Negotiating Brexit Under Extreme Uncertainty

A game theoretic analysis of the UK’s threat of no deal

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Abstract

The ongoing Brexit negotiations are the first ever negotiations about the withdrawal of a member state from the European Union. The result of the negotiations will determine the UK’s terms of withdrawal and the framework of the future relationship between the two. The outcome of the negotiations depends on the actions of both parties which are taken in an environment of extreme uncertainty as withdrawal negotiations have never happened before and the players’ preferences and the payoffs of the possible outcomes are uncertain. In this context has the UK government threatened that “no deal is better than a bad deal”. This thesis examines the role of the UK’s threat of no deal in the negotiations with the EU and, more precisely, the conditions for the threat to be efficient and coerce the EU to make concessions. To examine this problem the thesis applies a game theoretic model to assess the conditions of credibility and severity under different assumptions about the information available to the players. The conditions for the threat to be effective are less strict under the assumption of incomplete information than under complete information, as the former assumption opens up for misrepresentation of information by the two players. For the threat to be efficient under incomplete information the UK must make the EU believe that the threat is credible, and the EU must evaluate the threat to be sufficiently severe. I conclude that it seems unlikely, even under incomplete information, that the UK’s threat can meet the necessary conditions for the threat to be effective and a deal beneficial to the UK to materialize. This conclusion is drawn by evaluating the conditions deduced from the game theoretic model based on knowledge about the actual case of Brexit obtained from various sources, such as interviews with key informants, public documents and speeches.

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1 Introduction

On June 23 2016 the British people voted in favor of leaving the European Union (EU). Nine months later the British government triggered Article 50 in the Lisbon Treaty, formally starting the negotiations of the UK’s withdrawal from the EU. Since then, the issue of Brexit has been the topic of public and academic debate. Never before has a member state decided to leave the EU, to disentangle its ties with the Union and to commence a new relationship with it. The exit process has an undefined final destination as the terms of withdrawal and the future relationship between the two parties will be a product of the ongoing negotiations. These features give the Brexit negotiations both an unprecedented, complex and uncertain nature.

In this environment a tug of war between the UK and the EU is taking place. The two parties, although their relationship is of asymmetric interdependence, would both benefit from an agreement, rather than no agreement. Nonetheless, the two parties have conflicting interests concerning what kind of deal should be concluded. In order to obtain the best possible deal, the two players have incentives to engage in different kinds of strategic play. The use of threats is one type of strategic play and is quite common in international negotiations (Hovi 1998, p. 57). The British government has, since before the start of the negotiations, upheld the mantra of “no deal is better than a bad deal”1. This statement can be interpreted as a threat to leave the negotiations unless the EU makes some concessions, and is a part of the strategic tactic used by the UK to try to obtain the best possible deal. Some have doomed the mantra meaningless and unhelpful (Johnson 2017), while others have described it as “the best strategy” the UK has left (Muthoo and Benita 2017). Can the UK’s threat of “no deal” be an effective tool for the UK to obtain a better deal?

Negotiations about a member state’s withdrawal from the EU has no historic precedence. This thesis tries to provide a roadmap for understanding the process of Brexit and its strategic interaction taking place under high levels of uncertainty. Furthermore, it provides insights to the process of exit from the EU and political phenomena involving strategic interaction happening under extreme uncertainty, in general.

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1 Among other stated by Theresa May in her Lancaster House speech on January 17 2017 setting out the government’s negotiation objectives.
1.1 Objective of thesis and research question

In this thesis I will analyze the UK government’s use of the threat of no deal in the Brexit negotiations. In order to be effective, a threat must fulfill certain conditions. The objective of this thesis is to clarify the conditions necessary for the no deal threat to be effective. My research question is: What are the conditions under which the UK’s threat of leaving the negotiations will coerce the EU to make concessions?

In order to answer the research question, I will explicitly consider the interaction between the UK and the EU in the Brexit negotiations. The interaction is strategic, meaning that the outcome of the negotiations depends jointly on both players’ actions. In addition, the interaction is taking place under extreme uncertainty. The players’ unknown preferences and capabilities, the unknown payoffs and the unknown consequences of the negotiations set-up, as there are no priors, are all sources of uncertainty in the negotiations. To clarify the conditions under which the threat of no deal can be efficient, I model the Brexit negotiations as a simple game theoretic model. I analyze the model under different assumptions concerning the players’ preferences and the information available to them to account for the players’ beliefs and the uncertain nature of the negotiations.

1.2 Literature review

Brexit is a topic in need of theoretical analysis. Since the referendum in June 2016 there has been daily news about Brexit either in form of a new speech, debate, declaration or leaked documents. The Brexit process is unusually complex due to its broad scope of issues and many actors, both on the domestic and international level. In order to fully comprehend the process and its implications, some conceptual and theoretical grounding is needed. In the almost two years since the referendum that initiated Brexit, an academic literature has emerged. So far much of the “Brexit-literature” focus on three main areas of research: accounting for the path to the referendum and why it occurred, explaining the result of the referendum and, thirdly, assessing the likely consequences of Brexit. In this third area the negotiations themselves obviously feed into the analysis, as they will determine what kind of deal which can be agreed upon. However, to my knowledge no existing studies look at the strategic interaction between the UK and the EU by modeling the negotiations as a formal game. My research project looks at the negotiations themselves, not at the causes leading to
them or the consequences of them per se. In so doing it also represents a new contribution to the literature on Brexit. In this section I will briefly review the existing literature on Brexit, an area of research in growth, and place my own contribution in this emerging literature.

1.2.1 The causes of Brexit

The two former mentioned areas of research which study the path to the Brexit referendum and the referendum result, both investigate the causes of Brexit. They try to answer the questions of why the referendum occurred and why it produced a majority in favor of leaving the EU. The literature studying why a referendum on British EU membership took place look at both UK-specific developments and more general developments. In chapter 2 I present an overview of the relationship between the EU and the UK and discuss why a referendum was held in the UK and why now. This presentation and discussion relies on literature explaining the path to the referendum, therefore I do not review this literature further in this section.

Analyzing the referendum result is a core issue in the Brexit-literature and the focus of several scholars studying the causes of Brexit. The area of research investigate why Britain voted for Brexit and the importance of different factors in explaining the referendum result. The literature finds that socio-demographic variables such as age, education and occupation had considerable impact on the level of individual voters. An initial study of the referendum result was done by Goodwin and Heat (2016) who drew on aggregate-level data to study, amongst other, the effect of socio-demographic variables on the referendum vote. They argue that the referendum result “revealed a society which had, on the issues of EU membership and immigration, become divided by social class, generation and geography” (p. 324). They find that support for Brexit tended to be stronger in local authorities with high numbers of pensioners, low-skilled workers and less-educated citizens (Goodwin and Heat 2016).

Additionally, the result varies geographically and the support for Brexit was higher in rural areas than in urban areas. There were also differences between the regions, in England and Wales the leave vote got a majority while in Scotland and Northern-Ireland it did not (ibid.). As more sophisticated individual level data became available, closer examination of the factors explaining the vote became possible. In their article “Why Britain Voted for Brexit: An Individual-Level analysis of the 2016 Referendum Vote” Clarke et al. (2017) use a

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referendum voting model to study national panel survey data. By studying these data, they find that a particular coalition of voters came together to give the leave side its majority.3 Concerns for immigration and national identity, as well as economic cost-benefit calculations strongly shaped the voters’ decision (Clarke et al. 2017). The role of immigration is found to be a key factor in explaining the Brexit-vote by the recent Brexit-literature. How immigration influenced the vote is studied by, among other, Goodwin and Milazzo 2017 and Parker 2017.

1.2.2 The consequences of Brexit

Many scholars have engaged in the work of assessing the consequences of Brexit. The potential consequences of Brexit are many and complex. Brexit may, among other, affect the UK’s standing internationally (see Adler-Nissen et al. 2017), its relationship with the US (see Rees 2017 and Wilson 2017), its diplomacy (see Dee and Smith 2017), its internal territorial politics and devolution (see Henderson et al. 2016, Gormley-Heenan and Aughey 2017, McHarg and Mitchell 2017), the UK’s national sovereignty and the UK’s economy. Brexit will also produce a wide range of consequences for the EU. It may affect European integration in various ways, the internal decision making as the member states relative influence may change (see Hix et al. 2016) and it may have economic consequences for the EU. This thesis does not engage in assessing or predicting the consequences of Brexit. But the players’ perceptions of the cost and benefits of different possible outcomes of the Brexit negotiations play a role in the game and when deducing the game’s equilibria, as they determine the players’ actions.

My research project does not fall within the areas of research which look at the causes and effects of Brexit but aims at contributing to the theoretical analysis of Brexit by studying the negotiations themselves and the strategic interaction taking place between the UK and the EU in an environment of extreme uncertainty. Brexit is an extremely complex process and pose an overwhelming challenge to scholars and students, as myself, trying to understand it. Theoretic analysis is necessary to gain insights in this process. I find that game theory provides useful tools which make it possible to study the ongoing negotiations and take account for the strategic interaction and the high levels of uncertainties. In the next section I will present and discuss my methodological choices.

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3 Point made by Matthew Goodwin at a lecture at University of Oslo 07.03.2018.
1.3 Research design

I have chosen to model the Brexit negotiations formally and use game theory to address my research question. This formal game theoretic approach differs from the approaches taken by the literature reviewed in section 1.2. Given the strategic interaction between the UK and the EU taking place in the Brexit negotiations, game theory provides a useful methodological approach in order to better understand the process. The game theoretic model used in this thesis does not try to be a comprehensive representation of the negotiations, neither does it address all the complexity of the strategic interaction between the UK and the EU. That would be an impossible task given the complexity of the negotiations. Simplification is both necessary for the model not to become too complicated, and desirable because it enable us to draw implications from the model (Hovi 2009, p.24). The purpose of modelling the Brexit negotiations as a game theoretic model is to identify the most important elements of the negotiations, relevant information and likely outcomes, in order to identify equilibria conditions for the threat of no deal to be efficient (for similar considerations see Gates and Humes 1997, p. 8). In this section I will present the method and data which will be used to study my research question.

1.3.1 Method

This thesis seeks to clarify the conditions for the UK’s threat of no deal to be effective. To do so I use game theory to model the Brexit negotiations and to generate explanations and predictions concerning the efficiency of the use of the no deal threat. In this section I define game theory, present its main underlying assumptions and discuss how game theory can be used to study political phenomena. Finally, I discuss why game theory is a suitable and desirable method to study my research question.

Game theory can be defined as a theory of interaction among rational actors (Hovi 2008, p. 11). A game models a situation where the players are aware that their actions affect one another and is, thus, a situation of strategic interaction (Gates and Humes 1997, p. 5). Strategic interaction means that the outcome of the game depends jointly on the action of two or more decision makers (Hovi 1998, p. 3). Many political phenomena involve strategic interaction and, thus, makes game theory a useful method to study politics (Gates and Humes...
In this thesis game theory will be applied to study the strategic interaction in the Brexit negotiations.

Game theoretic modeling is one type of rational choice theory and is founded on the assumption of rational actors. The meaning of the assumption of rational actors is somewhat debated in the literature (Hovi 2008, p. 17-21 gives an overview). In this thesis I will apply Elster’s “thin theory of rationality” according to which an action may be characterized as rational if it stands in a certain relationship to the actor’s preferences (Hovi 1998, p. 4, see also Elster 1986). An actor is rational if it has consistent preferences and acts consistently with these preferences (ibid.). Thus, actors make rational choices if they have a set of preferences over possible outcomes and select actions that satisfy these preferences (Gates and Humes 1997, p. 9). The actors take into account both the assumption of rational actors and the assumption of strategic interaction when making their choices. All players know that all players are rational, and that the outcome of the interaction partially depends on their own actions and partially on the actions of the other actor(s) (ibid.).

In game theoretic models preferences are exogenous, meaning that they are derived outside the model. The players’ preferences are assumed to be (i) complete, (ii) fixed and (iii) transitive (Gates and Humes 1997, p. 8). The first assumption, completeness, means that the player is able to rank the possible outcomes. When comparing two possible outcomes, the player either prefers one of the outcomes over the other or is indifferent. Secondly, preferences are assumed to be fixed and do not change during the game. Thirdly, preferences are transitive which means that if the actor prefers \( x > y \) and \( y > z \), then it will also prefer \( x > z \). The game theoretic model in this thesis will be analyzed with different assumptions concerning the players’ preferences. Different preference assumptions make different equilibria materialize in the game theoretic model analyzed in this thesis. Deduction of equilibria, given certain assumptions about preferences, gives us explanations and predictions concerning the threat’s efficiency.

Game theoretic models further assume that all players of a game possess “common knowledge” concerning some aspects of the game. When something is assumed to be common knowledge every player knows it, everyone knows that everybody knows it, everybody knows that everybody knows that everybody knows, and so on (Gates and Humes 1997, p. 9). This affects the way the players’ expectations are shaped. What aspects of a game that is assumed to be common knowledge is defined by the game’s specifications. Most game
theoretic models assume common knowledge about the rationality of other players and the structure of the game. Complete information games also assume that the players’ preferences are common knowledge, while in incomplete information games the players’ preferences are not common knowledge. In this thesis I will analyze the game theoretic model both under the assumption of complete and incomplete information to account for the role of beliefs and uncertainty.

When game theory is applied to international relations (IR), states often constitute the players of the game. Game theoretic application to IR usually involves making the assumption of unitary actors (Hovi 2008, p. 22). This means that states are interpreted as actors with one utility function and one set of preferences. One way to see this, is to interpret the state’s utility function as an aggregated utility function of all the individuals’ preferences (Hovi 2008, p. 23). A second way to think about it is to imagine that there is one person that has the last word when a state is making a decision and, thus, represents the state’s utility function (ibid.). As states are complex entities which consist of many sets of preferences, this is an unrealistic assumption. However, it may be argued that this assumption is a necessary simplification to make modelling possible. It may also be argued that it is a reasonable assumption as states act as unitary actors on the international arena. In the Brexit negotiations the two parties do negotiate as if they were unitary actors. Additionally, I expect this assumption to enable an analysis which will produce interesting findings concerning the possibility of the threat of no deal to be effective. This simplification makes it possible to study the conditions for the threat to be effective in the strategic interaction between the UK and the EU. I will discuss the use of the assumption of unitary actors in this thesis more thoroughly in section 3.6, accompanied with a presentation of two-level games.

Game theory can be used in three manners: (i) to explore theoretical problems that arise directly from the development of game theory, (ii) to analyze actual strategic interactions in order to either predict or explain the actions of the actors involved and (iii) to analyze the logical consistency of certain arguments (Fink et al 1998). The purpose of this thesis falls within the second manner. Game theoretic analyzes that study actual strategic interactions can either examine general questions or specific cases (Fink et al 1998, p. 1-2). This thesis involves in both. Its primary concern is to study the specific case of the Brexit negotiations and identify conditions for the UK’s no deal threat to be efficient. Additionally, it engages with the more general question of what kinds of tactics in a withdrawal negotiation with the
EU enable a withdrawing member state to cause the EU to move in the direction it desires (for similar considerations see Zartman and Rubin 2000, p. 9). The Brexit negotiations are the first of their kind as no member state has ever left the EU. So, there are no priors to look to when assessing what tactics enable an exiting member state to force the EU to make concessions in withdrawal negotiations.

Is game theory a suitable method to study the Brexit negotiations in order to assess the conditions for the threat to be efficient while accounting for the role of uncertainty? Game theory is especially suitable as a method if the political phenomenon in question involves strategic interaction between actors and the objective of the study is to account for the role of information and uncertainty. The Brexit negotiations are a case of strategic interaction which is occurring in an environment of extreme uncertainty. This thesis seeks to account for the role of information when inferring explanations and predictions concerning the conditions for the threat of no deal to be effective. Game theory provides a method in order to explicitly model the role of strategic interaction and information (Gates and Humes 1997, p. 164). The objective of this thesis is to deduce the conditions for the threat of no deal to be efficient under different assumption about information and preferences. This will again contribute to the more general aim of the analysis, to gain new insight on and improve our understanding of the process of Brexit through the application of game theory.

The principal advantage of studying the Brexit negotiation using a game theoretic model is the clarity and rigor provided by formal analysis (Gates and Humes 1997, p. 7). However, in order for game theory to be an effective tool to study a political phenomenon, such as the Brexit negotiations, and contribute to the understanding of it, it must be used correctly. That involves being explicit about the assumptions made, making the analysis formal and explicit and the conclusions clear (Gates and Humes 1997).

1.3.2 Data

This thesis provides a theoretic and formal analysis of the conditions for the UK’s threat of no deal to be efficient and certain equilibria to materialize. The objective of this applied game theoretic analysis is to gain new insights on the Brexit negotiations. In order to obtain such insight through the application of game theory, knowledge about the actual case is necessary. Empirics serve as the foundation for assessments of which of the equilibria deduced from the
formal analysis of the model seem more plausible. The empirics are also used to assess the assumptions about the players’ preferences and the payoffs attached to the different outcomes.

The analysis is based on empirics from a wide specter of sources, such as public documents, speeches and statements, secondary literature, as well as interviews. Both parties, the EU and the UK, have made their negotiation positions available through publishing negotiation guidelines before the start of the negotiation. As the negotiations have taken place, the two parties have expressed their positions through, among other things, public speeches and negotiation papers. The Brexit negotiations are an ongoing event, and the parties have interest in intentionally distorting information about their respective preferences, motives and capabilities. Consequently, data from primary sources must be treated critically.

Additionally, I have conducted three interviews in order to complement the data from other sources. I have interviewed two scholars, Abhinay Muthoo and Christopher Lord, and one EU official. The interviews were semi-structured and served both to collect information, to help me interpret the motive behind actions and statements and to evaluate the threat’s credibility and severity. The interviewees were selected because they are key informants as they follow the negotiations closely and possess knowledge on different aspects of the negotiations relevant for my research project. This selection criteria makes my sample of informants unrepresentative and unbalanced. However, engaging key informants permitted me to explore and probe my assumptions and interpretations (see Andersen 2006 for further discussion). The information acquired by talking to my informants serve as a hybrid between scholarly advice and empirics in the analysis.

1.4 Structure of thesis

The thesis is organized as follows:

Chapter 2 presents an overview of the relationship between the EU and the UK in a historical and substantial perspective. Furthermore, it presents the exit option from the EU and how it became a legal and unilateral possibility. The set-up of Article 50 is also presented and discussed.

Chapter 3 presents the theoretical framework of the thesis. Central is the theoretical conditions for a threat to be effective and theory on asymmetric negotiations and bargaining.
power. Additionally, the chapter discusses the assumption of unitary actors and present Putnam’s two-level game framework.

Chapter 4 presents the main players in the Brexit negotiations, their preferences, strategies and the possible outcomes of the negotiation. These elements are defining parts of a game theoretic model and will serve as the fundament for the game theoretic analysis in chapter 5 and 6.

Chapter 5 sets up the game theoretic model which will be used to study the conditions of severity and credibility for the threat to be efficient. The threat game is then analyzed under the assumption of complete information.

Chapter 6 analyzes the threat game under the assumption of incomplete information and discusses the conditions of severity and credibility. The equilibria conditions and the possibility for the UK’s threat of no deal to be efficient as the payers’ beliefs have become a part of the game are discussed.

Chapter 7 will summarize and conclude.
2 Background

By activating Article 50 the UK is putting an end to 40 years of EU membership. In this chapter I will present an overview of the relationship between the EU and the UK in historic and substantial terms. Additionally, I present the legal possibility to exit from the Union and the set-up of Article 50.

