viewpoint

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BREXIT in Review

As soon as the votes were counted on Britain's recent referendum vote to leave the European Union (aka BREXIT), we sent out an email to our clients briefly outlining our strategy for working through the event as well as our initial outlook on the financial markets.

Of course, our work actually began many weeks prior to the vote as we scoured our portfolios in an attempt to identify positions that might be adversely affected over time by an affirmative BREXIT vote. Happily, we didn't find a single issue and now that the votes are counted and the financial markets have reacted accordingly, client portfolios appear to have weathered the storm of controversy reasonably well. As we go to print with this newsletter, most major markets have recovered after their initial pullbacks from the BREXIT vote.

That is not to say that Britain's affirmative referendum vote, doesn't concern us – it does. In the wake of BREXIT, we have now turned our attention to what is the most likely outcome for financial markets going forward and how the developing story might impact our long-term portfolio returns. As we continue to digest analysts and media coverage of the BREXIT dilemma, we have already found a few takeaways worth noting:

- First, no one seems to agree on the BREXIT vote ramifications as evidenced by the ever-present BREXIT headlines. The referendum vote was hardly a groundswell of public opinion as the measure narrowly passed by a margin of less than 2%. Northern Ireland and Scotland actually voted in favor of remaining in the European Union (EU). Current polling indicates that over a million voters would cast their vote differently if a re-vote of the referendum were taken today.

- Second, the referendum itself does not appear to actually require British Parliament to carry out the public mandate. Parliament itself must vote to depart the EU and only then can the process begin. Or, at least that is the current opinion in London. This belief is already being challenged in some legal circles. Regardless, the matter has created an intense political drama and now that voters have seen the potential impact of BREXIT with their own eyes, politicians are likely to seek middle-ground solutions.

- Third, the alternative solutions are limited. UK leadership is in a bit of a quandary and we see only handful of viable choices for Britain going forward: exit the EU cleanly and quickly; attempt to renegotiate their EU involvement with the other 27 EU countries; present a re-vote to the voters and hope the problem goes away by a reversal of opinion; or, be slow and deliberate with implementation and hope that time will provide a more considered and planned exit.

Unfortunately, none of these solutions are without tremendous economic and political risks so it is not surprising that Britain has not formally begun the process of withdrawal. Given the options available to UK leaders, we believe whatever course they choose over the next 6-12 months, we are likely to see continued BREXIT headlines producing continued volatility in the financial markets. In the long run, however, we believe the actual impact of BREXIT will be minimal – if at all – for clients with diversified portfolios.

Since our firm focuses primarily on corporate earnings – and, over time, so does the market – we feel any material fallout from BREXIT will be limited to specific stocks and industries and not the market as a whole. As with any equity position we own, if the company's earnings is negatively affected by long term forces, we will sell off the position. Conversely, short-term volatility often presents us with buying opportunities.

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