



Financial Markets Commentary – The Aftermath of Brexit

June 24, 2016

To the surprise of most investors around the globe, yesterday the U.K. voted 52% to 48% in favor of leaving the European Union (EU) after more than four decades in a stunning rejection of the continent's postwar political and economic order. Prime Minister David Cameron resigned, stating that he would serve another 3 months until his replacement is elected. Financial markets around the globe responded with stocks selling-off while bonds and gold are rallying.

The result of the vote is important for a number of reasons, but none more than the fact that global economic growth has been fragile since the Great Recession of 2008. Brexit (the British exit from the European Union) is a confidence shock to global economic growth. The U.K. now faces a period of long and drawn-out divorce talks with the EU. Under EU laws, the highly-negotiated process of withdrawal has up to 2 years to be completed. The level of uncertainty and volatility in financial markets will likely remain elevated for quite some time.

In the days leading up to yesterday's vote, global financial markets were positioning themselves for the U.K. to remain in the EU. Therefore, markets were caught offside and this swift and deep sell-off is the result of an imbalance of sell orders. Within the next few days, financial markets should move back into balance. Fortunately, global central banks and monetary authorities stand ready to maintain and if need be, increase liquidity in the financial system. The Fed will continue to hold off on raising interest rates, perhaps for the remainder of this year.

With no real way to assess the likelihood of the U.K. leaving the EU, from a risk management perspective we felt that it was prudent to tactically reduce all direct exposure to European stocks last week. We are now significantly underweight our strategic targets for international, developed market stocks and underweight risk assets in general. The proceeds of the sale remain invested in cash as we further assess the ramifications of this historic event and look for opportunities in risk-based assets.

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