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The Impact of Brexit on the Benelux States

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The citizens of the United Kingdom expressed their opinion on the referendum held on June 23, 2016, whether they wanted the country to remain a member of the European Union or leaving the EU would be the future of the UK. The turnout was 72.2%, and 52% of the voters opted for the leave – this result shocked many of the citizens of the EU. During the 43 years of membership, the British have fought their battles to protect their interests, and the EU-policy of the consecutive governments has shown diverse pictures about the relationship of the country and the EU. When the British government invokes Article 50 of the Treaty of Lisbon (which according to Prime Minister Theresa May is going to happen by the end of March 2017), the negotiations on the withdrawal could start, and they would last for at least two years. Since the treaty does not include any specific conditions for leaving the organisation, difficult rounds of talk are forecasted.

Various possible models have emerged as a possible outcome of the separation, ranging from an EEA-status, through a Switzerland-style (representing the group of possible Free Trade Agreements) to a WTO-style. As for the relationship of the UK with the EU following the exit, the two ends of the scale are the so-called hard exit and soft exit. The first one refers to the scenario, when no agreement would be reached regarding the free movement of people, and the UK would be out of the single market (thus trade relations would be similar as with any other non-EU countries and the trade barriers would emerge between the UK and the EU). As for soft Brexit, the country would retain access to the single market – in this case there would be some agreement on the free movement of people as well.

The first reactions of the markets echoed the previous forecasts: the value of the Sterling declined, and a minor economic crisis unfolded. On June 17, the International Monetary Fund (IMF) published a survey (IMF, 2016), which underpinned the former predictions, stating that Brexit would result in a significant slow-down on the economy of the UK, the decline of investors' confidence, and the weakening of the sterling. The Economic Outlook of the Organisation for Economic Co-operation and Development (OECD) published in June, also included a thorough analysis of the impact of Brexit. Regarding the forecasted trends, one cannot see a major difference between the opinions of the two organisations. The survey of OECD pointed out that although the markets gradually price the

Brexit, it would result in reduced confidence, which would have negative economic impacts, such as exchange rate depreciation, decline of GDP, and financial market shock. However, Brexit would have a negative effect on the EU as a whole, and on the individual member states as well – the magnitude of it depends on the linkages of the economies with the UK. The more an open economy of a state is linked to the UK markets, for example Ireland, the Netherlands and Luxembourg, the larger impact Brexit would have on their economies (OECD, 2016). The EU as an organisation would also have negative consequences of Brexit. On the one hand, this would be the first time a member states leaves the Union – which sheds a light on a certain failure of the organisation symbolising European unity. On the other hand, it can also be regarded as a failure of the founding fathers' dream of a united Europe. Would Brexit start the ball rolling in the EU?

In the last more than four decades, the economic ties between the Benelux countries and the UK have gradually strengthened, and now due to the economic and trade interdependence, Brexit would probably cause economic difficulties. What economic challenges and impacts would the Brexit would have on the three Benelux states?

Belgium –Different regions, different economic impacts

Belgium – similarly to the other Benelux states – has been the steady supporter of the European integration since its founding. Supranationalism (supported even by Paul Henri Spaak), and the devotion towards European unity have accompanied the European policy of the country. With the birth of the Belgian federal state, the integration that opened the possibility for the subnational entities to participate in the decision making of the EU, has become more and more important. In 1961, when the UK first submitted its application for EC membership, the governments of the Benelux states (including Belgium) supported the accession of the country. One of the reasons for it was to counterbalance the political dominance of France, another one was to compensate the German industrial weight (Jovanovic, 1997). Having access to new markets, and extending commercial ties with the former British colonies were among the economic reasons. In the last more than 40 years, rather strong commercial and economic ties have developed between Belgium and the UK. Analysts point out that Brexit would have negative consequences for the country, although regarding the extent of them, compared to the other member states of the EU, the opinions differ.

