GLOBAL
ECONOMY

11/18

Brexit special:

How things stand to develop from here – our in-depth analysis

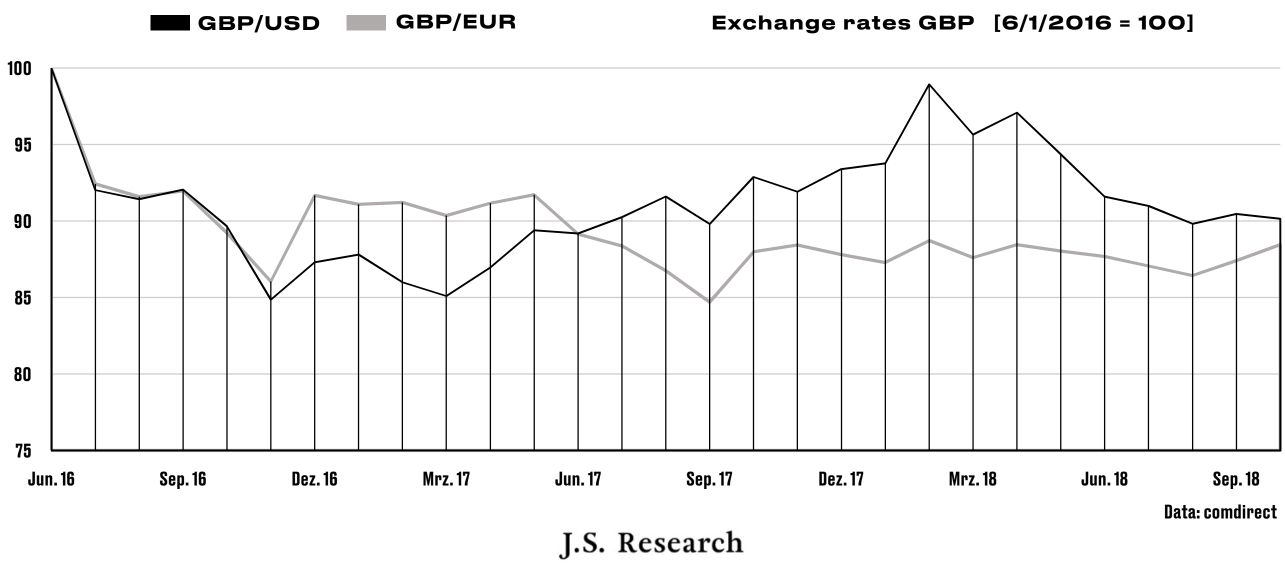
J.S. Research

A deal in Brussels is almost done – but then…

The Brexit process has arrived at its moment of truth. With an agreement between the UK and the EU seemingly imminent at the end of this month, all will then depend on Parliament in Westminster – which is where trouble lies ahead. As repeatedly stated over the past months, our analysis of the parties and factions in the Commons yields a sobering result: Just as numerous paths lead to a rejection of the deal reached in Brussels – with the gathering of Eurosceptic Tory MPs, the European Research Group (ERG) holding the balance –, only one with cross-party support results in the deal being passed. So if Parliament strikes down the Brussels accord, what comes next? Does it inevitably mean a no-deal Brexit? Might there be a change of government, and if so, with what consequences? And what would have to happen in order to even rescind Brexit altogether? To answer these complex questions, we have decided to dedicate this whole issue of our monthly bulletin to give you the most likely path of development in chronological order. The first juncture, of course, is Parliament's vote on the Brexit deal to be cut in Brussels. If, against all likelihood, the deal actually scrapes by, almost everything is fine for the time being – simply because then, the ratification of the deal by all 27 EU member states is all but a foregone conclusion. There is, however, a residual risk that the relatively pugnacious European Parliament, which has to agree to the deal, too, might vote it down. Assumed that isn't the case, the transition phase agreed early on in the negotiations will kick in on April 1st simply prolonging current conditions and thus changing nothing, so that the next round of talks on trade and the future relationship between the UK and the EU can begin. Though these will be fraught with intricacies and pitfalls, too, they no longer decide on the matter of Britain virtually crashing out of the EU without any agreement in place whatsoever. Alas, that is the relatively less probable path of development. After the shock

