

INVESTMENT VIEWS

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HERE WE GO AGAIN



Another year, another British political upheaval. 2015 had everyone expecting a hung parliament and we got a Conservative majority. 2016 gave us the delights of Brexit. 2017 completes the hat trick.

The exit polls at 10pm last night were the first sign of things to come – predicting that Labour would outperform expectations. It would leave the Conservatives as the largest party, but lack the majority needed to form a government. Once results began to trickle in during the early hours of the morning, it became clear that the swings around the country were wildly different, with some areas seeing large gains for Conservatives and others large gains for Labour. This two-way shift goes some way to explaining the different figures given by pollsters over the course of the campaign.

London and the South appears to have been the key battleground for Labour. The loss of Treasury Minister Jane Ellison's Battersea seat to Labour was a telling sign at 2am and, at 3am, we saw one of the architects of the Conservative manifesto, Ben Gummer, lose his Ipswich seat to Labour as well. In Canterbury, the Tories managed to lose a seat held for 99 years. This surge appears to have had two sources: a tactical backlash against Brexit and a large youth turnout. UKIP's vote collapsed, but former UKIP voters did not all swing behind Theresa May's Hard Brexit strategy, suggesting they would be happy to accept Labour's softer vision.

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One bright spot for both the Conservative and Labour party has been Scotland. The SNP has lost considerable ground to both sides. Perhaps independence is getting a bit 'old' north of the border – Alex Salmond's defeat may be evidence of that. Scottish voters prevented a humiliation for Theresa May, but their support throws another variable into the parliamentary mix: Scotland is far more Remain-orientated and dedicated to the European Single Market.

So what does this hung parliament have in store?

A Conservative government majority might just be manageable if the Irish Unionists continue to co-operate, and if Sinn Fein sticks to its usual approach of not taking up its seats. That explanation alone shows how fragile a continuing Conservative government could be – held hostage on domestic policy changes by the promise of support on Brexit. A Labour-led minority government would likely not be any stronger, pulled between a Soft and a Hard Brexit. Coalitions have been suggested, but it seems very unlikely that the Liberal Democrats will repeat their 2010 error of choosing a side, and the same is probably true of the SNP.

The Pound dropped almost immediately following the exit poll, falling from US\$1.295 down to \$1.275, where it stayed throughout the course of the night. Although this level is higher than the \$1.255 when the election was called on 17 April, this is more a reflection of the weakness in the US Dollar over that period. Against a broader range of currencies such as Yen and Euro, Sterling is now weaker than when the election was called.

Over the course of last night, our portfolios will have benefitted from the non-Sterling exposure we have – around 25% in the Balanced portfolio. We see no need to change our position. In the very short term, increased uncertainty over the immediate direction of Brexit negotiations seems likely. Will the Tory Eurosceptic wing have a larger say, or will the voice of the opposition and Remain-voting Tory MPs be heard? And, more pressingly, who will turn up to the first negotiation meeting in just 11 days (Nick Clegg now has some spare time on his hands...)? We believe that these factors explains Sterling's overnight reaction.



However, it will soon become apparent that expectations for Brexit have become softer, suggesting that the Pound can resume its upwards progress. Voters have rejected May's undefined Brexit vision, unaccompanied as it was by a compelling domestic manifesto. The large Remain minority proved itself to be a significant voting bloc. Remain-leaning Scottish MPs and voters have suddenly become very important to the government. Negotiations with the EU may have to be delayed, increasing the necessity for a transition deal that should cushion the impact of Brexit on the economy. While this result makes negotiations with the EU more complicated and difficult in the short-term, it almost certainly makes the likely outcome softer. After all, it couldn't get much harder than the current path, and a soft, Norway-style Brexit represents the path of least resistance both for the British nation and for our biggest trading partner.

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Chief Investment Officer

For more information call 0207 760 8777 or visit www.7im.co.uk

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Registered office: 55 Bishopsgate, London EC2N 3AS. Registered in England and Wales No. OC378740.