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DKM Commentary:

With the November recess in Parliament upcoming and a break in the negotiations, it's been a relatively quiet week on the Brexit front. However, developments in Stormont have captured the attention of the UK and Ireland, with Northern Ireland's public spending budget now being drafted in Westminster, prompting worries of direct rule should negotiations fail. This only makes debate on the border more complex, and places further pressure on Taoiseach Leo Varadkar who is now working with Theresa May to reach a solution, while also standing ground in the Brexit talks.

Brexit Secretary in the UK, David Davis, has admitted that the divorce bill will likely favour the EU financially, given where both parties are at this stage of the negotiations. In speaking to the House of Lords, Mr Davis explained that securing a good trade deal is more pertinent in the long run than the lump sum cost of leaving, and that he believes the UK is still in a good position to achieve this. As we hope to approach the second phase of negotiations, the EU has been showing support for Downing Street and speaking more positively on relations between them, as a means of securing open and productive communication

For the first time in a decade, the Bank of England has raised interest rates in an effort to control rising inflation. In response to the announcement a swift slump was seen in sterling against both the euro and the US dollar. It will be interesting to see if the new monetary policy will have any effect on budgetary planning by Chancellor Philip Hammond considering UK business are asking for access to cheap credit in an effort to remain viable in a Brexit environment .



Political Developments

United Kingdom

Westminster prepares for next round of negotiations

The Brexit negotiations will resume next week, on November 9th and 10th, and the UK Cabinet appears to be presenting a more united front than it had been [up to now](#). But this is not to say all Ministers are singing off the same hymn sheet, which makes negotiating an amiable agreement with the EU a constant challenge. Whether the parties will overcome the current impasses around the Irish border and the financial settlement remains a question. On Tuesday, David Davis told a House of Lords Committee that the EU was likely to come out on top in the Brexit negotiations, especially in relation to the financial settlement. This reflects a softening of Mr Davis's position on the issue and came a day after a [cross-party delegation](#) (including Nick Clegg and Ken Clarke) met Michel Barnier. The parties discussed the UK Government's Brexit strategy and the extent of its popular support. Some Conservative MPs argued the meeting reflected parallel talks, but this was dismissed by a Commission spokesperson.

Restricted Brexit impact reports causing dissonance in Parliament

Early this week, following a Freedom of Information request from Seema Malhotra, a Labour MP, the UK's Brexit Department refused to release its analysis of the effects of Brexit on key sectors of the [UK economy](#). At the same time the Department published the identities of the 58 sectors that had been analysed. Government officials stated that publishing the research would damage the UK's [negotiating position](#). As the week progressed, pressure mounted on the Prime Minister to release the analyses, with Labour said to be considering invoking centuries-old rules to force the PM's [hand](#). Over 120 cross party MPs have signed an open letter urging the research to be provided to Parliament.

New Brexit Minister's historic opinions deviate with May

While the Brexit negotiations are an ongoing challenge for Britain, politicians' vision for post-Brexit Britain is varied and opaque. Video has emerged of a speech made by a recently-appointed Minister at Department for Exiting the EU (DexEU), Martin Callanan, whilst an MEP in 2012, in which he proposes scrapping various EU Directives that protect [workers' rights](#). These views are in contrast to the Prime Minister's stated Brexit position on workers' rights, which she maintains will be protected post-Brexit.

Divorce bill will 'favour' EU financially

Brexit Secretary in Westminster, David Davis, has [conceded](#) that the financial 'divorce bill' will likely favour the EU, however 'the future relationship will favour both sides and will be important for both of us'. Speaking to a House of Lords Committee on Thursday, the secretary explained that even

though the bill is a make-or-break issue for some, he will not, as one business suggested to him, simply put £100 million towards the cause as it would not be fair on the taxpayer. However, he does accept that it may not be as favourable to the UK as hoped. On Wednesday, the National Audit Office in the UK [announced](#) that it will scrutinise the Brexit bill to ensure it represents value for taxpayers' money. Mr Davis also [told](#) the same Committee that 8,000 public employees will have been hired in preparation for Brexit by the end of 2017.

