

## THE EU IS THE MOST VULNERABLE ECONOMIC BLOCK OUT OF THE THREE MAJOR VULNERABLE ECONOMIC BLOCKS.

*The three major economic blocks that dominate the world economy are the USA, the EU and China. According to the IMF's 2019 projections, in nominal dollars, they accounted for 55% of global GDP. Of the 3 blocks, the US is the most decayed, the EU the most structurally unsound and China the most politically brittle. At the onset of this burgeoning crisis, it is the EU that is most at risk, because its structural problems has meant that its recovery from the 2008 financial crisis is the most partial.*

At the outset it is important to say that covering the final quarter of 2018 and the first quarter of 2019, the economic malaise besetting the global economy, as measured by profitability, output and global trade was deeper than the malaise which occurred just three short years ago at the end of 2015 and the beginning of 2016. According to Bloomberg, the IMF and other sites, current sentiment expressed by Chief Executives and Financial Officers is at its lowest for 26 years, and the change in sentiment has been dramatic as the "CFO Alliance" survey of 7,000 Chief Financial Officers has revealed: "Last year, more than 75% of survey respondents characterized their confidence in the global economy as strong or extremely strong, over ⅔ of this year's respondents did a complete reversal on this topic and characterized their confidence in the global economy as weak or extremely weak." <http://achievenext.com/wp-content/uploads/2019/01/2019-Sentiment-Study-Executive-Summary.pdf>

What the period at the end of 2015 and the current period share in common is that the collapse was ameliorated by the action of the major central banks and China's fiscal impulse. This should be qualified: it is far too early to judge whether the current malaise has been resolved despite the hunt for green shoots discovering a few such shoots. The key point here is how quickly the world economy has lurched from one mini-crisis to another, a matter of only 30 months.

In both cases the epi-centre for the slowdown is China. As Martin Wolf stated in his opinion piece in the Financial Times: "when China sneezes, the world economy catches a cold." (03/04/2019) He also cites figures which suggests that annualised Chinese GDP growth in December fell to only 4.4% the lowest in four decades. (Fulcrum NowCast data). It is correct to attribute the slowdown to China. China is the pre-eminent industrial economy, and it is always within the industrial economy that the seeds of a future economic crisis are laid.

### **Global Output and Trade.**

Marxist theory posits that investment drives production. Much of that investment took place in China. This investment not only produced industrial growth in China, but in many other areas of the world economy which provided inputs to the Chinese economy. The fall in this impulse is seen in Graph 1 prepared by *Trading Economics*. Investment growth fell from over 10% at the end of 2015 to a nadir of 5.3% by mid-2018 and has marginally risen to 6.1% for the first two months of this year. The growth rate currently is one quarter the rate that obtained before 2014.

Many commentators opine that this fall is inconsequential given that China has reached middle income status and now needs to boost consumption and services. The opposite is the case. Low investment has never served any economy very well. Just look at the United States itself where decay is endemic and where low paid "serving and servant" jobs are prevalent. It leads to low productivity growth and is one of the causes of inequality as the rich monopolise what little extra is produced.

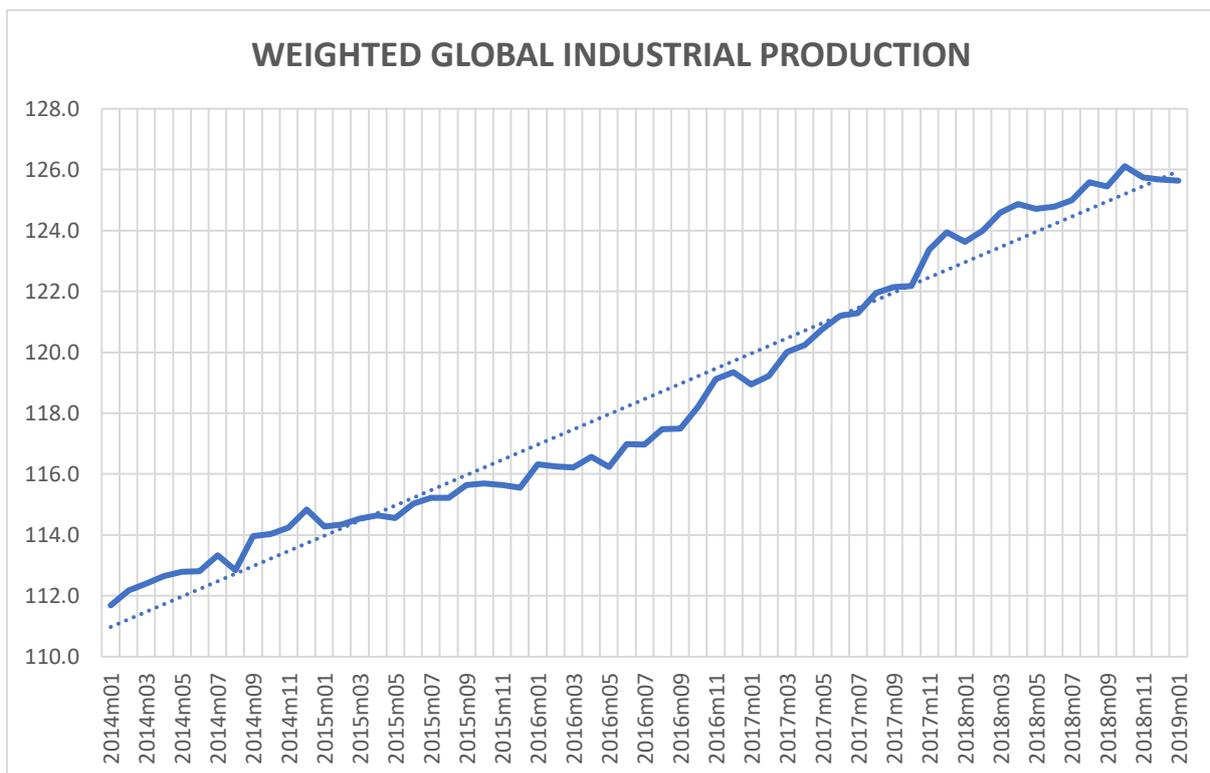
**Graph 1. Annual Fixed Asset Investment Growth (China)**



SOURCE: TRADINGECONOMICS.COM | NATIONAL BUREAU OF STATISTICS OF CHINA

One of the more insightful sites that is free to view is the *CPB Netherlands Bureau for Economic Policy Analysis World Trade Monitor*. Its most recent March report puts global industrial momentum at 0% (use link below Graph 2.) Over the last year global production has grown by under 1.5% all of which occurred in the first half of the year. Since July 2018 and for a period of six months, industrial production has flatlined. This duration exceeded that found in 2015/6.

