

Brexit negotiations set to move to next phase

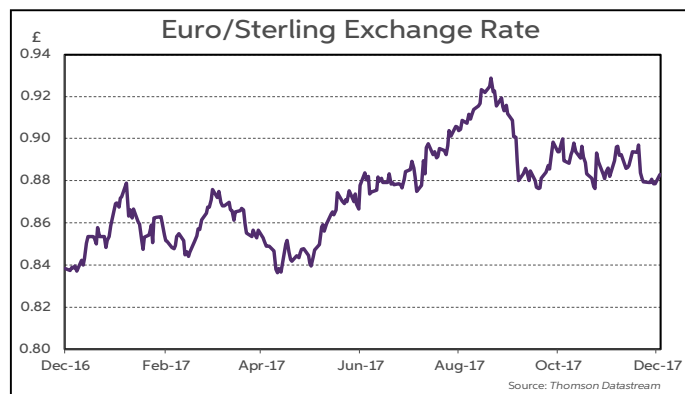
The European Commission is satisfied that sufficient progress has been made on Phase 1 of the Brexit negotiations between the EU and UK on the issues of citizens rights, the financial settlement and the Irish border to allow it recommend to this week's meeting of the EU Council that the talks can now move on to Phase 2. This will cover the transition arrangements to apply for a period of about two years after the UK leaves the EU in March 2019 and agreeing a framework for future trade relations between the EU and UK.

The move to Phase 2 is seen as increasing the prospect of a soft Brexit when the UK departs the EU in 2019. Both the UK and EU see the need for transition arrangements to cover the period between when the UK leaves and a full trade deal is concluded between the EU and UK, which it is hoped will be done by 2021. The fact that the UK has already indicated that it is prepared to continue to abide by EU rules during the transition period suggests that agreement should be able to be reached on this issue.

However, the UK's decision to leave the EU Customs Union when it exits the EU in March 2019 is complicating the Brexit process. Somewhat ironically, though, the UK has indicated that when it leaves the EU Customs Union, it is willing to form a new **UK-EU Customs Union during the transition period that will precisely replicate the existing arrangements.**

The really difficult discussions will be on future trade relations that will come into effect at the end of the transition period. The Phase 1 deal reached between the EU and UK has kicked to touch on this issue. The commitment in it to avoid a hard border in Ireland is not really compatible with the UK's desire to negotiate third country trade deals with its own tariff arrangements, following the end of the post-Brexit transition phase.

Customs arrangements will be the most difficult issue to resolve in the trade talks if there is to be a comprehensive free trade deal without barriers reached between the UK and EU post the transition phase. The **UK wants to retain all the benefits of free trade with the EU after its departure, while at the same time being able to negotiate free trade deals with non-EU countries,** offering them different tariff arrangements to the EU. It is hard to see how both these objectives can be achieved.



Michel Barnier, the EU's Chief Negotiator on Brexit, has clearly stated that by making the choice to leave the EU and Customs Union, **"the UK will naturally find itself in a less favourable position than that of a Member State"**. He also warned that the **post-Brexit trade arrangements "cannot be the equivalent of what exists today"**. A free trade deal will not equate to membership of the Single Market. The EU will also not allow the integrity of the Single Market to be comprised by a lack of border controls in circumstances where UK customs arrangements and regulatory standards deviate from the EU.

So the really tough discussions on the future trade and customs relations aspects of Brexit have yet to start. The UK will face some tough choices in terms of a **trade-off between regaining sovereignty and retaining access to EU markets.** Not surprisingly, then, the reaction of sterling was fairly muted to the deal struck to allow the Brexit negotiations move on to the next phase. As the Phase 1 document states "nothing is agreed until everything is agreed". **It may be some time before we know what Brexit really means. It would seem that the UK is moving slowly away from a cliff-edge, hard Brexit, but such an event still cannot be ruled out, possibly in 2021.**



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