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BREXIT Pitfalls 2016 and May in March: Neither Rhyme Nor Reason

A sense of fatalism seems to have pervaded the May government, as it seems to be quite unclear how the government can obtain a parliamentary majority before March 29, 2019, for approving the UK-EU Withdrawal Agreement that has been sitting on the table since December 2018. The government is trying to lure over a sufficient number of Labour MPs by offering financial sweeteners for their respective constituencies, but this a dangerous strategy since it could lead to a split of the Tory party, where ardent Brexiteers smell treason as soon as some form of compromise with the Labour Party appears on the horizon. Labour leader Jeremy Corbyn's strange BREXIT policy of not offering a clear alternative by proposing Remain through a second referendum also destabilizes the Labour Party since many Labour MPs consider Remain as a preferable option to any form of hard BREXIT. AT the same time, Prime Minister May is increasing the pressure on MPs by pointing out that it is their duty to implement the will of the people as represented by the majority vote of June 23 in the referendum which had a 51.9% majority for BREXIT. The entire process is characterized by neither rhyme nor reason – as the phrase coined in Shakespeare's The Comedy of Errors goes – since the expected normal result of an orderly referendum would have been 52.1% for Remain.

The problem with the EU referendum of 2016 is that the standard of information upheld by the Cameron government in 2016 was so much different from that of the Scottish Independence referendum of 2014 that a closer look at the information policy is required. In 2014, the Cameron government produced a brochure saying that the economic loss from Scottish independence would be £1,400 GBP per Scot "and the loss of all the benefits from British EU membership". In 2016 however, when the question at hand was the UK's membership of the EU, figures from the Treasury available in early April said that BREXIT would bring a loss of £1,800 GBP per capita in a scenario with a UK-EU trade agreement plus another 4% of GDP from not realizing the favorable agreement between the UK government and the EU obtained by David Cameron in the negotiations in early 2016: A deepening of the EU single market in telecommunications, electricity and financial services were key points here. Thus, the key message on the long-term benefits of British EU membership from Her Majesty's Treasury was that a loss of membership would entail a 10% income loss. In the 16-page information brochure sent to all households in England April 11-13 – and later to households in the other parts of UK - not a single sentence referred to this 10% income loss. The newspaper reports on the Treasury study, which was published a week after the mailing of the information brochure to voters in England - a strange finding in itself -, were scattered and could not replace this crucial information being provided by government in a referendum which is supposed to involve all potential voters.

Based on a standard UK popularity function, which shows the link between economic growth and government popularity, one can calculate that in the case that all voters had obtained that information on the income loss, the result of a normal, ordinary referendum would have been a 52% majority for Remain. From this perspective, the moral pressure of Prime Minister May on MPs to follow the apparent pro-BREXIT result of 2016 is unfair and totally inadequate. The natural way to correct the information pitfall of Mr. Cameron would be a second referendum. With May's approach, and heading inexorably towards March 2019, one can only expect one divided country and two divided parties, namely that BREXIT and May's policy will lead to an irresponsible BREXIT – an accidental BREXIT - based on a disorganized 2016 EU referendum and the splitting of both the Conservative Party and the Labour Party. If there would be an extension of Article 50 until the end of summer 2019, a second EU referendum could still be held if the British Parliament gave the green light for such a move in the spring.

If there were no second referendum, one may state that the primary losers of BREXIT will be British democracy and, in harsh economic terms, the British population which would face a welfare loss of about 20% in a No-Deal BREXIT. Not just the up to 10% loss of gross domestic product emphasized by the Bank of England in 2018, but also losses from a halving of the global market share of the Pound which would be much less attractive to central banks worldwide post-BREXIT and the losses for government and taxpayers from a rise of the real interest rate: If that rate for government bonds would increase by 0.3% - and the likely rise to come could actually be higher after an initial fall due to steeply increased inflation in the context of a strong Pound devaluation – this would be equivalent to the UK's net EU contribution payments in 2016. There are also losses from a reduced demand of money parallel to real GDP dampening and on top there will be, following the real Pound devaluation, a rise of the share of foreign ownership in the UK's capital stock – through international mergers & acquisitions – so that a higher share of profits will be transferred abroad post-BREXIT. If the share of foreign ownership rises from 16% in 2016 to 26% in 2025, the reduction of national income would be 3.3%. Finally, there would be a loss of institutional capital for the UK when leaving the EU and, of course, a much weaker international negotiation position for the UK due to its having 1/5th of the economic weight of the EU28.

If the UK would have a second vote this can bring all the clarity which the first vote and the subsequent May policy did not have. A hard BREXIT in March would indeed feature neither rhyme nor reason in what is more akin to a Tragedy of Errors.

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