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BREXIT: MPS REJECT WITHDRAWAL AGREEMENT - WHAT HAPPENS NEXT?

Berenberg Macro Flash

On the date that the UK was due to leave the EU the British parliament has voted against the Brexit withdrawal agreement (344 against, 286 for). We make three key observations:

1) The default outcome is a hard Brexit (15% risk) on 12 April unless the UK and EU can agree to a lengthy extension and a path forward;
2) The onus to find a Brexit solution on the UK side is now on parliament which is due to hold the second round of so-called 'indicative votes' on Monday;
3) The UK is potentially heading for a lengthy delay that could end with a snap election and/or second referendum.

Unlike the previous two votes where parliament had rejected the so-called 'May deal' which included the withdrawal agreement *and* the declaration for the future UK-EU partnership, today MPs only considered the former. Still, it was voted down for two reasons: a) hardline Conservative Brexiteers and the DUP reject the terms of the Irish backstop; and b) Remainers and moderates in the Conservative and opposition parties conclude that signing off on the UK's exit from the EU without a clear plan for the future relationship would be reckless.

What happens next?

- **Low chance - Hard Brexit on April 12:** A majority in UK parliament wants to a) retain close ties with the EU and b) is staunchly against a hard and disorderly Brexit. The UK will likely go to Brussels to ask for more time to sort out its affairs shortly. As all 27 EU members would need to agree to such a delay there is a small risk than one or two member states reject the UK's request. While this seems unlikely, it is not impossible. More likely in our view, the EU would accept a request for a longer delay as long as the UK had made a clear shift away from repeatedly debating and voting on May's deal towards a clear process to seek a softer Brexit outcome.
- **Low/moderate chance – quick resolution and a soft Brexit on 22 May 2019:** This could happen if the UK government soon adopts a soft-Brexit policy that is backed by a majority of MPs in the House of Commons. While parliament has the essential building blocks to back one of the soft options – customs or Norway (plus) models - with a majority, this might take more time than is currently agreed.
- **Moderate/high chance – Long delay that ends in a soft Brexit eventually:** Parliament fails to find a majority for softer Brexit outcome in time for the UK to leave on 22 May 2019. Instead, the UK asks for a long delay that the EU accepts. Then, through the continued process of cross-party negotiation, eventually parliament backs a soft option down the line that the government adopts as its plan for negotiating the future relationship.
- **Tail risk - snap election and/or second referendum:** If parliament eventually finds a majority for a softer Brexit that the Conservative-led refuses to adopt, a snap election might follow to solve the impasse. Separately, if parliament is not able to find a majori-

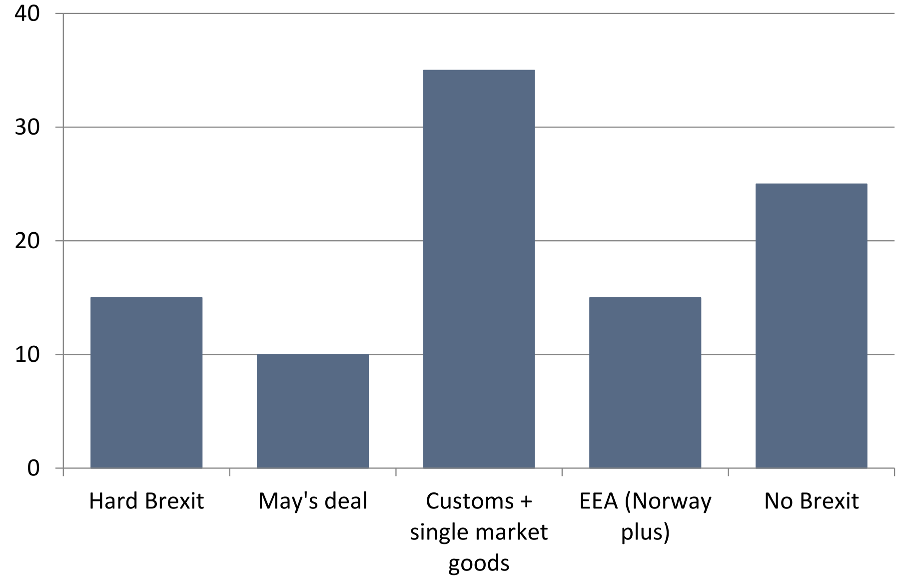
ty for a softer Brexit outcome, it may resort to backing a second referendum to shift the responsibility of deciding the Brexit back to voters again.

As the situation is in flux, we make no change to our probabilities for the potential Brexit outcomes; hard Brexit (15%); May's deal (10%); customs union model (35%); Norway model (15%); and no Brexit (25%). However, the uncertainty around these calls is high. See chart below.

Further reading

Brexit: Still no majority, but signs of progress
Parliament takes some control: implications
Brexit update: the UK's fate is in its own hands
UK: wage outlook warrants rate hikes, even in a long Brexit delay
Brexit mess: what can the EU do?

Potential Brexit outcomes and probabilities (%)



Source: Berenberg

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