

# Prospects Around Brexit

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# Brexit Basics

**Stage 1:** agreeing a Withdrawal Arrangement

**Stage 2:** agreeing a post Brexit trading relationship

**Stage 3:** pre/post leaving the EU:

- new arrangements with other non-EU countries;
- public service policies that replace current EU practice e.g. Agric;
- tax and spend policies out-with EU.

# Brexit and Forecasts

- not a readily forecastable event, unique one-off
- basic economic theory points to -ve impact due to increase in trade and human capital barriers
- but degree and pace and longevity highly uncertain
- wide spectrum of possible outcomes
- why bother with forecasts then?
- because alternative is acting without any guidance, also helps rule out unlikely events

# Economics - Brexit

## Growth

- likely to worsen, but less certain the longer the timeframe

## Inflation

- may rise or fall, in part due XR dep/appreciation (making imports more/less expensive) but goods specific and spikes rather than on-going

## Interest rates

- more likely to fall than rise in SR, but unlikely to go below zero
- but what happens if inflation rises above target?

# **Investment Impact**

## **Private Sector**

- on-going slump in company investment, due to Brexit uncertainty and cheap labour

## **International**

- potential disinvestment and lack of new investment, until post Brexit picture clearer

## **Public Sector**

- growing commitment to large scale infrastructure spend by all political parties

# Challenges and Opportunities

## Challenges

- retaining trade levels as tariff/non-tariff barriers rise
- skills gaps due to reduced migration
- productivity challenges via higher skills/trade/investment barriers

## Opportunities

- trade growth in faster growing economies
- more targeted worldwide migration policies
- more competitive business environment outside EU

# Economics - Wider Impacts

- Brexit trails behind Productivity slump and world Trade issues in terms of longer term importance
- Migration and Internationalisation issues will not go away
- Final form of 'Deal' still has many potential shapes, from WTO to Canada to Norway etc etc

# Household Effects

- Uncertainty over economy likely to keep wages in check and employment rate high
- Household spending not seriously impacted upon post Brexit vote and unlikely to change unless crisis
- Inflation under control and interest rates at unprecedentedly low levels encourages both everyday and large item expenditure
- Potentially higher domestic consumption given uncertainty over foreign travel and costs

