

# *UK Election Preview*

## *Conservative majority is our base case*

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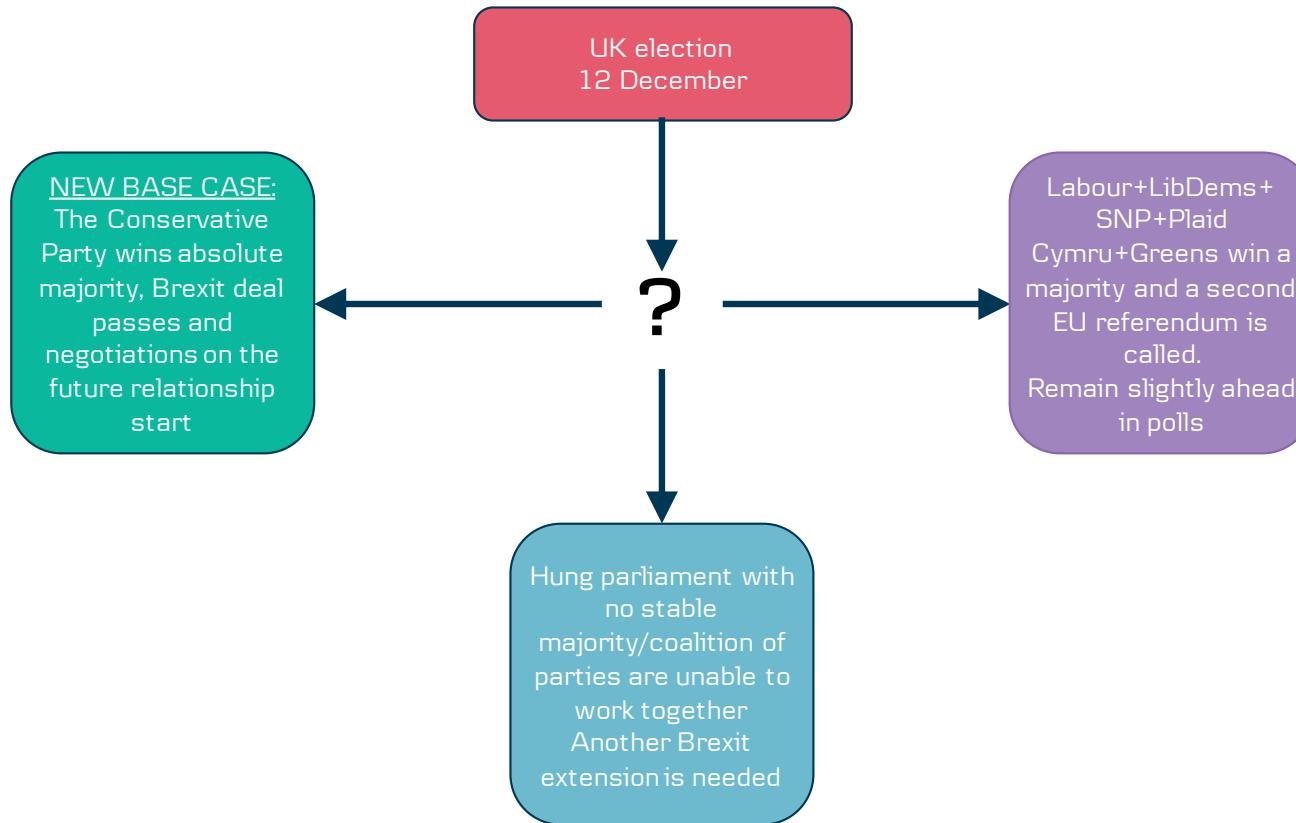
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Important disclosures and certifications are contained from page 20 of this document.

# *Conservative majority is our new base case*

- The Brits are going to the ballot boxes on Thursday 12 December, which will be decisive for what will happen on Brexit. The voting stations close at 23:00 CET, when we should also expect to get our first exit poll. The vote count starts immediately and we should know the final result by early morning on Friday 13 December. It is notoriously difficult to predict the outcome of the UK election due to the “winner takes all” voting system (see Appendix on slide 19 for details). Opinion polls show that the Conservative Party is around 10pp ahead of Labour.
- YouGov’s so-called MRP model, which was the only seat projection model correctly predicting Theresa May would lose her absolute majority in 2017, predicts a solid majority win for the Conservative Party (359 seats versus 211 for Labour, 13 for LibDems and 43 for SNP. 326 seats are needed to secure a majority), see slide 9. It may be the case that the model was lucky predicting the right result last election but we do not have much else to rely on.
- Our base case is that the Conservative Party will win an absolute majority, which would mean that PM Boris Johnson can get his Brexit deal through Parliament before Christmas (he will no longer need to rely on DUP votes and the moderate Conservative rebels who voted against him are either expelled or not seeking re-election, so the Conservative MPs will be more loyal to Johnson). Friday 20 December has been mentioned as a potential voting day.
- If, against our expectation, the opposition (Labour, LibDems, SNP, Plaid Cymru and Greens) secures a majority combined, we expect the parties eventually to call for a second EU referendum with “remain” as one of the options. Opinion polls show that “remain” is slightly ahead, but not by much.
- We may also end up in the situation with a very hung parliament, which is unable to pass anything. In this scenario, the UK will probably ask the EU for another extension, which we expect the EU to grant despite Brexit fatigue in Brussels. We are probably heading for another snap general election in this scenario.
- Our base case and consensus have been heavily converging on a Conservative majority. At the time of writing, Sterling is at 0.8445 and we think the embedded Brexit risk premium is essentially zero. However, momentum and euphoria can probably take Sterling even higher, even if only for a limited period of time. We would assume a drop to the tune of 0.5-1.0 percent in EUR/GBP under the base case, thus settling in at the high end of 0.83-0.84 in the days after the election. Under the alternative scenario of a hung parliament, we believe the market would sour and take EUR/GBP towards 0.86-0.88 range.