2.1 The UK and the EU

Brexit is a contemporary and ongoing event, but still deeply rooted in history. But where to begin the story of Brexit, how far back in time is it necessary to go in order to understand the background of the current events? One option is to start in recent history. Either with the result of the Brexit referendum held in June 2016 where a majority of the British population voted to leave the EU or, a little further back in time, with Prime Minister David Cameron’s announcement of his intention to hold an in-out referendum on the UK’s membership with the EU. Another option is to go even further back in time and start the story with the accession of the UK into the European Community (EC) in 1973, or all the way back to the negotiations about the Treaty of Rome in the 1950 with the UK not taking part. In this section I will present an overview of the relationship between the UK and the EU in a historical and substantial perspective, some longstanding positions in the UK’s policy towards the EU and, finally, the “path” to the Brexit-vote in 2016.

2.1.1 Britain in the EU: the “awkward” member state

Many scholars have described Britain’s relationship with the EU as awkward, reluctant and semi-detached (Bache and Jordan 2006, p. 4, Geddes 2013, p. 27). These descriptions build both on Britain’s early abstention from membership and its behavior as a member (Bache and Jordan 2006, p. 4). Britain was initially reluctant to join the EC and did not want to take part of the negotiations which lead to the signing of the Treaty of Rome in 1956 (Gamble 2012, p. 6, Bache and Jordan 2006, p. 4). The lack of interest in joining the EC among British politicians can be explained partly by the UK’s strong relations to the US and to the remnants of its Empire (ibid.). Churchill saw Britain as the center of three circles of influence, the

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4 Point made by Alan Finlayson during a lecture at Litteraturhuset on December 4 2017.
5 EC is here used to describe the EU before the entry into force of the Maastricht Treaty.
empire, the special relationship with the US and Europe, where the two former were given priority in post-war British policy (Geddes 2013, p. 34). It was thought, among political elites, that joining the EC would reduce Britain’s influence in the two other circles (Bache and Jordan 2006, p. 6). British policy towards the EU was reevaluated in the 1960 as Britain experienced relative economic decline and that its ties to the US were not as strong as the British had thought⁶ (Geddes 2013, p. 54, Bache and Jordan 2006, p. 6). The UK applied for membership twice in the sixties, in 1961 and 1965. Both times the application got vetoed by the French President Charles De Gaulle who feared that the UK would seek to dominate the EC and lobby American interest in Europe (ibid.). In 1970, the UK applied for membership for a third time. Georges Pompidou, who was in favor of British membership, had then replaced De Gaulle as President and the application led to British accession in 1973 (Geddes 2013, p. 56).

As a member state, Britain’s engagement with the Union has been described as conditional and differential (Geddes 2013, p.11). Conditional means here that the relationship is based on pragmatic calculations about costs and benefits, rather than ideals and attachment to the European project (ibid.). The British “path” of ambivalence towards the EU was established in the 1950 with the consequence that Europe has never become embedded within the preferences, identities or interests of neither Britain’s political elite nor the British people (Geddes 2013, p.11-12). This lack of British enthusiasm for and identity with the EU, together with the pragmatic cost-benefit calculating approach to EU membership, has set up Europe as a “choice” for the UK (Daddow 2013, p. 214). The perception of Europe as a choice – that the UK can choose to be in or out, or semi-attached – and not as a fixed part of the political landscape, makes the European question open for contestation in Britain (ibid., Copsey and Haughton 2014, p. 82). This perception of Europe has had persistent relevance, as seen in the development over the last years.

Further, the UK’s engagement with the EU is differential in the sense that Britain has opted out of key aspects of European integration (Geddes 2013, p.11). In its 40 years as a member state the UK has negotiated its own specific terms of membership. Other member states have also negotiated optouts, but no other has as many as the UK (Copsey and Haughton 2014, p. 76). The UK does not participate in the Schengen area of passport-free travel, is not a part of the single currency and has a rebate on its budget contributions (Geddes 2016, p. 280, Copsey

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⁶ This was manifested, among other things, by the Suez crisis.
and Haughton 2014, p. 76). It has been argued that the UK’s terms of membership are the most privileged terms of any member state in the EU (Copsey and Haughton 2014, p. 75). This characteristic of the UK’s engagement with EU makes it hard to see why the UK would want to leave the EU. Whereas the UK’s perception of Europe as a choice point in the opposite direction and helps explain why withdrawal was a possibility for Britain.

2.1.2 Elements of continuity in British policy toward EU

In Britain’s 40 years of membership, some strong elements of continuity in its approach to European integration can be identified. According to Geddes, successive British governments have demonstrated three longstanding positions on the EU (2016, p. 266): a preference for intergovernmentalism, a belief that the EU should be about markets not politics and concerns about sovereignty and national identity. Additionally, the UK’s European policy has been set against a longstanding and consistent preference for maintenance of strong transatlantic ties with the US (Geddes 2013, p. 27, Bache and Jordan 2006, p. 5).

British policy towards the EU has been characterized by the consistent preference for an intergovernmental EU of sovereign member states, rather than supranational integration (Geddes 2016, p. 266, Allen 2013, p. 109). British EU-policy has tried to limit the extent of European integration and rejected the idea of a “federal” EU (Allen 2013, p. 109). The UK has been in favor of an enlarged Union with increasing marked integration. It has been Britain’s view that the EU should be about markets and not politics (Geddes 2016, p. 267). The UK has ever since it became a member been in opposition to the development of an “ever closer Union”. Accordingly, British policy has been to promote the Single Market and the EU as a free trade area, but not deeper political integration. Third, concerns of national identity and sovereignty have been an important theme in the British discussion on the EU. Many Brits see European integration as a threat to national identity and sovereignty (Geddes 2013, p. 32).

The desire to maintain a close relationship with the US has been a consistent line taken by British governments (Bache and Jordan 2006, p. 5). This desire has affected the UK’s relation to the EU: “at key moments Britain’s relation with the United States and the EU respectively have created tensions, which have generally been resolved to the detriment of its pro-European credentials” (ibid.). Churchill words to De Gaulle during World War II demonstrate the British ambivalence towards the EU and its desire of maintaining a strong relation to the
US: “Each time we must choose between Europe and the open sea we shall always choose the open sea. Each time I must choose between you and Roosevelt I shall always choose Roosevelt” (cited in Gamble 2012, p. 473).

2.1.3 The path to the Brexit referendum

Against this backdrop one may ask why the UK decided to leave the EU at this point? Geddes argues that there are particularly three developments in the last decade that have changed the relation between the UK and the EU and “pushed Britain to the EU’s exit door” (2016, p. 270-277): the effects of the financial crisis and the refugee crisis, the mainstreaming of Euroscepticism, and the rise of UKIP. The two latter developments can largely be seen as consequences of the first development, as the EU’s dysfunctionality has led to the rise of Euroscepticism and the support of UKIP. A fourth development that has been central in the EU-debate in the UK over the last years and particularly in the referendum campaign, is the rise of EU-immigration to the UK.

The first development consists of the two crises that have hit the EU in the last decade. The financial crisis that evolved into an eurozone crisis has had implications for the UK even though it is not a member of the eurozone (Geddes 2016, p. 271). So have the large flows of migration to Europe, the refugee crisis, although the UK has an optout from the Schengen agreement (ibid.). The two crises have raised question about the EU’s ability to respond effectively to crises and intensified the debate about the legitimacy of the Union (Geddes 2016, p. 272). In addition to the concerns for migration to the EU, has the concern for intra-EU free movement grown in the UK. Immigration, in general, and immigration from EU-countries, in particular, has become a key concern for the British public (Geddes 2016, p. 271). Public worries about EU free movement has fueled the opposition to the EU and the support for UKIP (Geddes 2016, p. 272).

The second development, that is both a cause to and an effect of the changed British relation to the EU, is the rise of UKIP (Geddes 2016, p. 276). UKIP has called for Britain to leave the EU and has become, due to the party’s growing public support, a significant voice in the British public debate on the EU. Consequently, the rise of UKIP is one of the factors which explain the UK’s exit from the EU. However, UKIP’s rise can also be seen as an effect of the changed British relation to the EU as its growing support can be explained by how it has capitalized on the rise of Euroscepticism in the UK (ibid.).
The third development is the growth and mainstreaming of popular opposition to the EU in Britain (Geddes 2016, p. 272). With mainstreaming of Euroscepticism, Geddes means to say that Euroscepticism has moved from being a marginal concern for people on the side of mainstream politics to be a part of mainstream politics (Geddes 2016, p. 273). This is to a large extent the case for the Conservative Party, but not to the same degree for the Labour Party (ibid.). The European question has been an issue that has divided both parties internally, but in particular the Conservative party (ibid.). Consequently, the growth of Euroscepticism in the UK and, thus, the path towards the referendum has mainly been generated by the Tories. The shift in the nature of European integration is key to explain the rise of Euroscepticism in the Conservative Party (Copsey and Haughton 2014, p. 82). The development of European integration was the theme of Margaret Thatcher’s speech in Bruges in 1988 where she expressed her fear of the emergence of a Federal European Union (ibid.). This speech is argued to have legitimized Euroscepticism and provoked a debate in the Conservative party about Britain’s place in the EU and in the global economy (Geddes 2013, p.229). Three years later the Maastricht Treaty was signed and “signaled that European integration was about more than markets” (Copsey and Haughton 2014, p. 82). This development of the European integration project, which had been the idea from the start, as a project of wide political cooperation and supranationalism was in contrast to the UK’s desires of a Union that consist of market only.

Over the last years the Conservative Party has seen an internal tug-of-war about the form of Euroscepticism between different strands (Geddes 2016, p. 273). Geddes identify four different strands within the Conservative party: the outright rejectionists, the maximal rejectionists, the minimal rejectionists and the minimalists (ibid.). The first strand wants the UK to leave the EU even if that involves leaving the Single Market, the second strand would like a new settlement with the EU where the UK remains in the Single Marked while not accepting all the free movements (Geddes 2016, p. 273). The minimal rejectionists only want small changes and repatriation of some powers, while the minimalists want to continue with the existing opportunities of optouts from parts of EU-treaties to resist further integration (Geddes 2016, p. 274). These different strands have different views on what the future deal with the EU should look like, what the consequences of the possible outcomes are and how the UK should negotiate Brexit.
During the Conservative-Liberal Democrat coalition government between 2010-2015 the tensions over the EU-question grew, both inside the Conservative party and between the two coalition parties. The hardline Eurosceptics in the Conservative party thought that the government did not take a hard-enough stand on European integration, while the Liberal Democrats though that their views were not represented well enough. In order to respond to and try to calm the internal EU-debate in the Conservative party, Cameron announced in January 2013 his intention to renegotiate the UK’s terms of membership with the EU and then hold a referendum on the renegotiated terms, if the Conservatives got reelected in the upcoming election in 2015 (Geddes 2016, p. 276). The Conservatives won the election and Cameron initiated renegotiations of the UK’s membership conditions with the EU. Cameron’s strategy was to negotiate a deal with the EU that would be sufficient to convince the British people to stay in the EU rather than to exit. This process is somewhat an echo of the process in 1975, the first British referendum on its EU-membership. The settlement of the renegotiation discussion between the UK and the EU was agreed in February 2016 and Cameron declared “victory” even though the deal only partially met his renegotiation agenda (Geddes 2016, p. 283). Nonetheless, on the 23 June 2016 52 percent of the Brits choose the “Leave the European Union” over the alternative “Remain a member of the European Union” when voting over the referendum question “Should the UK remain a member of the European Union?” (Geddes 2016, p. 264).

The result of the Brexit-vote will change British politics, the UK’s place in the world and its relation to the EU (Geddes 2016, p. 264). How is uncertain and remains to be seen. UK’s future relationship with the EU will to a large extent be a result of the ongoing Brexit negotiations. Never before has a negotiation about withdrawal from the Union been held between the EU and a member state. Withdrawal negotiations with the EU under Article 50 are different from negotiations with the EU as a member state. In the next section I will have a closer look at how negotiating with the EU as a withdrawing member is different from negotiating with the EU as a member state.
2.2 The exit option

In this section I will present and discuss the possibility to withdraw from the EU, its origin, rationale and consequences.

2.2.1 The origin of the legal possibility to exit

An explicit option of withdrawal from the European Union was first set down in Article 50 of the Treaty of Lisbon. When the Lisbon Treaty came into effect in 2009, the legal right to withdraw was a novelty since none of the previous treaties of the EU had laid down such a provision (Lechener and Ohr 2010, p. 358). However, the issue of withdrawal from the EU was not something new. Whether or not it was possible for a member state to withdraw from the EU in a legitimate way had been a topic of debate (Berglund 2006, p. 150, Poptcheva 2016). There was, however, no definite conclusion to this discussion before the entry into force of the Treaty of Lisbon (ibid.).

The debate of whether unilateral withdrawal from the EU was possible or not was, by some scholars, linked to the broader discussion about whether member states had transferred sovereign powers permanently to the EU or delegated powers that could be retracted (Berglund 2006, p. 149). The latter view was supported by national courts and made withdrawal possible, the former was supported by the European Court of Justice (ECJ) and made withdrawal not possible (ibid.). Due to the different views on this question, this debate did not answer the question of the possibility of withdrawal (Berglund 2006, p. 150). Other scholars tried to find answers by studying international law. Some argued that the right to withdrawal was to be found in the principles of international law and in the Vienna Convention on the Law of the Treaties (Berglund 2006, p. 151, Poptcheva 2016). While others argued that international law did not give any specific guidelines and could not be used to bring any clarity to the question of unilateral withdrawal (Lechener and Ohr 2010, p. 358).

Furthermore, another view in the debate of the possibility to exit the EU was that all member states in agreement could decide to let a member state withdraw, thus making a negotiated withdrawal possible, but not a unilateral withdrawal (Berglund 2006, p. 150, Poptcheva 2016).

The work of including a legal possibility to exit the EU started before the Treaty of Lisbon. A provision for unilateral withdrawal from the EU was included in the Treaty establishing a
Constitution for Europe (TCE) which was signed by all member states’ governments in 2004, but then its ratification was rejected by referendums in France and the Netherlands (Berglund 2006, p. 152). The provision was then included in the following Lisbon Treaty.

2.2.2 The rationale of the exit option

What are the arguments for a legal, unilateral possibility to exit? When the exit option was agreed upon in the draft to the TCE, it was based on the (debatable) premise that withdrawal would be permissible anyway through international law (Poptcheva, p. 2). Another argument for a unilateral possibility to exit is that withdrawal would be politically possible even with no legal right to do so (Berglund 2006, p. 154). If a member state would want to withdraw from the EU, the other member states are not in a position to hinder the state to do so (ibid.). The EU can make it hard and costly for member states to exit the Union, but not impossible. An additional argument used in the work with the TCE was that the EU is a voluntary cooperation and states should be able to leave if they wish (Berglund 2006, p. 153). The member states wanted to send a political signal with the inclusion of a withdrawal provision that the EU is not, as stated in the Draft TCE, a “rigid entity which it is impossible to leave”.

2.2.3 Relevance and consequences of the exit option

The legal right to withdraw from the EU can be applied by member states that experience that the advantages of EU membership have become less beneficial and dominated by the advantages of being non-member (Lechner and Ohr 2010, p. 359). The right of withdrawal can also be used by the member states as a threat in order to obtain concessions for remaining a member (ibid.). I will in this section have a closer look at these two applications of the exit option.

The inclusion of a unilateral option of withdrawal has ended the debate about whether or not it is possible for member states to leave the EU legally. Nevertheless, it has enhanced a debate about whether political and economic considerations make withdrawal an unrealistic option for member states (Hofmeister 2010, Berglund 2006). There may exist both economic and political reasons for a member state to want to withdraw from the EU. Every member state has its own specific cost-benefit relation depending on its affiliation to the Union (Lechener and Ohr 2010, p. 259). To evaluate if EU membership is utility maximizing, a member state may compare the benefits from membership with the benefits of non-membership (Lechener
and Ohr 2010, p. 260). This cost-benefit analysis may change over time due to developments of the EU such as enlargement, increase in areas of cooperation and changed decision-making procedures (ibid.). The EU has since its foundation extended from 6 to 28 member states (including the UK). This enlargement has led to increased heterogeneity in preferences within the Union and thus a rising costs of coordination (Lechener and Ohr 2010, p. 259). The decision-making processes in the EU has undergone reforms to adapt to this increasingly heterogeneous Union (Lechener and Ohr 2010, p. 258). The use of unanimous voting has been gradually reduced in favor of majority voting in order to speed up the decision-making process (Lechner and Ohr 2010, p. 372). The increased use of majority voting gives the member countries less bargaining power, because they do not have a right to veto. This may lead to a situation where a country gets outvoted repeatedly and thus receives fewer benefits out of its EU membership (Lechener and Ohr 2010, p. 259). According to this, the unilateral possibility to withdraw from the EU may become an option for countries that experience that the benefits of membership has decreased.

Secondly, the inclusion of the unilateral possibility to exit has given the member states the possibility to threaten to leave the Union by triggering Article 50 in order to gain concessions from the EU. If a member state’s cost-benefit relation is modified, it may try to get compensation for these changes from the EU by threatening to leave. The use of the exit threat as a bargaining tool has changed the negotiation power of the member states in internal EU negotiations. Lechner and Ohr study the shifting negotiation power of member states under different decision-making rules (2010). They asses how the introduction of an explicit exit option may have changed the member states’ bargaining position within the EU. When assessing the question about whether the member states have regained negotiation power due to the exit option, they find that the exit option increases the member states negotiation power compared to a situation with majority voting with no explicit exit option. However, the member states’ negotiation power is not as high as in the case of unanimity voting (Lechner and Ohr 2010, p. 372).

The use of the exit option as a threat in internal EU negotiations has been made by several member states. Threatening to withdraw from the EU in order to obtain concessions from the Union was used as a bargaining tool even before the exit option became a unilateral and legal option with the entry into force of the Lisbon Treaty. Schneider and Cederman argue that the more laggard member states have, typically, used threats to blackmail the enthusiastic
member states (1994, p. 636). Laggard member countries have preferences for less integration than the enthusiastic member states which desire more integration, and the use of threat from the former have had consequences on the European integration process (ibid.). Obstructionist member countries may use three different threats to try to get their will in internal EU negotiations (Schneider and Cederman 1994, p. 637): (i) a threat of full exit from the EU or a threat of partial exit from some areas of cooperation, (ii) a ratification threat by claiming that its constituents will not accept the current suggestion or (iii) a takeover threat by claiming that if it does not get its will a less integration minded opposition will take over office. The other member states may counter any of these threats from a member state with a threat of excluding the respective member country (Schneider and Cederman 1994, p. 637). Britain can, in line with what has been said in section 2.1, be characterized as one of the EU’s laggard member states. We may find several examples of the use of threats by the UK in negotiations with the EU, see a non-exhaustive list under. Other member states have also used threats in their encounters with the EU. For example, De Gaulle threatened to withdraw from the EC in 1965 if the unanimity vote in the European Council was to be removed (Lechner and Ohr 2010, p. 361).

