SPECIAL MARKET COMMENTARY
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Brexit – What Happens Next?

As everyone now knows, the British vote on whether to stay in the European Union (EU) has now been decided by a narrow margin by the populace in favor of exiting. Global markets are reacting strongly to the news, as many were simply not expecting the vote to pass. But in the end, the vote came down to one primary issue that should sound familiar to US citizens – Immigration, particularly for the working class populations outside of London. As noted in a Wall Street Journal (WSJ) Interview, people voted to exit due to the huge influx of eastern European immigrants to Britain in recent years, which has changed the face and feel of many rural towns. While immigration was the issue that captured the attention of the people, there were other factors including burdensome EU regulations and perceived threats to British sovereignty. Recall also that Britain never joined the currency union, largely due to concerns of handing over British monetary policy to the EU.

The EU is in uncharted territory, both politically and economically, when it comes to the Brexit vote, as well captured by a recent WSJ column: *"The consensus for greater integration has been remarkably durable to date. Since the EU's founding in 1957, 28 countries have joined and none have left (other than Greenland, a Danish territory and Algeria, which ceased to be part of the EU upon independence from France). Indeed, it is rare for any country to deliberately withdraw from a trade pact except to join a better one. Since the World Trade Organization's inception in 1948 (as the General Agreement on Tariffs and Trade), 162 countries have joined and none have left."*

So what does the vote initially mean?

- The referendum itself does not remove the UK from the EU, but will put pressure on the British parliament and Prime Minister to begin the political process of notifying Brussels that Britain desires to begin the process of negotiating leaving the EU under article 50 of the Lisbon Treaty. The referendum itself was non-binding on parliament, and the way forward is murky and will likely be slow politically.
- *"Uncertainty is going to be a fact of life for the UK economy for a considerable time to come, while the country's foreign economic relations are renegotiated", said Howard Archer, Chief European Economist at Consultancy IHS Global Insight in London.* – Wall Street Journal
- The decade's long push for global integration and the removal of trade barriers could be coming to an end, and protectionist economic measures may rise.

While global bond and equity markets are beginning the process of digesting the news, we can speculate on some of the near and longer term implications:

- The Pound Sterling weakening and the US Dollar strengthening (Sterling is already down 11% versus the US Dollar in overnight trading.)
- The likelihood of a recession in Britain and Europe has risen, and likely to see a drag on US growth as well.
- London's position as a world financial hub is likely to decline – and will benefit the other European capitals.
- The US Federal Reserve will be largely on hold regarding raising overnight rates for the balance of the year, and possibly longer.
- As article 50 is discussed and withdrawal from the EU pursued, Britain will potentially need to renegotiate a number of trade agreements with other nations - inducing uncertainty on trade and business decisions.

Remember that market volatility can provide prudent and patient investors with investment opportunities, but one must first have a diversified investment plan so as to be best prepared to evaluate those opportunities.

Sources of information: The Wall Street Journal and WSJ.com.