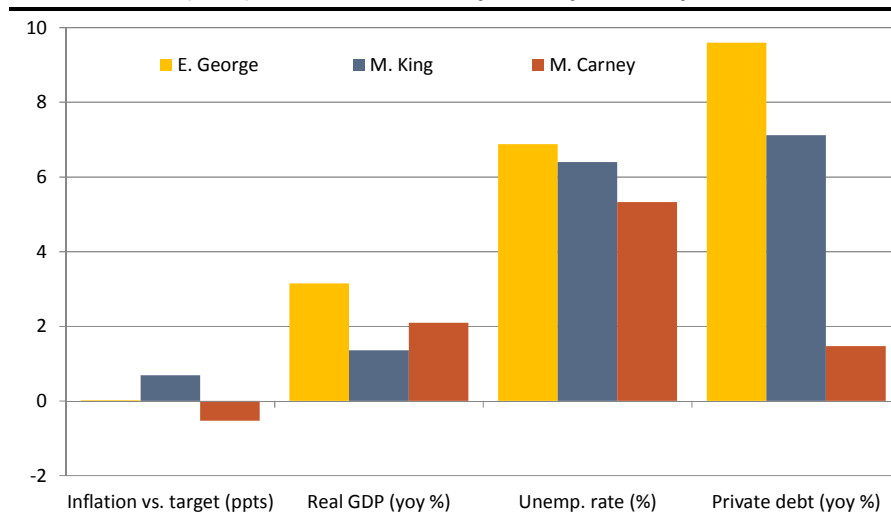


5 September 2018

Carney staying on at the BoE: implications

How does Carney compare? (data show averages during different governors' terms)



Quarterly data. Source: Office of National Statistics. Terms of BoE governors used for calculations: Eddie George – Q3 1993 to Q2 2003; Mervyn King – Q3 2003 to Q2 2013; Mark Carney – Q3 2013 to current. Data on inflation is adjusted for the change in the BoE's target in late 2003 to annual consumer price inflation of 2% from annual retail price inflation (excluding mortgage payments) of 2.5%.

- Will he or won't he?** Bank of England (BoE) governor Mark Carney signalled yesterday that he would be willing to extend his term beyond the currently planned exit in June 2019 to promote a “smooth Brexit”. Carney, speaking at the Treasury Select Committee, said that Chancellor Philip Hammond would make an announcement in due course. Amid the uncertainty and risks from Brexit and domestic politics, continuity in the top post provides a degree of predictability in the way the BoE would likely act in a crisis. The mere fact that markets are confident Carney would step-up to the plate with the BoE's firepower during a crisis significantly reduces the risk that a normal market panic that could follow a shock would not turn into a major catastrophe.
- Carney's record:** Three governors have led the BoE since it became independent in 1997: Eddie George (until June 2003), Mervyn King (July 2003 to July 2013) and Mark Carney (July 2013 to present). Of course, every governor faces different challenges. On the whole, however, Carney has done a decent job – see chart. Partly due to his shorter term so far, unlike King he has not presided over a recession. While Carney comes second to George in terms of average real GDP growth and hitting the inflation target, he is top for unemployment and debt growth.
- Why the head of an institution matters?** In normal times, when policy makers are simply deciding how to set policy amid banal economic trends and risks, the head of the central bank may not matter much. After all, a nine-member committee decides policy at the BoE. But in a crisis, a leader matters a lot. European Central Bank President Mario Draghi single-handedly stopped the rot of the euro crisis in 2012. And Carney, on the morning the Brexit vote was announced – as the ranks of government were lining up against each other to fight it out over Brexit and sterling was sliding – calmed the panic by promising to provide markets with all the liquidity needed to function. In the days that followed, he calmed markets further with the promise of a stimulus to prop up the economy.
- How would the BoE respond in a hard Brexit?** A hard Brexit in March 2019 would deal a major confidence shock to the UK and the EU (20% risk). The UK would be at risk of falling into stagnation or even a recession – with or without a transitional period to cushion the blow. In a similar fashion to after the Brexit vote, we would expect an early announcement of extra liquidity by the BoE to facilitate market clearing, and if the economy started to soften, later on a package of rate cuts and quantitative easing to stimulate demand (similar to the August 2016 package).
- Monetary policy outlook:** A hard Brexit is not our base case. As long as the UK avoids such a fate we look for the BoE to hike rates twice per year in 2019 and 2020 as lower uncertainty and improving real wage growth drive stronger rises in domestic demand (bank rate at 1.75% by Q4 2020). We look for the next hike in May 2019. This is a fairly boring outlook after a rocky couple of years for the UK. In the end, chances are that it will not matter much if Carney stays. But given the potential risks ahead, markets might sleep better if he does (just in case).

