BREXIT

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The year just ended has been marked by exhausting negotiations between London and Brussels. While the European Union has shown a significant – indeed, perhaps unexpected – degree of cohesion behind its chief negotiator Michel Barnier, the United Kingdom has turned out less and less united behind Prime Minister Theresa May. It is worth recalling that the Brexit referendum originated in the (unsuccessful) attempt by her predecessor David Cameron to heal the deep divisions within the Conservative party on EU membership. Labour, too, is divided: a deep rift clearly affects the whole of the political class and indeed the electorate. No surprise, then, that two and a half years after the referendum and just a few months from Brexit Day the country is still arguing with itself in a kind of endless parallel negotiation whose outcome is even more uncertain. Most people may have thought 2018 would be taken up with disputes between the EU and the UK, but that the outlook for 2019 would be rosier: the negotiations were to be concluded by the end of November in order to give the European Council time to approve the final agreement, consisting of two parts: the withdrawal agreement proper, and the Political Declaration on the future relationship between United Kingdom and EU. That was in fact approved on 25 November, when the Council dealt with the Brexit agenda item in record time – just thirty minutes – and all that was left to do, on Brussels' side, was the qualified majority voting in the Council and the final – generally expected – approval by the European Parliament. London was likewise to play its part, with a parliamentary vote on the agreement scheduled for 11 December. However, it had already become clear that this obstacle would be far harder to clear: dissension within the Cabinet, first on the con-

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duct of the negotiations and then on their outcome, led to the resignation of prominent Leavers, including the Foreign Secretary Boris Johnson and no fewer than two Brexit Secretaries. Driven onto the ropes by her own party, and facing a real risk that the agreement would be rejected, the Prime Minister opted to postpone the vote in the House of Commons until mid-January 2019, but had to undergo the humiliation of a vote of no confidence among Conservative MPs. She won a victory made very bitter not so much by her forced promise that she will not be leading the Tories into the next election – for even she can hardly have still been expecting that – but by its even clearer demonstration of her weakness and the deep divisions and heightened tension prevailing throughout the country.

All this goes to show that Brexit will be exercising Europe for much of 2019, too, long after the scheduled exit date of 29 March, if only because it is by no means certain that this official deadline will in fact be met. Article 50 of the Treaty on the EU allows for the remaining 27 member states to unanimously grant the leaving country an extension. Moreover, the European Court of Justice has ruled that the United Kingdom could unilaterally revoke its withdrawal demand under Art. 50. In the case of the UK, that would amount to disavowing the 2016 referendum, and would increase the likelihood of a fresh general election and/or a second referendum; but whether Brussels granted an extension or London revoked the withdrawal there would still be the matter of the forthcoming European elections in May: the paradoxical situation could in fact arise where a country which has voted to leave the EU has to hurriedly prepare for European parliamentary elections in just a few months.

The scenario seems an odd one; but it is a fact that some MPs want to avoid Brexit at all costs or at least – if leaving the EU is inevitable – to avoid a "no deal" exit, with no agreement and consequently no transition period in which the UK could keep access to the European single market, paying some contribution to it though no longer able to participate in determining its rules and standards. A transition period seems the only way of mitigating the adverse economic consequences of a "cliff edge" in which the UK would literally overnight start trading with the EU on the same WTO rules – meaning low but not zero tariffs – as any extra-EU country.

That scenario can be avoided if in January Westminster approves the agreement, and with it the transition period ending on 31 December 2020 (with the possibility of one extension, but no more). This is the period during which London and Brussels are to turn the framework outlined in the Political Declaration into a comprehensive agreement on future relations between the EU and the UK.

What happens at Westminster in January will be crucial; and there are a number of possible outcomes. The current agreement could be amended as May now intends to do to accommodate the demands of a sizeable proportion of her own party's MPs, both those who want a hard Brexit (leaving the single market and the customs union) and those who want to keep the closest possible relationship with the EU. The European leaders, however, repeated at the Council meeting in December that the current agreement is the only one on offer; so they will probably be willing to modify only the Political Declaration, which is not a legally binding text. They might, in particular, approve a formula offering the UK parliament reassurances concerning the duration of the so-called "backstop"; a customs union that would apply indefinitely unless and until an agreement or solution could be found which avoids any hard-border between Northern Ireland and the Irish republic (a key feature of the Good Friday agreement).

Then there is still the fact that, for a country like the UK whose success has been built on legal certainty and the pragmatic, pro-business attitude of its ruling classes, uncertainty and politicization are bound to damage the economy and depress investors' expectations: uncertainty concerning the manner of exit (deal or no deal), and therefore whether or not there will be a transition period; and uncertainty about the kind of agreement there will be with the EU-27. That looks at present like taking the form of a Canada-style FTA with some specific agreements bolted on: the City hopes, for instance, for one on financial services. Against this background it is not surprising that as early as April 2017 the UK regulators (Bank of England, Prudential Regulation Authority, Financial Conduct Authority) asked City operators to draw up contingency plans for the worst-case scenario of an exit from the EU without an agreement and therefore with no transition period to avoid falling off a "cliff edge". The ECB and the regulators in the 27 member states have done likewise.

In the face of the continuing uncertainty about the outcome of the negotiations and the real risk of a "cliff-edge" departure, financial operators have had no other choice than to implement their contingency plans and began transferring those activities which would inevitably have to be relocated if they lost their "European passports" and the UK changed from a member state to a "third country". The consequences of that transfer process and the reorganization of markets and financial activities cannot easily be predicted; certainly competition has already begun between London and continental financial centres, and for the moment seems to be producing a sort of "cannibalization" of activities and customers in a "lose-lose" game. The prospect of US or – more likely – Asian centres finally scooping the pot cannot be ruled out.

There is abundant reason to believe that Brexit will without any doubt continue to keep Europe busy in 2019 and well beyond. Everyone stands to lose in this situation: the UK most of all, but the EU-27 as well.