Quarterly Newsletter / Autumn 2019

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Brexit – will the saga ever end?!

For the first time in 37 years, the UK Parliament sat on a Saturday last week and saw the planned vote, i.e. the ratification process on the Government's Brexit deal, forestalled when MPs voted for a motion withholding Parliamentary approval for the deal until all legislation implementing it had been passed. Under the terms of the previously passed EU Withdrawal (No.2) Act (the so-called "Benn Act" or "Surrender Act") PM Boris Johnson was therefore required to write to the EU asking for a *third* extension to the UK's planned departure.

In the event, three letters were sent. The first one was the one he was forced by law to send - Boris Johnson decided that he would send it unsigned. In fact, it was copied and pasted directly from the so-called Benn Act. The second letter was written by the UK's Ambassador to the EU, addressed to the Secretary-General of the Council of the EU, and effectively was a cover note explaining the unsigned letter which had been required to be sent under the Benn Act. A third letter *was* signed by Boris Johnson. This one was addressed to Donald Tusk and made it clear that the PM wanted to distance himself from the first, unsigned letter.

Complicated? Well, it is simply another small instalment in the Brexit rigmarole.

On Monday of this week, John Bercow, the Speaker of the House of Commons, blocked the so-called meaningful vote and technically, he was right to do so. In truth, nobody really expected him to help the government in this matter. The Speaker is meant to be impartial, but it has been obvious to any onlooker that he has been firmly on the side of the 'remainers' for a long time. You may call him verbose, pompous, smug and hubristic, but impartial he is not. Fortunately, in September he announced his departure on 31st October this year. Hopefully, he will go, and we will be spared his bellowing the word 'Order' over and over again.

On Tuesday, our Prime Minister's 'do or die' pledge to leave the EU by that same date was thwarted by MPs despite the fact that they had voted, *in principle*, to approve his Brexit deal. Not unreasonably, they felt that three days was simply not enough to scrutinise and debate the details of the Withdrawal Agreement Bill. A caller to a radio station made the point that it had taken her and her husband longer to decide on the colour of a new settee…

So, the Brexit ball is once more back in the EU's court, and we are waiting to see how long an extension they will grant us. Donald Tusk suggested three months might be a good idea, but Monsieur Macron thought two weeks would suffice.

On Wednesday, the PM and Jeremy Corbyn met but couldn't agree on a timetable for the bill, and the thought of a general election must have been uppermost in their minds. The Leader of the Opposition said he was all for a general election, but only *after* the EU had approved a delay.

The question of when to hold a general election is not straightforward either. The Tories might like the idea of a snap general election as they are some 10 points ahead in the polls, but under the Fixed-term Parliaments Act of 2011, Boris Johnson has to get two-thirds of the Commons to agree. Bearing in mind that he struggled to get around 330 MPs to back him recently, the required 434 MPs seem a tall order. The Government clearly would need support from the Labour benches to get to that number.

There is an alternative: Boris Johnson could call a vote of no confidence in his *own* government, but that would risk the creation of a so-called national unity government, put in power for a limited time under a new, interim Prime Minister. It was first mooted in September, and Kenneth Clarke and Harriet Harman, the longest-standing male and female MPs, were mentioned as potential candidates when it became clear that Jeremy Corbyn would not be acceptable to some parties and MPs.

To make matters yet more complicated, we now hear that the Cabinet is somewhat split in their opinion as to when to go for a general election, and the same could be said of the Shadow Cabinet. And finally, MPs are worried about a winter election – bad weather might affect the turnout – and since most polling stations are situated in schools, it might disrupt the Nativity Play season. Oh dear!

Yesterday, on Thursday, Boris Johnson challenged Jeremy Corbyn by offering MPs more time to debate his Brexit deal, provided Labour would agree to a 12th December general election, but Jeremy Corbyn was not prepared to go along with that unless a 'no deal' Brexit is taken off the table.

We were told that the EU would tell us today (Friday) as to what sort of extension they would agree to, but the latest news out of Brussels suggests that we will have to wait until Monday or Tuesday, or possibly longer… It gets crazier by the day!

