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JOHNSON LETTER LACKS INGREDIENTS FOR A BREAKTHROUGH

Berenberg Macro Flash

Tell us something we don't know. In a [letter to EU Council President Donald Tusk](#), UK Prime Minister Boris Johnson last night set out the reasons why the Irish backstop should not 'form part of an agreed Withdrawal Agreement'. The letter does not represent a major step towards some resolution of the dispute with the EU and, in turn, an orderly Brexit on 31 October. It merely summarises the criticisms of the backstop long touted by the Eurosceptic wing of the Conservative Party. It offers little in terms of substance which the EU will require before any serious discussions could begin.

No need to speculate about the EU reply. Before publishing the letter, Johnson held an hour long conversation with the Irish Prime Minister (Taoiseach) Leo Varadkar. According to the press release published by the UK PM's office, the 'Taoiseach reiterated the EU27 position that the Withdrawal Agreement cannot be reopened'. Any office reply from Tusk will likely reiterate the message from Varadkar. As this issue uniquely affects the Republic of Ireland, Varadkar largely determines the EU27 position on this matter.

A major change from May? Johnson's predecessor Theresa May had agreed as part of the [declaration on future trade](#) to seek a future agreement based on a 'level playing field' in key areas of economic and regulatory policy including, but not limited to, state aid, competition, employment, environment and tax. Johnson now states in his letter that 'Although we will remain committed to world-class environment, product and labour standards, the laws and regulations to deliver them will potentially diverge from those of the EU'. At face value, this could potentially limit the scope of a future UK-EU trade deal significantly. In turn, this could have lasting negative implications on long-run UK growth potential.

Johnson on tour: Today, Johnson will meet with German Chancellor Angela Merkel. On Thursday he will meet with French President Emmanuel Macron. On Saturday, he will then attend the G7 meeting in Biarritz, France. Berlin and Paris will be intrigued to see if London has any serious solutions to the Irish border problem given its wish to remove the backstop from the Withdrawal Agreement. If Johnson hopes to persuade Merkel and Macron to sweet-talk Varadkar into changing his tune, he will likely be disappointed. In contrast to the logic often portrayed in the British press, Berlin or other EU capitals are unlikely to exert heavy pressure on pressure Dublin to yield. All of the EU's actions so far since the Brexit vote demonstrate that the EU's priority is the cohesion of the 27 – that means providing solidarity to smaller members such as the Republic of Ireland. The EU27 are ready to accept modest economic consequences in order to preserve that.

High-noon two weeks from now: On 3 September UK parliament will return from its summer recess. Expect a showdown between Boris, who is committed to leave the EU 'do or die' on 31 October even if that means a no-deal outcome, and moderates who will try to stop him. Johnson has a one-seat working majority in parliament. Moderate Conservatives could trigger elections or defect to the opposition parties to form a coalition government of so-called 'national unity' in order to block a hard Brexit. This matters for any UK-EU negotiations. Unless Boris can prove he has the backing of parliament or could win an election, he will remain toothless in discussions with Brussels that may not doubt his ability to force a hard Brexit onto the UK. This sets the stage for an accident. A lot has to go right for the moderates to stop a hard Brexit. For one, they need to form a majority against Johnson and then act. However, nothing has to change for a hard Brexit to happen – that is the default at the end of October.

For now, we keep our calls unchanged. We see a 70% chance of chaos on 31 October – hard Brexit (30%) or further extension (40%), with just a 30% chance of an orderly Brexit by then.



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