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UK Election reaction

The bookmakers have been wrong-footed yet again, and this morning's largely unexpected (at least by financial markets) political result is another item on a list of risks and uncertainties that does not seem to be getting any shorter.

It is clearly still very early days to be speculating on what the exact political make-up will look like, but it is difficult to see this result having a positive impact on the UK's near term economic prospects, or indeed strengthening its hand as Brexit negotiations get under way in a few days' time. Policy uncertainty in particular will not be helpful for the UK's economic momentum. Even if a quick coalition is formed, this would still be disruptive for the negotiation process and is likely to unsettle business and market confidence.

So far however, the market reaction has been quite calm, with the bigger moves being seen in currency markets. Although the damage here has not been as great as one might have expected, the pound is currently down just 2% versus the US dollar and euro. This brings us back to a similar level that we saw when the Election was called in April and is still stronger than it was earlier in the year. Larger UK-listed companies, particularly those with significant overseas earnings, have actually rallied this morning as a weaker pound will flatter their profits. Conversely, more domestically orientated businesses, predominantly found within the mid-cap part of the market, have fallen as their profits are likely to be weakened by higher import costs and businesses potentially face a more challenging environment of economic policy uncertainty.

The political fall-out and post mortem of today's result will no doubt run on for some time, but so far markets are reacting with reasonable restraint. Brexit implementation risks have probably increased and a delay whilst we get our own house in order (and potentially face the prospect of another hand on the tiller) are not particularly positive for general market sentiment, but having steadily reined in investment risk over the past year we feel we are well positioned and prepared for a period of elevated volatility in asset prices, which is the more likely outcome once some of today's dust has settled. The UK situation, and the interplay with the forthcoming Brexit negotiations, is just one part of a complex jigsaw for markets to interpret and react to – we should not forget, for example, that issues across the other side of the pond surrounding Trump, or other political upheaval in Europe, could yet become a more dominant market focus. Retaining a cautious stance at present does therefore seem merited and prudent.

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23 King Street | St James's | London SW1Y 6QY | t : +44 (0)20 7667 6600 |
bordieruk.com