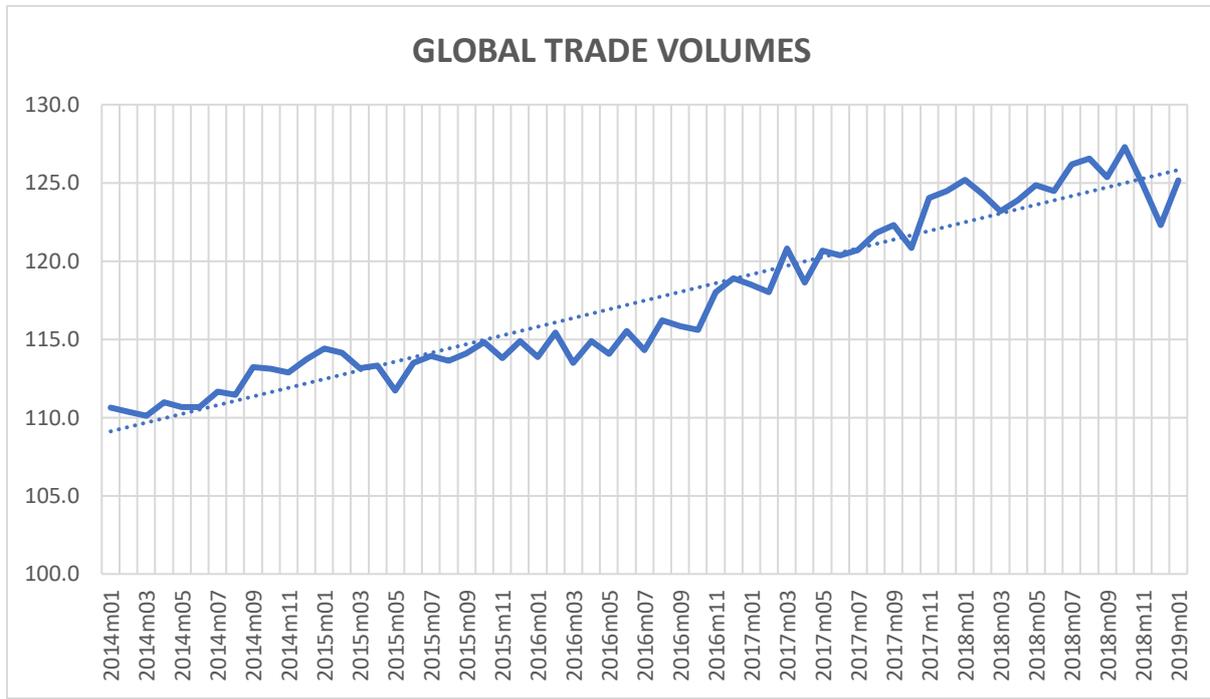
**Graph 2.**



<https://www.cpb.nl/en/worldtrademonitor>

The same stagnation appears when we examine global trade in goods provided by CPB within the same link (Graph 3). Global Trade has fallen in the second half of 2018 and in December it was no higher than in December 2018. Once again this fall has occurred over a longer period than before. Only part of this is due to the tariff war between the US and China.

**Graph 3.**



**Senile stock markets.**

*“There are three principal phases of a bull market: the first is represented by reviving confidence in the future of business; the second is the response of stock prices to the known improvement in corporate earnings, and the third is the period when speculation is rampant – a period when stocks are advanced on hopes and expectations.”* (attributed to Robert Rhea, *The Dow Theory*, 1932 cited by John Hussman <https://www.hussmanfunds.com/content/comment/>) (My emphasis added.) A senile market is one in which past lessons have been lost, the present is ignored amidst the fog of hope and expectation.

During the first quarter world stock market prices surged 11.4% according to the FT All World Index. This was the best start since late 2010. And yet as we shall see this recovery was built on sand.

Graph 4 below shows the extraordinary volatility that occurred in the leading stock index, the S&P 500, on Wall Street at the end of 2018. The two valleys and peaks far exceeded, both relatively and absolutely, the valleys and peaks that obtained in 2015/6. This is not surprising. The change in sentiment during the final quarter was more fundamental simply because it started from such a high degree of confidence in the economy at the time.

It was the reversal in the FED’s monetary stance, not a change in hard data that revived risk taking once again. It is part of the language of Wall Street never to bet against the FED. It is likely this homily is hardwired into the various algorithms that drive much investing these days. But we can go further. A quant working for J P Morgan has just declared that central banks have vanquished the business cycle. I remember a Chancellor of the Exchequer uttering the same words in 2007.

