

Brexit Referendum: Impact on Indian & Global Economy

S. Sathyanarayana*

Abstract

After the subprime crisis causing jolts in the global financial markets including India in 2008, Brexit is seen as the next colossal financial affair since. Most of the EU functions as one vast economy because of Schengen, a free travel agreement among its members, enabling movement of people belonging to the EURO countries. Britain voters backed the breach by fifty-two percent to forty -two percent after a stringent campaign of roughly three months. The polling created a storm in financial markets and its aftermath can already be witnessed in currency market too. Banks and financial institutions across the world have been crushed by Brexit. Indian companies have always been a base to the U.K.to reach the European markets because of its access to London financial hub and ease of doing business with European nation because of divergent European culture and language. Apart from that India has a trade surplus of approximately four billion US dollars with Britain. Moreover, the firms which have revenue earnings from England and Eurozone are going to be the worst hit, at least for momentary. India would save a lot on its crude import bill because of the shock of the slowdown caused by Brexit referendum in several nations globally leading to the prices of major commodities plunging, specifically crude oil. Indian stock market along with the currency may face volatility in the short run in the event of Brexit, but doesn't have much to fear.

Keywords: *Brexit, Sterling, European Union, Immigration, exposure.*

Introduction

The European Union (EU) is a rare cohesive economic and political union of twenty eight members of European countries that are based predominantly in

Europe. The EU is one of a kind because (i) it is not a government; (ii) it is an association of independent nations; (iii) the members have renounce part of their supremacy to European Union; (iv) EU's operation is through a combination system of supranational and

* Associate Professor, Bharatiya Vidya Bhavan's MP Birla Institute of Management, Bangalore, sathya4u.s@gmail.com

intergovernmental decision-making; (v) all the 28 members are independent fiscal and political entities.

The EU has an operational 4,324,782 square km area and 508,191,116 (density of 115.8 square km) of estimated population covering 7.3 percent of the world population with 24 official languages, where its administrative capital is Brussels. Its official estimated GDP of \$19.205 trillion (nominal GDP is \$16.220 trillion covering 24 percent of global nominal GDP) for the year 2015 with per capita income of \$37,852 (nominal per capita is \$31,918). The EU's HDI is 0.865 a very high rate with a common currency called Euro (only Nineteen of the countries use the euro as their official currency).

How Does It Work?

There are seven main controlling bodies regulating the EU. They are (i) the European Council (EC) – promote development of the European nations and provide direction. Its headquarters in located in Brussels; (ii) the Council of the European Union – it works as legislature, works jointly with the parliament, set out foreign policy and security issues of the members; (iii) the European Parliament – Quasi parliament (iv) the European Commission – does the executive role, submits proposal for new legislation and implements policies; (v) the Court of Justice of the EU – acts a judiciary headquarters at Luxembourg; (vi) the European Central Bank (ECB) – determines the monetary policy of the EU based in Frankfurt, and (vii) the European Court of Auditors - check the proper implementation of the budget placed in Luxembourg.

The major objectives of the EU

To stimulate economic and social progress, peace, common foreign and security policy, continuous development of the Earth, harmony and mutual respect among people, free and fair trade and moment of labour, eradication of poverty, protection of human rights and development of international law.

Key Benefits to the members

Free movement of capital and labour the citizens of the member nations are entitled to free and open movement between the member nations in the Eurozone. This leads to creation of more flexible economy. This concept opens up many more new jobs and education

opportunities among the member countries. An empirical study conducted by the Union has proved that migration has helped increase productive capacity and approximately three to four million jobs have been created over the years. Furthermore, through the European Working Time Directive they are able to protect the work force from exploitation such as regulations regarding holidays, working hours, breaks, etc.

Tax Free Trading among Members the major benefit of this union is that the members are free to trade without paying additional taxes

Lower prices of services and goods products in single large European Market are low-priced as there are no customs duty for all the member nations. Generally, goods sold between nations are charged with customs duty, but because the EU has a unified economy, no such duties are applicable.

Development of poor countries: Some nations of the EU are underdeveloped such as Portugal, Ireland and Spain. In order to bridge the gap between the developed and underdeveloped nations among the members, the Union has developed structural funds to create infrastructure in the underdeveloped regions. After this initiative taken up by the EU, the underdeveloped states have made significant contribution in terms of growth, employment generation and prosperity.

Health benefits The EU residents hold Health Insurance Benefit Card giving them easy access to necessary medical care as required, even while visiting the affiliated nations.

