It’s been over three years since the 2016 Brexit Referendum. During this period, British politics has been mired in a quagmire of confusion and uncertainty. Most Britons are understandably fed-up – as is the rest of the world – with endless discussion about the chaos of a no-deal Brexit; the Irish backstop; shortages of food and medicines; travel logjams and job losses.

What is not discussed – if ever mentioned – are the following set of questions: (1) how would a no-deal Brexit impact the city of London? (2) how does the average French or Spaniard feel about Britain dropping out of the common market? (3) how will a no-deal Brexit impact EU’s cohesiveness – could Brexit be an existential threat? (4) how will a no-deal Brexit impact the global economy? and (5) how will a disruptive break influence geopolitics, at a time when the US has gone rogue, and China and Russia are flexing muscle?

In our view, these questions are intentionally ignored as the answers will not suit the status quo. More simply, a no-deal Brexit will almost surely tip the EU and Britain into economic recession, and could become an existential threat to the EU. It would also strengthen Russia’s hand in Europe and make the US more isolationist. Finally, a messy break of the 5th largest economy from the world’s largest trade block, could easily tip the global economy into recession.

For many who are still shocked by the 2016 referendum; the election of Donald Trump; and the rise of nationalism in the western world, these are uncomfortable issues. Truthful answers may suggest that a return to a liberal, multicultural, and free trade world order, may no longer be possible. Brexit may be a pivotal point in history that will change the global outlook.

What has happened so far?

The economic cost of the leave vote cannot be understated. In the past week, MPs demanded that the British government publish its internal report about the likely impact of a no-deal Brexit (the report is called Yellow Hammer). The report warns of potential shortage of certain types of produce and medicines; price increases for imported goods; the closure of some British businesses; the loss of manufacturing jobs; delays in the transportation of goods (and people) across the English Channel; and possible riots.

While these economic costs are being debated, the political costs have already been realized. The list is impressive:

- Brexit has forced two British Prime Ministers to resign;
- Brexit has split the Conservative party, with a civil war raging amongst the Tories. Boris Johnson has repeatedly said that Britain should leave by end-October, even if that means accepting a no-deal Brexit. He has also said he will not request a further extension beyond October 31;
- Brexit has spawned a feature film called Brexit: The Uncivil War, which stars Benedict Cumberbatch. This is well worth watching, as the protagonist who engineered the leave victory in 2016 (Dominic Cummings played by Cumberbatch), is currently Boris Johnson’s chief adviser and the architect of

1 The author would like to thank Yavar Moini for several insightful discussions to better understand what could happen with Brexit.
the PM’s hardline strategy (Cummings could play a similar role as did Steve Bannon in getting Donald Trump elected in 2016). The point is, Brexit is now a media event with a pop culture appeal;

- Boris Johnson has lost the majority in the House of Commons (HoC), and has thrown out 21 prominent Tories from the Conservative party;
- Boris Johnson has twice failed to secure HoC’s support for snap elections in mid-October;
- Boris Johnson has not been able to stop a new law that decrees that the British government cannot consider a no-deal Brexit. Hardline Brexiers call this the surrender document;
- Boris Johnson has suspended parliament for five weeks, which most observers view as a blatant attempt to stifle parliamentary discussion about the impact of a no-deal Brexit;
- As per tradition, Queen Elizabeth is scheduled to address the country on October 14, where she will put forward the government’s agenda for the parliamentary year. In normal times, the Queen’s speech would be followed by a vote of confidence, and MPs would go about their business. What happens this time around, remains uncertain;
- The Scottish Courts have declared that the suspension of parliament is illegal. The English Courts have dismissed the judgment of the Scottish Courts, and the matter is now with the Supreme Court. Observers are not sure what will happen, but many feel the Supreme Court will want to avoid judicial intervention as this would create a new precedence in British politics; and
- Media reports claim that while Boris Johnson remains adamant that Britain will secure a special deal from the EU, he is playing hardball and aggravating the EU’s leadership.

Who’s in charge?

Despite the media lampooning of Boris Johnson, we believe he will remain in the driving seat and will shape the final Brexit outcome. Together with Dominic Cummings, Boris Johnson knows that the doom and gloom of a no-deal Brexit will not sway Britons. As they saw in the 2016 referendum, voters make their decisions based on emotions rather than hard economic arguments.

