News Focus

Opportunity knocks

Brexit could have a damaging effect on the Iberian economies and the future looks very uncertain – however, it also presents opportunities for Spanish and Portuguese law firms as well as potentially making Iberia a more attractive business base

Well, it actually happened. Despite many thinking it would never come to pass, the British public have indeed voted to leave the European Union. So, as the full implications of the result of the UK's referendum continue to sink in nearly two months later, where does this leave us?

Unfortunately, there is no easy answer to that question. It seems that Europe has entered what could be an extended period of uncertainty, which could potentially last as much as 10 years, according to some observers. The bad news is investors hate uncertainty, but as one partner at a "magic circle" firm commented in the aftermath of the referendum: "Uncertainty creates a market for lawyers." In addition, there is an even bigger opportunity for Iberia, and Spain in particular, to attract businesses looking to relocate from the UK, but will this opportunity be taken?

Though it is a little soon after the event to predict what impact Brexit will have on the economies of Spain and Portugal, the initial prognosis is not good. "It is still too early to make a reasonable forecast of how Brexit will affect the Iberian economies, although the IMF, among others, has recently predicted it will have a negative impact on the GDP of both Spain and Portugal," says Juan Carlos Machuca, partner at Uría Menéndez.

Indeed, Brexit will affect deal flow around the world. Baker & McKenzie's Madrid-based partner Enrique Valera says that, "unless an orderly and swift Brexit process is followed", the post-UK referendum global M&A market could see a deficit of up to $1.6 trillion. Meanwhile, Machuca says: "Brexit has created a great deal of uncertainty among market players, which is currently putting the brakes on investment flows." He adds that all sectors in Spain are affected by this slowdown, but the tourism, residential real estate and export industries are particularly so.

Cancelled investments?

The financial and telecommunications sectors will also suffer due to Brexit, according to King & Wood Mallesons partner Joaquín Sales. With specific reference to the financial sector, he adds that the depreciation of the pound could have a significant impact for the Spanish economy in that the "most relevant financial institutions are currently operating in the UK and a considerable share of their assets and profits come from their UK businesses".

Brexit may also have a negative impact on the Portuguese economy. Sara Estima Martins, partner at PLMJ, points out that, in 2015, the UK was the fourth biggest destination for Portuguese exports, particularly those in the automotive, textiles and food sectors. "The UK's exit may have some material negative impact on the Portuguese economy – moreover foreign investments by UK companies in Portugal may also be cancelled or suspended." However, Estima Martins does offer some hope. "We should keep in mind that Portugal and the UK have the oldest active treaty in the world – while its application has been put on hold while the two countries were part of the EU, it seems possible that such treaty is re-enacted after Brexit, allowing special relationships between the two countries."

A decade of doubt?

Unfortunately, the uncertainty that is making investors nervous is unlikely to end any time soon. Pedro de Gouveia e Melo, a lawyer at MLGTS in Lisbon, says that an agreement between the UK and the European Union on the UK's exit "will probably not happen in less than three years' time, and, considering recent precedents on complex international trade deals – may even take up to a decade to resolve". He adds that the immediate negative effects for the Portuguese economy will arise from this uncertainty, and for an economy that is just "starting to recover from a serious crisis, this uncertainty is not good news".

How will Brexit impact on Spain and Portugal's law firms? Sales speculates that there may be a decrease in transactional work, adding that with the IMF predicting slower GDP growth, "lower growth generally means less activity for law firms." However, there could be benefits. Though, Machuca acknowledges that in the run-up to the referendum, and in its immediate aftermath, firms suffered to an extent that some transactions were put on hold, he also believes there will be some positives for lawyers in Iberia. "Perhaps, given the current uncertainties, clients that were keen, in the past, to accept English law as the law governing their contracts will now be more reluctant to do so," Machuca says. "There will be a long and possibly painful transition period in which we will not know how English law will be applied and how the exit treaty will be implemented – however, over time, those English laws may be repealed or amended and will gradually deviate from the EU rules." Consequently, Machuca anticipates that UK law firms will be "fighting to demonstrate the continued efficiency of English law" and that continental firms will seek to take advantage of this period of uncertainty.

However, Paula Gomes Freire, partner at Vieira de Almeida in Lisbon argues that English law will retain its status. "There is debate as to whether Brexit could impact the popularity of the choice of English law for parties in cross-border commercial contracts and hence benefit local law firms as local laws would take over English law," she says. "I see this as unlikely and that the 'choice-of-law-landscape' will pretty much remain as is – English law is popular because it is comparatively certain, stable and predictable and Brexit will not change this."

Meanwhile, Portugal is also suffering from a slowdown in transactional activity. Gouveia e Melo remarks: "We have already witnessed international clients that were exploring business investments in Portugal abandoning a prospective deal because of the uncertainty." However, there are some grounds for optimism in Lisbon, according to Estima Martins. "The pound devaluation – and the subsequent devaluation of UK assets – may also create valuable M&A opportunities that compensate for the negative effect arising from the uncertainty," she says.

More work for law firms?

Similarly, the depreciation of the pound could potentially lead to an increase in workflow for lawyers in Spain. "It [the pound depreciation] may create an opportunity for Spanish companies and financial institutions to carry out strategic investments in the UK and that may result in more activity for law firms," says Sales. Similarly, Machuca is able to find some positives and refers to the words of Winston Churchill, who once said: "The optimist sees the opportunity in every difficulty." According to Machuca, clients will need lawyers to guide them through the process of altering the way they plan and carry out investments, as well as changing their relationships with their customers, suppliers, employees and competitors. "Factors such as the market and economic conditions, fluctuations in prices and disputes over the interpretation of existing contracts are already providing opportunities for a number of our practice groups to work on transactions and litigation, as well as advise on a wide array of areas, from data protection to tax," he explains.

Relocating to Spain?

However, there may be an even bigger opportunity for the Spanish economy. Machuca points out that Brexit will mean businesses have to review and restructure some parts of their activity to adapt to a new era in which UK and EU countries no longer have harmonised legal frameworks relating to tax, financial services and data protection. "This restructuring will provide a massive opportunity for us to attract these businesses to our country," he says. "The authorities should work together and make it a priority to develop a strategy to attract industries and entities that may be thinking about relocating – in the Iberian peninsula, we can offer fantastic infrastructure, plentiful office space, a young highly-skilled workforce, an excellent climate and attractive labour costs as reasons to set up their European headquarters here."

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Yet there are doubts as to whether Spain will be able to capitalise on this opportunity (see our Global Report on page 30). Ashurst partner Eduardo Gracia says Spain would be better able to benefit from uncertainty in the UK if it had a stronger government. He adds: "It would be better if Spain was less bureaucratic, Anglo-Saxon investors would fear this [bureaucracy in Spain]." However, it remains a fantastic opportunity, and it is up to the politicians, business leaders and lawyers of Spain to do the best they can to take it.