Study Report On

BRITAIN SEPARATION FROM EUROPEON UNION

BREXIT

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BRITAIN EXIT FROM EUROPE – IMPACT ON PAKISTAN ECONOMY

A referendum was held on Thursday 23 June, to decide whether the UK should leave or remain in the European Union.

Leave vote: 52%

The referendum turnout was 71.8%, with more than 30 million people voting. It was the highest turnout in a UK-wide vote since the 1992 general election.

What does Brexit mean?

It is a word that has become used as a shorthand way of saying the UK leaving the EU - merging the words Britain and exit to get Brexit, in a same way as a Greek exit from the EU was dubbed Grexit in the past.

Breakdown across the UK

Historical perspective of European Union:

The European Union grew out of a desire for peace in a war-torn and divided continent. Five years after World War II ended, France and Germany came up with a plan to ensure their two countries would never go to war against each other again. The result was a deal signed by six nations to pool their coal and steel resources in 1950.

Seven years later a treaty signed in Rome created the European Economic Community (EEC) - the foundations of today's European Union. **The UK was one of three new members to join in the first wave of expansion in 1973. Today the EU has 28 member states with a total population of more than 500 million.**

The EU has grown steadily from its six founding members to 28 countries.

Belgium,

France,

Germany,

Italy,

Luxembourg and the

Netherlands signed up to the EEC, or Common Market in 1957.

Britain, Ireland and Denmark joined in the first wave of expansion in 1973, followed by Greece in 1981 and Portugal and Spain five years later.

Eastern Germany joined after unification and

Austria, Finland and Sweden became part of the EU in 1995.

The biggest enlargement came in 2004 when 10 new member countries joined. Romania and Bulgaria joined in 2007 and Croatia was latest to sign up in 2013.

STRENGTH OF EUROPEAN UNION

The European Union - often known as the EU - is an economic and political partnership involving 28 European countries.

Member countries of the EU (year of entry)

Austria (1995)	Germany (1958)	Poland (2004)
Belgium (1958)	Greece (1981)	Portugal (1986)
Bulgaria (2007)	Hungary (2004)	Romania (2007)
Croatia (2013)	Ireland (1973)	Slovakia (2004)
Cyprus (2004)	Italy (1958)	Slovenia (2004)
Czech Republic (2004)	Latvia (2004)	Spain (1986)
Denmark (1973)	Lithuania (2004)	Sweden (1995)
Estonia (2004)	Luxembourg (1958)	United Kingdom (1973)
Finland (1995)	Malta (2004)	
France (1958)	Netherlands (1958)	

It has since grown to become a **"single market"** allowing goods and people to move around, basically as if the member states were one country.

Countries using the Euro

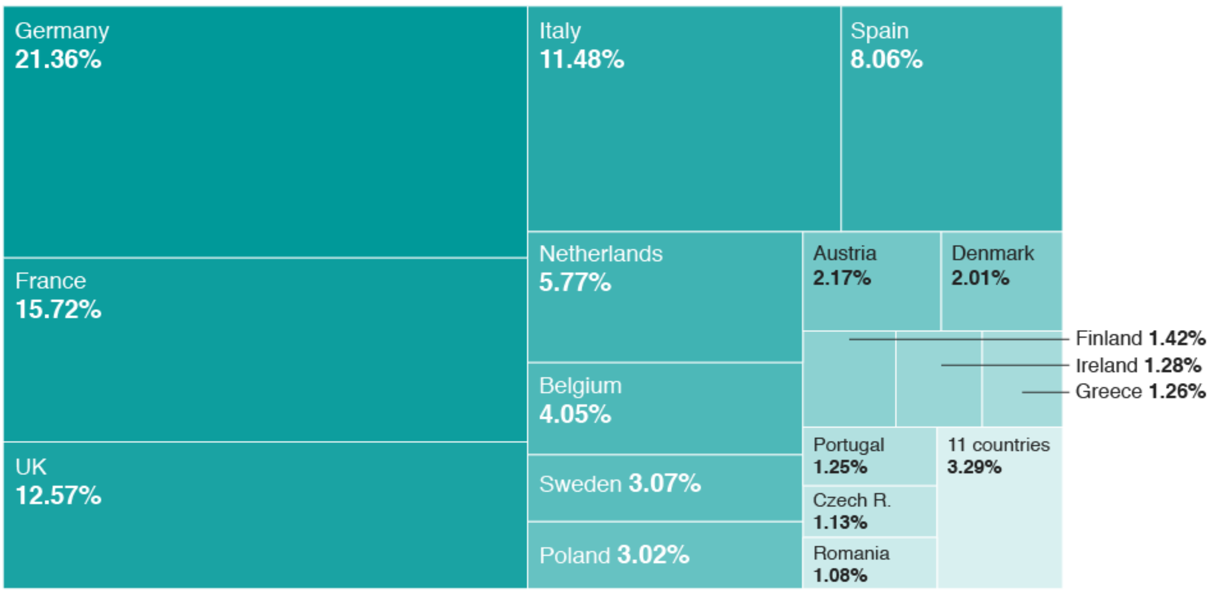
Austria	Germany	Portugal
Andorra	Ireland	Slovakia
Belgium	Italy	Slovenia
Cyprus	Kosovo	San Marino
Estonia	Lithuania	Spain
Finland	Luxembourg	Vatican City
France	Montenegro	Monaco
Greece	Netherlands	Malta
Latvia		

