GUEST BLOGS, **JEAN MONNET**, **RESEARCH**

How a Brexit Would Influence the British Economy, Part 2: The Insurance and Manufacturing Sector

A Four-Part Brexit Blog, hosted by CCCU Politics/IR Jean Monnet Chair in European Foreign Affairs, Dr Amelia Hadfield.

Featuring: guest Jean Monnet Scholar Mechthild Herzog.

Part 2: Who's Afraid of Leaving? The Insurance and Manufacturing Sector

In Part 1 of our 4-part series, "If Britain Leaves the EU, We Leave Britain (https://canterburypolitics.wordpress.com/2015/07/02/lets-talk-business-analysing-the-economic-impact-of-a-brexit/)", we explored the potential impact on the finance sector of the British referendum, forecasted for late 2016. In this second instalment, we dig a little deeper, enquiring into changes that could feasibly affect the insurance and manufacturing sectors.

(https://canterburypoli /2015/05/mechthild-herzog.jpg)
Guest blogger Mechthild Herzog

The UK Insurance Sector: the ultimate uninsurable

Based on our overview of key players, the insurance industry perceives itself to be considerably threatened by a potential Brexit, largely because current predictions indicate that it is likely to suffer not only short-term disruptions, but also permanent, and fragmenting ones. Unsurprisingly, the majority of representatives from the insurance sector strongly advocate the UK remaining an EU member. Gerry Grimstone, chairman of the Edinburgh-headquartered insurer Standard Life, sets the tone in this respect, describing a Brexit as "disastrous for London and the UK".[1]

Looking more closely at the details, British insurance companies may not be as exposed to high risks of negative impact as the financial sector, or the chemical and automotive industries. However, as argued by Open Europe, a Brexit could weaken prospects either to maintain, or to re-build, the currently strong position of British insurance companies, as they would be unable to sell their policies in Europe for the same pre-Brexit prices and conditions. The change entailed in post-Brexit conditions would also deter overseas players from opening offices in the UK. Insurers, themselves in the business of rendering risk preventative find themselves ironically in a particularly **precarious position** in which the risk to the overall sector remains at present fundamentally unmanageable. As a recent Reuters article suggested, the impact could affect not only current business strategies, but the loss of years of work on a common regulatory framework, including agreements on the amount of capital EU insurers require to establish and operate their businesses.[2]

At present, leaving the EU would leave British insurers with two choices: opening costly subsidiaries on the continent and reporting to local regulators, or ending their business with key EU countries completely. Like the financial sector, EU membership allows both British and third-country companies to have a corporate based in only one EU member state, but to operate in all twenty-eight. "The loss of those **passporting rights** could be a significant issue", suggested Catherine Thomas, an analyst at the insurance ratings agency, A.M. Best. Even if Britain were to remain a member of the European Economic Area (EEA), which would in principle allow British insurers to retain their 'passporting' rights, they would still lose their power to bargain on key sectoral issues, including regulations and failsafes, despite being required to comply with them.

Lloyd's of London and the International Underwriting Association, representing insurers and reinsurers operating in London, have issued clear warnings about the UK leaving the EU. In particular, they see a threat to the UK from countries like China and India, with expanding economies[3], relative to the potentially compromised economic strength and political influence of the UK.[4] From these stark warnings, one can determine a critical mass of large UK insurance companies, all of whom emphasise their pro-EU position. Sector nerves are especially strong among the 96 syndicates of the 300-year-old Lloyd's of London insurance market as a result.

Equally, however, the outlook of Standard & Poor injected a degree of calm, or at least pragmatism. A recent S&P report suggested a Brexit would be "costly but not game-changing"[5] for British insurers, as the sector was far more reliant on trade with non-EU countries like the US, than with EU member states. The *Financial Times* went even further, suggesting in February this year that due to the very domestic character of Europe's insurance market, the UK's insurance industry would experience "little direct or immediate impact"[6]. From this perspective, it is simply too early, or too ambiguous for some insurers to embark on concrete contingency plans, such as moving their headquarters from the UK. Huw Evans, Chief Executive of the Association of British Insurers, however fears the pain of an indirect impact, one that may arise as a Brexit consequence, namely Scotland leaving the UK. Such an outcome is, according to him, "the real political uncertainty for our sector", and one that poses a real risk of fragmenting permanently the domestic market. [7]

The UK Manufacturing Sector: heavy weather, or heavy lifting?

