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DKM Commentary:

A number of political developments over the past fortnight have further cemented the current deadlock in Brexit negotiations, with attempts on Theresa May's side to catalyse progress seeming to fall on deaf ears in the EU. While Michel Barnier acknowledged the aims of Prime Minister May's Florence speech two weeks ago, further clarification is being demanded of the UK government. In a knock to British negotiators, the European Parliament approved a resolution criticising the lack of progress during phase one of negotiations. EU leaders have confirmed that sufficient progress has not been made to warrant moving to the second phase which would deal with the newly proposed transition period.

Back in the UK, party conferences have come and gone, with varying reactions and conclusions. Labour speeches were met by cheers, and Mr Corbyn received applause at nearly every mention of his name. In contrast the Conservatives received a more subdued reception, as could be expected for a generally older membership, with Theresa May receiving more sympathy than praise in the media. Foreign Secretary Johnson continues to take headlines, and rumours of internal tension persist.

At home, politicians and businesses are gearing up for Budget 2018, with calls for 'Brexit-proof' measures, but there is little assurance of where the necessary funding will come from. Reports of tax revenue missing quarterly targets do not help matters. Ireland continues its bids for London-based entities, with a vote on two major EU bodies taking place in under a month, however there has been little news on this front otherwise.



Political Developments

United Kingdom

Labour ready for new role in government

The rapturous applause and cheering which greeted Labour Leader Jeremy Corbyn arguably injected further energy into the party base at their annual conference in Brighton last week. Mr Corbyn aimed to position himself as the next Prime Minister and sought to win over those who are not yet convinced by a Labour agenda. The opposition party leader [told supporters](#) that their recent election campaign success has brought them to 'the threshold of power'.

Theresa May struggles to reaffirm message

In contrast, Prime Minister May's keynote address at the Conservative conference yesterday was marred by numerous interruptions, including a protester and a persistent cough. What was hoped to be an energising reestablishment of Conservative momentum, was rather disjointed and underwhelming in the eyes of a number of [commentators](#). Sky's Adam Boulton first reacted with what will surely be a disappointing line for the Conservatives; 'a speech that will be remembered for a number of interruptions' – very much in contrast with hopes that the address would revive Mrs May's Premiership. The speech was used to reaffirm the government's commitments to improve social housing and education, and achieving the best Brexit deal for both the UK and EU.

Boris Johnson shows efforts to follow 'unity' line

British Foreign Secretary, Boris Johnson, again took the spotlight throughout the course of the Conservative Party conference in Manchester, with questions haunting Conservative MPs on the topics of his loyalty, and the Prime Minister's longevity. In his annual conference address on Tuesday, Mr Johnson [drew a picture](#) of solidarity for attendees, suggesting that the 'whole cabinet is united' behind Mrs May's Brexit Strategy. It is speculated however, that internal divisions have weakened the UK government's negotiating position in the eyes of EU counterparts, with the European Parliament Brexit coordinator, Guy Verhofstadt [telling](#) MEPs; 'I want to express a big worry of mine. And that is the lack of clarity – or I can even say disunity – at the other side of the negotiation table.' The Foreign Secretary seemed to toe the party line with more enthusiasm in his most recent speech, suggesting concerns may have been taken onboard.

Ireland

Taoiseach says Bombardier is a 'lesson' for UK

At the EU Summit last week, Taoiseach Varadkar [warned](#) of a trade war between the US and UK as a result of recent developments with Canadian company, and major employer in Northern Ireland, Bombardier. Weighing in on the US Department of Commerce decision to impose a 220% tariff on the Canadian aerospace company, Mr Varadkar suggested 'It could well turn out to be a lesson for the UK. There's been a lot

of talk of a new trade deal between the UK and the US and how great that would be for the UK but we are now talking about the possibility of a trade war.'

Brexit opportunity used to back up income tax reform

With less than a week to go until Budget day, speculation is mounting on how successful the government will be in delivering policy wins for its voters, particularly in light of fiscal space restrictions, and calls for a Brexit-proof budget. Given the comments made by the government on the topic of the budget, it has been [assumed](#) that a proportion of fiscal space will be allocated to income tax policy change. The Taoiseach has inferred that the impact of Brexit influenced this decision, at a recent speech to the Washington Ireland Program. Suggesting that Ireland's income tax levels are a substantial deterrent to workers post-Brexit, Mr Varadkar recounted: 'we hear it back all the time, the very high personal income tax burden is one of the things that's holding us back as a nation when we're fighting to bring jobs here from London as a consequence of Brexit', the Sunday Business Post reported. In trying to achieve reform in this area the Taoiseach will have to work with Fianna Fáil, who are calling for a lowering in the 5% USC rate, as stipulated in the confidence and supply agreement.

