Brinker Capital

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the impact of Brexit

June 28, 2016

The United Kingdom's decision to exit the European Union (EU) has unsettled global markets

Brinker Capital portfolios were well positioned prior to the vote with a meaningful underweight to developed international equity in favor of the U.S. equity markets. In our view the market uncertainty creates future opportunities in Brinker Capital's actively managed multi-asset class investing process.

Key highlights:

- Friday, June 24, was largely a retracement of last week's market action. Over the week prior to the vote, the MSCI EAFE Index was up over 7% and the Russell 3000 Index almost 2% as the market anticipated a "remain" vote. We've retraced that rally but global markets are only marginally down from levels seen a week ago.
- Brinker Capital portfolios have generally been underweight to international markets, specifically developed international markets.
- This vote is largely a political event, not an economic event. It marks the coming end of the UK's trade agreement with the EU, but the process will likely take years. What it has done immediately is increased the level of uncertainty in markets. We will likely see additional global central bank liquidity and easing in an effort to support economies and markets.
- Emotional trading can create opportunities, so our focus over the coming weeks and months will be to identify and take advantage of these opportunities.

Brexit's impact on global economies and markets

- The economic and political impact on the UK is decidedly negative, but the degree of which remains uncertain. In our view the currency and equity markets will be weaker in the near term while the long-term outlook is unclear, given the politics involved.
- The negative economic impact on Europe is less, but still meaningful. From a political perspective, the departure highlights the rising risk of populism and becomes another distraction for the EU from much-needed reforms. We expect a weaker euro and European risk assets in the near term; the central bank could try to cushion some impact.
- International markets will experience the indirect effects of lower global growth and general risk aversion.
- We do not see it as having a significant direct impact on the U.S. economy; however, a strengthening U.S. dollar as a result will be a headwind for U.S. companies with significant international business.
- Expectations for additional interest rate hikes by the Federal Reserve have plummeted. On June 27, the futures curve predicted a zero chance of a rate hike in September (down from 31% on June 26) and a 14% chance in December (down from 50%) [Source: ISI Group].

How Brinker Capital is positioned in strategic portfolios

- Portfolios have been positioned with a meaningful underweight to international equity markets in favor of domestic equity markets.
- The underweight has been concentrated in developed international markets, due to concerns over long-term structural issues in their economies that have an impact on economic growth.
- We don't anticipate any immediate changes to the portfolios as a result of these events as we feel we were well positioned ahead of the news, and we expect to reallocate portfolios in late July.

Overall summary

- We think this is an extended process that will develop over the coming months and years. Over the last few days, the market has been pricing in the uncertainty, but this will be a fluid and evolving process.
- The market selloff has been relatively orderly and largely a retracement of the gains over the week leading up to the vote.
- We believe our portfolios were well positioned in advance of the vote with an underweight to international markets.
- We expect the uncertainty to result in higher levels of volatility, which creates opportunities for active management.