# Base case: Conservative Party will win the election and deliver Brexit by 31 January 2020



We consider each scenario in the following slides

## Scenario 1 (base case): Conservatives win absolute majority

- A majority win for the Conservatives would mean PM Johnson would implement his Brexit deal without too many problems before Christmas (possible voting day is 20 December). Even a slim majority may prove sufficient, as long as Johnson achieves independence from the DUP and the Brexit Party. Prime Minister Johnson would become more powerful, as winning elections is what politics is all about. At the same time, some of the excluded Conservative rebels will no longer sit as MPs, making life easier for Johnson. In other words, the Conservative MPs will become more loyal.
- Focus will instead turn to the negotiations with the EU on the future relationship, where another type of 'no-deal' Brexit looms by the end of the transition period if no agreement is reached (see slide 12 for time-line). In our view, the negotiations on the future relationship are going to be much more complicated than the negotiations on the withdrawal agreement, as there are many more details and less time, assuming PM Johnson's promise not to extend the transition period by 1-2 years is credible.
- Michel Barnier, who will be the EU's chief negotiator in the upcoming negotiations, has said the EU will prioritise a trade deal but warned time is short, see [Financial Times](#).
- Looking beyond Brexit, Johnson's economic policy may also attract attention, as he has pledged increased government spending (but postponed some tax cuts to e.g. corporates). We do not know many details yet, but it could potentially be a significant fiscal boost to growth down the road.
- We also see a high risk of a second independence referendum in Scotland in coming years after the UK has left the EU (support for Scottish independence is increasing due to Brexit). Polls show the Scots are divided 48%-48% on the question, see slide 16. Further out, we may even see a unification referendum in Northern Ireland, as Northern Ireland is treated differently from the rest of the UK.

## *Scenario 2: Labour, LibDems, SNP, Plaid Cymru and Greens win a majority*

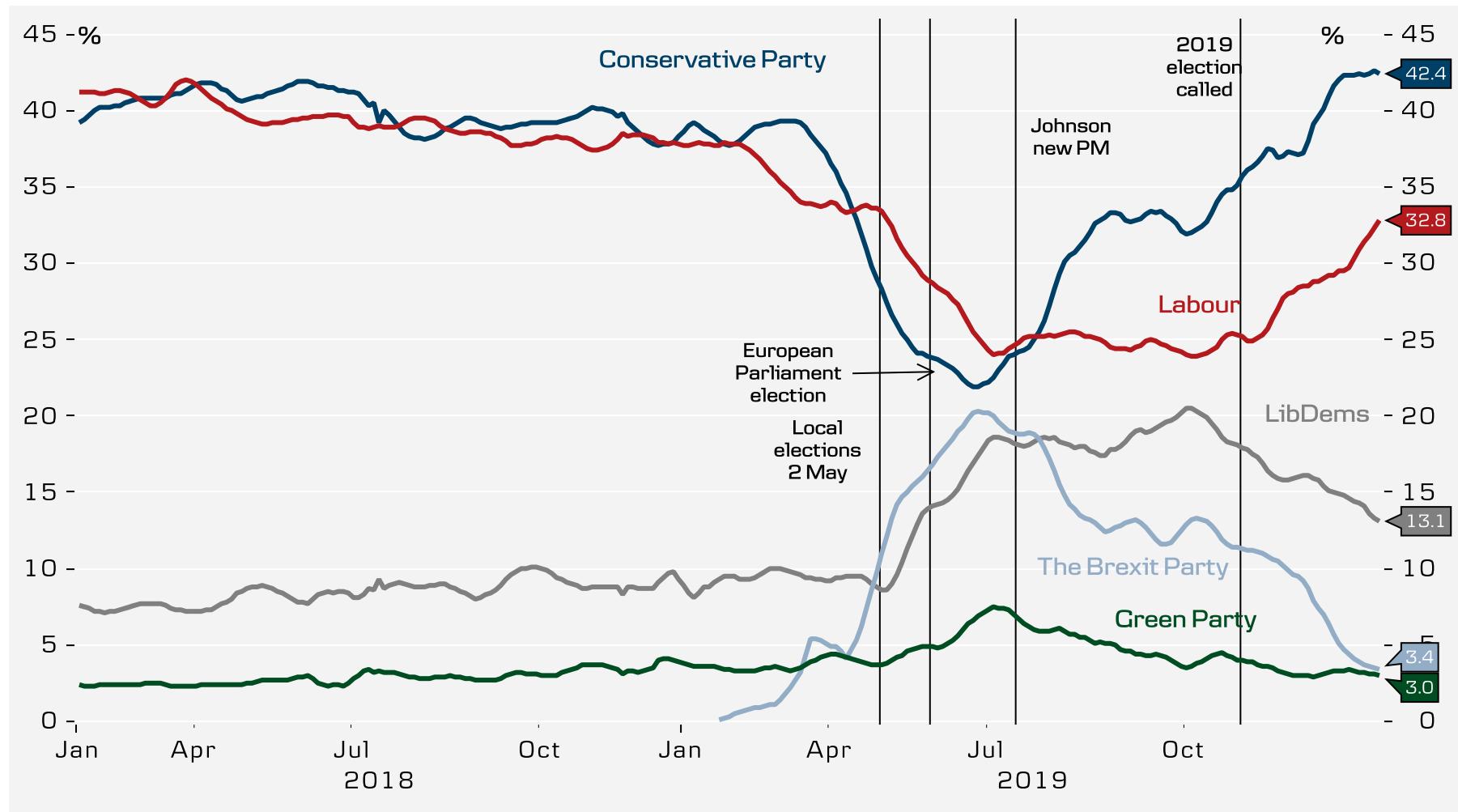
- While it would not be easy for the five parties to co-operate, they are more pro-EU and have indicated they want a second EU referendum with 'remain' as an option. Labour is most sceptical, as it wants to negotiate its own Brexit deal first, which would be included on the ballot paper. Whether this will be the case depends on the strength of the individual parties. The stronger the Liberal Democrats are, the higher the likelihood of a second EU referendum.
- We think a second EU referendum with 'remain' as an option is almost certain in this scenario.
- Looking at recent EU referendum polls, 'remain' is still slightly ahead but it is a close call, not least because polls seemed somewhat biased towards 'remain' ahead of the 2016 vote. The question is what alternative to 'remain' is set to appear on the ballot paper (Labour has said they want to renegotiate a deal with the EU).
- Following an EU referendum, it is difficult to see such a coalition being able to survive and we may head for another general election.
- In our view, it is highly unlikely Labour will get an absolute majority by itself, not least because the Labour Party is polling badly in Scotland. If we are caught by surprise, markets will focus not only on Brexit but also on Labour's overall economic policy.

