ECONOMIC RESEARCH

The NewsLine

July 26, 2017

} MACROECONOMICS | FINANCIAL MARKETS | ECONOMIC POLICY | SECTORS

UNITED KINGDOM

Brexit puts the brakes on the economy

Katharina Utermöhl
Phone +49.69.24431-3790
katharina.utermoehl@allianz.com
Allianz SE
https://www.allianz.com/economic-research/en

Ana Boata
Phone +33.1.84.11-4873
ana.boata@eulerhermes.com
Euler Hermes
http://www.eulerhermes.com/economic-research

Allianz Research
https://twitter.com/AllianzResearch

The British economy put in another weak performance in the second quarter of 2017. In a gradual process the UK will have to bid farewell to the high economic growth rates registered in recent years. Average quarterly growth will more than halve in 2017 compared with last year. In the long run Brexit does not have to be a disaster for the UK economy, but we expect the exit from the EU to cause significant economic damage during the transition phase.

According to the flash estimate published today, the British economy grew 0.3% q-o-q in the three months to June after 0.2% q-o-q in the previous quarter. The service sector provided the only positive contribution to growth (+0.5 percentage points). No breakdown of components is available yet, but higher frequency data suggests that private consumption was the main – albeit weakening – engine of growth in the second quarter.

The negative impact of the Brexit vote on the British economy is becoming increasingly clear. The initially feared slump in economic activity in the immediate aftermath of the referendum did not materialize, but instead the UK will have to say goodbye to the high growth rates of recent years in a gradual process. Since the turn of the year 2016/17 the British economy has cooled markedly. Especially the elevated uncertainty surrounding the outcome of EU exit negotiations and the sharp acceleration in consumer prices – as a result of the marked depreciation in sterling – are weighing on economic activity. In the current year average quarterly growth will more than halve from 0.5% q-o-q to 0.2% q-o-q. Overall we expect UK GDP growth to slow to 1.4%

in 2017, down from 1.8% in the previous year. With growth in the eurozone approaching 2% this year, the UK economy will clearly fail to keep up.

In the medium to long term the economic impact of the Brexit vote will largely depend on the outcome of the negotiations with the EU, an immensely complex process that will take years to complete. A free trade agreement between the EU and the UK, with considerable sectoral add-ons – in particular for services – is still the most likely scenario for us. But the agreement will fall well short of the degree of integration that has been achieved within the European Single Market. Key pillars of Britain's economic success – such as the financial services industry – could lose some of their importance going forward. Brexit does not have to be an economic disaster in the long run, but the UK's economic model will have to adapt to new conditions – with access to an EU market with more than 450 million people at least partially restricted – which will cause economic costs at least during a transition phase.

ABOUT ALLIANZ

The Allianz Group is one of the world's leading insurers and asset managers with more than 86 million retail and corporate customers. Allianz customers benefit from a broad range of personal and corporate insurance services, ranging from property, life and health insurance to assistance services to credit insurance and global business insurance. Allianz is one of the world's largest investors, managing over 650 billion euros on behalf of its insurance customers while our asset managers Allianz Global Investors and PIMCO manage an additional 1.3 trillion euros of third-party assets. Thanks to our systematic integration of ecological and social criteria in our business processes and investment decisions, we hold a leading position in the Dow Jones Sustainability Index. In 2016, over 140,000 employees in more than 70 countries achieved total revenue of 122 billion euros and an operating profit of 11 billion euros for the group.

These assessments are, as always, subject to the disclaimer provided below.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.

Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events), (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the euro/US-dollar exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

NO DUTY TO UPDATE

The company assumes no obligation to update any information or forward-looking statement contained herein, save