

Letter n°23

Brexit : when illusions give way to reality.

« Those who believe that the peoples will follow their interests rather than their passions did not understand anything in the 20th century » Raymond Aron.

Far from the 1870s when the United Kingdom dominated the world, when England's GDP exceeded that of the United States and British manufacturing output accounted for a quarter of world output. Far are the withdrawals of Palestine, India, Cyprus after UK departed by sowing divisions. Europe came out of 2020 just fine because UK only represents 16% of the GDP of its 27 member countries and its departure has not dismantled the European Union.

At first glance, the agreement signed under candlelight on December 24, four and a half years after the exit referendum, 47 years after joining the Union, fully illustrates Raymond Aron's point. Insular passion was at the origin of the result of the vote and, in the exit negotiations, political passion prevailed over economic interest, over the theory of comparative advantages advocated by the great English economist, **Ricardo**: the City, England's showcase on the international scene, 8% of the GDP, was ignored by Johnson who preferred to focus on fishing and its 0.1% of the GDP and other examples are presented in this Letter.

General de Gaulle had opposed Great Britain's entry into the European Union and on this point, as on others, he was right. Georges Pompidou lifted the veto in 1973 but very soon Margaret Thatcher waved the exit flag, requested and obtained special conditions and then the country refused to be a member of the Eurozone and to sign the Schengen agreements.

From Europe, the United Kingdom was looking for nothing more than the single market, i.e. the free movement of goods and services. English leaders never wanted a common policy, the integration and the federalism. As English Foreign Secretary **Palmerston** said around 1840, *« The English have neither eternal allies nor perpetual enemies but only interests »*.

It is no coincidence that Europe has made more progress in mutualization in 2020 than before. The British would never have otherwise accepted the €750 billion European recovery plan, the pooling of debt, "The Europe of batteries", the creation of a European Defence, the GAFAM regulation project among many other advances.

- The European Union preserves the essential and reinforces its integration:

The preservation of the essential by the European Union:

The European Union is built around four fundamental principles being the free movement of people, goods, capital and services. At the end of this long breaking negotiation with the United Kingdom, detailed in an agreement of more than 1,200 pages, Brussels succeeded in maintaining the free movement of goods, without customs duties, quotas and without seeking a competitive advantage through tax, social or environmental measures.

Some €700 billion of annual trade is thus concerned and fishing is not excluded. To see 60% of the fish fished by Europeans in British waters is unacceptable in the eyes of English nationalists, but they cannot ignore the European market for 80% of this fishing and the interests are therefore intertwined. Until 2026, European boats will be able to continue fishing in British waters and then they will give up 25% of their fishing rights to the British, which is €650 million in turnover, but they will be able to benefit from an adjustment reserve of €5 billion, set aside by Brussels to help the sectors penalized by Brexit.

Johnson's interventionist line is far from Thatcher's neo-liberalism:

From Boris Johnson, Barnier was able to extract a commitment to respect labor law and the environment. There is no question of envisaging a "Singapore on the Thames" at the gates of Europe, a term that is ludicrous because in Singapore the corporate tax rate is not much lower than the English rate, financial regulation is more restrictive, 85% of real estate is state-owned, the state controls more than a third of the capitalization, especially banks and telecommunications, which does not correspond to the English tradition.

But was there a risk? Great Britain, with Churchill at the beginning of the 20th century and then with Beveridge after the Second World War, is one of the countries that invented the Welfare State and it is not going to deny its culture. Just as Thatcher, with Ronald Reagan, was at the origin of "neo-liberalism", so Johnson, also a member of the conservative party, is broaching a more interventionist line and, since the beginning of the crisis, has announced £670 billion in spending or guarantees.

Elected with the support of the middle classes, strengthened by the recovery of the working-class electorate, Johnson, a proven populist, has promised an increase in the minimum wage, has initiated an increase in health care spending, has committed to the revitalization of the old industrial regions of northern England, has multiplied announcements of public investment projects in infrastructure and intends to be at the forefront of the fight for environmental preservation and the development of renewable energy with the encouragement of nuclear power, wind power and the banning of thermal cars from 2030. Nothing that suggests a disengagement of the State. Nothing that fundamentally distinguishes the United Kingdom from other European countries. One could also add the Bank of England's interventions, which already holds 35% of the English sovereign debt in the list of evidences.

Guarantees:

We know *Churchill's* warning, « ***The English never set a limit without blurring it*** ». There is indeed the idea put forward a few years ago by Philip Hammond, the former Minister of Finance, to open free ports, but this will remain marginal and the British must have an independent authority to control public subsidies. To settle disputes, there is provision for an arbitration tribunal and retaliatory measures could compensate for possible British subsidies or any form of dumping. Such procedures may seem surprising because the European Union does not offer the image of fiscal harmony, but the United Kingdom has not been able to make its singularity prevail.

- ***The United Kingdom cannot hide a weakening:***

The balance of power was unbalanced:

66 million, divided, facing a united block of 450 million, there was nothing to be done. For a long time, the "perfidious Albion" thought she could stir up dissension between the States of the Union, but in vain. Beyond Barnier's undeniable ability to forge a consensus, some states, such as the Netherlands and Germany, feared unfair economic competition. Other governments, struggling with a Europhobic political opposition, wanted to display an image of intransigence on Brexit's conditions in order to show the costs of an exit.

Economic integration was strong and left no alternative:

Great Britain is a trading nation, very open to external markets with 47% of its exports go to the Union. The free movement of goods is preserved but will be hampered by red tapes and non-tariff barriers that will deter foreign investors from setting up factories in the UK to target the European market. Spain is an excellent alternative for automotive plants, and France and Germany are just as good in aeronautics. The decline in foreign investment in the UK since 2016 will continue and this will be detrimental to employment. It's no coincidence that Jim Radcliffe, a British billionaire and fervent "brexiter", first relocated to Monaco and today prefers the East of France to England for the establishment of an automobile plant.