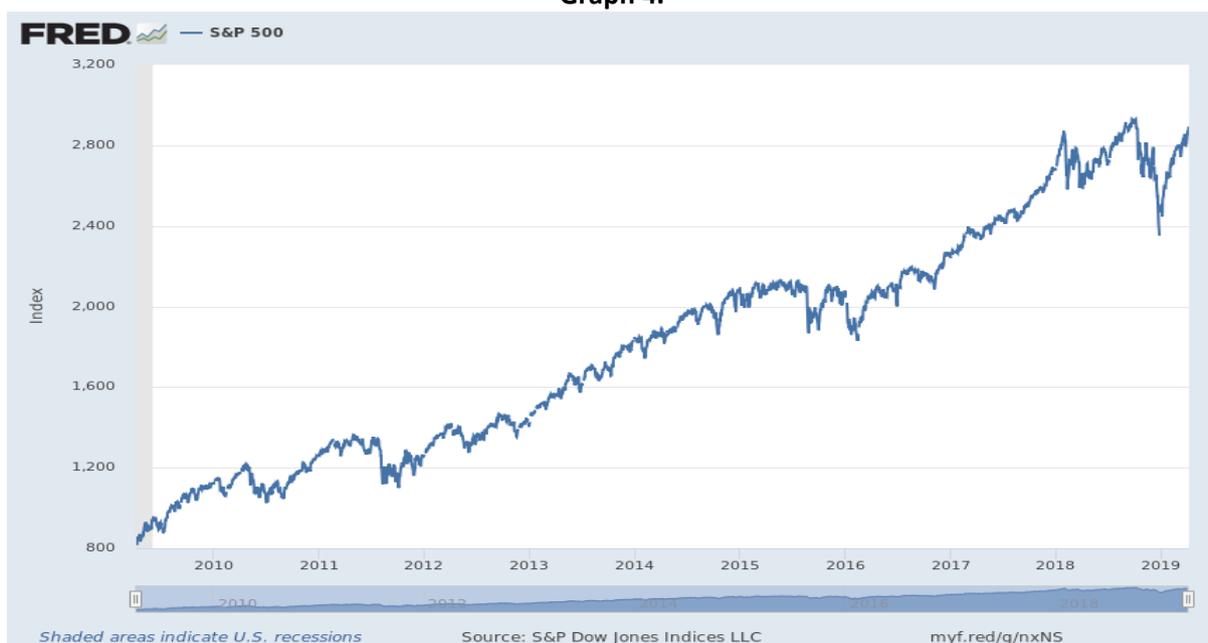
At first the sources of the inflows into the markets during the first quarter was hard to detect. Retail market funds did not see large inflows. Professional investors stood on the side lines and hedge funds sat on their hands. The financial blogs all expressed caution and confusion over the depth and breath of the upturn in stocks. It is likely that one of the drivers of this increase in stocks both in China and New York was to ensure that neither of the two adversaries showed weakness during the negotiations. Surely a case of grandstanding.

Whatever the reasons, the markets were propped up with soothing words from central banks and the promise of an imminent resolution to the trade dispute. Despite the assurances of a successful outcome to the trade talks, any resolution will represent a setback to global trade compared to the rules that applied previously. The global economy has been fractured and there will be more barriers and tariffs in place compared to the recent past. It is likely to favour the US more than for China for two reasons. Firstly, a significant element of production has relocated away from China to avoid tariffs already. Secondly, it will increase the penetration of China by US financial capital.

It is therefore surprising why China has the fastest rising stock market this year. Such price rises owe more to Government support than profit support. Additionally, the inclusion of Chinese shares into world indexes has also played its part albeit a minor part. Despite the US embargoes, it is clear that China is accelerating its integration into world financial markets.

One interesting development is Trump's call for QE4. Not only is he calling for interest rate cuts but for central bank support. He may have his eye on the next presidential elections, but he also may have his ear on the trade talks whose results could fall below expectations.

**Graph 4.**



It is often said that markets never look into the rear-view mirror but always forward through the windscreen. However, this time it appears that the windscreens are particularly rose-tinted and reliant on soft data. This is in accordance with the phase when stocks rise on a wave of hope and expectations. The point being made is that when market go "risk-on", they dial out bad news, and the hard data has been unremittingly negative as we shall see. I originally anticipated a brief bear bounce in January. I never expected such a strong quarter. Well that's sentiment and perfect markets for you.

The disparity between the data and the markets are at extreme levels, meaning that any disappointments will have pronounced consequences. In many ways the markets are senile having forgotten previous lessons, are oblivious to current conditions and living on illusions, while being medicated by low interest rates. However, such medication needs a warning label: “economic activity based on falling interest rates rather than increasing profit rates may produce speculative palpitations rather than the restoration of normal productive rhythm”.

**The USA.**

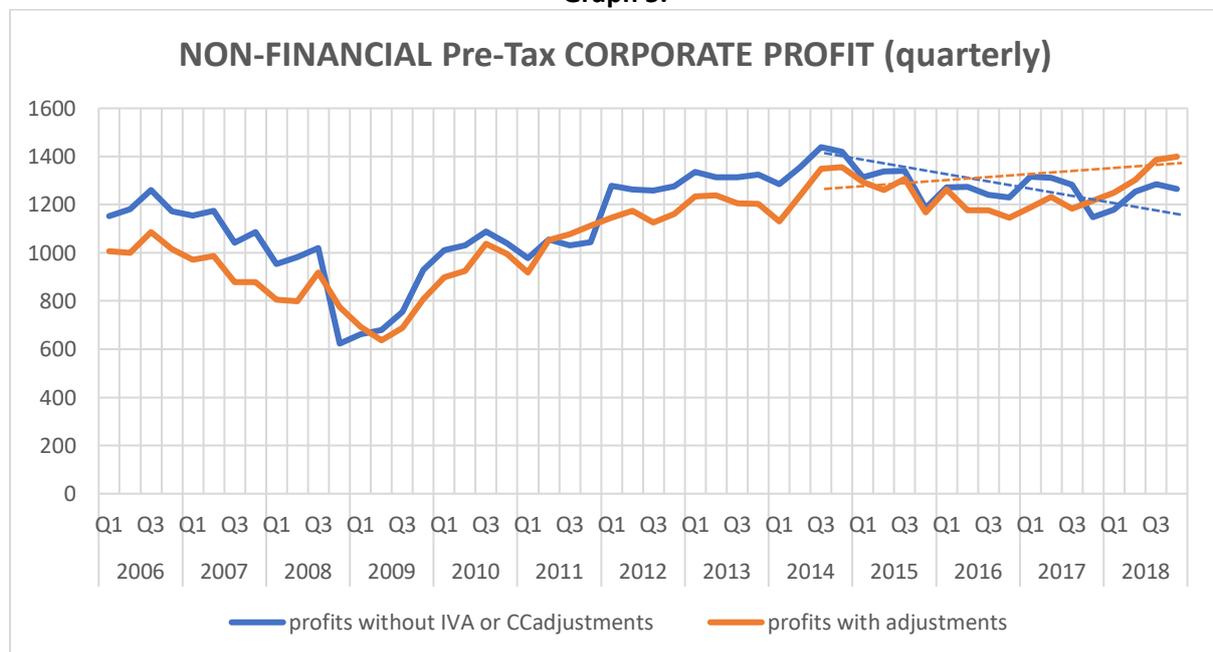
There have been two recent major lessons globally. The first is that given the current elevated value composition of capital, together with the phase of the industrial cycle, the normalisation of interest rates has the capacity to crash the economy. A one percent real interest rate on the 10-year bond was sufficient to arrest economic development. This is unprecedented.