To get a better handle on what could happen, let’s look at the three main players and summarize their thinking.

A. The European Union.

Even before Brexit became a noun, the EU faced many challenges. With an unhinged US President, France and Germany realize that the EU must remain united to retain its importance in the changing geopolitical landscape. It cannot be seen as making exceptions for member states seeking to leave, as this could create fissures within the EU. The fiscal austerity imposed by Germany has been criticized by nationalist parties, which are gaining political power in Europe. If Britain gets a “deal”, it will be hard for Brussels to impose discipline on other member states, especially the more problematic ones (e.g. Greece, Poland, Austria and Italy).

With or without Angela Merkel, Germany knows that its global power comes from its economy, and the latter had thrived in the common market. Similarly, Macron (who likes the taste of global leadership) also knows that France can only play an outsized role if it is part of a strong and robust EU. In a nutshell, France and Germany must show that the advantages of the common market comes at a price – members have to play by the rules, and cannot make up their own rules.

B. MPs who are against a no-deal Brexit

A no-deal Brexit will cause economic disruption on both sides of the English Channel. It would require a hard border in Ireland, and is likely to push Scotland to seek independence from the United Kingdom. For many people, these are sufficient reasons to stay within the EU. However, it is important to note that Northern Ireland largely voted to leave in 2016, knowing this would create a hard border in Ireland. The
EU insisted on the Irish backstop on behalf of the Republic of Ireland, which is a full member of the bloc. This has been rejected by Brexisters, not because it would create a hard border in Ireland, but because the backstop will keep Britain in the EU’s customs union, which means the break from the EU will only be cosmetic.

In the case of Scotland, if a no-deal Brexit does materialize, the Scottish National Party (SNP) could begin to agitate for a public referendum to seek independence. However, given Scotland’s monetary, fiscal and commercial dependency on England, there are strong arguments that Scotland will not break from England. On the other hand, it is not clear whether the EU would invite Scotland to become a standalone member of the common market; Spain may object to Scottish membership as this could flare up Catalonia’s aspiration for independence.

Finally, this group of MPs have an interest in London’s global dominance in finance, insurance and the enforcement of trade contracts. Furthermore, with the Big Tech companies setting up their European operations in Britain, they are aware of the positives from such investments. All said, the English language and English jurisprudence have a strong grip on global affairs.

Having said this, most of these MPs have reservations about the EU, and would want to rework the terms of engagement to satisfy their respective constituents. Their problem with hardline Brexisters is the make-or-break attitude towards the EU. These MPs feel that Britain has the economic muscle and global clout to renegotiate with the EU, but not to do it too aggressively.

C. Hardline Brexisters

It is important upfront to make a distinction between Nigel Farage and hardline Brexisters. Nigel Farage has been a member of the European parliament since 1999, and remains a vocal Eurosceptic. He recently created the Brexit Party, which has extreme views – as a politician, he is considered toxic.

The people who define this group are Boris Johnson, Jacob Rees Mogg and Michael Gove. Given his pivotal role in delivering the shock result in 2016, Dominic Cummings should be viewed as the driving force behind Boris Johnson. As Boris Johnson’s chief strategist, Cummings is most likely responsible for the PM’s early missteps, but this should not create the impression that the PM has failed. The Johnson-Cummings duo has the power to shape the public debate, which will be seen in the next elections (more later).

The intentionally disheveled but charismatic Boris Johnson, is a seasoned politician with a strong sense of history. Johnson believes that he comes from the same mold as British leaders like Winston Churchill and Margaret Thatcher, and perhaps also thinks that great leadership will only blossom when the country is facing a crisis. This means that even the threat of a no-deal Brexit would give Boris Johnson a platform that he would seize, and relish.

However, Johnson does not want a no-deal Brexit. What he wants is a firm commitment from the British people to play hardball to secure a better deal from Brussels. From Boris Johnson’s perspective, if Brussels knows that Britons are willing to accept a no-deal Brexit, this will strengthen his hand in the final round of negotiations. This is brinkmanship, pure and simple, which Johnson feels he is in a position to play, and more importantly, to win.

