Brexit update from our CIO - 16 November 2018

Yesterday was a truly eventful day. When it was announced that a Brexit deal was ready, the pound rose as expected. However, this was short lived as Ministers subsequently resigned later on Thursday morning, causing the pound to commence its decline. On the back of these events, gilts rallied, particularly Index-linked gilts. At the market index level, UK equities were bolstered by the increased value of overseas earnings (caused by the fall in the pound). However, this disguised a very wide dispersion of returns amongst individual stocks with domestic earners falling and international stocks rising. As a result, well-diversified portfolios with some international exposure should be positive. In what seems to be a Brexit obsessed world, we should remember there are many other influences on portfolio valuations.

The Conservative party membership is believed to be more in favour of Brexit than remain, so a pro Brexit candidate would be likely to win if Theresa May was to be replaced. MPs that favour remain or want to avoid a hard Brexit may want to stick with Theresa May rather than risk a hard-line Brexit leader. As a result, even if 48 members request a no confidence vote, May's leadership could survive.

At present it seems unlikely, despite the Prime Minister's best efforts, that she can get Parliamentary backing for the Brexit deal as it stands. Equally if Parliament was asked to vote for a hard Brexit falling back on World Trade Organisation rules, then that would probably not pass. No one wants to contradict the referendum so there may not be a majority to remain. With Parliament unable to decide, a General Election or a second referendum could be possible. The DUP and the Conservatives do not want to hand the keys of Number 10 to Jeremy Corbyn therefore a vote of no confidence is not likely to pass in Parliament. Theresa May has repeatedly ruled out a second referendum but faced with this type of gridlock it could be preferable to an election.

This is all speculation and no doubt there will be more surprises in the days to come. However, a well-diversified portfolio of international stocks and fixed-interest is benefitting from Theresa May's discomfiture. International stock markets are more likely to be more sensitive to changes in Trump's trade policy, US interest rates and negotiations on the Italian budget than Brexit. Thus, while following the twists and turns of domestic politics we will be watching the Chinese/US positioning on trade in the lead up to the G20 meeting at the end of the month, in addition to comments from the Federal Reserve ahead of their December meeting and Budget news in Rome, with equal interest.

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