Table 2.2: Examples of the UK’s use of threats as a member state

<table>
<thead>
<tr>
<th>Year</th>
<th>UK’s wish</th>
<th>EU’s wish</th>
<th>Kind of threat</th>
<th>Outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>Renegotiated deal on membership</td>
<td>Acceptance of original terms</td>
<td>Exit / ratification threat</td>
<td>UK got its wish and then held a referendum on EU-membership</td>
</tr>
<tr>
<td>1978</td>
<td>No European Monetary System</td>
<td>European Monetary System</td>
<td>Partial exit</td>
<td>British partial exit from EMS</td>
</tr>
<tr>
<td>1979-84</td>
<td>Renegotiation on Budget</td>
<td>No renegotiation on budget</td>
<td>Full exit</td>
<td>UK budget rebate</td>
</tr>
<tr>
<td>1991</td>
<td>No European social policy</td>
<td>Social policy part of Maastricht</td>
<td>Takeover</td>
<td>UK got partial exit</td>
</tr>
</tbody>
</table>

Source: the table is a revised version of Schneider and Cederman’s table (1994 p. 638)

EU member states’ use of threats in EU negotiations may be effective as long as the other member states prefer a solution which includes the threatening member state over a solution which excludes the member state (Schneider and Cederman 1994, p. 636). Such a situation can be described as a battle of the sexes game. A battle of the sexes game is a game where both players prefer to stay together than to be separated. The game can be used to analyze the unequal distribution of outcomes when both players want to cooperate (Hancké 2017). So as long as the UK was an “ordinary” EU member state, and thus playing a game of sexes with the EU, using threats and making demands worked in the UK’s favor (Hancké 2017).
However, when Article 50 has been triggered and the UK does not prefer to stay together anymore, the game being played is no longer a battle of the sexes game, it is more like a game of chicken. In a chicken game, both players want to avoid the mutually destructive outcome occurring if both play a hard strategy. But both players also benefit the most if it stands firm and the other player yields. Knowing this, both players try to convince the opponent that it will not bend off in order to make the other player yield.

2.3 Negotiating under Article 50

The formal requirements and procedure of withdrawal from the EU is set out in Article 50 of the Lisbon Treaty. The Article has never before been invoked, making the Brexit negotiations the first of its kind. This lack of priors makes the negotiations especially difficult because the parties do not have any experiences to draw upon when making up their expectations and preparing for bargaining. In this section I will address the formal process of Brexit as set out in Article 50. Further, I discuss two of the features of Article 50, the timeline and the ratification procedures, more thoroughly. These two features contribute to making withdrawal negotiations different from other types of negotiations with the EU.
The specific wording of Article 50 is as follows:

(1) Any Member State may decide to withdraw from the European Union in accordance with its own constitutional provisions.

(2) A Member State which decides to withdraw shall notify the European Council of its intentions; the European Council shall examine that notification. In light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State setting out the arrangements of withdrawal taking account of the framework of its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council of Ministers, acting by a qualified majority, after obtaining the consent of the European Parliament.

(3) The Treaties shall cease to apply to the State in question from the date of entry into force of the withdrawal agreement, or failing that, two years after the notification referred to in paragraph 2, unless the European Council, in agreement with the Member State concerned, decides to extend this period.

(4) For the purposes of paragraphs 2 and 3, the member of the European Council or of the Council representing the withdrawing Member State shall not participate in the European Council or the Council discussions or decisions concerning it. A qualified majority shall be defined in accordance with Article 238(3)(b) of the Treaty on the Functioning of the European Union.

(5) If a State which has withdrawn from the Union asks to re-join, its request shall be subject to the procedure referred to in Article 49.

Article 50 defines the EU member states’ unilateral right to exit and specifies the requirements of the withdrawal process from the EU. Some of the features of the negotiations’ set-up affect the course of the negotiations and the players’ room for maneuver. I will briefly elaborate on two of the requirements set out in Article 50, the negotiations’ timeline and the rules for ratification.

Article 50(3) set out a two-year timeline for the withdrawal negotiations from the triggering of the Article, unless the parties unanimously agree to expand this timeline. The UK government invoked Article 50 on March 29 2017 by sending a letter of divorce to the Council’s President, Donald Tusk. The deadline for reaching an agreement is, thus, 29 March 2019. If an agreement is not concluded within two years and no expansion is approved, the UK will leave the EU with no deal.
Furthermore, any deal negotiated between the EU and the UK must be ratified internally by the two parties. According to Article 50(2) the negotiated agreement shall be concluded on behalf of the Union by a qualified majority vote in the European Council, after obtaining consent from the European Parliament. According to Article 238(3)(b) in the Treaty on the Functioning of the European Union (TFEU) shall a qualified majority be defined as at least 72% of the members of the Council that comprise at least 65% of the population of the EU. To obtain consent from the European Parliament the voting rule is simple majority, and the Members of the European Parliament from the UK have a right to vote. The Brexit deal does not need to be ratified by the individual member states of the EU. The UK will ratify the agreement according to its own constitutional arrangements. It has been decided by the British Parliament that any final Brexit deal must be ratified by a vote in the Parliament. This vote will happen after the negotiations are concluded and some time before Brexit day 29 March 2019.

These two features of the negotiations’ set-up affect the parties’ leeway in the negotiations. The negotiations’ timeline gives the parties limited time to reach an agreement and the ratification rules set any negotiated deal up against the option of no deal at the time of ratification. The set-up given by Article 50 also distinguishes EU withdrawal negotiations from other types of negotiations because usually negotiations do not have a strict timeline and the option of no deal normally entails keeping the status quo. The consequence of the negotiations set-up is discussed further in section 6.1. Another characteristic of the Brexit negotiation process, which distinguishes it from other negotiations, is its undefined final destination, which will be discussed more closely in the next section.

2.3.1 The undefined and uncertain nature of exit

The withdrawal process from the EU does not have a clear final destination. The outcome of the exit process will be a result of the negotiations held between the withdrawing member state and the EU. These negotiations consist of both withdrawal issues and the issue of the future framework of the relationship between the EU and the withdrawing state. Since no final destination of withdrawal is specified in Article 50, but is an outcome of the exit-negotiations, a withdrawing member state does not know the result of leaving the EU when making the decision to leave (Nicolaides 2013, p. 210). The withdrawing state does neither know the terms of withdrawal nor the framework of the future relationship to the EU. This
undefined nature of the exit process stands in contrast to the process of entry. Entry into the EU has a clear final destination, EU membership with its respective obligations and rights (Nicolaides 2013, p. 210). Activating Article 50, on the other hand, sends the withdrawing member state out on a journey with no final destination.

In addition to having an undefined final destination, the exit process is unprecedented. Never before has a member country decided to leave the EU. Thus, there are no priors to look to when shaping ones’ expectations about how the exit negotiations will be approached by the EU and by the withdrawing member state, the UK. The unprecedented and undefined character of the exit process from the EU makes the Brexit negotiations a negotiation under extreme uncertainty. This characteristic of the Brexit negotiation will be an important part of the analysis later in this thesis.
3 Theoretical framework

The objective of this chapter is to present and discuss the thesis’ theoretic backdrop. The theoretical contributions have been selected as they contribute to shedding light on the Brexit negotiations in general and my research question in particular. I start by presenting the theoretical framework for evaluating the efficiency of threats and assess the UK’s threat of no deal based on it. Thereafter I will present a theoretical framework for studying power in negotiations and discuss how the weaker actor in asymmetric negotiations can use tactics in order to negotiate a better deal. Finally, I discuss the use of the assumption of unitary actors in formal studies of negotiations and how negotiations can be studied as two-level games.

3.1 Negotiations and the use of threats

Bargaining “occurs in situations where two or more parties are able to reap mutual benefits, provided that they can agree on one of several possible ways of sharing these benefits” (Hovi 1998, p. 57). In the Brexit negotiations the two parties are trying to agree on the terms of withdrawal from the EU and on the framework of the future relationship between the two. If they do, both parties will obtain benefits. But in order to obtain these benefits, they must agree on a way of cooperating. If they don’t the outcome will be no deal, which will cause costs for both parties. Nevertheless, the UK is expected to be hit much harder than the EU of an unorderly Brexit and, thus, suffer higher costs of no deal.

Negotiations have some main characteristics (Hovi 1998, p. 57-58): (i) they include both common interest and conflict, (ii) their decision criterion is agreement, (iii) the principal medium of communication is an explicit exchange of offers and counteroffers, (iv) the official purpose is to reach an agreement, (v) negotiations are costly processes and (vi) they typically involve threats. These characteristics can be found in the ongoing negotiations about the UK’s withdrawal from the EU. The Brexit negotiation involve both common interest and conflict. Both parties can benefit from agreeing on a deal, cooperation is mutually beneficial on several issues, while a no deal outcome would hurt them both. However, the two parties have conflicting interest when it comes to what kind of deal to agree on. Before the start of the negotiations both parties had drawn up several red-lines. To be able to reach a deal, compromise will be necessary, as the decision criterion is agreement. The parties have expressed publicly their intention to strive to find an agreement. In the EU’s negotiation
guidelines of 29 April 2017, it is stated that “The Union will work hard to achieve that outcome [a deal]” (p.1). In her letter triggering Article 50 Theresa May stated that a no deal outcome “is not the outcome that either sides should seek” and “we must therefore work hard to avoid that outcome” (p. 3). Despite the parties’ declarations of good intentions, there is no guarantee that they can find common ground and conclude an agreement. Furthermore, as is the topic of this thesis, the Brexit negotiations involve the use of threats.

The use of threats is quite common in international negotiations, particularly threats of ending the negotiations (Hovi 1998, p. 57). Threats can be used as tools to enhance a player’s bargaining position and, thus, bargaining outcome. Accordingly, I will assume that the UK’s aim with the no deal threat is to coerce the EU to make concessions in the negotiations in fear of a no deal outcome. If the threat proves efficient, it will make the EU give in on some demands and, thus, give the UK a better deal. However, it is not possible to be sure of the intention behind a negotiating part’s tactics from observation. Only the UK’s bargaining team know which intention they had and have when using a specific bargaining tactic, such as the threat of no deal. Furthermore, the threat of no deal can also be interpreted as a threat aimed at the domestic audience and a part of the internal game taking place between actors in the UK. This interpretation of the threat and the UK’s domestic level will be discussed in section 6.5, while for the main part of the analysis the threat will be assessed as a threat operating at the international level in the game being played between the EU and the UK.

3.2 Threat theory – how to effectively threaten

A threat can be defined as a “contingent assertion signaling to hurt somebody […] unless that somebody acts in a way prescribed by the threatener” (Hovi 1998, p. 11). Thus, a threat is a conditional commitment and will only be put into effect if the target does not change its behavior to comply with the threat (Hovi 1998, p. 13). A threat is distinct from a warning. In the case of a threat the harm will be inflicted by the threatener, while in the case of a warning, it is caused by a third party or nature (Hovi 1998, p. 12). A threat can be defined as effective if it causes the target to change its behavior in accordance with the threatener’s desires (Hovi 1998, p. 13). Hovi identifies five conditions for a threat to be effective in this sense (Hovi 1998, p. 13-16):

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7 The effectiveness of a threat depends on the threatener’s goal with the threat, which can be several things, but usually to change the targets behavior in a certain way.
(i) The threat must be relevant, meaning that it can have an impact on the outcome. This requires, firstly, that the target has some freedom of action and is able to change its policy in the direction wanted by the threatener. Secondly, the target must have incentives to act contrary to the threatener’s wishes to begin with. If these two requirements are not fulfilled, a threat will either not succeed, if no freedom of action, or be needless, if no incentive to act contrary to the threat.

(ii) The threat must be sufficiently severe to be efficient. In other words, the target must prefer to comply with the threat rather than to have it effectuated. A target’s evaluation of a threat’s severity depends on the threat’s magnitude, it must be more costly not to comply than to comply, but also on its character. A threat which is severe, might still be inefficient if the demand is in conflict with the target’s vital interests.

(iii) To be efficient, a threat also needs to be credible. A threat is credible if the target believes that the threat will be put into effect if it does not comply with it. A threat’s credibility can be evaluated as a function of the threatener’s preferences. If it is rational for the threatener to carry out the threat in case of non-compliance, then it is credible. In a game with complete information, all players know the preferences and capabilities of the other players and, thus, whether or not a threat will be effectuated. However, in a game of incomplete information the players are uncertain about the other players’ payoffs and capabilities, and thus of the credibility of a threat.

(iv) A threat must be complete, meaning that the threat is accompanied by an assurance that the threat will not be put into effect if the target complies. Hence, the target must believe that if it complies with the threat, it will not be carried out.

(v) A threat must be clear, to be effective. To be clear, a threat must make the target understand what the threatener wants and what the consequences of non-compliance are. If the target understands this, then its behavior can be understood as a consequence of the issued threat.

3.2.1 The no deal threat assessed – can it be efficient?

In this section I will assess the UK’s threat of no deal in light of the five criteria for efficiency listed above: relevance, completeness, clearness, severity and credibility.
Relevance: For the UK’s threat to be relevant, the EU must have some freedom of action to change its behavior and incentive to act contrary to the UK’s demands. First, the EU does have the possibility of changing its negotiation position and give concessions to the UK, if it wants to do so. However, the EU’s common negotiation position cannot easily be changed. To make changes to the EU’s negotiation position, a decision in the Council would be need. Hence, the EU does have freedom of action, but as the EU is composed of 27 member states and supranational institutions, its freedom of action is cumbersome. The nature of the delegation of negotiation mandate by the member states to their negotiation agent can, and has been, used strategically by the EU in the negotiations. As Schelling argues “the power of a negotiator often rests on a manifest inability to make concessions and to meet demands” (sited in Meunier 2000, p. 106). Michel Barnier has stated several times during the negotiations first phase that he cannot give the UK concessions nor move to second phase because he does not have a mandate to do so, to get that mandate a new Council adoption would be necessary. That would be time consuming, and time is not something the UK has much of in the Brexit negotiations. Second, the EU also has incentives to act contrary to the UK’s desires to begin with. Both actors want to negotiate the best possible deal and, in order to do so, stick to its negotiation position and not make concession to the other part. So, by threatening to end the negotiations if the EU does not give them a “good deal”, the UK is trying to make the EU act contrary to its initial incentives.

Completeness and clearness: In order to be complete, the UK’s threat must make the EU believe that the threat is contingent on its behavior. Hence, if the EU complies with the UK’s threat, and gives the UK some concessions, the UK will not end the negotiations. It seems reasonable to believe that the UK’s threat is contingent, and that if it gets what it considers as sufficient concessions, it will not leave the negotiation. This because the UK would not get any benefits from the concession made by the EU if it were to leave the negotiations, since they only come into effect if there is a deal. When it comes to what the UK considers as sufficient concessions and a “good deal”, there is considerable uncertainty. Consequently, the UK’s threat of “no deal is better than a bad deal” does not appear to be crystal clear. The threat can be considered clear if the EU understands what the UK wants and what it must do to avoid the threat to be effectuated. The UK’s negotiation position can be characterized as ambiguous and divided. One common negotiation position does not exist within government,

8 See for example Meunier 2000 and Hovi 1998 for discussions on the use of internal constraints as leverage in negotiations.
nor within the two big parties. I will discuss the domestic divisions on Brexit within the UK further in the section 6.1 and 6.5.

Severity: To be sufficiently severe, the no deal threat must make the EU prefer to comply with the threat rather than to have it effectuated. In other words, the EU must prefer a deal somewhat beneficial to the UK over no deal. The no deal scenario will imply costs to the EU, but so will making concession to the UK. The EU will have to evaluate these costs against each other, and for the threat to be sufficiently severe the costs of no deal must be considered superior to the cost of concluding a deal which is beneficial to the UK. The costs and benefits attached to the different possible outcomes of Brexit are of both political and economic character. They also have different time horizons, some costs and benefits are short-term while others are more long-term. The different costs attached to the possible outcomes of Brexit will be discussed further in section 4.4 and 5.2.

Furthermore, the character of the UK’s threat may make it ineffective because it has a bearing on the EU’s vital interests. The EU’s main goal is to secure the Union’s interests and, ultimately, its survival. Yielding to the UK’s threat might put the Union’s future and survival into danger if Brexit leads to a domino effect. The Brexit negotiations can be seen as a reputation game where the EU has a long-term interest of playing a hard strategy to gain reputation effects. If the EU yields to the UK’s threat and gives beneficial concessions, this sets a precedence for other member states. If exit is perceived as more beneficial than staying a member state, more members may want to withdraw from the Union. To avoid this, the EU has incentives to play hard and not give in to the UK’s threat. Additionally, a beneficial deal to the UK may cause another domino effect in terms of third countries wanting to renegotiate their deal with the EU in light of the new agreement between the EU and the UK.

Credibility: For the threat to be credible the EU must believe that the UK actually will carry out the threat and leave the negotiations if the EU does not make any concessions. The threat’s credibility is a function of the UK’s evaluation of the costs and benefits of the different outcome scenarios. For the threat to be credible, the UK must consider the benefits of no deal to be higher than the payoffs of a “bad deal”. In a game of complete information, the target can evaluate a threat’s credibility by looking at the preference ordering of the threatener. However, in a game of incomplete information, the players’ preference orderings

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9 See reputation literature for further explorations of similar arguments, for example Selten 1978, Kreps and Wilson 1982, Milgrom and Roberts 1982.
are not common knowledge and the threat’s credibility is up for assessment. In a non-cooperative game, threats and promises are not inherently credible and only credible threats can make a difference to the outcome (Hovi 1998, p. 4). In this environment of uncertainty, the players have incentive to misrepresent their actual preferences and capabilities to try to obtain a better deal. A threatener may try to increase the credibility of a threat through various strategic moves, the next section gives an overview (Hovi 1998, p. 31).

3.2.2 Strategies to make a threat credible

To increase the credibility of a threat a threatener can make it (i) impossible not to carry out the threat or (ii) make it costly to not carry out the threat (Hovi 1998, p. 61). The former is often very hard to do. In the context of a negotiation it may be done by providing the bargaining agent with fixed instructions that cannot be changed (Hovi 1998, p. 61-62). Alternatively, one might adopt a strict decision rule for ratification of the agreement which makes it impossible to agree a deal that do not comply to the issued threat (ibid.). Making it impossible not to impose the threat if the target does not comply, creates an ultimatum game, a take it or leave it negotiations. This is often neither possible nor rational to do for a negotiating party.

Making it rational to impose the threat if the target does not comply may also be hard and costly, but is often easier than making it impossible. In order to make it rational to carry out a threat, and thus increase the threats credibility, a threatener may change its payoff structure. This can be done by identifying outside options, making it less painful to carry out the threat and showing patience (Hovi 1998, p. 64-68, Muthoo 2000). Outside options are alternatives to striking a deal with the opponent in the ongoing negotiation (Hovi 1998, p. 64, Muthoo 2000). In other words, it is the options a player has external to the present negotiation (Hovi 1998, p. 64). If a player is able to demonstrate that it has alternatives to the possible deal in the ongoing negotiation, this may increase the credibility of the threat. But, as stresses by Muthoo, for outside options to increase the credibility of the threat to leave the negotiations, they must be sufficiently attractive (2000, p. 155). The outside option principle says that outside options only increase the credibility of a threat if the outside options are more attractive than what can be achieved in the ongoing negotiations (ibid.). In the Brexit negotiations it is somewhat diffuse what the actors’ outside options are and what terms of
agreement it would be equivalent to. The UK’s outside options will be discussed further in section 6.3.4.

A threatener can also increase a threat’s credibility by making it less painful to carry out the threat (Hovi 1998, p. 65). The credibility of a threat to end the negotiations would increase if the threatener can demonstrate that a no deal outcome would not be so costly. This can be done by identifying attractive outside option, but also by taking other kinds of measures to avoid the potential costs of no deal. In the Brexit negotiations preparing for a potential breakdown of the negotiations in different ways would increase the credibility of the UK’s no deal threat. The cost of no deal for the UK will be further discussed in section 5.2 and 6.5.

Showing patience is a third way to increase the credibility of a threat, because it shows willingness to incur costs in order to make the target comply with the threat and obtain its preferred outcome of the negotiations (Hovi 1998, p. 66). However, showing patience is not an available strategy in the Brexit negotiations in the same way as in other types of negotiations due to the Article 50 negotiations’ timeframe (see section 2.3). The capability to show patience, together with the existence of outside options and the cost of no deal, affect the ability of the parties to a negotiation to credibly commit to threats. Furthermore, actors’ ability to credibly threaten also depends on their bargaining power. In the next section I will have a closer look at the concept of power in negotiations.

