is reliant on the ports countries in the EU for trade in goods he stated that "I hadn't quite understood the full extent of this, but if you look at the UK and look at how we trade in goods, we are particularly reliant on the Dover-Calais crossing." (Sparrow, 2018), his comments have caused a backlash of criticism and has once again caused Brexit uncertainty, Jo Johnson has also called for a new vote to be carried out amidst the uncertainty.

In news closer to Europe, Brexit may be cancelled, and a case will be heard by the European Court of Justice, this can happen without the approval of other states. "Luxembourg justices will sit on November 27 to hear the "*Wightman case*" from a Scottish court after anti-Brexit politicians sought clarification on Article 50 of the EU treaty" (Charity, 2018), The news comes as Theresa May faces tense backlash over prolonged negotiations, which have hit a stalemate on the issue of an "Irish backstop", Establishing that reversing the Brexit process can be done without the approval of other EU states could, argue those who brought the case, boost remainers' argument that British lawmakers should block the withdrawal before it happens on March 29 (Charity, 2018). This however seems highly unlikely as the British government is dead set on the UK leaving the bloc, on the other hand a postponement can happen if no deal can be reached, which would beneficial, and help in negotiations but for this to happen the government need a rethink on their actions. The amount of tension and backlash against Brexit is still uncertain and as companies and big financial institutions make plans to move operations out of UK, I will investigate these claims further in my thesis and the amount of damage this can do to the UK economy and its financial industry.

November 14, 15 and 16 2018, has been a tough time for the current government and Brexit negotiations as a preliminary (draft) deal was being agreed and put to the vote in parliament many politicians have disagreed with the draft deal put in front of them which contains some 585 pages (CNN , 2018), although backed by the cabinet the deal was severely rejected by major Brexit politician and has seen the resignation by more than 7 MP's in those two days including the Brexit secretary Dominic Raab who stated that he cannot support the agreement where the EU holds an veto over the UK's ability to exit the union (BBC, 2018), he was quickly replaced by Stephen Barclay (Maidment, 2018).

Following the disaster of delivering this draft deal has seen the pound plummet against the EUR and USD with reuters reporting the fall of sterling by 1.8 percent against the dollar [GBP/] - Against the euro, it was down 2 percent, its biggest fall since shortly after the 2016 Brexit referendum (Reuters, 2018). Shares in Royal Bank of Scotland were down 9.6 percent, their biggest one-day fall since the June 2016 referendum. "*Barclays and Lloyds Banking Group dropped 4.1 and 5.0 percent respectively"* (Reuters, 2018). '*The stock markets also took a huge hit with the FTSE 250 down 1.3 percent'* (Reuters, 2018). Britain's financial services industry greeted the draft agreement with weariness and worry, spooked by a political revolt that could topple the government and bring fresh troubles to a sector already reeling from upheaval (Reuters, 2018).

The leadership of Mrs May was also challenged by her fellow colleagues with more than 20 submitting the letter of no confidence to the chairman of the party's 1922 Committee, Graham Brady, a vote is triggered if 48 Conservative MPs "*15 percent of the total*" submit the letter (Reuters, 2018), this will cause more chaos in an already unstable environment. Comments from the side of the EU state that they a readying for no Brexit as the UK can have a second referendum which is backed by the majority of the population after the news, however this is highly unluckily, and the likeness of the draft deal being reformed has also been disagreed by main EU leaders.

4 The United Kingdom's financial services industry

The UK and more precisely the City of London have a prolonged financial importance and history for both, the UK economy and the European governments. As London features a diversified portfolio of financial and investment market companies of all forms and experts of extensive fields, this in act dubbed London as a word leading global financial centre, it is home to some of the world's biggest and oldest banks to a wide arrangement of companies of financial and investment services like bonds and futures It is the place where the majority of wholesale finance takes place.

Also, as one of the most visited places on earth it is the most prominent places for trade and business and well known for its foreign exchange and bond trading as well as insurance services. The UK is also the home of the London stock exchange (LSE) which the largest stock exchange in Europe, the London metals exchange (LME) and the prominent the London bullion market that is managed by the London Bullion Market Association (LBMA), which is the world's largest location for gold and silver (precious metals) wholesale (over the counter 'OTC') trading, and the key organisation for standardising the purity, provenance of the precious metals and the way they are traded (LMBA, 2018).

The UK's central bank the Bank of England (BoE) is the world second oldest bank operating from London since 1694, nationalised in 1946 after ww2 (Bank of England, 2018), to maintain monitory and financial stability the parliament has given powers to bank through legislation, this also gives the power to of the government to decide on the governor of the BoE, the bank controls the monetary system and regulates the issue of currency notes in the country.

4.1 European Presence in the UK

The EU also benefits from the strong worldwide financial position of the “City of London”. To have London on their doorstep provides European governments and businesses with easy and fast access to the global markets and top financial expertise of the UK’s top institutions some examples are Slovakia Debt Management Office uses the UK banking system as primary dealers for its bond issuance. Another example of this beneficial relationship for both parties is how UK helped SAREB, the bad bank of the Spanish government, managing and selling its asset portfolio (City of London Corporation, 2016).

The UK’s financial institutions also manage a number of European client’s assets, the amount of assets under management (AUM) is around the 35 per cent mark or nearly £1.8trn of Europe’s investments, the UK asset management industry remains the European leader and is larger than the next three countries which happen to be Germany, France and Switzerland combined (Esnerova, 2018), who are also leaders of financial expertise and professionals in major fields, just so happens that the UK is a connection to a more open platform between professionals. Investor association (IA) chief executive Chris Cummings stated recently “The clear value the European market brings to the UK asset management industry underlines the urgent need for a Brexit deal to be completed by March 2019 which protects our industry, and more importantly, the savings of millions of people right across Europe” (Esnerova, 2018). This shows the importance of a deal being made as the UK will stand to lose EU holdings in the future and may cause instability of trustworthiness of UK’s institutions, as has already caused a number of firms move operations to inland Europe. Not only European holdings are under treat in the UK, there also a number of US firms that threat to leave operations in the UK for Europe.

5 The UK Economy

The analysis of the UK's balance of payments presents a broader view of the position of the UK economy in the world. By doing so, it will provide with a better understanding of the economic relationship between EU-UK and, thus, it will help answering the following questions: Is the EU the most important UK's trade partner? Which is the actual tendency, is the UK and the EU drawing closer together or the UK is becoming less dependent on the EU?

The answer of these questions will not show a final and accurate economical aftermath of the Brexit, as there is still a huge level of economic policy uncertainty and the reaction of foreign direct investors is unknown, although, businesses investment declined by 2% in the last quarter of 2015 (Rafal Kierzenkowski, 2016). However, by knowing the tendency and weight of the EU in the UK's balance of payments, it is possible to foresee if a "hard Brexit" would have a relevant effect in UK economy and the Pound. Following there is an analysis of the main components of the UK's balance of payments.

5.1 The balance of payments

The balance of payments (BOP) is an important aspect of a country's financial wellbeing. The BOP measures the economic transactions of the UK with the rest of the world, these transactions can be broken down into three main accounts: the current account, the capital account and the financial account, the accounts shows how healthy the accounts are, BOP shows whether a country saves enough to pay for imports, it also reveals whether the country produces enough economic output to pay for its growth.

A deficit in the BOP means that a country imports more goods, services and capital than it exports, therefore it must borrow from other countries to pay for its imports, this fuels the economic growth in the short term, in the long run having deficits the country may have to go into debt to pay for consumption and may have to sell off its assets to pay its creditors, these assets include natural resources, land, and commodities instead of investing in future growth.

A surplus in the BOP, the country exports more than it imports, the government and residents are savers and provide enough capital to pay for all domestic production and might eventually lend outside the country.

In the short term a surplus boosts economic growth as it will have enough savings to lend to countries buying products and services this increased size of exports boosts production and lowers the unemployment rate as people will have more job prospects.

In the long run dependency on export driven growth may be proven problematic, an incitement for residence to save less and spend more should be encouraged as a large domestic market will protect from exchange rate fluctuations and by using the home market this will encourage companies to develop its good and services further.

For my thesis it is important to look at these accounts of the UK to be able make assumptions and predictions for post Brexit state of the economy.

5.2 Current Account

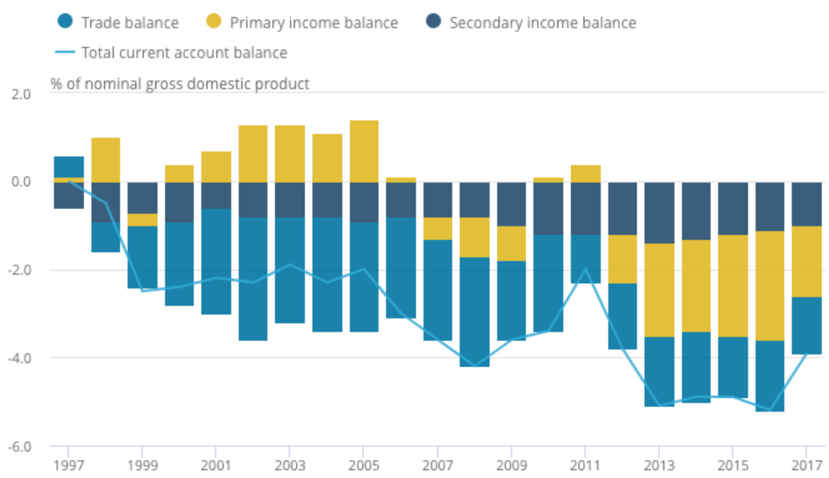
The current account (CA) measures trade balance and also the effects of net income and direct payments, the account is in balance when the said country's citizens provide enough income and savings to fund activities including purchases and usage of services, business and government infrastructure spending.

