

TRENDMACRO LIVE!

On the Brexit Referendum

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A big “screw EU.” But good for the UK, and ultimately Europe too. It’s a buying opportunity.

Britons have voted to leave the European Union, defying the relentless campaign of self-interested fear-mongering by [global elites](#), [central bankers](#), [speculators](#), [financial media](#), [trading firms](#) and [bookies](#). *We defy it too. We think this will turn out to be good for the United Kingdom, and good for Europe, and that the market panic going on as of this writing will be short-lived, and a buying opportunity.*

- The polls and the “prediction markets” were wrong – [just as they were a year ago](#) in the UK general election. *So there is a surprise for markets here, and that surprise occurs against the backdrop of fears stirred up in the campaign.*
- *But we think these fears have been based all along on gross inaccuracies and exaggerations* (see first [“Brexit: Opening Pandora’s Brox”](#) May 23, 2016 and most recently [“On the June FOMC”](#) June 15).
- To be sure, [all divorces](#) are messy and time-consuming. British Prime Minister David Cameron will [step down](#). And then various [uncertainties, delays and transaction costs](#) entailed by Brexit for a year or more will be headwinds for Britain, Europe and the world.
- *But those are small frictional costs, not big risks.*
- *Once again, we emphasize that the systemic risk that would have been entailed by the exit of any nation that uses the euro – even a small one like Greece – is utterly absent in the case of the UK, which has never been part of the common currency.*
- As a net importer – the UK will have no difficulty at all in quickly establishing new trade agreements with other nations, potentially on more favorable terms than it enjoys now.
- London will remain the financial hub of Europe, thanks to centuries of accumulated human, institutional and financial capital that cannot be created *de novo* in Milan, Brussels, Paris or Frankfurt.
- The biggest immediate risk we can think of is that speculators might use this as an opportunity to gin up an attack on the euro or fragile European banks or sovereigns. But such attacks can create, at most, liquidity issues – which at this point [the European Central Bank is quite prepared](#) to address with its existing tool-kit.
- And we suppose that a weaker sterling and euro will put pressure on China’s program to guide the renminbi lower against its reference basket of global currencies (see, among many, [“Yuan](#)

Update to strategic view

EUROPE MACRO, EUROPE STOCKS, EUROPE BONDS, FX:

The polls and the “prediction markets” were wrong. So the success of Brexit comes as a surprise to markets – and against the backdrop of months of fear-mongering by global elites. But the extreme reaction in markets overnight is, quite simply, ridiculous. We continue to think that the fears are false and exaggerated. There will be some costs and uncertainties, but this will make the UK better, and could make Europe better too. The UK will be free of over-reaching interference from Brussels, and Brexit opens up a dialog that could lead to the reform of the European Union’s autocratic, brittle and anti-growth governance. We reiterate our call to use this as a buying opportunity, and a chance to lighten up on haven assets.

[\[Strategy dashboard\]](#)

[Direction](#)” February 16, 2016). Overnight China has responded with a large but appropriate weakening, and so far it’s orderly.

- [And we must keep our eyes on Spain’s general election this weekend.](#) This is a do-over of the indecisive election last December, in which Mariano Rajoy’s ruling *Partido Popular* – having delivered reforms that have given Spain the best real GDP growth over the last three years of any major developed economy – nevertheless couldn’t muster the votes to form a government.
- In the wake of the Brexit vote, there’s a case to be made that the far-left *Podemos* will emerge in Sunday’s election as more of a power-broker, moving Spain toward populism and away from growth. Such a move would echo the boldness and embrace of change embodied by Brexit, but the situations are in fact quite different. Brexit is a nationalist-libertarian movement, and Podemos is an internationalist social-justice movement. Be that as it may, Spain is a large high-deficit country that uses the euro. It matters.
- By the way, here at home, our own nationalist-libertarian – Mr. Trump – has [congratulated the UK](#) on its move toward liberty and self-determination. His opponent, as of this writing, has not put out any statement.
- [But all in all, we reiterate our longstanding thesis – this is mostly a phony, politically driven scare. The extreme reactions in markets overnight are, quite simply, ridiculous.](#)

The politics at stake here is the wish, by the elites in Brussels and [their internationalist collaborators around the world](#), to perpetuate the autocratic governance structure of the European Union. As it stands, the EU is [by construction an unaccountable technocracy](#) that offers its constituents [inadequate opportunity to drive necessary corrections or innovations](#). [It is a structural impediment to growth.](#)

- [Brexit opens Pandora’s Box – now any nation can very credibly threaten exit in order to lobby for special treatment in Brussels.](#)
- This would have been the case to some extent even if the UK had voted to Bremain.
- Remember, Cameron was only willing to put Brexit to a vote in the first place because, on February 19, he was able to return from Brussels having won a package of [concessions that he demanded](#) for the UK – which he could claim were so favorable that, because of them, Bremain should surely carry the day.
- [According to Cameron](#), the package gets the UK “Out of the open borders. Out of the bailouts. Out of the euro. And out of all those schemes in which Britain wants no part.”
- With Cameron having won so many concessions from Brussels under the mere Brexit threat – and now with Brexit itself having prevailed – [other nations will demand concessions](#).
- It won’t just be nationalist movements. Why would integrationist Italian Prime Minister Matteo Renzi not demand his own package of concessions under a threat of “Itexit”? Surely he would like to get some relief for Italy’s banks from the EU’s new [Bank Resolution and Recovery Directive](#) – a version of Dodd-Frank for Europe, and

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a typical one-size-fits-all cramdown appropriate for some EA nations' banks, but not all, and least of all Italy's (see "[On the March ECB Policy Decision](#)" March 10, 2016). [There are hints already.](#)

- Such demands usually involve some measure of brinksmanship. We can imagine Renzi reminding Brussels that Italy is the fourth most indebted country in the world – and would make a real mess if it decided to leave the EU and, of necessity under the existing treaties, stop using the euro currency.
- Germany is willing to stare down little Greece over such threats – but Italy, or Spain for that matter, will be much more powerful negotiating counterparties – especially now that Brexit has demonstrated that most essential of all bargaining tactics: the willingness to walk away.
- If the UK had voted to Remain, perhaps Brussels would have felt stronger going into these inevitable negotiations. But now the elites know that the electorates of the nations they rule – with no accountability, they thought – will in fact, walk away. *That actually lowers the risk in future negotiations, because Brussels will fully understand the nature of the threat it faces across the table.*
- *Further, even in the absence of better governance, the European Union might at least be improved by an ever-changing network of negotiated bilateral concessions that fine-tune each nation's special place in the collective.*
- *But now, with Brexit having fired a shot across Europe's bow, perhaps we can do better – maybe fundamental governance reform now has a chance.*

Bottom line

The polls and the “prediction markets” were wrong. So the success of Brexit comes as a surprise to markets – and against the backdrop of months of fear-mongering by global elites. But the extreme reaction in markets overnight is, quite simply, ridiculous. We continue to think that the fears are false and exaggerated. There will be some costs and uncertainties, but this will make the UK better, and could make Europe better too. The UK will be free of over-reaching interference from Brussels, and Brexit opens up a dialog that could lead to the reform of the European Union's autocratic, brittle and anti-growth governance. We reiterate our call to use this as a buying opportunity, and a chance to lighten up on haven assets. ▶