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Level 20, One IFC, 1 Harbour View Street, Central, Hong Kong. Tel: 852 3167 4591, Mob 852 9738 0944

Email: afreris@ecognosisadvisory.com, Website: www.ecognosisadvisory.com, Facebook: @ecognosis

## ECONOTE No. 83: Brexit: Trade and Democracy issues

8/5/2019

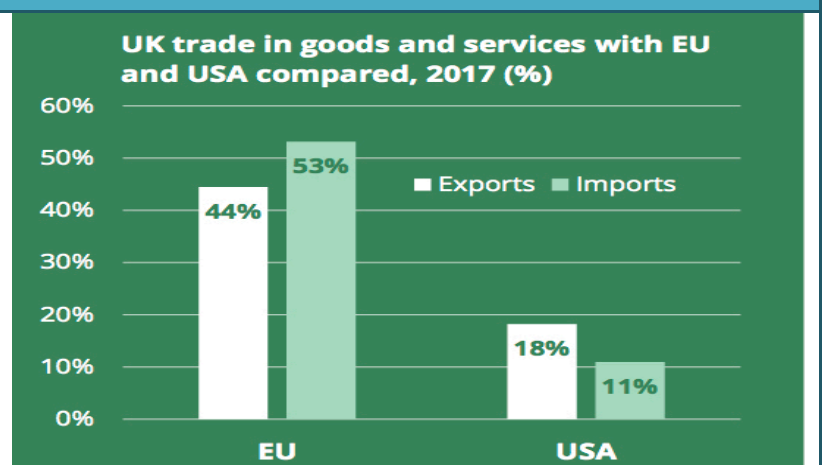
Summary	Investment Conclusions
<p>The Brexit charade in the UK is rapidly coming now to a close after causing deep divisions in the country and a complete paralysis in the government and legislative system. As the topic has occupied three years of interminable debate both inside and outside Parliament, it has led to a "Brexit-fatigue" and, hence, it is difficult to raise interest on a bleeding body bereft of life. But Econotes will have a go by summarizing the costs and disruption to UK's trade that a "No Deal" exit would cause. We also focus on the pure mechanics, and even technicalities of the elections and the referendum, a simple set of analytics but with sobering conclusions. Our position on the outcome of this process has always been the same; the UK will not exit the EU and will remain a member. This is not a matter of wishful thinking but a logical conclusion of the paths available now.</p>	<p>On the basis of our Remain expectations, it follows naturally that the event will be very bullish for the UK economy and, hence, for the FT100 and the GBP, even if it may take a while to percolate through after the Brexit is abandoned.</p> <p>More importantly, the event will be bullish for the EU as a political union and for the EU economy and the EUR. The event will prove the viability and the capacity of the EU to sustain severe blows and still stay united. Throughout the Brexit negotiations the 27 members acted in full unison. The failure of the UK to leave will also act as a deterrent for Italy, Hungary, Poland and any other member country considering breaking away. Incidentally Greece is now one of the most vociferous supporters of EU union. How things change!</p>

### Trade between the UK and EU and losses of a No Deal Brexit

The UK is an economy greatly dependent on international trade. In 2017 exports accounted for 30.5% of GDP and imports 31.9%. Of all UK's exports, 44.0% were sold to the EU while 53.0% of all the imports came from the EU. ( Fig. 1 ) The share of UK's trade with the EU has declined over time from 55.0% of exports going to the EU in 2006 versus 44.0% in 2017. ( Fig. 2 ), but the EU remains overwhelmingly the main trading partner. In 2017 the US, UK's next biggest partner, bought 18.0 % of all exports and supplied 11.0 % of all imports . ( Fig. 1 ) All import-export UK trade with the EU is tariff free. If the UK leaves with no deal, the EU will levy tariffs on UK imports. How much will be levied is difficult to calculate as an average, as the rates can vary quite widely from good to good. However estimates of the cost of these tariffs have ranged from 2.2% to 9.0% of 2018 GDP, or GBP 46.0 bl to 189 bl, although there is a considerable margin of error. The UK government has announced that in the event of a no deal Brexit, it will cut import duties to zero on 87% of all imports to UK to "compensate" consumers and producers from any price increases caused by the fact that goods previously imported from the EU had zero tariffs. These duty cuts will cost money in terms of foregone revenues for the Treasury and will imply that the remaining 13% of all imports may now have import duties imposed. Matters are more complicated, however, as 47% of all imports to the UK are not

from the EU and, hence, have some import duties imposed on them unless they come under "free trade agreements" negotiated by the EU, of which there are about 40. But once the UK leaves the EU it will also stop participating in these agreements and will have to renegotiate them individually. Incidentally the argument that intra-EU trade exaggerates the importance of the EU for the UK (The Rotterdam Effect) may have at, most a 4.0% distortion impact, still leaving the EU the biggest trading partner. Leaving without a deal will have a major impact and cost on UK's trade. Hoping that bilateral agreements will substitute all that, should only look at the ruthless negotiating practices of the US with its trading partners, and the US is our largest partner after the EU. Welcome to the

