From Russell Napier of ERI-C

Now only one question matters for global investors --- Wo ist der Hubschrauber? (Where is the helicopter?).

The decline of European commercial bank share-prices before Brexit made it clear that a monetary reflation of Europe was failing. The collapse in these same share-prices post-Brexit means that even the politicians now realise that the ECB acting alone cannot stabilize the European economy. Indeed, given the evident political strains in the European Union, saving the economy from recession is now key to saving the European political union project itself.

So, will Mrs Merkel abolish fiscal austerity across Europe and permit each of the states of the European political union expand their debt mountains at the same time that the ECB is buying that debt? Are the keys to der Hubschrauber to be handed over? To save the European political union Germany must now confront its greatest fear and enfranchise the political union's central bank to conduct outright monetary financing of all its constituent governments.

Investors need to remain very cautious indeed as it is in no way clear that Mrs Merkel will hand over the keys to der Hubschruaber. Should she do so, however, major changes in investment allocation are necessary as helicopter money will be raining from the skies in Japan, the Eurozone, the UK and even in the USA if President Clinton also wins the House and the Senate. This form of reflation will likely work and in due course work too much. Few things are binary in investment, but this huge decision to be taken in Berlin is the biggest binary event for investors this analyst has yet come across. The repercussions will reverberate throughout this century.

This analyst would like to present you with a firm forecast as to the possibility of 'helicopter money' coming to the European political union. However, it is too close to call. Even if that assertion is correct, this is truly dire news for financial markets.

Investors seem to have no doubt that Mrs Merkel will indeed endorse an end to fiscal austerity in the Eurozone and, in the process, further breach the constitution of the ECB and ignore the ghost of Herr Haverstein (Germany's Weimar/hyperinflation central banker). These are truly existential decisions for any Chancellor of Germany to make and it is too dangerous to invest clients' hard-earned savings on a bet that The Chancellor will sacrifice everything for the political union project.

Time is ticking away and a decision will have to be made within weeks if a European recession, which will raise severe questions about the survivability of the European political union, is to be averted. We will know soon enough just how large the ghost of Herr Haverstein still looms in Germany, as a failure to endorse helicopter money within a few weeks most likely means Germany is ultimately backing away from the European political union project. This is amongst the most important political decisions of the 21st century and one full of pain for global equity investors if Germany decides not to act. Early clues as to which way The Chancellor might swing are to be found in Italy.

The Solid Ground has been warning for well over a year that the introduction of the Bank Resolution and Recovery Directive (BRRD) would undermine the stability of European banks and, if actually implemented, would cause bank-runs across Europe. The collapse in European bank share-prices since January does suggest that bank stability has been undermined. Now we face the prospect of a BRRD implementation in Italy and the biggest public policy error since Hank Paulson allowed Lehman Brothers to fail.

At this stage the best bet must still be that Germany will back away from insisting upon implementation of the BRRD and the bail-in of Italian commercial bank-bond holders and, conceivably, large-scale deposit holders. However, the German response to the unilateral announcement by the Government of Italy that public funds would be used to recapitalize their banks, without any bail-ins, was uncompromising. While one might have expected a representative of the European political union to have insisted that laws be implemented, Mrs Merkel intervened directly, presumably representing the Union as a whole when she stated: “We wrote the rules for the credit system, we cannot change them every two years.”

If that is a true representation of what The Chancellor thinks then a financial crisis is just a few days away. Not only will it create runs on banks across Europe, it will also signal that the German commitment to the European political union cannot be taken for granted. In the opinion of this analyst this double-whammy from a BRRD implementation would create a shock as large as the bankruptcy of Lehman Brothers. Given the scale of the consequences from such a public policy error, this is not the time for risk-taking.

Should The German Chancellor hand over the keys to der Hubschrauber, then global equity markets will rise materially and very quickly. Investors can afford to miss this first move given the risks that the keys to the helicopter might remain hanging on the kitchen door at the Bundeskanzleramt. However, responding rapidly to the sound of whirring rotors is very important as the very positive impact on European equity and global equity prices will continue for months, quarters and conceivably even years. It is not a time to be a hero and second-guess The Chancellor, but instead be ready to move quickly to accept the Haverstein bonus for equity investors this Chancellor is prepared to endow on investors almost 100 years after Germany last sought this particular economic solution to a political problem. Equity investors know only too well where such bounty ends, but this will not stop them from enjoying the early reflationary spring.

Meanwhile, in a sideshow to the increasingly likely reversal of the European political union, the United Kingdom continues to flex. The constitution is flexing, the exchange rate is flexing, the political parties are flexing. This flexing is in marked contrast to the brittle constitutional and economic framework, in the form of a single currency, placed upon the sovereign states of Europe. Scotland’s place in the UK is guaranteed because who would vote for the creation of a border, joining the Euro and a European political union which will either be dissolving or rapidly centralizing; in addition there’s also the impact of the oil price to consider.

Most or even all the politicians who lied and condescended to their electorate in the referendum are gone or going. It is not that naïve to assume that the next bunch will be better, albeit that is a low hurdle to jump. Meanwhile, the grossly overvalued exchange rate that produced a huge current account deficit has gone. The cost of government borrowing, crucially, has declined and this has created the flexibility to launch a more expansionary fiscal policy. Ironically, the banking system is sound because it had to be bailed out by the government in 2008. A recession is very likely as business investment slows, but this is all part of a flexing and not a breaking.

In short, the so-called chaos represents a fairly smooth and rapid realignment in politics and finance. Brittle systems fracture under strain and those are not the systems in the United Kingdom.

The people of the United Kingdom voted not to delegate their sovereignty to a European political union. While the timing of that decision was a surprise, the fact that the UK would not become one of the Federal States of Europe has been clear for a very long time indeed. The pain associated with such a decision is lessened the sooner it is taken, so the fact that it has happened now should be seen as a relief.

The minority who voted Remain have convinced themselves that their economic prospects have been dented by uneducated xenophobes from places they have never heard of. The 17.4 million who voted Leave brace themselves to expect a painful economic adjustment they deemed a price worth paying to defend the sovereignty of the people in parliament. In due course there will be an election to that parliament and all citizens will get to have their say on the free movement of goods, the free movement of services and freedom of establishment, the free movement of persons (and citizenship), including free movement of workers and the free movement of capital. For the first time in some decades all their votes will count on these issues and, for any party securing the backing of the 48% of the population who voted Remain, true power awaits.

Throughout this flexible democratic process humus will continue to be widely available, café culture will continue to thrive and a cappucino will never revert to being called ‘a frothy coffee.’ Just how our four freedoms will be exercised, though, will ultimately depend upon our fellow Europeans and how committed they actually are to the extinction of the sovereign state in their pursuit of a European political union. There remain grounds for significant optimism that they too will revert to a desire to pool the interests of states without pooling the sovereignty of states.

If you don’t hear the rotors of der Hubschrauber very soon then what has begun is an economically painful but constitutionally necessary journey back to a common market and away from a political union. The United Kingdom would be at the centre of such a realignment of interests. While welcoming such a constitutional realignment, investors need to realise that the free movement of capital will be suspended in any such process. For years The Solid Ground has warned that this is by far the most important change that investors will face in ‘the new normal’. Meanwhile, still no sound of rotors!