Better bargaining power The Union is able to ensure that all their interests are taken seriously by various agencies across the globe and heard internationally since the EU is s \$13.8 Trillion economy which is larger than that of the US and comprising of 7.8% of the world population of 28 members state.

Environmental restoration The EU has reduced global warming emissions by not less than twenty percent by diligently enforcing emission norms among the member states and improved the quality of sea water and beaches by implementing regulations on water standards.

Consumer benefits the new EU policy has restored the regulation of cartel power among members. It prohibits abusive power of cartel and monopoly especially in the essential services sectors like airlines, electricity, mobile and gas. The main intention is protection of consumers from exploitation. Consumers are not expected to pay any additional duties and can shop duty free in any member nation.

Political and legal benefits The EU has been created with an intention to bring European harmony in the form of a single European socio-political entity to end the centuries of intense rivalry among European nations. The EU has achieved this objective to a larger extent except the Yugoslavian civil war. By promoting human rights and peace in the Euro region, the EU was awarded the Nobel Peace Prize in 2012. Now, many Eastern European nations are showing desire to become members of the Union for economic and political stability.

BREXIT

“Brexit” is the name given to U.K.’s potential exit from the EU. Most of the British believe that the EU is invading into British sovereignty. Britain is subjected to billions of pounds each as fees to remain in the EU. Majority of the British don’t opine that remaining a member of the EU is worth the cost. In addition, EU regulations on European trade, commerce and law, inter alia, make pro-Brexiters believe that their country is held back by the rest of European Union at Brussels.

The major arguments advocating Brexit are as follows:

1. Euro currency issues!

England, as part of the UK, is the most significant member of the EU. The UK has elected not to use the Euro and continue to use the Pound, because they can enjoy the independent monetary policy, fiscal policy and exchange rate. Though, the EU does not insist all its members to convert to Euro, they stress on it and insist on the use of the common currency in the region. Sadly, the Euro is creating problems throughout the EU, including fluctuations in interest rate, increase in unemployment, low economic growth. However, post 2020 all EU members must adopt Euro as their common currency. This would force U.K. to abandon

its stronger currency Pound Sterling and to adopt the weaker currency the Euro. The British economists’ main concern is that since the Euro is not only an unstable currency against Pound Sterling but it would be able to be influenced by weaker countries like Greece.

2. Money matter

Great Britain is the second-largest economy in the Eurozone by economic productivity and the third-biggest in terms of population, after Germany and France. Like Germany and France, U.K. is a net contributor to the European Union. The contribution is used across Europe for the development of poorer countries to build infrastructure. But, the economic argument of the pro Brexit is that Union is blocking the Britain’s trade link outside the European Union. For example, Germany exported 74.5 billion euros to China last year, more than five times the value of British exports to China. Since emerging economy like China and India are the largest market for England, she wants free trade with leading emerging markets for the economic gain. Therefore, Britain would negotiate with these economies without being bound by common European law.

3. Trade and Economy

With regard to trade, anti Brexiteers argue that access to the single largest European market, without tariffs or duty and border controls, is critical to U. K’s economy since 45 per cent of its trade is associated with the EU. However, pro Brexiteers argue that the European Union is in need of British markets and that trade deals with European nations can be effortlessly handled. When it comes to economy the remain argues that the decision of leaving the EU will put an end of London as the Europe’s financial hub, However, the Brexiteers argue that London’s position as the financial hub will not be affected as it is already a global power in finance.

4. The UK can retain the money, currently sent to the EU

The European Union does not have the right to collect taxes directly from the member nations, but it requires member nations to make an annual contribution to the main the EU budget. Currently, the Britain’s contribution is about \$19 billion per annum, which is approximately about \$300 per U.K. citizen. Brexit supporters argue

that it would be better for the English parliament to take the decision of spending money rather than people at Brussels.

5. Overpopulation due to liberal immigration policy

EU has permitted citizens of the member states to travel across the territory. This leads to loss of immigration control that resulted in overcrowding. Although migration works both ways, but the population in the UK is expected to reach at an estimated seventy million because of the EU rules. However, net migration gap has been crossing at around two lakh a year. Approximately seven lakh UK migrants to EU are the major tax payers to the UK government and the state need not to spend much on their health care and pensions. Since, Britain is a wealthy country, immigrants from poorer European member nations flock to U.K. for jobs. As the European Union has an open door policy, immigrants don't require visas to live and work in the UK and can also demand all amenities and welfare. Pro Brexit population feel immigrants are replacing them in their jobs and destroying the system, and officials worry about foreign criminals moving into the UK undiscovered. Another major logic is that the migrants are more likely to be of working age 20-40. However, the UK native citizens are quickly ageing, this poses more stress on public spending by the UK government in the form of health care and old age pension. Brexit defenders argue that this puts a severe dent on the economic resources of the nation.

