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The Baltic States on Brexit and EU Reforms

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In shaping the future relations between the EU and the UK as it withdrawing from Union membership, the Baltic States will opt for restraint and wait for a coalition of major countries to develop. Lithuania, Latvia and Estonia are eurozone members and support deeper European integration in connection with the negotiations with the UK on the conditions of its exit from the Community and the future shape of relations.

The Baltic States are developing relations with the UK, not only at the EU level but also within NATO and regional forums, such as the "NB8 plus" format, which brings together most of the countries around the Baltic Sea. They have many links with the UK, mostly political but also some socio-economic, which will condition their positions on Brexit. They cautiously comment on their preferred model of the EU's relations with the UK and monitor the positions of the other Member States and institutions. Even before the informal summit of the EU-27 in Bratislava this fall, European Council President Donald Tusk and German Chancellor Angela Merkel visited Tallinn. For Lithuania, Latvia and Estonia, the EU-27 should work to reduce the risk of variable integration, strengthen EU solidarity, and focus on security issues.

Strategic Importance of the UK. The United Kingdom is an important partner for the Baltic States, primarily in security issues and secondly in terms of economic policy governance in the EU. These countries hold a similar assessment of the threat from Russia, which they see as having the long-term goal of changing the post-Cold War political and legal order, including Eastern Europe—the post-Soviet areas—and Central Europe, along with a return to the archaic 19th century Great Power model in world affairs.

Brexit may therefore weaken the existing coalition of Member States interested in active EU policy opposing Russia's aspirations and supporting restrictions on its government. The UK has often proved an ally of the Baltic States in support for Ukraine and the continuation of sanctions on Russia. At the NATO Warsaw Summit, UK leaders confirmed the country's role as the framework nation of the battalion-level battlegroup that will support Estonia in 2017. As part of the Alliance's "extended presence," NATO forces will be increased along its Eastern Flank. This does not mean, however, that the Baltic States wholeheartedly support strengthening EU cooperation in security and defence. Clearly, they favour the development of cooperation between NATO and the EU and are particularly sensitive to any initiative that might harm the implementation of the provisions detailed at the Warsaw Summit.

Moreover, in economic terms, the UK promotes a model of EU development compatible with the approach of the Baltic States, especially Estonia. Their liberal attitude towards economic governance and regulatory policies link them together. So far, the UK has been the main proponent of decreasing economic restrictions in the EU, including in services. The governments of the Baltic States, backed by a good investment climate for foreign entities, are concerned about the negative consequences of Brexit on the future of the common market and the rise of protectionist measures in the EU.

Another challenge for the Baltic States is the potential for EU budget reductions if the UK—the second-largest net payer in terms of contributions to the common budget—leaves the Union. The Baltic States are net beneficiaries and are more dependent on EU subsidies than the average (amounting to about 14% of their budgets). Therefore, all three countries fear both a reduction in future transfers as well as the potential for increases in their own EU commitments.

Socio-Economic Ties. Of crucial importance to any Brexit negotiations will be the various economic interests of the Member States and this significantly determines their preferred model of the future EU-UK relations.[1]

Internal EU migration is for the Baltic States the most important issue because of the relatively large number of people from these countries residing in the UK. The mass emigration seen since joining the EU was due to the global economic crisis and rise in unemployment (in 2010, in Lithuania, the rate was 18%, in Latvia, about 20%, and in Estonia, 16.9%). According to official statistics, the most emigrants from the region were from Lithuania (about 150,000, or 5.4% of the country's population) and in the United Kingdom, they are now the third largest group of EU citizens. Also, 61,440 Latvians are in the UK (amounting to 3% of Latvia's population) and 8,700 Estonians (0.7%).

Because of this emigration, the importance of financial transfers to the Baltic States from the UK has increased. They are an important part of household budgets and it is estimated they amount to a significant share of the national income. In Lithuania, transfers constitute about 1.2% of GDP (about €300 million). Estimates of transfers to Latvia from its people living abroad in 2014 reached, according to the Bank of Latvia, 2.5% of GDP (€595 million) or, according to the World Bank, up to 4%, with a large share coming from the UK. Estonia also benefits from emigrant transfers to about 2% of its GDP, but the source is mainly Finland.

In trade, the UK is an important, though not the main partner for the Baltic States. Lithuania estimates that the mere risk of Brexit may cost it 0.5% to 0.8% of GDP in 2017. The UK is currently the seventh-largest partner in exports (€1.027 billion in 2015., which is about 5% of exports), and eleventh in imports (€750 million euro, or more than 2%). The most-affected industry would be furniture-makers because the UK takes about a fifth of the production in this segment. Latvia expects similar losses in its economy of a bit under 1% of GDP. Services provided to the UK is an important market for Latvia and is valued at €388.3 million (15%). These are mainly related to air transport, finance and tourism. Although less important, the UK is Latvia's seventh-largest export market (€537 million, or 5%) and fourteenth for imports (€236 million, or 5%). For Estonia, the UK is only its ninth-largest export partner (€326 million, or 2.8%) and eighth for imports (€350 million, or 2.6%). Of these, the most important segments are electrical equipment, innovation, and technology development.

These figures mean that, especially in the short term, a dramatic change in economic relations with the UK and the scale of the effects on them may be more unfavourable than follows from a simple accounting of economic and financial risk.

Perspectives. Lithuania, Latvia and Estonia are waiting for the larger Member States' positions on Brexit. As small countries with only a few votes in the EU Council, they will try to find a place for themselves within the emerging coalitions.

The Baltic States' but especially Lithuania's and Latvia's economic ties to the UK and potential for losses after Brexit mean they probably will opt for a relationship with the closest possible ties between the UK and the EU, including maintaining full access to the common market along the lines of the European Economic Area. Given the scale of internal EU migration, they will lobby to preserve freedom of movement, in particular treatment of their citizens in the UK, including social support guarantees.

Moreover, the Baltic States will try to exploit the EU institutional and personnel changes that result from Brexit to expand their role in the Union, especially over economic policy. Although the UK's departure would increase the value of Lithuania's and Latvia's votes in the European Council only slightly—from 0.6% to 0.7% and from 0.4% to 0.5%, respectively, according to the report "Global Counsel"—their bargaining power in building coalitions will grow. Furthermore, other Member States may count on their support in siding with either a liberal approach to the economy or on regulatory policy, and as supporters of closer EU integration and in coordination of fiscal policy.

The chances of promotions of Baltic States' representatives to EU institutions are also favourable. One such person is Latvian Valdis Dombrovskis, the vice-president of the European Commission who oversees the euro portfolio and, after the resignation of the UK's Jonathan Hill, is also responsible for the EU Directorate-General for financial stability, financial services and the capital markets union (DG FISMA). This allows him to guide the political dialogue on relevant issues. Meanwhile, Estonia will take up the presidency of the EU Council at an earlier date instead of the UK and will try to use the opportunity to lobby for a digitalization agenda. This would make it easier for former Estonian Prime Minister and current EC Vice-President Andrus Ansip to push the Commission forward with plans for cybersecurity, the development of technological innovation, and the "digital single market."

[1] K. Borońska-Hryniewiecka, S. Płóciennik (eds.), *Probable EU-UK Relationship after Brexit: Perspectives of Germany, France, Italy, Spain and Poland*, PISM Report, June 2016, www.pism.pl.