The Kingdom of Belgium – like the other Benelux states – has a small, open economy, dependent on foreign trade. When examining the impact of Brexit on the economy of the country, three areas might be important to look as closely: foreign trade, investments, and financial markets with attention to the exposure of the banking system (ING, 2016). Trade relations between the two states are rather close: in the first 9 month of

2016, the value of Belgian export amounted to €23.364 billion (8.8% share of the exports), while the value of import coming from the UK reached €11.814 billion (representing 4.9% of imports) (Belgian Foreign Trade Agency, 2016). As it can be seen from the data, the country has a considerable trade surplus in relation with the UK. The value of Belgian investments in 2013 reached €19.4 billion, with annual earnings of €1 billion in the same year.(Global Counsel, 2015) The FDI of Belgium in the UK amounts to close to 7 % of the GDP, and the revenue from them reaches 0.05 % of the GDP (ING, 2016).

Looking at the economic growth, the exit of UK would bring a 0.3-0.7 % cumulated GDP decline in 2016-2017 according to ING (ING, 2016). Before the British referendum, Kris Peeters, Minister of Employment, Economy, Consumer Affairs stated that the DGP slowdown caused by Brexit would cost Belgium €2.1 billion (Blomme, 2016). One should not forget about the impact on the labour market either: according the Belgian analysts, 12,000 workplaces could be lost due to the leave of the UK, which would pose a challenge to the country striving to reduce its relatively high, 8.7 % (Expansión, nd.) rate of unemployment. The Belgian construction industry is rather concerned about another possible phenomenon, the so-called *Brexodus* – the settling of Polish, Bulgarian, Rumanian employees in Belgium, who work in the construction industry in the UK now. This would lead to an intensified competition for the Belgian enterprises, since the companies (originating from Central-Eastern-Europe) could resettle to Belgian soil – the chance of which is quite large (De Redactie, 2016a). Regarding the economic sectors, the vehicle, chemical, textile, food, leather and shoe industries are the ones the most exposed to the negative impacts of Brexit. The financial markets of the two countries also have strong ties with each other – and any obstacles to the free movement of capital could harm the position of Belgium.

Another aspect of Brexit is also worth considering which might reduce the losses, although it is hard to predict its quantifiable consequences. In several sectors of the economy, there are companies operating in the UK, for which it is of primary importance to have access to EU markets. A possible consequence of the British exit might be, that these companies would relocate their headquarters in another country within the EU – and at this point, Belgium can be a possible target country. Prime Minister Charles Michel, mentioned in a radio interview that 20% of the companies settled in the UK would plan to relocate their operations. In this case, Belgium would like to attract as many of them as possible (De Redactie, 2016b). As far as the country's contribution to the EU is concerned, it might rise due to the exit of the UK. Belgium contributed by €3,660 million to the budget (from which €287.1 million is paid as part of the UK rebate), and receives €7,044 million in 2015 (European Parliament, 2015). In case of Brexit, although the rebate payment would end, the contribution to the budget might increase.

In case of Belgium, it is also important to evaluate the impact of the British exit on the three regions (Brussels Capital Region, Flanders, Wallonia). The volume of trade of the three with the UK is different, thus

Brexit would have diverse consequences on them. From the previously mentioned €18.3 billion of exports heading to Britain, the share of Brussels Capital Region is € 0.8 billion, that of Wallonia is €2.6 billion, and of Flanders is €15.2 billion (the UK is the fourth largest export market for the region; 83% of the Belgian exports originate from Flanders). Regarding the value of imports from the UK, Brussels Capital Region's part is €0.4 billion, while Wallonia's share is €1.1 billion, and Flanders proportion is €11.8 billion (approximately 88% of total imports of the country) (Lambrecht, 2016). In case of Wallonia, the exports to the UK amount to 7 % of the total exports of the region. Among the main export products, chemicals, machinery, optical products, metals, food products, and pharmaceuticals can be mentioned among others (Andersen, 2016b).