Secondly, the market gyrations during the last quarter of 2018 shows how dependent the economy is on bubbles or what is the same thing “capital gains”. It is more accurate to say dependency has given way to addiction. The top 10% spend as much as the bottom 80% and the former’s spending habits are predicated on the gains they make primarily in the stock exchange. Wall Street has not acknowledged this link which is why it consistently underestimated the fall in retail spending towards the end of last year and the beginning of this year.

But it is not only aggregate sales that is important, it is also the composition of sales. Nowhere is this clearer than with top end motor vehicles – trucks, cross overs and SUVs. In the aftermath of the market falls at the end of 2018, this segment of sales fell for the first time in years. Sales of this segment only recovered in March this year when the recovery of the markets appeared “enduring” and the rich felt confident to present their bank cards once again.

The toxic combination of low interest rates and speculation has to be set against what is developing in the real economy. And what is developing is a crisis of profitability. It is likely that a global profit recession occurred in both the final quarter of 2018 and the first quarter of 2019. This was as true for the US as anywhere else.

**Graph 5.**

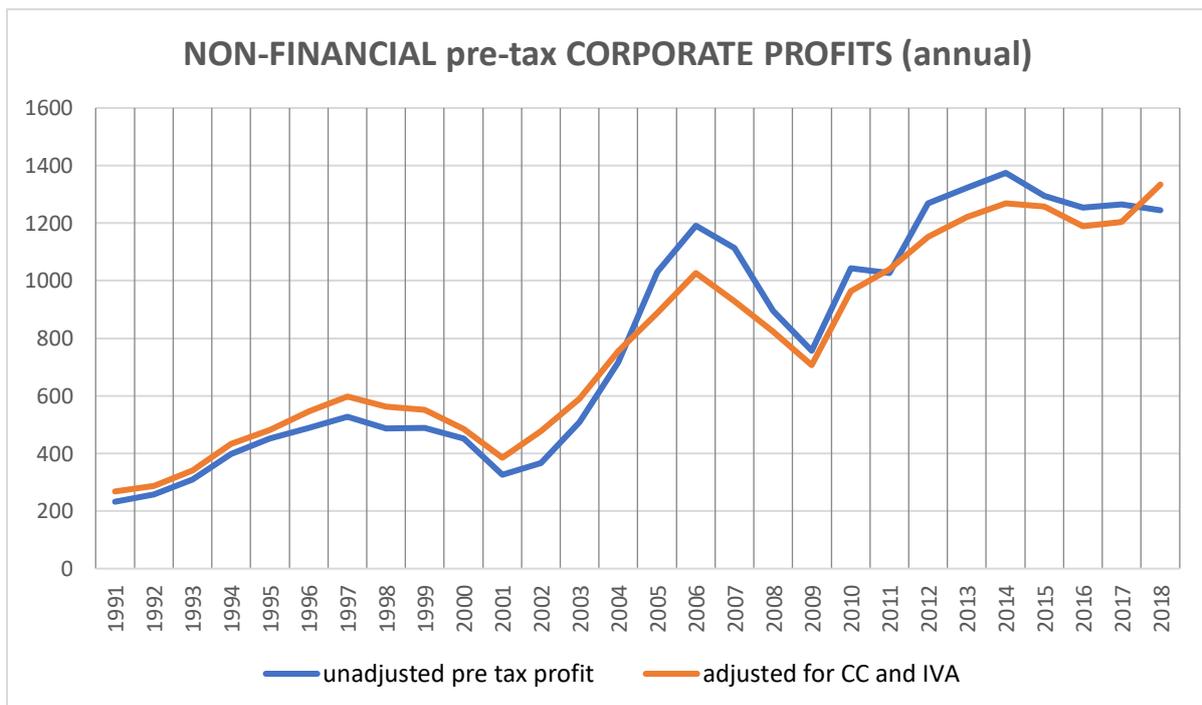


(See attached spreadsheet for Table 1.14)

Graph 5 shows that unadjusted (pre-tax) corporate profits fell 1.5% quarter on quarter. I estimated a larger fall, but this was offset by a rise in energy profits. The most recent survey by FactSet puts the fall in earnings this quarter at 4.2%. If this is the case, and, when adjusted for share buy backs, this will take corporate profits in real terms back to 2012 levels. There is certainly no support for current share prices which have increased 50% in real terms since then adjusted for inflation and share buy-backs.

It can be argued that enterprise profits, (post-tax profits) is more important. They have risen because taxes have come down, but that is a 12-month trick. After that the annual comparisons are no longer flattered by the tax cuts which are now baked in. The other anomaly is the divergence between adjusted and unadjusted profits. In nominal terms since 2014 adjusted profits are up 4% while unadjusted profits are down 12%. While adjusted profits can rise faster than unadjusted as they did up to 2004 (Graph 6 below), it is unusual for the trends to diverge so sharply as they have done since 2016. The only time this happened was in 2011 and that occurred for only one year. Should these trends continue to diverge, further investigation will be required.

