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Market Info

UK General Election

Theresa May's failed gamble, Conservatives falling short of majority

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Britons elected a new parliament on June 8 in what will be the country's third nationwide vote in two years, after a general election in May 2015 and the Brexit referendum of June 2016 that put the UK on the road to leaving the European Union (EU).

At the UK General Election yesterday June 8, **the Conservative party won the majority of seats but lost its absolute majority. Theresa May finds herself particularly fragile and her line of a "hard Brexit" considerably weakened in the negotiations with Europe that are due to begin soon.**

The Ukip (United Kingdom Independence Party), a Eurosceptic party, won only 5% of the votes and won no MPs, despite having dominated the British political agenda over the last three years. It had gathered 13% of the votes in the previous legislative elections of 2015.

This result is highly unlikely to stop the Brexit since the Labour Party wants to respect the result of the June 2016 referendum. However, this electoral defeat for Mrs. May should disrupt the negotiating process and produce a different kind of Brexit from the one she was defending.

Political consequences

The political party who wins the majority of seats in the General Election will form the new Government. The leader of this party is traditionally appointed prime minister. If no party obtains an absolute majority, two or more parties can form a coalition. To continue to govern, the Conservatives can also form a so-called minority government. In this case, they would secure the occasional support of other parties to vote their projects in Parliament. But a minority government would prove very unstable.

Since the Conservatives lacked an absolute majority they must form a coalition government. The Liberal Democrats, their partners from 2010 to 2015, were badly scarred by that experience and say they have no wish to repeat it. A Conservative-Labour "grand coalition", similar to Germany's Christian Democrat-Social Democrat government, appears unthinkable. Outside of wartime, the UK does not go for such coalitions. The Labour party will also certainly try to form a coalition. **A period of political uncertainty thus opens in the UK while the negotiations with the EU must begin in a few weeks.**

Pre-election political environment

UK legislative elections seemed far more risky than expected. When Theresa May called early elections in April 2017, her party's advance in the polls was such that a large victory seemed certain. **But this legislative vote has fueled downward pressure on the pound sterling given the published polls over the past few weeks. In this campaign, the dynamics were clearly reversed against Theresa May, increasing the risk of her losing absolute majority.**

In the coming weeks

After the formation of the new government and probably the appointment of a new prime minister, **Brexit negotiations would start on June 19 with a report back to the European Council summit of June 22-23 by the EU chief negotiator Mr. Barnier.** This is the first important step of the two-year process that will see the UK leave the European Union the March 29, 2019.

Portfolio positioning

Our investment policy remains unchanged. It consists of a significant overweight to equities, justified by the improved outlook for the global economy; a very clear underweight to fixed income which should be penalized by the continued monetary normalization of central banks. We think a neutral position to UK assets is the best way to hedge against a high active risk that will continue, depending on the EU negotiations process.

Within the equity market, we overweight European and Emerging countries as a result of a significant improvement in activity and attractive valuations, and **we underweight US equities** which is suffering from tight valuations.

Within the fixed income market, a broad diversification is carried out through an underweight in government bonds and an overweight in corporate bonds, Emerging debt and convertible bonds. **The duration is very moderate,** facing the risk of a gradual rise of yields and a yield curve steepening.

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