

Brexit: Optimism returns, but is it justified?

There are a growing number of reasons to be cautiously optimistic about UK-EU talks. Negotiations seem to be heading slowly in the right direction, while political pressure is building in the UK. That suggests a deal can still be achieved, but with the de-facto deadline still a few weeks off, there's also plenty of scope for things to go wrong



Things are starting to look a little brighter

It's now three weeks since the UK unveiled its controversial Internal Markets Bill (IMB), legislation that would grant powers to override parts of the withdrawal agreement agreed just last year between the UK and EU. The fireworks created by this move led many, ourselves included, to conclude that the chances of a deal were slipping. [We wrote at the time](#) that we thought the odds of a deal were at best 50:50.

But as another round of trade negotiations draw to a close, there is a renewed sense of optimism that a deal might still be on the cards after all.

The first piece of good news is that despite the bill having gone through the House of Commons this week, Brussels has not shut down trade talks - wary perhaps of avoiding the blame if both sides were to fall back on WTO trade terms next year. Instead, the EU has signalled it is pursuing legal action against London, but this will take time and doesn't preclude a deal being done in the meantime.

And in light of the critical global reaction to the bill - including from Joe Biden - the UK government appears to be taking a more conciliatory approach. It has, for instance, offered Parliament a veto over the controversial powers in the IMB. While this in itself will do little to dampen concerns in Brussels, it does signal flexibility from ministers.

Importantly, [the bill will also reportedly](#) not go to the House of Lords until much later in the year, and that too has helped take some of the immediate heat out of the situation.

The Internal Markets Bill isn't necessarily a barrier to a deal

Now, clearly the EU won't ratify a trade deal with the UK while the threat of overriding the withdrawal agreement remains. And equally the UK won't want to be seen to be climbing down over the bill as talks enter their final stages.

There's no clean way out of this impasse. But there's a growing expectation that Brussels will require the bill to be adapted as the price of a deal and at that point, with some careful political manoeuvring, the UK could find an off-ramp. The UK government could for instance publicly claim that the tactic was successful in securing an agreement, and that the 'safety net' provided by the bill would no longer be required.

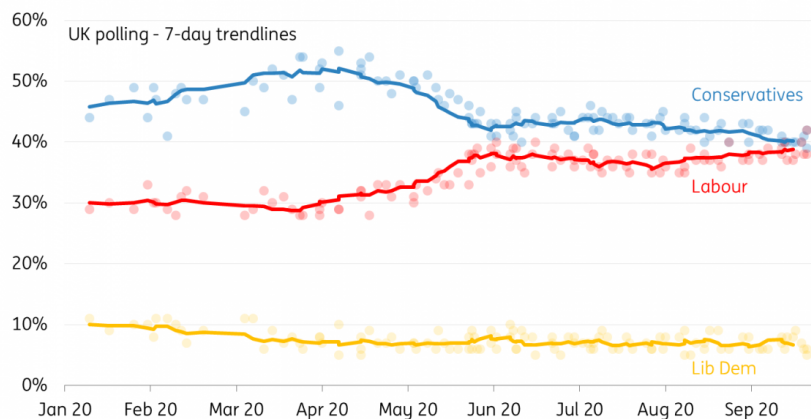
In short, the IMB is not necessarily a barrier to a deal being done, and encouragingly there have been signs that negotiations have taken a more positive turn.

The UK this week [reportedly](#) put forward a range of papers on different issues, including on state aid and fishing. So far there has been no breakthrough, but the fact that Britain is putting forward new proposals is undoubtedly a step forward compared to the previous past few rounds.

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All of this comes as pressure grows on the UK government to avoid 'no deal'. The return of Covid-19 risks a volatile winter for the economy, and a chaotic start to 2021 would only add further challenges. The Conservatives have also now slipped below Labour in the polls for the first time since 2019, according to an [Opinium](#) poll over the weekend. We know too that support for Scottish independence is rising, and it's widely believed that a 'no deal' scenario could add further impetus to the campaign.

The Conservatives are now neck-and-neck in the polls with Labour



Source: Various polling agencies via Wikipedia

Individual dots represent polling from YouGov, SavantaComres, Deltapoll, Opinium, Redfield & Wilton Strategies, Kantar, Ipsos MORI, Survation, Number Cruncher Politics, BMG

A deal would still require big compromises from the UK

Putting all of that together, there does appear to be a case for some cautious optimism. But it's not all positive - and there are still a few key ways that it could all go wrong.

Firstly, none of what we discussed above changes the fact that the UK is going to have to make some serious compromises if it wants a deal - chiefly on state aid. The EU will, at the very least, want Britain to create an independent regulator to police the government's state support policies. So far, the UK has been very reticent to do this, instead signalling that it wants greater scope to support industry in the post-Covid era.

The UK is going to have to make some serious compromises if it wants a deal

But even if PM Johnson is willing to accept these choices, there will undoubtedly be dissent among some Conservative MPs in Parliament. And while the government does have a strong majority in the House of Commons, recent experience with coronavirus legislation has shown that ministers increasingly need to strike compromises with MPs to secure ongoing support.

That potentially opens the door to an alternative scenario, where no agreement is reached this year, and instead UK negotiators return to the table in 2021 to chart a course towards an even more distant agreement (e.g. one that waives some but not all tariffs), involving fewer so-called 'level-playing field' commitments. Whether or not this is realistic is, of course, the subject of plenty of debate. At the very least it would take a while, and in the meantime, there would still be all of the initial disruption expected in a 'no trade deal' scenario.

Returning to the original question, have the chances of a deal gone up? Well the answer seems to be yes, but even so, the risk of there being no deal is still pretty high - and indeed much higher than we always felt the risk of 'no deal' was back in 2019 surrounding the original Brexit deadlines.

[For more on what all of this means for the economy, read our recent piece](#)

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