How does the EU work?

There are four key institutions which work together to run the EU - the European Commission, the European Parliament, the European Council and the Court of Justice.

What does it all cost?

2015 EU budget 145bn euros: Contributions by country (%)

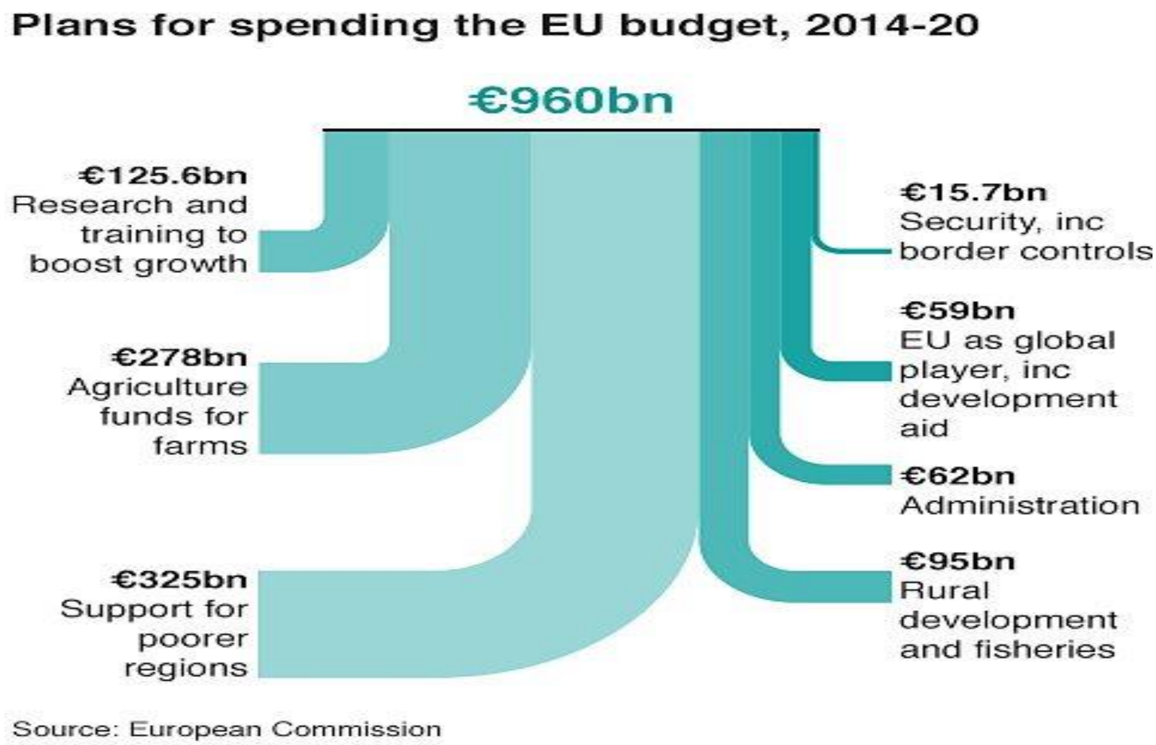


Source: European Commission/HM Treasury

The UK's estimated net contribution in 2015 was £8.5bn - according to Treasury figures. Each country receives money back from the EU to support development and other projects. **The UK also gets a rebate, or money back, on its contribution, because much of the budget is spent on agricultural subsidies and the UK does not gain nearly as much as other countries like France.** After all repayments were taken into account in 2015, Britain contributed about 12.6% of the entire EU budget. Germany paid the largest share, 21.36% and France was the second-biggest contributor at 15.72%.