6. Employment issues

Pro-exit campaigners argue there would be a job boom if the U.K. leaves the EU. While the other side claims that as 3 million jobs are tied with the EU there could be employment crisis if the U.K. leaves the EU.

7. Security issues

Security is another major concern from the perspective of Brexit supporters. They argue that the security risk will increase if England does not have control over its boundary. While the EU supporters say that the cooperation with the EU would make UK safer.

8. EU laws are not practical it is affecting the British Sovereignty

U.K. is also apprehensive about the EU's restrictions levied on the immigration laws. The EU instructs the member countries to provide employment and all the benefits to the migrants. However, the British PM has been working to restrict benefits and housing to only those who have been in the country for at least four years. This move has been opposed by the EU leading many British think tank to question the extent of EU's interference in British welfare and policy makers seem to have lost control over the trade, human rights and migration. Therefore, pro Brexit thinkers believe that EU regulations will not encourage British interest.

Who really runs this country?

On 23 June 2016, the UK government finally decided to go for a poll to answer the key question "should the country remain within the EU or go it alone?" The final verdict went against the Euro zone that is 51.9 per cent votes for Leave as opposed to 48.1 per cent for remain, on a turnout of 72 per cent. The voters supported the split. However, post poll survey shows that Scotland and Northern Ireland are in support of staying in the Europe Union, with almost two thirds of participants wanting to remain in the Union. Interestingly, 73 percent of the voters those aged between 18-29 wanted Great Britain to remain in the EU. At the same time 63 percent of those older ones (aged above 60) opted to leave the EU. The middle-aged voters are divided almost equally on the Brexit. Almost with seven in 10 young voters backing the European Union.

The exit of the U.K. from the European Union would definitely affect the Union, as loads of the EU's money comes from its prominent member states and U.K. is one the largest contributor to the EU. The entire funds are spent on each member country, assisting poorer nations in European Union, managing natural resources, aid activities across the globe etc. Therefore, England exit would jolt the Union as it already rattled by Greece crisis, slow down and differences over the migration issues among the member nations. Apart from this Britain is one of the military super power definitely it affects the security spending of the EU. Consequently, this would also give rise to few more countries to think of exit from the European Union.

What does Brexit mean for the economy?

“Brexit” has led to wealth erosion in the U.K. and across the globe. London’s premier Index FTSE 100 opened to a drop of 8.7 percent, and the FTSE 250, fell by 12 percent. Since the exit, global stock markets lost about dollar two trillion in value on Friday, and the British currency suffered its biggest one-day setback in recent history with the economic shock waves impacting far beyond the U.K. stock markets. The DAX, German stock index, fell seven percent. France’s CAC 40 index fell 8.6 percent. The IBEX, Spanish Index, is down eleven percent. Crude prices settled 5 percent lower on 24th after England’s vote to leave the EU. The traditional safe avenues like guilt edged government debt, gold and the Japanese yen all jumped. Brexit poll wiped off eight percent of the Japanese stock market and sent the yen up strongly against the American dollar. Now the key questions rolling across the British economy is the rise or fall in pensions and other investments. What would happen to the value of Pound sterling in the currency market? Sadly there are no positive answers to these questions. The consequences of the Brexit is huge for the people of U.K now and in the future. England’s economy and legal system are greatly linked with the Union. On the other hand, referendum supporters have argued that with U.K’s exit, they will be better off in the long term with full mastery and full control over immigration, economic governance and control over its borders. Brexit effects can already be seen in financial markets. According to a Goldman Sachs analysts Pound will collapse by twenty percent. Economists and bankers forecast an immediate slowdown in the economy as investment goes into hibernation although it is almost impossible to foresee the outcome. According to few economists Pound, the liquid British financial asset, is most unprotected to Brexit horror.

