

The Market Observer

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UK Referendum

The unexpected UK Referendum result has increased the level of uncertainty and volatility on global markets. Reactions have been swift and generally negative. But any concrete changes to the Law or the ultimate membership of the European Union and the subsequent trading relations within and external to that Union, will probably take considerable time to determine and enact. Ausbil will take a measured approach to the situation.

The key international policymakers, namely the European Central Bank (ECB) and the Bank of England (BoE) have started to deal with Brexit by releasing substantial additional liquidity into the system, while the US Federal Reserve (Fed) has already stated that the risk of Brexit was one of the reasons for delaying any further interest rate hikes. There is also likely to be a more co-ordinated global effort by Central Banks to ensure liquidity remains sufficiently available.

Nevertheless, the impact will be widespread. In general, we expect global growth forecasts to be lowered and currency, bond, equity and commodity volatility to continue, while Bank funding may also be impacted and consumer sentiment would likely ease. The question is, however, to what extent? And that is impossible to answer accurately at this very early stage. What we do know is that UK growth forecasts will be lowered and therefore global growth expectations will be pared back, the US Fed will keep rates lower for longer and the thirst for yield will continue.

On a positive note, the decline in the value of the British Pound would improve the competitiveness of the UK's exports and may well be the silver lining under the latest developments. We also expect UK interest rates to move lower.

Ideally, the Brexit decision will primarily hand the ability to pass laws and set taxes back to Britain from the European Court of Justice in Luxembourg, while maintaining the overarching benefits of free trade and access to the single market. This, however, remains to be determined. Security, foreign policy and counter-terrorism considerations are also obviously paramount.

Locally, the Reserve Bank of Australia (RBA) has room to move by lowering interest rates to more accommodative levels, while any further depreciation of the Australian Dollar will also provide a buffer against international developments.

Pockets of the Australian share market have actually benefitted from the Brexit-led uncertainty, such as the high yielding domestic telecommunications, infrastructure and utilities stocks, as well as the domestically focussed REITs, while the Gold sector has also been keenly sought. We have been increasing our exposure to high yielding stocks and we have investments in a number of gold stocks across our Portfolio.

The wild gyrations in global markets have had an impact on a small number of UK exposed holdings within the Ausbil Portfolios. Needless to say, we will continue to monitor the entire situation extremely closely and our assessment of each holding may change pending further developments.