## *Scenario 3: Very hung parliament with no stable majority*

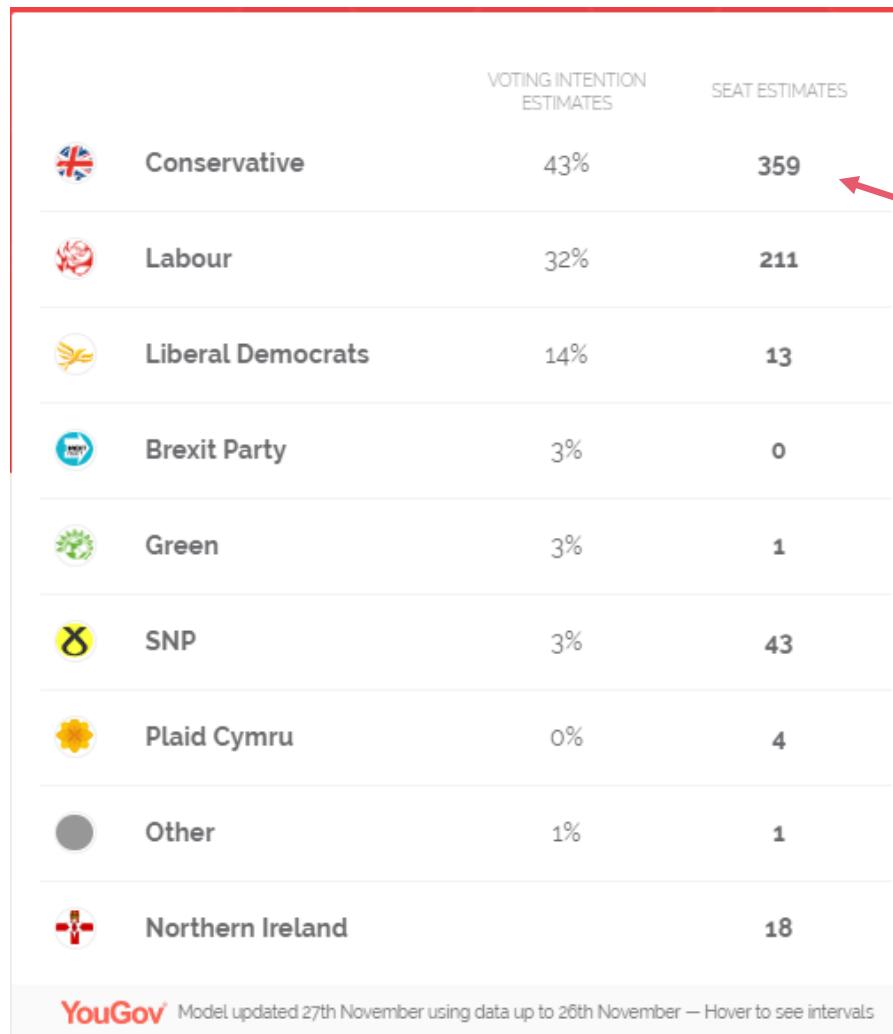
- We may end up with a hung parliament without a clear/stable majority for any party or coalition of parties (or the parties refuse to, or are unable to, work together in coalition). **In this scenario, it is difficult to predict what would happen.**
- **It is likely that another extension beyond 31 January would be needed in this scenario.**
- **Despite no political stability, we think the likelihood of a no-deal outcome is still low in this scenario.** Either the UK will ask the EU for another extension (with the risk of the EU rejecting it, which we doubt despite Brexit fatigue) or a majority of Conservatives and Labour Brexiteers will eventually pass something like PM Johnson's deal (or former PM May's deal).

# *Charts and time-lines*

*The Conservative Party is back at its ‘normal’ level around 40% while Labour is now above 30%*

