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## No more Mr. Nice Guy

"The EU is threatening sanctions to prevent Britain from undercutting the continent's economy after Brexit, including "tax blacklists" and penalties against state-subsidised companies, according to a strategy paper."

- From 'Brussels lines up sanctions to stop Britain undercutting EU economy' by Alex Barker, Jim Brunsden and George Parker, *The Financial Times*, 2 February 2018.

**As Marcus Brigstocke** has learnt to his cost, Brexit is probably the most polarising topic in British politics for a generation. (For this reason we've tended to underemphasise it within these commentaries.) As a reminder to anyone who has been living under a rock for the past 18 months, on 23 June 2016, the United Kingdom voted to leave the European Union. The outcome was relatively close, but conclusive. 17.4 million (51.9%) voted to Leave; 16.1 million (48.1%) voted to Remain. Remain lost, so we are out.

You might think that being not particularly funny would be something of a drawback for a stand-up comedian. Not as much as insulting approximately half of your audience, though. Mr Brigstocke was reportedly shocked when he noticed that, in response to his anti-Brexit material, some of the audience at his gigs simply walked out:

> People have been angry; people have walked out of shows and people have booed.. A lot of the people that I think of as my audience will not be back - they won't come again - they're that angry.

Who could have thought that being a supporter of "the hideous social and political turn we have taken as a country" would be treated by the majority of those who voted as "comedic poison" ? Mr Brigstocke is now featuring in ads for the Experian consumer credit agency. That ***is*** actually quite funny.

Watching the UK government conducting its Brexit negotiations with Brussels over recent months has, however, been a dispiriting experience for the 51.9%. As the FT's quote above indicates, the EU is in full-on punishment mode, and British offers of money and gestures of goodwill have simply been trousered without reciprocation. It is difficult not to feel sympathetic to the argument of Ambrose Evans-Pritchard, International Business Editor of *The Daily Telegraph*, when he writes:

Those who called for a clean Brexit from the outset were right. The Franco-German axis is determined to make a soft arrangement impossible. Any further talking at this point wastes time and tightens the noose around our own necks.

If Britain is to leave the EU – as it must, after a clear popular vote, endorsed by Parliament, and written into the Tory and Labour manifestos – the only way to do so with economic and political coherence is to reassert full sovereign self-government.

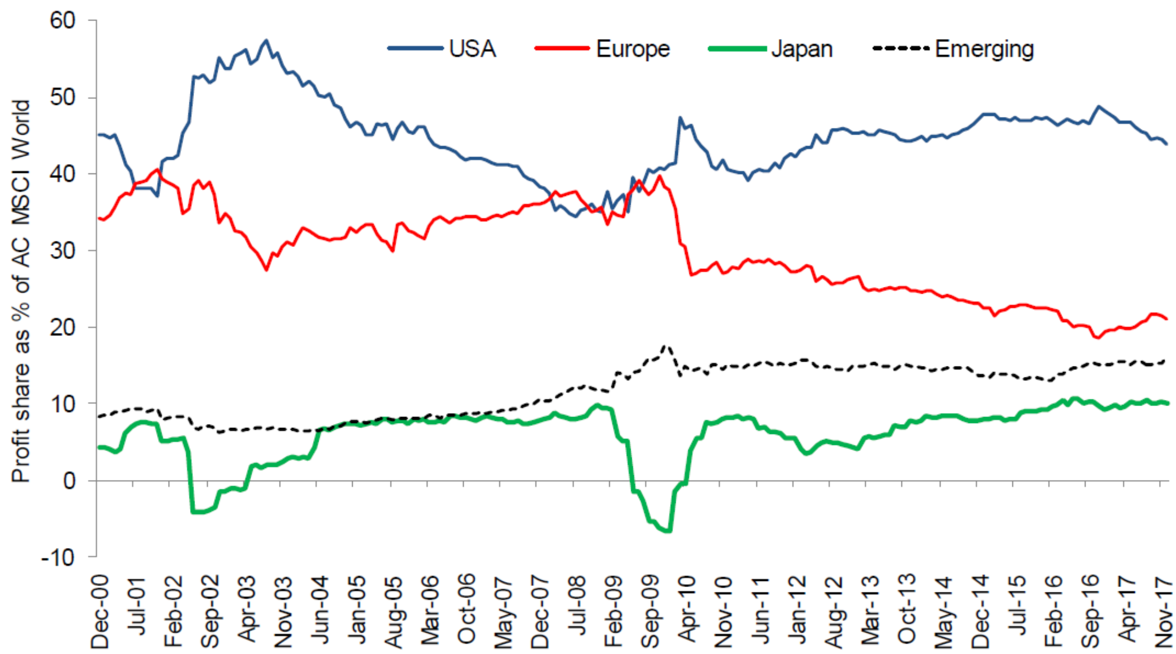
Sadly, I have concluded that we are left with no choice other than to invoke our rights as members of the World Trade Organisation and accept tariffs (mostly very low, but still unwelcome) until free trade deals can be agreed one by one with the US, China, Japan, India, and other countries. The wheels should be set in motion immediately. It will be impossible in another six months.

Berlin, Paris and Brussels have stated with crystal clarity that no deal on services is available. The only free trade pact they are willing to offer is on goods.

This is prohibitively asymmetric: it locks in their huge surplus (mostly German) in manufacturing, while locking out Britain's surplus in services, which partly compensates. Those who talk loudest about cherry picking pick the biggest cherries.

As we highlighted two weeks ago, there is one over-arching reason for loosening our ties with Europe and strengthening them – economically, at least – with other, faster-growing economies: ***the EU isn't working***.

**Profit share of listed companies in various regions as % of global profits**




Source: SG Cross Asset Research / Equity Quant, FactSet, IBES

As SocGen pointed out last month at their annual investor conference in London, while the profit share of global profits attributable to US and Japanese companies has largely held its ground over the last two decades, the profit share generated by European listed businesses has roughly halved. As SocGen put it, "The European quoted sector is losing global relevance". They followed up with arguably an even more damning statistic about the comparative weakness of European profitability. Japan (population 127 million, and shrinking) now generates the equivalent of 50% of European profits – with Europe's population standing at 743 million, and growing. Did anybody say ***uncompetitive*** ?

And we now see the direction of travel that Brussels wishes the UK, post-Brexit, to take: backwards, like the rest of the EU economy.

The FT's chief economics commentator, Martin Wolf, made the following comment on 29 March 2017:

> Mrs [Theresa] May has no mandate for the threat she has made of turning the country into a low-tax, minimum-regulation country.

In what kind of world are lower taxes and less regulation some kind of threat ? The world of the EU, obviously. Ambrose Evans-Pritchard again:

> The Whitehall memo leaked this week – EU Exit Analysis – claims that the WTO option would shave 8pc off British GDP over fifteen years compared to the trend line of EU membership.. The assumption that the EU itself is a viable project over those same fifteen years must be contested since it lacks the policy machinery and the cultural cohesion to avoid a crisis in the next global downturn.

These are turbulent times, both in politics and in financial markets. As Paul Rodriguez makes clear in our latest podcast, there are growing signs from a technical perspective that (Anglo-Saxon) stock markets are topping out. A (so far) small number of high-profile companies have recently issued profits warnings, notably in the UK outsourced services sector, and in the US consumer goods sector. The interest rate cycle is on the turn, and as SocGen also point out, a large number of US smaller and mid-size companies are heavily levered – at exactly the wrong stage in the cycle. This is not the time for countries to be competing with each other to strangle their economies in red tape, nor for resorting to crude protectionism. As for the UK and its Brexit negotiations, economic logic alone suggests that we should just walk away. Now.

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