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BREXIT FALLOUT: UK GfK CONFIDENCE FALLS, GERMAN SUPPORT FOR EU RISES

Berenberg Macro Flash

UK: SHARPEST PLUNGE IN CONSUMER CONFIDENCE IN 21 YEARS

Following the UK vote to leave the EU, consumer confidence in the UK has suffered its sharpest fall in 21 years. The GfK index plunged by 8 points to -9. 60% of respondents now expect the economic situation to worsen over the next twelve months. In the previous survey, only 46% had been pessimistic. Consumer confidence fell particularly sharply in the North of England (drop of 19 points to -15) and among young people (drop of 13 points to +6). Whereas those who had voted to leave the EU are less concerned (GfK index at -5 for this sub-group), confidence among “remainers” dived to -13 points. Therein lies a warning: if the economy indeed turns sour contrary to the promises of the Brexiters in the referendum campaign, confidence among disappointed “leavers” may eventually follow suit, bringing the overall GfK index down even further.

Consumer confidence is only loosely related to actual spending. We currently project stagnation rather than recession for the UK economy for the remainder of this year. But if concerns about commercial real estate spread to the residential market, possibly with expectations of house price declines to come, the risk of a genuine recession could loom very large.

The short-term business cycle is driven to a large extent by sentiment. Whether sentiment can stabilise soon will depend a lot on the political outlook: does it seem likely that the UK will in the end agree a half-amicable divorce with its major market, the EU, that preserves access to much of the Common Market – or could a hotly contested divorce with a drawn-out uncertainty about future market access cause a more protracted slump in UK investment? Seen from this angle, the fact that the candidates with the most confrontational attitude to the EU, Michael Gove and Liam Fox, have dropped out early and clearly from the Conservative leadership race could be mildly encouraging. However, that the Conservatives still want to wait nine weeks before they actually announce the future leader of the country prolongs the painful uncertainty unnecessarily.

From a UK economic perspective, the best that could happen to contain uncertainty might be a nice photo opportunity between a female UK prime minister (Theresa May with her somewhat pragmatic image in pole position) and Angela Merkel. If both smile and exude confidence that they will agree in the end despite very serious disagreements at the outset, concerns about the economic future of the UK could fade just a little. But as things stand, we may have to wait for quite a while for such an opportunity. Meetings between Cameron and many of his EU-27 counterparts at the NATO summit now won't have the same effect. And we believe that the EU-27 mean what they say: no negotiations before the UK has officially filed for divorce.

GERMANY: RISE IN SUPPORT FOR EU

Will the UK vote to leave the EU weaken or strengthen the cohesion of the EU-27? Will the result embolden those who clamour for their own EU or euro-referendum elsewhere – or will the uncertainty that has befallen the UK turn voters elsewhere away from the populist peddling impossible promises? In Germany, support for the EU has surged to a record high in the wake of the UK vote, with the share of Germans seeing mostly advantages from EU membership rising by 13 points to 52% and the share of those seeing disadvantages falling by 10 points to just 11% relative to a survey taken just before the Brexit vote. As in similar polls in Denmark and Finland a few days ago, the knee-jerk reaction to the UK uncertainty so far seems to



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be to strengthen rather than weaken the EU-27. In a similar vein, the Infratest-Dimap poll for German ARD TV also reveals some rebound in popularity for chancellor Merkel and her coalition government and a drop in the projected votes for the radical right and anti-immigrant AfD from 15% to 12%. Of course, it is very early days. It will take many months before we can really gauge the impact of the UK experience on the continent.

ITALY: RENZI AT RISK

The major concern in the Eurozone remains the political outlook for Italy where the renewed focus on the fragility of the banking system is the bigger issue than Brexit. Opinion polls indicate a further erosion of support for prime minister Matteo Renzi's centre-left and a rising risk that Renzi will lose the October referendum on constitutional reforms. Most polls project a small majority against the constitutional reform, some polls now put support for the radical left "Five Stars", which demands a euro referendum, ahead of Renzi's mainstream centre-left. This continues a trend we had commented on repeatedly in recent weeks. The earlier the EU and Italy can agree on a way to strengthen the Italian banks without damaging Renzi's political position even further, the better. Italy is the risk to watch in the Eurozone.

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