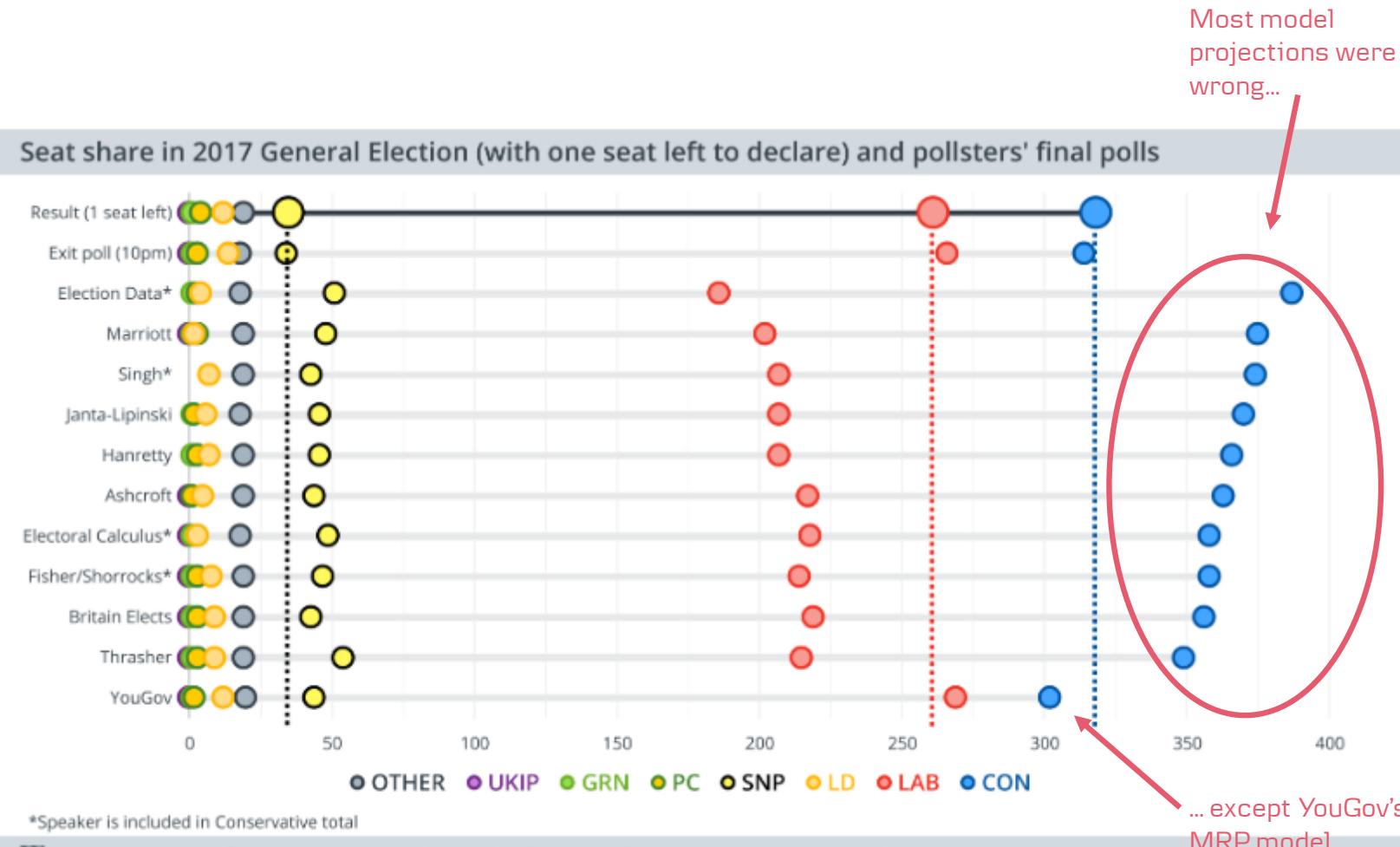


# YouGov's MRP model predicts a big win for Boris Johnson (359 seats versus 326 needed for a majority)

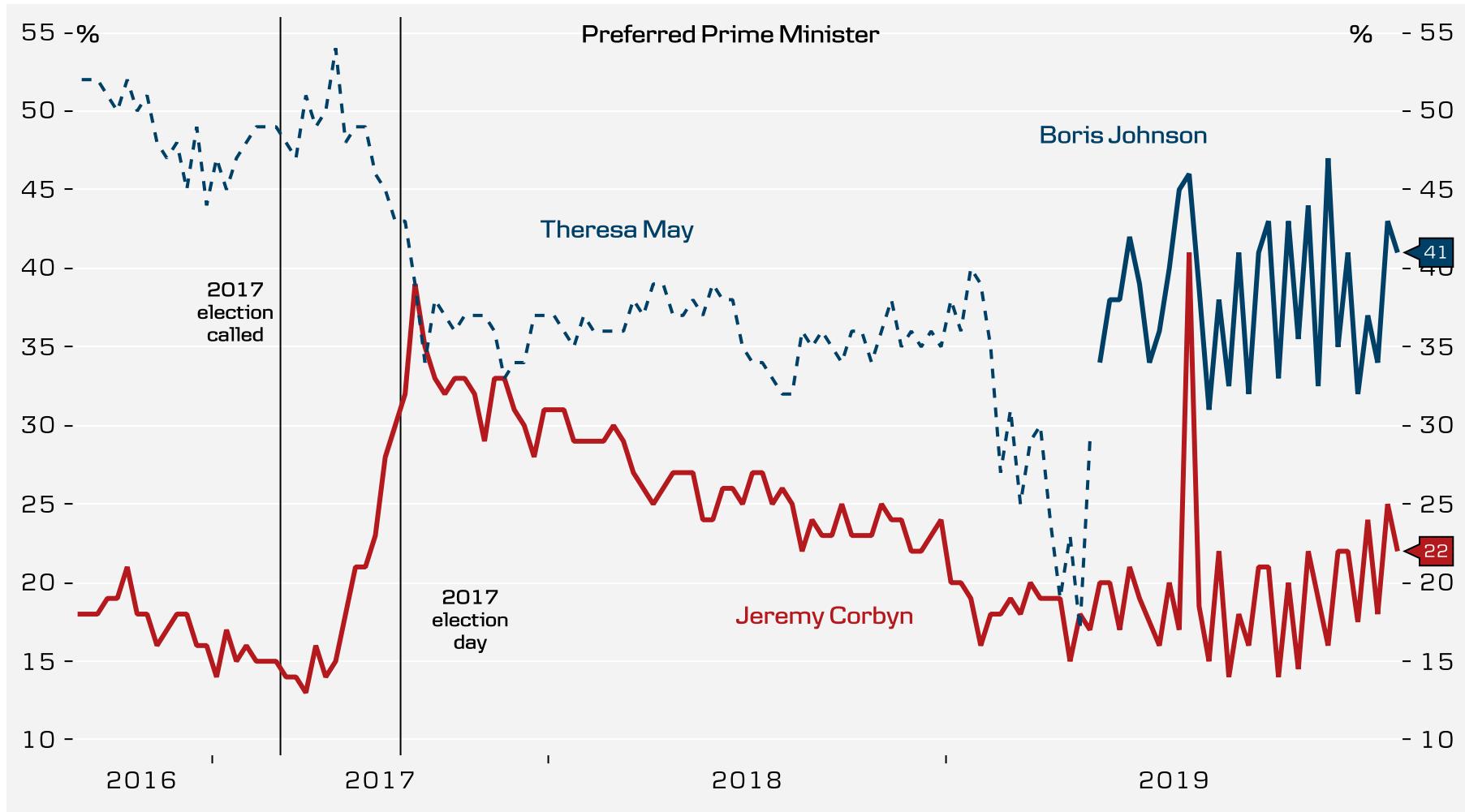


326 seats out of 650 are needed to secure an absolute majority in the House of Commons. In practice the number is actually smaller.