A deficit in the CA occurs when spending on imports exceeds the level of saving, to fund this deficit the country can turn to lenders who are oblige and provide the funds as they will profit from exports and a deficit can be good for both parties, however in the long run a deficit this may slow economic growth, a decline in currency which inevitably may lead to inflation occurring from higher import prices, the secondary effect of this is also higher interest rates as the government will have to pay higher yields on bonds.

The main aspect of the current account is the measure of trade balance, this itself is also a main component of BOP, the goal of a country is to avoid a trade deficit, as the UK is about to lose a main trading partner the question on the politicians minds should be how will trade be fulfilled if the UK exits without a deal, I have deemed it necessary to analyse the effects of the of the trade levels and the level of income. By analysing this closely it will give an insight of what effects Brexit will bring for the future. UK's overall debits exceed credits, in other words: the UK has a current account deficit every year since 1995 as shown in appendix B. This deficit of 5.4% of nominal GDP means that the UK is a net importer and a net borrower economy, the situation can be seen in the chart 1 below.

Chart 1

Current account balance as a percentage of nominal gross domestic product (NGDP) 1997-2017



Source: (Office for National Statistics, 2018)

All three components of the current account represent a deficit in the account. However, the catalyst of the 2015 deficit level, the largest deficit in UK history, is an all-time low primary income balance. In 2015 the primary income balance, or the difference between the returns of British direct foreign investment abroad and the returns of foreign direct investment in the UK, hit a lower record deficit of 2% of nominal GDP. The reason for this situation is a drop in the UK residents' returns from their assets abroad and stable foreign returns of their assets in the UK (The Office for National Statistics, 2016).

In other words it, ***converts the UK into a profitable market for foreign direct investors*** (FDI).

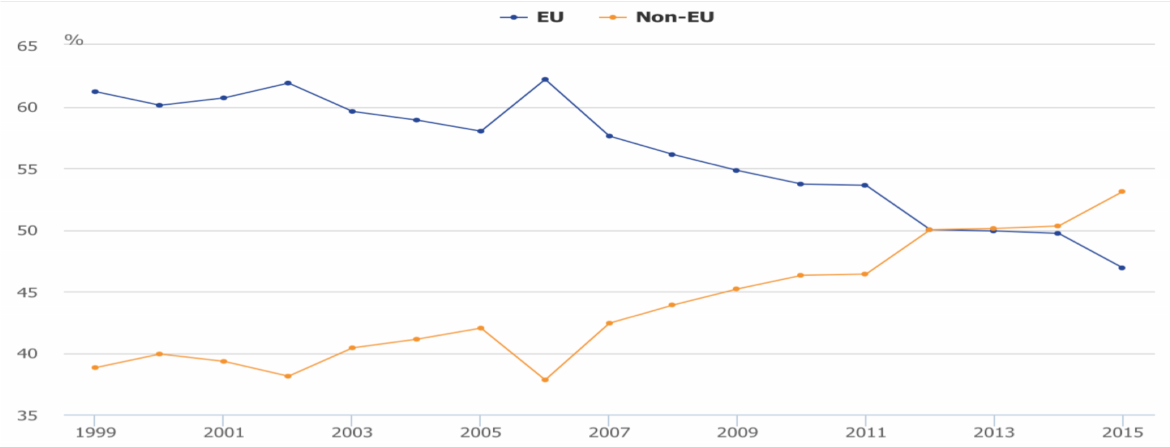
As seen in chart 1 and appendix b, the UK has been facing a deficit trade balance since 1997, however this is a deficit balance in trade in goods "*6.9% of nominal GDP in 2015*" which is partly offset by a surplus in trade in services "*4.7% of nominal GDP in 2015*", indicator of the British strength in services activities. The biggest net export industry in the UK is the financial services sector, which, due to its important position in the UK balance of payments, will be analysed in more detail. With the effects of the vote 2016 sees the gap in the trade balance widen and shows scepticism in investments.

Closer to the Brexit date shows a different story, or, a kind of calm before the storm. Looking at the chart for 2017 The UK current account "*deficit narrowed in 2017 to 3.9% of nominal gross domestic product (GDP) from a record 5.2% in 2016, the narrowest deficit since 2012"* (Office for National Statistics, 2018).

The chart 2 shows the value of UK exports of goods and services to the EU and to non- EU countries. In 2013, exports of UK goods to non-EU countries exceeded UK exports to the EU. This scenario is a direct result of the financial crisis in 2007 and the uncertainty in the euro area in 2012. And, thus, it shows an increasing economic power of UK non-EU trading partners over EU partners.

Chart 2

Value of UK exports of goods and services to the EU and to non- EU countries



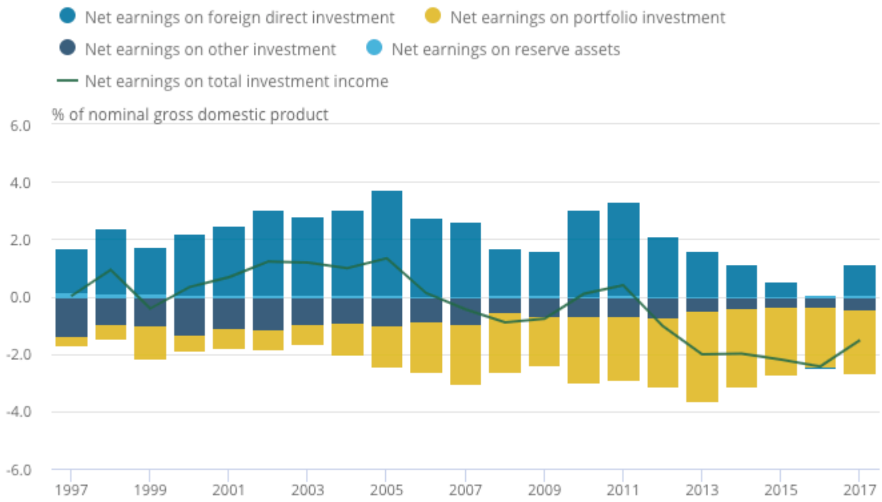
Source: (The Office for National Statistics, 2016).

As a result, the UK trade balance with EU countries is worsening and the deficit has expanded further. In 2015 the deficit with EU economies stood at £69BN, this means an increase of 17.9% compared with 2014. UK's biggest deficit is with Germany, followed by France, Spain and the Netherlands (The Office for National Statistics, 2016).

With this is mind, it is easy to appreciate an increasing importance of the UK as a trading partner for the EU economies. As the former British foreign secretary, Boris Johnson said: "*the EU will have in mind safeguarding Britain's substantial imports of Italian prosecco, luxury German cars and French wine*" (Stephens, 2017).

Chart 3

Investment income balance as a percentage of NGDP 1997-2017

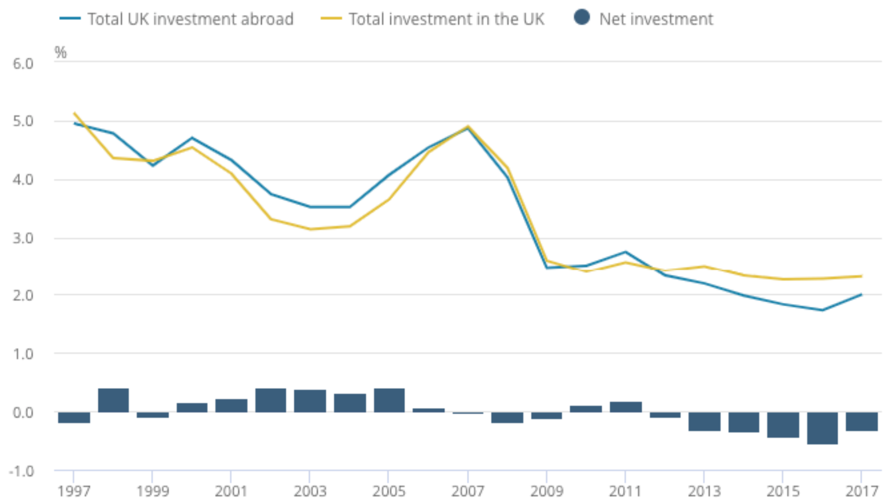


Source: (Office for National Statistics, 2018)

Chart 3 shows a breakdown of investment income, in 2017, much of the narrowing of the primary income deficit was due to increased investment income of £17.2 billion (0.9% of nominal gross domestic product), the largest improvement since records began in 1946 (Office for National Statistics, 2018). The data seen here suggests that after the Brexit date the UK will stand to lose more foreign direct investments (FDI) which can harm the economy, this will mean business will turn to new ways of investing their money and into other countries that offers investor benefits, remaining with the EU where the main source of FDI comes from is more beneficial for the economy and the recovery time of the can take a number of years to stabilise and return investor confidence.