Brexit might pressure nation’s budget and current account deficits, damaging the currency and ultimately demote creditworthiness. According to an expert The British Stock market is commanded by multinational corporations, whose performance is not associated to Brexit controversy, rather their performance is linked to Federal interest rate, crude prices, Chinese economic conditions etc. Banks across the Globe are crumpled

by Brexit. Non-UK banks have been unsuccessful in bouncing back from their losses, in spite of other parts of the markets recovering, the reason being major global banks presently base themselves in London and reaching out the other members of the EU. Now they need to wait to get a new banking licences in European Union and relocation of their corporate headquarters.

For non-European Banks facing a regulatory burden of having to set up a subsidiary in the EU and a branch in the UK would weigh heavily on non-EU banks: they would have to satisfy the requirements of their home country as well as those of the EU Member State in which they established their subsidiary in, and also adhere to any further supervisory requirements demanded by the British authorities. As a result, many banks might choose instead to move their operations from London to the EU. At present, the EU banks still have the probability of setting up a wing in London. It is inconvenient for non-EU banks, which would no longer have the opportunity to set up a subsidiary in London and then branch out to EU Member States. Currently, UK is the hub for foreign bank branches. To have access to a banking operations, non-EU banks will be required to open up a branch in an EU member nation. The regulatory burden of having to set up a subsidiary in the EU and a branch in the UK would weigh heavily on non-EU banks: they would have to satisfy the requirements of their home country as well as those of the EU Member State in which they established their subsidiary in, and also adhere to any further supervisory requirements demanded by the British authorities. As a result, many banks might choose instead to move their operations from London to the EU.

With unregulated control over immigration and economic regulations, Brexit advocates contend that England will do better off in the long term without the European Union. According to experts at Goldman Sachs, Pound Sterling is expected to crash by twenty percent during which stock markets are expected to crash by another thirty percent, savaging pension and Isa investments.

Economic impact on the U.S. The main setback for the U.S. economy on account of Brexit referendum comes from financial link such as investors queuing up

to buy Federal T Bills or other financial instruments to substitute Eurozone financial instruments leading to the appreciation of dollar. The effects of Brexit referendum on the U.S economy are nominal except Brexit referendum motivate the exit of additional nations to exit the EU.

Currency value. It is notably tough for U.K to negotiate similar extent of access to the EU markets, for exports from U.K. to EU countries will fall. The drop in the Sterling's value will make English exports cheaper and balance the decline in trade with European Union to an extent, but England is likely to face ongoing losses.

The Brexit triumph sent economic collapse through global markets and FTSE 100 stocks on Friday had their worst drop since the financial crisis. England has lost its top AAA credit rating. The pound, on Friday, 23 June 2016 collapsed and recorded the lowest level since 1985 and necessary steps are now being taken to ease the financial uncertainty. The EU advocates claim that offshore companies are less likely to invest in UK and might relocate their headquarters, if Britain loses gateway in to the European Union's common market. However, the Confederation of British Industry report that Brexit would cause a one hundred billion pound "shock" to the British economy.

INVESTMENT AND PRODUCTIVITY

The terms and conditions of trade between the U.K. and the EU will have to be redrafted, but the outcome of these arbitration is far from clear. The ambiguity and loss of confidence in the future will upshot into fewer investments in the Britain, decreased new projects and little ardour to engage in long-term contracts.

INDIAN CONCERNS

Britain is the third largest FDI investor into India, with cumulative equity investments of \$ 22.7 billion from 2000 to 2015. India, on the other hand, is the third largest investor in terms of number of ventures into England. The combined sales turnover of these ventures have increased from £ 22 billion in 2014 to £ 26 billion in 2015. Therefore, it's very difficult to predict today what Brexit will actually look like, or how the EU itself will function, in five or ten years' time and its impact on Indian economy. However, Indian financial

markets would experience a limited impact from England's exiting the EU, because, other major factors such as weak global demand, sluggish rural incomes, low nominal domestic growth, inflation etc. are likely to have an immediate impact on the Indian economy. Moreover, India's Exports to the Britain and the EU account for 0.4 per cent and 1.7 per cent of India's GDP respectively. Therefore, it is not a major concern for Indian economy. On Friday, 23 June 2016, Sensex closed the day with a deep cut of 605 points or 2.24% and our debt market remained relatively unchanged on Brexit. Indian investors lost nearly Rs. two lakh crore in wealth on Friday, 23 June 2016 following Brexit or Britain's decision to pull out of the EU. However, the rupee lost on both Monday, 26 June 2016 and Friday, 23 June 2016 and ended the week with a loss of 89 paise against the American dollar. Apart from that Brexit has an impact on the inflow from foreign portfolio investors (FPIs) to India. FPI stood at Rs 539 crore last week which is lesser than the expected inflow. Precious metal Gold raised to the highest level since March 2014 in more than two years in a mad global hunt for a safe assets. Gold jumped to USD 1,358.54 an ounce approximately 8.1 per cent to USD 1,358.54 an ounce, the momentum was the highest one day jump since 2008.