3.3 Power, negotiations and tactics

The goal of much of the literature on negotiations is to predict or explain the outcome of the negotiations. When trying to do that, the concept of power is important. The assumption in much of the literature is that the outcome of a negotiation is a function of, among other, each side’s power. However, in order to be used to analyze negotiations and explain outcomes, the concept of power must be sufficiently comprehensive (Habeeb 1988, p. 13). Habeeb presents a framework for analyzing power in negotiations as a three-dimensional concept: aggregate structural power, issue-specific structural power and behavioral power (1988, p. 17-25). This framework is especially useful when looking at negotiations where the power resources and capabilities of the two actors are asymmetric, as is the case in the Brexit negotiations.

An actor’s aggregate structural power is defined by the actor’s total resources and capabilities relative to the other actors in the world (Habeeb 1988, p. 17). Aggregate structural power in
useful to describe the actor’s position in the international system and define the components of its resources that can be used in negotiation tactics (ibid., p. 18). It can be measured, to some extent, in terms of material resources, population and territory (Habeeb 1988, p. 18). The structural power balance between the EU and the UK in the Brexit negotiations is in the EU’s favor. In terms of aggregate resources, population and territory the EU27 is far more powerful than the UK.

Issue-specific structural power is concerned with the actors’ resources and capabilities within the context of a specific issue or relationship (Habeeb 1988, p. 19). The actors’ issue-specific power is determined by their alternatives, commitments and control (ibid., p. 21). If an actor is able to achieve its goals through alternatives that do not involve the current opposing negotiating actor, this may “increase an actor’s issue power by decreasing its dependence on the other actor” (Habeeb 1988, p. 21). This is in line with the discussion about outside options above in section 3.2.2.

An actor’s commitment refers to the extent to which an actor desires or needs its preferred outcome and to the values that it attaches to different outcomes (ibid., p. 21). If based on ambition and aspiration, commitment may increase issue power, but if based on need, issue power may be decreased (Habeeb 1988, p. 23). This distinction may be hard to make in real cases, such as the Brexit negotiations, but assessing the players’ commitments may give meaningful insights. The EU’s commitment in the Brexit negotiations is based on values of protecting the Union and the integrity of the Single Market. While the UK’s commitment is based on values of sovereignty and control, as well as access to the EU’s Single Market. Overall, one might describe the UK’s commitment to be more based on need than the EU’s commitment, due to the asymmetric interdependency of the two actors.

Thirdly, an actor’s control depends on its ability to unilaterally achieve its preferred outcome (Habeeb, p. 22). In negotiations, outcomes are not unilateral, but an actor’s control depends on its ability to gain a relative greater share of its preferred outcomes than the other actor on its own (Habeeb, p. 22). In the Brexit negotiations the EU is not dependent on the UK to protect its vital interest: the survival of the Union and the integrity of the Single Market. The UK can achieve increased sovereignty on its own but relies on the EU for access to the Single Market. Due to its relative stronger dependence on the EU to reach its goals, the UK seem to have less control than the EU.
The issue-specific power balance determines the players’ relative dependence on each other (Habeeb 1988, p. 22). The relationship between the UK and the EU in the Brexit negotiations is one of interdependence, both actors are dependent on each other to the extent that both can withhold agreement or end the negotiation process. A relationship of interdependence entails that both sides would incur costs if the relationship, or negotiation, was ended (Habeeb 1988, p. 19). However, this interdependence may be asymmetric. In the relationship between the UK and the EU, the former will, according to evaluations of the consequences of Brexit, incur higher costs than the latter if there is no deal. Being the less dependent actor in the Brexit negotiations, gives the EU a beneficial negotiation position.

Behavioral power is defined as an actor’s ability to use its aggregate and issue-specific structural power resources to achieve preferred outcomes (Habeeb 1988, p. 23). Behavioral power is in many ways the power of the weaker actor in a negotiation, as negotiation tactics can, if efficient, help the weaker part to negotiate a better deal. In order to succeed, tactics must alter the issue power balance by modifying each side’s alternatives, commitment or control (Habeeb 1988, p. 24). Near all negotiation tactics are means to increase an actor’s alternatives, its commitment to its preferred outcome or the degree to which it can reach an outcome unilaterally (Habeeb 1988, p. 24). The UK’s threat of no deal can be seen as a negotiation tactic in order to increase its issue power. By threatening that it prefers a no deal outcome over a bad deal, the UK is trying to communicate that it has alternatives that are better than a bad deal with the EU. The threat also tries to communicate the UK’s commitment to negotiating a good deal for itself by excluding the alternative of a bad deal with the EU. For the UK’s no deal threat to coerce the EU to make some concessions it must change the initial issue-power balance between the two players. The UK’s threat can do so by convincing the EU that it has alternatives to a deal with the EU and that it is committed to its negotiation stance. This thesis seeks to answer the question of under what conditions the no deal threat enables the UK to coerce the EU to make concessions. When doing so it is with this framework of power as a backdrop.
3.4 Unitary actors versus two-level games

In the literature that uses formal models to study negotiations, it is often assumed that the actors are unitary. This is also the case in the game theoretic model used in this thesis. The assumption entails that states, organizations or other entities are interpreted as actors with one utility function and one set of preferences. The unitary actors assumption is often a necessary assumption in order to model negotiations formally. However, the assumption of unitary actors is far from the reality in most negotiations. In the Brexit negotiations, both the UK and the EU are complex actors with more than one set of preferences. In the UK there are several domestic actors, nations and regions with different preferences concerning the outcome of the negotiations. Similarly, the EU consist of 27 member countries and different EU institutions which all have their own distinct set of preferences. This complex composition of actors at different levels makes analysis difficult. By applying the assumption of unitary actors, it makes formal analysis possible by simplifying. It also makes the analysis about the game being played between the EU and the UK at the international level, and not about the game being played internally within the two actors.

Nevertheless, since the assumption of unitary actors rarely reflects the reality in international negotiations, it can be useful to study negotiations as two-level games. Putnam presents an analytic framework to study international negotiations where negotiations take place both within and between the parties to the negotiation in two-level games (Putnam 1998). This allows for domestic division and conflict about what “the nation’s interest” requires (Putnam 1988, p. 460). To entangle domestic politics with international negotiations analytically, Putnam breaks the negotiation process down into a negotiation phase (level 1) and a ratification phase (level 2) (Putnam 1988, p. 436). At the first level the bargaining between negotiators from each side takes place, while at the second level the internal discussion about whether or not to ratify the agreement takes place (Putnam 1988, p. 436). If the parties to the negotiation are states, the first level is the international level and the second level is the national level. The requirement that any agreement reached at level 1 must be ratified at level 2 imposes a theoretical link between the two levels (Putnam 1988, p. 436). The negotiation, thus, become constrained by both what the opponents will accept at level 1, and also by what can be ratified at level 2 (Moravcsik 1993, p. 4). The negotiations at level 1 is affected by the players’ win-sets, the set of deals that would be accepted domestically (Putnam 1988, p. 437). Win-sets are important, argues Putnam, both because larger win-sets make level 1 agreement
more likely and because the relative size of the actors’ respective win-sets will affect the
distribution of gains (Putnam 1988, p. 437-441).

The Brexit negotiations can be analyzed as a two-level game as the final deal reached at level 1 must be ratified at the actors’ respective level 2. On the British side, the deal must be ratified by a vote in Parliament. While on the EU-side any deal must first be approved by the European Parliament, then voted on in the European Council. Final ratification of a Brexit deal at level 2 is simply a vote in favor or against the deal negotiated at the international level, there is no room for making modifications unless these are approved by all parties, this is in line with Putnam’s framework (Putnam 1988, p. 437). Thus, in the ratification phase, the national decision makers have a choice between the negotiated deal presented and the option of no deal (ibid.). Usually, the option of no deal corresponds to the status quo, but this is not the case in the Brexit negotiations.

Neither the EU nor the UK are unitary actors. However, both parties are negotiating as if they were unitary actors. In the UK’s letter to the EU triggering Article 50 it is stated: “From the start and throughout the discussions, we will negotiate as one United Kingdom, taking due account of the specific interest of every nation and region of the UK as we do so” (UK government). The same intention to act as a unitary actor is found in the EU’s guidelines for the negotiations from March 29 2017: “Throughout these negotiations the Union will maintain its unity and act as one […]” (EU Council, p. 1). The EU’s member states have put down a great deal of work to ensure that the Union will negotiate as one actor by coordinating their preferences in internal negotiations in the European Council and also in the General Affairs Council (GAC). The EU’s guidelines also exclude the possibility for the member states to engage in separate negotiations with the UK. At the negotiation table the two sides are represented by their respective chief negotiators, David Davis (UK) and Michel Barnier (EU). I will assume that the UK and the EU are unitary actors in the game theoretic analysis about the threat’s efficiency in chapter 5 and 6. However, in order to corroborate the findings done in this analysis I will use two-level game considerations as an analytical robustness test of the analysis on the first level (see section 6.5).

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10 The EU’s second level is more complicated as it consists of several levels. But since a Brexit deal only has to be ratified by the Council and the EP, and not by national parliaments, it makes sense to treat the EU as a two-level entity in this context.
4 Goals, strategies and outcomes

The objective of this chapter is to introduce the main actors in the Brexit negotiations, the UK and the EU, their preferences, the strategies available to them and the possible outcomes of the negotiations. These elements are fundamental in any game theoretic model, which may be defined by five elements: a set of players, a set of strategies, a set of possible outcomes, the players’ payoffs at each of the possible outcomes and other rules of the game, such as information assumptions and the sequence of moves (Hovi 1998, p. 3-4). Together the components of a game theoretic model presented in this chapter serve as the fundament for the game theoretic analysis in chapter 5 and 6.

4.1 The players

The players in the game theoretic analysis of the Brexit negotiations are the UK and the EU, who are assumed to be unitary actors. Thus, both are assumed to have one set of preferences and common policy positions. This assumption permits me to answer my research question as the assumption puts the analytical focus on the game taking place between and not within the two main actors. However, the assumption about unitary actors does not reflected the full reality of the negotiations. When discussing the players’ policy positions in this chapter I will take into account the main internal divisions within the two players.

4.2 The players’ policy positions

In this section I will have a closer look at the parties’ interest and policy positions in the Brexit negotiations. The two parties have, both before the start of the negotiations and during the talks, made their policy positions available through public negotiation papers. The most central documents concerning the EU’s position are the negotiation guidelines adopted by the European Council on 29 April 2017 and the negotiations directives of 22 May 2017. In addition, the EU has published position papers on specific issues as the negotiations have proceeded. The British government’s objectives for the Brexit negotiations and for their future relationship with the EU were set out in Theresa May’s Lancaster House speech of 17 January 2017 and the subsequent White Paper published on 2 February. Furthermore, Theresa May’s Florence Speech from October 2017 is also of importance. Through their policy
position, the players express their preferences which play a central role in the analysis of the game theoretic model in chapter 5 and 6.

4.2.1 EU’s overall positions and goals

The EU’s guidelines of 29 April 2017 for the Brexit negotiations state that: “[…] the Union’s overall objective in these negotiations will be to preserve its interests, those of its citizens, its businesses and its Member States” (p. 1). In order to reach this overall objective, the guidelines further set out the general positions and principles which the EU will pursue throughout the negotiations. The EU iterates in its guidelines the wish to continue to have the UK as a close partner in the forthcoming and that the future ties should encompass more than just trade (p. 3). A close future relationship is of interest to the EU and will derive both economic and political benefits. However, the EU puts some constraints on the shape of the future relationship by setting out some core principles which apply to any agreement with the UK:

**Balance of rights and obligations:** The principle of balance of rights and obligations is central to the EU in the Brexit negotiation. In the guidelines it is stated: “A non-member of the Union, that does not live up to the same obligations as a member, cannot have the same rights and enjoy the same benefits as a member” (p. 1). In other words, non-membership cannot be better or more attractive than membership.

**No cherry-picking:** The EU is, furthermore, clear about its position concerning the indivisible character of the Single Market. To secure the integrity of the Single Market, the EU excludes the possibility of participation in the Single Market based on a sector-by-sector approach. Hence, there can be no “cherry picking” of the four freedoms.

These two interlinked principals are meant to protect the vital interest of the EU, the survival and prosperity of the Union. The Brexit negotiations’ unprecedented character makes Brexit an especially important case which will state an example and have reputational effects. Giving in to some of the UK’s demands could possibly be beneficial in a short-term perspective, but the long-term cost could possibly be great. Thus, the EU faces a trade-off between short-term and long-term costs and benefits.
4.2.2 The UK’s overall position and goals

Prime Minister Theresa May stated in her Lancaster House speech on 17 January 2017 that the UK’s objectives for the negotiations amount to one big goal: “a new, positive and constructive partnership between Britain and the European Union”. This overall goal involves leaving the EU as a member state and agreeing a deal that sets out the future framework for the relationship between the two. The UK’s negotiation objectives, as the EU’s, put some constraints on how a deal on the future relation can be. The UK’s main negotiation objectives are as follows.

**Taking back control of own laws:** The British government wants to take back control over own laws, and to no longer be bound by the jurisdiction of the European Court of Justice (ECJ). As May stated in her Lancaster House speech: “We will not have truly left the European Union if we are not in control of our own laws”.

**Taking back control of immigration:** The British government wants to be able to control the immigration to the UK from the EU and stop the free movement of EU-nationals to the country. Participation in the EU’s Single Market involves the free movement of “the four freedoms”, in which labor is one. The issue of immigration was one of the main issues in the debate before the referendum, as the issue is of grand public concern. Immigration was also emphasized by May in the Lancaster House speech: “[…] The message from the public before and during the referendum campaign was clear: Brexit must mean control of the number of people who come to Britain from Europe. And that is what we will deliver.”

**Ensure free trade with the European market:** As the EU has stressed their “no cherry picking” policy, the UK has stated that it does not seek membership of the Single Market, but a bespoke trade-deal. The UK government seeks to conclude an “ambitious” free-trade agreement and a new customs agreement. The UK does not want membership of the Single Market due to the free movement of people that membership entails and, also, to avoid paying financial contributions to the EU budget, as it would be required to do as a member of the Single Market.

**Free-trade with third countries:** The UK is not only interested in free trade with the EU, but also with third-countries. As a member of the EU, the UK is prevented from agreeing its own trade-deals with non-EU countries. The UK government wants to be able to strike free trade agreements with other countries as they like. As stated by May in the Lancaster House
Speech: “A Global Britain must be free to strike trade agreements with countries from outside the European Union too”.

The two “taking back control”-goals are in large political goals concerning sovereignty, while the two trade related goals are of an economic character. There exists a trade-off between these two genres of goals for the UK. According to the EU, the UK cannot “have its cake and eat it too”, meaning that the UK has to make a choice between these two types of goals which cannot be reconciled. The EU’s policy positions exclude the option of a Europe à la carte where the UK can pick and choose the parts of EU membership that it likes and reject the parts that it does not like. Wincott calls this trade-off the “Brexit-dilemma”: a dilemma between retaining access to EU markets, on one side, and gaining control of immigration while limiting EU’s authority over the UK, on the other (Wincott 2017, p. 681). The British public opinion wants both, there are majorities for both reducing immigration and for extensive access to EU markets (ibid.). However, there is an internal division in the UK between those who emphasize the former goal in the “Brexit dilemma” over the latter, and those who emphasizes the latter over the former. The “Brexit supporters” put more importance on regaining sovereignty over immigration and laws and, thus, want a hard Brexit. While “Remainers” or “soft-Brexit supporters” prioritize economic growth over sovereignty issues and want to ensure continued access to the EU-market for the UK.

These two groups face their distinct dilemmas. The “Brexit supporters’ dilemma” relate to sustaining economic growth while restricting immigration (Wincott 2017, p. 681). The opposing side who wants a soft form of Brexit faces a dilemma of assuring access to the Single Market, while protecting the UK’s democratic institutions and parliamentary sovereignty (Wincott 2017, p. 682). These internal divisions in the UK over the importance of the different issues in the negotiations has made it hard for the UK government to take a firm negotiation position. The importance attributed to the issues of economic growth and sovereignty by the UK governemnt will be decisive for the outcome of the negotiations.

4.3 Strategies and possible outcomes

In order to reach their respective policy goals, the players may use different strategies. The combination of the two players’ chosen strategies will determine the outcome of the game. Thus, what outcome the UK and the EU will take from the negotiations depends jointly on
both actors’ negotiation strategy. What strategy they choose to play depends on their preferences and the expected output from playing the different strategies.

4.3.1 Strategies

A strategy is a “plan which prescribes an action for any situation where the relevant player can make a decision” (Hovi 1998, p. 3). The literature has distinguished several classifications of strategies: integrative versus distributive, value-claiming versus value-creating, arguing versus bargaining (see Dür and Mateo 2010b, p. 682 for an overview). All of these classifications are ideal types and a negotiating part may combine different tactics that belong to different ideal types (ibid.). Rather than to be based on one of these typologies, I will do as Dür and Mateo (2010b) and perceive negotiating strategies as varying on a continuum between the two ideal-types of “hard bargaining” and “soft bargaining”. But in order to avoid confusion between type of negotiation strategy and type of desired Brexit, I will call the strategies tough and weak bargaining. A tough negotiating strategy is characterized by conflictual and aggressive tactics, while a weak strategy by friendly and cooperative ones (Dür and Mateo 2010a, p. 561). More specifically, tough strategies entail tactics such as taking an explicit stance on the beginning of the negotiations, making commitments not to compromise, criticizing the other side and using threats (Dür and Mateo 2010b, p. 683). Weak strategies involve signalling flexibility, making concessions and compromises in order to find agreement (ibid.). In the game theoretic model in the next chapter, the two players’ choice of strategy is limited to the choice between a tough and a week strategy.

4.3.2 Possible outcomes

An outcome is a possible end state of the game and is described by the actions that are needed to reach that specific end state (Hovi 1998, p. 3). The outcome of one player’s choice of strategy depends on the other player’s choice of strategy. The possible combination of the players’ two strategies, tough and weak, produce four different outcomes.
4.3 Game matrix: Two strategies and four possible outcomes

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<thead>
<tr>
<th></th>
<th>Weak</th>
<th>Tough</th>
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<tbody>
<tr>
<td>Weak</td>
<td>Moderate deal</td>
<td>Bad deal for UK</td>
</tr>
<tr>
<td></td>
<td>(4)</td>
<td>(3)</td>
</tr>
<tr>
<td>Tough</td>
<td>Bad deal for EU</td>
<td>No deal</td>
</tr>
<tr>
<td></td>
<td>(2)</td>
<td>(1)</td>
</tr>
</tbody>
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1: Both players play a tough strategy: If both the UK and the EU play a tough strategy this will lead to a no deal outcome. A no deal outcome imply that the UK will leave the EU on the 29 March 2019 with no deal. This “clean break” entails no deal on the withdrawal issues nor on the transition period or the framework of the future relationship. A no deal outcome would give an unorderly exit of the UK from the EU.

2: The UK plays a tough strategy, while the EU plays a weak strategy: This combination of strategies will produce an outcome which is beneficial to the UK. The EU will give the UK some concessions and maybe break some of its initial red-lines. The UK will stand firm on its red-lines and give very few or no concessions to the EU. The outcome will be a bespoke deal which will facilitate a deep and special relationship between the EU and the UK.

3: The EU plays a tough strategy, while the UK plays a weak strategy: In this scenario, the outcome will be a deal beneficial for the EU. The UK must give concessions to get a deal with the EU who stand firm on most or all of its demands. In this case it is natural to think that the EU wants the relationship with UK to fit with already existing models of affiliation for countries outside the EU, a so called “off the shelf” deal. If so, there are different models to choose from, such as the Norway-model, the Swiss-model or the Canada-model.

