Hogan Lovells

The view from outside the UK:

How would international business navigate a post-referendum world?

Amidst all the sound and fury about what Brexit might mean for the UK, many questions still remain largely unexplored.

This report considers where the challenges and opportunities of the new and potentially very different post-referendum landscape would lie. How would international business navigate the uncharted world that Brexit represents and make the most of the dramatic new trading environment?

This paper is based on a recent panel discussion hosted by Hogan Lovells, the International Chamber of Commerce UK (ICC) and the Council of British Chambers of Commerce in Europe (COBCOE). The event convened senior international business leaders from a range of sectors to garner their insights about what Brexit might mean, and what their priorities would be post-referendum, whatever the result.

Project guesswork: the post-Brexit world

It's 24 June, the morning after, and the 'Out' vote has won. Financial markets are gripped by uncertainty...

No one knows what comes next, or how much economic, business and political disruption a post-Brexit world would entail. Even the most sanguine Brexiteer would surely concede that some degree of disturbance is inevitable. The hope is that this volatility would be short-lived. Beyond the immediate upheaval, the broader medium to long-term implications of Brexit would dominate boardroom discussions at international companies in the UK and overseas. The question would no longer be 'In or Out' but 'how can we secure and grow our position in a newly re-drawn marketplace?' What do we want that marketplace to look like?

Responding positively to this new set of circumstances would require a profound shift of mindset for many: all of the surveys to date suggest that international business is very largely in the 'In' camp. The ICC and Hogan Lovells recently conducted a survey of 220 respondents in 21 countries, representing large companies, mid-sized and small firms. The results showed that 86% of respondents wanted the UK to stay in the EU.

Securing full and fair market access

Right at the top of the corporate wish-list is continued market access on reasonable terms, if the UK should find itself no longer part of the EU and existing Free Trade Agreements (FTAs). Having enjoyed access to a Single Market of 500 million customers via the gateway of the UK, businesses would be looking for ongoing access to and from that market, as well as the creation of viable alternative trading agreements with the rest of the world.

Keeping close ties with the markets of the EU is essential, as they would remain key from a UK viewpoint – not least because emerging economies, previously seen as offering superior growth prospects, are facing multiple challenges: Brazil, Russia and China being prime examples.

> Business would be looking to keep the EU and UK preferential trade relations with third countries which go well beyond the World Trade Organisation (WTO) commitments governed by the "most favoured nation" (MFN) principle.
>
> *Lourdes Catrain, Partner, Hogan Lovells*

Trade negotiations: the short goodbye

Securing as advantageous a deal as possible, as quickly as possible, is critical. Article 50 of the Lisbon Treaty stipulates that exit negotiations must be completed within two years, unless all 27 other Member States agree to an extension. Yet there is widespread concern that the complexity of the negotiations means that putting new arrangements in place with the EU could take anything up to eight years; some 50 trade agreements with third countries currently up and running would need to be recast. There is even speculation that a new Ministry would need to be created in the UK to cope with the burden of renegotiating scores of different treaties.

A timeframe of that length would pose serious challenges for business, prolonging uncertainty as to the final terms, and running the risk of Foreign Direct Investment (FDI) being deferred or redirected to other countries within the EU.

'It is in most of Europe's interests to secure a deal more quickly with the UK in order to ensure stability for the region as a whole,' pointed out one senior partner at a city consultancy firm.

Any renegotiation would need to be carried out in as orderly – and amicable – a manner as possible. The UK Government would need to do its utmost to retain the goodwill of other EU governments, some of which might be tempted to push through punitive measures in order to deter other countries from following the UK's lead. Above all, companies would need a clear sense of direction from the Government on timelines and impacts. Equally, they would require early clarification as to the situation regarding other trading partners, particularly the US and China, both of which are major sources of inward investment to the UK.

Business and Government, side by side at the table

Business needs to be fully engaged in the negotiation process, international business leaders insist. Companies have a role and responsibility to support the Government in ensuring that a fair and viable result is achieved post-Brexit; reducing the risk, for example, of punitive tariffs being imposed in sectors, such as the automotive industry and securing continuity of key access rights for sectors, such as 'passporting' for financial services.

That process needs to start immediately, rather than waiting until a Brexit has already taken place. The need for business and its advisors to support Government in this process in order to secure the optimum outcome will be particularly acute, given the intense pressure the re-negotiation of all the replacement arrangements will place on limited resources.

'Business has a legitimate voice and should be speaking up,' agreed Paul Kahn, UK President at Airbus. 'Businesses don't generally like to enter into politics but politics has brought us into this situation. People trust the views of business, believing we'll do what we say.'