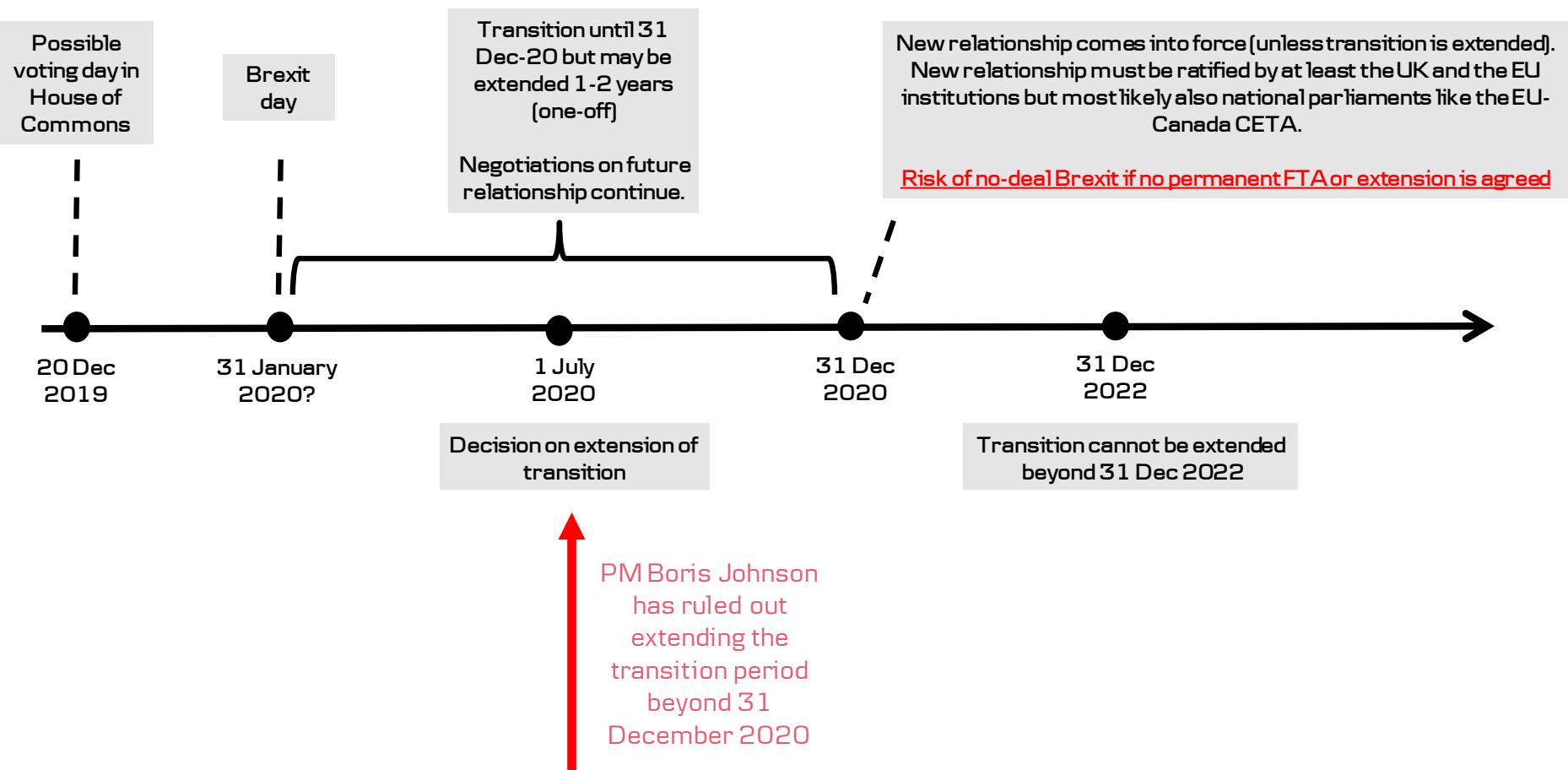
YouGov's MRP model was the only one to correctly predict Theresa May would lose her absolute majority in 2017