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Contacts



BERENBERG

PARTNERSHIP SINCE 1590

JOH. BERENBERG, GOSSLER & CO. KG

Internet www.berenberg.com

E-mail: firstname.lastname@berenberg.com

EQUITY RESEARCH

AEROSPACE & DEFENCE

Ryan Booker +44 20 3753 3074
Andrew Gollan +44 20 3207 7891
Ross Law +44 20 3465 2692

AUTOMOTIVES

Cristian Dirpes +44 20 3465 2721
Alexander Haisl +44 20 3465 2749
Viktoria Oushatova +44 20 3207 7890
Fei Teng +44 20 3753 3049

BANKS

Adam Barras +44 20 3207 7923
Stephanie Carter +44 20 3207 3106
Michael Christodoulou +44 20 3207 7920
Andrew Lowe +44 20 3465 2743
Alex Medhurst +44 20 3753 3047
Eoin Mullany +44 20 3207 7854
Peter Richardson +44 20 3465 2681

BEVERAGES

Javier Gonzalez Lastra +44 20 3465 2719
Matt Reid +44 20 3753 3075

BUSINESS SERVICES, LEISURE & TRANSPORT

Zaim Beekawa +44 20 3207 7855
Tom Burlton +44 20 3207 7852
Roberta Ciaccia +44 20 3207 7805
Najet El Kassir +44 20 3207 7836
William Fitzalan Howard +44 20 3465 2640
Stuart Gordon +44 20 3207 7858
Annabel Hay-Jahans +44 20 3465 2720
Joel Spungin +44 20 3207 7867
Adrian Yanoshik +44 20 3753 3073

CAPITAL GOODS

Nicholas Housden +44 20 3753 3050
Sebastian Kuene +44 20 3207 7856
Philippe Lorrain +44 20 3207 7823
Rizk Maldi +44 20 3207 7806
Jaroslaw Pominkiewicz +44 20 3753 3035
Simon Toennesen +44 20 3207 7819
Ethan Zhang +44 20 3465 2634

EQUITY SALES

SPECIALIST SALES

AEROSPACE & DEFENCE & CAPITAL GOODS

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AUTOS & TECHNOLOGY

Edward Wales +44 20 3207 7815

BANKS, DIVERSIFIED FINANCIALS & INSURANCE

Calum Morris +44 20 3753 3040

BUSINESS SERVICES, LEISURE & TRANSPORT

Rebecca Langley +44 20 3207 7930

CONSUMER DISCRETIONARY

Victoria Maigrot +44 20 3753 3010

CONSUMER STAPLES

Ramnikue Sroa +44 20 3753 3064

MEDIA & TELECOMS

Jonathan Smith +44 20 3207 7842

HEALTHCARE

David Hogg +44 20 3465 2628

THEMATICS

Chris Armstrong +44 20 3207 7809

SALES

BENELUX

Miel Bakker +44 20 3207 7808
Bram van Hijfte +44 20 3753 3000

FRANCE

Alexandre Chevassus +33 1 5844 9512

SALES TRADING

LONDON

Charles Beddow +44 20 3465 2691
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Joseph Chappell +44 20 3207 7885
Stewart Cook +44 20 3465 2752
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Tom Floyd +44 20 3753 3136
Tristan Hedley +44 20 3753 3006
Peter King +44 20 3753 3139
Simon Messman +44 20 3465 2754
A.J. Pulley +44 20 3465 2756
Michael Schumacher +44 20 3753 3006
Paul Somers +44 20 3465 2753

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Sebastian Bray +44 20 3753 3011
Anthony Manning +44 20 3753 3092
Rikin Patel +44 20 3753 3080

DIVERSIFIED FINANCIALS

Chris Turner +44 20 3753 3019

FOOD MANUFACTURING AND H&PC

Rosie Edwards +44 20 3207 7880
Fintan Ryan +44 20 3465 2748
James Targett +44 20 3207 7873

FOOD RETAIL

Dusan Milosavljevic +44 20 3753 3123

GENERAL MID CAP - DACH

Saravana Bala +44 20 3753 3043
Martin Comtesse +44 20 3207 7878
Charlotte Friedrichs +44 20 3753 3077
Gustav Fröberg +44 20 3465 2655
James Letten +44 20 3753 3176
Alexander O'Donoghue +44 20 3207 7804
Gerhard Orgonas +44 20 3465 2635
Henrik Paganetty +44 20 3453 3140
Benjamin Pfannes-Varrow +44 20 3465 2620

GENERAL MID CAP - EU core

Beatrice Allen +44 20 3465 2662
Christoph Greulich +44 20 3753 3119
Andreas Markou +44 20 3753 3022
Anna Patrice +44 20 3207 7863
Trion Reid +44 20 3753 3113