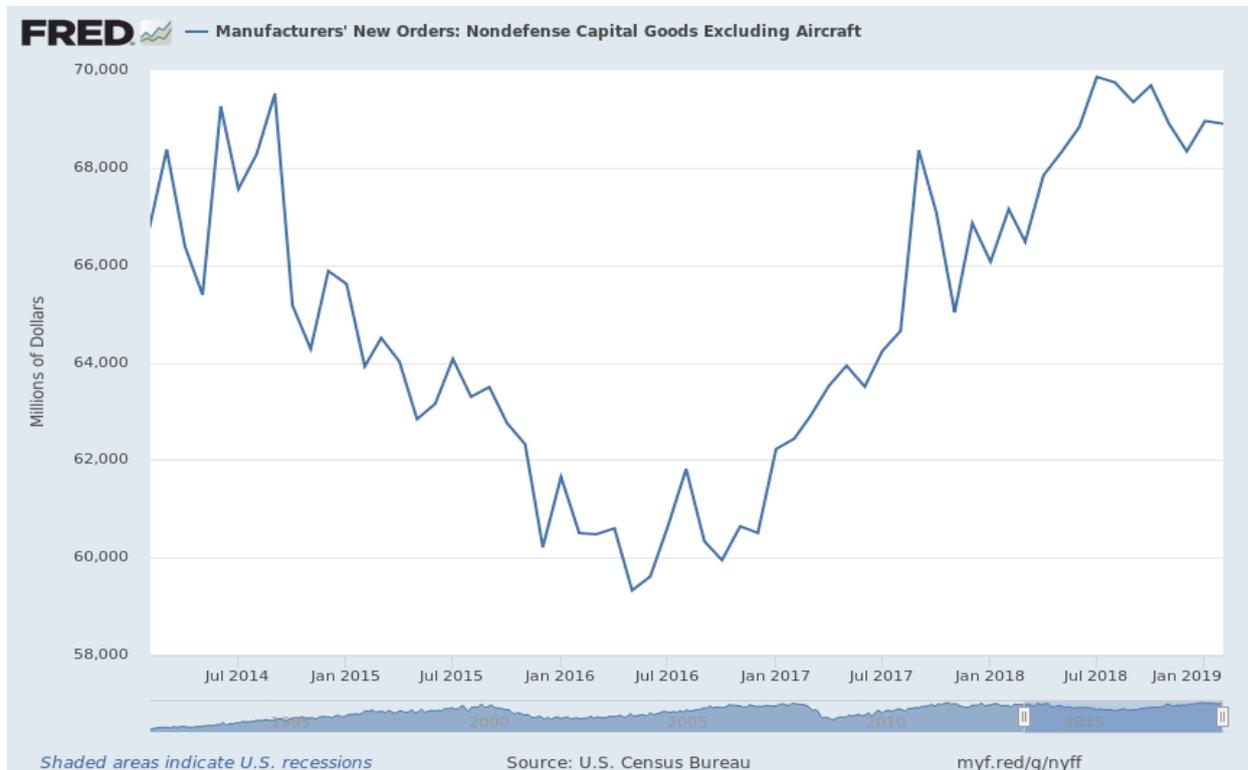
**Graph 6.**



Away from the soft data being used to define green shoots, the hard evidence, that is actual data provided by the BEA, The Census Bureau and so on paint a picture of a weakening economy. *“there has never been an economic contraction without there first being a contraction in freight flows.”* Thus, spoke the CASS Freight Index Report which has shown a sharp contraction from the 10% quarterly increases registered in the first 9 months of 2018 to minus 2% in the first quarter of 2019. This is a sharp reversal from a high positive to a low negative within the space of nine months. (<https://www.cassinfo.com/hubfs/Freight%20Payment%20/Transportation%20Indexes/Cass%20Freight%20Index/Charts/Cass%20Freight%20Index%20Report%20-%20February%202019.pdf>) Allied to this report, orders for Class 8 heavy trucks fell 66% in March, a figure so large it must include significant numbers of cancelled orders. This is the third month in a row where orders have fallen below 20,000 per month, a trough not seen since 2010.

This trend was evident in the broader market for capital goods as Graph 7 below shows. Orders peaked in mid-2018 and have fallen since then in line with declining underlying profits. The fall in orders has not been as precipitous as at the end of 2014 when the rate of profit contracted sharply, but the trend of falling orders is now well established. New orders for January & February 2019 up a nominal 1.2% are in real terms below the equivalent period in 2018.

**Graph 7.**



(RELEASE DATE 09/04/2019)

Additionally, inventories increased significantly in both the final quarter of last year and the first quarter of this year. This is indicative of a sharp fall in the rate of turnover which remains subdued compared to 2014. This build will restrain production in the coming period compounding the decline in fixed investment. In sum GDP is trending down to 1%. Currently the body of analysts give a reading of 1.4%. Of this 1.4%, around 1% is statistical noise generated by the increased budget deficit, imputed sales and so on.

The budget deficit courtesy of Donald Trump's tax give away continues to soar. For the first six months tax revenue rose only by 1%, somewhat at odds with an economy that grew nominally at 4.5% over the same period. Consequently, the budget deficit has grown by 15% to \$693 billion. <https://www.cbo.gov/system/files/2019-04/55095-MBR.pdf> At current rates of projection the deficit looks likely to break the \$1 trillion barrier this year rather than as expected, next year. Approaching 5% of GDP, the real threat of the deficit is its effect on interest rates. It acts as a floor to longer term interest rates. In an economy dependent on low interest rates, the longer-term deficit thus far outweighs the tax stimulus enjoyed during 2018.