Deadlocked Parliament is to strike down Theresa May's deal

resignation of no other but the Brexit Secretary himself, and for the reasons given by us time and again (see earlier issues of this bulletin), the risk is considerably higher that the deal is rejected in the Commons, either by a majority of ERG MPs



with or without support by Labour Brexiteers, or even by a bizarre coalition of Brexiteers and Remainers, probably as soon as in early December. Next in line would be the all but inevitable fall of Theresa May's government in such a scenario, which in turn would result in a new Tory government, if fleeting. Though it is the expressed intent of the Labour leadership to force a general election over the matter of Brexit, the Tories remain the largest party in the current Parliament and would at least try to form a new government. Such a step, however, will necessitate a leadership election within the Conservative party in the first place, taking up weeks. That election itself will then probably produce a relative Eurosceptic such as Sajid Javid or even an outspoken Brexiteer such as Boris Johnson as new Tory leader. Would that already necessarily result in a break-down of the negotiations and, consequently, a no-deal Brexit? No. Because almost by default, the first measure taken by the government once the new Prime Minister will have been kissing hands would be to present the Commons with a motion to ask the EU for an extension of the negotiation phase framed in Article 50 of the EU treaty, currently set to eject the UK from the EU on the eve of 30 March 2019. There is no way around such a motion, because if it's not presented by the government, it will undoubtedly be put on the order paper by Parliament itself one way or the other. It is reasonable, then, to expect a huge, non-partisan majority to vote for such a motion, because more time is playing into just about everyone's hands – with the exception of visceral Brexiteers who would find themselves powerless in such a situation. Then follows the most crucial of all turning points: The EU's reaction to such an application by the UK, or better: The reaction of each and every single member state of the EU's remaining 27. From there, we thus have to draw the map for two scenarios: the EU27 agreeing and the EU27 rejecting Britain's demand, respectively. Either way, that is, during the time needed to organise the formal reply of all 27 EU member states, Labour would certainly try to press home its advantage against the new Tory government still torn by internecine warfare over its Brexit strategy, sooner or later (depending on the EU27's reaction) resulting in a general election in the first quarter of 2019. Interestingly, it is not necessary to predict that election's result to know what path Brexit might take from there, because there already is cross-party support for a soft Brexit in the House of Commons, so that every new party majority resulting from that election would not change the votes on matters of Brexit (that change would only be augmenting the soft-Brexit support, anyway).

EU's consent to extension of Art. 50 is crucial

Back to Brussels: If the EU27 rejects the UK's application, then the game is truly and unequivocally over: Time would simply run out before a deal can be ratified, and the dreaded no-deal scenario kicks in. Deplorably, that again is way more likely than a unanimous consent by the EU member states in time to avoid a no-deal Brexit; loads of experience with the EU's often drawn and convoluted arrival at decisions allows for no other analysis. Brexit in particular would provide one or the other member state with huge leverage to eke out some individual gain by withholding its consent as long as possible, thus wreaking havoc with the tight schedule. If, however, the member states agree to the UK's demand, it is highly likely that after the general election envisaged above and Labour's taking office in its wake, the new government would then rejoin the negotiations with the EU27 which, in due course, ought to result in a withdrawal agreement one way or the other. That is what the so-called "meaningful vote" of the Commons has been intended by its proponents to yield all along: In this scenario, Parliament with its cross-party majority against a no-deal Brexit would take the driving seat, regardless of the party in office. To sum it all up, just read this analysis backwards through time – and it yields these two key insights: The EU's preparedness to accept an extension of the timeframe stipulated in that infamous Art. 50 is absolutely crucial to avoid a no-deal Brexit, even more so than the outcome of the Commons' vote on a Brexit deal pending in the weeks ahead. Yet that latter vote in itself is of great relevance, too: If the Commons agree to the deal presented to it by Theresa May, than crisis point has at least been successfully kicked down the road again – only to re-emerge in the ensuing negotiations on Britain's future relationship with the EU. What you probably have missed in our analysis is the so-called People's Vote, a second referendum on the UK's remaining in the EU with the aim to rescind Brexit altogether. That is because it still is an absolute outlier: The only place in which it might come about is the scenario

People's Vote is a total outlier

described above where, first, an extension of Art. 50 has been obtained and, second, the government then if office surprisingly opts not to continue the negotiations with the EU, but rather to hold that referendum. Judge for yourself whether that's a likely path.