4: Both players play a weak strategy: This combination of the players’ strategies will lead to an outcome of a moderate deal for both parties. Both the EU and the UK make compromises and give concessions.

A fifth possible outcome, which seems very unlikely, is the outcome of an “incredible U-turn”. That the UK turn around, and do not leave the EU after all. This outcome seems unlikely because it would not respect the result of the referendum, and, thus, not the “will of
the people”. One may argue that the Brexit referendum does not reflect the will of the people on the EU-question, but that it rather mirrors the opinion’s discontent with the state of affairs. However, not respecting the referendum result seems politically impossible and may cause further political divisions and conflict in Britain. If the decision to leave is reversed, it would deepen political disillusion and hostility towards the “Westminster elite” (Wincott 2017, p. 682). Furthermore, there are no evidence that the public opinion has changed considerably on its view on Brexit. Data show that the public opinion is largely split in half over whether it was wrong or right to vote to leave the EU (YouGov). After the referendum and up until March 2017 there was a small majority that thought that the UK was right to vote Leave, after this there has been a small trend in the public becoming slightly more negative about the choice of Brexit (ibid.). But this small shift of opinion can hardly be used to argue that the British public has changed its mind over Brexit. Additionally, the EU has remained silent on whether or not it would be possible to deactivate Article 50 once it has been triggered. This outcome, that the UK will not leave the EU after all, is not an outcome in the two-strategy and two-player matrix above and will neither be included in the game theoretic analysis in chapter 5 and 6.

4.4 Costs and benefits of EU membership versus non-membership

The costs and benefits of leaving the EU for the withdrawing member state and for the EU depend on the result of the exit negotiation. Withdrawal negotiations may lead to a no deal outcome or a deal which can be more or less beneficial to one of the players. In this section I will assess the costs and benefits of EU membership and different types of non-membership.

4.4.1 Cost and benefits of EU-membership

EU membership involves both costs and benefits to the member countries. These costs and benefits are of political as well as economic character, and they are state-specific according to the respective member-state’s terms of membership (Lechner and Ohr 2010, p. 359). The EU can be perceived as an entity which provides its member states with club goods (Ahrens et al. 2003, p. 419). Club goods are non-rival in consumption, but excludable (ibid.). The EU provides several goods to its member states, some of them comprise all EU members, some only a sub-group of EU members and other some or all EU members as well as non-members
(Ahrens et al. 2003, p. 419). A member state’s costs and benefits from EU membership depends on its participation in different EU-goods. Generally, the costs and benefits of EU membership can be defined, amongst other, by the following elements (Lechner and Ohr 2010, p. 359-360, Ahrens et al. 2003, p. 421-424):

(i) The European Single Market: Benefits of participation in the internal market relate to the possibility of unrestricted trade of goods and services and the free mobility of capital and labor. Participation in the Single Market also incur costs in form of organization, coordination and adjustment costs. Furthermore, participation in the Single Market, and its four freedoms, may cause economic and political costs to member states in terms of not being able to restrict intra-EU immigration and not having a (formal) sovereign economic policy.

(ii) The Monetary Union: Provides economic benefits by reducing transaction costs in trade and capital movements and by omitting exchange rate risks. But also involve cost by restricting the members possibility of a sovereign and autonomous monetary and exchange rate policy based on its specific preferences. The UK does not take part in the Euro-cooperation, and thus these benefits and costs do not apply directly to the UK.

(iii) Regional and structural policy: some member countries receive financial support from the EU with the goal of reducing regional income differences. It is possible to distinguish between net-contributors to and net-receivers of money over the EU-budget, and the benefits and costs of the regional and structural policy for member countries depend largely on whether it is a net-receiver or net-contributor. Furthermore, the reduction of income differences in the EU is good in itself, and it may also give the member countries further benefits by causing other positive effects such as augmented demand.

(iv) The Common Agricultural Policy (CAP): gives benefit to member countries in terms of securing the supply of agricultural goods in the EU and by stabilization of the agricultural markets within the EU area. The cost of the CAP involves high prices for consumers, and different costs on member countries depending on whether they are net-contributors or net-receivers of EU funds.

(v) The EU trade policy towards third countries: EU membership gives a stronger bargaining position and, thus, benefits due to the possibility to negotiate good trade deals with third countries. However, EU member states lose their possibility of an autonomous foreign trade policy and the possibility of striking its own free-trade agreements.
(vi) Benefits that are inherent in EU membership: Benefits caused by being a part of the integration process and taking part in the decision-making process, as well as benefits from the Union’s protection. These benefits are only fully accessible to EU members.

When a member state leaves the EU, the costs of membership become benefits of leaving and the benefits of membership become costs of leaving. However, the costs and benefits attached to non-membership depends on the result of the withdrawal negotiations. In the Brexit referendum voters had to choose between EU membership and exiting the Union, thus the cost-benefit calculation was between those two options. This choice of membership versus non-membership did not include any pointers on what kind of non-membership a withdrawal would entail. In the Brexit negotiations, the cost-benefit analysis involves comparing the different possible outcomes.

4.4.2 Costs and benefits of non-membership

The UK has decided to leave the EU and has triggered Article 50. Hence, the country is not comparing the costs and benefits of membership with non-membership, but rather the different forms of non-membership and the option of no deal with each other. The costs and benefits of leaving the EU depend on the withdrawal deal the UK negotiates with the EU and the costs and benefits derived from an independent position as a non-member (Lechner and Ohr 2010, p. 359). The same goes for the EU, the different possible outcomes of the exit negotiations impose different costs and benefits on the Union. However, some elements that may define the potential benefits of non-membership for states are (Lechner and Ohr 2010, p. 359-360):

(i) Benefits of autonomous use of state revenues and not having to contribute to the EU-budget.

(ii) Benefits of an autonomous foreign trade policy as non-membership gives the state the possibility of concluding free trade agreements with third-countries as it like.

(iii) Benefits of an independent economic and monetary policy.

In addition to the three potential benefits listed above, non-membership may give political benefits in terms of regained sovereignty over immigration and laws. To which degree these
potential benefits come into effect for a withdrawing member state depends on the result of the negotiations and the form of the state’s future affiliation to the EU.

Moreover, uncertainties exist about the consequences and payoffs of the different outcomes of the Brexit negotiations. There are no priors to Brexit, never before has a member state withdrawn from the EU. Experiences shape beliefs, but in the Brexit case there are no experiences to draw on for the actors. This extreme uncertainty opens up for different perceptions and beliefs concerning the benefits and costs of leaving the EU since the actual payoffs are obscured by uncertainty.

4.4.3 Different perceptions of the costs of leaving the EU

Different actors evaluate the implications of the possible outcomes of Brexit differently. Accordingly, there is disagreement about the costs and benefits connected to the different forms of non-membership within the UK. A main distinction can be made between the Brexiteers and the Remainers. In the referendum debate, the Brexiteers evaluated non-membership as more beneficial than membership, while the Remainers did the opposite. In the Brexit negotiations, different forms of non-membership are held up against each other for comparison, and these two groups also evaluate the different possible outcomes differently.

The issue of economic costs was essential in the referendum campaign and is now essential in the Brexit negotiations. During the referendum campaign both the leave and the remain side used arguments of economic costs. The leave side argued that withdrawal would be economically beneficial by ending the UK’s required contributions to the EU budget and by ending the economic costs produced by EU-immigration to the UK. The leave side famously claimed that Brexit would give the UK additionally £350 million a week to spend on the National Health Service.11 On the other side, the remain campaign argued that exit from the EU would entail large costs in terms of, among other, losing access to the EU-market and by creating uncertainty for business.

The Remainers and the Brexiteers evaluate the different possible outcomes of the Brexit negotiations differently. Both because they emphasize different issues, as discussed in section 4.2.2 about the UK’s policy positions, but also because they perceive the costs and benefits

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11 The Vote Leave campaign bus was decorated with the slogan “We send the EU £350 million a week, let’s fund our NHS instead”.

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attached to the different possible outcomes differently. Most Remainers or “soft-Brexiteers” sees the no deal outcomes as a worst case scenario which will induce big economic costs in terms of no trade deal with the EU and uncertainty for business. “Hard-Brexiteers” on the other side, perceived a no deal outcome as an outcome which will give the UK back sovereignty, but some of them also perceive it as an outcome which may give the UK economic benefits in terms of being able to strike free trade deals with the rest of the world and not having to contribute to the EU-budget. Thus, some Brexiteers do not only value the no deal outcome because of the sovereignty-issue, but also because they believe that it may give economic benefits. Accounting for this uncertainty about payoffs and the players’ beliefs play a central role in the analysis in chapter 6.
5 The formal threat game

The use of threats may be an effective bargaining tactic for a player in order to negotiate a better deal for itself. However, for a threat to be effective it must fulfill some conditions. In chapter three the theoretical conditions for a threat to be efficient were thoroughly discussed. Recall that in order to be efficient, a threat must be relevant, complete, clear, credible and sufficiently severe (Hovi 1998, p. 13-16). In the following analysis I will treat the three former conditions as given, and assume that the threat is relevant, complete and clear. Hence, the analysis in chapter 5 and 6 will assess the conditions of credibility and severity. In order to examine these two conditions for the UK’s threat to be effective, I will use a formal game theoretic model. In this chapter I analyze the conditions of severity and credibility under the assumption of complete information, thus not taking into account the role of uncertainty. In chapter 6 the same model will be analyzed, but under the assumption that the information available to the EU and the UK is incomplete. The game theoretic model being analyzed in this chapter serves as a baseline model for the analysis under incomplete information. Comparing the analyzes will permit me to capture and account for the role of uncertainty in the Brexit negotiations.

5.1 The threat game

The game theoretic model applied in this thesis draws on the general threat model used by Hovi 1998. The model will assess the conditions of credibility and severity for the UK’s no deal threat to be effective in the Brexit negotiations. I have made some adaptations to Hovi’s original threat game regarding the players’ payoffs and regarding the assumptions about the information available to the players, while the structure of the game is kept the same. My adaptations permit me to apply the game to the case of Brexit and account for the role of uncertainty and beliefs.

In the threat game which will be analyzed the two players are the EU and the UK. The UK has threatened to end the negotiations if the EU does to make any concessions and it gets a “bad deal”. The EU will evaluate the threat’s credibility and severity, and then decide whether to concede to some of the UK’s demands. The model assumes that the players can choose between playing a tough and a weak strategy. In the threat game playing a tough strategy for

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12 See section 3.2 for a discussion about what these conditions imply.
the target (EU) entails not yielding to the threat, while playing a weak strategy means that it yields to the threat. For the threatener (UK) playing a tough strategy entails imposing the threat if the target does not yield, while playing a weak strategy means that it does not carry out the threat regardless of the target’s behaviour.

5.1.1 The sequences of moves

The sequence of moves is as follows. Before the game starts, the UK has threatened to end the Brexit negotiation if the EU does not succumb to some of the UK’s demands. The first move in the game is made by the EU which needs to decide whether to yield to the UK’s threat or to stand firm. If the EU yields to the threat and give the UK some concessions, the game ends without the UK making a move and the outcome will be a deal beneficial to the UK (deal1). If the EU decides to not yield to the threat, then the UK must decide between imposing the threat or not imposing the threat. If the EU does not yield to the threat and the UK imposes the threat, then the outcome will be no deal. If the EU stands firm and the UK chooses to not carry out the threat, then the outcome will be a deal beneficial to the EU (deal2).
5.1 Game tree: The threat game with complete information

Key:

\( B_{\text{nd}}^{\text{UK/EU}} \) = benefit of a no deal outcome

\( C_{\text{nd}}^{\text{UK/EU}} \) = cost of a no deal outcome

\( B_{2}^{\text{UK/EU}} \) = benefit of a deal_2 outcome

\( C_{2}^{\text{UK/EU}} \) = cost of a deal_2 outcome

\( B_{1}^{\text{UK/EU}} \) = benefit of a deal_1 outcome

\( C_{1}^{\text{UK/EU}} \) = cost of a deal_1 outcome
5.2 Payoffs associated with the different outcomes

The objective of this section is to discuss the different costs and benefits attached to the three possible outcomes of the threat game. This is a complex task since the relevant costs and benefits in the Brexit negotiations are many and of both political and economic character with different time horizons. Additionally, there is a great deal of uncertainty concerning the consequences of the different outcomes. This uncertainty, in addition to diverse political views, gives ground for different beliefs concerning the costs and benefits of the different outcomes. However, I will assume that the costs and benefits of different outcomes can be represented in generalized terms.

No deal outcome: Withdrawal from the EU with no deal, a clean break, will liberate the UK from its obligations as a member state. The UK will no longer have to make payments to the EU budget and it will get back (formal) sovereignty over its border, its economic policy and its foreign trade policy. Furthermore, it will not have to fulfill any commitments from a withdrawal deal, like paying a financial settlement to the EU or giving EU citizens extensive rights after withdrawal. However, exit from the EU will also remove the benefits connected to membership. In the case of a no deal outcome the UK will not retain access to the Single Market nor other EU-goods it had access to as a member. When leaving the Single Market without a deal with the EU, the default position is that the withdrawing member state will have to trade with the EU on WTO-terms. In formal and generalized terms, the net payoff of a no deal outcome for the withdrawing member state, the UK, can be expressed: \( B_{nd}^{UK} - C_{nd}^{UK} \).

For the EU, a no deal outcome will involve costs in terms of the loss of a withdrawal deal. This entails losing the benefits of an orderly exit, such as a financial settlement, securing EU citizens’ rights in the UK and certainty for businesses. Additionally, the no deal outcome will have economic costs in relation to trade. The UK is a big economy in the EU and an important export country for many EU member states. Not agreeing on the framework of the future relationship and, thus, not on a free-trade agreement, will have negative economic consequences for the EU. On the other side, a no deal outcome will give the EU benefits in terms of reputation effects. Not yielding to the UK’s threat, but playing hard, can give the EU a reputation of being a hard negotiator in withdrawal negotiations. This may have a signaling effect on other member states which consider the option of exit and deter Brexit from creating a domino effect. Playing tough also avoid a domino effect in terms of third countries wanting to renegotiate their agreement with the EU because of the beneficial Brexit deal the UK got.
Hence, playing tough gives the EU benefits by securing the Union’s long-term interests and survival. The net payoff of a no deal outcome for the EU is assumed to be: $B_{nd}^{EU} - c_{nd}^{EU}$.

In the case of a deal-outcome of the negotiations, the costs and benefits for the two parties depend on what kind of deal is agreed. In the framework of the threat game there are two strategy combinations that create a deal outcome, but different kinds. Both parties prefer a deal resulting from playing a tough strategy while the other party plays a weak strategy.

Deal$_1$: A deal$_1$ outcome is assumed to be beneficial to the UK and less so to the EU. A deal beneficial to the UK, a “good deal”, gives the UK concessions to some of its demands (see section 4.2.2 for UK’s policy positions). However, how many and which of the UK’s demands that need to be fulfilled for a deal to be a good deal, depends on who you ask as there are different views among domestic actors. Nevertheless, a deal$_1$ outcome will give the UK benefits in terms of economic benefits related to a trade deal and benefits provided by an orderly exit in terms of clarity. This outcome may accrue some costs for the UK in terms of a withdrawal agreement that oblige the UK to fulfill certain obligations. The EU is assumed to receive economic benefits of a deal$_1$ outcome in terms of a trade deal, as well as benefits in terms of securing citizens’ rights and a financial settlement of the UK’s liabilities. However, a deal beneficial to the UK is assumed to incur costs on the EU in terms of negative reputation effects. The net payoff of a deal$_1$ outcome for the EU and the UK is assumed to be: $B_{1}^{UK/EU} - c_{1}^{UK/EU}$.

Deal$_2$: The deal$_2$ outcome of the threat game is a deal that is beneficial to the EU because it has given few or no concessions to the UK and stood firm on its main policy positions. The deal gives the EU benefits in terms of a withdrawal deal and a deal on the future relationship that is in line with the EU’s red-lines (see section 4.2.1). Additionally, the deal gives the EU benefits in terms of reputation effects. On the other side, the deal is less beneficial to the UK as it has had to give in on many of its initial demands in order to secure a deal with the EU. The UK will receive benefits in terms of a trade deal and the clarity provided by an orderly exit. But the UK will also incur costs, by giving in on demands, in order to get a deal. The net payoff of a deal$_2$ outcome for the EU and the UK is assumed to be: $B_{2}^{UK/EU} - c_{2}^{UK/EU}$.
5.3 Preferences over outcomes

To summarize the discussion in the previous section, the different payoffs connected to the possible outcomes are as follows. The EU gets a net benefit of a no deal outcome equivalent to $B_{\text{nd}E}^{\text{EU}} - C_{\text{nd}E}^{\text{EU}}$, the EU’s net benefit of a deal\textsubscript{1} outcome is $B_{\text{1}E}^{\text{EU}} - C_{\text{1}E}^{\text{EU}}$ and of a deal\textsubscript{2} outcome is $B_{\text{2}E}^{\text{EU}} - C_{\text{2}E}^{\text{EU}}$. The UK receives a net benefit of $B_{\text{nd}U}^{\text{UK}} - C_{\text{nd}U}^{\text{UK}}$ in case of a no deal outcome, $B_{\text{2}U}^{\text{UK}} - C_{\text{2}U}^{\text{UK}}$ in case of a deal\textsubscript{2} outcome and $B_{\text{1}U}^{\text{UK}} - C_{\text{1}U}^{\text{UK}}$ in case of a deal\textsubscript{1} outcome.

I assume that the EU always prefers a deal\textsubscript{2} over a deal\textsubscript{1} and that the UK always prefers a deal\textsubscript{1} over a deal\textsubscript{2}, these assumptions are inherent in the model. In the following equilibria the evaluation of the outcome of no deal is what varies. For the threat of no deal to be credible, the UK must prefer a no deal outcome over a deal\textsubscript{2}. For the threat to be sufficiently severe, the EU must prefer a deal\textsubscript{2} over a no deal outcome. In the threat game of complete information, the players’ preferences and payoffs are assumed to be common knowledge and the players’ beliefs are not a part of the game.

5.4 Equilibria under complete information

In this section I will investigate the conditions for the threat of no deal to be effective under complete information. The EU and the UK are assumed to know each other’s set of strategies and preferences. Given this assumption, I will deduce the game’s equilibria for different assumptions about the players’ preferences.

**Equilibrium 1:** The threat is credible and sufficiently severe under the assumption that

1. $B_{\text{nd}U}^{\text{UK}} - C_{\text{nd}U}^{\text{UK}} > B_{\text{2}U}^{\text{UK}} - C_{\text{2}U}^{\text{UK}}$ and
2. $B_{\text{nd}E}^{\text{EU}} - C_{\text{nd}E}^{\text{EU}} < B_{\text{1}E}^{\text{EU}} - C_{\text{1}E}^{\text{EU}}$

These payoff-assumptions imply that the UK prefers a no deal outcome over a bad deal (deal\textsubscript{2}). While the EU prefers giving concessions to the UK to secure a deal (deal\textsubscript{1}) over a no deal outcome. Backwards induction can be used to find the game’s subgame perfect equilibria (SPE)\textsuperscript{13}, given this payoff structure: If the EU does not yield to the threat, but play a tough
strategy and stand firm, the UK will impose its threat of leaving the negotiations due to assumption (1). Knowing this, the EU prefers to yield to the threat and play a weak strategy due to assumption (2). The SPE under assumption (1) and (2) is hence \{yield; put threat into effect\}. This SPE equals a deal$_1$ outcome.

**Equilibrium 2:** The threat is not credible, but sufficiently severe under the assumption that

(3) $B_{nd}^{UK} - C_{nd}^{UK} < B_{2}^{UK} - C_{2}^{UK}$, and assumption (2) is kept unchanged.