European Union

Macron steps up as EU's champion

French President Macron has moved to position himself firmly as the EU's guardian and leader, through proposed reforms set out in his recent speech at Sorbonne University. The 90 minute [address](#) identified goals for a renewed, unified and resolute EU. Following this thought, Mr Macron further extended a hand to the UK as he [believes](#); '[in] this revamped, simplified European Union [he] can't imagine that Britain could not find its place.' Ironically, some have [interpreted](#) the speech to in fact be a warning to Member States, including Ireland, whose interests could be seen as averse to those of the EU – on the issue of corporation tax policy for example. Macron tempered his enthusiastic language slightly when he emphasised; '[no] state must be excluded from this dynamic, but no country should be allowed to block those who want to go farther or faster.'

Second phase negotiations blocked in EU

Chief EU negotiator, Michel Barnier, conclusively [stated](#) to MEPs on Tuesday that sufficient progress has not been made to warrant moving to the second stage of Brexit negotiations, concerning future partnership and a transition period. Mr Barnier recognised Theresa May's efforts to clarify the UK's position in her Florence speech last month, however the EU did not receive it well enough to ameliorate the deadlock in discussions, as Mrs May might have hoped. The EU's chief negotiator also [pronounced](#) there are 'serious divergences' between the two sides on the topic of the divorce bill, leaving little hope at present for a breakthrough.

Budget 2018 and the SME Landscape

Pre-Budget Submissions Focus on 'Brexit-Proofing' Measures

Over the past number of weeks and months, pre-budget submissions have been making their way to the Department of Finance, many addressing similar concerns on the unknown effects of Brexit on trade. A number of key business and trade interest groups have proposed industry-specific policies to help mitigate future economic shocks. However, with an estimated fiscal space of €350 million, the only certainty at present is the lack of flexibility on the government's part to protect all markets. A number of submission requests are outlined below, with some overlap relating to Brexit:

Chambers Ireland

- Establishment of an Export Working Capital scheme to assist SMEs to expand in foreign markets.
- Increase the lifetime limit of €1 million in qualifying gains under Entrepreneur's Relief to €10 million to remain competitive.
- Reduction in Irish Capital Gains Tax rate of 33% to be closer to the UK's standard rate of 23%.

The Consultative Committee of Accountancy Bodies Ireland

- An SME share-based remuneration tax measures should be fully integrated with entrepreneur's relief, company buy-back of shares CGT treatment and the Companies Act 2014.
- A frictionless border which relies on a sophisticated IT system to implement border controls to facilitate customs payments and declarations.

Dublin Chambers

- Improvement of Entrepreneur's relief on Capital Gains Tax by increasing the cap to €10m.
- Implement lower rate of CGT (20%) for all investments in unquoted companies.

Irish Business Employers Confederation (Ibec)

- Increase fiscal space for infrastructure investment.
- Brexit-proof the budget by establishing funds that support innovation, diversification and upskilling.
- Defend the current FDI investment model.

Irish Congress of Trade Unions (ICTU)

- Increase the social wage, i.e. the level of state remuneration available to citizens, with a view to protecting workers who experience decline in income in light of Brexit.
- Reform the tax base by addressing the tax expenditure system and introducing a net wealth tax, among other measures, to increase investment potential.

Irish Small & Medium Enterprise Association (ISME)

- Reduce all business CGT rates to 20%.
- Increase the limit on capital gains to €15 million.
- Increase investment in workforce training programs.

All submissions highlight the housing crisis and investment bottlenecks as issues to be addressed before the impact of Brexit shocks are felt. The Capital Gains Tax regime also appears to be a pressing issue for many in the business community.

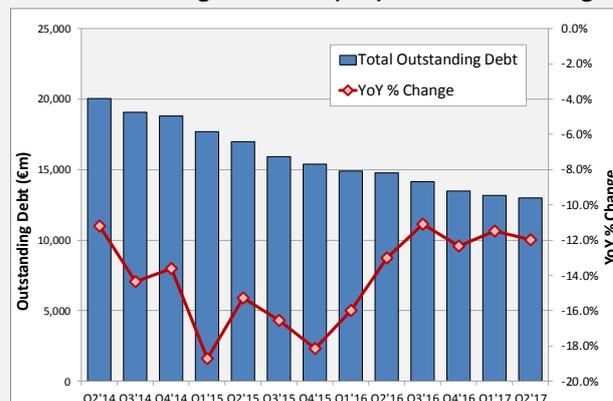
Pre-Brexit SME Sector

Much has been said on the exposure of Irish SMEs to economic shocks in the lead up to, and as a result of Brexit. With this in mind, what are the economic indicators suggesting about the current outlook for SME activity in Ireland?

