**Chris Bailey**
European Strategist, Raymond James Euro Equities

RAYMOND JAMES®

## Brexit is certain, defining it on the other hand may prove more difficult

So we have voted to leave the European Union. Despite 48% of the voting population feeling pretty sore, rumours of a legal challenge to the democratic verdict and even calls for a second referendum, this is the reality ahead. As the new Prime Minister Teresa May asserted in her coronation speech "Brexit means Brexit".

With that firmly established the correct attitude is to concentrate on the opportunities emerging from this.

The most pressing question is over what trade agreement the UK will strike with the EU. Will we opt for the Norwegian model which grants full access to the single market but with concessions on free movement and payments to the EU, a Swiss model where we have to negotiate an insurmountable number of trade deals raising questions over capacity or any number of other permutations?

In short whilst the referendum was a simple binary vote, 'in' or 'out', what happens next exists in grey.

And in the meantime the economic clock is ticking. The plunge of the latest IHS-Markit Purchasing Managers' Index data to a seven-and-a-half year low has shown the immediate sentiment hit on business confidence and expenditures.

Reaction to this data also pushed the Pound down, embedding the currency caution kicked off on 24 June 2016 with the 7.5% fall in the value of GBP against the U.S dollar, a decline greater than anything seen on any individual day during other Sterling crises in 2008 or for those with longer memories (and probably more grey hairs) in 1992 or 1981.

At first glance this sharp downward shift in the pound appears to be a policy safety valve that could offset any post-Brexit impact. You know the theory: depreciate your currency and boost your exports – and given the UK's high trade deficit position, such a move is just what the economic doctor order especially in the light of the shabby PMI data noted above. Even the FTSE-100 index has rallied strongly as the benefits of overseas earnings derived from the Americas and Asia are perceived to hold more worth.

But economic theories – and stock market movements - are informed by context. What made sense from an overvalued position currency depreciation, as in Sterling's White Wednesday September 1992 exit from the Exchange Rate Mechanism, will not provide a strong foundation for economic recovery for a pound that was not particularly overvalued in 2016. This is shown by the far patchier performance of the more domestically centred FTSE-250 mid cap index or the property and housebuilding sectors since the Brexit vote. The FTSE-100 index cannot be thought of as being even mildly representative of the UK economy.

Policy makers will just have to step up. The newly liberated UK will have to go completely in the opposite direction to the perceived economically sclerotic EU. This means avoiding where possible – and preferable at all - imposing tariffs to protect domestic industries, restrictions on skilled citizens from other parts of the globe who can add value to the overall country or imposing a burden of new legislative red tape that entangles businesses in a web of regulation and high costs.

In the global, dynamic markets of the 21st Century, the UK must adopt a mind-set that encompasses the entrepreneurial zeal of East Asia and the laissez-faire can-do-ism of the United States, mixed up with our own style and global outlook. In short, a supply side revolution not seen in this country since the 1980s.

All of the above is essential…but necessarily longer-term.  Clear shorter-term actions are also required.

The Bank of England may have passed on cutting interest rates in July in favour of waiting for more data but the pressure to cut rates proved insurmountable…and sensible. In August the Bank of England cut rates to an all-time low of 0.25%, and signalled that they are poised for further action if required, irrespective of the niceties of any upcoming inflation data. The European Central Bank are also likely to join this new stimulus party by the end of the year too with their meeting in September now a key focus.

With the clouds of uncertainty showing no sign of dissipating it can be difficult to maintain equanimity and make sound investment decisions especially when the reaction of some indices like the FTSE-100 has been to rise sharply following the fall in the value of the Pound. A crisis in domestically-centred UK investments and financial exposures can also presents opportunity, so keep the faith, do your homework and – in the words of legendary investor Warren Buffet – be 'greedy whilst others are fearful'.