

Deloitte Brexit Briefing | 2  
**Brexit Scenarios 2.0**

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# Introduction

## Scenario design is required to manage the high uncertainty and complexity resulting from the Brexit

Since the British referendum about the United Kingdom's exit from the European Union, held in June 2016, the 'Brexit' has dominated political and media agendas, as well as those in many companies.

The Brexit will have far-reaching consequences, both for the United Kingdom and for the economic and political landscape of the European Union. The impact of the departure of the second-largest EU economy will be a great uncertainty among investors and entrepreneurs in the coming years.

In particular, threats to business models and value chains of European companies with connections to Great Britain or Northern Ireland arise from potential legal divergences and trade barriers. In addition, the Brexit poses risks to British and European economies, volatility in the financial markets, and existing

investments in the European Union or the United Kingdom. On the operational side, numerous legal and tax risks arise for European companies, as well as restrictions on the free movement of workers.

In order to enable an early response to emerging opportunities and risks, it is necessary to determine the exposure of industries and individual business units to Brexit risks and to take appropriate preparatory measures.

The challenge is to capture the high uncertainty and complexity of the current economic and political situation and to develop suitable solutions on the basis of individual needs for action.

# Introduction

## New insights require a refinement of the previous scenarios

By breaking down and analyzing the current complexities and uncertainties, Brexit scenarios provide the clarity, flexibility and capacity to act required to develop future-proof strategies. Scenarios offer a clear understanding of potential negotiation outcomes and form a key basis for Brexit-related decision-making.

Prime Minister Theresa May's plans for a hard Brexit demonstrate that as well as our [original scenarios for the future](#), other options are now thinkable, which could significantly alter the relationship between the United Kingdom and the European Union.

Theresa May plans both an end to British membership in the EU Single Market and in the European customs union. Free trade agreements are intended to ensure ongoing maximum access to the EU Single Market.

The UK no longer wants to submit to EU membership fees or the judgments of the European Court of Justice. Immigration limits also spell the end of free movement of people to and from the United Kingdom.

While the EU's willingness to compromise will have to be seen, this new knowledge allows us to identify specific trading models that could determine the future relationship between the EU and the United Kingdom.

# Methodology

## Future EU-UK trade relationships and the EU's internal organization will determine the magnitude of Brexit consequences

We have therefore expanded on our original four scenarios, casting a new light on our previous assumptions from three distinct perspectives.

The occurrence of any Brexit consequences, and their magnitude, depend on the one hand on the success of negotiations with regard to future trade relations between the EU and the UK. The option of a liberal or a protectionist policy line allows for various scenarios and trade models, such as a continental partnership, a customs union, a comprehensive free trade agreement or a return to WTO rules. Consequently, the first critical uncertainty of our scenario analysis can be defined as:

1. The formal relationship between the European Union and the United Kingdom

On the other hand, the magnitude will also be determined by the future internal organization of the European Union. There could be different scenarios here, too: economic and political disintegration, as opposed to further integration between EU Member States.

Possible visions of the political future include the formation of a common European government, the optimization of the European Union's current organization, a step back to a looser federation, or a return to autonomous nation states. As a result, the second critical uncertainty of our scenario framework is represented by:

2. The political integration of the European Union

# Methodology

## Three critical uncertainties characterize the post-Brexit future

On the economic side, as well as the continuation of the current Economic and Monetary Union, other possibilities are a reduction to the European Single Market, a pure customs union, or free trade agreements. Thus, the third critical uncertainty of our analysis refers to:

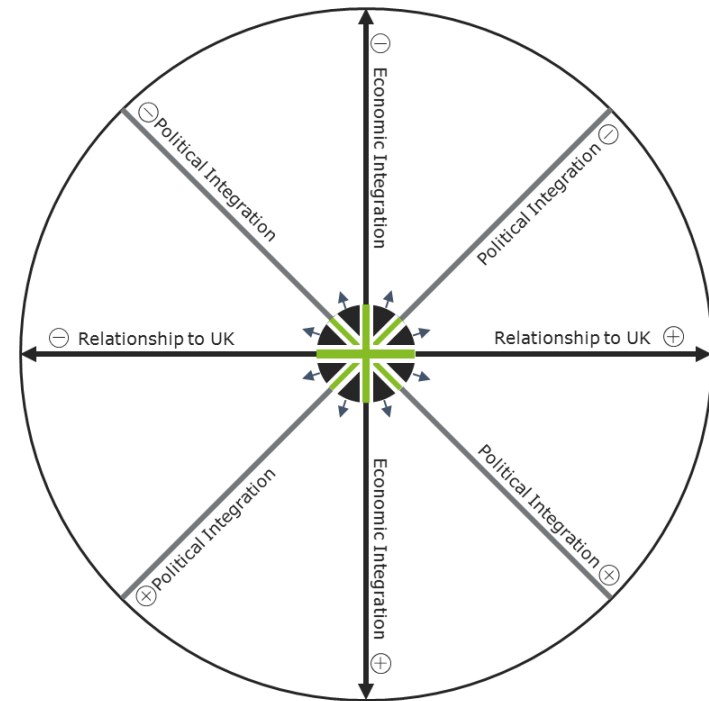
### 3. The economic integration of the European Union

The combination of these three critical uncertainties results in eight visions of the future, differentiated with regard to internal European organization and openness to trade.

The further course of the exit negotiations will show which Brexit scenario is most likely to occur, and which strategies and measures will need to be developed to

successfully counteract the effects of the Brexit.

Let us look into the future again and see possible Brexit scenarios in 2025.