Chart 4

Rates of return: assets, liabilities and net, percentage



Source: (Office for National Statistics, 2018)

Chart 4 above showing the rates of return agrees that the down sloping of FDI into the UK and that the net investments are widening the gap. UK investments are recovering, this is mainly due to UK businesses investing outside the country, will this counteract Brexit? It is too early to estimate exactly how many companies will invest abroad to as the hot topic at this point in time of the Brexit negotiations is to leave operations in the UK to be closer to Europe and have operation elsewhere, if the UK and EU cannot come to any agreements and the UK crashes out the economic and financial burden will be exceptional, as the tax lost from companies will also mean that the unemployment rate will rise.

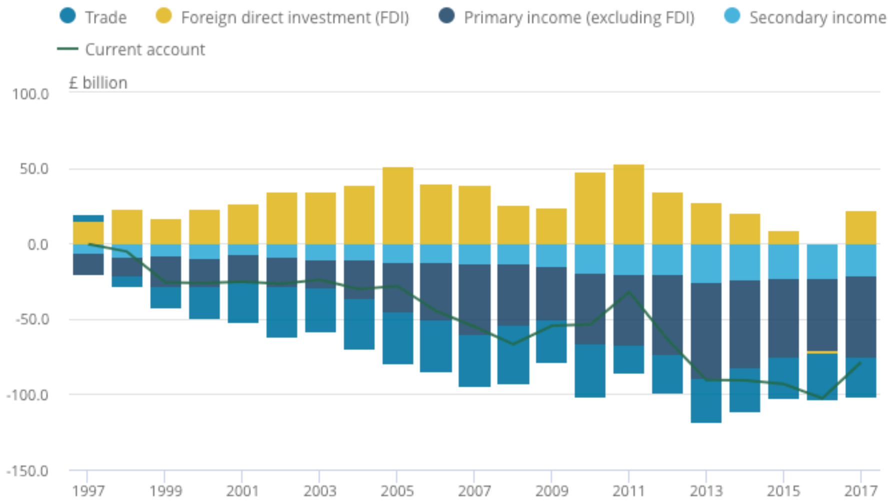
The Office for National Statistics has now confirmed that GDP growth in the UK in the first quarter of 2018 was 0.1%. the comparable data for 19 other EU countries, all of which other than Romania grew a lot faster. Austria grew at 0.7%, Belgium 0.4%, Denmark 0.3%, Finland 1.1%, France 0.3%, Germany 0.3%, Italy 0.3%, the Netherlands 0.5% and Spain 0.7%, many of which also had bad weather (Blanchflower, 2018).

Some business like Schaeffer an automotive supplier already make plans to shut down operations in the UK with the job loss of 220 (ITV News, 2018), plane maker Airbus says Britain crashing out would force it to cut thousands of jobs in the UK and move production to other countries can lead to thousands on job losses (Murrey, 2018). These are just a few companies preparing to part ways of the UK due to Brexit, the loss of capital gain will in the billions of pounds with an unpredictable time to recover unless new trade deals and offers for FDI will be negotiated elsewhere.

The balance on FDI as shown in chart 5, earnings have been in surplus in every year since 1997 except in 2016. In fact, the surplus on FDI earnings narrowed considerably in recent years, going from a surplus of £53.5 billion in 2011 switching to a deficit of £1.6 billion in 2016 (Office for National Statistics, 2018).

Chart 5

Current account balance and components]1997-2017



Source: (Office for National Statistics, 2018).

Brexit will bring some negative effects for the trade balance, as the UK risks the no deal Brexit and essential will crash out of the EU in March 2019, these will take some time to settle in FDI will decrease. It important to take some key facts as published by the office of office for national statistics (ONS) The narrowing in the current account deficit in 2017 was mostly caused by a narrowing in the primary income deficit from 2.5% to 1.6% of GDP which was driven by an improvement in net FDI income (Office for National Statistics, 2018). The trade "*deficit narrowed from 1.6% to 1.3% of GDP due to a widening in the services surplus which was driven by a widening in the financial services surplus and a narrowing in the travel services deficit"* (Office for National Statistics, 2018).

The current account deficit in 2017 was mainly funded by investments made into the UK which was primarily made up of "other investments" which were specifically deposits and loans; this contrasts with 2016, where the majority of investments made into the UK were foreign direct investments (Office for National Statistics, 2018).The net international investment position (IIP) widened to negative 8.1% of nominal GDP in 2017 from negative 2.4% in 2016, as investments into the UK outweighed UK investments made abroad while the slight appreciation in sterling also decreased the sterling value of the stock of UK investments made abroad (Office for National Statistics, 2018).

5.3 Financial Account

The financial account (FA) is an important part of the BOP as it measures the changes in domestic ownership of foreign assets and also foreign ownership of domestic assets, if the foreign owned assets increase more than domestic ownership, this creates a deficit in the FA. What this means is that the country is selling off assets more frequently that it buys them, the components include direct investment, portfolio investment and reserve assets broken down by sector (Investopedia, 2018) of such assets as the likes of gold, commodities, derivatives and corporate stocks, In effect it covers claims on or liabilities to non-residents, specifically with regard to financial assets (Investopedia, 2018).

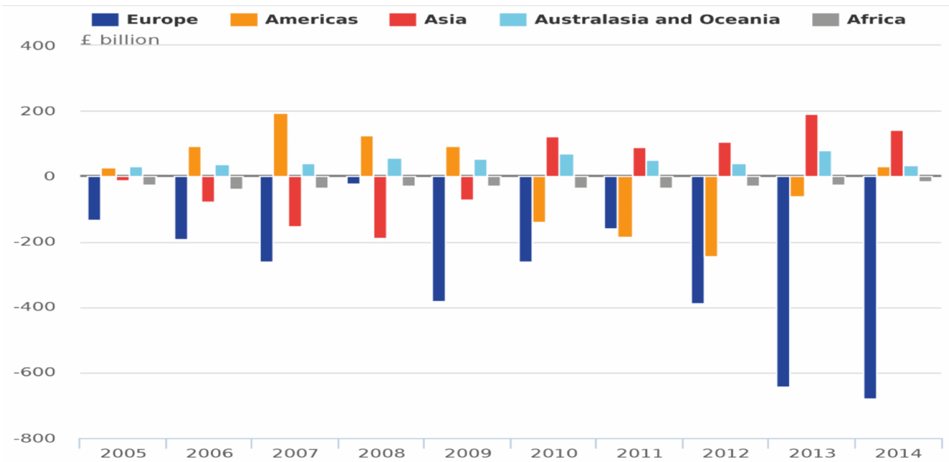
The UK Net International Investment Position (NIIP), the difference between UK assets abroad and UK liabilities (UK assets hold by foreigners), shows a net liability position. This scenario has worsened in recent years showing a net liability position of 14.4% of nominal GDP in 2015 (The Office for National Statistics, 2016).

This deterioration is mainly produced by the worsening of the UK FDI net position, or an increase in FDI liability stocks and a decrease in FDI asset stocks, and a decline of their rate of return, in other words, the rate of return of liability stocks has risen slightly while the return of asset stocks has slightly fallen. “This likely reflects the relative strength of the UK economy, in particular relative to the euro area, where a large fraction of the UK’s overseas assets is based” (The Office for National Statistics, 2016).

Chart 6 represents the geographical distribution of UK assets and liabilities throughout the NIIP. In 2015 the UK has a net liability position with Europe and Africa and net asset position with the Americas, Asia and Australia & Oceania. The Graph also shows that most of the UK’s inwards investment comes from the EU “*52% of total liabilities*” and most of the UK asset stocks are held in the EU, “*45% of the total UK’s investment abroad*” (The Office for National Statistics, 2016).

Chart 6

Geographical distribution of UK assets and liabilities



Source: (The Office for National Statistics, 2016).