Ireland

Agreement still not reached Stormont

[Talks](#) between the Democratic Unionist Party (DUP) and Sinn Féin on reforming the power sharing assembly in Northern Ireland have captured the attention of British Prime Minister Theresa May and Taoiseach Leo Varadkar. While neither party would like to see direct rule imposed in Stormont, the British government has announced it will have to set the budget for Northern Ireland so that a bill can be considered and passed by Westminster following the November recess. While the deadlock is not new, having begun last January, the increased likelihood of a return to direct rule for the first time in ten years brings with it a new level of pressure on all involved. The Northern Ireland Secretary of State in Westminster, James Brokenshire, [suggesting](#) that there are only a small number of issues hampering a deal, and that the budget bill imposed by his Department was done so with 'utmost reluctance and only in the absence of any other option'. Mrs May and Mr Varadkar have held [phone calls](#) on the matter in an effort to identify ways of breaking the deadlock. The official spokesman of the Prime Minister said both leaders agreed on a 'shared endeavour to see the restoration of devolved government' in the North. The DUP is supporting Mrs May's government after the Conservatives fell short of seats in the summer election. Therefore, the Prime Minister must balance her relationship with the Northern Ireland party, while still remaining fair to all involved in her diplomatic handling of the situation. Similarly, given the Taoiseach's public commentary on the lack of acceptable progress seen in UK – EU negotiations, he must work with Mrs May in achieving a workable solution, without changing his dynamic with Westminster, and consequently damaging any bargaining power or influence he may have. Difficulties in Stormont will only make border negotiations more difficult as the absence of a unified voice could weaken their position.

European Union

Juncker defends May and Downing Street

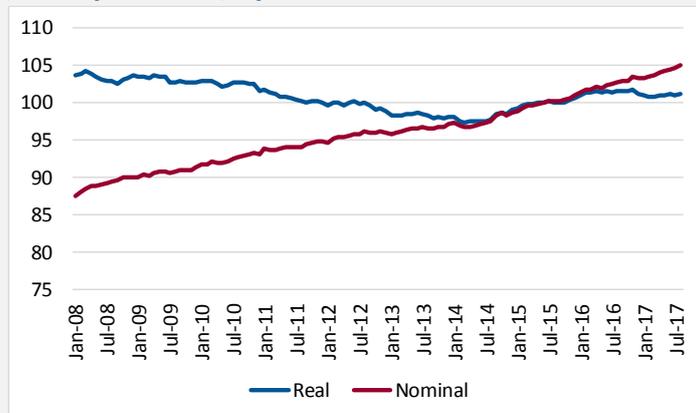
Following the EU Summit two weeks ago, the European Commission (EC) President, Jean-Claude Juncker has [come out publicly](#) to dispel rumours of a weak Theresa May, in an effort to secure relations with Downing Street. The EC President said in a private dinner held recently, that the UK Prime Minister had not 'begged for help' but rather was in 'good shape' and 'fighting'.

Interest Rates and Brexit

Bank of England raises interest rates for the first time in 10 years

On Thursday the Bank of England (BoE) [raised its interest rate](#) for the first time since 2007. The Bank announced an increase of 25 basis points, bringing the rate to 0.5 per cent, a level last seen in 2009. The highly anticipated announcement caused the pound to fall to a three and a half week low against the US dollar, and was on track for the biggest one day fall against the euro in 13 months (as of Thursday evening). There has been some [backlash to the decision](#) taken by the Monetary Policy Committee at a majority of 7 to 2 as it will adversely impact variable rate mortgage owners who have not seen a real wage increase over the last decade.

Real and Nominal Wage Growth Index in the UK January 2008 to July 2017

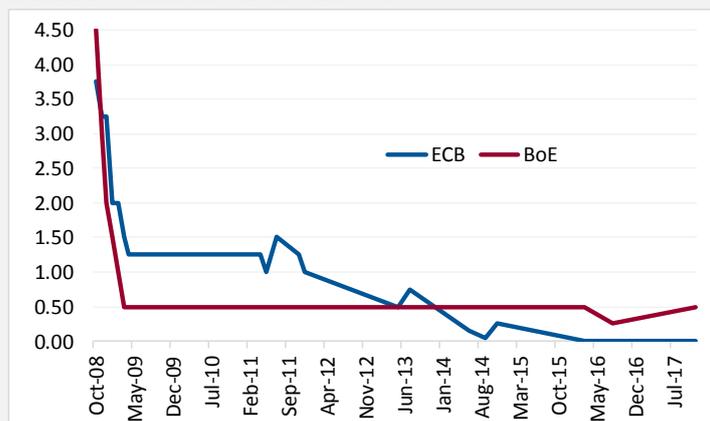


Source: Office for National Statistics

Base: 2015 = 100

BoE Governor, Mark Carney, explained that the Committee decided now was the right time to raise rates given the 'noticeable impact on the economic outlook' that Brexit has posed. He also suggested that the rise was a one-off, and markets should not react as if it was the beginning of a series of hikes

