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# David Cameron's Dangerous Game

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## The Folly of Flirting With an EU Exit

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*Matthias Matthijs*

**D**espite his innate caution and usually sound political instincts, British Prime Minister David Cameron is gambling with his country's future. In January, in a long-anticipated speech, he called for a wide-ranging renegotiation of the terms of the United Kingdom's membership in the European Union and promised to put the result up for a straight in-or-out popular referendum by the end of 2017 (assuming his party wins the next election, due in 2015). A British exit from the EU is now more likely than ever—and it would be disastrous not only for the United Kingdom but also for the rest of Europe and the United States.

If London does ultimately cut the rope, it will not be the result of rational political or economic calculations. British Euroskepticism boils down to a visceral dislike of Brussels—the host of a number of European institutions and the EU's de facto capital—on the part of an ill-informed conservative minority that clings to an antiquated notion of national sovereignty. These sentiments are on display every day in the right-wing tabloids, which play on voters' fears

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with vitriolic commentary and sensationalistic headlines, such as “EU Wants to Merge UK With France” and “EU Will Grab Britain's Gas,” both of which recently appeared in the *Daily Express*.

By caving in to the demands of the right wing of his party, Cameron appears to be falling into the same trap that his predecessors fell into. Both Margaret Thatcher and John Major, the previous two Conservative prime ministers, were eventually thrown out of office as their party tore itself apart over the issue of European integration during the late 1980s and mid-1990s. In 1995, these divisions among the Conservatives led a young Labour opposition leader named Tony Blair to ridicule Major on the floor of the House of Commons, scoffing, “I lead my party; he follows his.” Even Cameron himself, back in 2006, less than a year after he took over the Conservative Party, wisely counseled his colleagues to “stop banging on about Europe” if they ever wanted to win elections again.

And yet, seven years later, Cameron faces a simmering rebellion on an issue that most Britons still do not care much about but that has once again turned toxic in his party. In a 2012 survey of the British electorate, only six percent of respondents described Europe as the most salient issue facing the country, compared with 67 percent who prioritized the economy, 35 percent who worried most about unemployment, and just over 20 percent whose main concerns were immigration and race relations.

With his January speech, Cameron had hoped to achieve four short-term objectives. First, he wanted to stop the growing threat on his party's right flank from the anti-EU and anti-immigration UK Independence Party, whose populist



leader, Nigel Farage, positions himself as a champion of British common sense and defender of British sovereignty against Brussels' encroachment. Second, Cameron aimed to neutralize his own party's increasingly restless Euroskeptical backbenchers, many of whom also advocate a British exit from the EU. Third, he hoped to put the losing political issue of Europe to rest until the next parliament. Fourth, he tried to portray the country's economic woes as a result of the eurozone crisis rather than of his own government's biting austerity measures.

On all four fronts, however, it appears that Cameron miscalculated. The UK Independence Party wildly outperformed expectations in the local

elections in May, earning close to a quarter of the overall vote. The Euroskeptics in the Conservative Party are still insisting on a referendum during the current parliament, underscoring once again that they cannot be appeased on the European question and do not trust the prime minister to deliver on it. Cameron's leadership is more tenuous than ever, especially after he pushed through a contentious bill in support of gay marriage, a stance that many party activists find hard to swallow. (The fact that one of Cameron's close advisers referred to these activists as "mad, swivel-eyed loons" has not helped.) And finally, a slew of recent scholarly studies, including one published by the International Monetary Fund, have blown a giant hole

in the intellectual case for austerity, undercutting the government's economic strategy. But far more is at stake than one prime minister's political career. If the United Kingdom ends up abandoning Europe, it will feel the negative economic and political effects for decades to come.

### **A MARRIAGE OF CONVENIENCE**

The United Kingdom's relationship with Europe has never been warm, much less passionate; it is more like a loveless arranged marriage. Based on cost-benefit analysis rather than lofty rhetoric about a common European destiny, the country's European affair has been fraught with abysmal timing and shattered hopes. When the country first knocked on Brussels' door in the 1960s, it found its applications unceremoniously rejected by France's Charles de Gaulle. In 1973, when Edward Heath, a Conservative prime minister, successfully steered the United Kingdom toward membership in the European Economic Community, the Western world was about to slip into its first deep postwar recession. The subsequent Labour government, facing opposition to European integration from its left-wing backbenchers, felt the need to put Heath's decision to a national referendum, which eventually passed in 1975 by a two-to-one margin.

During the 1980s, Thatcher told her European partners that the United Kingdom wanted "a very large amount of [its] own money back" and warned them that she had not successfully rolled back the frontiers of government at home only to see them reintroduced through the backdoor by Brussels. At the beginning of the next decade, against her better judgment, she let her country

join Europe's Exchange Rate Mechanism, a precursor to the monetary union. Major, then chancellor of the exchequer, had convinced her that this was the best way to tame inflation, which had been creeping up again at the end of the 1980s. But joining the ERM meant dancing to the tune of Germany's monetary policy, and soaring German interest rates to fight inflation and finance German reunification meant that the Bank of England had to follow the Bundesbank's lead in hiking up interest rates. Doing so at the onset of another domestic recession meant political suicide, however, and the United Kingdom was forced to leave the ERM only a few years after it joined.

