

# The Impact of Brexit on Financial Competitiveness



I must admit that the UK's vote on 23 June 2016 to leave the EU came as a bit of a surprise, and judging by the ensuing financial market turmoil, much of the world felt the same way. The effects in the global financial markets were felt hard and fast—the day after Britain voted leave, \$2.1 trillion in market capital was lost on 48 global stock markets.

The repercussions of Brexit raise questions regarding its impact on other economies, including those in the Middle East. In a recent global survey conducted by the CFA Institute, 71% of CFA professionals in the U.A.E. responded that Brexit will not affect Dubai's competitiveness as a global financial centre. I am a CFA professional, and part of that 71%, so let's look at the reasons why.

Competitiveness is a relative term and due to the interconnectivity of the global markets, I do not see any reason why Dubai will feel the effects more strongly than other markets. Correlations between global markets have been increasing over time due to rising free trade, greater integration of capital markets and increased capital mobility through active institutional investors. Additionally, these correlations increase during periods of increased volatility. In a nutshell, everyone is feeling the Brexit effect.

The advantages of Dubai that bolster its competitiveness remain unchanged—including efficient financial regulation, promotion of free enterprise, legal and accounting support services and a time zone conveniently placed between the working hours of Asia and Europe.

To take a closer look at how the finance industry in the U.A.E. will be affected on an absolute level (rather than a relative one) let's examine the areas of international trade, regional liquidity and asset allocation.

International trade in financial services has expanded significantly over the last 20 years as financial markets have become increasingly open and globalised.

According to the latest statistics published by the World Trade Organization, financial services are the second-most dynamic global services sector after computer and information services.

**Brexit had a strong and direct impact on global oil prices, which dropped the day after the referendum by 6% to reach \$48 per barrel, a natural reaction to the anticipated weak global economic growth.**

In 2014, world exports in financial services stood at \$349 billion.

Britain is one of the largest economies in the world, importing billions of pounds worth of goods and services from other countries. It is likely that the UK will focus on improving its trade and investment partnerships with markets outside Europe. An EU exit will therefore enable the UK to broker bilateral trade agreements with emerging markets, which could have a positive impact on the U.A.E.'s financial services sector in the long-term.





In terms of regional liquidity, U.A.E.-based companies obviously feel liquidity constraints when the price of oil drops. Although much has been achieved in the way of diversification efforts, the U.A.E. still relies heavily on oil exports. Oil revenues currently contribute 30% to the U.A.E.'s GDP, a significant drop from 90% in the 1970s, but still a reasonable percentage. Brexit had a strong and direct impact on global oil prices, which dropped the day after the referendum by 6% to reach \$48 per barrel, a natural reaction to the anticipated weak global economic growth. Reduced revenues from Gulf-based oil exporters will likely lead to mounting financial pressure. However, there are a number of fiscal policy levers that can be pulled to counter reduced oil revenue, and many of these (such as taxation and subsidy reduction) have either already been implemented or are in process.

Along with oil, the British pound took a significant hit, dropping to its lowest value in more than 30 years on 25 June. It keeps testing these lows and currently stands at around GBP/USD \$1.30. Gulf Sovereign Wealth Funds and asset managers with

holdings in the UK will obviously see a reduction in portfolio value. Fortunately for Sovereign Wealth Funds, they have the luxury of a long-term strategy, making it a perfect time to be opportunistic, especially those with cash-rich balance sheets who want to acquire real estate at relatively low valuations. As one example, the Investment Corporation of Dubai had over 18% of its \$196 billion portfolio allocated to cash at the end of 2015, which puts it in a perfect position to be opportunistic with investments.

From an economic standpoint, I am confident that Brexit will not impact Dubai's financial industry. From a philosophical standpoint however, I am concerned about what the Brexit vote represents. There seems to be a populist belief sweeping the developed world that yesterday was better than today; this wave of anti-globalization, anti-immigration, anti-trade and protectionism has Brexit as its most recent example. But Europe is a market of 500 million people—the world's third largest population after China and India—why would you not want to be a part of it? **■**

**The repercussions of the Brexit vote are unlikely to have a significant impact on Dubai.**