If the UK’s payoff structure is changed to assumption (3), then the threat is no longer credible. The UK prefers a bad deal outcome over a no deal outcome. If the EU does not yield to the threat, the UK will prefer to not effectuate the threat rather than to carry it out.

Knowing this, the EU will prefer to not comply to the threat because it prefers a deal$_2$ over a deal$_1$. Hence, using backwards induction, and given the payoff-assumptions, the SPE is \{not yield; not put threat into effect\}. This SPE equals a deal$_2$ outcome.

**Equilibrium 3:** The threat is not sufficiently severe, but credible under the assumption that

(4) $B_{nd}^{EU} - C_{nd}^{EU} > B_{1}^{EU} - C_{1}^{EU}$, and assumption (1).

If the EU’s payoff structure is changed from (2) to (4) then the threat is no longer sufficiently severe. The EU would prefer to have the threat effectuated rather than to yield to it. The threat is credible, and the UK will effectuate the threat if the EU does not yield. Thus, in the game’s second decision node, the UK will choose to carry out the threat and, knowing this, the EU will choose to not yield to the threat in the game’s first decision node. The SPE for these payoff-assumptions is \{not yield; carry out threat\}. This SPE equals a no deal outcome.

**Equilibrium 4:** The threat is neither credible nor sufficiently severe if both assumption (3) and (4) in common knowledge. The EU prefers to stand firm and play a tough strategy rather than to comply with the threat and the UK prefers to not effectuate the threat if the EU does not yield. In the second decision node the UK will chose to not carry out the threat. Knowing this, and also because it prefers no deal over a deal$_1$, the EU will not yield to the threat in the first decision node. The SPE under these preference assumptions is \{not yield, not carry out threat\}. This SPE equals a deal$_2$ outcome.

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with an information set that is a singleton, (ii) includes all succeeding nodes and (iii) does not cut across any information sets (Hovi 2008, p. 66).
The only equilibrium of the threat game under complete information that produce a deal\textsubscript{1} outcome is the equilibrium which assumes (1) and (2) are common knowledge. The threat is not efficient in any of the three other equilibria with their respective preference orderings. The outcome will be a deal beneficial to the EU (deal\textsubscript{2}) both in the case where the threat is not credible (3), but sufficiently severe (2), and when the threat is neither sufficiently severe (4) nor credible (3). If the threat is not sufficiently severe (4), but credible (1), the outcome of the game will be no deal. For the threat to be efficient in the model of complete information it must fulfill both condition (1) and (2). Accordingly, the model demonstrates that the threat must be both credible and sufficiently severe in order to induce the EU to make concessions to the UK under the assumption of complete information.

5.5 Implications and conclusion

In this chapter I have used a game theoretic model to examine the conditions for the UK’s threat of no deal to be effective under the assumption of complete information. The equilibria results of the analysis of the threat game show that to be effective, the threat must be both credible and sufficiently severe, in addition to the three other conditions of clearness, completeness and relevance. In other words, for the threat to be effective, the UK must prefer to carry out the threat rather than not imposing it if the EU does not yield. The EU, on its side, must prefer to yield to the threat rather than standing firm and have the threat carried out. This is the case only in equilibrium 1 of the game’s four equilibria.

In a game of complete information, there is no room for misrepresentation of information. The players base their actions on their preferences and the other player’s preferences, which are assumed to be common knowledge. This is not a realistic modeling of negotiations. In the Brexit negotiations the players do not have full information about the other players’ preferences but use available information to shape their beliefs about the other player’s preferences. In order to negotiate the best deal possible for oneself, negotiating parties may engage in strategic play which includes misrepresentation of preferences or capabilities. In order to account for uncertainty and beliefs, I will in I the next chapter analyze the threat game and the conditions for the threat to be effective under the assumption of incomplete information.
6 The threat game with uncertainty

Negotiation and the use of threats under complete information does not make much sense for two main reasons. First of all, if the players have complete information, then bargaining or the use of threats would be superfluous because the players already know everything about the game. They know each other’s preferences and types, and thus what kind of deal that would be possible to strike. Secondly, the assumption of complete information differs from how bargaining actually occurs (Morrow 1994, p. 237). The essence of negotiating is communication under uncertainty and strategic use of private information about preferences and capabilities. Games of complete information do not allow for misrepresentation of information and to not account for the role of beliefs in negotiations. In reality, the Brexit negotiations involve negotiating under extreme uncertainty. The players’ preferences are unknown, and so are the payoffs attached to the different possible outcomes. Moreover, the unprecedented nature of the Article 50 negotiations adds an additional element of uncertainty to the Brexit process. In this environment of extreme uncertainty, the EU and the UK must rely on their beliefs, as well as their preferences, when making decisions.

In this chapter I will analyze the threat model under the assumption of incomplete information to account for the role of beliefs and uncertainty in the Brexit negotiations. I will start by discussing some of the known unknowns of Brexit that are sources of uncertainty in the negotiations. These uncertainties can be used strategically by the players in the negotiation in order to try to make the other player move in a desired way. Then I will present the threat game under the assumption of incomplete information and assess the threat’s credibility and severity. Finally, in order to corroborate the findings from the analysis of the threat game, I will briefly study the Brexit negotiations as a two-level game and explore the players’ win-sets.

6.1 The uncertainties of Brexit

In the Brexit negotiations there are many unknowns, things we do not know that contribute to uncertainty for both the actors themselves and for the analysts trying to understand the process. Some of the unknowns are known unknowns, things we know that we do not know (Lord, 2017). The UK’s and the EU’s preferences over the possible outcomes are uncertain, so are their balancing of different priorities and elements in the negotiations. The payoffs
attached to the different outcomes are also uncertain and perceived differently by different internal actors. Additionally, the effect the set-up of the negotiations has on the outcome, as there are no priors to withdrawal negotiations, pose another source of uncertainty. These known unknowns affect the strategic interaction between the UK and the EU, as well as the conditions for the no deal threat to be efficient. This because the different uncertainties permit the players to misrepresent information concerning their preferences and types. Both the UK and the EU may engage in strategic play in order to make the other player believe that it prefers to play a tough strategy or that it is incapable of playing a weak strategy due to domestic constraints.\textsuperscript{14} In addition to the known unknowns, there are surely several unknown unknowns\textsuperscript{15} in the Brexit negotiations, things we don’t know that we don’t know. However, I will not undertake to uncover some of the unknown unknowns in this thesis, rather I limit myself to account for how the known unknowns affect the negotiations.

**The unknowns of British politics:** The slogan “Brexit means Brexit” has been uttered several times by Theresa May and the British government since the UK voted to leave the EU. But what does Brexit really mean? The UK government has found it difficult to agree on what precisely it wants Brexit to mean and, thus, what outcome it would prefer from the negotiations with the EU. The preferences of the UK are ambiguous. The political parties are split internally and the public divided. There does not seem to be any approach to Brexit that is a stable equilibrium in British politics (Lord, 2017). When assessing the UK’s threat of “no deal is better than a bad deal”, several unknowns arise. There exists considerable uncertainty connected to what is meant by a “bad deal”. It is very unlikely that the UK is able to negotiate a deal with the EU that is more beneficial than EU membership in terms of benefits derived from affiliation with the EU. In terms of market access and various cooperation benefits, any deal would be a bad deal compared to EU membership. Whereas economic indicators will suffer compared with full membership of the bloc, national sovereignty is expected to be strengthened. A Brexit deal with the EU may give the UK benefits in terms of “taking back control”, in addition to giving it some kind of association to the EU that is not full-membership. Given that control over immigration was a main concern in the campaign prior to the referendum, there is reason to think that this criterion will weigh for much when the

\textsuperscript{14} The EU has, for example, stated that it is unable to change its negotiation position because of its bureaucratic and legislative nature.

\textsuperscript{15} Inspired by a quote of Donald Rumsfeld: “There are known knowns. These are things we know that we know. There are known unknowns. That is to say, there are things that we know we don’t know. But there are also unknown unknowns. There are things we don’t know we don’t know”.

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value of any post-Brexit deal is assessed. However, the phrasing of the threat “no deal is better than a bad deal” is malleable and gives Theresa May leeway in the negotiations facing the domestic audience. As an EU official pointed out, by not specifying what a bad deal is, Theresa May can have any deal with the EU and then present it as a good deal domestically [Interview 04.04.18]. This allows her to keep her word regardless of the outcome of the negotiations. Consequently, what it takes for a deal to be a “good deal” compared to a no deal outcome for the UK remains unknown, and so do the UK’s preferences.

The unknowns of EU’s preferences: The EU has appeared as the united, clear and strong party to the Brexit negotiations. However, there do exist uncertainties concerning the Union’s preferences over the different possible outcomes. Particularly, the Union’s weighting of long-term versus short-term concerns is uncertain. For the EU the Brexit negotiations can be seen as a part of a repeated game, where withdrawal negotiations with other member countries may occur later on. In a long-term perspective, the EU has interest in establishing a reputation for being a tough bargainer in withdrawal negotiations in order to deter member states from exiting. In a shorter-term perspective, the EU may gain benefits from a deal with the UK in terms of cooperation and trade benefits. How the EU weigh these benefits against each other is a part of what determine its preferences. However, my interviewee, scholar Christopher Lord, assesses the EU’s concerns for remaining united as more important than the concerns for potential costs and benefits of different outcomes: “I think that much more important [than balancing different costs] is hanging on to the cohesion of the remaining 27 member states” [Interview 06.04.18]. Staying united is essential for the EU to exploit its negotiation position, and therefore a main concern for the EU. Lord thinks the EU made a hard-headed calculation that went something like “as long as we [the EU] can hold on to the cohesion of the remaining 27, then the UK would eventually have to reach an agreement with us, on our terms” [ibid.]. However, what it would take for the EU to give in on some of its terms remains unknown.

The unknown payoffs of different outcomes: The costs and benefits caused by the different outcomes are unknown and, hence, the players do not know what the payoffs are. There exist different typologies of deals, the Norway model, the Swiss model or the Canada model etc. These typologies give some insights in the potential costs and benefits of the different deal-outcomes. The no deal outcome, on the other side, has no typology or priors. Never before has an EU-member withdrawn from the Union to end up with no deal. Most economic analyzes about the consequences of an unorderly Brexit predict that a no deal will entail considerable
economic loss for the UK. However, these forecasts only project the short-term consequences, the long-term consequences cannot be projected. This was pointed out by economist Abhiney Muthoo: “A no deal will most likely be bad for the UK in the short term, but nobody knows the long-term consequences of no deal” [Interview 12.03.18]. A no deal outcome will hit the EU less hard than the UK but is likely to impose costs on the EU, as well, in terms of reduction in trade and economic cooperation with the UK. A no deal will also entail that UK’s budget contribution to the EU disappears. The EU’s member states will be affected to varying degrees depending on their trade relations with the UK and how they suffer from a reduction of the budget. These uncertainties about the payoffs make the players’ beliefs about the consequences of possible outcomes important. There are also different beliefs and perceptions of the payoffs within the two players. Considering different perceptions of costs among internal actors adds another level of uncertainty to the analysis. In order to take account for internal perceptions of payoffs, the Brexit negotiations can be modeled as a two-level game. I will briefly explore the players’ internal level in section 6.5, but a full two-level analysis is beyond the scope of this thesis.

**The unknowns of negotiations:** Never before has Article 50 been triggered, and withdrawal negotiations from the EU have no priors. Thus, the effects of the negotiations’ set-up given by Article 50 is uncertain. However, it can be argued that Article 50 “skews the process against the departing member state” (Hanké 2017). The Article sets out, among other things, a two-year timeline for the negotiations (see section 2.3 further discussion on Article 50’s set-up). A short timeline is beneficial to the EU because it puts substantial pressure on the UK and excludes the possibility of using patience as a negotiation strategy. Another feature of the Brexit negotiation process is the phasing of the negotiations. This structuring of the negotiations is not set out in Article 50, but was something the EU wanted and not the UK. The fact that the negotiations ended up being held in two phases demonstrates the EU’s relative bargaining power, but also gives the EU the power to call the shots and decide what to be negotiated when (Hanké 2017). The ratification rules set out by Article 50 also constrain the parties and their respective win-sets (see section 6.5 for further discussion on win-sets).

Moreover, negotiating with the EU is negotiating with a bureaucratic organization. This feature is not particular to the Brexit negotiation, but to all negotiations between the EU and third countries. The EU is the creation of law and is built on institutional rules. Christopher Lord put it this way: “It [the EU] can only do what it is authorized to do by its member states
in the treaties, and that means it can’t quickly reach a political agreement to do something completely different” [Interview 06.04.18]. This restricts the EU somewhat in the negotiations, but the institutional constraints can also be used strategically by the EU.\textsuperscript{16} According to the EU official I interviewed, the exit process is not a negotiation between the EU and the withdrawing member state, it is only about application of rules [Interview 04.04.18]. The EU cannot give the UK a deal which is not in accordance with its treaties, the EU official stresses [ibid.]. Christopher Lord points out that Michel Barnier has said the same thing during the negotiation, that he is not negotiating, but simply performing an administrative and technical task of arranging separation [Interview 06.04.18]. However, in addition to being a rule based bureaucratic organization, represented by the Commission, the EU also has a more volatile side to it, represented by the member states. The claim that the Brexit negotiations are simply application of rules, don’t seem to fit the facts, as there is bargaining going on between the two parties which requires political agreement. The claim seems rather to be an expression of a negotiation tactic which tries to obtain leverage by accentuating institutional constrains. Still, negotiations with the EU under Article 50 have no priors and there are uncertainties about what is possible to negotiate, the consequences of the institutional set-up of the negotiations, as well as of the EU’s nature.

\section*{6.2 The threat game with incomplete information}

In this chapter I analyze the threat game under the assumption of incomplete information. I will assume that the players have incomplete information about the other player’s preferences and, thus, type. Consequently, the players’ beliefs about the other player’s type become a part of the game. I assume that the EU and the UK can be one of two types, “tough” or “weak”. If the UK prefers to effectuate the threat if the EU does not yield, it is a tough type. If it prefers to not carry out the threat if the EU does not yield, then it is a weak type. The EU is a tough type if it prefers to stand firm and not yield to the threat of no deal, and it is a weak type if it prefers to yield to the threat and give the UK some concessions. In this environment of uncertainty, the players have incentives to misrepresent their actual preferences and capabilities to try to obtain a better deal. Both players want to be perceived as a tough type regardless of their actual type. The players’ beliefs, together with their preferences, determine

\textsuperscript{16} See for example Schelling 1980 and Meunier 2000 for elaboration on such considerations.
the outcome of the interaction. Hence, bluffing and strategic behavior become a part of the game.

**6.3 Assessing credibility – uncertainty about UK’s type**

The Brexit negotiations have two-sided incomplete information, there exist uncertainty concerning both the EU’s and the UK’s type. However, I will in this section assume that it is common knowledge that the EU’s type is weak, and that the threat is sufficiently severe. Thus, if the EU believes that the UK’s threat is credible, it will prefer to yield to it rather than to have it effectuated. This is a simplification of reality in order to make the game a game of one-sided incomplete information and the threat’s effectiveness dependent on its credibility. This measure is done for reasons of simplicity. A game with one-sided incomplete information is easier to model than a model of two-sided incomplete information. Nevertheless, this assumption also permits me to make the analysis about the threat’s credibility rather than severity in this section. The threat’s severity will we assessed in section 6.4. The threat’s credibility is possible for the UK to affect with the use of different types of strategies (see section 3.2.2). But the no deal threat’s severity, on the other hand, is more difficult to change for the UK since it has to do with the EU’s payoff structure and the implication of a no deal outcome for the EU. I assume that the EU does not know the UK’s type when the game begins, but that the UK’s type can be one of two: weak or tough. I further assume that the EU believes the UK to be a tough type with probability $p$ and a weak type with probability $1-p$. The EU does not know the UK’s type, but it knows the two possible types’ respective payoff structure.

**6.3.1 The sequence of moves and the players’ preferences**

The uncertainty about the UK’s type is modelled by introducing “Nature”\(^\text{17}\) as a player which serves to determine the UK’s type. Nature makes the first move in the game which randomly decides the UK’s type with the probabilities stated in the previous section. The UK is assumed to be able to observe Nature’s move and, hence, knows its own type. The EU cannot observe the move made by Nature and is consequently not aware of the UK’s type at the start.

\(^{17}\) Nature has no strategic interest in the outcome of the interaction, it serves only as a measure to make the UK’s type random and unknown to the EU.
of the game. The probability distribution is known to both players, but Nature’s move is only known by the UK. When Nature has made its move, the game continues as described in the timeline under.

1: Nature makes the first move and decides the UK’s type with probability \( p \) that the UK is a tough type and \( 1 - p \) that it is a weak type. The UK is informed of Nature’s move and, thus, knows its type.

2: The EU has to choose between yielding to the threat or to stand firm, not knowing if it is facing a weak or a tough UK. This is visualized in the game tree under by the dotted line connecting the two decision nodes. When the EU makes its move, it does not know if it is situated at the left or right side of the game tree. If the EU yields, the game ends, and the payoffs are those of a deal \( ^1_{EU/UK} \).

3: If the EU stands firm, then the UK must choose between carrying out the threat and not carrying out the threat. If the UK carries out the threat, the outcome will be no deal. If the UK chooses to not carry out the threat, the outcome will be a deal \( ^2_{EU/UK} \).
6.3 Game tree: The threat game with incomplete information

Key:

p = probability that UK is tough
1 - p = probability that UK is weak

\[ B_{\text{UK/\text{EU}}}^{\text{nd}} \] = benefit of a no deal outcome
\[ C_{\text{nd}}^{\text{UK/\text{EU}}} \] = cost of a no deal outcome

\[ B_{\text{2UK/\text{EU}}}^{\text{}} \] = benefit of a deal\textsubscript{2} outcome
\[ C_{\text{2}}^{\text{UK/\text{EU}}} \] = cost of a deal\textsubscript{2} outcome

\[ B_{\text{1UK/\text{EU}}}^{\text{}} \] = benefit of a deal\textsubscript{1} outcome
\[ C_{\text{1}}^{\text{UK/\text{EU}}} \] = cost of a deal\textsubscript{1} outcome
6.3.2 Equilibria under incomplete info

If the EU does not yield to the threat, but stands firm on its demands, its outcome of the negotiations depends on whether the UK carries out the threat or not. The EU’s expected utility of standing firm can be described as: \( p (B_{nd}^{EU} - C_{nd}^{EU}) + (1-p) (B_{2}^{EU} - C_{2}^{EU}) \). While the EU’s expected utility of yielding is \( B_{1}^{EU} - C_{1}^{EU} \). It is rational for the EU to yield to the threat only if the expected utility of yielding is perceived as higher than those of standing firm:

\[
\text{Expected Utility(yield)} > \text{Expected Utility(not yield)}. 
\]

To find the critical value of \( p \) for the EU to yield to the threat the following inequality is solved for \( p \):

\[
P > \frac{(B_{1}^{EU} - C_{1}^{EU} - B_{2}^{EU} + C_{2}^{EU})}{(B_{nd}^{EU} - C_{nd}^{EU} - B_{2}^{EU} + C_{2}^{EU})} 
\]

(5)

It is rational for the EU to yield to the UK’s threat when the probability of the UK being a tough type meets the criteria in (5). However, if the probability of the UK’s type being tough is smaller than the critical value, as shown by criteria (6), then it is in the EU’s interest not to yield to the threat.

\[
P < \frac{(B_{1}^{EU} - C_{1}^{EU} - B_{2}^{EU} + C_{2}^{EU})}{(B_{nd}^{EU} - C_{nd}^{EU} - B_{2}^{EU} + C_{2}^{EU})} 
\]

(6)

To verify that these conditions put meaningful restraints on \( p \), I will briefly evaluate whether or not the fraction on the right side of (5) and (6) takes on values between 0 and 1. From the payoff structure we know that \( B_{1}^{EU} - C_{1}^{EU} < B_{2}^{EU} + C_{2}^{EU} \), so the nominator is always negative. We also know that \( B_{nd}^{EU} - C_{nd}^{EU} < B_{2}^{EU} + C_{2}^{EU} \), thus the denominator is also negative. Also, the EU’s preference ordering is assumed to be deal\(_2^{EU} > \text{deal}_1^{EU} > \text{no deal}^{EU} \), thus, the nominator

\[ B_{1}^{EU} - C_{1}^{EU} - B_{2}^{EU} + C_{2}^{EU} > 0 \]

\[ B_{nd}^{EU} - C_{nd}^{EU} - B_{2}^{EU} + C_{2}^{EU} > 0 \]

\[ B_{1}^{EU} - C_{1}^{EU} > 0 \]

\[ B_{nd}^{EU} - C_{nd}^{EU} > 0 \]

\[ B_{1}^{EU} > 0 \]

\[ B_{nd}^{EU} > 0 \]

\[ C_{1}^{EU} > 0 \]

\[ C_{nd}^{EU} > 0 \]

\[ C_{2}^{EU} > 0 \]

\[ 0 < p < 1 \]
is smaller than denominator. Consequently, the fraction takes on values between 0 and 1 and, thus, puts a meaningful restrain on p.