The exposure of the Flemish Region is the largest in case of Brexit, as the aforementioned figures show. The main export products are that of the food, chemical, pharmaceutical, and textile industry. According to pessimistic forecasts, the Flemish GDP might fall by 2.5% by 2030 (Torfs, 2016) in case of hard Brexit, and by 1.8% if the outcome would be a soft Brexit (Torfs, 2016). Trade relations with the UK would shrink, and jobs might be lost, although the exact impacts cannot be seen yet. What is the standpoint of Flanders regarding Brexit? Flemish Minister President Geert Bourgeois underlined the support for a soft Brexit, which would maintain free trade, but would have special arrangements (for closer cooperation) in the fields of R&D, energy, innovation, and North Sea issues (such as fisheries) (De Redactie, 2016c).

The internal affairs of the country might also be affected, since the political life intensified due to the Brexit. Disagreements surfaced between the two larger coalition partners (MR, N-VA) in relation with the European Union. The Walloon liberal MR is the fervent supporter of the EU, and would like to move towards a federal Europe (keeping in mind the vision of the founding fathers). The N-VA in contrast to it, belongs to the group of Eurosceptic parties, although it is important to underline that it does not aim to leave the EU (La Libre Belgique, 2016).

The rise of secessionism might be another possible impact of Brexit, which poses a greater challenge to Belgium. In case Scotland would decide to leave the UK, it might fuel Flemish separatism (Flanders Today, 2016) – and it would raise the problem of Belgian unity again.

Netherlands – stronger ties, greater exposure

One of the cornerstones of the foreign policy the Netherlands after the Second World War was integration, and multilateral cooperation. This latter started even during the war with the other two Benelux countries, and then the country joined the security and economic organisations of the Western European continent. Following the Second World War, the French-German reconciliation meant the pledge of peace for the Dutch – the European Coal and Steel Community and the organisations established by the Rome Treaties served this aim. The European integration itself became the framework for economic development for the Netherlands with creating a single market. The country was an advocate of the first enlargement and the accession of the UK to the European Community, partly because of the new markets and partly because of the pro-Atlantic stance of the British. The two countries found common grounds in certain questions, and developed close ties in those, although in some areas, their interests did not correspond within the integration. Prior to the referendum, the Netherlands supported the maintenance of British membership.

Among the Benelux countries, the number of the inhabitants and the size of the economy are the largest in case of the Netherlands. It has an open economy, which is dependent on the external markets, thus free trade and competition (alongside with maintaining international competitiveness) are important for the country (Janning, 2016). The economic and investors relations of the UK and the Netherlands have evolved to be strong during the years: the UK is the second most important trading partner for the country after Germany (Pieters, 2016d). Analysts agree that Brexit could have serious consequences for the Netherlands, and, compared to the other EU member states, the possible shrinkage of trading relations would affect this country the most.

The survey of CPB (Bollen et al., 2016) points out that Brexit could cause a 1.2% reduction of the Dutch DGP, and the loss in trade could reach €10 billion by 2030. In addition to it, the lack of trade-induced innovation could also add another 65% to the amount of projected loss. The study of Rojas-Romagosa differentiated between two models, the WTO model and the FTA one, and came to the conclusion that in the first case, the reduction of GDP would be 1.2% by 2030, and in the second one, the shrinkage would amount to 0.9% (Rojas-Romagosa, 2016). The forecast of Euler Hermes Netherlands predicts that the possible loss in exports could be 4.3% on a yearly basis, and could amount to €36.7 billion (De Telegraaf, 2016). Based on the 2014 figures, the value of Dutch exports to the UK was €50.7 billion, its share from the whole exports was 9.7%, which put the UK to the fourth place among the trading partners of the Netherlands. The value of imports from the UK amounted to €34.2 billion, representing 6.2% of the Dutch export, and making the UK the sixth most important import partner of the Netherlands (OEC, n.d.). The structural adjustment to the increasing costs of trade would be the most costly for this country according to the forecasts (Steen, 2016). The impact of Brexit on the capital flows should not be forgotten either, since the UK is the third largest source of FDI for the Netherlands (Korteweg, 2016).