The timing of the negotiation was not favorable to Boris Johnson:

No European country is more affected by the Covid crisis. Badly managed by the Prime Minister, it has deteriorated and in 2020, UK has observed the strongest recession, a drop in GDP of 11 to 12%, and recorded

the most serious budget deficit, more than 15% of GDP. A percentage without comparison in Europe, since Spain, the worst example, has a deficit of 11%!

The weakness is perceived by the rating agencies (Moody's in particular) which, early on, lowered the country's rating and by the markets which do not offer the benefit of zero or negative rates for long-term debt. While Germany, the Netherlands and France can borrow at 10 years between -0.55% and -0.33%, and Spain and Portugal, borrow at 0% on the same maturity, the United Kingdom has to pay 0.24%. Admittedly, this is insignificant compared to the interest paid the year prior, but it is an additional cost.

The setbacks for the United Kingdom are obvious and damaging:

This is glaring for the City and financial services, 8% of the British GDP, its international showcase, was neglected by Johnson who preferred a political joust on fishing, a modest contributor to the prosperity of the country with its 12'000 employees and less than 0.1% of the GDP. 40% of financial services are destined for Europe but, after a period of 18 months, the United Kingdom will lose the benefit of the European passport and the London clearing houses will no longer be able to deal in Euros. The agreement is also regrettable for British universities and research centers deprived of European manna, for students now excluded from Erasmus exchange programs, for farmers who will no longer be able to count on aid from the CAP ("Common Agricultural Policy"), and lastly for retired people wishing to settle in Spain, Portugal or France.

The preservation of the unity of the Kingdom is far from being assured:

Nicolas Sturgeon's Scotland is waiting for the right moment for a new referendum on independence and Ireland could aspire to reunification.

Conclusion: « ***The British Lion, so fierce and valiant in bygone days, so dauntless and unconquerable through all the agony of Armageddon, can now be chased by rabbits from the fields and forest of his former glory*** » Churchill in 1937.

The last-minute negotiations were detrimental to the United Kingdom:

Pressed by worried British business circles, jostled by his party's deputies, destabilized by the election of the native Irish, Jo Biden, Boris Johnson had to admit that a lack of agreement would have been a disaster for the British economy. Poorly initiated, long neglected, the last-minute negotiations could only lead to an unfavourable agreement for the United Kingdom. The Europhiles, aware of the depth of the British recession and the risks of a break-up of the United Kingdom in the event of a lack of agreement, and witnessing the seriousness of the epidemic in the country, were able to impose their points of view. The only consolation for the "Brexiters" was that a lack of agreement would have been much more costly.

The asymmetry in the balance of power was obvious:

Following the example of Trump's America, which was able to impose a renegotiation of the NAFTA free trade agreement on Canada and Mexico, the European Commission was able to set red lines to the English claims. After all, only 8% of European exports go to the UK, while 47% of British exports end up in Europe. In both cases, the asymmetry was too great to envisage a fair agreement. In a world increasingly defined by power relations, what is the strength, what is the attractiveness of a British economy with a GDP of \$2.8 trillion in 2018 (according to International Monetary Fund figures) compared to the \$20.5 trillion of the United States, the \$15.9 trillion of the 27 members of the European Union and the \$13.4 trillion of China?

The disappointed illusions of Brexit's supporters:

The "Brexiters", with their illusions of greatness, independence, alternatives, and a halt to immigration, were deceived in 2016 by Mr. Farage's erroneous figures on the cost of belonging to Europe, recently confused by Johnson's political opportunism, and today, gradually sobered up by the harsh realities: the privileged relationship with the United States, £250 billion in trade, or 15% of British trade, is a chimera because Great Britain is no longer the Trojan horse in the European Union, the ambition displayed with the Commonwealth countries is limited because they represent only 13% of trade, the trade agreement with Japan is minuscule, £30 billion in trade, compared to the €700 billion in trade with the European Union, the possibility of an agreement with Russia is being disintegrated by the bad political relationship, the dream of an agreement with

China is temporarily stayed by the political tensions over Hong Kong, the positions taken against Huawei and against the mistreatment of the Uyghurs, the aspiration for an insularity protected from immigration finds no translation because if the Polish and other Europeans are less numerous to cross the borders, the immigrants from the rest of the world, often even more difficult to integrate, are more numerous.

A new disappointment for the populists:

The populists are militating for a return to borders, exalting the idea of nationhood, but this has an economic cost and no one can ignore interdependence. Between the two populist experiences of the Anglo-Saxon countries, at the origin of neoliberalism and its excesses with regard to inequality and the downgrading of the middle classes, one was a parenthesis, the other a rupture. Trump will soon be only a memory, Brexit will remain a nightmare. One wonders how Johnson, Prime Minister since July 2019, could have imagined an exit agreement preserving the advantages of a member state and freeing it from its obligations. He thought he was making the British richer, instead he was impoverishing them without offering a clear vision of the path he was going to take and the £ will depreciate, thus making imports more expensive, especially the 50% of food products bought abroad.

Europe comes out a winner:

With the United Kingdom, the agreement protects against possible unfair competition, and without the United Kingdom, the European Union has finally begun, as we pointed out in our Letter 22 « The New European dynamic », to move forward on the road to integration. The English in Brussels had managed to instill a liberal spirit but wanted to limit the Union's ambition to a commercial Europe, a free trade zone. With the British out of Brussels, the deepening of Europe could be continued.

Geneva, December 30, 2020



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