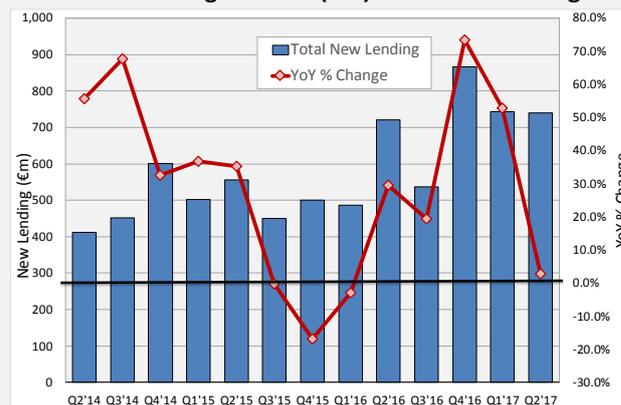
DKM/BPFI SME Market Monitor

DKM has recently published the October 2017 [DKM/BPFI SME Market Monitor](#), and a mixture of positive and negative trends have been observed. One of the key indicators of a healthy economy is the debt burden, and total outstanding debt in the SME sector continues on a downward trend. However, debt is not the only barometer indicative of the strength of the economy; investment in both capital and R&D increases productivity, and improves competitiveness. New Lending statistics are also used to analyse the sector's willingness to engage in investment, but with very modest year-on-year change in lending levels in Q2'17, mostly it is believed for short-term working capital purposes, this may reflect a degree of caution amongst enterprises who may be less inclined to make major investments before future Brexit costs are known. The risk is that this caution may continue in the medium to long term, which would potentially mean lower levels of output for SMEs. Notwithstanding this, lending in a strong economy to grow business as opposed to sustain it, is generally viewed as a positive sign of business confidence. More detailed analysis is available [here](#).

Total Outstanding SME Debt (€m) and Rate of Change



Total New Lending to SMEs (€m) and Rate of Change



Source for both: Central Bank

Relocations News

Commission highlights 'generalities' of Irish plans

On Saturday last, the European Commission published an unranked [assessment](#) of the bids made to host the European Medicines Agency (EMA), of which there are nineteen bids, and the European Banking Authority (EBA), of which there are eight. Ireland is currently lobbying for both, submitting a glossy brochure and video application, introduced by Taoiseach Varadkar, and has committed up to €10 million to help the relocation, and rental support of €13.5 million for the EBA, and €78 million for the EMA. The proposals identify a number of buildings/sites in the docklands that would be appropriate and made available if successful. However, the initial [comments](#) from the EC on Ireland's submission highlight the lack of clarification on issues such as available school places for the children of staff, and only a general level of detail on suitability and staff opportunity. A final decision will be taken by the 27 Member States in November.

Business & Finance

PMI records 52nd successive growth reading

As discussed in the most recent [SME Market Monitor](#), figures for the Markit/Investec Manufacturing Purchasing Manager's Index measured at 55.4, down slightly from the previous month's reading of 56.1. However, this is still well above the '50' mark used to distinguish growth from contraction. One of the drivers of growth in the index is the *New Export Business Component*, in part contributed to by UK export increases. This indicates that, at least

in a pre-Brexit economy, Irish manufacturing production has capacity to grow. The identification of new markets abroad is being seen as a way to insulate Irish industry from potential Brexit shocks.

US executive named for EU hub in Dublin

Bank of America Merrill Lynch is moving forward with [plans](#) to expand operations in Ireland, having announced the relocation of one of the bank's top executives, vice-chairman and head of risk, Bruce Thompson, from the New York subsidiary to head up operations in Dublin. The move marks one of the first personnel announcements, with full operations relocation not expected until Brexit is seen through. The bank has committed to the establishment of its European hub in Dublin which will require the merging of the current Irish subsidiary – Merrill Lynch International Bank - with its main subsidiary in London. Mr Thompson's new role is in addition to his existing responsibilities.

EU memo suggests all-island, agri-food sector in light of Brexit

A memo has been [leaked to RTE](#), reportedly from the office of EC President Claude Juncker to the Irish government, suggesting that the agri-food sector could operate on an all-island basis post-Brexit. The note acknowledges the challenges facing industry of this nature, and suggests that an invisible border might be the best way forward. This is not only a financial concern, but also a regulatory one as, after Brexit, food products and animal health would no longer be regulated by the EU, and will require extensive border checks to ensure compliance, thus necessitating a hard border. A number of EU officials have recently [suggested](#) that the border be established between the two islands. It is yet to be fully seen how either approach would be implemented.



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