Political Uncertainty Intensifies In UK

- Two main UK parties punished in EU parliamentary elections
- Pressure in both parties to adopt more clearly defined positions on Brexit
- Brings increased political risks over remainder of 2019

The message from the EU parliamentary elections in the UK (where voter turnout increased 1.5% from 2014) was that public opinion was split between those in favour of a swift exit from the EU (even without a deal) and those that want to remain in the EU. The newly formed Brexit Party and UKIP combined collected just under 35% of the vote share while those parties supporting a second referendum (the Liberal Democrats, Greens, SNP, Plaid Cymru and Change UK) amassed just over 40% of the vote. In contrast, the Conservative and Labour parties collectively only captured just over 23% of the vote. This has significant implications for UK politics and, as a result, GBP.

For the Conservative Party this means pivoting away from the approach taken by Theresa May’s government. As there is little point moving towards supporting a second referendum given their core voter base, it’s possible they will throw their weight behind a leadership candidate that supports a harder Brexit stance. At the same time this candidate must try to keep One Nation Tories on board and also have a strong enough personality to lead the party into

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Newswatch

1. **US/China:** The South China Morning Post reports (citing a source) that the Politburo overwhelmingly decided at a meeting on May 13 “that the Americans had gone too far and that China should put its foot down”. >
a possible general election. However, even if a candidate is chosen than manages to meet all these criteria, the risk remains that were a hard Brexit to be on the cards then some of the remain supporting wing of the party might be prepared to support a no confidence motion in the government.

**For the Conservative Party**

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If the Conservative Party needs to pivot towards a more clearly defined stance on Brexit then so too does the Labour Party given that much of the collapse in support is being blamed on their failure to back a second referendum. So far all Labour leader Jeremy Corbyn has said is that it is "clear that the deadlock in Parliament can now only be broken by the issue going back to the people through a general election or a public vote. We are ready to support a public vote on any deal." Meanwhile, Len McCluskey, head of the Unite union, urged colleagues to “hold our nerve” and wait for a general election. He tweeted that “Labour losing votes, as we expected. But these elections aren’t relevant to where we are now.”

However, there have been signs of movement overnight with The Daily Mirror reporting that Mr Corbyn is “poised to support a people’s vote on Brexit” and could announce his backing within days (see Newswatch). Were he to do so then the pressure on the Conservative Party to pivot towards a more clearly defined position would likely intensify rapidly.

**Much of the collapse in support (for Labour) is being blamed on their failure to back a second referendum**

The volatility seen in 2010 (at a time when the main parties were essentially vying for the center ground of UK politics) highlights perfectly GBP’s dislike of political uncertainty (something in abundance in the UK right now). That period saw realized volatility in GBP/USD reach levels that have

2. **US/China**: The NDRC says (in a questions-and-answers bulletin): “Will rare earths become China’s counter-weapon against the US’s unwarranted suppression? What I can tell you is that if anyone wants to use products made from rare earth to curb the development of China, then the people of the revolutionary soviet base and the whole Chinese people will not be happy.”

3. **South Korea**: Reuters cites a BOK official as saying that herd like behaviour in the FX markets is “excessive”

4. **UK**: The Daily Mirror reports that Labour leader Jeremy Corbyn is “poised to support a people’s vote on Brexit”. It cites “senior figures” as saying he could announce his backing within days.
only subsequently been breached in the months immediately following the 2016 referendum.

Given this it is therefore interesting to note that there is some evidence the market is beginning to focus on the issue of political risk. In particular there has been a noticeable widening in the gap between six-month at-the-money forward implied volatility over the past two weeks, reaching its widest level since Q1 2016 (in the run up to the referendum).

On the Radar

May 29, 2019

- DE May unemployment rate (0855 BST): Reuters consensus forecast 4.9%; previous 4.9%
- CA BOC rate decision (1500 BST)

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