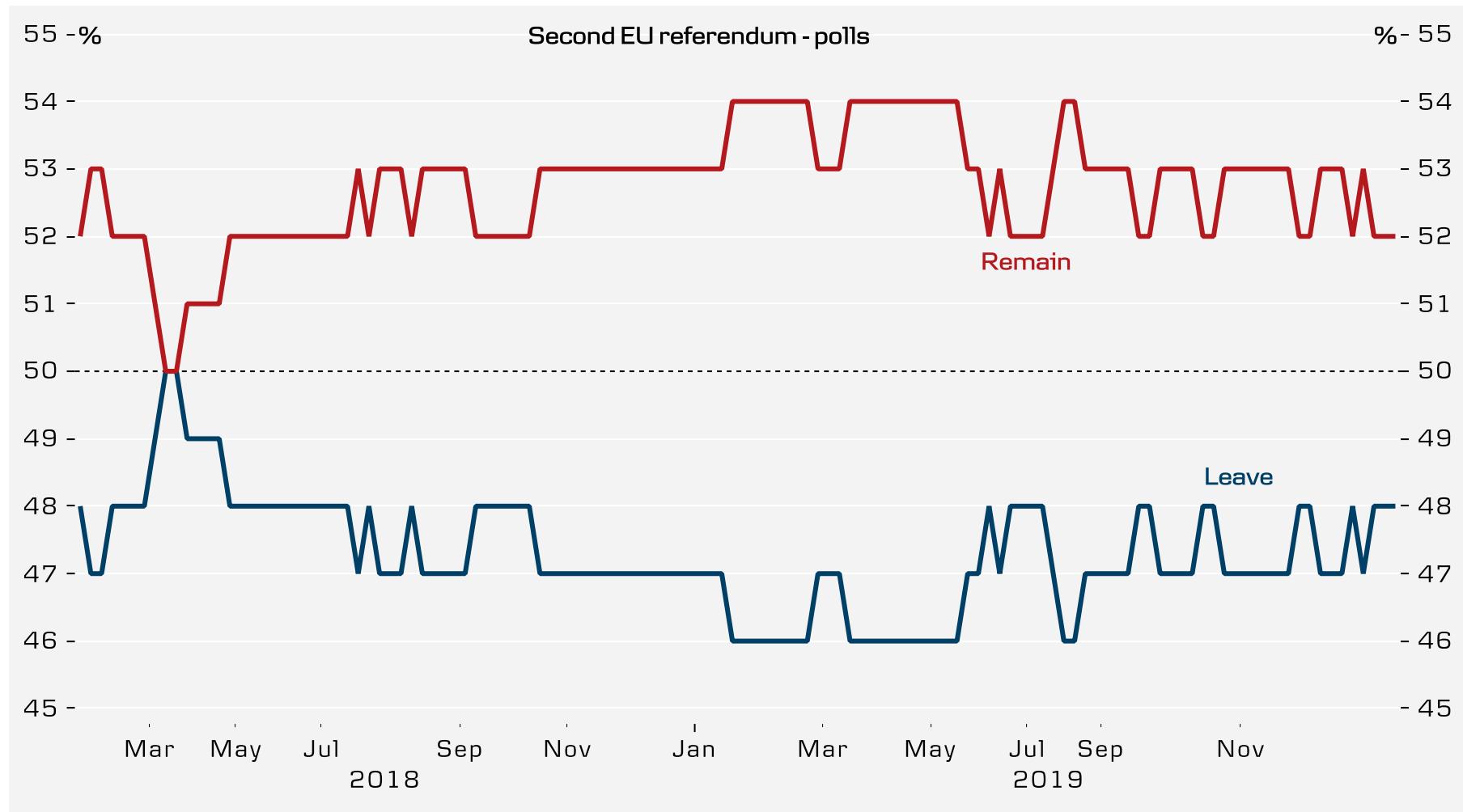


*Boris Johnson's rating lower than Theresa May's in early 2017, but way above Jeremy Corbyn's*