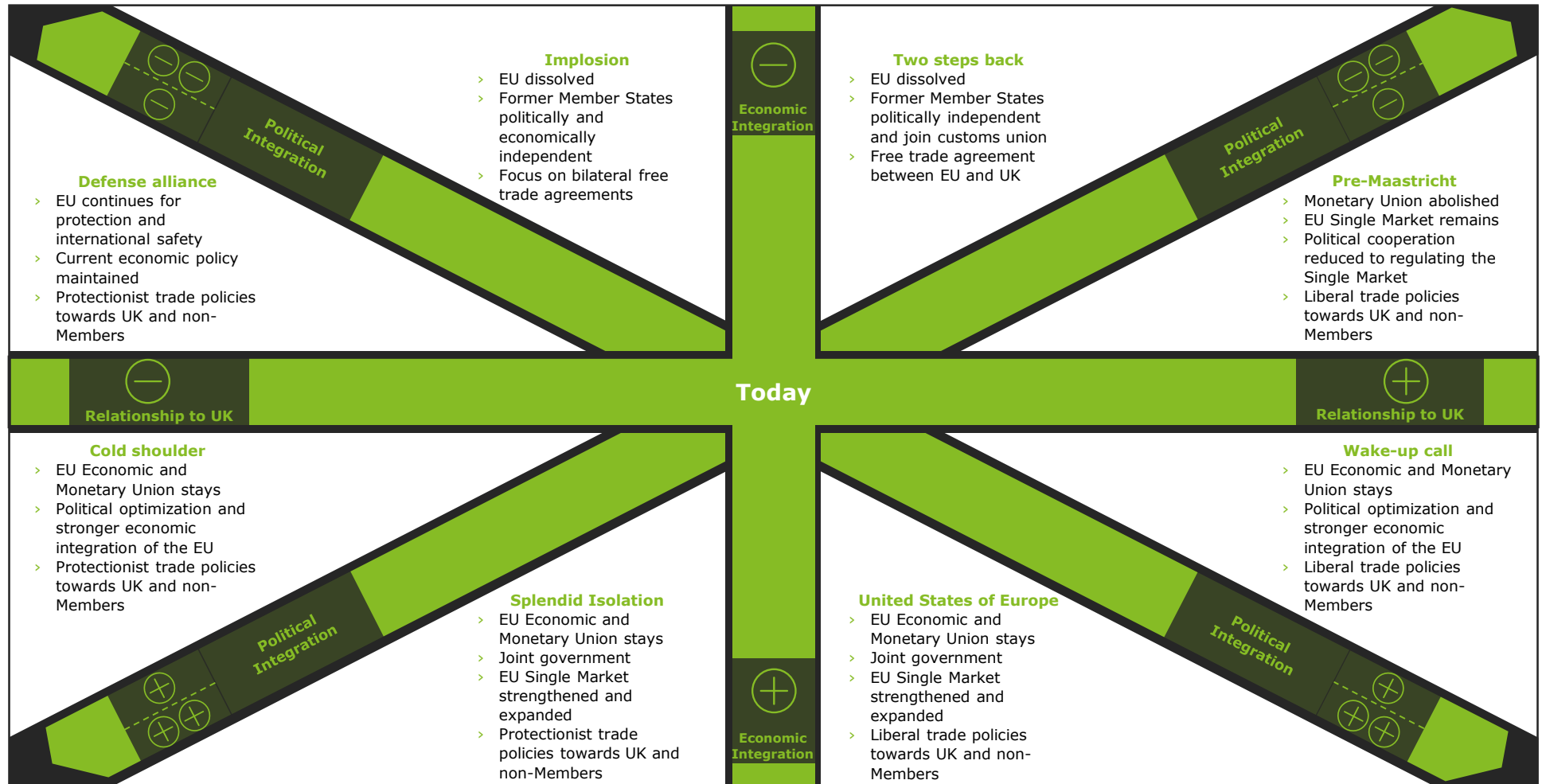


# **Executive Summary**

Our most important findings

# The scenarios, illustrated

Combining the variables yields eight visions of the future



# The scenarios, tabulated

Differences result from the various trade and integration models

Scenario	Trade relationship EU - UK	EU Political Integration	EU Economic Integration
1. Two steps back	+ Free trade agreement	- - Autonomous states	- Customs union
2. Pre-Maastricht	+ Free trade agreement or customs union	- Loose alliance of states	- European Single Market
3. Wake-up call	+ Free trade agreement or customs union	+ Optimized European Union	+ Optimized Economic and Monetary Union
4. United States of Europe	+ Continental Partnership	+ + Central EU Government	+ Optimized Economic and Monetary Union
5. Splendid Isolation	- WTO Membership	+ + Central EU Government	+ Optimized Economic and Monetary Union
6. Cold shoulder	- WTO Membership	+ Optimized European Union	+ Optimized Economic and Monetary Union
7. Defense alliance	- WTO Membership	- European Union (limited cooperation)	- Reduced Economic and Monetary Union
8. Implosion	- Free trade agreement	- - Autonomous states	- Free trade agreement





# **Brexit scenarios in detail**

A concrete description

# Scenario 1

## Two steps back



**Relationship to UK:** + | **EU Political Integration:** - - | **EU Economic Integration:** -

The European Economic and Monetary Union has been dissolved. The former EU Member States are politically independent and have organized themselves in a new customs union so that they can continue to trade goods and services without paying customs duties. No agreement has been reached so far with regard to the free movement of capital.

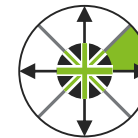
The lack of political coordination, as well as increasing divergences between national laws, lead to non-tariff trade barriers, which makes trading between countries more difficult.

Free trade agreements have been concluded with the United Kingdom, allowing duty-free movement of goods as well as selected services. The previous free movement of persons and workers between the former Member States has been abolished for security reasons.

Considering the economic and political regression, the European Community is similar to its beginnings in the 1960s.

# Scenario 2

## Pre-Maastricht



**Relationship to UK:** + | **EU Political Integration:** - | **EU Economic Integration:** -

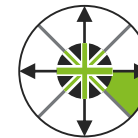
The European Community has regressed to its form in the late 1980s, before the Maastricht Treaty. Demands by EU Member States for more independence have led to the dissolution of the European Monetary Union, the European Commission, and the European Court of Justice.

The European Single Market has been maintained to allow the free movement of goods, services and capital. The free movement of persons was restricted by national immigration and visa regulations. Political coordination between Member States has been reduced to joint market organization.

The majority of political decisions are made at a national level. Free trade agreements with the United Kingdom regulate the free movement of goods, and restricted movement of services and capital. As part of the EU Single Market, the UK is consulted on issues affecting the common market.

# Scenario 3

## Wake-up call



**Relationship to UK:** + | **EU Political Integration:** + | **EU Economic Integration:** +

Political turmoil after the Brexit showed the EU the necessity and urgency of change. The EU has moved closer together as an economic and monetary union in order to further promote the power of the four freedoms of the Single Market.

Progress in economic integration has resulted in the strengthening and expansion of the Single Market into a digital internal market.

This was made possible, in particular, by more effective policy-making and ratification processes, as well as the harmonization of economic, fiscal and labor market policies across Europe.

Liberal trade agreements with the UK allow for duty-free trade in goods, as well as restricted services and capital movements. The free movement of persons and workers was abolished in the course of the Brexit. Due to the British connection to the European Single Market, the UK was granted a right to be consulted on internal market issues.