Finally, what about that other area of investment the FED holds so dear, the hiring of workers. Last week the markets were buoyed by one piece of seasonally adjusted hard data, the employment release for March which jumped from 30,000 in February to nearly 200,000 in March. On the face of

it, a good release. However, this headline figure is not an accurate reflection of the labour market. The household survey showed a sharp rise in part-time work and a fall in full-time work. The number of layoffs jumped in the first quarter: *“Job layoffs hit 190,410 in the first quarter, a 35.6 percent increase over the previous year and the worst first quarter since 2009, according to Challenger, Gray & Christmas.* [www.cnbc.com/2019/04/04/job-layoffs-surge-35percent-to-highest-level-to-start-a-year-in-a-decade.html](http://www.cnbc.com/2019/04/04/job-layoffs-surge-35percent-to-highest-level-to-start-a-year-in-a-decade.html) It seems paradoxical that a rising trend of layoffs should reside alongside rising hires unless of course the hires are taking place in low paid and low value occupations while the layoffs are occurring in better paid industrial jobs. This conundrum has now been resolved with the 585,000 collapse in job openings in March. The last time this happened was in August 2015. <https://www.bls.gov/news.release/jolts.htm> Furthermore, longer term unemployment claims, rather than new claims, continue to rise showing there is difficulty finding work. Overall, despite the seasonal adjustments, employment prospects are deteriorating which is why wage rises are subsiding.

## CHINA.

Not only was China the first country to ground the 737 MAX, it was the first country out of the block with a fiscal stimulus. And it needed to, because China’s complex rate of return (profit) collapsed in the first two months of the year as industrial profits dropped 14%, after rising on average 10.3% during the whole of 2018 thanks to a sharp rise in the first half of the year.

As I reported on the rate of profit for China in 2018, the complex rate of return for the year had risen to 6.2% from 5.7%. This rise had occurred despite the reversal in profits towards the end of 2018. <https://theplanningmotivedotcom.files.wordpress.com/2019/01/chinaprofit26turnover2018pdf.pdf> Using the latest release by the National Bureau of Statistics of China 2019-03-28 the complex rate of return annualised has fallen to only 3.9% for the first two months.

This is a significant fall, one that puts the rate of return below the CPB Bank Rate of 4.35%. This means that effectively, industry is making a loss on average on new investments. The beauty of the Chinese data is that it places great stress on the elements of turnover. *“; the turnover days of finished goods were 19.3 days, 0.4 day increase than that in the previous year; the days of Notes receivable and Accounts Receivable hit an average of 57.5 days, an increase of 4.6 days year-on-year.”* [www.stats.gov.cn/enGliSH/PressRelease/201903/t20190328\\_1656767.html](http://www.stats.gov.cn/enGliSH/PressRelease/201903/t20190328_1656767.html)

In my earlier cited report, turnover based on inventory plus notes receivable for 2018 amounted to 5.49. Using comparable data for the first two months of the year the rate of turnover of circulating capital in China has decelerated to 4.75. Once again, the importance of the link between turnover and profitability is established.

This fall in turnover is reminiscent of the fall that occurred in the USA after 2014, since which time the mass of unadjusted profits has not recovered, causing the rate of profit to fall absolutely. I cannot berate fellow Marxists enough for ignoring turnover. One thing is certain, the systemic decline in turnover in China from >6.5 a few years ago to <5 means that profit growth will be hard to find no matter how much money is thrown at the economy.

But it is not only profits that are hurt by this elongation of the period of circulation of over 5 days, it is the requirement for more working capital to finance these extra days. *“Less profits realised but more capital required”* - this is the substance of all credit crises. Such a credit crisis is in play in China. In an article in the FT titled *“Bank Loans at small China banks sparks fear.”* (9/04/2019) the Chinese National Audit Office reports that a number of small banks in Henan province have bad debts amounting to 40% of their outstanding loans. 42 banks have bad debts above 5% with 12 banks above 20%. These

smaller banks make up 26% of all bank assets and this is where the loan risk is highest. (Richard Xu, Morgan Stanley) This is likely to apply to more provinces than Henan.

Of course, the article goes on to say that the large state banks have brought their loan book under control. All this says, is that large banks have deeper vaults into which to secrete bad loans. Given the credit to output ratio it is likely that bad debts are endemic within the large state banks as well. The stimulus at the end of 2017 was designed to ease this pressure. Now we have another stimulus aimed at boosting profits once again. Once more it is the larger enterprises that are benefiting as the March PMI showed. But this is the law of diminishing returns. As the stock of older poorly performing loans builds, it tends to overwhelm any new stimulus. Just as the Trump tax bump lasted all of 9 months, so the last Chinese effort lasted all of 12 months.

The outlook for the Chinese economy is not improving as Helen Wong of HSBC would have us believe. Instead its fundamentals continue to deteriorate. The latest data on smartphones and autos reveal this. In China in the last quarter smartphone sales measured by value fell 27%, sufficient to depress global totals. (<https://9to5mac.com/2019/02/25/global-smartphone-revenue/>) Retail auto sales in March issued by the China Passenger Car Association fell by 12% to 1.78 million units bringing the average annual fall for the quarter to 11.5%.

These are not the figures consistent with an economy growing over 6% in real terms. But they are consistent with a stimulus in March that is 80% larger than March 2018, and, when taking the quarter as a whole, Total Social Funding was 40% higher than the first quarter of 2018. This is an act of desperation in the face of diminishing returns and one, combined with the collapse in pork production, which carries the threat of higher inflation.

#### BREXIT OR EUXIT.

The north/south divide in the EU is often highlighted. That divide has been eroded, not because the South has been lifted up, but because the North's economic prospects have come down. Germany's economy has been skirting with recession for three quarters now. The flash German March PMI for manufacturing fell to 44.1, with output at the worst level for 6 years. For Europe as a whole the PMI stood at 47.6. Admittedly this is soft data, but the degree of weakness found in the data suggests that the EU economy is deteriorating more rapidly than elsewhere.

The EU, because it is an assembly of countries rather than a federated state, hampered its recovery from the 2008 crash. This is particularly evident when examining its largest banks and their share of important investment markets. Before 2008 EU banks were not only gaining on US banks, but in some cases they were overtaking them because the EU market was then larger than the US market. Now the roles are reversed. Less capitalized (financially weaker) EU banks are being elbowed out of the way by their better capitalized US banks in vital markets.

The EU budget at £145 billion in 2015 represented just 1% of EU GDP. In the USA, Federal Taxes amount to 16% of GDP while state taxes amount to 14%. This is the reverse of what takes place in the EU where national taxes add up to 40% of GDP. This lack of centralised tax income is a potential source of weakness for the Euro.

