

# MARKET COMMENTARY

UK election: Winds of change after the landslide Labour victory

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**July 5, 2024**

- Yesterday's parliamentary election resulted in a landslide Labour victory giving it a comfortable absolute majority of 411 (+210 seats) out of 650 seats while the faction of the governing Conservatives was cut to just 119 (-249 seats), the worst in its history.
- Amid a participation of only around 60%, close to a record low, the rise of the right-wing populist Reform UK party that got 14% of the votes and 4 seats in parliament contributed to the weak Tories result.
- The new government traditionally becomes operative quickly after the election. Following Mr Sunak's resignation, the new Prime Minister, Keir Starmer, will immediately be appointed by the King and is expected to lay out his government's program on July 17.
- While the Labour Party manifesto suggests an overall unchanged fiscal outlook, the comfortable majority might be tempted to embark on a loser fiscal path. Testing times will be the 2025 budget, presented in late September or early October.
- As the UK government change had already been anticipated, the financial market's reaction has been limited.

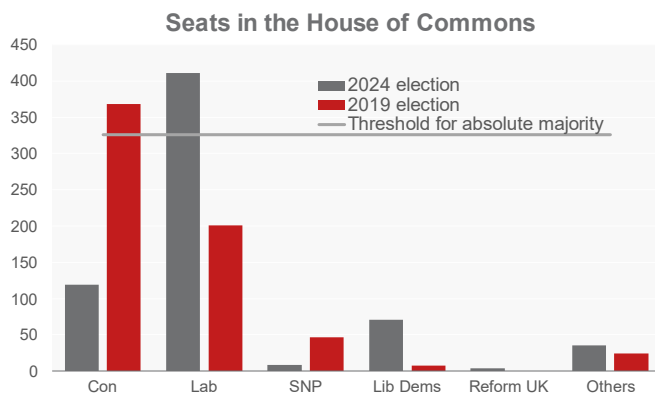
**Landslide Labour victory and historical defeat for Conservatives.** In yesterday's parliamentary election, the governing Conservatives suffered a historical defeat by losing almost two-thirds of the seats they got in the 2019 election (119 from 368 at the time of writing) whereas the Labour Party broadly doubled the number of its seats (to 411 from 201). This is the worst outcome in the Tory party's history ending the 14 years of Conservative governments. The rise of the right-wing populist Reform UK party of the formerly Chief Brexit supporter Nigel Farage that got 14% of the votes and 4 seats in parliament contributed to the weak Tories' result. A participation rate of only around 60%, close to a record low, likely also played a role. The Labour now has a comfortable buffer of 85 seats above in simple majority of 326 votes needed to pass legislation in the 650 seats comprising the House of Commons. Apart from that the EU-friendly Liberals gained (from 8 to 71) the Scottish National Party also lost strongly.

**The new government will soon take office.** The new government traditionally becomes operative quickly after the election. Outgoing Prime Minister Mr Sunak's resignation to the King will be done by today and the leader of the strongest party, Mr Starmer from Labour, will meet the King and be appointed as the new Prime Minister. While appointing ministers the parliament will resume its work as early as July 9 and the new government is expected to lay out its government's program on July 17.

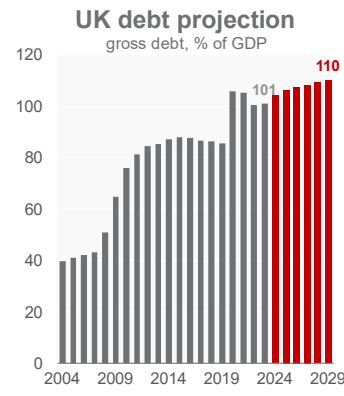
**Lots of challenges for the new government.** During the electoral campaigns, the key topics were the fall in living standards, poor public services, especially in the National Health Service, a high tax burden and immigration. Starmer has promised to

improve relations with the EU to resolve issues created by Brexit while re-joining the EU is not on the table. On foreign issues, however, not much difference to the former government is to be expected.

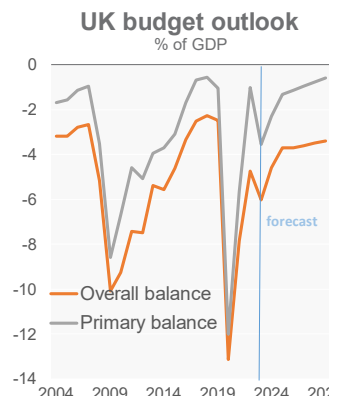
**Fiscal policy will be in the spotlight.** The pandemic significantly lifted the UK's debt ratio to around 100%. With the previous government's fiscal plans, the primary balance is set to improve but as the average rate of government debt likely lacks behind nominal GDP growth, the debt-to-GDP ratio is set to rise, reaching 110% by 2029 according to the IMF. The Labour's fiscal plans look not so different from the current ones suggesting that the projected debt path will not change significantly. Clearly, with a huge majority, Labour might be tempted to pursue a somewhat more expansionary policy than in its manifesto. There is also the question of whether changes will be made to the UK's self-imposed fiscal rules, which require public sector debt to fall as a share of GDP over five years.



Source: BBC newsticker as of 10:30 MEST, GenAM



Source: GenAM, IMF, Datastream



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**Autumn budget is testing time.** The autumn budget is likely to come in late September or early October and it is widely expected that additional revenues are needed to stabilize spending in real terms. During the electoral campaign Labour pushed back against hiking income, VAT or corporation tax. Hence the new government will probably have to consider pension tax reliefs, capital gains taxation and inheritance tax reliefs to prevent spending cuts. We are confident that the lesson from the 2022 Truss mini-budget crisis has been learnt and that the fiscal rule will be respected. Longer term, however, we could imagine a twisting of the fiscal rule to allow for higher investment spending.

**Markets unimpressed.** As the UK government change had already been anticipated by polls financial markets were not surprised and barely reacted to the election result. Longer term, however, the outlook for the debt ratio could affect the rating which is currently at AA- by Fitch and Moody's and AA by S&P.