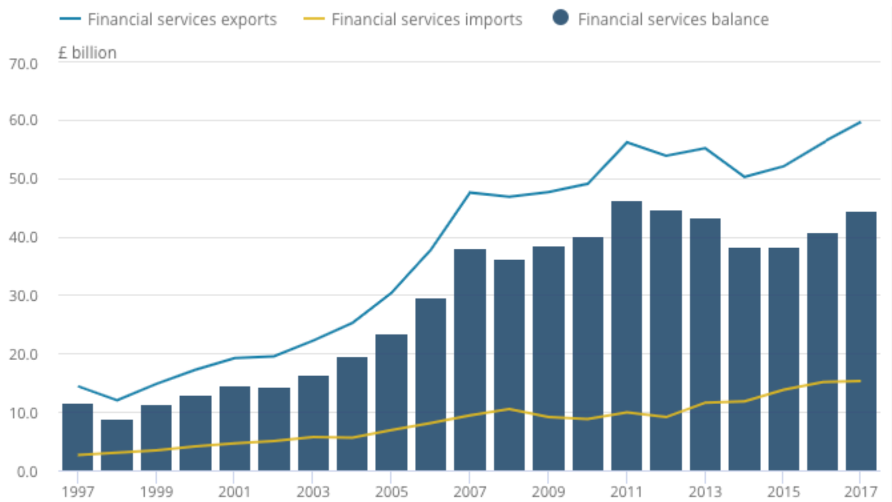
Following there is a summary highlighting the relevance of the UK financial industry for the UK economy and the degree of the sector's economic interconnection and interdependence with the EU.

Chart 7 looks at the level of financial service exports and imports the upwards slopping export curve shows how important the expertise of financial services in the UK is important to the country, Brexit's negativity will largely hit firms operating within the UK who can essentially move operations to other countries like Luxemburg, Germany and the Czech Republic where they can operate within the boundaries of the EU at lower costs and growing business opportunities.

Chart 7 shows UK exports, imports and the trade surplus for financial services from 1997 to 2017. Exports of financial services increased £3.6 billion in 2017, whereas there was a relatively small increase of £0.1 billion for imports. This resulted in a £3.5 billion increase to the UK's surplus in financial services (The Office for National Statistics, 2018).

Chart 7

Financial services exports, imports and trade balance

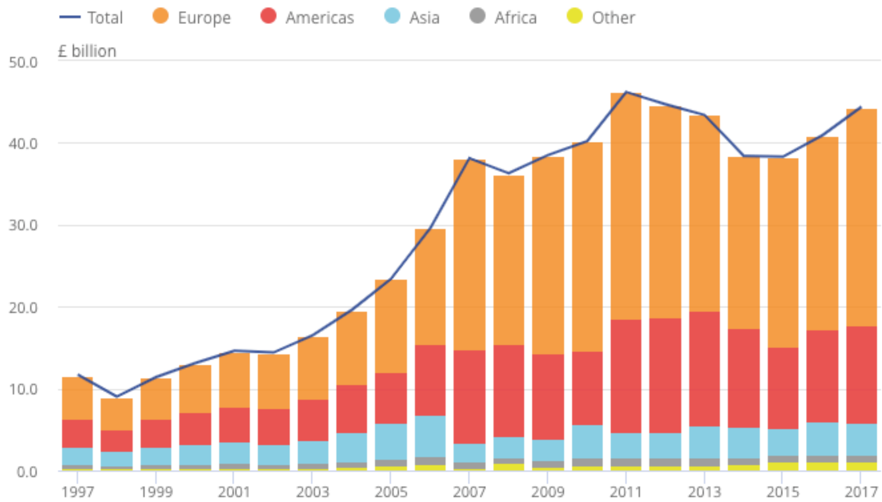


Source: (The Office for National Statistics, 2018).

Financial services were the largest contributor to the increase in the trade in services surplus in 2017. Financial services accounted for 21.5% and 9.2% of total UK services exports and imports respectively in 2017 (The Office for National Statistics, 2018). However, with the Brexit date approaching it is important to see how much of that comes from the EU, chart 8 shows the contributors by region.

Chart 8

Contribution by region to financial services trade balance 1997-2017



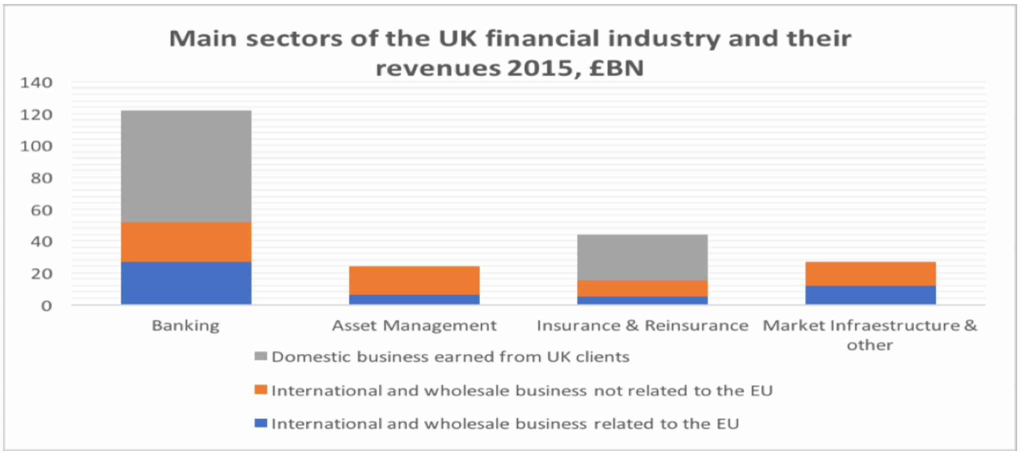
Source: (The Office for National Statistics, 2018).

Contributions by region to the UK's surplus in financial services, a "*£3.5 billion improvement in the financial services surplus in 2017 was mainly due to a £2.9 billion widening of the financial services surplus with Europe*." Exports of financial services to Europe increased by £2.2 billion whilst imports fell £0.7 billion. The surplus with Americas improved by £0.8 billion, while it worsened by £0.3 billion with Asia (The Office for National Statistics, 2018).

There has been an upward trend in the financial services balance since 2015, a £2.6 billion improvement to the financial services surplus in 2016 was due to exports of financial services rising by £4.0 billion and imports increasing by £1.4 billion, of which Europe contributed £1.7 billion to the export rise and £1.3 billion to the import increase (The Office for National Statistics, 2018), however risking a no deal Brexit can have severe complications for UK-EU financial services trade.

Chart 9

Main sectors of the UK financial industry and their revenues 2015, £BN



Source: (Wyman, 2016)

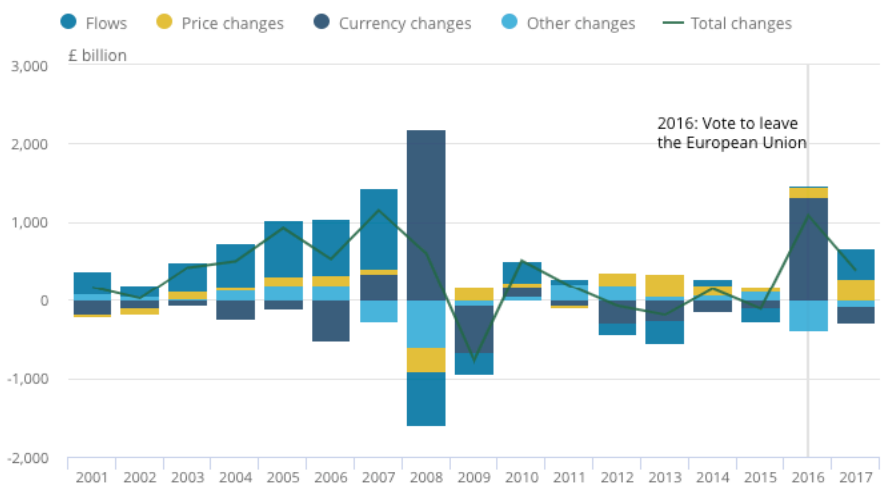
The banking system is the largest sector of the UK financial industry followed by the insurance sector in the 2nd place and the asset management and the market infrastructure sectors in the 3rd and 4th place respectively. The 4 financial sectors are related to a lesser or greater extent with the EU, turning EU states and businesses into important financial trading partners. Therefore, it can be said that the future revenue of these financial sectors will partially depend on the new relationship UK-EU.

However, as depicted in the chart 9, the volume of trade of financial services is slightly bigger with non-EU economies. A trade volume which may not be directly affected by the results of the referendum. Exports of financial services have increased by 7.3% to non-EU countries since 2000, 0.3% more than exports to EU countries in the same period (The Office for National Statistics, 2016).

It may seem strange that in both, the asset management and the market infrastructure sectors, there are no revenues generated from UK clients. This is because in both cases UK client revenues are included in the international and wholesale business not related to the EU. It is highlighted above that the UK financial sector accounted for £58BN of UK's total trade surplus in 2014 (TheCityUk, 2016). This number does not only helps offsetting the trade deficit of goods "*over £120bn*", but this amount accounts for a trade surplus which is bigger than the aggregated surplus created by all the others net exporting industries.