Riding the global wave of nationalism (which Cummings can claim to have started in 2015), Britons could be lured into demanding a no-deal Brexit. Cummings is an anarchist, which makes him very...
dangerous for traditional British politics. In our view, the Johnson-Cummings team is a formidable force that could end many political careers and transform Britain’s political narrative. This duo understands the public frustration with Brussels, and knows how to appeal to British pride and its lost glory.4

Far from apologizing for how the Tories have bungled the Brexit referendum, Cummings and Johnson are likely to launch a blistering political campaign that could sway the next vote.5 Despite the dire scenario of a no-deal Brexit, hardline Brexeters have greater clarity of what they seek to achieve, and this clarity may sway public sentiments.

How this could play out

We would summarize the outlook as follows

- We do not see the British House of Commons reconvening before October 15. With the release of the Yellow Hammer report, there is little more to gain from a parliamentary debate about the cost of a no-deal Brexit, as the consequences are now public.

- To steer Brexit, Boris Johnson will have to remain the Prime Minister. This means he needs to avoid a vote of no-confidence, which would pave the way for a time-bound unity government. However, with the EU summit scheduled for October 17 and 18 (just two days after reconvening), there is little time for this unity government to be formed, which could then negotiate with the EU.

- This means Boris Johnson (as PM) would have to ask for an extension as he is now rule-bound not to advocate a no-deal Brexit – he would very publically have to eat his own words. The EU is likely to enjoy Boris Johnson’s discomfort, and will “reluctantly” agree to the extension (the EU would not want to be blamed for a no-deal Brexit two weeks later). Let’s assume the EU extends the deadline till end-December 2019, but states that it will not change the deal that Theresa May was offered.

- Humiliated by this experience, and facing a hostile parliament, Boris Johnson could either demand snap elections or ask for a second referendum on the Brexit issue. Many would prefer a second referendum, but as the Brexit issue cuts across party lines, seasoned politicians would realize that another referendum would further damage their political parties. It would become obvious that rightwing and leftwing policy debates are being overshadowed by the stay-leave divide, which would make future political campaigns more challenging.

- In view of this, Boris Johnson is likely to propose snap elections, with a clear understanding that this would also be a referendum on Brexit. This would give Tories and Labourites the opportunity to forge their platforms, and ensure that party members stay with the party line. With Labour likely to push for Remain, it will gain the support of the SNP, the Liberal Democrats and independents.

- Snap elections will allow Boris Johnson to remake the Conservative party, and impose his strategy that Tories must accept the possibility of a no-deal Brexit, to make it easier to secure a deal from the EU. He will have to ensure that if Tories win the elections, the HoC will have to rescind the recently promulgated law against a no-deal Brexit. Boris Johnson will package the election as a referendum

---

4 Cummings and Johnson could charge up public sentiments by talking up Britain’s past (i.e. facing down the fascist threat from Germany and Italy in WW2) and its resilience to stand alone (the blitz of London, Dunkirk and the Battle of Britain). By highlighting the impact of their little Island on the world, this will surely gain traction in Britain, while the disruption of a no-deal Brexit could be used as the adversity needed to show what makes the English so unique.

5 In our view, there is little difference between a second Brexit referendum and snap elections, as both votes will focus on Brexit.
with two stark choices: (1) Brexit by end 2019, even if this means the no-deal option; and (2) stay with the EU, and its current terms of engagement. The EU would publicly support this clarity.

• In the run up to the elections, Cummings is likely to take charge of the leave campaign. Britain is likely to witness a bitter political campaign, but the greater clarity of Brexiter and the political skills of Dominic Cummings, are likely to tip public support towards the Tories. As stated earlier, Britons are not likely to vote according to traditional party lines, which means voters will be open to debating much broader issues. This will create the space for political manipulation.

• With a public mandate to walk away from the EU without a deal, Boris Johnson would then be able to bully the EU into a sweeter divorce deal. Facing the real possibility of a no-deal break, public pressure in France, Spain, and other EU countries that trade heavily with Britain, will finally come into play. Till now, only the British public has had to weigh in on the issue, but if Johnson has the mandate to walk away, he will force Europeans to weigh in. Since Europeans have a strong voice in government policies designed for their social protection, they will put tremendous pressure on EU’s leadership not to allow for a no-deal Brexit.6

• In terms of the deal, Boris Johnson will insist on two issues: (1) the EU must drop the Irish backdrop, which means border controls would be required in Ireland; and (2) the free movement of people between Britain and the EU must be checked (in our view, this is the real reason for the leave vote). Johnson could then negotiate quid pro quo trade arrangements with EU countries to ease political pressure on both sides of the Channel. In all likelihood, the EU will concede much more compared to what it offered Theresa May.