Main Refinancing Options Interest Rates October 2008 to November 2017



Source: ECB and BoE

As can be seen from above, both central banks dropped their interest rates quickly at the time of the financial crisis coming

into 2009, and while the BoE is bringing the rate back to 0.5 per cent, the ECB has not indicated thus far that it will do the same in the immediate future.

Why do central banks raise interest rates?

As explained in Issue 13 of this publication, the key goal of central banks is to ensure price stability. The Bank of England, along with the ECB and many others, aims for annual inflation (price increases) of 2 per cent. The ECB has engaged in quantitative easing in order to stimulate inflation which has been very low in Ireland, and Europe generally, over the past five years. On the other hand, since the Brexit referendum was held and sterling decreased significantly in value, the UK has witnessed strong inflationary growth, reaching a year-on-year inflation rate of 3.0 per cent in September. This puts pressure on the purchasing power of wages, as real wage growth is not increasing at the same pace as is seen in inflation. By increasing the interest rate, i.e. the price of borrowing money, the BoE is using a contractionary monetary policy in an effort to slow inflation to a more sustainable level.

Mr Carney [stated](#) that 'Brexit-related constraints on investment and labour supply appear to be reinforcing the marked slowdown that has been increasingly evident in recent years in the rate at which the economy can grow without generating inflationary pressures'. A low interest rate attempts to act as a stimulus for demand, as money is relatively cheap, therefore any increase in the interest rate is observed as a tightening of monetary policy. Although, one of the [key issues](#) restricting economic growth, and therefore real wage growth, is the lack of productivity growth, which has been aggravated by Brexit.

The ECB has [announced](#) that it will be restricting its Asset Purchase Programme from January 2018 until at least September 2018, from a monthly pace of €60 billion per month, to €30 billion per month. This is a cut to the current stimulus package, however in the case of the ECB, President Mario Draghi has [indicated](#) they will still work to boost inflation which is consistently below target, in contrast with the Bank of England.

What does this mean for Ireland?

The [slump in sterling](#) witnessed this week, in light of the announcement, will put more pressure on Irish exporters in the short term. In the longer term however, interest rate increases are usually expected to strengthen a currency as investors will be enticed by the higher rates of return. Therefore, the stronger sterling becomes over the next number of years, the more competitive Irish exports will remain in the UK market.

Relocations News

Irish efforts shifting to European Banking Agency bid

In an update on news reported in [Brexit Watch Issue 12](#), Ireland is [reportedly](#) moving lobbying efforts away from its bid to secure the European Medicines Agency post-Brexit, and is now focusing on securing the European Banking Agency. A decision is due from the EU General Affairs Council by the end of November, with eight countries including Ireland vying for the opportunity to host the agency (EBA) currently based in London. Two Ministers have been speaking to the Irish Times and suggest that Ireland's chances are slim given the 'lack of allies in the process'. The decisions regarding when the agencies will relocate to is purely political and will be voted on by EU member states.

Hard Brexit will push thousands of jobs out of London

The Bank of England is expecting job losses of up to 75,000 in Britain's financial services sector in the event of a "hard Brexit" in which the UK loses its [passporting rights](#). This would be a significant blow for the City of London and for economic output. The uncertainty surrounding the issue is a major concern, but it provides opportunity for Ireland to offset some of the losses faced by a hard Brexit, in the form of increased employment and industry activity here. Many banks have already relocated staff elsewhere in the EU, although some, such as HSBC, are [delaying their announcement](#) until the UK's future relationship with the EU becomes clearer.