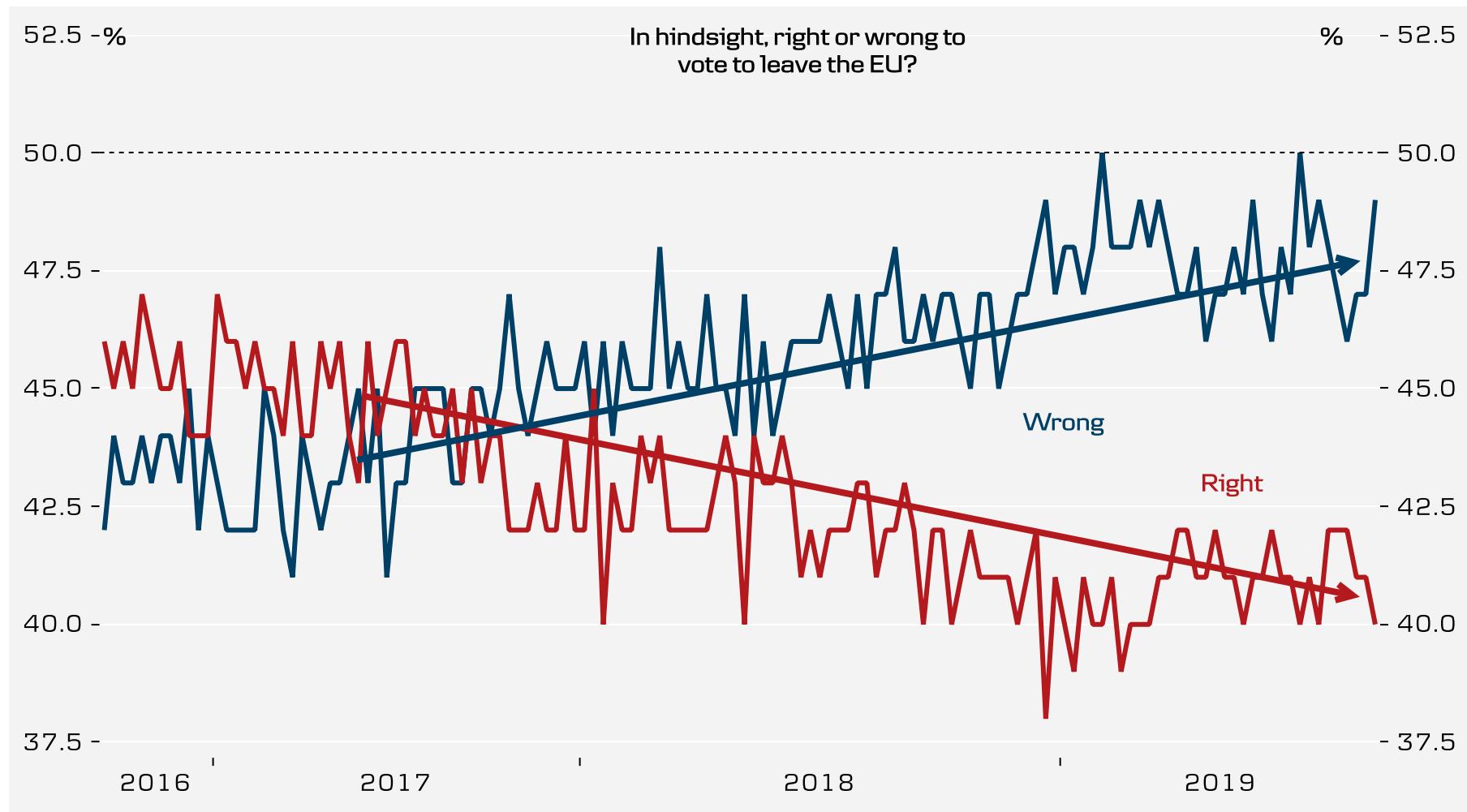


# Brexit time-line assuming Conservative majority

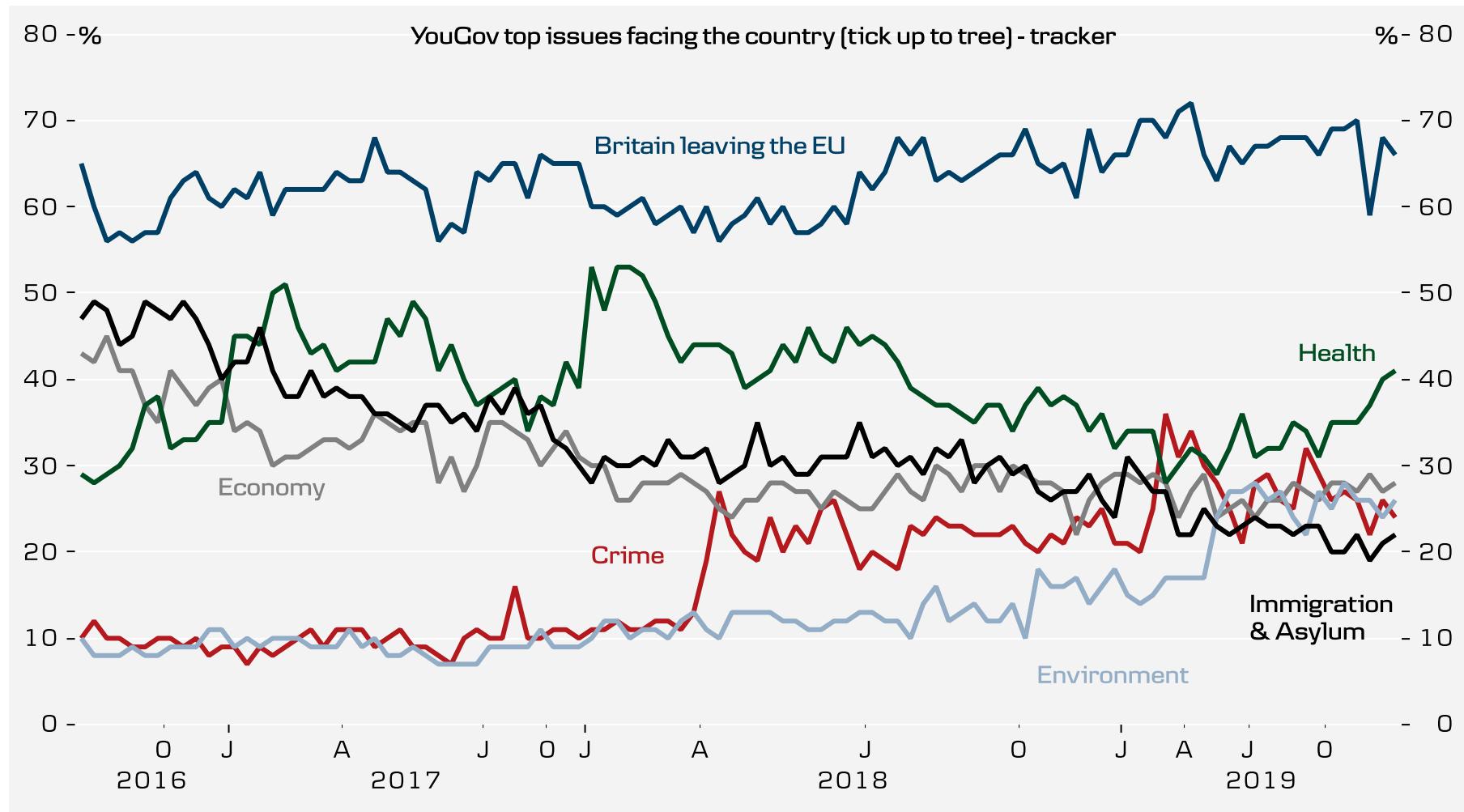


*'Remain' slightly ahead in second EU referendum polls*

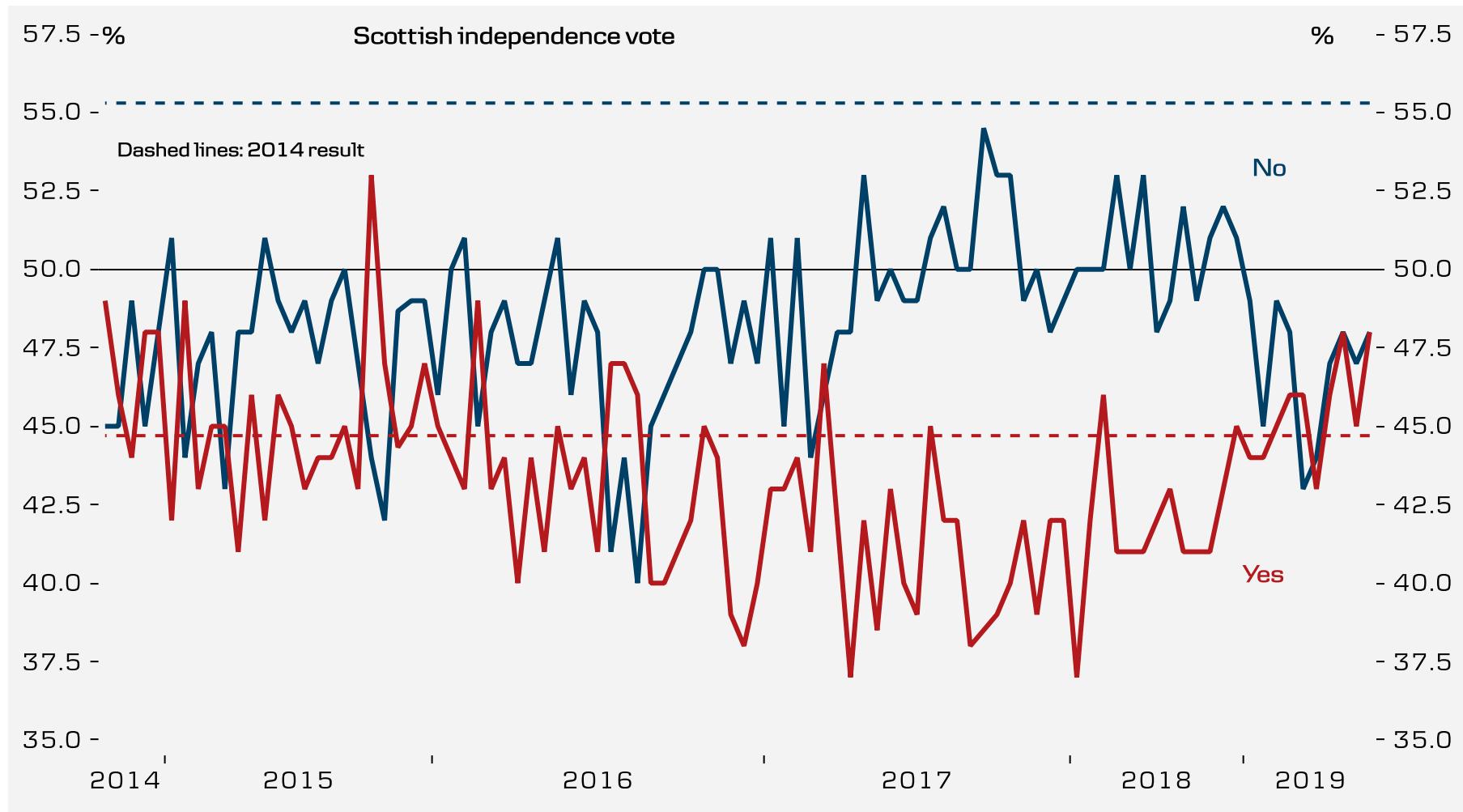
*More (but not a majority) think it was the wrong decision to leave the EU*