Looking at the Dutch export sectors more closely, in case of those of which the UK is a considerable consumer market, like chemicals, plastics, and rubber products, electronic equipment, motor vehicles, and parts, food processing products, metals and minerals, CPB forecasts a possible 5% drop of production (Bollen et al., 2016). These product groups represent 12% of the Dutch GDP (AFP, 2016a). On the other hand, the so-called low-tech sectors and agriculture are less exposed to the impact of Brexit. The decline of production in the aforementioned sectors might result in the loss of jobs in the sectors concerned – according to CPB, the drop of employment would be around 0.5% in those sectors. On the other hand, in the low-tech industries and in the field of other financial serviced, the demand for labour could increase (Bollen et al., 2016), which might compensate the possible losses.

As was mentioned in the previous section, Brexit might lead to an exodus of companies that are settled now in the UK, and that would result in a certain competition among the EU member states to attract them. The Netherlands can be a favourable destination for relocation due to the country's endowments, and internal characteristics as well. The companies on the field of corporate serviced might head for the Netherlands, and within the country, Amsterdam and Rotterdam could become potential target destinations. The Deputy Mayor of Amsterdam, Kajsa Ollongren said in an interview following the Brexit referendum, that some companies had already shown some interest in relocating some of their operations from London to the Dutch capital (Lundberg, 2016). The Deputy Mayor referred to some Asian financial companies working in London, which showed interest in settling in Amsterdam (Pieters, 2016c). The Dutch capital is attractive for the companies for several reasons, such as the English knowledge of the employees, the nice environment, the cosmopolitan characteristic of the city, the international airport (Schiphol). However, the taxation rules might make the members of the financial sector think, since in the Netherland there is a 20% cap on the bonuses in the bank sector (Lundberg, 2016).

Regarding the EU policy of the state, the economic aspect of the integration had a primary importance for the Dutch. From the 1990s on, the EU policy of the country has become increasingly pragmatic, looking at the functioning of the integration in a critical way. From the beginning of the 2000s the approach of the political elite has become more critical, and Euroscepticism has been on the rise. In 2013, the government issued a list of 54 policy areas where the Netherlands would like to see a change in the distribution of powers, notably a shift towards the national instead of the EU level (Government of the Netherlands, 2013).

Brexit would also influence the power structure of the EU: the UK was among the three large players influencing the EU policies together with Germany and France. Without the British, the German-French tandem would remain influential within the Union. From the Dutch point of view, the UK was the one, that could counterbalance the tandem on the one hand (Dutch News, 2016b), and could be the country's ally with its economic liberalism and pro-Atlantic stance on the other hand. The British leave could raise the importance of the Netherlands for Germany and for the Scandinavian EU member states alongside their common interest (Janning, 2016), such as strengthening the Eurozone and the environmental policy.

The EU budget would also feel the impact of Brexit, since the UK is one of the largest contributors to it, thus both the income and the spending side would feel the changes. The losses in the income should either be compensated through increased contributions, or the structure of the expenditure should be revised. Some forecasts even predict that Brexit might cost another €750 million to the Netherlands, if the county would account for 5% of the budget afterwards as well (Dutch News, 2016a). Taking into account that the Netherlands is a net contributor, it is not very likely to support a major increase in the contribution – not at least without a reform of the expenditures (Dutch News, 2016b).

As for the internal political life of the Netherlands, the Eurosceptic voices became lauder following the Brexit referendum. Geert Wilders, leader of PVV welcomed the result of the referendum, and on June 28 he even initiated a Dutch referendum on the EU membership of the country in the Parliament – this was refused by the majority of MPs (Pieters, 2016b). Opinion polls show that the majority of the Dutch citizens do not want a referendum on the question, but in case there would be one, the majority would vote for continued EU membership (Pieters, 2016a).