GENERAL MID CAP - UK

Joseph Barron +44 20 3207 7828
Calum Battersby +44 20 3753 3118
Robert Chantry +44 20 3207 7861
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Ned Hammond +44 20 3753 3017
Omar Ismail +44 20 3753 3102
Anthony Plom +44 20 3207 7908
Edward James +44 20 3207 7811
Lush Mahendrarajah +44 20 3207 7896
Benjamin May +44 20 3465 2667

FRANCE (cont'd)

Dalila Farigoule +33 1 5844 9510
Kevin Nor +33 1 5844 9505
Guillaume Viret +33 1 5844 9507

SCANDINAVIA

Mikko Vanhala +44 20 3207 7818
Marco Weiss +49 40 350 60 719

UK

James Burt +44 20 3207 7807
Fabian De Smet +44 20 3207 7810
Marta De-Sousa Fialho +44 20 3753 3098
Jules Emmet +44 20 3753 3260
Katie Ferry +44 20 3753 3041
Robert Floyd +44 20 3753 3018
David Franklin +44 20 3465 2747
Karl Hancock +44 20 3207 7803
Sean Heath +44 20 3465 2742
Stuart Holt +44 20 3465 2646
James Hunt +44 20 3753 3007
James McRae +44 20 3753 3036
David Mortlock +44 20 3207 7850
Eleni Papoula +44 20 3465 2741
Bhavin Patel +44 20 3207 7926
Kushal Patel +44 20 3753 3038
Richard Payman +44 20 3207 7825

PARIS

Vincent Klein +33 1 58 44 95 09
Antonio Scutto +33 1 58 44 95 03

GENERAL MID CAP - UK (cont'd)

Eoghan Reid +44 20 3753 3055
Owen Shirley +44 20 3465 2731
Donald Tait +44 20 3753 3031
Sean Thapar +44 20 3465 2657

GENERAL RETAIL

Thomas Davies +44 20 3753 3104
Michelle Wilson +44 20 3465 2663

HEALTHCARE

Scott Bardo +44 20 3207 7869
Alistair Campbell +44 20 3207 7876
Klara Fernandes +44 20 3465 2718
Tom Jones +44 20 3207 7877
Samantha Osborne +44 20 3207 7882
Michael Ruzic-Gauthier +44 20 3753 3128
Laura Sutcliffe +44 20 3465 2669
Charles Weston +44 20 3465 2746

INSURANCE

Charles Bendit +44 20 3465 2729
Trevor Moss +44 20 3207 7893
Emanuele Musio +44 20 3207 7916
Iain Pearce +44 20 3465 2665
Philip Ross +44 20 3465 2726

LUXURY GOODS

Mariana Horn +44 20 3753 3044
Lauren Molyneux +44 20 3207 7892
Zuzanna Pusz +44 20 3207 7812

MEDIA

Robert Berg +44 20 3465 2680
Keisi Hyas +44 20 3207 7817
Laura Janssens +44 20 3465 2639
Alistair Reid +44 20 3207 7841
Sarah Simon +44 20 3207 7830

METALS & MINING

Charlie Clark +44 20 3207 3133
Richard Hatch +44 20 3753 3070
Laurent Kimman +44 20 3465 2675
Michael Stoner +44 20 3465 2643

UK (cont'd)

Christopher Pyle +44 20 3753 3076
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Joanna Sanders +44 20 3207 7925
Mark Sheridan +44 20 3207 7802
George Smbert +44 20 3207 7911
Alexander Wace +44 20 3465 2670
Paul Walker +44 20 3465 2632

GERMANY

Michael Brauburger +49 69 91 30 90 741
Nina Buechs +49 69 91 30 90 735
André Grosskurth +49 69 91 30 90 734
Joerg Wenzel +49 69 91 30 90 743

SWITZERLAND, AUSTRIA & ITALY

Duncan Downes +41 22 317 1062
Andrea Ferrari +41 44 283 2020
Gianni Lavigna +41 44 283 2038
Jamie Nettleton +41 44 283 2026
Yeannie Rath +41 44 283 2029
Mirco Tieppo +41 44 293 2024

COO Office

Greg Swallow +44 20 3207 7833
Fenella Neill +44 20 3207 7868

EQUITY TRADING

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Philipp Wieschmann +49 40 350 60 346
Christoffer Winter +49 40 350 60 559

LONDON

Christopher Brown +44 20 3753 3085
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Richard Kenny +44 20 3753 3083
Chris McKeand +44 20 3207 7938
Ben Tappin +44 20 3753 3382

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Henry Tarr +44 20 3207 7827
John Gleeson +44 20 3465 2716
Ilkin Karimli +44 20 3465 2684

REAL ESTATE

Kai Klose +44 20 3207 7888

TECHNOLOGY

Josep Bori +44 20 3753 3058
Georgios Kertsos +44 20 3465 2715
Tej Shankiya +44 20 3753 3099
Tammy Qiu +44 20 3465 2673

