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# The Prize of Sovereignty

*Through the Looking Glass*

## **RaboResearch**

Global Economics &  
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This column is part of our new *"Through the Looking Glass"* series, in which we discuss unconventional ideas that challenge mainstream thinking. By turning the world upside-down we hope to glean valuable insights into an increasingly complex world. These thought experiments do not necessarily match our house view.

***"Who in the world am I? Ah, that's the great puzzle."***

– Alice's Adventures in Wonderland, Lewis Carroll

### **What if... the Brexiteers are right and Brexit is a great success?**

The bullish predictions and forecasts of the Brexiteers make an easy target for most commentators. A truly 'Global Britain' could easily obtain a pivotal role in an ever-changing world, and a vote for Brexit would be a vote to unleash this enormous potential. Yet in reality, only relentless uncertainties have been unleashed. This has led to a notable slowdown in economic growth, primarily due to structural weaknesses in business investments.

But even then. One of the more compelling arguments for Brexit has always been that the world's centre of gravity is shifting away from Europe. This still holds true. And sometimes it is necessary to take one step backward to take two steps forward. So even though it's very clear that Brexit presents its challenges, now is not the time for naysayers. Instead, it's time that the government takes full ownership of Brexit and starts sowing the seeds of its opportunities.

### **Packing quite a punch**

Because the UK still has a lot going for it. For a relatively small country, it packs quite a punch. It has a permanent seat on the UN Security Council and leading roles in NATO and the G7. The UK has plenty of world-class institutions, hosts some of the world's best universities, and can rely on a highly-educated workforce. It also has the capabilities to make full use of this workforce. The UK is an important centre for technology and research, while the City of London is one of the world's leading financial hubs. Indeed, its open and liberal markets are well equipped to find the perfect match between human, physical and financial capital.

It doesn't stop here. The UK is also a "soft superpower". English remains the global lingua franca through which much of the world's media, art and culture is expressed. In sports, for instance, the Premier League reaches hundreds of millions of people across the globe. Even though the direct and indirect economic value is hard to quantify, it is certain that the UK's central role in global society is a key strength that will continue to draw people to look to the country in a positive way.

### **Heading straight for the exit**

The government is banking on this. It sees the UK in a unique position to act on the premise of strength, and clearly expresses that there is no will to be subservient to EU technocrats. The forthcoming choice to not accept dynamic alignment with EU rules and regulations shows that the government's primary objective is to recoup its full sovereignty. The simplest way to achieve this is to head straight for the exit, to negotiate a very basic free trade agreement, and to explore other opportunities elsewhere.

### **Time for the mavericks!**

Standard economic theories predict that this will lead to economic disruption. This might well be, but prime minister Johnson is not afraid of a controversy. In fact, his chief strategic adviser, Dominic Cummings, thrives on chaos. He currently leads a recruitment drive to overhaul the civil service, aiming to hire *"weirdos and misfits [...] who are dissenters, who are maverick and who have a different point of view"*. With a new band of nonconformists, the government should use Brexit as a catalyst for positive change, using the expected disruption as a platform to force radical changes to the current economic system.

## Never let a good crisis go to waste

Because it's clear that the post-Thatcher consensus only works for the few, not the many, and has effectively passed its expiration date. Inequality is one of the country's many economic challenges that finds its roots in weak productivity growth, which in turn is particularly evident in the domestically-oriented sectors and companies. The prime minister has won the confidence of the voters in the relatively unproductive Red Wall. He must now repay their trust while keeping the Tory shires happy at the same time.

It was Winston Churchill who first said: "*Never let a good crisis go to waste*". Indeed, Brexit is a challenge *and* an opportunity: the vast impact of Brexit on economic output is expected to come from knock-on effects on productivity. The future of Brexit and of Johnson's government will therefore depend on the prime minister's abilities to address long-standing productivity challenges.

## Open up, open up

The government should therefore take the lead in an investment push to improve the performance of the 'long tail' of unproductive companies. Once the UK is no longer subject to stringent EU state-aid rules, there is greater scope to implement selective industrial policies. This should encourage R&D spending, innovation and new technologies and make up for the expected loss in private FDI. The government should also counteract the impact of rising UK-EU (non-tariff) trade barriers by fully opening up its trade routes with the Americas and Asia. The reduction of a broad set of import tariffs could provide UK consumers and businesses with lower-cost or better-quality imports, which generates increased competition, stimulates innovation and re-accelerates creative destruction. Not being tied to the EU's rulebook, the UK will also experience that it will have the freedom to relax burdensome regulation. And the proposed points-based immigration system keeps low-skilled workers out, while the UK remains accommodative to talent. As the marginal price of labour to capital will then undoubtedly rise, firms will finally be incentivized to start investing more.

## Push on the gas pedal

It is expected that such a radical transition will provide a short-term shock to the economy. But there is no doubt that the government can ease this transition and avoid a deep recession, provided that it simultaneously stimulates demand. We could very well expect Johnson's 'mavericks' to take such an MMT view of the economy, which argues that a recession is effectively nothing more than a spending gap. They will then quickly come to the conclusion that a recession is the result of a government spending too little. Fortunately, this could be easily prevented. The UK is no longer bound to the archaic Stability and Growth Pact, and there's no obligation to follow some made-up fiscal rules.

The first thing that it should therefore do is to announce a war on poverty, which in itself leads to an unproductive workforce. This will go a long way in dealing with the short-term shocks, while it helps to paint the Red Wall deep blue. Along the way, the 'mavericks' may even conclude that a truly sovereign nation will never experience a debt crisis: as long as its liabilities are denominated in its own currency, a country will always be able to service its nominal debts. Downing Street 10's recent capture of Downing Street 11 and the appointment of Rishi Sunak – a yes-man Chancellor – already gives a good clue as to which direction public finances are going: the UK is ready to push on the fiscal gas pedal. Expect assistance from the Bank of England, too.

## A one-size-fits-all Europe is doomed to fail

Brexit will soon prove to be a very interesting test case of a new economic model, one that is miles away from the current neoliberal consensus. The quite presumptuous conception that the UK itself will be the biggest loser of Brexit may therefore not stand the test of time.

A successful Brexit will then undermine everything that the EU stands for. Other member states will use it as an example to rethink their economic model, and to try to exploit their own strengths rather than to blindly follow EU-made rules and regulations. The EU will then soon learn that a one-size-fits-all Europe is doomed to fail. Indeed, internal unravelling will become a very realistic threat.

## Through the Looking Glass

This column is part of our *Through the Looking Glass* series. Read more unconventional ideas in earlier publications:

1. [Hooray for Protectionism\(?\)](#) by Michael Every, 17 January 2020
2. [The Red President](#) by Philip Marey, 14 February 2020

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A summary of the methodology can be found on our website [www.rabobank.com](http://www.rabobank.com)

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