The sector which so far has the strongest pro-Brexit voice is that of manufacturing, led publicly in this respect by JCB, the world's third-biggest construction equipment firm. JCB Chairman and owner, Lord Anthony Bamford (also a major party donor to the Conservative Party) stated in May of this year: "We are the fifth or sixth largest economy in the world. We could exist on our own – peacefully and sensibly."[8] Encompassing both national, and sector-specific perspectives, Bamford argues that Britain should not fear leaving the EU, principally because a Brexit would have no serious negative impact on British trade with the rest of Europe. Indeed, the move could cut down on the red tape currently strangling British business. His political affiliation apart *The Independent* suggests two possible motivations behind Bamford's logic:[9] first, JCB makes the majority of its capital from within the UK itself, which would not be substantively reduced by a switch away from the EU single market. Second, JCB could itself benefit from possible regulatory changes that may come from severing ties with Brussels, particularly when negotiating deals with non-EU countries, such as the United States.

Lord Bamford is supported in his views by JCB chief executive, Graeme MacDonald, who suggested that the impact of a Brexit on business has been overhyped. Arguing the benefits of quitting an unreformed EU, MacDonald was clear enough in his argument: "I really don't think it would make a blind bit of difference to trade with Europe. There has been far too much scaremongering about things like jobs. I don't think it's in anyone's interest to stop trade. I don't think we or Brussels will put up trade barriers".[10] While the UK is clearly an important export market (e.g. the fourth-biggest market for German cars), MacDonald's attitude is not categorical, but rather qualified by his support a further membership of the UK in a reformed EU: "What is needed is a lot less red tape and bureaucracy. Some of it is costly for us and quite frankly ridiculous. Whether that means renegotiating or exiting, I don't think it can carry on as it is. It's a burden on our business and it's easier selling to North America than to Europe sometimes." [11]

However JCB is still something of a voice in the wilderness within the wider manufacturing sector. In September 2014, 85% of EEF members, the UK's manufacturing trade association (formerly the Engineering Employers' Federation), voted emphatically for continued EU membership, while only 7% signalled their support for a Brexit.[12] In a recent study[13], the UK's Aerospace, Defence, Security and Space Sectors came to a similar conclusion, with 86% of their members arguing that it would be better for their business if the UK remained an EU member, with only 2% perceiving leaving as a better option. For fully two thirds of the EEF, the most crucial benefits retained by EU membership are free trade, followed by the simplification of regulations, and overall economic growth. In the case of a Brexit, the British manufacturing sector would likely be hit hard by highly skilled workers from the EU staying away, and overseas investors regarding seeing the UK as a less-attractive business destination.

Aerospace, as another manufacturing giant, has also stated its clear opposition to the UK leaving the EU.[14] Paul Kahn, President of Airbus UK, which employs 16,000 people, argued in May that the best way for Britain to compete internationally would be to stay within the EU. A Brexit would not only put investments at risk, but also thousands of jobs. Killing off the aerospace sector may not happen overnight, as time would be needed to transfer manufacturing skills; however, once gone, it could not easily or swiftly be wooed back. Kahn has spoken clearly in favour of remaining within the EU: "I don't believe that there is anyone who has run a global business who can truly, and clearly, argue that there will be greater value and economic benefit outside of the EU, as opposed to in it."[15]

Airbus is not the only firm in the plane-building business that would consider leaving the UK: Bombardier, a manufacturer of both planes and trains, could shift from Northern Ireland.[16] Impacts to Northern Ireland have not been much focused upon, but they should be included in our Brexit coverage. It terms of manufacturing, the American industrial giant General Electric (GE), which produces a raft of items, including aircraft engines, made its pro-EU standing clear, with its head of the UK and Ireland Mark Elborne declaring in June: "I think that an exit from the EU would be hugely damaging and would cause a lot of difficulties in the short term." Despite criticising the plethora of EU red tape, and emphasising the need for reforms, Elborne made clear that: "we want to be part of a trading group where we can continue to benefit from the lack of barriers, we want to benefit from large-scale trade agreements, the convergence of standards, and we want to be able to operate seamlessly between our different businesses across Europe."[17]

Turning to the automotive sector, companies here too have largely positioned themselves in favour of the EU, although as yet they have not joined any organised pro-European campaign. Here, the strongest anti-Brexit voice comes from Germany, chiefly because of the heavy reliance of the German car industry upon Britain. Not only do Volkswagen (with a headquarter in Blakelands, Milton Keynes) and BMW (with plants in various UK locations including Hams Hall and Oxford) have production facilities based in the UK, Brits continue to buy every fifth car produced in Germany. A Brexit could cause a 2% fall in German car sales to the UK over the next twelve years, predicted a study by the Bertelsmann Foundation in April.[18] This may not seem enormous numerically, but it is well within the margins of risk and loss that have promoted increasingly pessimistic outlooks amongst German carmakers.