Chart 10

Total annual change in IIP assets broken down into impacts 2001-2017



Source: (The Office for National Statistics, 2018)

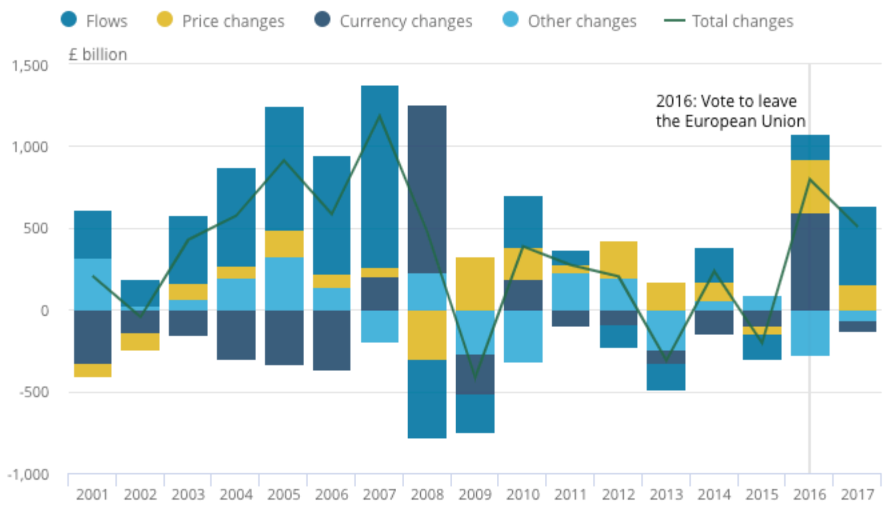
Financial flows are some of the main components driving the changes in IIP of UK assets and liabilities, the change in stock not only looks at the accumulation of new assets and liabilities, but also the re-valuation of existing ones and the changes in the pound exchange rate, which affects UK assets held abroad as they are mostly held in foreign currencies.

In 2017, the sterling exchange rate appreciated, which in 2016 was at its lowest level in eight years primarily caused by the vote to leave the EU. The appreciation in the effective exchange rate by 1.0% from 2016 led to a lower revaluation in the stocks held abroad when converted back into sterling. This is the opposite of what happened during 2016, with currency changes causing a higher revaluation in the stocks held aboard when converted back into sterling (The Office for National Statistics, 2018).

From chart 10 we can see that in the year 2017, currency changes were the main factor behind the decline in the value of UK stocks from 2016. This was despite financial flows of UK investment abroad increasing to the highest level in 10 years and price changes leading to a higher revaluation of stock. Currency changes also had a large impact on assets in 2016 and at the start of the economic downturn in 2008 (The Office for National Statistics, 2018).

Chart 11

Total annual change in annual IIP liabilities broken down into impacts



Source: (The Office for National Statistics, 2018)

As to liabilities the chart shows the same impacts will affect the liabilities side, although only other investment will be impacted by the sterling exchange rate as the majority of these investments are held in foreign currency due to the UK's large banking sector. Using the same method as described previously, we can split out the total changes into main impacts which is, other changes, currency changes, price changes and flows (The Office for National Statistics, 2018.

The levels of investments made into the UK from abroad declined slightly from 2016 and this was mainly due to the appreciation in pound which led to a lower re-valuation of stocks held in the UK when converted by into pound sterling. This was despite investment flows, which seen the investments made into the UK increase to the highest level in ten years and price changes leading to a higher re-valuation of stocks held in the UK. Similar to those of the assets side, currency changes had a large impact on total changes in liabilities during 2016 and at the start of the economic downturn of 2008 (The Office for National Statistics, 2018). The negative impacts of Brexit will hit the UK economy, this although depending on the final exit deal.

5.4 Capital Account

The capital account measures financial transactions that don't affect a country's income, production, or savings. For example, it records international transfers of drilling rights, trademarks, and copyrights. Many capital account transactions happen infrequently, such as cross-border insurance payments. The capital account is the smallest component of the balance of payments.

The City of London may "*lose up to £18 billion in revenue and up to 30,000 jobs by leaving the single market*" (Oliver Wyman 2016). The analysis in this brief suggests that these estimates account for about 15 percent of financial sector revenue and 3 percent of employment in the City. Other estimates show similar magnitudes: £14–20 billion in revenue and 70,000 jobs lost (PWC 2016) or 83,000 jobs lost (EY 2017). According to these estimates, for the City of London the direct negative effect of Brexit on the financial sector will be a 12–18 percent loss of revenue and a 7–8 percent drop in employment, clearly significant effects. In macroeconomic terms the initial effects of Brexit on the country's financial sector are modest: UK GDP may shrink by 0.5 percent and employment by 0.2 percent. These estimates are smaller than those predicted by the government prior to the referendum. In April 2016 the UK Treasury predicted declines of "*£38 billion in revenue and up to 230,000 jobs in the financial sector"* as a consequence of Brexit. These effects may materialize in the longer term. (The Report of the UK Treasury on Brexit)

6 Consequences of Brexit for UK trade and living standards

In this chapter I will focus on the consequences the UK faces in terms of trade and ultimately the living standards as it is closely related to the volumes of trade a country experiences, I will cover tariffs and customs associated with such trade and that the UK would be subject to when exporting to the EU, if no trade agreement is negotiated upon exit, Furthermore, I will closely examine and calculate the duties applied to UK's exports and imports in selected sectors, assuming the trade volume remains the same after Brexit. The next section covers the consequences for the UK-EU trade volume and the assessed costs of trade lost, followed by a section on the indirect costs of leaving the Single Market, to conclude this chapter I will examine the possibilities that the UK would turn to other close partner countries for trade agreements such the commonwealth countries. Looking at publications on the subject matter the following is as of interest.

In a paper published on 04 April 2016 before the British vote, looks at some of the effects the vote will have on trade and fiscal policies and the effects that the termination of EU membership will have on the living standards. The panel of the paper focused on two scenarios focusing on trade and net fiscal contributions from the UK to the EU using both structural gravity trade model and empirical estimates. Presented in both cases, they find that leaving the EU reduces living standards in the UK, although the exact magnitude of the loss is subject to considerable uncertainty as it is not known what policies the UK would adopt following Brexit and how this will be carried out. The panel focused on two scenarios or "views" on Brexit, an optimistic and pessimistic, this was to analyse the so called soft or hard Brexit as what are the impacts Brexit would have after the leave date. As for trade in 2014, the other 27 EU members accounted for 45% of the UK's exports and 53% of UK imports. EU exports comprise 13% of UK national income, this shows that the UK is very much dependent on EU trade, and that membership is necessary to maintain the UK economy to the high level.

Table one shows some results for both cases the optimistic and pessimistic and show that the percentage change in income per capita that has the same effect on the living standards in the UK. The optimistic scenario shows that there is a calculated fall in income of 1.28% which is mainly driven by the current and future changes in non-tariff barriers.

Table 1

The effects of Brexit on UK living standards

	Optimistic	Pessimistic
Trade effects	-1.37%	-2.92%
Fiscal benefit	0.09%	0.31%
Total change in income per capita	-1.28%	-2.61%

Source: (Swati Dhingra, 2016)

Non-tariff barriers have a particularly important role in restricting the trade in services, an area where the UK is a major global exporter, the pessimistic scenario shows the overall loss increase to 2.61%. This shows that the cost of trade reductions as shown by the decrease in income per capita majorly outweigh the fiscal savings that UK might make, when it comes to actual money Brexit reduces average income per household in the UK by £850 per year in the optimistic scenario and £1,700 per year in the pessimistic scenario. The paper also talks about the unilateral liberalisation after Brexit and that the UK would no longer be bound by the EU's common external tariff on imports. Supporters of the leave vote or "Brexteers" argue that the UK could benefit from this change by unilaterally removing all tariffs on imports into the UK. liberalisation policy, the analysis in table two shows these effects with the additional assumption that the UK removes all import tariffs.

Table 2

The effects of Brexit and unilateral trade liberalisation on UK living standards

	Optimistic	Pessimistic
Brexit trade effects (from Table 1)	-1.37%	-2.92%
Fiscal benefit (from Table 1)	0.09%	0.31%
Unilateral liberalisation	0.30%	0.32%
Total change in income per capita	-0.98%	-2.29%

Source: (Swati Dhingra, 2016)

The findings show, that, unilateral liberalisation reduces the costs of Brexit by 0.3 percentage points in both of the scenarios. But the overall effect of Brexit will be still negative. They reason that WTO tariffs are already low, so further reductions don't make much of a difference. Integration is not a matter of lowering tariff rates. It requires policies, such as taking out regulatory differences in services provisions that depend on international agreements and cannot be achieved unilaterally. These published estimates shown above are based on a static model which does not include the dynamic effect of trade productivity and that the Recent research finds that dynamic effects may double or triple the size of the static effects reported in Table 1 (Swati Dhingra, 2016) This paper has shown that the living standards following Brexit will fall with the income per capita lower and far outweigh the positive side of fiscal policies, peoples living standards will be worse and however fiscally the UK will benefit. If the UK does not reach a deal with the EU the consequences for trade can have a huge impact for both economies, the next chapter I will concentrate on the trade effects for both the UK and the EU, I will look at the trade statistics and how they will be affected.

