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making business sense

Prepare the fancy dress for our Parity Party if sterling falls below the euro..

My reading of the economy post-PBR is that the UK economy is now walking only 5 yards away from the edge of the cliff. An unexpected gust could blow us over.

The gilts markets gave an unambiguous thumbs down to the PBR with an immediate 30 basis point hike in bond yields. But the real risk to the UK economy probably comes across the exchanges. Familiar to anyone who studied or worked as an economist in the 1960s and 1970s, market confidence in the government's economic strategy is critical.

It appears that the markets are betting on David Cameron and hoping that he will slash excessive public spending. Labour's PBR, which added £6 billion to public spending and continued to assume that an implausible above trend economic growth rate post 2010 would bail them out, did not go down well. The markets are giving the UK some slack and giving Brown and Darling the credit of assuming that either they are not telling the truth and will also cut public spending after the election or that they will be voted out. It is a sad state when the Chancellor's economic strategy depends on convincing the financial markets that he is a liar!

What this means that if the opinion polls between now and March 25 or May 6 show the Tory lead dropping well into the single figure zone, they will have kittens and probably start a sterling sell off. Meanwhile the rating agencies, who generally run behind the real world, are looking for an excuse to downgrade the UK government from its AAA rating, following countries like Greece.

There are far too many variables and far too much uncertainty for us to have a very firm view about what will happen. But opinion polls are volatile (the techies believe that this reflects some of the weighting used to 'improve' the crude results) and it would be unusual for there not to be at least one wild poll showing Labour doing well, even if the underlying views are different.

Meanwhile, the euro has also got a potential downside, because to be frank it has not worked. When it was set up, it was assumed that economic performance between Germany and the rest of Europe would converge. This has not happened – quite the reverse - and when Germany is forced to bail out much of the rest of Europe it is hard to see the euro remaining as strong.

Whether the markets react to the UK's fragile public finances before they react to the divergence of performance in the euro zone will determine whether sterling drops below parity with the euro.

If I had to bet, I would bet on the side of parity being broken. If it happens, then cebr will schedule a parity party. Reflecting the underlying economic reality, it will be BYOB (for those who were not students once this means Bring Your Own Booze). The cautious amongst us should probably prepare by buying their skiing cash in advance while the opinion polls still show a strong Tory lead.

Douglas McWilliams *chief executive*
centre for economics and business research ltd
dmcwilliams@cebr.com 07525287112

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