# Public Finances - Historic

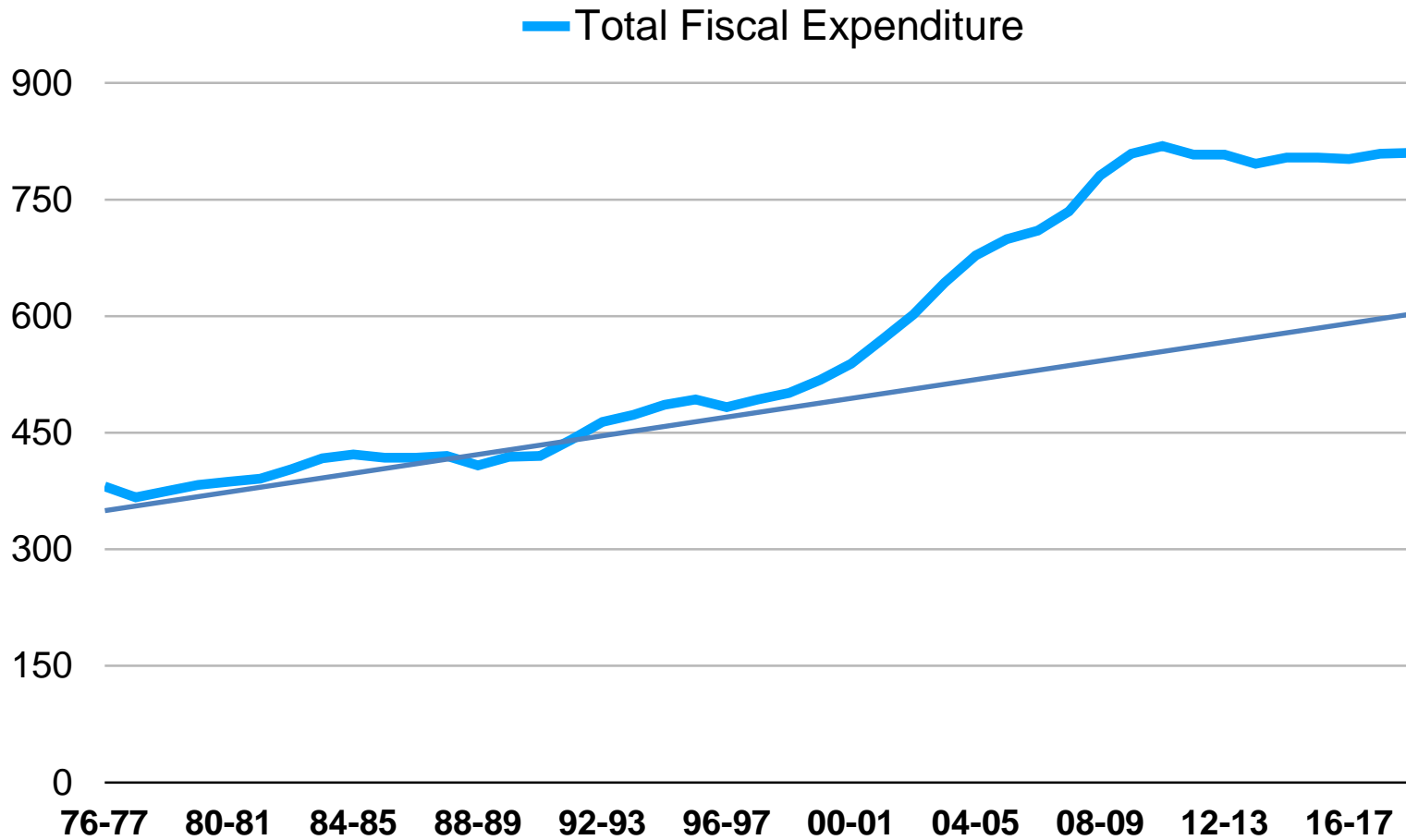
## UK Spending

- surge in spending in first decade of 2000's followed by an unprecedented decade of stagnation
- net, spending still above trend line from mid 70's to mid 2000's
- but ratcheting down more difficult than up AND different budgets have suffered to different degrees