TELECOMMUNICATIONS

David Burns +44 20 3753 3059
Nicolas Didio +44 20 3753 3091
Usman Ghazi +44 20 3207 7824
Laura Janssens +44 20 3465 2639
Carl Murdoch-Smith +44 20 3207 7918

THEMATIC RESEARCH

Nick Anderson +44 20 3207 7838
Oyvind Bjerke +44 20 3753 3082
Steven Bowen +44 20 3753 3057
Asad Farid +44 20 3207 7932
Robert Lamb +44 20 3465 2623
Paul Marsch +44 20 3207 7857
Salha Shariff +44 20 3753 3097

TOBACCO

Jonathan Leinster +44 20 3465 2645

UTILITIES

Oliver Brown +44 20 3207 7922
Andrew Fisher +44 20 3207 7937
Lawson Steele +44 20 3207 7887

ECONOMICS

Florian Hense +44 20 3207 7859
Carsten Hesse +44 20 3753 3001
Kallum Pickering +44 20 3465 2672
Holger Schmieding +44 20 3207 7889

CRM

Laura Cooper +44 20 3753 3065
Jessica Jarmyn +44 20 3465 2696
Madeleine Lockwood +44 20 3753 3110
Vikram Nayyar +44 20 3465 2737
Rita Pilar +44 20 3753 3066

CORPORATE ACCESS

Lindsay Arnold +44 20 3207 7821
Maz Gentile +44 20 3465 2668
Robyn Gowers +44 20 3753 3109
Dipti Jethwani +44 20 3207 7936
Ross Mackay +44 20 3207 7866
Stella Siggins +44 20 3465 2630
Lucy Stevens +44 20 3753 3068
Abbie Stewart +44 20 3753 3054

EVENTS

Charlotte David +44 20 3207 7832
Suzy Khan +44 20 3207 7915
Natalie Meech +44 20 3207 7831
Eleanor Metcalfe +44 20 3207 7834
Rebecca Mikowski +44 20 3207 7822
Sarah Weyman +44 20 3207 7801

LONDON (cont'd)

Ross Tobias +44 20 3753 3137
Robert Towers +44 20 3753 3262

ELECTRONIC TRADING

Jonas Doehler +44 40 350 60 391
Matthias Führer +49 40 350 60 597
Sven Kramer +49 40 350 60 347
Matthias Schuster +44 40 350 60 463



BERENBERG CAPITAL MARKETS LLC

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Internet www.berenberg-us.com

E-mail: firstname.lastname@berenberg-us.com

EQUITY RESEARCH

GENERAL MID CAP - US

Samuel England +1 646 949 9035

HEALTHCARE - MED. TECH/SERVICES

Ravi Misra +1 646 949 9028

HEALTHCARE - SPECIALTY PHARMACEUTICALS

Patrick R. Trucchio +1 646 949 9027

LEISURE

Brennan Matthews +1 646 949 9024

INDUSTRIAL MATERIALS

Paretoosh Misra +1 646 949 9031

SHIPPING & TRANSPORTATION

Donald McLee +1 646 949 9026

SOFTWARE & IT SERVICES

Alexander Frankiewicz +1 646 949 9029

Gal Munda +1 646 949 9021

EQUITY SALES

SALES

Albert Aguiar +1 646 949 9218

Enrico DeMatt +1 646 949 9230

Kelleigh Faldi +1 617 292 8288

Ted Franchetti +1 646 949 9231

Shawna Giust +1 646 949 7216

Rich Harb +1 617 292 8228

Zubin Hubner +1 646 949 9202

Michael Kaye +1 646 949 9216

Jessica London +1 646 949 9203

Anthony Masucci +1 646 949 9217

Ryan McDonnell +1 646 949 9214

Emily Mouret +1 415 802 2525

Peter Nichols +1 646 949 9201

Kieran O'Sullivan +1 617 292 8292

Rodrigo Ortigao +1 646 949 9205

CORPORATE ACCESS

Adriane Klein +1 617 292 8202

Olivia Lee +1 646 949 9207

Robert Meyers +1 646 949 9215

Panthea O'Connell +1 646 949 9208

CRM

LaJada Gonzales +1 646 949 9213

Monika Kwok +1 646 949 9212

Stephanie Rieben +1 646 949 9240

EVENTS

Laura Hawes +1 646 949 9209

ECONOMICS

Mickey Levy +1 646 949 9099

Roiana Reid +1 646 949 9098

SALES TRADING

Ronald Cestra +1 646 949 9104

Mark Corcoran +1 646 949 9105

Michael Haughey +1 646 949 9106

Christopher Kanian +1 646 949 9103

Lars Schwartau +1 646 949 9101

Bob Spillane +1 646 949 9102