• Even with a deal, Britain’s economic relationship with the EU will change substantially. The extent of these changes will depend on the negotiations, but it is highly unlikely that Britain would be able to retain the positives and reject the negatives. Britain’s economy would have to adapt even if Boris Johnson secures a deal.

What are the possible outcomes?

**Chart 1** shows what could happen if British MPs call for snap elections. We assume a well-defined Labour coalition and a unified Tory party, which is able to secure votes from the Brexit Party.7 If the Tories win, they will talk to the EU with greater political clout. However, as shown, the EU still has the final say on whether it would offer Britain a deal. As shown in **Chart 1**, there are three distinct outcomes.

A. "**No-deal Brexit.**" This shows what would happen if the Tories win the elections, but Boris Johnson is unable to secure a deal from the EU. This means the EU stands firm to protect the common market, even at the cost of economic disruption. This would be a *stable* equilibrium,

---

6 Europeans will suddenly have to grapple with the idea of losing the second largest economy in the common market. With less time to prepare, and the fear that a no-deal Brexit could stoke nationalist sentiments across Europe, EU’s leadership would lose bargaining power.

7 We do not see a formal alliance between the Tories and the Brexit Party, as Nigel Farage is a wild card.
as Britons have voted knowing that a no-deal Brexit is possible, while the EU could argue that Britain wanted too much and was being stubborn.\(^8\) In this scenario, Britain will have to create a hard border in Ireland, and both Britain and the EU would have to clarify the legal status of their nationals living on the other side of the Channel.

**B. Brexit with a deal.**
The Tories win the election, and Boris Johnson uses the people’s mandate to get what he wants from the EU. While this would be a significant political victory for Johnson, it could also be the beginning of the end for the European Union. At the initial stages, this scenario would boost both economies (Britain’s and the EU), but it could politically weaken the EU as member countries use Britain’s perceived victory to push for better terms with the EU. This will be particularly challenging with member countries that use the Euro, and must follow a fiscal master plan. This outcome will put tremendous pressure on Germany (the EU’s fiscal watchdog), and may force the founding members to consider removing some countries from the EU. While economically positive at the initial stages, this is an *unstable* equilibrium.

**C. Remain in the EU.**
If the Labour coalition is able to secure a majority and forms the next government, Britain would immediately inform the EU that it intends to stay within the union. This will be welcomed by the EU, and used as a cautionary tale for those members who are unhappy with Brussels. However, the Labour coalition is not likely to act collectively on non-Brexit issues, especially the hardline socialist policies that Jeremy Corbyn has been advocating. More simply, after Brexit is no longer an issue, the new government will not have a coherent policy agenda and could quickly become dysfunctional. This would be an *unstable* equilibrium, whereby the Tory opposition could keep flagging immigration and Brussels’ interference to keep alive their dream for better terms with the EU.

**Some analytics**

If we assume that the Tories win with a 5% margin (or \(X = 0.55\), see Chart 1), and the EU does not stand firm (or \(Y = 0.20\), or an 80% chance that the EU gives in to Britain’s demands), the probability distribution for Scenarios A, B and C are: 11%, 44% and 45%, respectively. This is a bit surprising as it implies that Britain is just as likely to *remain* as it is to get a deal from the EU. It also shows that if the EU is stricter in its bargaining (say there is only a 40% chance that the EU would concede to Britain’s demands), the probability distribution for A, B and C would be: 33%, 22% and 45%, respectively. This means the only stable outcome (a no-deal Brexit) only has a one-third probability of being realized.

In effect, this model shows a near-certainty that either Britain or the EU would face political instability.\(^9\) It also means the most stable equilibrium – a no-deal Brexit – is also economically the most damaging. This is a Lose-Lose situation for both Britain and the EU, and there is no way to start again. David Cameron’s political miscalculation with the 2016 referendum, will either have an economic toll or a political toll on Britain and the EU. The interesting insight is that if the EU remains principled (\(Y = 1\), which means the EU will not negotiate with Britain), it will create the most stable outcome but also maximize the chances of a no-deal Brexit. By our assumption, this could happen as early as 2020.