Statistical Bulletin

Wage growth (y/y)

Netherlands (Oct.): +2.3% ↑ Wages are on the rise in many economies not only in the G10, but among emerging economies, too. The Netherlands are no exception: With unemployment at multi-year lows, labour supply shortages start to bite.
UK (Sep., rolling 3m): +3.0% ↑ Speaking of labour supply shortages, ask the Brits: In the run-up to Brexit, immigration from the EU has fallen to troughs unknown for years. Though fêted by some, employers in industries such as agriculture, basic services, and meat processing are feeling the pinch, and wages behave accordingly.

Retail sales (Sep., y/y)

Singapore: +1.9% → Singapore's consumers have re-emerged from their relative reticence over the summer, if in a decidedly modest manner. Sales growth, too, was not driven by a general upturn but by selected product groups only.
Czech Rep.: +1.4% ↓ Shoppers in the Czech Republic have recently begun to cool down their profligacy displayed in the past three years, and the momentum of that might yet take growth figures into negative territory in the months ahead.

Imports (Oct., y/y, USD)

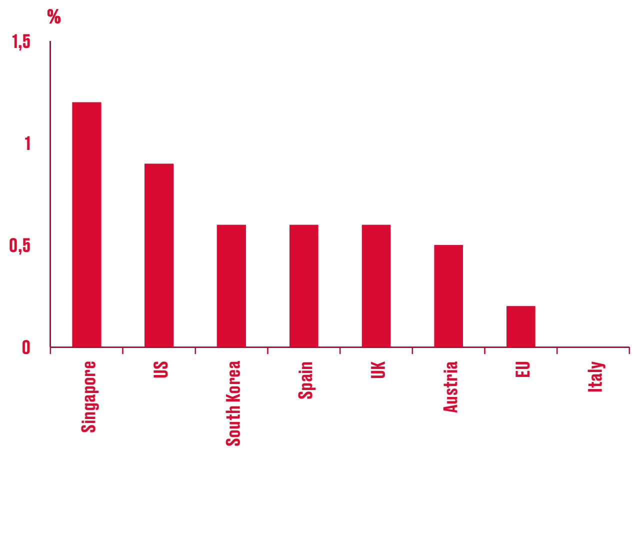
Brazil: +17.7% ↑ Brazil's imports are an indicator of what the economic effect triggered by the election of Jair Bolsonaro might be looking like. Though the economy still is mired in a recessive environment, the new President's (for all his political shortcomings) taking office takes away the choking political uncertainty hanging over the country all over the past two years.
China: +21.4% ↑ Jugded by its import activity only, the Chinese economy does not appear anywhere near cooling down. But beware: First, these figures are computed in US dollar, hence a good part of the growth comes from currency effects when the Renminbi has devaluated quite a bit against the greenback. And second, Chinese trade these days is distorted by the Sino-American trade war where traders on both sides of the Pacific pre-empt those tariffs by ramping up their inventories.

Industrial production (y/y)

China (Oct.): +5.9% ↓ The picture becomes more complete when looking to data more related to domestic activity such as industrial production: This metric is stuck at its troughs, and even though healthy in absolute terms, it yet indicates that the Chinese dragon has been losing a good deal of its fire.
France (Sep.): -1.1% → France seems to have been experiencing a veritable freeze over the late summer, just as other Eurozone countries and Germany in particular. As of yet, the statistic looks not too bad, considering the decent growth before. But September's has been only the third contraction in over a year, and the first in excess of one percent.

GDP growth (Q3, q/q, real)

The US are still playing in another league when it comes to economic growth these days. Fired up by the tax cuts and other fiscal stimuli by the Trump administration, the American economy remains under full steam. Yet at least in the third quarter, is has to share its top position with Singapore: Even though facing collateral damage from the Sino-American trade war, the very anticipation of that triggering early orders by traders around the Pacific and frantic cargo shipments have aided the Lion City's economy to stage a veritable surprise with growth numbers far beyond expectations. Alas, we do not believe this halcyon to stay, as our economic indicator for Singapore, the SiNGES indicates (see our website).



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