So, we have just spent quite a time looking at the events of just a week, but in reality, the Brexit saga could go on for a lot, lot longer. Madness, indeed!

Let us now turn to a more rational environment, namely that of financial markets.

They have behaved well, if unspectacularly. The upward trend has continued, but we are very aware that this cannot go on forever. We therefore pay close attention to any signs that suggest a reversal of fortune.

In the Summer Newsletter we touched on various indicators which can often highlight the direction of travel in markets but also cautioned that these cannot be taken as fool-proof. Market sentiment will often play a crucial role in either exaggerating or dismissing the importance of a particular event, but long-term trends can also have an influence.

One of the indicators mentioned was the oil price which, broadly speaking, has a direct impact on the level of economic activity and levels of inflation, particularly on those economies that are dependent on imported oil. As noted during the summer, the rising tensions in the Gulf between the United States and Iran did indeed have such an impact, causing a spike in the price of some 20% from the beginning of the year. However, the effect has been somewhat short-lived and, in hindsight, relatively mild.

We have subsequently witnessed confrontation between Iranian ships and a tanker with a British frigate escort, the shooting down of an Iranian drone by the United States and the seizure of an Iranian tanker by Britain, all symptomatic of continued tension. Things were further enflamed in early September, with the attack on Saudi Arabia's oil processing facility at Abqaiq which interrupted some 5% of the world supply with a loss of 5.7 million barrels per day.

And yet the price of Brent Crude is, at the time of writing, around $61, barely 10% up for the year to date with current price pressures being downwards.

The contrast with the OPEC (The Organization of the Petroleum Exporting Countries) embargo of 1973 and the events of 1979 when the Iranian Revolution resulted in a 4% drop in global production and a doubling of oil prices within twelve months is marked.

A number of longer-term trends have played into this. The broadening of oil production has seen a decline in the power of OPEC to control prices and this has been further compounded by the expansion of America's shale gas facilities to the extent that the US is now self-sufficient in oil.

With the world's largest economy able to expand energy production in a matter of months when required (as opposed to the expansion of traditional oilfield production which can take years), the impact of the oil price seems less critical especially as developments in the automotive industry are moving away from the internal combustion engine. In short, supply levels seem more than adequate at present.

The avowed policy intention of reducing the global dependence on oil, albeit only half-heartedly pursued in many economies, places a question mark over the future value of those already discovered assets which show as a positive in the balance sheets of the major oil production companies. Indeed, a cynic might regard the proposed listing of Saudi Aramco through an IPO as an attempt to realise some value today from assets which, in future years, might be of questionable importance.

Moving away from oil, recent moves in the United States to resume the purchase of Treasury Bills by the Federal Reserve are an indication that Jerome Powell is aware of the downward pressures on economic activity. Whilst the most recent 'Jobs Report' highlighted the lowest level of unemployment for fifty years, it also showed an unanticipated *fall* in manufacturing employment as the effects of the trade dispute with China are beginning to show. Whilst Powell has insisted that the expansion of the balance sheet through the purchase of Treasuries is not a long-term programme, it does raise the possibility of a boost to inflation. The previous rounds of quantitative easing were criticised for merely inflating asset prices ("Wall Street rather than Main Street") and did not feed through to create a broader inflationary pressure. If things prove different on this occasion, the subsequent inflationary spike and weakening dollar will both serve to support the gold price.

It is these and other concerns that lie behind the current portfolio holdings in gold. Whilst we have not witnessed an inflation spike induced by a rising oil price, typically positive for gold prices, the fear of global recession and potential political conflict are sufficient to support the demand for gold in its traditional role as a 'safe haven'.

We have not abandoned equity markets, however, as there has been a steady appreciation over the first three quarters, albeit with frequent bouts of volatility as sentiment over the possibility of a resolution to the trade war waxes and wanes. By taking a cautious but balanced approach in portfolios we have been able to post gains in both the growth and defensive elements but remain alert to the possibility of unfolding events triggering a swing in sentiment.

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