6.1 UK and EU trade

The aim of this chapter will be to make an analysis on the effects of the UK leaving the EU will have on the trade levels between both parties. As one of the main trading partners with the EU and one of the biggest contributors to the EU budget, Brexit will negatively affect both Britain and the EU. Amidst Brexit talks are the impacts on agreements and customs union (the single market). A customs union is a group of countries that have agreed to trade freely amongst themselves and agree on a common external tariff to countries outside the customs union (Krugman & Obstfeld 2009). Therefore, having a customs union is beneficial for trading members as would enjoy essentially free trade amongst themselves and have set tariffs for third party trading countries, which economically is beneficial. As theory shows, the main benefit of a customs union is trade creation (see Appendix A) this in-fact increases the economic welfare. If no agreement is reached regarding the continuation of the Single Market and the customs union after exiting the EU, the UK will face some hefty economic consequences.

The reduction in tariff barriers tends to lead to lower prices for consumers, which in turn switches consumption to lower cost producers, the end result is higher output and lower unemployment rates. In a customs union, there are also additional benefits from increased exports as other participating countries remove their tariffs, though according to theory, a country can gain solely from removing its tariffs without receiving reciprocations from other trading partners. Thus, when the UK exits the EU on terms, theory predicts that economic welfare will fall, due to a switch in producers from to high cost producers, a fall in consumption and output will also occur, Government revenues will increase, though the change in producer surplus will depend on the difference between lost exports to the customs union and gains from a revitalized domestic market shares.

On the other side of the spectrum, if the external barriers of the customs union are set high rates, trade created through the EU may simply have replaced trade with third party countries outside the union. If such trade diversion has taken place, the UK could instead benefit from trade creation with those countries after exiting the customs union and lowering its barriers to trade. Hence, the fallout would depend on whether the EU has created trade rather than diverted from it, as well as the new costs of doing trade with the EU as a non-member also play a big role for the future.

As comparative advantage ensures trade is mutually beneficial for all countries participating in trade, countries derive their gains by specialising in the production of goods or services offered, thus allowing them to trade on larger scales and more efficiently. Assuming that UK's total export volume will decrease as a consequence of exiting the customs union, the UK will not be able to exploit its comparative advantages to the same extent as within the union, since companies will have a smaller market and less possibility of specialisation. As previous chapters mention one of the main exports of the UK is in-fact the services offered to the financial industries. The effects of leaving will be quite drastic as those who trade specifically with the EU could see a move of operations to mainland Europe where they can enjoy the benefits. The no deal exit will also see a fall in economies of scale, average costs increase and a loss in competition for the domestic markets which will cause a loss in consumer surplices' as incentives for cost cutting and improving efficiency will also fall. To understand the extent off the loss in trade I will look at figures for trade between the EU and the UK, this will enable me to examine the extent of damage that Brexit will bring on the economies.

Before I look at the trade effects of what will happen after the UK leaves the EU as member state it is important to examine the statistical figures of trade that both the UK and the EU stand to lose, I will also cover the topic of the budgetary impact of Brexit on the EU further in the chapter.

To provide a basic overview of trade with the EU I have chosen some points to note looking at the latest figures, figures taken from a house of commons library briefing paper.

- The EU, taken as a whole is the UK's largest trading partner. In 2017, UK exports to the EU were £274 billion (44% of all UK exports). UK imports from the EU were £341 billion (53% of all UK imports).
- The share of UK exports accounted for by the EU has fallen over time from 55% in 2006 to 43% in 2016, increasing slightly to 44% in 2017.
- The share of UK imports accounted for by the EU fell from 58% in 2002 to 51% in 2011 before increasing to 53% in 2017.
- The UK had an overall trade deficit of -£67 billion with the EU in 2017. A surplus of £28 billion on trade in services was outweighed by a deficit of -£95 billion on trade in goods.
- The UK had a trade surplus of £41 billion with non-EU countries. A surplus of £83 billion on trade in services outweighed a deficit of -£42 billion on trade in goods.
- Services accounted for 40% of the UK's exports to the EU in 2017. Financial services and other business services (a category which includes legal, accounting, advertising, research and development, architectural, engineering and other professional and technical services) are important categories of services exports to the EU – in 2017 these two service categories made up 52% of UK service exports to the EU.
- Wales followed by the North East of England had the highest percentage of goods exports going to the EU of all the countries and regions in the UK in 2017. The East of England followed by Northern Ireland had the joint highest proportion of goods imports from the EU.
- EU tariffs are generally low but are high on some goods, especially agricultural products.

Source: (Ward, 2018)

Judging by the figures provided above the UK stands to lose a serious trading partner which, if lost, has to find alternative solutions of filling in or face being hit with tariffs to that of non-EU members. On the other hand, the EU also has some big shoes to fill as they also stand to a great trading partner and as a the UK will distance itself from the EU the options are open to have a new member state which could bring capital, labour and trade deals to the table, I will also have a small suggestion on countries which in effect can take UK's place for a new member to the EU. The trade effects as mentioned in the previous chapters are negative as the UK risks of crashing out of the EU the consequences can be dreadful for UK economy, this is by far the most complex European political environment since WW2, the complications of Brexit will continue as government uncertainty continues to grow.

6.2 The budgetary impact of Brexit on the EU

Since the British vote to leave the European Union, the economic consequences of cancellation of membership with the EU are at the heart of all Brexit debates. Most of the talks are supported with misinformed backers, and full of government uncertainty. A large issue has arisen and that has to do with the European budget and how it will be affected following the Brexit.

The United Kingdom is one the main contributors to the EUs' budget as shown in the table below as Britain in preparing itself to leave membership and with the exit date closing in the European Union will be losing a main contributor to its budget, which can have severe implications on the way the EU operates and plans spending.

Table 3

Main contributors to the EU budget.

Main contributors to the European Budget (millions €)

	2014	2015	2016	Average
Germany	25 816	24 283	23 274	24 458 (21.1 %)
France	19 574	19 012	19 476	19 354 (16.7%)
Italy	14 368	14 231	13 939	14 179 (12.2 %
UK	11 342	18 209	12 759	14 103 (12.2 %)
Total national contributions *	11 6532	118 604	112 080	115 739 (100 %)

Source: (Joannin, 2017)

With the UKs' contribution being around 12% of the budget it's a big game player in European economics and a strong candidate to lose, table two shows the British contribution a bit closer with rebates and money spent in the United Kingdom.

Table Four

UK contribution broken up into segments.

British Contribution to the European budget and spending in the UK (millions €)

	2014	2015	2016	total	average
National contribution before rebate*	17 458	24 337	18 566	60 361	20 120
Rebate	6 066	6 083	5 870	18 019	6 006
Real contribution**	11 341	18 209	12 759	42 309	14 103
EU spending in the UK (or return)***	6 985	7 457	7 052	21 494	7 164

Source: (Joannin, 2017)

The United Kingdom also has one of the biggest percentage of rebates from the EU as in the agreement, however it is still one of the biggest contributors to the budget the main rebates are the monies that is essentially invested back into the UK and has proven to work for the communities in the UK It is the second biggest net contributor, far behind Germany and just ahead of France. The net contribution totals 38.7 billion € over 5 years (2012/2016). The recent average has been 7.5 billion €. Normally this represents the loss of potential revenues caused by Brexit, Table three focuses on the figures of net contribution by the main member states, the budgetary particularity of the UK mainly emerges via the British rebate. The principle, approved by the European Council, it has been decided that any Member State that has to bear an excessive budgetary burden in comparison to its relative prosperity is eligible, in due course; to enjoy an adjustment to their contribution.

Table Five

The main net contributors to the European Union

The EU's main net contributors

	2014 (in million €)	2014 (in % GNI)	2015 (in million €)	2015 (in % GNI)	2016 (in millions €)	2016 (in % GNI)	Average 2014 -2016
Germany	- 15 502		14 309		10 988		13 600
UK	- 4 929		11.521		6 272		7 574
France	7 165		5 522		9 216		7 301

Source: (Joannin, 2017)

Table three above shows the main net contributors to the budget quite far behind Germany and close with France these are countries that make the European Union of it is a vastly rich and well-established community with laws and regulations, these contributions to budgets are what holds our infrastructures together and help us enjoy our freedoms as we do so well, Brexit will mainly not affect our freedoms however it will affect the business side of things with the trade flow to and from the United Kingdom. Some business, schools, universities and government provided facilities depend on contributions to maintain and grow, with the budget being lower some might be affected.

The threat to the budget from Brexit is not that a rushed British departure would trigger a cash crisis and bring ongoing EU business to a halt. If there is a danger, it is that the U.K. Countries in Central and Eastern Europe that are supposed to receive large allocations from the EU's budget, mainly Poland and Hungary who fear a move to cut programs in the wake of Brexit but given how much the overall spending is behind schedule, the pain can probably be put off until well after the Britain has left the EU. The sluggish overall performance of the EU's internal aid programs is not something that its supporters like to shout about perhaps because it reflects badly both on the national administrations and the EU itself. But it may yet provide a cushion against the disruptive effects of Brexit.