> We need businesses to step up to the plate and make their voice heard in terms of their concerns and priorities.
>
> *Thomas Spiller, President of the British Chamber of Commerce in Belgium*

Government needs to re-engage constructively with the EU

In the same way, the UK Government must reinvigorate its relationship with the EU in order to support the needs of international companies and encourage a pro-business environment in Europe in the aftermath of the referendum, irrespective of the result. That would include taking the opportunity to cull unwanted or suffocating bureaucracy, where it acts as a drag on business efficiency.

'We need to be better at doing Brussels,' is how one European lawyer put it. Some believe that the UK has taken a step back in recent months, for example, in the trade debate on China's Market Economy Status, and this situation needs to be reversed – and fast. 'UK fatigue' has already started to set in in Brussels and some other European capitals, a situation which does nothing to promote the cause of international business.

After all, the UK has weighty political and economic clout. 'The EU has one of the most competitive regulatory environments in the world and the UK helped shape it, evident in innovations such as the Single European Sky for air travel,' said Alan Houmann, the Head of Government Affairs for Europe, Middle East & Africa at Citi. Others pointed to the UK's diplomatic influence and expertise – in helping drive through EU sanctions against Russia, for example – as yet further confirmation that the UK must have a seat at the top table, whatever the outcome of the referendum.

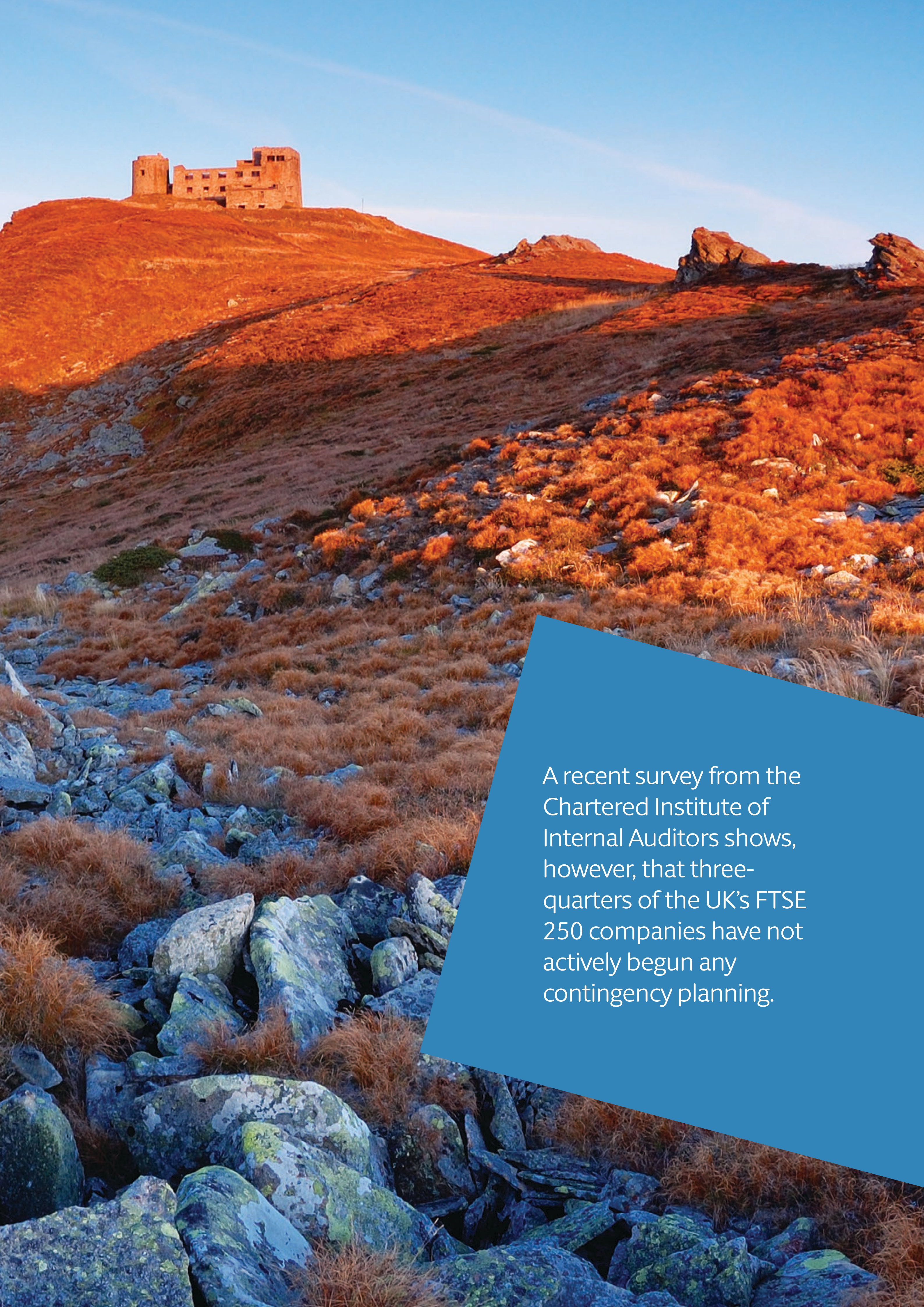
Opinion was expressed that a loss of the UK's influence on decision-making in the EU could result in a shift in its political centre of gravity, reducing focus on becoming more competitive and reducing the regulatory burden. This shift could be disadvantageous to businesses across the EU, as well as to businesses in the UK still bound to comply with EU rules in trading with its markets.