The backing for state currency stems from its tax base. To compensate for such a small base, the EU has implemented a rule-based system, really a Germanic rule-based system to discipline the various national economies in the Eurozone. This has not been without its successes, as according to the European Central Bank, "... *the dispersion of growth performance was lower since the introduction of the euro ... compared to the respective dispersion of real GDP growth across U.S. states.*"

(<https://www.ecb.europa.eu/mopo/eaec/diversity/html/index.en.html>) In other words the relative economic disparity in growth between Eastern Europe and Germany was less than between the Southern States and California.

Furthermore, the mandate of the European Central Bank is reduced to price stability. Since the introduction of the Euro, inflation within the countries covered by the Euro has fallen, again marking a success for the currency.

The problem with rule-based systems is that they work in an environment characterised by prosperity. They become punitive in a recessionary environment. In a period of abundance, market prices coincide with the output prices of less efficient producers. In a period of falling demand, market prices coincide with the output prices of the more efficient producers which are lower.

Thus, a rule-based system turns into its opposite. Disparity grows. The rules weigh heaviest on the least efficient economies. It causes them to slow down further than would have been the case. For example, these rules forbid greater governmental spending and support. Resentment grows. The Euro, formerly supportive of broader market trade, is now seen as suffocating.

This is where an institutional remedy is needed. This institutional solution has a name: federalism. But the rise of populism has cut off that option. The right-wing fatherland populist vote now adds up to 25% of the total vote, sufficient to block the move towards a greater and grander supra European state, one which submerges the nation state and cedes more power to a remote elite in Brussels.

The proposal for common financial institutions should not be confused with the legal institutions currently in force where commonly agreed EU laws takes precedence over national laws and are enforceable by the EU through the European Court of Justice. *“The European Court of Justice has observed that domestic laws must be reconcilable with the need to apply European law uniformly so as to avoid unequal treatment of economic operators [Joined Cases 205/82 to 215/82].”* [www.https://europedia.moussis.eu/books/Book\\_2/2/3/3/index.tkl](http://www.europedia.moussis.eu/books/Book_2/2/3/3/index.tkl)

Instead what is being discussed are financial institutions. The European Commission and the ECB recognise that full monetary and economic union is a work in progress. *“As robust as it is today, the EMU remains incomplete. The ‘Monetary’ pillar of the EMU is well developed, as illustrated by the role of the European Central Bank (ECB). “However, the ‘Economic’ component is lagging behind, with less integration at EU level hampering its ability to support fully the monetary policy and national economic policies.”* (REFLECTION PAPER ON THE DEEPENING OF THE ECONOMIC AND MONETARY UNION 2015. [https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu\\_en.pdf](https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu_en.pdf)) The Commission has set the goal of full implementation by 2025. Except like China, the EU does not have the luxury of waiting for 2025.

The 2008 crisis showed the problems facing the single currency as private capital flows between countries dried up. This left the weaker EU countries, especially in the South, short of capital. This forced structural changes in these countries, changes to the labour market and austerity. It built up political resentment which was redirected towards Brussels.

*“Monetary policy is centralised at the euro area level. Yet, it is coupled with decentralised budgetary and sectoral policies that mainly reflect national circumstances and preferences.”* (REFLECTION PAPER ON THE DEEPENING OF THE ECONOMIC AND MONETARY UNION) The commissioners recognise the contradiction at the heart of the EMU between monetary policy and fiscal policies. It is this contradiction, essentially the absence of an EU treasury bolstered by a strong tax regime, that ensured

the EU could not respond to the 2008 crisis as spontaneously and comprehensively as did the US Treasury, FED and Federal Government.

This is the direct responsibility of the German government. They resisted the deeper integration of the EMU fearing it would fall disproportionately on the Bundesbank. It may have, but the longer-term advantages would have outweighed the disadvantages. It would have prevented the mini-crises that broke out in the Eurozone until 2012 when Draghi unleashed his famous commitment: *“Within our mandate, the ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough.”* (<https://www.ecb.europa.eu/press/key/date/2012/html/sp120726.en.html>)

With that the ECB launched its own particular form of quantitative easing. Monetary policy would take the strain. *“This overburdens monetary policy with the responsibility of cushioning and counterbalancing economic developments.”* (REFLECTION PAPER ON THE DEEPENING OF THE ECONOMIC AND MONETARY UNION) The result of this over-reliance of monetary policy, in the absence of financial integration, has been to drive interest rates to zero and beyond.

Abnormally low interest rates worked to a degree. The injection of liquidity throughout the Eurozone stabilised the economy. The problem with this kind of intervention is that it is not repeatable. It will be insufficient for the next financial crash, which is imminent. The Reflection Paper may laud the steps that banks have taken to make themselves more robust, but banks are robust until they aren't.

What is needed is a fully-fledged Eurozone Treasury. The Document skirts around the issue. It knows such a demand, if spelt out would be a political hot-potato, not least of all with the German Constitutional Court. Instead it talks of a common insurance fund to protect individual depositors called EDIS (similar to the Federal Deposit Insurance Corporation in the USA), it talks of a “common fiscal backstop” and a *“European safe asset (that) would be a new financial instrument for the common issuance of debt, which would reinforce integration and financial stability”*. But nowhere does it state the necessity for national treasuries ceding sovereignty to an all-powerful centralised EU treasury.

Instead, it is advancing additional joint financial instruments that will be tagged onto existing and unstructured national treasuries and financial departments as found in the 19 members of the Eurozone. There will be more collaboration, more joined up risk-taking, more common assets with which to firefight, but this will not be enough to withstand the next financial storm. There is every reason to believe that the EMU will not withstand this storm putting the whole EU project at risk. Germany may rue its intransigence, now that China's booming investment wave which Germany rode so well, is subsiding. Germany has now become much more reliant on the fortunes of the EU market, a market it has undermined by refusing to fund and support the move to a common Treasury and finance department.