Luxembourg – small country in the wind of changes

„Luxembourg has no future without the European Union" (Chronicle.lu, 2016) – affirmed the Prime Minister of Luxembourg, Xavier Bettel in his speech in the Parliament which was held following the Brexit referendum. Why does PM Bettel see the situation of the country this way? Due to its geostrategic position, Luxembourg has been a fervent advocate of the European integration process after 1945. The two world wars had devastating effects on the country – it became a victim of invasions in both wars as a neutral state. In the post-1945 era, one of the main priorities of the foreign policy of Luxembourg was securing peace in Europe (not least to ensure its own survival), the pledge of which was French-German reconciliation. The framework of it was the European integration, and the Grand Duchy became one of its founders. Another important objective for the country was to ensure the economic development and wellbeing of the inhabitants – and the integration could also contribute to it. Luxembourg has a small, open economy, so realisation of free trade among the six and the enlargement of the Community both served the interest of the country. Thus, it was an advocate of the first enlargement including the UK.

Although the Grand Duchy is one of the world's richest countries (it is ranked among the first three based on purchasing power parity GDP per person), Brexit could have a negative impact on the country as well. The earlier mentioned OECD Eonomic Outlook put Luxembourg into the groups of states that would suffer from the impacts of Brexit due to their relatively large economic exposure (Luxembourger Wort, 2016b). Other studies rank the country to the 14th place on the list of most exposed states (Global Counsel, 2015).

When looking at the trade relations of Luxembourg, in the case of the services exports (which makes a larger share of the whole exports), the UK is the second most important partner of the country. As for the service imports, the UK stands on the first place among the EU members. It should not be ignored either, that the British are the largest investors in Luxembourg, and the Luxembourgish capital also finds its way to the UK (Thelen, 2016). At the same time, the volume and value of the merchandise trade should not be forgotten either, and in this case, plastic and rubber products, machinery, vehicle equipments, electronic equipments and other products can be mentioned alongside with iron and steel products, etc form important elements of the export (Merler, 2016). All together, the export to the UK amounts to 8% of the GDP of the country (Reuters, 2016).

Luxembourg city is one of the financial centres of the continent. The sector of financial services is of paramount importance for the country, and comprises one third of the GDP. The assets of the investment funds operating in Luxembourg augmented to €3.5 trillion in 2015, making it the second largest centre for investor funds after the USA (Paul, 2015). The country's favourable economic background, the geostrategic situation of it, and the fact that the employees speak three languages, are all very attractive for the investors. Even before the Brexit referendum, some information leaked out considering the possibility that some firms operating in the financial sector and in other ones were planning to leave the City. The reason for it is that they would not like to leave the single market, since this way they would face narrowed opportunities (it might be especially true for the larger number of American firms operating in the sector of financial services). When relocation comes to the picture, Luxembourg could be a possible target destination (Huberty, 2016). If it was realised, that would increase the economic weight of the Grand Duchy, and would give a boost to the development of the financial services sector. Due to the possible moves of the financial market players, Luxembourg looks for the opportunities to make the country more attractive to the companies that plan to leave London. The signs of it are visible even now. On the one hand, in the beginning of July an advertisement occurred on the website of *Luxembourg for Finance,* the aim of which was to propagate the financial sector of the Grand Duchy for potential employees as well (Luxembourger Wort, 2016a). On the other hand, Economics Minister Etienne Schneider and Minister of finance Pierre Gramegna visited both London and Bristol between July 25 and 27, in order to promote Luxembourg as a good alternative for the business circles in case of Brexit (AFP, 2016b). However, looking at another aspect of it, the resettlement of companies would have effect on the infrastructure of the country, and could result in the upward movement of the property prices (Thelen, 2016).

