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INVESTMENT ADVISORS

Brexit Vote

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On June 23, 2016 the people of the United Kingdom (UK) voted to leave the 28-country European Union (EU). This is the first country to elect to leave the EU since its formation in 1993. The results of the popular referendum will lead to several months of unprecedented negotiations between the UK and the EU to determine the terms of the exit. As stated by **G. David MacEwen**, CIO of American Century, "The UK parliament must now enact a series of legislative moves to implement any changes in the UK's status." The UK is approximately 4% of global Gross Domestic Product (GDP) and is the second largest economy inside the EU, after Germany.

Rank	Country	2016 Projected Nominal Gross Domestic Product ($B)	% of World
1	United States	$18.6	25.1
2	China	$11.3	15.4
3	Japan	$4.4	6.0
4	Germany	$3.5	4.7
5	United Kingdom	$2.8	3.7

Source: StatisticsTimes.com (June 24, 2016)

Britain's decision came as a surprise as the markets were expecting the UK to vote to remain. The vote reflected a highly divided nation as London, Scotland and Northern Ireland all had a majority vote to remain, while Wales and the English shires (counties) had a majority vote to leave. The results prompted **Prime Minister David Cameron**, who led the campaign in favor of the EU, to resign by Oct. 2016, which set off a leadership contest among his political party.

News of a "leave" vote lead to a significant sell-off of risky assets around the world on Friday, 6/24/16, with the Dow Jones Industrial Average (DJIA) down 610 points. US economic growth may take a small hit. A Brexit may result in a stronger dollar, which could hurt the earnings of multinational corporations and make domestic manufacturing less competitive. The dollar's rise could slow emerging markets and also be a negative for commodity prices (*IBD*, 6/27/16). US stocks remain more insulated from global developments than any other major equity market as American companies generate 70% of revenue domestically, compared to 49% for Europe. Friday's correction caused the US S&P 500 to drop 3.6%, while the Euro Stoxx 50 dropped 8.6% (*Barron's,* 6/27/16). The markets experienced steep declines, however, the losses primarily reversed the gains that were made in the days leading up to the vote, when investors were expecting the UK to vote to remain in the EU. Major US stock markets are now slightly negative for the year, but are well above February 2016 lows (as of 6/27/16).

According to **James Paulsen**, Chief Investment Strategist at Wells Capital Management, "Once the emotion of this event fades, investors may get back to the fundamentals, which at least in the US, are looking better" (*Barron's*, 6/27/16). It will take months to see actual economic impacts, but the Brexit news instantly adds uncertainty to a global economy that has been struggling for growth. Uncertainty leads to increased volatility, as markets reprice and digest new information.

While few economists see a Brexit as positive for the global economy, perhaps the largest long-term concern will lie with the remaining members. If more member countries consider exiting the EU, it will become very difficult for the entire European economy, which is one of the reasons, according to **Dr. David Kelly**, Chief Global Strategist at JPMorgan, why the EU is likely going to be firm in exit negotiations; to discourage other countries from leaving. The good news is that the United States economy is expected to see limited immediate economic impact and the Federal Reserve is now unlikely to raise interest rates any time soon.

In times of uncertainty, it is especially important to remember your long-term goals and to not let fear control your investment decisions. Consider your investment time horizon and remember what **Warren Buffett** once said, "Choose a portfolio you can stick with, no matter what tomorrow's news brings."

One of the success factors of investing is avoiding emotional reactions to sharp changes in the market. Historically, when economic shocks arise, markets have the tendency to gradually bounce back to their levels before the shock. The stock market recovery after the financial crisis of 2008 is a perfect example of this. Since the bull market began in March 2009, stocks have almost doubled. This means that if investors stayed the course, did not let their emotions get the best of them and continued to contribute to their retirement plan during the market's worst months, their plan balance would likely be more than it was prior to the correction. Past performance is not necessarily an indication of future results.

The recent volatility in the global markets reinforces the need for a diverse portfolio made up of an appropriate combination of stocks, bonds and cash for your age and investment goals, as well as the need to rebalance when your investments get too far out of line. If you are thinking of opportunities to buy in this market, be careful and wait for Europe to stabilize, especially European banks, before investing too much.

Volatile markets may bring many opportunities for investors who are aware of their risk tolerance and refrain from making emotional investment decisions. Although the volatility and uncertainty has been intensified due to the Brexit, it is important not to panic and keep your money invested with a long-term perspective in mind. **Be proactive, not reactive.**

If you need advice, please contact Spectrum at 1-800-242-4735 or sia@spectruminvestor.com.

Important Disclosures

- Gross Domestic Product (GDP)—The total value of goods produced and services provided in a country during one year.
- The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ.
- US S&P 500 Index—A market capitalization-weighted index composed of the 500 most widely held stocks whose assets and/or revenue are based in the US.
- Euro Stoxx 50 Index—Europe's leading Blue-chip index for the Eurozone, provides a Blue-chip representation of supersector leaders in the Eurozone. Covers 50 stocks from 12 Eurozone countries.