6.3 The effects of Brexit

Brexit as a whole will definitely have an impact on the European Union, just how big? economists and government bodies have not yet been able calculate the full effects, what we have to go on is the estimations which are also quite bland as some predict the affects to be minor and inconsistent to the EU big economy, others do predict a far worse scenario for an EU without the Britain as a trading partner. Britain's departure will be too significant, however their contributions will be covered by other member states, however with many fairly new and some small members whose economy is not a major player this gap will be difficult to fill.

Brexit will complicate the issue a great deal. Because the main budgetary arrangements granted to the Member States all hang on the British rebate. The European Union has introduced several measures to reduce those in-balances in forms of reimbursements, rate reductions and targeted spending. But the best known and most widespread are "the rebates on the rebate" which comprise a reduction of the share of some States in the financing of the British rebate. It is the rebate on the rebate that helps to control Germany's net balances, also that of Sweden and the Netherlands. Without the rebates the States will have to contribute in full, according to their share in the Union's GNI, and their contributions will majorly increase.

Sooner or later it is likely that this situation will be deemed worrying by those affected. With the British departure some beneficiary States might become net contributors. The situation in Spain for example might change. In Denmark, the Netherlands, Austria, in a context of increasing contestation against Europe it is possible that some States will consider that their budgetary costs are quite excessive.

The effects will cut back on transfers, trade will ultimately fall or have a significant gap and with the implementation of other tariffs the EU will feel a massive burden after the UKs departure.

UKs exit will lead to a reduction in the overall GDP and GNI and the average per capita. This reduction lies at around four percent for, around a thousand euros. This reduction will have a direct, mechanic effect on the aid that Europe provides to certain regions of the community. Therefore, some regions that are on the threshold of eligibility of two categories receiving the most aid, in view of the most recent statistics show to be least developed or in transition, will change category. This statistic effect involves twelve regions of the European Union. Even though the Union has experience in this type of situation and has adopted a transitory, digressive aid system, but which has remained generous, this new statistic effect cannot be ignored.

7 The effects of Brexit on the British Pound and the Gold markets

With its strength as a world leading currency, the Great British Pound (GBP) has been through some significant events in recent history including the financial crisis of 2008 where dips in value have seen almost catastrophic fluctuations, it has however seen an increase in value after some years of recovery. However, as my thesis is regarding Brexit and the effects it has, as it will also continue to cause, I will concentrate on the more recent history.

The Brexit vote has seen the currency slump again which has caused effects against both the US dollar (USD) and the Euro (EUR), in this chapter I will analyse how significant the changes in the pound have been and the effects these fluctuations will cause after the exit date and what the future will hold for GBP. Another important commodity which the UK has great amounts invested in and as a world leading trader in gold, the gold markets are also of great interest when analysing the prices before coming to conclusions on the extent Brexit will cause for the future of trading. I will analyse the effects of Brexit on the exchange of the Pound against the EUR and the USD, using historic graphs to show the fluctuations. The broken line on both graphs shows the 23rd of June 2016, Brexit referendum date.

Graph 1

5-year Cross Financial Exchange rate GBP to EUR

Source: (Financial Times, 2018)

Graph one shows the cross rate of GBP/EUR, the cross rate is a term used by traders to refer to currencies which do not involve the USD when being expressed. The graph shows a clear drop of the pound on the day of the vote. the immediate reaction of the market has seen the pound fall ten points. A downward trend can also be seen for the year to July 2017 with slight stability keeping between 1.10/1.15 EUR to GBP, this has been the lowest rate the pound has been at in last five years, the fluctuations between GBP and EUR are closely linked to the Brexit negotiations.

Graph 2

5-year Spot Financial Exchange rate GBP to USD

Source: (Financial times, 2018)

The spot rate was used to express the price for GBP/USD, also called the spot price it is the price which is often quoted for the immediate settlement and is based on the value at the moment of exchange. As in graph one a clear drop in the exchange rate can be noted as the pound immediately reacts to the results of the vote, with a downward trend following to the next year. The pound has fought against the dollar seeing a slight increase seeing the pound go to 1.30 in recent months. The fall can also be directly linked to the turmoil of what it is Brexit, as the negotiations carry on the weakness in the pound strengthen which can take in the region of ten years to recover as history shows.

The price of gold on the other hand has different effects in times of economic instability, lets' take a look back at the 2008 financial crisis which has seen the gold price rise significantly as the economy copes with instability.

Graph 3

Gold Spot price in Pounds Sterling

Source: (Gold Broker, 2018)

The graph of the gold prices from 2006 to 2012 shows the impacts the 2008 financial has had on the economy and essentially the price of the commodity, it shows the prices in 2007 well below the £400 spot price selling in the regions of £350 per ounce. As 2007 comes to years end the effects of the financial crisis takes effect and gold price rise significantly as investments take a turn from risky currencies, the commodity is a valuable asset to the UK as London is a main hub for trades and operations for investors.

Graph four on the next page shows the spot prices of gold between the years 2013 up to current month of 2018. The significant change in price as shown in the years 2013 to 2015 is where the pound gained strength against the EUR an USD, this strength is strongly reflected in the gold price and good time for commodity investors.

Graph 4

Gold Spot price in Pounds Sterling

Source: (Gold Broker, 2018)

The broken line in the graph shows June 23, 2016 the date of the referendum vote. The reaction of the vote caused a significant spikes in the gold price. after the vote date the price of gold fell causing investor risk aversion effects which has seen the gold prices to rise again to well above pre-Brexit levels and above the 1000GBP mark. Risk aversion is a tactical manoeuvre by investors and refers to the risk which is taken, in this case it's a low risk and mid to high reward as the market's reaction is somewhat unpredictable and concern government uncertainties.

Economic and geopolitical uncertainties traditionally drives' investors away from the money markets and into a more reliable sectors like the metals exchange, where gold is seen as a safe haven for investors, as shown in previous chapters this is the case to be true, as the value of a currency declines investors flock to what is widely thought as a more secure return on investment. Looking at the graphs together they show what proves to be true, that as the pound is hit hard by Brexit the gold prices surges in value proven to be a right decision and investment opportunity, these price hikes are mainly driven by the uncertainties of Brexit and as there is yet a deal to be done the markets may react in different ways, as I look further into my analysis it is important to state that the UK is the first case in which a country is leaving the union and there are many aspects which will negatively affect its economy and financial stability, it is my work to examine the extent of these effects, however fuelled by many uncertainties and governmental decisions, the predictions for the future after Brexit is uncontrollable and highly volatile.

7.1 The future of the GPB rate and gold market

In this chapter I will look into what the future holds for the rate of the pound and the price of gold after the UK leaves the EU in March of next year, as I have mentioned in the previous chapters it is highly likely that the recovery time for the UK will take ten years depending on the decision made during the negotiations with the EU leaders but also the negotiations that the UK will have to make for new trade agreements, with other UK partners like the Commonwealth countries, USA and China.

No one can predict with any certainty the full effects Brexit will have on the pound as the exit date approaches, other factors such the inflation rate and cost of living standards are also important aspects which I will cover in my thesis in future chapters. Depending on the agreement reached by the exit date and more importantly which can influence the currency is the type of exit the UK take, however looking at the facts covered it can be made clear that the UK is heading for a hard Brexit with tough negotiations ahead in the coming years.

The volatility of the pound is highly likely to happen as the governments try to come to term of Britain's departure, the short-term effects without any preferential agreement with EU would almost certainly be bad for GBP as it could face a highly volatile phase where investors will turn once again to the commodities market like gold and other bullion.
As reported by Reuters "the British pound has suffered its worst quarter since the vote to leave the European Union in June 2016 triggered one of the biggest selloffs in the currency's history" (Carvalho, 2018). These facts have triggered investors for speculations on the pound and hedge funds having a short positioning for the pound, Carvalho also mentions; "the

pound has traded within tight ranges recently and volatility has fallen, possibly because markets already price in the worst-case scenario --"hard Brexit"" (Carvalho, 2018).

As it goes to the gold market the prices seem to stabilise at the new high or around 1000GBP per ounce and that price will keep for the years to come after Brexit, gold itself offers a safe position as the pound will weaken following the trends of the economy which will be analysed further in my thesis.

The pound having further tumbled in recent deal negotiations as mentioned in the previous chapters the future does hold some uncertainty for the future, as it is strongly connected to the political situation. If the deal proposed currently, is accepted it might take an estimated five years to recover and become a strong currently and might lead to levels of 2006 when sterling was a stronghold against the USD and EUR, if however no deal reached and the UK crashes out the pound being politically linked will see the pound further decline and estimate recovery time will also see an increase which can take as long as ten years after Brexit date to recover to normal positions.

Conclusion

In conclusion Brexit will have a huge impact on the UK economy and the economy of the European Union as a both, the EUs budget will decrease by a significant amount prompting the EU to increase contributions of the 27 other members and decrease spending on some infrastructures and smaller members. The UK might stand to lose more, with the decrease in trade and the movement of companies to mainland Europe, this will have an impact on the UK however its positive for Europe with new companies which will provide jobs for the local community and pay taxes to the member state.