The alternative trading models on offer

What would be the impact on international business of the alternative trading models most frequently mooted for a post-Brexit UK?

The FTAs with the EU negotiated by Norway, Switzerland and Canada all offer alternative models of association, as does operating within the WTO framework. Each option brings both advantages and disadvantages. To take Norway's EEA-based arrangement as an example, the UK would continue to be able to be part of the EU's Single Market on that basis without being part of its administrative machinery, whilst also having the opportunity to open up FTAs bilaterally with partners outside the EU. Yet, under that model it would not be part of the EU's customs union creating additional tariffs and non-tariff costs on UK manufacturing businesses, less of an issue for Norway's core business sectors of energy and seafood. Plus access to the Single Market from outside comes at a price. Norway accepts free movement of people and is party to the Schengen agreement. Also, the UK seems likely to end up paying almost the same amount to the EU budget as it does now – Norway pays proportionately 90% of the UK's net contribution. All this while being excluded from the EU decision-making process.

Business leaders point out that 80% of the UK's GDP derives from services, so any new agreements would have to work for the UK's services industry, the City being a key example, as much as for the traded goods sector. If new alternative trading deals could be agreed and delivered quickly, that would clearly be very beneficial.



A recent survey from the Chartered Institute of Internal Auditors shows, however, that three-quarters of the UK's FTSE 250 companies have not actively begun any contingency planning.

Preparing for all eventualities

Effective contingency planning must be at the heart of any company's approach to life after the referendum.

The current unpredictability of a post-Brexit world means that businesses should be considering the implications of a wide range of scenarios, not least as part of their governance responsibilities towards shareholders and investors. The post-EU environment could bring with it anything from currency fluctuations and the risk of a drop in inward investment to a change of rules on immigration and therefore possibly a review of the composition of a firm's workforce. To take a specific example, financial services firms who rely on the EU's passporting arrangements may need to take steps to adapt their business which could involve significant decisions, such as whether (and when) to apply for a banking licence elsewhere in the EU and on the impact of associated cost/capital requirements. Other organisations might be forced to consider opening up an overseas base within the EU in parallel to London, to retain a foothold in the Single Market. All of these factors and far more besides would need to be addressed as part of the process of redefining risk management strategies.

Moreover, contingency planning embraces not only the immediate impact of a Brexit vote, but also any possible longer-term economic and political developments. Some international businesses question, for example, whether the EU would respond to a Brexit by deepening integration. Others argue that fragmentation or even disintegration of the Single Market might occur, with the EU's equilibrium suddenly tilted away from the more pro-business, pro-open-markets of the Northern European countries.

There's no going back now

'If the UK votes to stay in the EU, maintaining the status quo would be unacceptable', argues an international business. Instead, it would be the perfect opportunity to push for urgent reform of the EU, attacking the bureaucracy and red tape that hinders business operations and streamlining the often cumbersome decision-making processes.

> There are 24 official languages in the EU, but they are all speaking the language of reform. Business should and must support the UK push to make the EU a better place to do business.
>
> *Senior business leader*

'We would like to see the lack of reality that sometimes exists within the EU, the gulf between intention and delivery, addressed,' concurred Simon Fraser, the Managing Partner of Flint Global. 'A vote to remain would be a platform to be proactive and tell the Government and the EU what we need.'

The UK is widely-recognised as one of the most pro-business countries in Europe, fertile breeding ground for Fintech technology innovations, the development of start-ups and all forms of entrepreneurial activity. Its continued leadership in those areas would be widely welcomed. Government and business should work closely in tandem after an EU vote to stay in the EU to promote increased benefits for very small enterprises, the Digital Single Market and the progress on the Capital Markets Union.

Finding the positives, whatever the outcome

Business hates uncertainty just as nature abhors a vacuum. No one can accurately forecast the implications if it is Brexit at the ballot box: the situation is without precedent. The vote itself is a binary choice, but the spectrum of future outcomes is extremely wide. The more that international companies are prepared, informed and engaged, the more they can look ahead with clarity and confidence. Both Government and business would need to approach that world with pragmatism, imagination and flexibility if they are to adapt well to the circumstances which unfold in the months and years after this momentous vote.

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