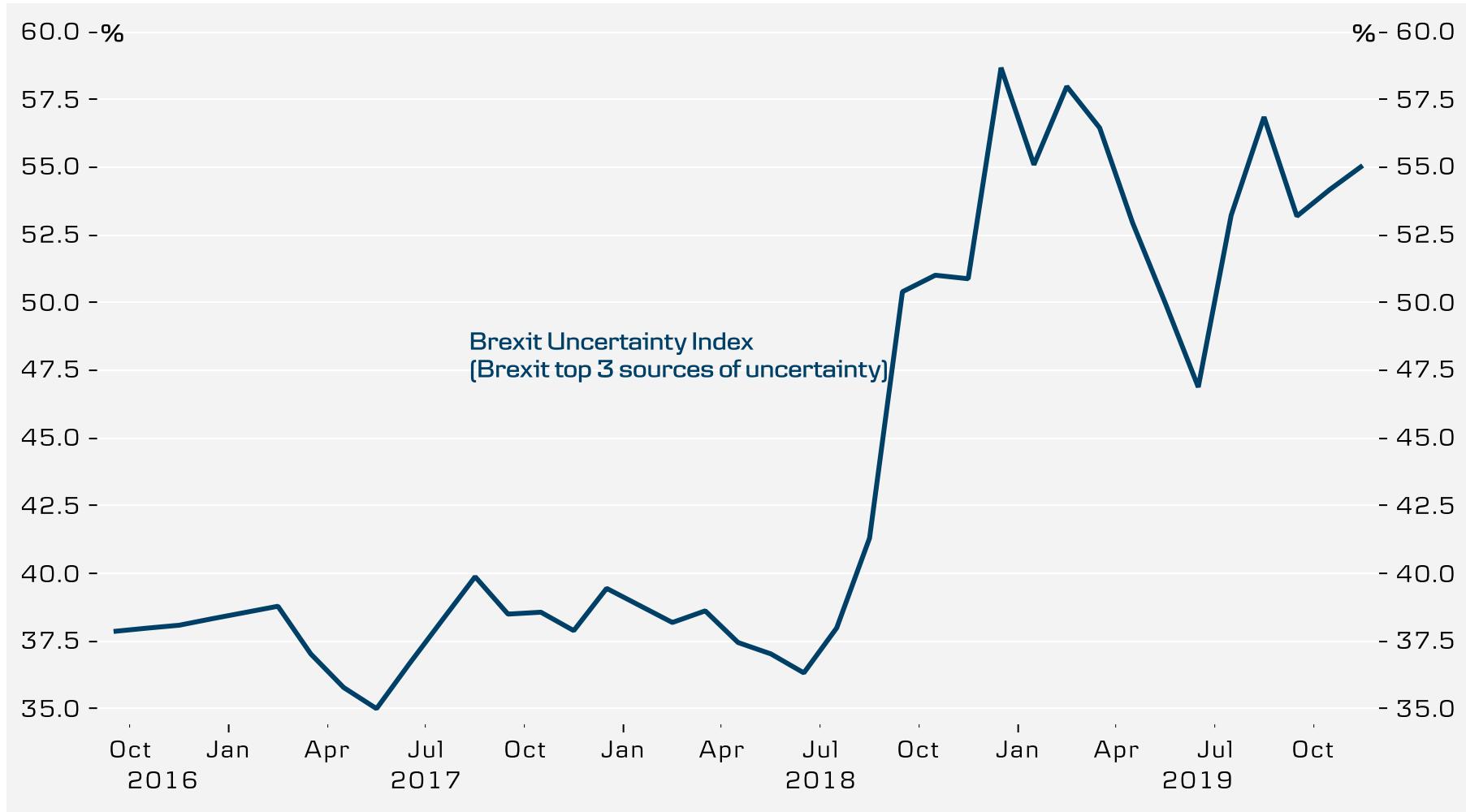
## *The election is an EU referendum in disguise*



# Scottish independence after Brexit?



## Brexit uncertainty remains high



## *Appendix: UK General Election system*

## Appendix: UK election system

- Each of the 650 constituencies elects one Member of Parliament by the so-called ‘first past the post’ system, where the candidate with most of the votes (not necessarily the majority of the votes) takes the seat (‘winner takes all’). This election system benefits the big parties and explains why the Conservative Party and the Labour Party have taken turns leading the government. This has been breaking up more recently with hung parliaments (i.e. no party with an absolute majority by itself) following the 2017 and 2010 elections.
- The ‘winner takes all’ system also means there is a higher degree of tactical voting, as there is a high risk of a wasted vote. If Party A gets 30%, Party B gets 30% and Party C gets 40%, then the candidate from Party C wins the seat. However, if Party B’s voters vote for Party A instead, Party A wins the mandate. This explains why the Scottish National Party (SNP) has many MPs, while its share of the national vote is small. It also explains why it is very difficult to translate national voting intentions into number of seats and why were caught by surprise both in 2015 and 2017.
- The magic number for a majority is 326 seats but in practice the number is a little lower, as historically Sinn Fein (the Irish Republican Party) MPs have not taken their seats. The number of mandates for Sinn Fein changes from election to election. The Speaker is also considered neutral.
- The Fixed Term Parliament Act of 2011 introduced fixed-term elections with an election every fifth year with two exceptions: (1) the House of Commons dissolves itself by a two-thirds majority, or (2) the government loses a no-confidence vote and no new government is formed within two weeks.
- A person is eligible to vote only if he/she is a registered voter, which usually explains why historically the turnout among young voters has been low.
- Polling stations are open from 08:00 CET to 23:00 CET. Exit polls are released when polling stations are closed. We usually know the election results early in the morning of the following day.

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Ad hoc.

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