## Scotland

- no long term data but probably similar profile to UK

# Long Run UK Finances



# Public Finances - looking forward

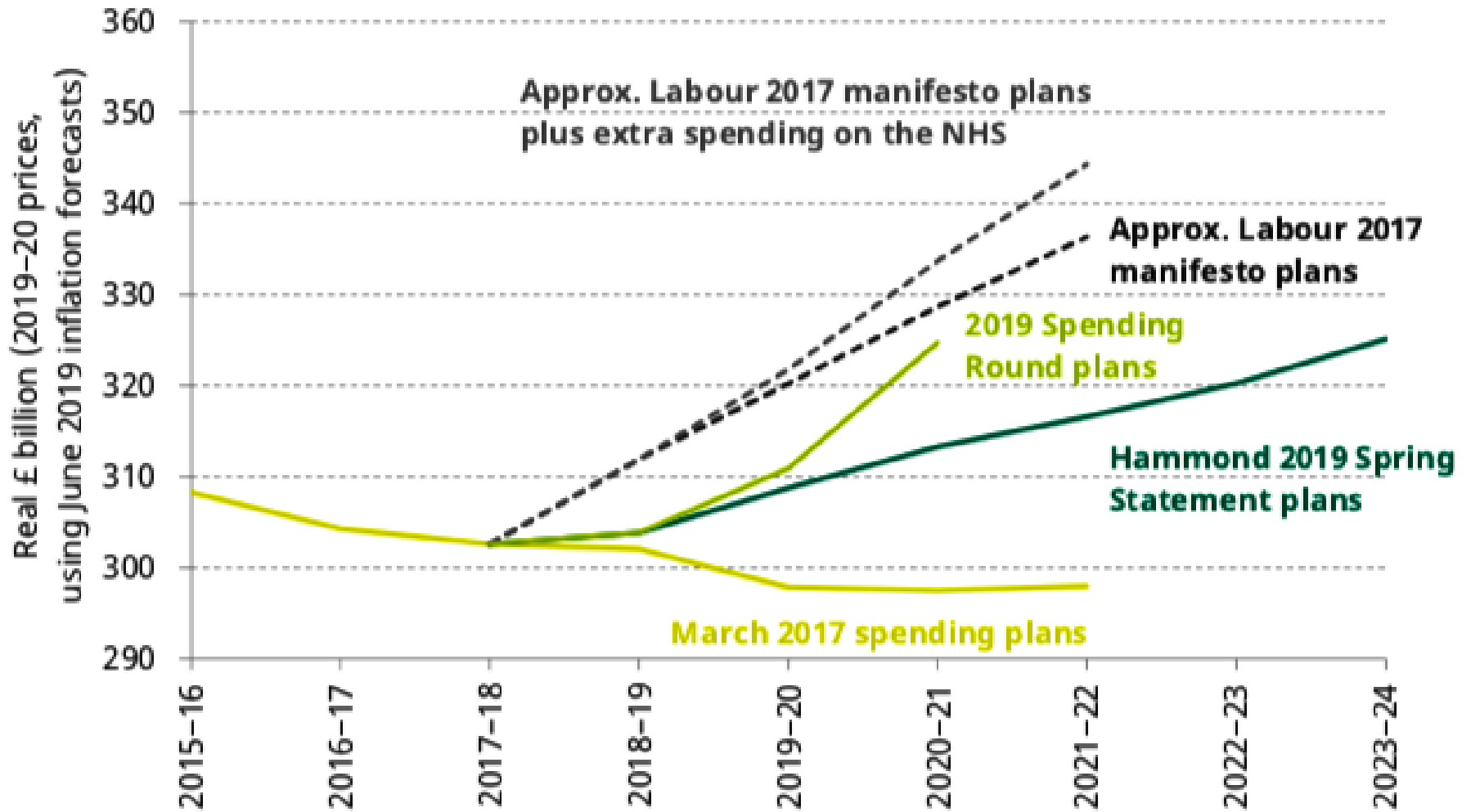
## UK Spending

- September Budget significantly boosted Resource (day-to-day) spending for 2020-21
- similar boosts likely for later years, regardless of who is in power and of type of Brexit
- protected vs non-protected public service budgets?
- capital expenditure boosts committed to by all
- longer term -ve Brexit impact likely, also ageing impact

## Scotland

- Barnett consequential's plus Scottish Income Tax

# Future UK Finances



# **Sectors Most Affected by Brexit**

## **Industries most at risk**

- Agriculture, Fisheries, Construction, Tourism related, Exporters, Just-In-Time businesses

## **Public Services most at risk**

- Health and Adult/Elderly Social Care, due to: shortage of medicines; potential rise in UK citizens living in the EU; staffing issues

# Housing Sector

## Areas of risk

- Construction material prices
- Supply of skilled staff
- Consumer demand

**House price falls** - forecasts of around 6-7% across the UK but potentially up to 20-30% (KPMG, BoE)

**Council and Housing Budgets** likely to improve in short run but unclear by how much in real terms

# Interest Rates and Housing - a Diversion

**Switzerland** has seen negative nominal interest rates for five years (currently -0.75%) and expected to continue

This **ultra-accommodative monetary policy** is to keep the Swiss franc competitive but has side effects

Some banks in Switzerland (and Denmark) offering **negative mortgage rates** (i.e. banks paying customers to take out a mortgage), as cheaper than depositing money with the Swiss National Bank

Can lead to **asset price distortion** & property boom

# Brexit Politics - EU

- **Economics:** Irish economy; exporters; Fishing
- **Irish issue:** essentially - UK in EU then no border, UK outside EU then some kind of border. Not clear how to resolve. Norway/Swiss solution? (but both within Schengen)
- ‘Withdrawal Agreement’ seems increasingly likely, but shape of post Brexit ‘**Trade Arrangement**’ deal still very unclear
- Trade an area where less likely to be universal agreement across all EU members than for Withdrawal Agreement

# Brexit Politics - UK

- UK election out-come highly uncertain
- Coalition government makes 2nd referendum more likely
- Potential, though now lower, for continued stalemate between UK Government and Parliament
- All political parties committed to higher public spending in short to medium term

# Overall: uncertainty dominates

- **Economics:** productivity; interest rates; inflation?
- **Public spending:** growth constrained; end of austerity splurge; tax rises?
- **Politics:** populist leaders; less open economies; coalition governments?

# In Conclusion

- Unique situation so outcome highly uncertain, in terms of both final form of both Withdrawal and final Trade 'Deals' OR implications of any 'No-Deals'
- Issues like cost increases and job insecurity impossible to predict accurately due to: i) timing unknown; ii) final trade arrangement unknown; iii) changes in behaviour of government/company/household uncertain
- Extreme forecasts have so far proved inaccurate, rather a slow drip effect is more likely to apply, negatively in the short to medium term, more ambiguous in the long run