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## **BREXIT UPDATE: UK-EU STRIKE A DEAL, SHOWDOWN IN PARLIAMENT AHEAD**

### Berenberg Macro Flash

#### **Progress yes, but the biggest challenge is still ahead**

The news from the UK last night that UK and EU negotiators have agreed the draft text of the Withdrawal Treaty is merely a pre-condition for the final political agreement on Brexit. Before we can drop the no-deal hard Brexit risk - 20% chance - UK Prime Minister Theresa May will need to convince her party and parliament to back her deal.

#### **What do we know about the deal so far?**

Not much beyond the broad strokes. UK and EU negotiators have reached a draft technical agreement that encompasses: (1) the Brexit bill; (2) a transitional plan – the UK will likely remain in the single market and customs union until the end of 2020 or 2021; (3) the political declaration about the broad aims for future trade - a comprehensive trade deal in goods with some limited access in services; and (4) a so-called “backstop plan” that ensures the Irish border remains open in case the UK and EU have not agreed a trade deal - which achieves this - by the end of the transitional period. The final point is the most contentious among hard-line Brexiteers within the Conservative ranks and with the DUP (Democratic Unionist Party) whom the Conservatives rely on for a majority in parliament.

*The FT reports that the backstop plan for the Irish border includes a U.K.-wide customs union and that the specific Northern Ireland “backstop to the backstop” insurance policy has been dropped. While this could help May quell DUP fears that the deal cannot result in a border down the Irish Sea, Hardline Brexiteers will probably balk at such an agreement that could keep the U.K. in the customs union indefinitely. The U.K. will not be able to unilaterally withdraw from the backstop as some hardline eurosceptic ministers had hoped.*

#### **What happens next?**

Following one-on-one meetings with her cabinet ministers last night, PM May will hold a cabinet meeting to review the deal at 2pm GMT today. If the UK cabinet approves the deal, the government will likely set out a schedule for parliament to debate and vote on the final Brexit bill. As we have argued before, PM May is only likely to have agreed to a technical deal with the EU if she thinks she can get it through parliament. If this is indeed the case, expect her to try to get the deal passed as soon as possible. Meanwhile, the UK and EU are apparently aiming to hold a Brexit summit on the 25 of November. This will only happen if May's cabinet signs off her deal today. Otherwise, it could be back to the negotiation table (unlikely but not impossible).

#### **Big challenge ahead for May**

Agreeing the draft deal with the EU was the easy part. As Chart 1 shows, the Conservative-DUP alliance only has a 13-seat working majority in parliament. The DUP threatens to vote against the deal if PM May has committed to a backstop agreement that would divide the UK. Meanwhile, some hard-line Brexiteers within the Conservative ranks that seek a harder version of Brexit also threaten to vote down the deal. Until the text of the agreement is published, and the various Brex-



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it-factions of government take their positions, it is difficult to judge exactly how the numbers are shaping up ahead of the parliamentary vote. Suffice to say that, the Prime Minister may have a political mountain to climb. While the whips are likely to be already doing the rounds in her own party, May will probably be forced to court opposition bench MPs to boost the chances of getting the deal through.

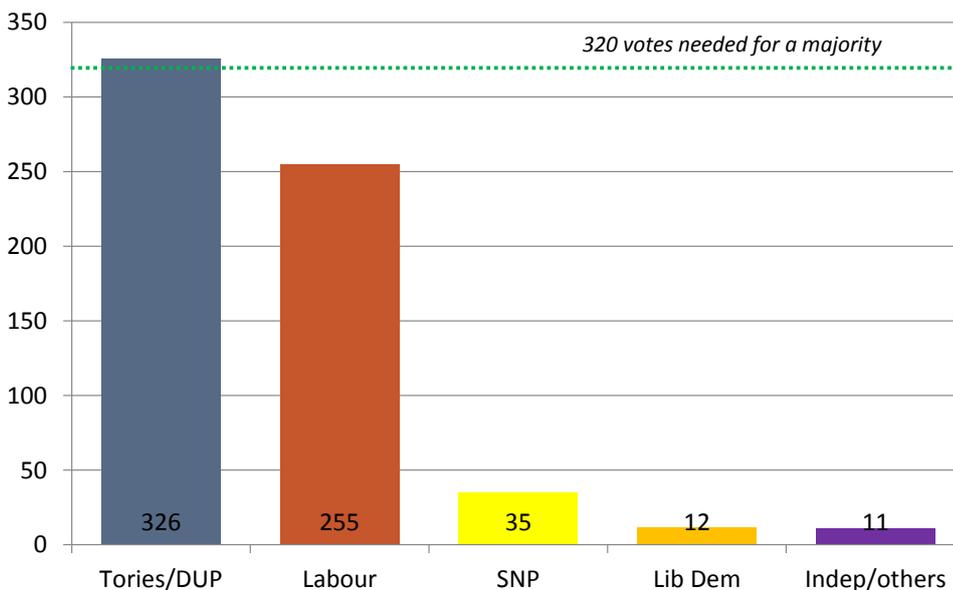
### 80% chance of a deal

We see a 60% chance that the UK parliament will pass a deal by mid-December (the end of November if we are lucky), and a further 20% probability that the UK will accept such a deal, or an even softer version of Brexit, after some initial political turmoil just in time for Brexit day 29 March 2019.

### UK set for a growth spurt if parliament passes the deal

The prospect of a deal presents considerable upside potential for the UK economy over the medium-term. Just as the market consensus overestimated the extent to which the UK economy would soften after the Brexit vote, we think the consensus is now underestimating the extent to which growth will pick up next year following a deal. Domestic fundamentals are in good shape. Driven by stronger consumption and business investment, we look for UK real GDP to accelerate from 1.3% in 2018 to 2.0% in 2019, before slowing to 1.8% in 2020. (Bloomberg consensus 5 November: 1.5% (2019) and 1.7% (2020)). See ['UK: growth spurt ahead if Brexit deal is struck'](#) for more detail on our outlook.

**Chart 1: May's slim working majority makes for tricky balancing act to pass a Brexit deal**



Source: UK Parliament (<https://www.parliament.uk/mps-lords-and-offices/mps/current-state-of-the-parties/>). Only 639 of the 650 seats in the House of Commons are active. To calculate the active seats remove: a) the four neutral seats which go to the speaker and the three chairs of the ways and means committee (two each for Labour and Conservatives); and b) the seven seats that Sinn Fein hold (this party does not participate in parliament). A further adjustment must be made to calculate the majority: two MPs that won Conservative seats in the 2017 election have been removed from the party – they now sit as independents but vote with the government.



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