It is important to understand that the EU is a grand experiment. The United States formed in the youth of capitalism, the EU in its pensionable phase; the United States was formed by the expropriation of the indigenous population who were replaced by waves of immigrants who had abandoned their original national identities for a new identity, while in the EU the indigenous populations in the main retained their national identities; finally the USA was born in blood, wars of independence, wars of territory climaxing in a civil war all of which necessitated a federal structure, while the EU was born through political agreement against the backdrop of a previous calamitous war.

It is the fragile state of the EU following the financial crash of 2008 that makes BREXIT such a challenge. A hard BREXIT would rock the EU to its core. If this form of BREXIT occurs amidst a new financial crash it will doom both Britain and the EU. Under these conditions, Marx's prediction that the expected socialist revolution will occur first in Britain, may well come true.

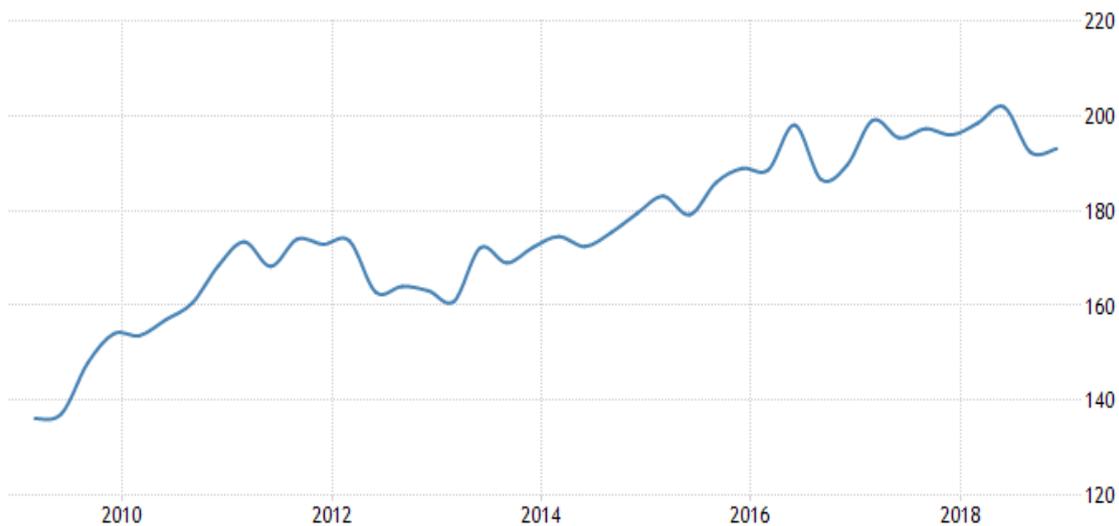
More prosaically it is precisely this vulnerability that led to the concessions found in the “Withdrawal Agreement”. An agreement which respected May’s red lines, red lines inserted not for the overall interest of the British capitalist class but for the purpose Tory Party unity. Of course, the extreme Brexiteers have declared that the Agreement is unfair to Britain. It is not. Anything short of the EU allowing Britain both free trade with Europe and free trade outside Europe, would be deemed unfair by them. In fact, the Agreement allows more freedoms for Britain than British negotiators had first anticipated at the outset of negotiations.

I remain convinced the Withdrawal Agreement will be passed by the Tories with support from Labour renegades, if only because the alternative will be a customs union added on. The question is timing. The EU economy is deteriorating and so is the UK economy despite the creative statistics put out by the ONS. Both economies require an agreement sooner rather than later.

The Crash of 2019 was temporarily circumvented in the first quarter when the global economy was most vulnerable. However, the Crash of 2019 has not been avoided, only averted. The conditions leading up to the gyrations during the last quarter in financial markets are still very much in play. In many cases they are deepening. Crucially we are now at the beginning of the financial reporting season covering the first quarter of 2019 and stock markets are not braced for shocks.

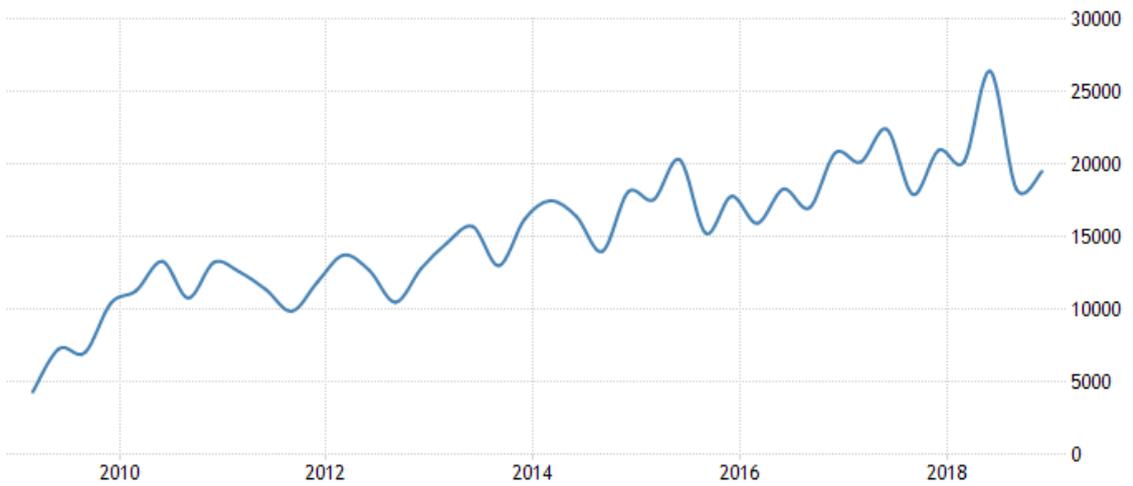
**Addendum. Profitability in Germany and Japan.**

**Graph 8.**



SOURCE: TRADINGECONOMICS.COM | DEUTSCHE BUNDESBANK

**Graph 9.**



SOURCE: TRADINGECONOMICS.COM | MINISTRY OF FINANCE, JAPAN

Brian Green, April 2019.