The European union will probably increase its contributions of member states so they are able to protect the economy and the infrastructures already in place this will have a negative impact on contributions and individual members economy, also rebates, another talking point which will essentially be lowered meaning main contributors will have a smaller pay-out of their contribution to be able to use on its own economy. However, these affects are not fully studied and followed by Britain's uncertainty it will be many years before the full effects on Brexit will be felt and even more to overcome them.

Following my studies for my thesis Brexit will impact the economy harshly and those negative effects will spread throughout the economy of the UK, although the full effects Brexit will have is highly unpredictable only educated estimates can be made, looking at the history of political events and financial crisis suggests that the UK's economy will suffer and that the recovery time will be in the region of ten years, however no other country has ever left the union, Brexit is a mistake that will take some time to be fully accepted.

As the EU is a union of nations who encourage growth and stability it seems likely that a deal will be agreed, however the time implications set will see more challenges in the future of the negotiations and it looks more promising that the March 29 2019 date will be postponed to a future date, the other hand of the negotiations which also looks promising is that the UK will cancel Brexit altogether, however for that to happen an political overturn will need to take place and reform of the plans in place as to not worsen the economy and the financial stability of the UK and the pound sterling.

During my research and my own experience, the pound will be hard hit as the exchange rate is closely connected to the politics of the current situation the dips can be seen clearly during speeches and phases of the negotiation process. A hard Brexit is a definite mistake for the UK to make, as the unpredictability of the events to follow can be drastic, the negotiation process will need to be see the UK make other agreements with countries such as Canada, USA and China, if the UK wants close relations to the EU than the neighbouring countries to the union will see a good agreement in future trading.

The financial services industry, in my view will make changes in their operations, companies will tend to move operations closer to the EU, those who trade specifically with the USA or Asian countries will not see any changes of the operations unless a move to mainland Europe will see them more beneficial in their trading.

As for the job market, the will definitely be increase in the unemployment rate as companies move or adjust to operations after Brexit. The economy will essentially be on the brink of inflation and instability which can cause a crisis far worse than that of 2008.

The European Union who will lose a huge player will also see a decline in their budget as the UK will pay much less into the community after the final terms have come to an end although the EU will not be as hard hit as the UK its overall economy will see some damage which will take some time to recover, however the stability of the EU will see this quickly change. UK's exit also gives the opportunity for some countries to enter the union such as Ukraine mentioned above, and Turkey of which the opportunities in these countries will bring great benefits to the EU.

The Brexit topic has to be the most studied but it's the most unpredictable of all as it is surrounded by biased opinions, unpredictability of governments and the uncertainty of it all is highly likely that the UK's economy will take a huge tumble of which the recovery time will be past ten years.

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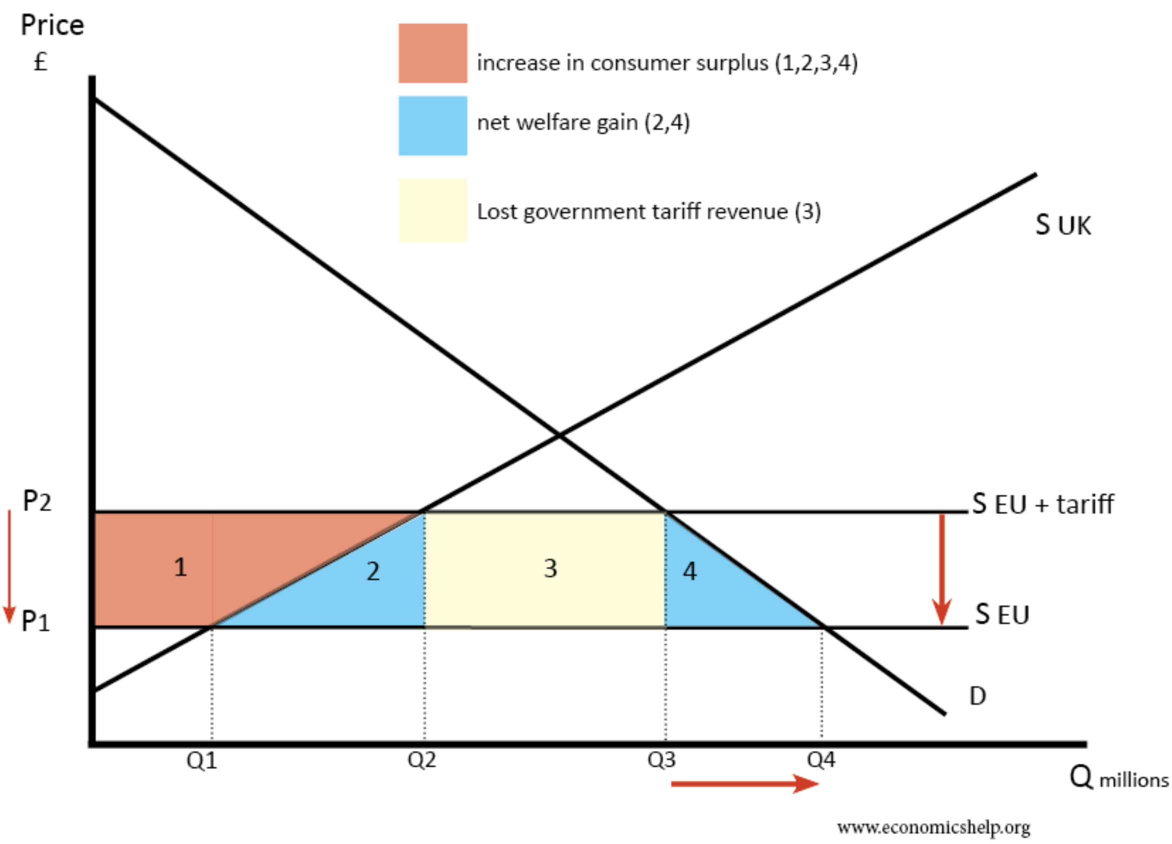
Appendices

Appendix A: Trade Creation

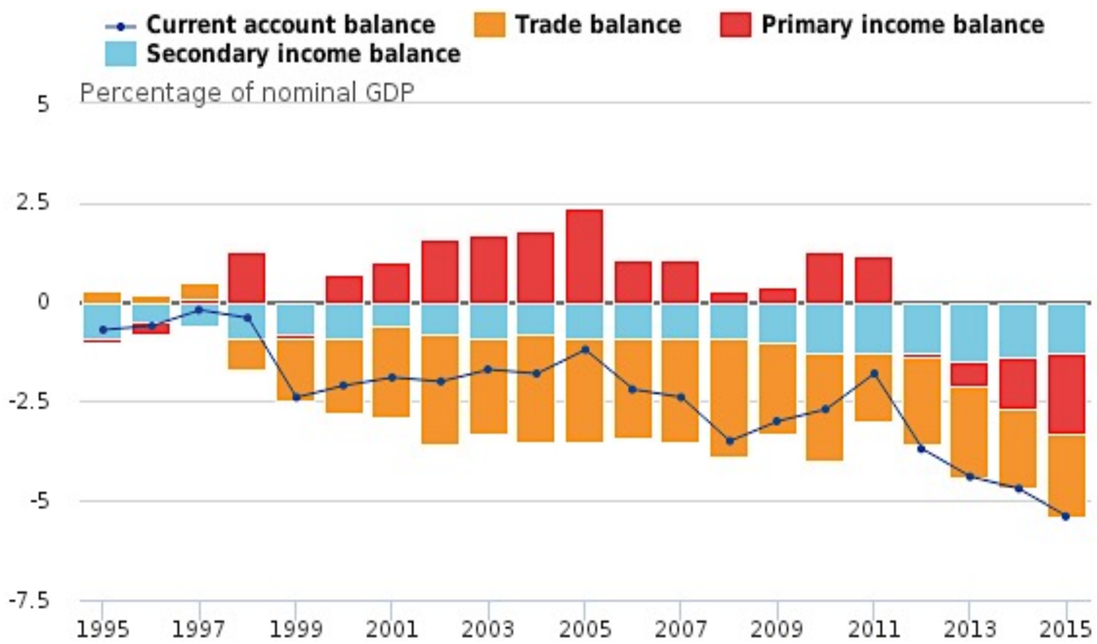
The effects of trade creation are depicted in Diagram 1, where the removal of tariffs reduces the price of imports from P2 to P1, and increases the imports purchased from Q3 to Q4. Hence, the consumer surplus increases, adding up to the area 1+2+3+4. Domestic producers sell less, and their surplus declines by area 1. Further, the government loses tax revenue from tariffs, equivalent to area 3. Therefore the net gain from trade creation is the areas 2+4. The extent of this gain depends upon the elasticity of supply and demand, meaning that if the demand is elastic, consumers will have a significant increase in welfare.

Diagram 1



Source: (Pettinger, 2016)

Appendix B: Current account balance as percentage of nominal gross domestic product



Source: (The Office for National Statistics, 2016).