



COMMENT

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BREXIT: TO LEVERAGE ON POSSIBLE SHORT-TERM OPPORTUNITIES

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The victory of the Brexit camp in yesterday's referendum - which came with a high participation rate and a relatively low majority (52% vs. 48%), but nevertheless stronger than recent polls had led us to believe – is sending shock waves across financial markets. Investors had settled on a “Remain” scenario. Furthermore, this political shock is a first in European history, particularly as it concerns a major country, and has sparked a flurry of uncertainties. The consequences, mostly unknown, could take the European political and economic agenda in all sorts of directions.

RISK PREMIUMS ARE UP - BUT NO SYSTEMIC OR MAJOR LIQUIDITY RISK

Unlike the Grexit issue which had caused turmoil on the markets between 2011 and 2015, the British decision does not cause systemic risk because the country was not a member of the monetary union. The higher risk premiums will therefore have to be factored into the market. Furthermore, no major disruption in liquidity was observed this morning – central banks stand ready to inject massive amounts of cash into the system if required.

UNCHARTERED WATERS

The ultimate decision is down to the British Parliament

Yesterday's referendum is a public consultation that has no legal value. Only the British Parliament is able to call upon article 50 of the European Union Treaty. The Parliament then has two years to organise the procedure for leaving the European Union, although this timeframe may be adjusted if both parties mutually agree. It seems unlikely that events will unfold differently. However, in a context of extreme political tension, no scenario should be excluded outright. The British people wanted their Parliament to regain its full sovereignty – so it is ultimately down to the Parliament and to the Parliament alone, to make the decision.

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The economic impact of Brexit

Many simulations have been run in an attempt to assess the mid-term impact of a Brexit. Virtually all estimations result in a negative impact on economic growth in the U.K., with a drop of 1% to 7% compared to an ordinary state of affairs. These gaps vary according to the terms of the new agreement which will govern relations between the United Kingdom and the European Union – relations which are yet to be determined, and on the basis of a highly uncertain timeframe. The impact on growth in the Eurozone is not as simple to identify, but it is generally believed to be relatively modest. It is important to weigh the negative effect of possible lower exports towards to the U.K. with the positive effects caused by the relocation of some businesses from the U.K. to the Eurozone.

Nevertheless, the short-term dynamics are clearly negative. Considering that the U.K. will remain in the European Union for a further two years, it will be able to export to the Eurozone with a highly competitive currency. However European export companies will suffer if one of their large trading partners is affected by weak domestic demand and a low currency; the profitability of Eurozone companies will therefore be negatively impacted.

The political impact of Brexit

It is very likely that the referendum result will galvanise the anti-EU forces that are already at work in Europe. The risk is that markets anticipate further European disintegration, possibly extending to the European Monetary Union.

We have naturally taken this risk into account in our analysis. However we have also included other factors:

- It is not so easy for a country to leave the European Union when it is also a member of the Euro, as the economic and financial consequences would be that much more material and systemic. The Greek experience confirms this observation.
- The United Kingdom had always slowed down the European integration process. And yet – at the very least for Eurozone countries – further integration seems inevitable. The Brexit has removed a major hurdle. Nevertheless it remains to be seen whether there is enough political support for further integration in core European countries. Initiatives should be announced in the near-term to give Europe a new impetus. In the coming weeks, we shall be in a position to assess the direction taken by the Old Continent in the wake of this political tsunami.

While Europe may never have been as politically fragile as it is today, we believe excess pessimism is uncalled for. Europe has the resources it needs to recover from this crisis. The region is in better economic shape today – unemployment on a downward trend, return of economic growth - and has already demonstrated its ability to reform following the Greek financial crisis (new intervention mechanisms set up during the Greek crisis have proven to be efficient; responsibility for the banking industry transferred to the ECB, harmonisation of banking and financial regulations, European deposit guarantee fund).

IMPACT ON OUR INVESTMENT STRATEGY

Since the beginning of 2015, Europe has been our main regional conviction – both for equity and fixed income investments. During the past two months, we had reduced risk by lowering our overweight position on European equities and periphery country bonds, while increasing the weight of the dollar in our portfolios in order to factor in the Brexit risk.

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The electoral calendar is busy, with uncertain outcomes (general election in Spain on Sunday, referendum in Italy over constitutional amendments); from a political perspective, it therefore seems unlikely that the market risk premiums will fade quickly. From an economic point of view, the situation should remain more or less stable, with central banks further strengthening their accommodative stance. We do not expect to see a tightening of U.S. monetary policy before the 4th quarter, as the Fed - and investors alike - factor in the rising uncertainties.

This morning's stock market plunge is very pronounced but at this stage remains within the extreme limits that would trigger a review of our investment policy. More than ever, we are on the lookout to leverage on possible short-term opportunities and to rethink our mid-term investment policy.

Über die Edmond de Rothschild Gruppe

Die Edmond de Rothschild Gruppe ist eine unabhängige Unternehmensgruppe in Familienbesitz, die auf die Bereiche Asset Management und Private Banking spezialisiert ist. Die im Jahr 1953 gegründete Gesellschaft wird seit 1997 vom Baron Benjamin de Rothschild geführt. Die Gruppe verwaltet ein Vermögen von rund 150 Milliarden Euro, beschäftigt 2.800 Mitarbeiter und unterhält weltweit 33 Niederlassungen (Stand: 31. Dezember 2015). Neben dem Asset Management und Private Banking ist die Edmond de Rothschild Gruppe in den Bereichen Corporate Finance, Private Equity und Fondsverwaltung tätig.

Die Edmond de Rothschild Gruppe positioniert sich heute mit ihren 6 Knotenpunkten weltweit (in Frankreich, der Schweiz, Deutschland, Hongkong, Luxemburg und Großbritannien) als eine mehrfach spezialisierte Investmentgesellschaft für Asset Management. Sie zeichnet sich durch ein umfassendes Produktangebot aus, das unter anderem die Bereiche Europa- und US-Aktien, Corporate Debt, Multi-Manager, Overlay Management, Asset Allokation und Quantitatives Asset Management umfasst.

Im Asset Management verwaltet die Edmond de Rothschild Gruppe etwa 53 Milliarden Euro (Stand: 31. Dezember 2015) und beschäftigt 530 Angestellte einschließlich 100 Investmentspezialisten.



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