# Scenario 4

## United States of Europe



**Relationship to UK:** + | **EU Political Integration:** ++ | **EU Economic Integration:** +

The EU exit by the United Kingdom and other former EU Member States has reduced the European Economic and Monetary Union to its core. The determination of the new federation of states resulted in the introduction of a common European government, to which national decision-making competences have been transferred.

The centralization of economic and fiscal policy has greatly increased the digitization, value creation and competitiveness of the European Single Market.

The former Member States have been granted access to the EU Single Market through continental partnerships, which allow them to trade and/or move goods, and to a limited extent services and capital. The free movement of persons is limited to temporary periods.

In return for continued EU contribution payments, partner countries are given a voice in matters between countries as well as a political right to be heard on issues relating to the EU Single Market. Coordination in the fields of foreign, security and defense policy remains in place.

The resulting model is similar to that of the United States of America in 2016.

# Scenario 5

## Splendid Isolation



**Relationship to UK:** - | **EU Political Integration:** ++ | **EU Economic Integration:** +

The Brexit caused other Member States to leave the EU. The remaining members used this as an opportunity to intensify the economic integration of the Economic and Monetary Union by establishing a common EU government in order to further promote the European idea of an integrated federation of states.

National markets were merged into a single, digitized market and strengthened the industrial base of the EU.

In order to promote the independence of the European Single Market and to sanction former Member States, protectionist trade barriers were introduced against non-Member States and trade relations were reduced to WTO conditions.

As a result, there has been a sharp decline in global trade, leading to the emergence of new trading blocks.

The world seems like a modern remake of the United Kingdom's 'Splendid Isolation' during the 19th century.

# Scenario 6

## Cold shoulder



**Relationship to UK:** - | **EU Political Integration:** + | **EU Economic Integration:** +

Hard Brexit negotiations led to a distancing of the EU from the UK. The other 27 Member States feared further EU exits after the Brexit, and this triggered a wave of optimization measures to resolve critical issues in the European Economic and Monetary Union.

In addition to the harmonization of economic, fiscal, and labor market policies, policy-making and ratification procedures were made more efficient to reduce bureaucracy.

In the course of closer political cooperation, there was also a push towards strengthening and developing the common European market into a digital internal market, which significantly increased the EU's economic power and competitiveness.

Tariff and non-tariff barriers were introduced as a result of a protectionist trade policy with the aim of increasing the autonomy of the EU Single Market and preventing further EU exits.

Trade relations with former Member States were reduced to their common WTO membership as a means of sanctioning.

As a consequence, the new European model resembles the United States of America during the 1920s.

# Scenario 7

## Defense alliance



**Relationship to UK:** - | **EU Political Integration:** - | **EU Economic Integration:** -

The British exit from the EU did not bring about hoped-for optimization initiatives in the European Economic and Monetary Union. The political and economic situation carried on without further integration or disintegration being pursued.

The EU is maintained above all for its security function - internally for its members and externally to preserve international power structures. Due to power ambitions by continental European countries outside the EU, political cooperation focuses on joint foreign, security, and defense policy.

Political coordination between Member States has been reduced to joint market organization to ensure the free movement of goods, services, and capital.

The free movement of persons was restricted through individual regulations at the national level.

Protectionist trade policies seal off the European Single Market through trade barriers, in order to reduce the attractiveness of further EU exits and to ensure economic independence.

This world is reminiscent of the idea of a European defense community in the 1950s and '60s.



# Scenario 8

## Implosion



**Relationship to UK:** - | **EU Political Integration:** - - | **EU Economic Integration:** -

The project of an integrated European federation has failed. The European Economic and Monetary Union has been completely dissolved. The former Member States act independently according to their national interests and sovereignty.

Bilateral trade agreements between individual Member States ensure the free movement of goods, and restricted movement of services and capital. The free movement of persons was abolished.

Owing to the low level of political coordination and the growing divergences between national legislation, non-tariff trade barriers were created, which make trade between countries even more difficult.

As a result, the world is like Europe in the 1920s.



