

FIXED INCOME

Tory Victory Offers a Boost to UK Market—But for How Long?

December 13, 2019



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The Conservative victory in the UK General Election should bring some relief for UK markets, according to our Head of European Fixed Income, David Zahn. But he warns investors' attention is likely to turn quickly to how the new government can really "get Brexit done."

Markets are likely to see the Conservative victory in the UK General Election as the most positive outcome.

Although it was considered the most likely result in the run-up to the poll, we'd expect markets to react favorably, with gilts yields likely to fall and the pound likely to strengthen. We think risk assets such as corporate bonds will probably rally, too.

The Conservative manifesto centered on "getting Brexit done," so we'd anticipate a rapid move to ratify Prime Minister Boris Johnson's EU withdrawal agreement bill. If that's successful, the United Kingdom would leave the European Union on January 31, 2020.

Markets, keen to see an end to Brexit uncertainty, are likely to respond positively in the short term.

However, a market relief at a Conservative victory may be quite short-lived as investors pivot quickly to think about what's next, particularly with Brexit.

Once the EU withdrawal agreement passes Parliament, the United Kingdom will enter a period of negotiations on a future trade agreement. That negotiation process can last up to 11 months, which doesn't give much time for the complex discussions required. We don't think the EU negotiators will be as amenable as they were when agreeing to the withdrawal agreement.

There are a lot of likely sticking points in the discussions, with fishing rights being potentially tricky to resolve. There will be some room for negotiation, but we think talks will likely be robust.

If the UK government wants to extend the negotiation period, it needs to make a request by the summer. That really compresses the timetable to just four or five months in which to calculate whether there is a viable trade deal.

If there are no signs of early breakthroughs, we'd expect the markets to start wondering whether a damaging no-deal Brexit is back on the cards. Markets are likely to start reflecting more uncertainty if there are no signs of progress by the start of the summer.

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