In July of this year, German Industry UK (GIUK), the organisation representing a majority ality of German industry in Britain, published the results of a survey on a potential Brexit.[19] A range of companies including Bentley Motors, Zeiss, E-ON, Bosch, Siemens and also Haribo together sent a strong 'please stay' appeal to 10 Downing Street. While they too support the demand for less bureaucratic hurdles and regulations, this key group clearly fear the results of a Brexit that would force a host of bilateral agreements to negotiate subsequent deals, viewed as a both time-consuming and expensive process. Reluctance in planning future business is already perceivable: with 2013 forecasts for job creation and tax revenues remaining unfulfilled, and subsequently being adjusteddownward

All such uncertainties flowing from the manufacturing sector inevitably have impacts upon the British economy itself. George Gillespie, chief executive of the vehicle-testing company MIRA, complained in April that it would currently be hard for him to answer foreign investors' questions regarding mid-term developments.[20] Gillespie is currently two years into a ten-year plan to create a large R&D cluster within MIRA. Naturally, his business partners want to know the state of the market into which they are investing; yet he cannot give them a satisfactory answer. Uncertainty about the investment so crucial to underwriting a healthy manufacturing sector is spreading. As Daniel Boese, head of the education department of the German factory automation firm Festo argues: "If you want to get the support of the European Union I would not invest into the UK before the referendum" – a stark ambiguity that will cost UK business investment capital, and trust.[21]

According to Open Europe, Brexit-driven uncertainty thus remains the biggest risk for the manufacturing sector. Yet it can also be argued that Brexit uncertainty may be more proximate and not necessarily absolute; it may drive away anticipated deals in the short-term, but should the UK strike a deal permitting it to retain some more of access to the EU market similar to the current trade conditions, the overall outcome may not be too fundamentally disturbing, despite initially high levels of disruption affecting the sector.

At the halfway point of our four-part blog, we continue to debate, to Brexit or not to Brexit? Our survey of British manufacturing suggests that actors small and large are voicing their concerns. The critical mass of major sectors, and the big players within those sectors, are increasingly and publicly speaking out against leaving the EU, while a raft of single or smaller players, have waded into the on-going debate – from restaurant chains to airport operators, from communication firms to waste management companies. Join us for our third part of the series "**Let's Talk Business: How a Brexit Would Influence the British Economy**", where we'll look at key players in the **British energy sector**, with a survey of other players across **related industries**.

[1] http://www.euractiv.com/sections/uk-europe/brexit-could-hit-london-insurance-market-314970 (http://www.euractiv.com/sections/uk-europe/brexit-could-hit-london-insurance-market-314970).

[2] Cf. http://www.reuters.com/article/2015/06/04/britain-eu-insurance-idUSL5N0YP3TC20150604 (http://www.reuters.com/article/2015/06/04/britain-eu-insurance-idUSL5N0YP3TC20150604).

[3] Following the lead of the Wall Street Journal, we'll assume the recent Chinese blip is just that, at least for now: http://www.wsj.com/articles/global-markets-rally-after-two-day-tumble-following-yuan-plunge-1439452638/ (http://www.wsj.com/articles/global-markets-rally-after-two-day-tumble-following-yuan-plunge-1439452638/).

[4] Cf. http://news.sky.com/story/1491379/eu-vote-lloyds-of-london-boss-warns-over-exit (http://news.sky.com/story/1491379/eu-vote-lloyds-of-london-

boss-warns-over-exit) and http://www.euractiv.com/sections/uk-europe/brexit-could-hit-london-insurance-market-314970 (http://www.euractiv.com/sections/uk-europe/brexit-could-hit-london-insurance-market-314970).

[5] Cf. http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/11693103/Brexit-could-push-global-banks-away-from-UK-warns-SandP.html (http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/11693103/Brexit-could-push-global-banks-away-from-UK-warns-SandP.html).

[6] Cf. http://www.ft.com/intl/cms/s/0/1fa0f3dc-a70a-11e4-b6bd-00144feab7de.html#axzz3efJ8Njpm (http://www.ft.com/intl/cms/s/0/1fa0f3dc-a70a-11e4-b6bd-00144feab7de.html#axzz3efJ8Njpm).

[7] http://uk.reuters.com/article/2015/06/02/britain-eu-insurance-idUKL5N0YO3MS20150602?feedType=RSS&feedName=rbssFinancialServicesAndRealEstateNews (http://uk.reuters.com/article/2015/06/02/britain-eu-insurance-idUKL5N0YO3MS20150602?feedType=RSS&feedName=rbssFinancialServicesAndRealEstateNews).