The slowdown that Brexit will cause in several nations globally will lead to a fall in the prices of commodities especially crude oil, which would help India save a lot on its import bill. The crude prices have come down sharply for example, the Brent crude oil from \$50 to around \$47 to \$45. According to some analysts every \$1 drop in crude prices leads to approximately \$1 billion savings in India's crude import bill. Lower commodity prices especially crude would reduce the inflation. Analysts believe that Brexit may make crude prices more volatile in the short run, but it is not likely to disrupt the crude industry's fundamental drivers, production and consumption. "India will benefit from steady prices of commodities, especially crude oil," observed an economist. The lower prices of commodities will help companies rein in costs and boost earnings. In the meantime, the markets could, however, become more expensive with earnings downgrades being expected for sectors such as automobiles and IT. "We expect earnings cuts in automobiles, IT and metals sectors

due to 'Brexit' and related weaker global economic growth..."

Generally, Britain has always taken as a base for Indian companies to reach the European companies, because of the access of London financial hub and ease of doing business with European nations. Further, India has a trade surplus of 3.64 billion US dollars with Britain. Since Brexit the pound sterling is continuously falling against rupee and thus the companies which are engaged in exporting goods and services to U.K. and Europe are going to be hit. Indian pharmaceutical sector which has more exposure towards Europe, will also be affected by the Brexit. On the other hand, the imports from Britain would be getting cheaper on the event of Brexit, mainly rough uncut diamonds, spirits etc. The companies which have revenue from Britain and Europe are going to be hit, at least for short term. The major companies which have large exposure in U.K. are Tata Steel, which has sales turnover more than 2 billion Pounds from 12 UK Steel Plants spread across U.K. Tata Motors, the largest automotive company is U.K. TCS, once again rendering services to the London financial hub and European Union and Britain together are major sources of its revenue. Bharat Forge has three plants in Germany and one in U.K. rendering the needs of European major automotive companies. Tech Mahindra, serving the Banking and Financial institutions from London, and recently acquired London based firm Fintech. Marksans Pharma, Britain and European Union market account for sixty percent of their sales revenue. For Hidalgo almost 9 per cent of sale revenues is generated from the European markets.

CONCLUSION

Anti Brexiters claim that the consequences will be huge for the British. U.K.'s economy and legal system have become intensely integrated with the EU. Untangling those relationships is likely to be culturally and economically disturbing. On the other hand, Brexit supporters have argued that U.K. will be better off in the long run outside the European Union, with sovereignty and control over immigration, economic regulations and to get control of England's own borders. U.K. exit from the European Union would be disturbing but not devastating for other EU nations. The 2008

financial crisis hit Eurozone very badly and the current Syrian refugee crisis have put the EU's broken political institutions under strain. Now the British exit could further depress Europeans' morale and confidence that the concept of EU can sustain over the long run, causing other countries to eye the exits. It creates a colossal gloom of uncertainty over financial markets across the globe particularly for higher risk class assets like stocks, forex. Stock markets may react temporarily and the magnitude is likely to be small especially from the perspective of Indian stock markets. The financial markets will go into risk-off mode for some time, and money will move out of riskier assets to safer ones especially on bullion market. If Brexit becomes a reality, the impact on India are unlikely to be large in magnitude, except few companies that have significant exposure to the EU and U.K. Apart from that, Brexit will also have currency implications meaning that the uncertainty surrounding U.K. and European Union nations will dampen the Sterling and the Euro values. This, in turn, would push capital flows into the dollar, bolster the currency greenback, which as always, has a depressing effect on oil prices. India Inc invests more funds in U.K. and Brexit would jeopardise those investments. According to the industry experts, more than 800 Indian firms now operate in Britain as being based in London provides them with easy access to the rest of Europe. In the event of Brexit, these firms may find it more challenging to directly access EU economy. India doesn't have to concern much, although the currency and stock market may turn little volatile in the short run. India makes more investments in Britain than in the rest of the EU put together. Brexit could endanger those investments in the UK as it may hamper the business operations and bottom line of these corporations.

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