Fig. 1: The importance to UK of its trade with the EU and the US. 2017



Source: House of Commons Library Briefing paper, Jan 2019

## Democracy, the referendum and elections

The June 2016 Referendum produced a 52.0% majority to Leave. ( See the official voting paper in the Fact Box). Note that the Question/Option is to “Leave the EU”. It is not “Leave with or without a deal”. Anyone who decides to interpret it as “Leave without a deal” is basing this purely on a matter of conviction or opinion. Equally the same reasoning applies to people who interpret this as “Leave, but with a deal” “The official government position during the Referendum was “Remain” but the Tory party was neutral, and with the exception of UKIP, the rest of the parties were lukewarm Remain or full Remain. Undoubtedly there were people for whom “Leave” was “Leave Now”, without a deal. It is, of course, totally impossible to calculate how many of the 52.0% were Leavers with no Deal or Leavers with a Deal. The June 2017 election saw the Tories lose 13 MPs and their House majority and caused the subsequent paralysis.

### Fact Box: Ballot paper of the June 2016 Referendum

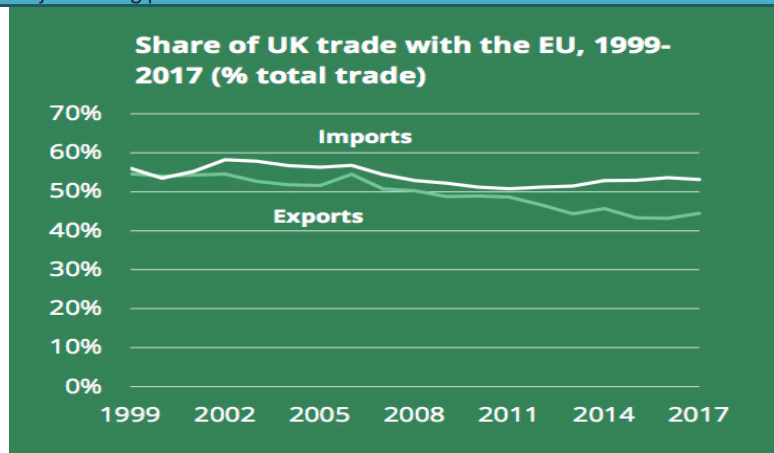
SCHEDULE 4 Regulation 83  
FORMS

Form 1 – Form of ballot paper  
Front of ballot paper

Referendum on the United Kingdom's membership of the European Union	
Vote only once by putting a cross <input checked="" type="checkbox"/> in the box next to your choice	
Should the United Kingdom remain a member of the European Union or leave the European Union?	
Remain a member of the European Union	<input type="checkbox"/>
Leave the European Union	<input type="checkbox"/>

The democratically elected Parliament of the 2017 elections was totally unable to accept a deal, any deal, having rejected Prime Minister May's deal three times. The public debate since June 2017 has been on the deal and not on leaving without a deal. So much so, that of the few things that this Parliament decided, and by two separate votes, was not to permit an Exit without a Deal, once with a majority of 312-308 and then again on March 13 2019 with a majority of 321-278 This vote does not necessarily stops a no-deal Brexit by end of October 2019, which is the default position of the Article 50 process which the UK is using to exit EU. The only way for the UK to avoid a no-deal exit is by approving an agreement with the EU or canceling Brexit altogether. It would now logically follow, that as the Parliament can not agree on a deal, but also will not exit without one, then the only option is cancellation of Brexit, which, incidentally, does not

Fig. 2: The declining share of UK's trade with the EU still leaves the bloc as the major trading partner. 1999-2017



Sauce: House of Commons Library Briefing paper, Jan 2019

### Some inevitable conclusions

need the approval of of the EU. There is a strong possibility of a new general election between now and the end of October 2019, as well as the May European elections, the latter acting as further signals as to the mood of the country, and the former giving, hopefully, a firm and unequivocal direction to leave without a deal or to remain. A new deal is highly unlikely not only because there is no time but because the EU has stated clearly that it will not renegotiate, again, the thrice rejected May deal, which is the only one on the table.

On a purely personal basis, I accept the 52.0% result. If at the end of October the UK leaves with deal or no deal, as a democrat, I will accept and live with that, too.

Whether the 52.0% majority voted out of ignorance, fear, or misled by fake news, it is their democratic right to do so and also their right to make enormous national inter-generational mistakes on false information and expectations and on pure envy and prejudice. Unfortunately that is the price of democracy.

Equally, I accept that people have the right to change their minds after three years of totally inconclusive public and parliamentary debate, plus the April 2019 6.0 million petition to remain. Let the people decide through a parliamentary vote or through new and clearly phrased referendum. Again, I will fully accept a decision to Leave with or without a deal despite the huge cost of the latter both in terms of politics and of money. My tiny contribution to the Remain effort is to carry on writing, appearing in the global TV and social media and trying to show the enormous political error and cost of Brexit.

Andrew Freris ( writing completed 8 May 2019)