How Britain Leaving the EU Could Affect the Single Currency

In 2016, the majority of UK voters opted to leave the EU. A lot of people, fuelled by the opinion of the mainstream media, seemed to be disappointed with the referendum vote due to this common sentiment: Brexit will bring nothing but tough times.

However, when you look at the numbers, it is clear that the UK is already at an unfair advantage, as Britain is one of the biggest contributors towards the EU budget. In an article by Full Fact it was recorded that the UK pays more into the EU budget than it gets back. The site says that in 2016, the UK government shelled out £13.1 billion to the EU budget, which was more than the forecasted £4.5 billion that the EU spent on the country. In short, the UK's net contribution was around £8.6 billion, which was used to help develop other countries.

Uncertainty with the Euro

Without aid from the UK, and if a hard Brexit happens, the EU will have to find another country that will generously provide £8.6 billion in order to offset the budget losses. If the EU fails to compensate for the losses, the Euro will most likely become extremely volatile since the European Central Bank (ECB) would need to print more money to provide funding to member states.

Below is a chart that shows the balance of UK contributions, and public sector receipts from the EU budget, which was inflation-adjusted for 2016.

The Economist suggests that only a few British people have changed their mind about whether to stay or go. The polls discovered that should there be another vote, the result would be similar to the 52:48 split last June. The article also mentions that most leavers want a hard Brexit if possible.

A hard Brexit would most likely affect the Euro negatively due to investor sentiment regarding the risks. FXCM notes that global market participants frequently flock to riskier assets, in this case the GBP, in hopes that doing so will generate strong returns. There may be uncertainty within the UK market because of Brexit, but that doesn’t mean that the EU will benefit from it. After all, there is no direct evidence of an inverse correlation of the GBP/EUR, at least not until a final Brexit vote happens. If there’s anyone who would benefit from Brexit, it is the U.S., especially since the greenback has always been viewed as a safe haven against the Euro.

The European Commission is now looking to reduce regional spending by up to 30% in order to balance the budget and keep the Euro’s strength. If the European Commission doesn’t cut regional spending, its other option is to reactivate the EU’s aggressive bond buying program. Whether or not that may happen soon is moot, especially since the ECB’s stimulus weakened the Euro significantly. The EU had already under spent on regional funds before. That being said, it wouldn’t be surprising if this is the route that they will take once again.