Being a small country, Luxembourg was a fervent advocate of multilateralism, and membership in international organisations was a constant political aim of the country. The EU plays an outstanding role for the country, partly because of the aim to establish economic prosperity and welfare, partly because of the aim to preserve the independence of the Grand Duchy. It is a unique Luxemburgish interest that the EU institutions situated in the country and their employees would remain, and besides that, it is also an interest of the state to preserve the influence of small states in the organs of the EU (Hey, 2002). Brexit would have an impact on the EU budget – it can be an issue, whether the reduction of administrative expenditure of the EU would be put onto the agenda together with the reduction of the number of employees working for the EU administration due to the changing nature of the budget. This would pose a challenge for Luxembourg, partly because of the local characteristics (property market, local consumption), and partly because at the moment, the country receives a significant amount from the EU budget to finance the operation of the EU institutions. Parallel with Brexit, the German-French tandem would become stronger, and the relative position of the other member states would change within the EU. Luxembourg is an advocate of free trade, and of the single market – and regarding these issues, it found a common stance with the UK. Thus the country would lose an ally in these issues. On the other hand, following Brexit the EU might further integration on policy areas that are important for the Grand Duchy, such as the Eurozone.

The interests of Luxembourg and the objectives of the EU coincide in most areas, so for the Grand Duchy, the membership in the EU can also be regarded as an instrument to increase its influence in the international arena. Thus the relative size and the global weight of the EU is important for the country. The inhabitants of the UK amount to 13 % of the EU's total number of inhabitants, and the British GDP is 17 % of that of the EU – thus, with Brexit, the integration would become weaker on a global level. Together with it, Luxembourg as a member state of the integration would weaken as well (Huberty, 2016). It is not surprising then, that for the country Bremain would have been a better choice – according to an opinion poll conducted in May 2016, 86 % of the people asked articulated this opinion (Luxembourger Wort 2016c). In the new situation following the referendum, the country's main aim is to end the uncertainties around Brexit, and to conclude a beneficial agreement.

Conclusion

Considering the economic consequences of Brexit, all the three Benelux states would face challenges – although the extent and area of them would be diverse. The exposure of the three open economies is significant, thus facing barriers in the trade relations with the UK (in case of hard Brexit, if the country would be outside the single market) would result in the reduction of exports of the three countries. Soft Brexit could also have similar impact on the export relations, though the extent of the decline might be smaller. Export would also be affected by the changes of the exchange rates of the Sterling – following the referendum, the financial markets reacted nervously, and the UK had to face approximately 10 % depreciation against the dollar and the Euro, and it could not gain back its pre-referendum value. In the beginning of December 2016, after David Davis, secretary of state for Brexit stated that the UK was willing to pay to the EU to have further access to the single market (Cuskelly, 2016), the value of the Sterling appreciated. The consequence of it is that the products of the Eurozone became more expensive in the UK, which would in its own result in declining exports. Both investments and the financial markets might be effected negatively by the exit of the UK. The labour markets of the three states might also face challenges because of the consequences of reducing trade with the UK. As was mentioned earlier, the economic consequences of soft Brexit would be less harmful for the three states.

On the other hand, there is another possible impact of Brexit, which might reduce the extent of losses in case the UK would not retain access to the single market. Those companies, which are afraid of losing the advantages of the single market in case of exit, might relocate their operations to the continent. In this case, all the three Benelux states could become potential target countries – and also each others' competitors. However, the exact impacts and processes cannot be seen now, since the exit talks might take a rather long time. The outcome of the negotiations, namely the type of exit agreement (hard or soft) could also have different impacts on the economies of the Benelux states, since their interest is to keep the UK in the single market.

The EU as an economic block would weaken due to the Brexit, which effect the three states unfavourably. Considering the internal distribution of powers within the EU, the exit of the UK would result in the strengthening of the French-German tandem, and the pro-Atlantic states would lose an ally. Another negative consequence of the Brexit would be the rise of popularity of the (hard) Eurosceptic parties.

The standpoint of the Benelux countries coincide in terms of regarding uncertainty the worst case – their interest is to start exit negotiations as soon as possible. As for the outcome of the negotiations, the three states are for retaining the access of UK to the single market – but not at all costs.

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