---

\(^8\) The political stability comes from the fact that both Britain and the EU remain firm on their principles, and are willing to accept the economic costs. An unstable equilibrium is where the outcome itself plants the seeds for political discontent, which spreads and could undermine the ruling government.

\(^9\) Since B and C are unstable equilibria, this means there is an 89% probability that either Britain or the EU will experience political instability in the near future.
How will this impact Pakistan

Since Pakistan’s economy is not driven by its exports, a no-deal Brexit will not have a direct impact on the country. Furthermore, Pakistan doesn’t export fresh produce or processed foods, which are markets that could open up on both sides of the Channel. However, Pakistan will be impacted indirectly, as a no-deal Brexit will surely push Britain and the EU into recession, and possibly tip the US economy into recession as well. In this environment, Pakistan will find it challenging to increase exports in the years ahead. The only plus point of a global recession is that it could soften oil prices, which should help the country.

For the small number of Pakistanis who own businesses and assets in England, a no-deal Brexit will hurt. Property values in London are already down, and are likely to fall further with a recession. However, we would argue that a no-deal Brexit and the global economic slowdown, may actually suit Pakistan. As the next 12-18 months will be tough with the on-going IMF stabilization program, the economic pain in Pakistan will be easier to bear when seen in the context of a global recession. As the saying goes, misery loves company.

History matters

David Cameron recently gave an interview to Tom Bradby to promote his recently published memoirs. In it, Cameron apologized for the Brexit mess and held himself responsible for how the remain campaign was run, the final vote and the chaos that ensued. However, he shocked most viewers when he said that he would do it again – that is, he would again allow Britons to decide whether to remain or leave the EU. In our view, Cameron is being honest on both counts: he does regret how the 2016 referendum was managed and its aftermath, but he would still have opted to let the people decide. To understand this apparent contradiction, readers should have a sense of how complicated Britain’s relationship with Europe is.

History is a useful guide. Britain’s request to join the European Economic Community (EEC) was rejected by France in 1963 and again in 1967. Just two years after it joined the common market in 1973, the Labour government held a public referendum to determine whether Britain should remain in the union. Subsequent decades have witnessed wild swings in how Britons view Europe: Margaret Thatcher was a Eurosceptic while Tony Blair once considered adopting the Euro. This confusion remains: after the abovementioned interview, Bradby said he was shocked that Cameron could lead the remain campaign as PM, while in his memoirs he “comes across as a raging Eurosceptic.”

Britain’s ambivalence towards the EU can partially be explained by the fact that unlike most other EU members, by having its own currency, Britain has complete fiscal and monetary autonomy from the EU. Furthermore, the Brexit chaos has overshadowed an inconvenient fact: the EU is not sustainable as an economic bloc. The unending economic turmoil in Greece is a reflection that German discipline can only be matched by Greek freeloading. The issue is whether countries with such distinct characteristics could belong to the same economic club?

Brexit may be an existential threat to the EU, but even before Brexit became a thing, there were valid questions about how long the EU would last.

Conclusion

Britain has a celebrated history, while its bureaucracy is very much a part of British culture (think Yes Minister). With Dominic Cummings’ political smarts and the English being used to setting the rules (not following them), it is not a stretch to characterize Brussels as anti-democratic (and perhaps anti-British);
to stir up emotions of how England stood up to fascism and did so alone; and to convince EU leaders that they stand to lose if they kick Britain out without a deal. Emotions will run high in the snap elections, and Britons are likely to participate vigorously.

In our view, Boris Johnson will take many knocks but still remain PM; he will call snap elections; Cummings will help him win these elections; and Boris Johnson should be able to secure a deal with the EU. In short, Boris Johnson may actually win. But the victory will not be at the expense of the Europeans, but against the vision of the founding leadership (France and Germany) about what the EU should be.

Even if Johnson manages to secure a deal, Britain and the EU will not be the same. Both will have to adapt their economies, and trade flows will ease and cross-border immigration is likely to fall sharply. Britain will promote its national identity, and London may lose some of its global luster. This adjustment will negatively impact the global economy, but President Trump will welcome the change and offer Britain trade deals. Lastly, the EU will have to rethink what it seeks to be, and could shrink in size.

As this all plays out, expect lots of political drama. For my part, I look forward to stirring speeches by Boris Johnson (playing Winston Churchill), and the next feature film on Brexit (with Benedict Cumberbatch reprising his role as Dominic Cummings).