After succeeding Thatcher as prime minister, Major negotiated various areas in which the United Kingdom could opt out of the Maastricht Treaty, which created the EU, most notably keeping the United Kingdom out of the common currency while allowing it to retain full EU membership. Blair, who as prime minister passionately told the French National Assembly in a 1998 speech that he shared the European ideal, at one point sought to bring his country onto the euro, but he was blocked by his powerful chancellor of the exchequer, Gordon Brown.

In some ways, the United Kingdom's quandary today looks like it did 40 years ago, when the country first joined the European Economic Community. Then, as now, the British were in deep, mostly self-inflicted economic trouble. In the 1970s, however, the politics of the issue were flipped: the Conservatives saw integration with Europe as a liberalizing move, and the Heath government believed it was the only way to reverse the country's relative economic decline.

Thatcher, for her part, campaigned strongly in favor of staying in the European Economic Community during the referendum of 1975, arguing that access to the large and growing continental market would fuel British growth. At the same time, a majority of Labour Party members, although not the leadership, resolutely opposed membership on the grounds that Brussels was too market-friendly.

Today, the British economy is again struggling to emerge from a slump, but this time, Europe is seen as the source of the malaise, not its cure. In an attempt to play down the negative effects of their austerity policies, both Cameron and his chancellor of the exchequer, George Osborne, have been blaming the European sovereign debt crisis for the British economy's lack of growth. They usually justify their draconian spending cuts by pointing to Greece's fiscal tragedy. And whereas Labour is now moderately in favor of staying in the EU, seeing the union as the guarantor of certain social rights in the United Kingdom, the majority of Conservatives have turned against Europe and want to see the repatriation of key powers back to the national government. According to the most recent opinion polls, more Britons are in favor of leaving the EU than are in favor of staying in it.

Cameron's stance on Europe constitutes a break with Conservative tradition. Although Thatcher was never enamored with Brussels, she was a driving force behind the effort to establish a European common market in the 1980s, which culminated in the signing of the Single European Act in 1986. She was always careful to nurture relationships with

like-minded leaders on the continent and keen to avoid British isolation. Major had a tougher time navigating the European question, but in the end, he signed the Maastricht Treaty, albeit while opting out of the euro. But when Cameron decided in December 2011, during the height of the euro crisis, to completely stay out of a new fiscal pact, forcing the EU to move forward with an intergovernmental agreement without the United Kingdom, he radically changed that Conservative tradition. His demand for a renegotiation of his country's EU membership terms went one step further, and it has infuriated many European leaders, who fear it will reignite old debates that were settled through compromise a long time ago.

#### **BETTER TOGETHER**

The economic argument for why the United Kingdom should leave the EU goes something like this: The continent is preoccupied with fighting a full-fledged sovereign debt crisis, one that has fundamentally changed the dynamics of European integration. The crisis has made integration a much more inward-looking project, requiring all kinds of new regulations in the financial sector aimed at completing the monetary union with common banking supervision, joint deposit insurance, and closer fiscal cooperation. These new regulations will allegedly hurt the City of London (the United Kingdom's financial hub) and therefore the entire British economy. And since fixing the euro once and for all can be achieved only by granting more powers to European institutions, the role of the British parliament and government as the legitimate representatives of the country's citizens will be

threatened. This would further widen the democratic deficit within the EU, a particularly sensitive issue for the United Kingdom.

But on close inspection, none of these concerns holds up. The idea that the United Kingdom would be better off outside the EU is misguided, since it is based on a finance-centric view of the British economy. This view holds that the United Kingdom's comparative advantage is in financial services, a sector that needs to be protected at all costs from burdensome regulations. According to this school of thought, Thatcher's liberalization and deregulation of the economy in the 1980s and Blair's consolidation of finance as the core sector of the British economy in the late 1990s were unmitigated successes.

Proponents of this view suffer from collective amnesia about what has happened to the British economy over the past five years. Although finance lifted many boats during good times (some much more than others), when the sector crashed in 2008, it led to a collapse in government revenue, as close to one-quarter of all the Treasury's income came from finance. Even as the government's coffers were emptying, London had to dole out large bailouts to the very banks that had caused the crisis. The Cameron government then chose to respond with big expenditure cuts, and the pain seems set to continue for at least another five years. And that is the optimistic scenario.

