Recent comments by Mohamed A. El-Erian

Yahoo Finance reached out to Mohamed A. El-Erian to get his take on the Brexit referendum and its aftermath. Among other things, we were surprised to learn that he saw not one, but two silver linings to this development, which has been the source of much volatility in the world financial markets. Read our Q&A below.

Were you surprised by the outcome of the Brexit referendum?

While I expected it to be extremely close, I thought that the status quo would ultimately and just prevail – and especially so in the immediate aftermath of the tragic killing of Jo Cox, the pro-Remain member of parliament.

When Sterling started rallying strongly right after the poll closed on Thursday, I wondered what traders were seeing that suggested an easy win by the Remain camp. It was fascinating to witness the subsequent shift in market sentiment, starting first with the results from Newcastle and Sunderland.

Do you understand why the majority of British voters opted to Leave?

Yes I do.

As you know, I have been cautioning for a while now about improbables and unthinkables turning into realities when western economies get stuck in a prolonged period of low economic growth and worsening inequality. In fact, the list is getting longer by the month.

I also paid attention when a college friend of mine from our days at Cambridge University told me that he would vote Leave despite being pro free trade all his life. Like others, the referendum had come down for him to a single emotional issue, that of Britain regaining sovereignty over its immigration policy. And this issue was so emotional and dominant for him that it totally crowded out a calm and comprehensive assessment of the multiplicity of factors in play.

So what happens in the next few weeks and months?

There are a lot more questions than answers, including how the UK parliament follows up on the referendum. I certainly would not rush to rule out a range of possibilities. I would also be cautious about isolating the economic and financial effects as national and regional politics will be very influential in the months ahead.

Having said that, and without under-estimating the uncertainties, a few things are already clear on the political front.

First, we will see major convulsions in British politics. While Prime Minister Cameron has resigned, the Conservative Party still faces an enormous challenge in reunifying behind a new leader. A Labour Party rebellion against its leader, Jeremy Corbyn, is likely. The political integrity of the Union will be challenged, not just by a Scotland that wishes to remain in the European Union but also a Northern Ireland that is keen on maintaining the free flow of goods, services and people with the Republic of Ireland.

Second, politics on the European continent will find it hard to strike the right balance between forces that embolden anti-establishment movements there and, on the other hand, a buyer's remorse given all the complications that are being raised in the aftermath of last Thursday referendum.

Third, if Brexit does eventually occur, the UK's European partners may have talked tough but, ultimately, would have little choice but to agree to some type of association agreement that maintains a free trade zone.

Is there a Brexit silver lining?

Yes. In fact, there are two!

First, the referendum could end up solving a fundamental contradiction within the EU.

Since it first joined 40 years ago, the UK has treated the EU as a super free trade arrangement. That is, an end in itself.

Not so for some other influential members, including Germany. For them, the EU was a means to the "ever closer union" that the founding fathers envisaged. And this has economic, financial, political and social aspects that the UK could never accept.

A Brexit resolves this basic inconsistency, albeit with a sizeable transition cost, including lower growth and a higher threat of recession, and considerable risks to the overall integrity of the EU.

Second, the referendum could act as a wakeup call for polarized politicians who have repeatedly failed to implement the package of required policies. A Sputnik economic moment if you like.

What does all this mean for the global economy in 3 years?

Brexit has accelerated what I have characterized in my recent book as the journey to the neck of a T junction – that is to say, the exhaustion of the current road that the global economy is on, and the possibility of two contrasting transitions.

In the event that governments finally step up to the economic policymaking responsibilities and stop relying excessively on central banks, the recent period of low growth and artificial financial stability would evolve into high growth and genuine financial stability. The improvements would be turbo charged by the productive engagement of cash that currently resides on the balance sheets of companies, as well as technical innovations.

But if politicians continue to disappoint, low growth would turn into periodic recessions, and artificial financial stability would give way to disruptive instability. The inequality trifecta – that of income, wealth and opportunity – would worsen. Already-alarming youth unemployment would get even more deeply embedded in the structure of the economy. Political tensions would increase, as would the trust deficit in business and political elites, as well as expert opinion.

What is key to stress is that there is nothing pre-destined, at least as yet, when it comes to the road out of the T junction. It depends in large part on the political decisions that will be made in the comings months and quarters.

If you were forced to opt for just one outcome for Europe what would that be?

Having suffered short-term disruptions, both the EU and the UK would have regained their economic and financial footing in three years. The UK would have an association agreement with the EU that allows for the smooth trade in goods and services, and that lowers the risk of tariff wars. The EU would be a somewhat smaller but much more coherent, confident and operational unit.

And your biggest fear in the short-term?

It would be that de-stabilizing combination of policy mistakes and financial accidents.

Thank you for your time.

My pleasure.

Mohamed A. El-Erian is the chief economic advisor to Allianz, the corporate parent of PIMCO where he served as CEO and co-CIO (2007-2014). He is Chair of President Obama's Global Development Council and the author of two New York Times Best Sellers: the 2008 "When Markets Collide" and this year's "The Only Game in Town."