The equilibria of the threat game under the assumption of incomplete information, and that the EU is a weak type, depend on the EU’s beliefs concerning the value of p, the probability that the UK is a tough type, as well as the actual type of the UK. Four different equilibria can be detected in the game.

The UK’s type is tough:

**Equilibrium 1:** The UK’s type is tough, and the EU believes that the UK is tough. The UK would have carried out the threat if the EU did not yield. The EU believes that the UK is tough and, according to its preferences, the EU prefers to yield to the threat. The UK will not make a move, and the game ends after the EU’s move with a deal\(_1\) outcome. The Bayesian perfect equilibrium (BPE)\(^{19}\) is \{yield; impose threat\}, and the outcome will be a deal\(_1\).

**Equilibrium 2:** The UK’s type is tough, and the EU believes that the UK’s type is weak. The UK will impose the threat if the EU does not yield, but believing that the UK’s type is weak, the EU does not yield to the threat. Thus, the UK carries through with the threat and the outcome of the game is no deal. The BPE is \{not yield; impose threat\}.

The UK’s type is weak:

**Equilibrium 3:** The UK’s type is weak, and the EU believes that the UK’s type is tough. The UK would not carry out the threat, but the EU believes that it would and, therefore, yields to the threat. The game ends and the UK will not have to make a move. BPE is \{yield; not impose threat\}, and the outcome will be a deal\(_1\).

**Equilibrium 4:** The UK’s type is weak, and the EU believes that it is weak. The UK will not impose the threat and, believing that the UK will not impose the threat, the EU does not yield. The BPE is \{not yield; not impose threat\}. The outcome will be a deal\(_2\).

In equilibria 1 and 3, p fulfills condition (5), and the Bayesian perfect equilibria are pooling equilibria. In these equilibria the EU evaluated the probability of the UK being a tough type to be sufficiently big to prefer to yield to the threat of no deal rather than to stand firm. Thus, the

---

\(^{19}\) BPE is an equilibrium concept which takes into account the players’ beliefs. BPE is a pair of strategies that is the best response vis-à-vis each other, given the players’ beliefs. Additionally, BPE takes into account that the players’ beliefs can be updated during the game using Bayes’ rule.
EU will yield to the threat, and the UK will not have to make a move. Since the EU’s move ends the game, the UK’s type will not be revealed by the sequence of moves. If p fulfills condition (6), such as in equilibria 2 and 4, then the Bayesian perfect equilibria will be separating equilibria. The EU prefers to not yield to the threat and the UK must decide whether to carry out threat or not and will, consequently, reveal its type. In the separating equilibria the EU’s beliefs can be updated by using Bayes’ rule, I show how in the next section.

6.3.3 Bayesian updating of beliefs

If the UK moves in the threat game, the EU gets new information concerning the UK which can be used to update the EU’s beliefs about the UK’s type. This is the case in the separating equilibria 2 and 4 where the condition (6) is fulfilled. The updating of the EU’s prior beliefs about the UK’s type based on new information, is possible by applying Bayes’ rule. Bayes’ rule uses “conditional probabilities of events given states to deduce the conditional probabilities of states given events” (Morrow 1994, p. 163).

\[
P(A/B) = \frac{P(B/A) \cdot P(A)}{P(B/A) \cdot P(A) + P(B/\bar{A}) \cdot P(\bar{A})}
\]

\[P(A/B)\] = probability of A, given B (posterior belief)
\[P(B/A)\] = probability of B, given A
\[P(B/\bar{A})\] = probability of B, given not-A
\[P(A)\] = probability of A (prior belief)
\[P(\bar{A})\] = probability of not-A (prior belief)

B= new evidence

Applied to the threat game between the EU and the UK, A, \(\bar{A}\) and B, \(\bar{B}\) are defined as:

A = the UK is tough
\(\bar{A}\) = the UK is weak
B = the UK imposes the threat

\( \bar{B} \) = the UK does not impose the threat

The probabilities for the UK to be tough or weak have been assumed to be:

\[ P(A) = p \]

\[ P(\bar{A}) = 1-p \]

When the threat game has a separating equilibrium, it follows from the players’ equilibrium strategies that:

\[ P(B/A) = 1 \]

\[ P(B/\bar{A}) = 0, \text{ and} \]

\[ P(\bar{B}/A) = 0 \]

\[ P(\bar{B}/\bar{A}) = 1 \]

Plugging the values of equilibrium 2 into Bayes’ rule gives the result:

\[
P(A/B) = \frac{P(B/A) \cdot P(A)}{P(B/A) \cdot P(A) + P(\bar{B}/\bar{A}) \cdot P(\bar{A})} = \frac{0 \cdot p}{0 \cdot p + 1 \cdot (1-p)} = \frac{0}{1-p} = 0
\]

This result means that if the UK does not impose the threat after the EU has chosen to stand firm, then the EU will update its subjective probability that the UK is tough to 0. In other words, given that the UK does not carry out the threat, it follows that the UK with certainty has a weak type (in the separating equilibrium 2).
Plugging the values of equilibrium 4 into Bayes’ rule gives the result:

\[
P(A/B) = \frac{P(B/A) \cdot P(A)}{P(B/A) \cdot P(A) + P(B/\bar{A}) \cdot P(\bar{A})} = \frac{1 \cdot p}{1 \cdot p + 0 \cdot (1-p)} = \frac{p}{p} = 1
\]

This result means that if the UK carries out the threat, then the EU will update its subjective probability that the UK is tough to 1. Consequently, given that the UK carries out the threat, it follows that the UK with certainty has a tough type (in equilibrium 4). Thus, after the UK moves in the threat game, the equilibria are separating equilibria and the EU can know with certainty what type the UK has by updating its beliefs using Bayes’ rule.

In the pooling equilibria of 1 and 3, Bayes’ rule is inapplicable because it would give the result 0/0, which is undefined. This is explained by the probabilities inferred from the players’ strategies along the equilibrium path which are \(P(B/A) = 0\) and \(P(B/\bar{A}) = 0\). Plotting these values into Bayes’ rule will give the result 0/0\(^{20}\). Thus, in the pooling equilibria Bayes’ rule cannot be used to update beliefs. More intuitively, Bayes’ rule cannot be used because the UK does not make a move in these equilibria and, thus, no new information is given the EU in order for it to update its beliefs. When applying Bayes’ rule, one asks what the EU should believe about the UK’s type if the UK imposes or do not impose the threat, but in the pooling equilibria neither can occur.

In the formal threat game, new information about the UK’s type only occur if the EU does not yield, and the UK then make a move. By observing whether the UK imposes the threat or not, the EU can be sure of the UK’s type. In reality, new information that can be used by the EU to update its beliefs about the UK’s type occur more often, but can not be used to draw certain conclusions about the UK’s type. The UK has incentive to appear as a tough player regardless of its true type. The EU is aware of this and will be careful to draw conclusion about the UK’s type based on new information of different sorts. Additionally, the EU is interested in assessing the UK’s type as correctly as possible before it makes its move. It does not help the EU much in deciding what move to make to know the UK’s true type after the game has ended. The EU’s beliefs about the UK’s type is important when deciding whether to yield or not. The UK tries to affect the EU’s beliefs in different ways. But in order to affect the EU’s beliefs about the UK’s type, the new information must be credible. In other words, the new

\[
20 \quad P(A/B) = \frac{P(B/A) \cdot P(A)}{P(B/A) \cdot P(A) + P(B/\bar{A}) \cdot P(\bar{A})} = \frac{0 \cdot p}{0 \cdot p + 0 \cdot (1-p)} = \frac{0}{0}.
\]
information must be of such a sort that it changes the EU’s beliefs about the UK’s type. That is, the UK must send costly signals, and not only cheap talk, in order to persuade the EU.

### 6.3.4 The role of credibility – findings and implications

The analysis of the conditions for the threat to be credible demonstrates how important credibility is for the threat to be efficient. As stated by Abhinay Muthoo: “Credibility is crucial for the UK’s no deal threat to be effective” [Interview 12.03.18]. However, credibility under complete and incomplete information imply different things. Under complete information, the EU must know that the UK prefers to impose the threat over not imposing it. Incomplete information makes the players’ beliefs a part of the game and misrepresentation of information possible. Consequently, for the threat to be credible it suffices that the EU believes that the UK will carry it out.

Under the assumption of complete information, one of the four equilibria deduced from the model give the outcome of a deal\(_1\) (equilibrium 1). For the threat to be effective and a deal\(_1\) to be an equilibrium the EU must know that the UK wants to carry out the threat and the threat must be sufficiently severe. Given incomplete information, two of four equilibria give the outcome of a deal\(_1\) (equilibria 1 and 3). For the threat to be effective and give a deal\(_1\) outcome, it is sufficient that the EU believes that the UK will impose the threat, given that it is sufficiently severe. Hence, the conditions for the no deal threat to be credible and efficient is less strict under incomplete than complete information.

Under incomplete information the UK has the possibility to affect the credibility of its threat in different ways. The UK has taken several measures that can increase the threat’s credibility, regardless of whether they initially were intended to serve that purpose. One measure that has been taken is to increase spending in order to prepare for a no deal outcome. In the budget presented in November 2017 Chancellor Phillip Hammond allocated considerable amount of money to be used to prepare for a no deal Brexit. Preparing for this possible outcome and, hence, reducing the costs of it, serves to increase the threat’s credibility by making the outside option more attractive. Additionally, the Department for International Trade’s effort to prepare the ground for the UK to strike trade deals after Brexit plays a part in defining the UK’s outside options [Abhinay Muthoo, Interview 12.03.18]. Thus, although the department does not take part in the Brexit negotiations per se, their work is essential for the no deal strategy to be credible [ibid.]. However, the measures taken by the UK in order to
increase the threat’s credibility, whether they are deliberate at that purpose or not, don’t seem to be sufficient to make the threat come across as credible.

Which of the equilibria in the game of incomplete information appears to be more plausible? For the pooling equilibria 1 and 3 to be likely, and thus a deal$_1$ outcome, the EU must believe that the UK is prepared to leave the negotiations unless it gets some concessions. Taking into consideration that a no deal outcome will be much more harmful to the UK than the EU, and the internal divisions in the UK over which outcome is more preferential, the threat does not seem very credible. Christopher Lord says he thinks the EU perceives the threat as having very low credibility: “I would guess near zero credibility. First, because the EU reckon that the threat cannot be sustained domestically, and, secondly, because the UK would be hit five times as hard as the EU itself in the case of a breakdown” [Interview 06.04.18]. Consequently, the separating equilibria 2 and 4 seem more plausible than the pooling equilibria because in the former the EU does not believe that the UK is a tough type. And between the two separating equilibria, it can be argued that number 4 seems more likely to occur than number 2. In equilibrium 2 the UK’s type is tough, which means that it prefers a no deal outcome over a “bad deal” (deal$_2$). Due to the predicted economic costs of a no deal for the UK, it seems unlikely that the UK will prefer a no deal over a deal, even a “bad deal”. In equilibrium 4 the UK’s type is weak, which means that the UK prefers a deal$_2$ over no deal and will, thus, not impose the threat.

In this section I have assessed the no deal threat’s credibility, assuming that the threat is sufficiently severe. While credibility is key to make the threat efficient, it is not a sufficient condition. For the threat to coerce the EU to make concessions, it must also be evaluated as sufficiently severe by the EU.

6.4 Assessing severity – uncertainty about the EU’s type

In this section I will take a closer look at the no deal threat’s severity under incomplete information about the players’ types. In order to do so, I will assume that it is common knowledge that the UK’s type is tough. Hence, the UK’s threat is credible, and it will be imposed if the EU does not yield. The game becomes a game of one-sided incomplete information with the EU’s type being unknown. Consequently, the analysis in this section
concerns the threat’s severity and the EU’s assessment of the payoffs attached to yielding to the threat or standing firm. Recall that for the no deal threat to be sufficiently severe, it has to make the EU prefer to yield to the threat rather than to have it carried out. The EU can be one of two types, tough or weak. If the EU is weak it prefers to make concessions in order to strike a deal with the UK. If the EU is tough it prefers to stand firm and have a no deal outcome. Assuming that the threat is credible, the UK has a dominant strategy to carry out the threat if the EU does not yield. Knowing this, the EU has the choice between yielding, which will entail a deal\textsubscript{1} outcome, and not yielding, which will lead to a no deal outcome. To evaluate the threat’s severity, the EU must consider the payoffs attached to the two different outcomes. For the EU to consider the threat as sufficiently severe, it’s preference ordering has to satisfy assumption (2) from chapter 5: \( B^{\text{EU}}_{\text{nd}} - C^{\text{EU}}_{\text{nd}} < B^{\text{EU}}_{1} - C^{\text{EU}}_{1} \). The threat game can be modified as shown in figure 6.4, with the probabilities \( q \) that the EU is a tough type and \( 1-q \) that the EU is a weak type.

6.4.1 Game tree: The threat game with credible threat

The outcome of yielding or not yielding is in this game known to the EU, since the UK’s type is common knowledge. However, the payoffs connected to the two possible outcomes are unknown and the EU’s beliefs concerning the potential costs and benefits will be essential. The payoffs attached to a no deal and a deal\textsubscript{1} outcome have political and economic character, as well as short- and long-term horizons. The EU’s beliefs and emphasis on the different elements will determine its perception of the threat’s severity.
6.4.1 Reputational concerns versus maintaining a close relationship

For the EU, the Brexit negotiations can be perceived as a game which may get repeated with the remaining 27-member countries as potential withdrawing members. Considering the possibility that the game will be repeated, gives the EU incentive to not give in to any of the UK’s demands in order to establish a reputation for being a tough negotiator. A reputation of being tough may give future beneficial effects in terms of deterring other member countries from withdrawing. Additionally, there exist another type of possible domino effect caused by the Brexit negotiation, and that is third-states wanting to renegotiate their agreement with the EU in case of a deal beneficial to the UK. Playing a tough strategy sends a signal to states with a third-state affiliation to the EU, such as Norway, that it is not possible to get a better deal with the Union.

However, playing tough will entail costs for the EU if the UK also plays tough. In the threat game this combination of strategies would give a no deal outcome. A cliff edge Brexit will be costly for the EU since it will reduce trade and cooperation between the Union and the UK. The outcome of no deal will imply short-term costs for the EU, but the costs can be expected to decrease over time as adaptations to the new relationship comes into place. The Union’s evaluations and weighing of the threat’s long-term and shorter-term costs and benefits is decisive for whether or not the no deal threat is considered sufficiently severe. The balancing boils down to considering what is the most important for the EU, to gain a reputation for being a tough negotiator in withdrawal negotiations or maintaining a close relationship with the UK.

It can be hard to resist short-term benefits in order to obtain benefits in the future. Institutional devices can be used to limit choices that maximize short-term benefit at the expense of long-term benefits (Gates and Humes, p.151). The EU is a bureaucratic organization with a lot of institutional devices which gives the Union the “power to bind oneself” (Meunier 2000, p. 106). EU’s institutional rules for decision making and for delegating bargaining authority serve as devices for making decisions ex ante which reduce the risk to make decision to maximize short-term benefits ex post. One of the advantages of the EU in negotiations is that it needs the agreement of its member states, not necessary all of them all the time, but a lot of them. Interviewee Christopher Lord put it: “It’s one of the strikes of the EU, that it can credibly threaten, we can’t reach an agreement […] because we can’t get all of our 27 member states to sign on” [Interview 06.04.18]. These institutional devices and the nature of
the way the EU reaches decisions, makes the EU a tough bargainer. Additionally, according to the EU official I interviewed, the risk of a domino effect is not something the EU is concerned with when negotiating Brexit [Interview 04.04.18]. Besides, the official stresses, creating a deterring effect is being taken care of by the UK itself. No other country would want to have such a mess as the UK has made of Brexit and, the official further stresses, the support for the EU has even increased in several member states after the process of Brexit started [ibid.]. However, if it had not been the case that Brexit came across as a huge chaos, it is possible to imagine that the EU then would worry about the possibility of a domino effect. The presumably lack of fear of a domino effect does not mean that the EU don’t think about the precedence that Brexit will create, as it is the first ever negotiation about withdrawal from the EU.

6.4.2 The threat’s severity – findings and implications

For the EU to consider the threat as sufficiently severe, it must prefer the outcome of a deal beneficial to the UK over no deal. This is a necessary condition for the UK’s threat of no deal to be effective and lead to a deal,1 outcome. Does it seem probable that the EU can believe the threat to be sufficiently severe? Yielding to the UK’s threat would have a bearing on the EU’s vital interest (see section 3.2.1) and be in opposition to earlier positions undertaken by the EU. As Christopher Lord put it: The no deal threat tries to “force the EU to abandon all of its principles, such as the indivisibility of the four freedoms, such as the jurisdiction of the ECJ, such as being a part of the administrative structures” and then suddenly say to the UK: “we have been telling Norway for twenty years that it cannot possible have all of this access to European Union policies without being a full member”, and now, because the UK is so much more important to us than Norway ever was, “we are going to eat all of our words and say that the UK can have access to the Single Market after all” [Interview 06.04.18]. This seems unlikely. As the EU is the creation of law, it can only act based on its treaties and on the consent of its member states. Consequently, in order for the EU to yield to the UK’s threat it would need to reach a political agreement to do something in opposition to what is laid down in the treaties. “The chances of the European Union agreeing to all of that depend on all 27 member states agreeing to that”, stresses Christopher Lord.

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6.5 Negotiating Brexit and the no deal threat

According to the EU official I talked to, the Brexit process is not a negotiation between the UK and the EU, it is only about application of rules [Interview 04.04.18]. Consequently, it is not possible to threaten the EU or coerce the EU to make concessions in the context of the Brexit negotiations because the EU cannot be negotiated with [ibid.]. Besides, the EU official stresses, it is a delusion that the UK could have threaten the EU at all. The UK is in no position to threaten as it is not vital for the EU to reach a deal, but it is for the UK [ibid.]. This asymmetric interdependence gives the UK the role of “le demandeur”. Therefore, according to the EU official, the EU does not “give a damn” about Theresa May’s statement that no deal is better than a bad deal [Interview 04.04.18]. Let us assume that the EU is not negotiating with the UK over Brexit, due to the nature of the negotiations and of the EU itself, but is only performing a technical and administrative task. One way of modeling this in the framework of the threat game is to assume that the EU can only be a tough type by rule and, thus, cannot be negotiated with. This changes the game so that it is the UK that has to choose between accepting whatever deal the EU can offer (deal₂) and a no deal outcome. If the UK has a tough type (p), it will impose the threat and have no deal, if it is a weak type (1-p) it will not carry out the threat and accept the deal offered by the EU.