[8] http://www.bbc.co.uk/news/business-32775396 (http://www.bbc.co.uk/news/business-32775396).

[9] Cf. http://www.independent.co.uk/news/business/news/three-reasons-why-the-jcb-chairman-may-think-brexit-is-nothing-to-fear-10258300.html?origin=internalSearch (http://www.independent.co.uk/news/business/news/three-reasons-why-the-jcb-chairman-may-think-brexit-is-nothing-to-fear-10258300.html?origin=internalSearch).

[10] http://www.theguardian.com/politics/2015/may/17/jcb-boss-says-eu-exit-could-lift-burden-of-bureaucracy-on-uk-businesses (http://www.theguardian.com/politics/2015/may/17/jcb-boss-says-eu-exit-could-lift-burden-of-bureaucracy-on-uk-businesses). Cf. also http://www.telegraph.co.uk/news/newstopics/eureferendum/11611936/EU-exit-may-be-in-UKs-best-interest-says-top-manufacturing-firm.html (http://www.telegraph.co.uk/news/newstopics/eureferendum/11611936/EU-exit-may-be-in-UKs-best-interest-says-top-manufacturing-firm.html).

[11] htttp://www.theguardian.com/politics/2015/may/17/jcb-boss-says-eu-exit-could-lift-burden-of-bureaucracy-on-uk-businesses (//www.theguardian.com/politics/2015/may/17/jcb-boss-says-eu-exit-could-lift-burden-of-bureaucracy-on-uk-businesses).

[12] Cf. http://www.cnbc.com/id/102039709 (http://www.cnbc.com/id/102039709).

[13]Cf. https://www.adsgroup.org.uk/articles/47832 (https://www.adsgroup.org.uk/articles/47832). The ADS Group employs more than 310.000 people.

[14] Cf. http://www.euractiv.com/sections/uk-europe/airbus-says-british-exit-eu-would-pose-huge-risks-314748 (http://www.euractiv.com/sections/uk-europe/airbus-says-british-exit-eu-would-pose-huge-risks-314748); and also http://www.link2portal.com/brexit-would-damage-business (http://www.link2portal.com/brexit-would-damage-business).

[15] Cf. http://www.reuters.com/article/2015/05/20/britain-europe-airbus-idUSL5N0YB2HO20150520 (http://www.reuters.com/article/2015/05/20/britain-europe-airbus-idUSL5N0YB2HO20150520).

[16] Cf. http://www.belfasttelegraph.co.uk/news/northern-ireland/bombardier-will-leave-northern-ireland-if-uk-exits-europe-claims-naomi-long-31139893.html (http://www.belfasttelegraph.co.uk/news/northern-ireland/bombardier-will-leave-northern-ireland-if-uk-exits-europe-claims-naomi-long-31139893.html).

[17] Cf. http://www.telegraph.co.uk/finance/newsbysector/industry/11701786/American-behemoth-General-Electric-warns-of-hugely-damaging-Brexit.html (http://www.telegraph.co.uk/finance/newsbysector/industry/11701786/American-behemoth-General-Electric-warns-of-hugely-damaging-Brexit.html).

[18] Cf. http://www.ft.com/intl/cms/s/0/f6cda050-20bb-11e5-aa5a-398b2169cf79.html?ftcamp=crm/email/201573/nbe/EuropeMorningHeadlines/product#axzz3eo5D828Z (http://www.ft.com/intl/cms/s/0/f6cda050-20bb-11e5-aa5a-398b2169cf79.html?ftcamp=crm/email/201573/nbe/EuropeMorningHeadlines/product#axzz3eo5D828Z).

[19] Cf. http://www.independent.co.uk/news/uk/politics/eu-referendum-german-companies-issue-a-please-stay-appeal-ahead-of-membership-vote-10375103.html (http://www.independent.co.uk/news/uk/politics/eu-referendum-german-companies-issue-a-please-stay-appeal-ahead-of-membership-vote-10375103.html).

[20] Cf. http://www.britishinfluence.org/our_place_in_europe_the_politicians_might_be_silent_but_business_has_found_its_voice (http://www.britishinfluence.org/our_place_in_europe_the_politicians_might_be_silent_but_business_has_found_its_voice).

[21] Cf. http://www.wired.co.uk/news/archive/2015-05/20/festo-uk-eu-referendum-investment (http://www.wired.co.uk/news/archive/2015-05/20/festo-uk-eu-referendum-investment).

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