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BREXIT UPDATE: WILL PARLIAMENT PASS THE DEAL?

Berenberg Macro Flash

Critical days ahead

If UK Prime Minister Theresa May can survive the next few days, the chances that the UK parliament will pass her Brexit deal could rise. She has already vaulted the first major hurdle when, last night, the UK cabinet decided to accept the Withdrawal Treaty text that UK and EU negotiators had agreed on Monday. UK news reported that nearly a third of her cabinet did not support the deal. This divide at the top of the UK government highlights the major challenge that lies ahead for May. The Conservative-DUP alliance only has a 13-seat working majority in the House of Commons. Any small group of MPs within the government could theoretically scupper the deal. For the time being, the heightened uncertainty is likely to temper any market optimism that the UK will avoid the no-deal hard Brexit risk (20% chance).

What to watch out for next?

While the UK parliament will probably begin to debate the Withdrawal Agreement in the coming days, it cannot vote and pass the deal until it has been formally agreed by the UK and the EU on 25 November at a special Brexit summit. During the next ten days markets will be watching carefully for cues on how likely it is that the UK passes the deal. We will focus on two issues: (1) will May face a vote of no confidence; and (2) will any senior ministers resign?

While a vote of no confidence in May would panic markets, and the chance of such a vote is probably quite high at this stage, the likelihood that May is actually ousted is low. 48 Conservative MPs would need to support the motion to hold a vote of confidence in May. However, with no obvious challenger that can carry a majority among Conservative MPs, and probably, with no party majority to bring her down in a vote of no confidence (there are 315 Conservative MPs in the House of Commons), May is probably safe. Since whoever replaced May would face the same challenges as her, any moderate that could carry a majority within the Tory ranks probably does not really want the top job at the moment. Keep in mind, if May survived such a vote, her MPs would not be able to make another such challenge for another 12 months.

The deal is contentious among both Brexiteers and Remainers. The bigger risk, in our view, is that a significant number of senior ministers resigned from May's government. Although no senior ministers have resigned yet, it is still early-doors. It took two days for ex-Brexit Secretary David Davis and ex-Foreign Secretary Boris Johnson to resign after May's cabinet agreed on the so-called 'Chequers-plan' back in July. Over the next few days, as MPs begin to comprehend the implications of the 585 page withdrawal agreement, we may be better able to judge the level of genuine support for May's deal. A couple of resignations would not change the outlook. If the senior members of the cabinet stick together and continue to support the deal, May probably has a good chance of carrying the party. If not, the deal could be dead on arrival.



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The key points from the deal

- The UK will enter a transitional period from 30 March 2019 until the end of 2020. During this period the UK will remain part of the economic framework of the EU (i.e. the single market for goods, services, capital and labour, and the customs union). Although the UK will leave the political institutions of the EU on 29 March 2019, it will continue to apply EU law in full during the transitional period.
- There is a one-time option to extend the transitional period for an undefined period if, by July 2020, the UK and the EU have not yet agreed the terms of future trade that meet the objective of maintaining an open border on the island of Ireland, while preserving the integrity of the UK and EU internal markets. The option to extend the transition had not been widely anticipated ahead of the publication of the draft agreement.
- To ensure the Irish border remains open, the agreement includes a special protocol for Northern Ireland that covers the unique arrangements between the UK and the Republic of Ireland, including the common travel area, that predate the UK's EU membership. This protocol includes the details on the "backstop plan" that ensures the Irish Border remains open under all circumstances, most notably, in case the UK and the EU do not agree new terms of trade – that achieves this – by the end of the transitional period. Under the backstop agreement Northern Ireland would be bound to the rules of the EU single market for goods – potentially implying checks on some trade between Northern Ireland and Great Britain. That UK will not be able to exit the backstop unilaterally is a major bone of contention among hardline Conservative eurosceptics.
- The backstop is underpinned by an EU-UK wide customs unions. This prevents a customs border between the Northern Ireland and Great Britain. PM May probably hopes this will be enough to get the DUP to support her deal. Although the DUP have not yet fully rejected May's deal yet, the early signals from senior DUP MPs are not promising.
- The UK will pay a financial settlement of around EUR45bn – according to UK Treasury estimates. Most will be paid by 2025, but some payments such as for EU officials pensions will last until 2064.
- Existing EU residence and social security rights will be maintained for the c3m EU citizens living in the UK and the c1m UK citizens living in the EU.
- UK and EU negotiators also set out a short seven page political declaration on the future relationship that sets out objectives for an economic partnership - goods and services trade (including financial services), a security partnership and any necessary institutional arrangements.

Prime Minister May has 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. 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.

Less uncertainty on the EU side

Because chief EU negotiator Michel Barnier had operated during the negotiation within a mandate agreed by the EU27, the chances of the deal not passing the necessary political steps on the EU side is lower than in the UK. We do not expect objections of substance that could seriously



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derail the process on the EU side. That EU Commission President Jean-Claude Juncker and EU Council President Donald Tusk have publicly backed the deal supports this view. EU27 national governments are currently checking the withdrawal agreement. Their ambassadors will meet by the end of the week to share assessments of the agreement. At this meeting, national governments could voice any objections.

As long as “nothing extraordinary happens” as put by President Tusk earlier today, there will be an EU Council meeting in order to finalise and formalise the Brexit agreement (scheduled for Sunday 25 November - starting 9.30 am). Note, while the Withdrawal Agreement only needs a qualified majority to pass through the EU council, any future trading agreement will probably need to be agreed by all EU parliaments. (*A qualified majority is as at least 55 % of the members of the Council representing the participating Member States, comprising at least 65 % of the population of these States*)

Above consensus – the economic outlook

The prospect that the UK will pass the deal presents considerable upside potential for the UK economy over the medium-term. 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 15 November: 1.5% (2019) and 1.6% (2020)). See ['UK: growth spurt ahead if Brexit deal is struck'](#) for more detail on our outlook.

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