6.4.2 Game tree: The threat game with insufficiently severe threat

However, the EU official’s description of the EU is not the full picture. The EU can be seen as a coin with two sides. A rule based bureaucratic organization, is one side of the coin, while on the other side we find a political hinterland. The latter side is much more dynamic and consist of a political leadership which can change the course of the Union and be negotiated
with. But, as pointed out by Christopher Lord, in order for the EU to change its political course, consent from its member states is required. So far, in the context of the Brexit negotiations, the EU has managed to keep impressively united over a hard approach to Brexit. The EU has come across as so united that it seems easier to depict the EU as a unitary actor than depicting the UK as one. This is rather paradoxical given that the EU is an organization of 27 member countries and the UK a sovereign country. Against this backdrop, it does not seem likely that the EU and its members states will easily abandon its political foundations and yield to the UK’s threat.

The EU official dismisses all considerations of the no deal threat’s severity, both because the Brexit process is not a negotiation and because the UK is in no position to threaten. The first claim, that the Brexit negotiations are not negotiations, does not seem to fit the facts. But the latter claim, that the UK is in no position to threaten, somewhat matches the findings made in this analysis. In order to effectively threaten the EU, the threat must be both credible and sufficiently severe. Taking what has been said in this chapter into consideration, it does not seem probable that the threat of no deal will be considered as credible nor sufficiently severe by the EU. Consequently, it can be argued that the prospects for the UK’s threat of no deal to be efficient seems very small.

However little effective the threat of no deal seems at this point, some internal actors certainly believed that the UK could threaten the EU in various ways before the start of the negotiations [Christopher Lord Interview 06.04.18]. Some of the hard-Brexiteers even believed that the UK had a strong negotiation hand before the negotiation started, either based on the calculation that a no deal outcome would be mutually destructive and therefore not a desired outcome for the EU or the calculation that the UK could unilaterally promise to continue a Single Market relationship with the EU (ibid., Legatum Institute Report, 2017). Theresa May doubtfully shared any of these calculations, but she had to exhaust the no deal strategy which was calculated to work among some in the Conservative party, in order to move on to other more promising strategies [Christopher Lord, Interview 06.04.18]. This interpretation of the UK government’s motive behind the threat sees the threat in the context of a two-level game, where there are negotiations going on both within and between the two players. Christopher Lord thinks that “the British government spends much more time negotiating with itself than negotiating with the European Union” [Interview 06.04.18]. The EU official I talked to don’t think the UK government is negotiating with the EU when it uses the threat of no deal, but
with internal actors and the press [Interview 04.06.18]. According to this, the no deal threat is aimed at a domestic audience and a way for Theresa May to pacify the press and the hard-Brexiteers and keep them at bay. However, the threat may play several games at once and both be aimed at the domestic audience and the EU. This thesis has been limited to study the conditions for the UK’s threat to be efficient in the game being played with the EU. But, in order to corroborate the findings from the analysis concerning the threat’s credibility, I will end the analysis by looking at the UK’s second level and its respective win-sets. The objective of including two-level game considerations is to verify the analysis at the first level.

6.6 Two-level game considerations

In this thesis I have modeled the Brexit negotiations as a game between the EU and the UK at the international level with the assumption that the players are unitary actors. This measure has allowed me to circumvent a lot of complexity, but it also has some shortcomings as it does not take fully into account the actors’ internal level. Nevertheless, it can be justified as my analytical focus is on the strategic interaction taking place between the EU and the UK, and not on the negotiations taking place within the players between internal actors. When I choose to include considerations of the players’ second level it is with the purpose to corroborate the findings made in the analysis of the negotiations taking place at the international level. When assessing what is possible at the international level, studying the negotiating parties’ domestic levels is useful. The respective sizes of the players’ win-sets may say something about the possibility for the threat of no deal to be efficient (see presentation of Putnam’s framework in section 3.4). The UK’s win-set affects the threat’s credibility, while the EU’s win set affects the threat’s possibility to be sufficiently severe. I choose to only assess the UK’s second level and not the EU’s. This permits me to verify the findings about credibility from the analysis at the first level (see section 6.3.4) by looking at the UK’s second level. In the context of this thesis this limitation can be justified by both space considerations and because credibility considerations are relatively more important as the UK can affect the threat’s credibility, but not to the same extent its severity. Thus, in the following I will have a look at the UK’s win-set and assess how it affects the possibility for the UK’s no deal threat to be effective. The exploration of the UK’s second level serves as an analytic robustness test of the findings from the analysis on the international level and is not meant as a full two-level analysis of the negotiations. A thorough assessment of the players’
second level bypasses the primary concern of the thesis, is too extensive to be included here and is left as a task for further research.

6.6.1 Determining win-sets

In the Brexit negotiations a deal must be ratified at the UK’s and the EU’s second level. In Putnam’s two-level game, ratification theory makes up the formal link between the two levels, as any deal agreed at level 1 must be ratified at level 2. In this process the negotiating parties’ win-sets are of importance. Win-sets can be defined as “the set of potential agreements that would be ratified by domestic constituencies in a straight up-or-down vote against the status quo of “no agreement” (Moravcsik 1993, p. 23). From this logic of ratification, it follows that the choice for the constituencies is between the negotiated deal presented to them and the option of no deal (Putnam 1988, p. 437). This is also the case for the EU’s and the UK’s constituencies in the European Parliament, the European Council and the British Parliament who will ratify a negotiated deal.

The contours of the win-sets at level 2 are important to understand level 1 deals because of two reasons (Putnam 1988, p. 437-441): (i) the larger win-sets, the more likely a deal at level 1 is and (ii) the relative sizes of the parties’ win-sets will determine the distribution of gains. The former reason implies that agreement is only possible at level 1 if the parties’ win-sets overlap. Thus, the bigger the win-sets are, the more likely are they to overlap. The latter reason implies that a small win-set relative to the other player’s win-set can be a bargaining advantage. The negotiating parties’ win-sets affect level 1 deals and win-sets are again, in their turn, affected by different factors.

Putnam identifies three factors that are particularly important when determining win-sets (1988, p. 442-452). The first factor considers the effect of the distribution of power, preferences and possible coalitions among level 2 constituents on the win-set (Putnam 1988, p. 442). Putnam highlights the effect of the evaluation of a no deal outcome among the constituents: the lower the cost of no agreement, the smaller the win-set. The second factor considers the domestic level’s political institutions and the effect of ratification procedures on the win-set. The stricter the ratification rules, the smaller the win-set (Putnam 1988, p. 448). Thirdly, the size of the win-set also depends on the strategy used at the international level by the executive. Putnam identifies two basic strategies (Putnam 1988, p. 450): (i) to shrink domestic win-sets in order to increase bargaining leverage with the objective of a good deal or
no deal and (ii) to increase the domestic win-set in order to secure a deal with the objective to reach any deal rather than no deal. I will, based on these factors, explore the contours and size of the UK’s win-set. I will look on the UK’s cost of no deal, its ratification procedure and the strategy applied at the international level.

The no deal option

The costs of no deal, or rather the perceptions of the costs of no deal in the Brexit negotiations, among the constituents affects the size of the win-set. The lower the costs of no deal to constituents, the smaller the win-set because the constituents are less dependent on reaching an agreement. The no deal scenario in the Brexit negotiation do not represent the status quo, as in many other types of negotiations, but a whole new situation. A no deal Brexit means an unorderly withdrawal of a member state from the Union, which has no priors. The consequences of a no deal outcome for the UK and the EU are uncertain. However, all estimates of cost indicate that a no deal will hit the UK much harder than the EU.

Constituents may face different costs of a no deal or weigh different issues and elements differently. The size of UK’s win-set is bigger the bigger the group of constituents in parliament that face considerable costs of a no deal outcome. There exist different perceptions of the cost of no deal among the British constituents (see section 5.2). These differences stem from different evaluations of the two elements that the majority of the British constituents agree are most important for determining cost and benefits: economic growth and national sovereignty. Another important source of costs of a no deal is the Irish-boarder question. A no deal outcome will entail that the border between Ireland and Northern Ireland becomes a part of the EU’s external borders and, thus, a hard boarder.

So, how do the different political parties in the British Parliament, who are ratifying a potential deal, evaluate the cost of no deal? In Labour’s manifesto before the 2017 election it is stated that “leaving the EU with a no deal is the worst possible deal for Britain”. Hence, Labour evaluate the cost of no deal as bigger than any deal with the EU. For the Democratic Unionist Party (DUP), the Conservatives’ partner in government, a no deal outcome will be costly because it would mean that the boarder separating Ireland and Northern Ireland will become the EU’s external boarder and, thus, a hard boarder, and not a frictionless boarder as the DUP desires. Within the Conservative party there exists different views on the economic
cost of a no deal. However, a majority of the Tories seem to perceive no deal as a worst-case scenario.

**Ratification of a Brexit-deal**

Ratification procedures affect the size of the win-set, the stricter the ratification rules, the smaller the win-set (Putnam 1988, p. 448). Consequently, the structure of the ratification process of a Brexit deal at the end of the Article 50 negotiations will affect the UK’s and the EU’s win-set\(^2\). It has been decided by British MP’s that any final agreement with the EU must be ratified by parliament. A parliamentarian vote will be held sometime after a deal has been agreed and some time before the exit day on 29 March 2019. However, there is conflict over how a parliamentary vote should be structured in order to be “meaningful”. At this stage, it is decided that the vote will be a choice between the deal negotiated and no deal. Consequently, if a Brexit-deal is voted down, it will imply leaving with no deal and cannot have other interpretation, such as new negotiations or a reversion of Brexit. This structure of the vote serves to minimize the domestic win-set compared to not having any parliamentary vote to approve the deal negotiated by the government. However, if the chances of a no deal outcome to be judged better than a negotiated deal with the EU by British MP’s are considered low, as in line with what was said in the section on the no deal option above, the structure of the parliamentary vote does not really make the UK’s win-set so small (for similar arguments see Fowler 2017). Furthermore, as the Article 50 negotiations have a timeline of two years and a parliamentary vote will take place after the negotiations have been concluded, it is difficult to make the vote anything else than a binary choice between the deal presented by government and a no deal. This because it will not be possible to make changes at that point. The time limit, set out by Article 50, somewhat hinders the UK in shrinking its win-set by making its ratification vote stricter, as there is no time to negotiate further.

**The strategy used at the first level**

At level 1 both sides to a negotiation have the interest of increasing the opponents win-set. However, regarding their own win-sets, the parties face a tactical dilemma. A player may try to minimize its win-set in order to increase its bargaining leverage towards the opponent. This may be risky and lead to a no deal outcome because the win-sets no longer overlap. But if

\(^2\) On the EU-side a Brexit deal must first be ratified by the EP and then by the European Council.
successful, it gives the player a better deal. An actor has incentives to pursue this strategy if its objective is a good deal or nothing and it prefers no deal over a bad deal. If the player prefers any deal over no deal, then it has incentives to pursue a strategy that increases its win-set. What strategy an executive should choose depends on its preferences. But in a game of incomplete information the choice of strategy might reveal a player’s preferences and type. Knowing this, the player has incentives, regardless of its true type, to pursue a strategy to minimize the win-set in order to make the opponent believe it has a tough type. In order for the UK’s strategy of no deal to make the EU perceive the UK’s win-set as smaller, it must be credible. If the EU recons that the British parliament would back any deal, not only a “good deal”, the no deal strategy will not decrease the UK’s win set considerably in the eyes of the EU. The findings from the analysis of the no deal threat’s credibility suggest that the threat is not credible and, thus, does not serve to minimize the UK’s win-set. Another fact which further weakens the strategy of the no deal’s credibility is that the UK government has rejected proposed alternative ways of structuring the parliamentary vote even though restructuring could give stricter constrains on the UK’s win-set. If the British government really preferred no deal over a bad deal, such a restructuring could be beneficial (Fowler 2017).

6.6.2 Two-level game considerations – findings

Studying the UK’s win-set by looking at three main determinants suggest that the UK has a relative big win-set. This is mainly because a majority of the UK’s constituents perceive the costs of a no deal outcome to be high. Furthermore, the ratification procedure does not seem to put substantial constraints on the UK’s win-set, as it appears unlikely that a majority of the parliamentarians would judge a no deal outcome to be better than any negotiated deal. Thus, the strategy of “no deal is better than a bad deal” can be used at level 1 by the government without fearing that parliament actually will vote down a negotiated deal for a no deal. But the strategy cannot be expected to shrink the UK’s win-set as the EU will make the same assumption and recon that the British parliament will back any Brexit deal.

These findings from the exploration of the UK’s win-set are in line with and underpin the findings from the analysis of the threat’s credibility. The UK’s win-set seems relatively

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22 The EU has used its rule-based nature to pursue a strategy to minimize its win-set by claiming that a Brexit deal must be something the EU can offer or no deal at all.
expansive due to the high cost of no deal, minor constraints from the ratification procedure and little credibility connected to its “no deal is better than bad deal’’-threat. Consequently, the UK’s big win-set makes the threat of no deal seem little credible. I have not evaluated the EU’s win-set in this section, but in the light of the assessment of UK’s win-set, the EU’s win-set appears relatively small due to lower costs of no deal and stricter constrains caused by ratification rules and the strategy pursued at the international level.
7 Conclusion

Activating Article 50 has sent the UK out on a journey with an unknown destination. Unknown because the destination will be the result of the Brexit negotiations taking place under extreme uncertainty. In the context of these negotiations, the UK government has stated that “no deal is better than a bad deal for Britain”. This statement can be interpreted as a threat with a twofold motive, to threaten the EU in order to negotiate a better deal for itself and to keep internal actors, such as the press and hard-Brexiteers, at bay. The latter interpretation sees the statement as a threat in the game being played at the national level in the UK with the domestic actors as its primary audience. The former interpretation perceives the statement as a part of the game being played between the UK and the EU. I set out to investigate the role of the UK’s threat of no deal in the negotiations with the EU and, more precisely, the conditions for the threat to be efficient. For the UK’s threat to be considered efficient, it must make the EU give in to some of the UK’s demands. My research question was the following: “What are the conditions under which the UK’s threat of no deal will coerce the EU to make concessions?”. In order to answer this question, I apply a game theoretic model. The model is used to analyze the conditions of credibility and severity for the outcome of a deal beneficial to the UK (deal_1) to materialize, given different assumptions about the information available to the players.

This thesis uses formal modeling to study the concrete case of Brexit. To my knowledge no existing studies analyze the Brexit negotiations nor the UK’s use of the threat of no deal by explicitly modeling the negotiations game theoretically. Consequently, my thesis represents something new in the emerging literature on Brexit. By applying game theory to study the case of Brexit, I contribute to the literature by both providing new insights on the Brexit process and by offering a way to address the high levels of uncertainty in the Brexit negotiations. Through the application and adoption of Hovi’s original threat game to the case of Brexit I provide a method that can be used to address the big amounts of uncertainty in the Brexit negotiations, as well as in other situations of politics with great levels of uncertainty. However, the main contribution of this thesis is not the game theory itself, but the new insights into the Brexit process gained through the application of game theory. Modeling the strategic interaction between the UK and the EU as a game theoretic model makes it possible to predict and explain the actions of the two players by deducing equilibria. The main findings provide clarifications of the conditions for the UK’s threat of no deal to coerce the EU to
make concessions. Combining the conditions deduced from the threat game with knowledge about the case of Brexit obtained from various sources, such as interviews with key informants, public documents and speeches, provides an explanation of why it is unlikely that the UK’s threat of no deal will be efficient. Furthermore, the findings made in this thesis have a broader implication than just the case of Brexit. It contributes to the understanding of the process of withdrawal from the EU, the strategic use of uncertainty in international negotiations and of the role of credibility in bargaining situations, by looking at the case of Brexit.

Application of game theory to the case of Brexit demonstrates the utility of game theoretic analysis. The use of game theory is especially suitable when the political phenomenon to be analyzed involves strategic interaction under uncertainty, which is the case in the Brexit negotiations, because it provides tools to account for these features. One of the main advantages with game theory is the explicit nature of its assumptions (Gates and Humes 1997, p. 167). By making my assumptions explicit I have been able to distinguish which factors are important, such as the role of information, credibility and severity, and account for them in the analysis of the strategic interaction. The formal analysis provided in this thesis is explicit about the structure of the game and the deduction of equilibria, which makes the results replicable. My conclusions concerning the conditions for the UK’s no deal threat to be efficient are drawn from the equilibria analysis of my game and not on extra-game reasoning. However, in order to assess which of the equilibria deduced from the threat game seem more probable, extra-game reasoning is necessary, and I lean on knowledge about the actual case of Brexit to draw conclusions.

The game theoretic model applied is not meant to be a comprehensive representation of the negotiations, nor to address all of the negotiations’ complexities. Given the unusually complex process of Brexit, that would be an impossible task. The purpose of modelling the Brexit negotiations as a game theoretic model is rather to identify and account for relevant elements of the negotiations and for the role of uncertainty in order to identify equilibria conditions for the threat of no deal to be efficient. Applying game theory to Brexit has allowed me to cut through the vast complexity of the negotiations and focus on particular aspects of the process. By doing this, however, the thesis runs the risk of not being able to account for what is really going on due to model misspecification and underspecification. This is a shortcoming of game theoretic models, as well as of methodological techniques in
general. In order to account for and avoid such problems, I have been explicit about the assumptions taken, made the analysis formal and explicit and the conclusions clear.

7.1 The role of credibility and severity – findings and conclusion

The formal analysis demonstrates the importance of the threat’s credibility and severity in order for it to be effective. They are both necessary conditions for the no deal threat to coerce the EU to give concessions. By first analyzing the model under complete information and then under incomplete information I explicitly take account of the role of information. The conditions for the threat to be effective are less strict under incomplete information than under complete information as the former opens up for misrepresentation of information by the two players. The complete information game assumes that the players’ preferences and payoffs are common knowledge. In reality, the actors in the Brexit negotiations face high levels of uncertainty. Thus, the players’ beliefs become relevant. In a game of incomplete information, the players must rely on their beliefs about the other player’s type when making decisions. To make the opponent move in a desired way, a player can misrepresent information to manipulate the opponent’s beliefs.

The equilibria of the threat game under complete information (chapter 5) predict that in order for the UK’s threat to be credible, the EU must know that the threat will be carried out if it does not yield. The equilibria of the threat game under incomplete information predict that in order for the UK’s threat to be credible, it is sufficient that the EU believes that the threat will be carried out unless it yields. For the no deal threat to be sufficiently severe in the game of complete information it must make the EU prefer to yield to the threat rather than standing firm and have a no deal outcome. In the game of incomplete information, the EU must believe that not yielding to the threat incurs higher costs than yielding, in order for the threat to be sufficiently severe.

When assessing which of the deduced equilibria seems more probable under incomplete information, I conclude that it seems little likely that the necessary conditions for the threat to be effective will materialize. This assessment is based on information about the actual case of Brexit and predicts that the threat will neither meet the condition of credibility nor severity. These findings provide an explanation for why the UK’s threat of no deal has not proved
effective so far and for why it probably not will coerce the EU to make concessions. The explanation is based on considerations about the different sources of costs and benefits that the UK and the EU are balancing, the players’ beliefs and their win-sets. According to the findings in this thesis, the UK’s threat of no deal will not serve as an effective tool for the UK to obtain a better deal. Accordingly, the unknown destination of the UK’s Article 50 journey will most likely be a deal which is in line with the EU’s demands and, thus, a “bad deal” for the UK.
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