

Economic Alert iQ



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International

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Brexit Update

Highlights

- There are less than 8 weeks remaining for the United Kingdom (UK) to leave the world's largest trading bloc on March 29th 2019 and chances for a no-deal Brexit are mounting.
- The UK's main options are currently leaving the bloc without a deal "no-deal Brexit," with a deal "deal-Brexit" or by remaining within the bloc by holding a second referendum for which the majority vote must be to remain.
- It took Prime Minister Theresa May roughly 2 years to secure an agreement on her Brexit deal with the European Union for it to be voted down by the UK Parliament in January 2019.
- Following the defeat of May's deal in Parliament, the opposition won several debates that would mandate the government to prepare a new deal or an alternative plan within 3 working days. Additionally, the government needs parliamentary approval for the UK to leave the EU under a no-deal scenario.
- Much of the debate surrounding May's Brexit deal is due to the Northern Ireland Backstop arrangement that the EU insists must exist in order to see the UK withdraw with a deal. However, various ministers in the UK parliament are strongly against the Backstop.

- The Northern Ireland Backstop arrangement is an insurance policy to ensure the open border between the Republic of Ireland and Northern Ireland to avoid a hard border when the UK leaves the EU.
- The Backstop arrangement if initiated will see Northern Ireland having different regulations for trade than the rest of the UK, the union it belongs to and as such the parliament is strongly against it.

Figure 1. Bank of England (BoE) Rate Hike Probability as at February 5th, 2019.

Meeting	Hike Prob	Cut Prob	0.75	1	1.25	1.5	1.75	Fwd Rate
02/07/2019	1.0%	0.0%	99.0%	1.0%	0.0%	0.0%	0.0%	0.71
03/21/2019	2.5%	0.0%	97.5%	2.5%	0.0%	0.0%	0.0%	0.71
05/02/2019	16.5%	0.0%	83.6%	16.1%	0.4%	0.0%	0.0%	0.75
06/20/2019	17.4%	0.0%	82.6%	16.8%	0.5%	0.0%	0.0%	0.75
08/01/2019	33.8%	0.0%	66.2%	29.9%	3.8%	0.1%	0.0%	0.80
09/19/2019	33.7%	0.3%	66.0%	29.8%	3.8%	0.1%	0.0%	0.80
11/07/2019	48.4%	0.3%	51.4%	37.9%	9.6%	0.9%	0.0%	0.85
12/19/2019	45.0%	4.9%	50.1%	35.3%	8.8%	0.8%	0.0%	0.83

Source: Bloomberg

- The next monetary policy meeting of the BoE is scheduled for February 7th, with the probability of a rate hike currently at 1% and a probability of 99% that the rate will remain unchanged at 0.75%.
- Although the inflation rate stood at 2.1% as at December 31st 2018 it is still within the BoE's target range of 2% +/- 1% and with real GDP growth remaining modest it is difficult for the BoE to implement a rate hike in the near term. Heavy uncertainties surrounding Brexit also hinder the BoE's ability to adjust bank rates freely.

- In the monetary policy meeting held in December it was noted “the monetary policy response to Brexit, whatever form it takes, will not be automatic and could be in either direction.”

Figure 2. United Kingdom Selected Economic Indicators

<i>Indicator</i>	<i>2016</i>	<i>2017</i>	<i>2018</i>	<i>2019 f</i>	<i>2020 f</i>
<i>Real GDP Growth (% YoY)</i>	1.8	1.8	1.3	1.5	1.6
<i>Unemployment Rate (%)</i>	4.9	4.5	4.1	4.1	4.1
<i>Current Account Balance/GDP (%)</i>	-5.2	-3.3	-3.8	-3.4	-3.2
<i>General Government Balance/GDP (fiscal year %)</i>	-2.8	-1.9	-1.4	-1.5	-1.4
<i>Manufacturing Production (% YoY)</i>	-	2.2	1.1	0.6	0.7
<i>GBP/USD</i>	1.23	1.35	1.28	1.37	1.44
<i>EUR/GBP</i>	0.85	0.89	0.90	0.87	0.87
<i>Central Bank Rate (%)</i>	0.25	0.50	0.75	1.10	1.50

Source: Bloomberg, First Citizens Research & Analytics *f* – Forecasted Data

- Industrial production has been negative in November 2018 at -1.5% YoY and total business investment fell 1.81% in Q3 2018.
- UK Composite PMI has been recorded at 50.3 in January 2019 the lowest since July 2016 when it fell to 47.7. The decline in the PMI indicates rising risks of the UK crashing out of the EU without a deal. A reading below 50 signals weaker sentiment in the market.
- Banks, insurers and money managers are planning to move roughly 800 billion pounds of assets as well as 7000 jobs from the UK to the rest of the EU as Brexit uncertainty takes its toll according to a survey conducted by EY.

Figure 3. United Kingdom Credit Ratings as at February 5th, 2019.

United Kingdom of Great Britain and Norther...			
Moody's			
1) Outlook	STABLE		
2) CC LT Foreign Bank Depst	Aa2		
3) CC LT Foreign Curr Debt	Aaa		
4) CC ST Foreign Bank Depst	P-1		
5) CC ST Foreign Curr Debt	P-1		
6) Long Term Rating	Aa2		
7) LC Curr Issuer Rating	Aa2		
8) FC Curr Issuer Rating	Aa2		
9) Foreign Currency LT Debt	Aa2		
10) Local Currency LT Debt	Aa2		
Standard & Poor's			
11) Outlook	NEG		
13) Foreign Currency LT Debt	AAu		
14) Local Currency LT Debt	AAu		
15) Foreign Currency ST Debt	A-1+u		
16) Local Currency ST Debt	A-1+u		
Fitch			
17) Outlook	NEG		
18) LT Issuer Default Rating	AA		
19) LT LC Issuer Default	AA		
20) Foreign Currency LT Debt	AA		
21) Local Currency LT Debt	AA		
22) Foreign Currency ST Debt	F1+		
23) ST Issuer Default Rating	F1+		
24) ST LC Issuer Default	F1+		
DBRS			
25) Outlook	STABLE		
26) Foreign Currency LT Debt	AAA		
27) Local Currency LT Debt	AAA		
28) Foreign Currency ST Debt	R-1H		
29) Local Currency ST Debt	R-1H		

Source: Bloomberg

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