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EU Referendum Summary

Britain Takes Back Control. Or Does It?

This is our report on the result of the UK's Referendum on continuing EU membership and its likely consequences. It was written over the weekend of 25th/26th June and completed at 5am on Monday morning.

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BRITAIN TAKES BACK CONTROL. OR DOES IT?

This is our report on the result of the UK's Referendum on continuing EU membership and its likely consequences. It was written over the weekend of 25th/26th June and completed at 5am on Monday morning. It's our attempt to give you an overview of how things currently stand following the victory for Leave, but you will appreciate that events are moving very quickly so there may be a slight disconnect between the comments we wrote early on Monday, and events that developed later in the day.

THE RESULT

> "I declare that the total votes cast for Remain were 16,141,241. The total votes cast for Leave were 17,410,742"

> "I will do everything I can as Prime Minister to steady the ship… but I do not think it would be right for me to be the Captain."

Two announcements, coming little more than an hour apart, which together sent the UK political system and its economy into wholly uncharted waters and sent stock markets and currency markets around the globe into turmoil.

The UK joined the European Union – then popularly known as the Common Market – on January 1st 1973. Ireland and Denmark joined at the same time, taking the original six members up to nine. On June 23rd 2016 the UK voted to leave the EU, now comprising 28 members and with five candidate countries hoping to join. There was a majority of over one million in favour of Leave, and – despite a petition calling for a second referendum passing the two million mark over the weekend – that appears to be that. And as several European leaders have said, 'out is out.' The 'most complicated divorce in history' is about to start.

Both the FTSE 100 index of leading shares and the pound rose steadily throughout Thursday, as the markets anticipated a win for Remain. The bookmakers reported several six-figure bets on the status quo. However, as the early results came in and it became apparent that Leave had done far better than expected, both the pound and FTSE Futures (trading in the Far East) went sharply in the other direction.

The FTSE fell by 8% after opening in London, with shares in banks and housebuilders being especially badly hit: at one point shares in Barclays and RBS were down by more than 30%. By the end of trading, the FTSE had bounced back and it closed 2.8% down on the day at 6,139. To give that some context, the FTSE ended 2015 at 6,242 and finished both January and February below that level. Supporters of the 'business as usual' school of thought would also point out that the FTSE finished Friday 17th June at 6,021 – up 70 points on the day. If you follow that line of thought, then the prospect of Brexit was worse for the stock market than the reality.

The pound was also hit sharply. Having been as high as $1.50 on Thursday, it touched levels on Friday that hadn't been seen since 1985, at one point falling by 10% to $1.33. It finally closed the day down 9% at $1.36. In early trading in the Far East, on Monday 27th the pound was continuing to fall against the dollar.

In truth, there was always going to be a sharp reaction, whichever side won. But with Leave having triumphed, the next few days and weeks will be especially critical. Bank of England Governor Mark Carney will undoubtedly be a key figure. He says the bank is 'well prepared' and he stands ready with £250bn to pump into the banking system: whether that would be enough to stand up to market sentiment and determined selling of sterling by the hedge funds remains to be seen.

George Osborne – the UK Chancellor and a man whose political ambitions appear to have been fatally wounded by Brexit – will make a statement at 8am on Monday, seeking to provide reassurance about the UK's economic and financial stability.

THE REACTION AROUND EUROPE

There was a pre-Referendum boost for the Leave camp when Markus Kerber, the head of Germany's equivalent of the CBI, said that post-Brexit trade barriers would be 'very, very foolish.' The UK is a highly significant market for many German and continental firms, and when the decision was announced there was plenty of conciliatory language. German Chancellor Angela Merkel was quoted as saying 'there is no need to be nasty to Britain' over the 'divorce' terms.

However, pressure was developing over the weekend for the UK to speed up those 'divorce' talks. EU President Jean-Claude Juncker said it 'was not an amicable divorce' – but then again, he claimed, it had never been 'a deep love affair.'

Several right wing groups across Europe saw Brexit as legitimising their own calls for referenda on continuing membership. But pro-Europe groups were also opening the champagne, claiming that the UK had always been a brake on further European integration and cooperation.

THE UK'S CREDIT RATING

One of the first casualties of the Brexit vote was the UK's credit rating. Credit ratings agency Moody's cut the outlook for the UK's credit rating to negative, saying that the result would herald 'a prolonged period of uncertainty.'

SO WHAT HAPPENS NOW?

First and foremost, the UK needs a new Prime Minister. Jeremy Corbyn's position as Labour leader is also in question, but it is the next leader of the Conservative party who will be negotiating Britain's exit from the EU. The early frontrunner is Boris Johnson, supposedly in a 'dream team' with Michael Gove. At the time of writing, Home Secretary Theresa May is emerging as the 'Stop Boris' candidate. May supported Remain, but did so very, very quietly.

David Cameron has said that he will stay on until October. However, it may be that events force him to step aside rather more quickly. Several European leaders are now calling for a 'quickie' divorce and the world's financial markets are unlikely to grant the UK three months to find a new leader. You can see an argument that Cameron is now the lamest of lame ducks and on that basis it may be hard for him to continue in office until the Autumn.