## **Implications & Conclusion**

A consideration of the consequences

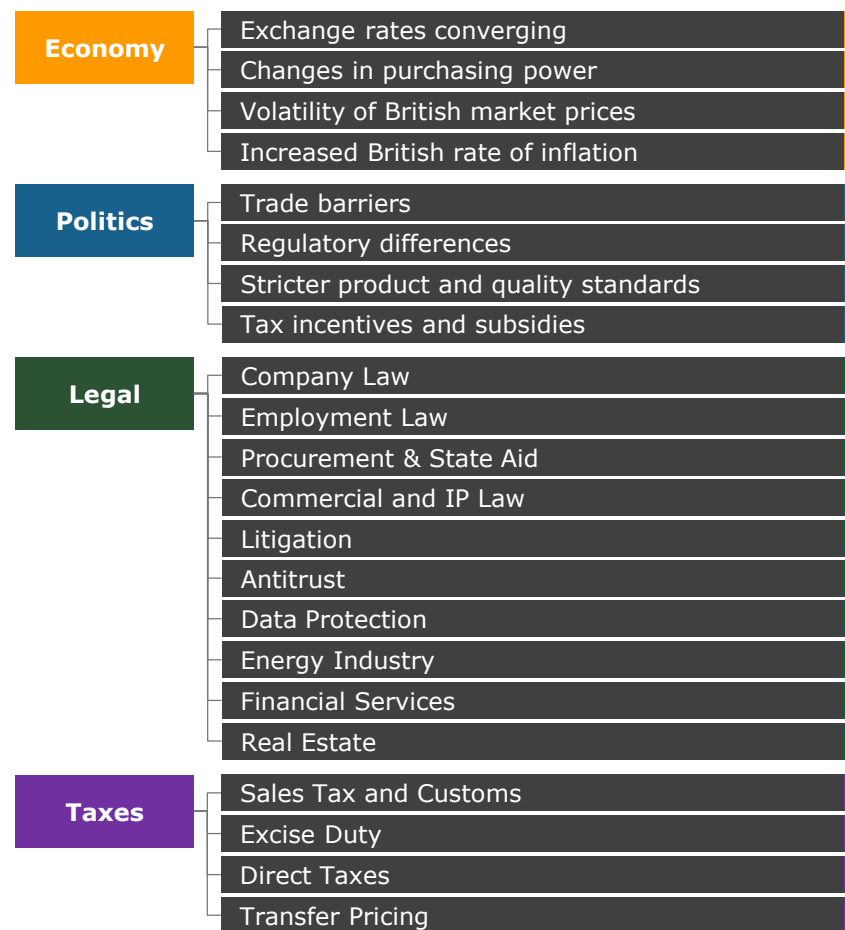
# An overview of implications

Depending on the future scenario, the Brexit affects different business and topic areas

In addition to economic implications, such as the convergence of the euro-pound exchange rate, increased inflationary pressure, market price volatility, and changes in purchasing power, especially high risks arise for companies through trade barriers and regulatory divergences.

In addition to trading companies, the early effects of the Brexit particularly hit the automotive sector, the transport and logistics sector, and the financial and insurance industries.

This requires a holistic analysis of the Brexit risk potential with regard to the industrial landscape as well as the various business sectors and functions. The majority of potential risks result from the following factors:



# Conclusion

The variety of potential Brexit scenarios and implications requires strong vigilance and strategic foresight

Although the range of possible post-Brexit models of cooperation and trade between the EU and the United Kingdom has been limited by Theresa May's plans, potential future scenarios and implications remain multifaceted.

The willingness to compromise between the two parties will determine the nature of the future trade policy and thus the ultimate extent of the Brexit. Will there be a comprehensive free trade agreement or a return to WTO rules?

At the same time, the future organization of the EU is becoming increasingly important. What conclusions will the EU Member States draw from the Brexit? Will weak spots be eliminated? Will further integration take place?

Or will the Member States distance themselves from the European federation model?

In order to overcome this uncertainty and identify opportunities and risks at an early stage, a clear understanding of possible negotiation results is required, as well as comprehensive monitoring of further developments.

Close attention to the exit negotiations allows the identification of the scenario with the highest probability of occurrence, along with a corresponding adjustment of commercial and business strategies.

# Brexit Strategic Response Team

## Our Brexit Briefings and Services

### Brexit Briefings Series

1 – June 2016



Deloitte and the Federation of German Industries (BDI) examines how German companies estimate a possible Brexit and which consequences they expect.

[Link to the Study](#)

2 – February 2017



Our scenario analysis provides an overview of scenarios on potential trade models with the United Kingdom and organizational models of the European Union

[Link to the Study](#)

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