How does the EU spend its money?

Sankey chart showing how EU budget is spent on different sector



The EEC started out as a trading bloc - with free movement of goods and services within the Common Market - now its interests include reducing regional inequalities, preserving the environment, promoting human rights and investing in education and research.

The EU is Britain's biggest trading partner. British citizens are free to work in any EU country and EU funding is spent on supporting farmers, boosting jobs in the UK, redeveloping rundown areas, and grants for university research. The EU has contributed to cheaper travel by challenging monopolies and boosting competition. It has reduced the cost of mobile data roaming and set water quality standards in Europe.

REASONS BEHIND THE BREXIT

But giving subsidies to farmers led to over-supply of some crops and so the EU was forced to rethink its agriculture policy. Critics say the EU has taken too much power from the UK government, its regulations are costly to the British economy and without them, Britain would be able to sign other trade deals with growing economies like China and India. They also say that the EU wastes taxpayers' money on excessive bureaucracy - citing MEPs monthly trips to Strasbourg which cost 180m euros (£136m) per yen.

Why is there a referendum?

Prime Minister David Cameron wants Britain to remain in the EU

The British government has promised to hold a referendum on EU membership before the end of 2017. There have been growing calls for a vote on whether to stay or leave the union, as it has grown and become more powerful.

CONSEQUENCES OF BREXIT

- For the UK to leave the EU it has to invoke an agreement called Article 50 of the Lisbon Treaty.
- Cameron or his successor needs to decide when to invoke this - that will then set in motion the formal legal process of withdrawing from the EU, and give the UK two years to negotiate its withdrawal.
- Mr Cameron has said he will be stepping down as PM by October.
- The article has only been in force since late 2009 and it hasn't been tested yet, so no-one really knows how the Brexit process will work, according to BBC legal correspondent Clive Coleman.
- EU law still stands in the UK until it ceases being a member - and that process could take some time.
- The UK will continue to abide by EU treaties and laws, but not take part in any decision-making, as it negotiates a withdrawal agreement and the terms of its relationship with the now 27 nation bloc.

Has any other member state ever left the EU?

No nation state has ever left the EU.

IMPACT OF BREXIT ON PAKISTAN ECONOMY AND EXPORTS

Country's exports, which are expected to be around $ 20.9 billion in 2015-16, 12.4 per cent or $ 4.6 billion, are less than the target of $ 25.5 billion set in Strategic Trade Policy Framework (STPF) 2015-18.

Brexit has suddenly created new challenges for Pakistan as follows:-

In GSP-plus Pakistan will have following three impacts:

(i) UK was Pakistan's biggest supporter in the European Union (EU) and when UK exits from the EU, Pakistan has to find new friends able to maintain the concessionary regime of the EU;

(ii) When the UK exits the EU after two years, Pakistan has to negotiate a request for similar arrangements with UK itself but whether the UK will accept it or not would be in question;

(iii) If the UK doesn't get a sweeter deal with the EU and the UK products face some duties in the EU, then Pakistani products which are channeled to the EU through the UK will also face tariff issue. The UK is 20 per cent of Pakistan's total exports to the EU.

(iv) When the EU will become less important for the UK then Commonwealth bloc will get importance as intra Commonwealth trade will overtake intra EU trade by 2017 which implies that Commonwealth will be a major player. However, major challenge for Pakistan in intra Commonwealth trade will be that India will be the major player and Pakistan will be secondary player in the market.

(v) with the Sterling and Euro down, the UK and EU's imports would be more expensive and that alone is going to have a significant impact on Pakistan's trade, at least in the short run. The reduced appetite in the region will weigh on our textile businesses, which will be seeing lower margins as is due to the fall in the currencies. Regionally, the Indian Rupee and Vietnamese Dong have also appreciated against the GBP by around the same – 11 percent. So, at least there's no threat of exchange rates causing a relative disadvantage. **However, we might see imports from the regions spike, as they are now relatively cheaper.**

(vi) Britain will now have to renegotiate all its trade agreements. Government of Pakistan will start inter-ministerial consultations regarding an FTA with Britain as "GSP Plus benefits may be threatened in the event that the country decides not to accord the same preferences." The biggest customer of our GSP Plus exports was the UK and now they might be a little hot on the negotiating table,

not as eager to allow duty-free inflows from certain countries in light of the prevailing circumstances.