ARTICLE 50

Cameron appears to want the next PM to invoke Article 50 – the formal process giving two years' notice of our intention to quit the EU. Should the process not be completed within two years, then it can only be extended with the consent of all the other EU members.

Cameron had said that Britain would immediately invoke Article 50 – but the uncertainty of his own position calls this into question. If he is replaced by a pro-Brexit candidate (as seems likely), he or she is likely to argue that Article 50 works against the interests of the country leaving the EU: the new PM may seek a period of informal negotiation first.

As mentioned above, however, if there was one clear trend that emerged over the weekend, it was the desire of many European leaders to see Brexit happen quickly. They fear that an amicable, drawn-out settlement would simply encourage other countries to seek their own version of Brexit. David Cameron is due at a European summit on Tuesday: he can expect to hear 'get on with it' in several different languages.

HOW WILL BREXIT AFFECT YOUR FINANCES?

At this very early stage, the full impact of Brexit on our personal finances remains unclear, but we can already observe the following points.

The Pound and Prices

If the pound continues to fall then importing goods from other countries will be more expensive. This will push prices up and lead to a rise in inflation: but it's good news for exporters as their goods become cheaper to buy.

Petrol

An early example of prices going up will be seen on the petrol forecourts. Wholesale petrol prices are quoted in dollars, so as the pound falls against the dollar, petrol prices will rise. The Petrol Retailers Association are already talking of a rise of 2-3p per litre.

Savings and Investments

Without question, the biggest area for review is going to be your savings and investments. Assuming everything is worked out relatively quickly then the stock market should return to a normal pattern of trading – and as George Osborne will say today, the fundamentals of the UK economy are relatively strong. We certainly cannot assume that Brexit would be bad for shares: in the long run the stock market will be affected by events around the world – China's economy, growth in the Eurozone, the outlook for the US – as much as it will be affected by Brexit.

Clearly any rise in interest rates (see below) would be good news for savers.

Interest rates and Mortgages

Before the Referendum vote, Remain were saying that a vote to Leave would push up borrowing costs, leading to higher mortgage payments and increasing renting costs. But if Brexit were to lead to a period of low growth then interest rates could be cut in a bid to stimulate the economy. David Tinsley, UK economist at UBS, has said that he expects two interest rate cuts from the Bank of England over the next six months, taking rates from the current 0.5% to zero.

House Prices

There appears to be some consensus that Brexit could lead to a fall in house prices, especially in London and the South East. The Treasury has spoken of a fall of 10-18% over the next two years. Clearly not good news for existing homeowners, but anyone with children struggling to get a foot on the housing ladder may take a different view.

Tax

During the campaign, George Osborne gave dire warnings of tax rises in the event of a victory for Leave. This would be directly contrary to the Conservative's election pledge and would be difficult to implement: much more likely is an extension of 'austerity' for a further two years beyond 2020.

The Leave campaign did give a pledge to remove the 5% VAT on domestic fuel required by EU law – but there were so many pledges flying about that it is perhaps best to not build this into your household budget just yet.

Pensions

David Cameron did claim that a vote to Leave would threaten the 'triple lock' on pensions, but this presumes a poorer economy and a lower national income. If economic performance did deteriorate after Brexit, then the Bank of England might opt for a return to Quantitative Easing (QE) and/or lower interest rates. More QE would push down bond yields and with them annuity rates: so anyone buying a pension annuity would get less income for their money.

WHAT WILL THE UK'S RELATIONSHIP WITH EUROPE BE WHEN THE DUST HAS SETTLED?

At this stage, it's almost impossible to say. As of Monday, the Labour party is in turmoil with 20 members of the Shadow Cabinet having resigned. The papers are reporting that pro-Remain MPs may attempt to block the decision of the Referendum. SNP leader Nicola Sturgeon is also threatening to veto Brexit and is demanding a second Scottish Independence referendum.

But let's assume that Brexit goes ahead. The more rational Leave campaigners have been at pains to stress the UK's links with Europe: the more rational European leaders will not risk losing such a big market, especially as Europe moves slowly out of a recession. Perhaps the best guess is that the UK will leave the EU (and quite quickly) but will retain some sort of 'associate' status. This would involve the UK making some contribution to the EU budget, accepting some of its trading rules and doing its best to control immigration with a points-based system, all things which potential Prime Minister-in-waiting, Boris Johnson, has started to discuss publicly. In the best traditions of politics and darkened rooms, a compromise may be reached – with both sides spinning it as a win. Will it work? No one knows; but when the dust finally settles, we may find that 'out' was not quite 'out' after all.

The next few days and weeks will be interesting, to put it mildly. We appreciate that our clients may have concerns and questions, so please don't hesitate to get in touch with us at any time.

This guide is based on Kymin Financial Planners understanding of the EU Referendum as of 5am Monday 27th June 2016.

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