



Countdown to Brexit— 10 Days to Go

An extension to Article 50 and a no-deal exit are the most likely scenarios.

March 2019

The UK remains scheduled to leave the European Union (EU) on March 29, although it is unclear whether this will happen and under what terms. The prospect of Theresa May's deal with the EU being brought back to Parliament for a third time seems to have diminished sharply following an intervention from House of Commons Speaker John Bercow. This has increased the likelihood of both an extension to Article 50 and a no-deal Brexit.

In the third of a series of updates, Quentin Fitzsimmons, fixed income portfolio manager and T. Rowe Price's resident Brexit specialist, provides an overview of the current state of play.

What Are the Potential Scenarios?

We have previously outlined four scenarios:

1. After several votes, Parliament finally agrees to a modified version of the deal that the UK government has agreed with the EU and the UK leaves the bloc on March 29.
2. The UK government fails to get a deal approved by Parliament and the UK exits the EU on March 29 without arrangements in place



Quentin Fitzsimmons
Fixed Income Portfolio Manager

and with no transition period to enable businesses and people to prepare. UK trade with the EU would immediately be governed by World Trade Organization rules.

3. The UK seeks—and is granted—an extension to Article 50, the legislation that sets March 29 as the legally binding exit date from the EU, to give the UK government more time to get a deal approved by Parliament. This could potentially involve the UK electorate voting on the deal in a second referendum.
4. Prime Minister Theresa May decides to call a snap election in a bid to increase the ruling Conservative Party's majority and make it easier to push a deal through. However, time has almost certainly run out for this scenario.

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What Has Changed Over the Past Two Weeks?

UK Prime Minister May’s EU withdrawal deal was rejected by Parliament by a large majority for a second time, albeit by a smaller majority than when it was dismissed in January. Members of Parliament (MPs) were not convinced by the fresh legal assurances on the Irish backstop that Prime Minister May had agreed with the EU.

Parliament then voted to reject a no-deal Brexit under any circumstances, although the vote was nonbinding and under current law the UK could still leave without a deal on March 29. The following day, MPs voted by an overwhelming majority to ask the EU for an extension to Article 50.

Next, an amendment that would have effectively shifted control of Brexit to Parliament if May’s deal was rejected for a third time was very narrowly defeated. MPs also rejected a second referendum, although the proposal could return to Parliament at some point.

Finally, in a dramatic intervention the Speaker of the House of Commons John Bercow said that Prime Minister May will not be able to bring her deal back to Parliament for a third vote if the motion remains “substantially the same”. Citing a convention that dates back to 1604, Bercow said that the government would not be able to repeatedly put the same bill before Parliament if it had previously been rejected. This means that in order to put May’s deal before MPs again, the government will have to find a way of materially altering it—something that will be difficult to achieve in the time frame.

Based on Events Over the Past Week, What Are Market Expectations About the Likelihood of the Various Outcomes?

Leave with May’s deal and letter of comfort on Irish backstop	10%	↓
No-deal exit on March 29	50%	↑
Extension to Article 50	40%	↑
Snap election	0%	↓

Source: T. Rowe Price; as of March 15, 2019.

What Are the Current Prospects for Financial Assets Given the Most Likely Outcome Above, in Your View?

Fixed income: While the prospect of a sharp depreciation of UK assets may have diminished after Parliament voted against leaving the EU without a deal, uncertainty over Brexit is likely to weigh on the UK economy for a longer period, keeping credit markets subdued. If an extension to Article 50 does not materialize and the UK leaves on March 29, credit markets will be hit, which could create opportunities to purchase corporate bonds whose values have fallen far below their fundamental quality.

Equities: Investors in UK stocks are looking for one of two things to occur: either tangible evidence of whether, when, and how Brexit is likely to occur or a shock that brings a deep discount and therefore a buying opportunity. At present they have neither, so it remains a matter of wait and see for equity investors.

Currencies: There has been extensive buying of sterling, indicating a widespread conviction that the currency is likely to appreciate. However, this position could be vulnerable if a no-deal Brexit unexpectedly materializes at the last

minute or an extension to Article 50 is offered that does not result in the anticipated relief rally. Companies have been building inventories as a precaution against Brexit and may destock if Article 50 is extended, resulting in lower growth.

What We're Watching Next

As things stand, it seems unlikely that May's deal with the EU will come before Parliament again. However, this still could happen if the government finds a way to substantially alter the motion. If the deal is presented to Parliament again and is approved, the UK will ask the EU for a short technical extension to Article 50 to ensure the necessary legislation is enacted. The request for an extension is highly likely to be granted in these circumstances.

If the government cannot put May's deal before Parliament again or does so and it is rejected, it will likely ask the EU for a longer extension to Article 50. However, all 27 EU leaders would have to agree to an extension, and it is not clear whether they will do so. Even if an extension is offered, it could come with strings attached—for example, the EU could ask the UK government to hold another referendum or a general election to resolve the country's political impasse.

If the EU does not agree to an Article 50 extension or offers an extension under terms that the UK finds unpalatable, and May is unable to present her deal to Parliament again, the UK will very likely exit the EU on March 29 without a deal.

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