Surely, the Cameron government's alternative to the EU banking regulations designed to thwart future crashes is not to get rid of financial rules altogether. For better or worse, this is now a post-Lehman Brothers era, and some amount

of regulation is politically inevitable. What is more, London would certainly not be able to maintain its status as the leading financial center in Europe if the British left the Common Market, since doing so would make capital flows from the continent to the United Kingdom more regulated and thus more restricted than they are now.

The moment the United Kingdom leaves the EU is also the moment it loses all influence on European economic policymaking. And London would still have to accept most of Brussels' regulations and standards if it wanted free access to a market of over 400 million well-off European consumers, who currently buy more than 50 percent of all British exports. By leaving, the United Kingdom would also miss out on the free movement of labor, forfeiting the ability to attract many of Europe's best brains and the ability to take advantage of an influx of low-wage workers from central Europe.

The fact that the United Kingdom today remains in the EU but out of the eurozone means that it can have its cake and eat it, too. An independent monetary policy has allowed the country to keep down the value of the pound, boosting British exports to Europe and the rest of the world. And thanks to its membership in the Common Market, the United Kingdom remains influential in setting its rules. It is difficult to imagine a better position.

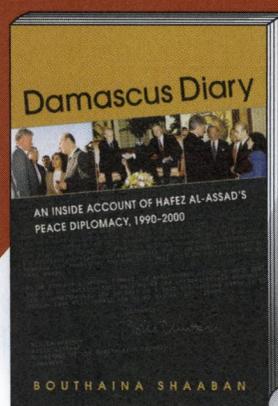
A British exit from the EU would be equally disastrous for the United Kingdom's standing in the world. Speaking at West Point in 1962, former U.S. Secretary of State Dean Acheson observed that the United Kingdom had lost an empire and had yet to find a role. By the 1970s,

that role had started to take shape: the British would help shepherd European integration and maintain a “special relationship” with the United States. The alliance between the United Kingdom and the United States saw its heyday during the 2003 invasion of Iraq, when U.S. Defense Secretary Donald Rumsfeld spoke of Europe as divided into an antagonistic “old Europe”—led by the United Kingdom’s traditional rivals, France and Germany—and a more supportive “new Europe.”

But at that time, Washington still feared a common European defense policy, seeing a unified continent as a potential competitor. A decade later, the Americans no longer hold that view. Because of Germany’s renewed economic strength and quasi-hegemonic status within the eurozone, Washington now sees Berlin, not London, as its preferred partner in Europe. The interests of the United States and Europe are more closely aligned than they used to be, as both try to cope with an economic slump, rising powers, and common security threats. Although the Obama administration has made clear that it sees Asia as the strategic battleground of the future, it is also encouraging European countries to cooperate more closely on defense so that they can help the United States bear the burden of global security. It would be a strategic mistake for London to leave the EU just as Washington is starting to warm to it.

As austerity takes its toll on the British armed forces, the only way for the United Kingdom to play any role in global security is if it pools its resources with the rest of Europe. In a sign of things to come, Europe’s two nuclear powers, the United Kingdom and France, have

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agreed to share their aircraft carriers. A truly common European defense policy, however, has remained elusive. As a French diplomat recently told me, "You cannot do anything without Britain, but you also cannot do anything with Britain."

Still, as the wars in Iraq and Libya demonstrated, EU membership has not stopped the United Kingdom from acting in its own interests. Those campaigns have shown that the EU member states less inclined to intervene militarily, such as Germany, will not prevent others from resorting to force. NATO countries have adopted the flexible strategy of acting in "coalitions of the willing"; there's no reason why a formal EU defense alliance could not do the same thing. And now is the right time for such a move, since London's strategic interests have never been more closely aligned with those of the rest of Europe.

### THE END OF THE AFFAIR

On the eve of the Allied troops' landing in Normandy in June 1944, British Prime Minister Winston Churchill warned de Gaulle that "every time we have to decide between Europe and the open sea, it is always the open sea that we shall choose." Elaborating on his point, Churchill explained that if he ever had to make a choice between de Gaulle and Franklin Roosevelt, between Europe and the United States, he would always pick the latter.

Ironically, Churchill was one of the first European leaders to call for a "United States of Europe," not long after World War II. De Gaulle, however, would never forget Churchill's wartime rebuke, and it certainly was on his mind both times he vetoed the

United Kingdom's application to join the European Economic Community. Today, almost 70 years after Churchill's comment, U.S. President Barack Obama is sending the opposite message to his British counterpart, in equally firm terms: if the United Kingdom wants to retain any influence on the open sea, it must choose Europe.

But Cameron might well have already set his country inexorably on the road to isolation and irrelevance. Even if some European leaders would be willing to make substantive concessions to the United Kingdom to help keep it in the club, they are unlikely to ever go far enough for Cameron to appease the Euroskeptics in his party, much less to convince those British voters who favor withdrawing from the EU. There is a real danger, then, that the United Kingdom will end its relationship with Europe—making the tragic mistake of trading genuine power for the mirage of national sovereignty.🌐