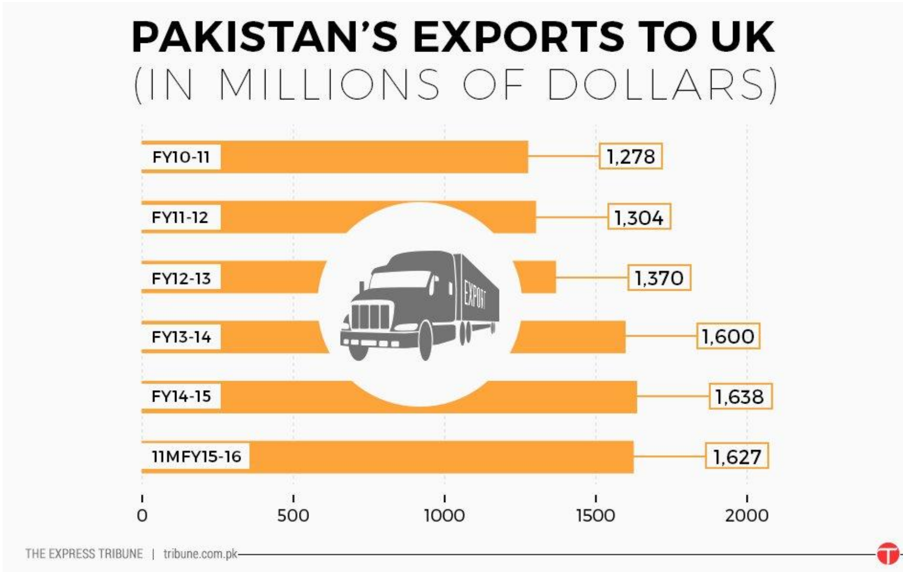
(vii) In another sign that Pakistan's exports will continue to fall, some analysts as well as stakeholders are upset over UK's decision to exit the European Union, saying that the development is more negative than it is neutral for the economy.

(viii) Pakistan's stock market falls over 1,400 points in the aftermath of UK's historical referendum, with textile and auto sectors bearing the brunt of the decision.

(ix) The threat came amid expectations that Pakistan's exports, majority of which are textile-related, will be decreased to the European Union (EU) after UK exits the 28-nation trading bloc.

(x) At a time when world's markets are reeling with uncertainty, some analysts say the negative impact emanating from Brexit will be comparatively less for Pakistan's economy as it is relatively insulated from global markets. The reason is that Pakistan's exports are only 7% of the country's total Gross Domestic product (GDP).

(xi) Since the EU is the largest trading partner of Pakistan, exporters are concerned that political uncertainty in Europe, depreciation of the euro and the pound sterling may slow down their exports even further in the coming months. A weaker euro and pound sterling makes Pakistan's exports relatively expensive, causing demand to drop, while a slowdown in foreign economies is also likely to result in declining imports.



Negative implications

- ***It is clear that 8 percent of Pakistan's total exports (Valued $ 1.6 billion) go to United Kingdom. Since the EU is the largest trading partner of Pakistan, the political uncertainty in Europe and UK, the depreciation of the euro and the pound sterling may tumble Pakistan's exports.***
- ***Pak Rupee will appreciate against a depreciated euro and pound sterling.***

1. **Another unavoidable negative impact would be on around $ 1.8 billion remittances coming from the UK. Due to depreciation of the pound sterling by 11 percent during the past few days the real value of remittances from the UK would also be down by 11 percent for recipients.**
2. **Another adverse effect would be the UK's possible cut in about $ 2 billion grants-in aid-in for development of Pakistan social and development sectors.**

- **Traditionally a Conservative government has been sympathetic to Pakistan's causes. Thus, the political turmoil and uncertainly in the UK will negatively affect Pakistan's economy.**
- **Foreign Direct Investment (FDI) in Pakistan would also be adversely affected as the UK had been the biggest foreign investor in Pakistan so far. Since future of the United Kingdom seems to be uncertain the FDI will surely be hit hard.**

Textile:

