

Redwood Bulletin

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Brexit: To leave or to stay

The Brexit referendum in the United Kingdom delivered a surprise outcome, with the decision to leave the European Union (EU).

It is too early to provide any definitive conclusions however, at this stage, Redwood views the event as a political issue with meaningful economic consequences for the UK rather than a systemic problem. That said, we watch cautiously the flow on impacts on European and more broadly global economies. We note that central banks globally stand well placed to provide liquidity if and when required.



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While the decision was unexpected, the immediate impact is uncertainty, and this may remain for some time. To give some context, the UK is only 4% of global GDP and its current contribution to global growth is about half of that. However, markets dislike uncertainty and we expect to continue to experience volatility as negotiations progress between the UK and the EU.

Should the UK invoke Article 50 of the Lisbon Treaty (required before formal negotiations between the UK and EU can proceed), we believe the exit process will be prolonged and it is unlikely the EU will allow the UK an uncomplicated exit. The EU has little incentive to allow an amicable exit for fear of setting a precedent for other EU member states to follow. The EU will want to make it abundantly clear, there is no benefit in leaving.

As long-term investors at Redwood, we must remember that volatility is a normal part of investing. During times of heightened uncertainty we must avoid being swayed by our emotions. History shows that long-term investors can be rewarded during times of market stress as this tends to create attractive opportunities.

We remain very comfortable with the high quality companies we own in portfolios. Despite events in the UK, we expect them to continue to generate sustainable earnings, cashflows and dividends. We expect to continue to own these companies for the long term.

Further, we have been happy to hold reasonable cash weightings of late and believe the benefits of these holdings outweigh the current low interest rates on offer as it provides us with the ability to deploy cash into attractive opportunities when they present.

During these times we are reminded of the benefits of a truly diversified portfolio strategy. By diversifying risk across a range of asset classes rather than exposing portfolios to a single dominant asset class (such as equities), we believe clients will be better positioned to withstand periods of volatility.

We will continue to analyse the many possible computations, with the objective of managing risk in the context of longer term investment objectives.

Should you wish to discuss the events in further detail, please feel free to contact us at Redwood.

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