



Political paralysis grips the UK even as May hangs on to office

British Prime Minister Theresa May defeated the no confidence motion in her as leader of the Conservative Party by 200 votes to 117 of Conservative Members of Parliament.

Under the Conservative Party leadership rules Theresa May cannot face another leadership challenge for twelve months, although she was forced to concede that she will not lead the Conservative Party into another general election. But sooner or later she will face another challenge to her Premiership, when the Labour opposition table a motion of no confidence in her government.

Despite successfully fending off the challenge to her leadership of the Conservative Party, political paralysis continues to grip the UK as it stumbles towards leaving the European Union in March next year.

Prime Minister Theresa May remains in office but not in power, trapped between a parliament united only in opposing her withdrawal deal and an EU unwilling to make concessions - notably on the so-called 'backstop' to prevent a 'hard border' on the island of Ireland that is opposed by so many parliamentarians, including the ten MPs of the Northern Ireland Democratic Unionist Party (DUP) that underpin her slim majority in the House of Commons.

The Irish backstop arrangement is insurance against the failure of the UK and EU to reach a new trade arrangement after Brexit that would

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avoid a 'hard border' between Northern Ireland and the Republic of Ireland, the only land border between the UK and the EU.

An open border on the island of Ireland is a key element of the 1998 Good Friday agreement that brought an end to the violence that scarred Northern Ireland over previous decades.

Under the backstop the UK would remain in a customs union with the EU (with the EU setting a common external tariff on imports from the rest of the world) along with close 'regulatory alignment' between Northern Ireland and the EU. Under the draft Withdrawal Treaty the UK could not leave the backstop without the consent of the EU. The DUP oppose the backstop because it implies a different status of NI relative to the rest of the UK.

Brexit leaning MPs also reject the backstop because the UK will be locked into the 'temporary' backstop possibly indefinitely and unable to strike new independent trade deals with other countries such as the US.

Prime Minister May will attend the gathering of EU leaders today and tomorrow but is very unlikely to secure a revision to the draft Withdrawal Agreement Treaty she has negotiated. She will return from Brussels with, at best, a 'clarifications' on the temporary intent of the backstop but it is doubtful that it will be sufficient to secure support for her deal from the DUP and the 117 Conservative MPs that voted against her in yesterday's leadership no confidence motion to be approved by parliament.

The Prime Minister has committed to submit the withdrawal agreement she has negotiated with the EU to parliament by the 21 January. In the event that her deal is voted down, parliament will be forced to make the difficult decisions it has so far shied away from, if it is to avoid an economically damaging 'no deal' EU exit on 29 March.

A 'no deal' exit would be without a transition period (under Theresa May's deal the UK would effectively remain a member of the EU, albeit without a political voice, until December 2020) and extensive disruption to trade and financial flows between the UK and EU.

The options facing the majority of MPs that wish to avoid a 'no deal' Brexit, including those Conservative MPs that unenthusiastically backed Theresa May in yesterday's no confidence vote but are unwilling to support the current withdrawal agreement, are limited as the clock ticks down to 29 March.

One option would be for parliament to agree new terms of withdrawal that are acceptable to the EU including assurances on avoiding a hard border in Ireland. Such a proposal would require conceding at least some of Theresa May's 'red lines' on free movement of people, role of the European Court of Justice and continuing payments into the EU budget.

Alternatively, parliament could instruct the government to revoke Article 50 – the notification of leaving the EU – but it is very fearful of doing so in defiance of the EU referendum vote in June 2016.

The remaining option would be for parliament to pass legislation for a second referendum, an option Theresa May has consistently rejected, and the precise question posed to the public would be highly contentious. Parliamentary support for a second referendum could only be secured after the opposition Labour Party has tried and failed to pass a parliamentary vote of no confidence in the government in an effort to force a general election.

It is evident that Theresa May's success in fending off the no confidence vote in her leadership of the Conservative Party does not change the unpleasant parliamentary arithmetic against the withdrawal deal she has negotiated nor the hard choices that the UK must urgently address.

In our view, only when the UK is on the brink of a 'no deal' exit and the EU steps up its preparations (already well advanced of those of the UK) for a no deal Brexit will parliament break out of its paralysis.

Parliament will either put the issue back to the public in a second referendum, trigger a general election or propose a 'soft Brexit' whereby the UK retains the obligations as well as benefits of EU membership but without political representation in the EU institutions (a 'Norway style' arrangement). But the possibility that parliament fails to act to prevent a 'no deal' exit on 29 March cannot be discounted despite the majority of MPs being against such an outcome.

The political crisis that is already imposing a meaningful economic cost on the UK will intensify over the coming weeks and continue to weigh on the value of the British pound and sterling assets. The UK is far from cutting the Gordian knot of Brexit.

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