- The EU awarded the Generalized System of Preferences (GSP) Plus status to Pakistan in December 2013 for the next 10 years, which has already helped the country in adding over $1 billion per year in its exports since January 2014. Exporters are worried whether Pakistan will receive the same benefits once Britain exits the EU.
- However, since Pakistan has good political relations with the UK and the country also supported Pakistan's case within the EU in gaining GSP Plus status, some exporters believe Pakistan will succeed in getting the same duty concessions from the UK.
- Publicly traded textile companies will also take a hit as a result of Brexit. Textiles constitute more than half of Pakistan's exports, with the EU being one of the major destinations of Pakistani products. Investors expect export-oriented listed companies in the textile sector to take a hit going forward, as a cheaper sterling will make Pakistani exports less competitive in the UK.
- The textile sector will be affected as a weaker pound sterling and the euro (down 2.3% in a single day) will render Pakistan's exports more expensive.
- Out of total Pakistan's textile exports of $11.6 billion during the first 11 months (Jul-May) of current fiscal year 2015-16, textile exports' share to the UK was $1.2 billion (10%).

<u>GLOBAL MARKETS:</u>

The Brexit resulted in global markets coming crashing down with pound sterling and the euro taking a massive hit. On the other hand, safe havens like the yen and gold appreciated significantly. The appreciated yen was trading at 101.9 against the dollar, up by 3% as of yesterday. The yen also appreciated about 3% against the Pakistan rupee on Friday.

Gold price increases 3%, will continue to rise

The price of the precious metal increased 3% overnight in the local market, as Britain decided to leave the European Union.

With the sterling undergoing the biggest one-day drop of over 10% against the dollar, international investors turned to safe-haven assets, thus increasing the gold price 5.3% to over $1,326 per ounce in one day.

As a result, the local price of gold surged Rs1,500 to Rs50,200 per tola (11.6 grams) in just 24 hours, according to All Sindh Saraf and Jewellers Association (ASSJA).

ASSJA President Haroon Rashid Chand said gold prices are expected to keep rising in the next few weeks. “The sterling is losing value … people want to avoid volatility in the currency market. Gold prices will gain strength in the near future,” he said.

Gold’s consumer demand in Pakistan in the first three months of 2016 recorded a major increase on a year-on-year basis, according to statistics on global gold demand released by the World Gold Council (WGC).

It clocked up at 9.4 tonnes in Jan-Mar, showing an increase of 12% from consumer demand of 8.4 tonnes in the same quarter of the preceding year.

Consumer demand of gold consists of two major categories: jewellery demand and total bar and coin demand. The year-on-year increase in the country’s consumer demand for the Jan-Mar quarter in each category was 13.2% and 9.6%, respectively, according to WGC.

Pakistan’s share in the global consumer demand of gold is miniscule. With world consumer demand at 735.8 tonnes in the first quarter of 2016, Pakistan’s share was less than 1.3%. Given the small size of the Pakistani gold market, local prices are determined largely in line with global trends.

Stocks Fall as textile, auto, oil take beating

In a sign of increasing interconnectedness with the rest of the global economy, the Pakistan Stock Exchange (PSX) took a hit on Friday following Britain’s decision to leave the European Union (EU).

Brexit-induced panic selling on the Karachi bourse resulted in the benchmark index shedding 848 points, down 2.2% from a day earlier. After losing over 1,400 points in early trading, the KSE-100 Index recovered some losses to close at 37,389.88.

> **The decision of the United Kingdom (UK), which constitutes about one-sixth of the economic output of the EU, to quit the economic bloc will have a direct impact on at least two sectors of the Pakistan economy: automobile and textiles. The investors would surely take long time for their future investments in stock exchanges that have already lost $ 2.8 trillion in the first jolt all over the world.**

Silver lining would be if the future British government gave more importance to strengthen the Common Wealth Organization that includes fifty former colonies of the Great Britain, including

Pakistan, India, Canada and Australia It would have positive effects on the economies of these countries if UK works for free trade and movements among members of the Common Wealth Organization in future.

Trade volumes increased 108.4% to 236.8 million shares compared with Thursday's tally of 113.6 million shares.

Shares of 341 companies were traded. At the end of the day, 44 stocks closed higher, 276 declined while 21 remained unchanged. The value of shares traded during the day was Rs15.3 billion, up 131.5% from Thursday.

K-Electric Limited was the volume leader with 24.1 million shares, losing Rs0.14 to finish at Rs7.76. It was followed by World Call Telecom with 15.2 million shares, gaining Rs0.37 to close at Rs1.96 and Dewan Cement with 13.1 million shares, gaining Rs0.42 to close at Rs14.84.

Foreign institutional investors were net sellers of Rs506.1 million during the trading session, according to data maintained by the National Clearing Company of Pakistan Limited