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UK UPDATE - THE ONLY WAY IS BREXIT

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Gossip, denial, multiple stories that are somehow linked... is it a reality TV show? No, it is Brexit. Not for the first time since the UK voted to commit an act of economic and political self-harm in June 2016 are events seemingly building up to some big moment. Next week, the House of Commons will debate and vote on the UK's European Union (Withdrawal) Bill following a series of major amendments proposed by the House of Lords. Prime Minister Theresa May's Brexit 'war cabinet' is currently deciding its preferred customs policy on the Irish border and has put forward a revised version of the 'backstop' plan - in case the Irish border question cannot be solved. And finally, Brexit is on the agenda at the upcoming June 28-29 EU summit – the penultimate summit before October when the UK-EU withdrawal agreement needs to be finalised in order to be ratified in the UK and EU parliaments in time for Brexit (29 March 2019).

In principle, all three issues have the potential to change the course of Brexit. Whether they will in practice is a very different matter. We discuss them in turn:

The Brexit bill

Beginning on the 12 June (next Tuesday), the House of Commons will debate, amend and vote on the UK's European Union (Withdrawal) Bill. The upper chamber (House of Lords) and the lower chamber (House of Commons) of UK parliament must both agree and pass bills before they can become law. Although the bill could go through a back-and-forth process between the two houses, colloquially called 'ping-pong', the unelected upper house usually offers only one set of amendments for the elected lower house to consider. As the Commons de facto has the final say, the most relevant question is how the lower house will respond to the Lords' 15 amendments. Three of the amendments are potentially significant:

- 1) That the UK should remain in the European Economic Area (EEA) – the so-called Norway model. The government is likely to win the vote to reject this amendment despite reports that around 12 Conservative rebels would support it. Even though the Labour Party's official policy under socialist leader Jeremy Corbyn is for the UK to pursue 'the softest Brexit possible', Labour's 'shadow' Brexit secretary Keir Starmer has made it clear that remaining inside the EEA is unlikely to get large support from his party.
- 2) That the government must report on its efforts to agree a customs union. Because this amendment does not explicitly commit the government to agree a customs union but just report on its 'effort to do so', it is unlikely that many Conservative MPs would risk wasting their political capital by voting in favour of this amendment and thus against the government
- 3) That parliament must have a 'meaningful' vote on Brexit. This is the big one. While the current bill already contains a similar line, the Lords' new version is more powerful. Instead of simply giving parliament a yes or no vote on the final deal, the new amendment states that, if parliament vote down the final deal, the government must then follow the instructions of parliament in future negotiations, i.e. parliament will take control of Brexit. The government has proposed to soften this amendment materially (its version states that ministers are given 28 days to make a statement to parliament if the final deal is voted down). If the government loses this vote and the Lords' amendment stands, it would force PM May to further soften her stance on Brexit in order to avoid parliament rejecting the final deal.



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The Irish Border

Can the UK leave the EU customs union but preserve the current status quo of no physical border on the Irish Isle? This has proven to be the most difficult issue so far in the negotiations. The UK government is currently considering two options: 1) a customs 'arrangement' (UK collects duties for the EU for goods passing through the UK but destined for the EU market) – this is May's favoured solution; or 2) 'maximum facilitation' (UK uses technologies such as cameras and barcodes to limit the frictions on UK-EU trade at the border) – the Brexiteers' favoured solution.

So far, Brussels has said that neither of the UK's proposals would achieve the desired result of maintaining the Irish status quo. As a result, it is likely that a so-called 'backstop' plan will need to be implemented after the transition period finishes at the end of 2020. The UK government will seek to change the current wording of the backstop option already agreed last December to keep the whole of the UK aligned with the EU customs union and regulations for a time limited period (intended to be one year) – whereas the original version would only apply to Northern Ireland and include the single market with no time limit. The Democratic Unionist Party of Northern Ireland, with whom the Conservatives are in government, will insist on the new version as they will not accept any arrangement that would assign Northern Ireland a different legal status than mainland UK. Will the EU accept the UK's change to the backstop? That is not clear. The EU may possibly seek to change the backstop so that the UK would remain inside the customs union after Brexit with no cut off date – but with the option to renegotiate the status in the future.

June 28-29 EU Summit

The upcoming June EU summit was set as the original deadline to resolve the Irish border problem. Unless May's Conservatives capitulate and accept that the UK will remain inside the customs union indefinitely after Brexit within the next three weeks, which seems unlikely, the deadline will be missed. It will instead be pushed to the October 2018 EU Summit – when the final framework deal should be ready. We doubt that the EU or the Republic of Ireland – which has a de facto veto on the EU side – will soften their position to accept one of the UK's customs proposal before October. When faced with the option of a hard Brexit (25% chance), or accepting a deal that will keep the whole of the UK inside the customs union after the transition – in principle but maybe not in name – we expect the UK to choose the latter. That is our base case.

For more on the different Brexit scenarios, please see [Brexit hurts already: GDP analysis and outlook](#).

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