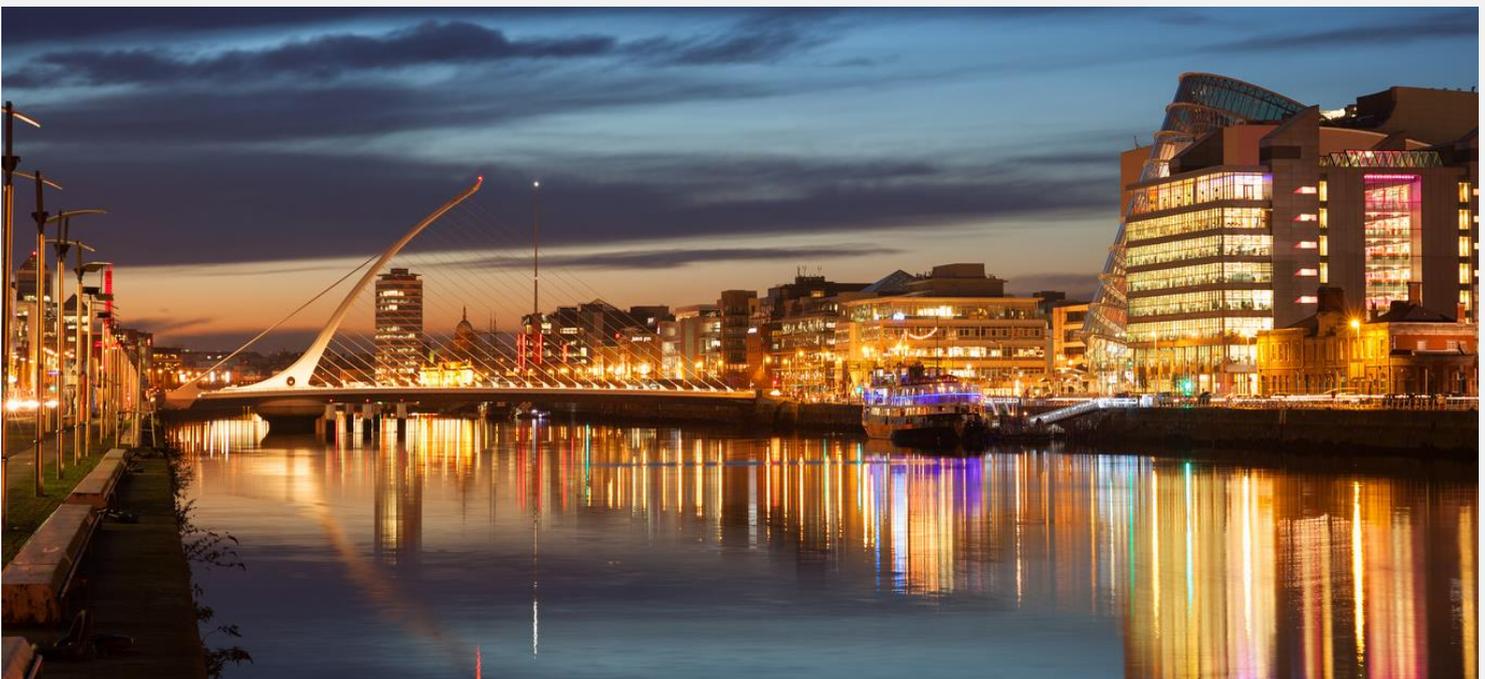
Business & Finance

Taoiseach meets Silicon Valley executives and secures jobs

Taoiseach Leo Varadkar has been in the US this week meeting Silicon Valley companies, in an effort to bring more jobs to Ireland at a time when employment is threatened by Brexit and a decline in trade. Mr Varadkar's networking trip is paying dividends as [Facebook](#) have announced up to 800 more jobs in Ireland in 2018, and business software firm [Twilio](#) will create 100 positions by the end of 2019. The shift to the US follows a recent spate of [announcements](#) regarding jobs relocating from London to Frankfurt, which have possibly pushed the government to look beyond the City for increased employment opportunities to bring to Ireland.

Sterling weakness remains a concern for exporters

The [latest figures](#) from the Bank of Ireland Economic Pulse index increased over the month of October. The index is a combination of the Consumer and Business Pulse and shows that both elements are increasing as we come into the final quarter, with 2 in 3 firms indicating ambition to expand over the next 1 to 3 years. The Consumer Pulse stood at 97.3 at the end of the month, up 2.0 on September and a year-on-year increase of 4.4. This is indicating that consumers are becoming more optimistic, however the Economic Pulse measured at 90.5, up on September's figure of 88.8, but down by 4.0 on last year. This is caused by the year-on-year decrease in the Business Pulse of 6.1. Group Chief Economist for the Bank, Dr Loretta O'Sullivan said that 'the weakness of the pound remains a key concern for firms exporting to the UK' and will have an impact on sentiment going forward.



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