



# Weekly Digest

Week ending 26 June 2016

## BRit is what it is

Today, the UK (and Europe) can be forgiven a brief period of soul searching, but protracted self-pity is not in anyone's interest. Ultimately the public have spoken and regardless of one's view of the result it is incumbent upon everyone in Europe – businesses, politicians and consumers alike – to do their utmost to make the best of it. Business' natural inclination is to do just that – management is paid by shareholders to make money in all environments – but while there is such great uncertainty over the region it is understandable that businesses may sit on their hands. Doing so raises the spectre of a recession both in the UK and on the continent and as a result we would do well to see the politics settled as soon as possible. We will also likely see further intervention from central banks, but arguably we have seen diminishing returns on their actions for the past couple of years already. The last piece of the puzzle, the consumer, will be concerned today, but we need leadership to calm the nerves and to keep sentiment on as even a keel as possible, ensuring the engine of our economy continues to consume and provide a backstop to business. Companies will change and adapt to prosper in the long run, but management will not invest meaningfully until they understand the regime in which they operate.

It seems all too often in recent years that we have written about 'once in a generation' events: Lehman going bust and the ensuing financial crisis; the unprecedented levels of government asset purchases; negative interest rates; and, as of last week, the momentous decision by 52% of UK voters to leave the European Union. The overarching feeling is one of surprise, with even high profile pro-Exit campaigner Nigel Farage conceding that it "looks like Remain will edge it" soon after the polls closed. The coverage in both social media and traditional media has been sensationalist and with many bemoaning that the referendum has been

used as a vehicle for the expression of political dissatisfaction rather than a genuine and well informed desire to leave the European Union. This is over simplistic and forgets that globalisation and the opening up of our continent's internal borders has not been kind to all, with less educated and lowly paid workers feeling the brunt of changes in recent decades. There has been substantial pressure felt in our industrial heartland thanks to the slow decay of traditional heavy industries such as mining and manufacturing, which have changed beyond recognition since Britain joined the EU. Whether this change is coincidence or not is moot. What is clear, both with respect to national politics for a number of nation states and for the EU edifice as a whole, is that large swaths of voters do not feel that the distant machinations of the Union represents them. The EU seems resolute and inflexible to change and while it has a large number of benefits, polls within founding states such as France and the Netherlands suggest that popular opinion runs well short of the 'ever closer union' that is surely necessitated by a currency union. The EU will do its best to ensure that this is not a watershed moment for the bloc, but if they try to make an example of the UK then it would risk the longer term prospects for both the EU and the UK because there are mutual benefits that stem from trade.

Friday brought with it significant market moves. Some seem justified while others seem indiscriminate and arguably overdone. It is difficult to see why, for example, the US should end the day down 3.6%, whereas given the question marks hanging over the European project, a fall of 5.9% for the continental markets seems more appropriate. Identifying where asset class returns are likely to be muted going forward and/or require a higher associated risk premium, compared to those areas of the markets where the falls have been overdone and offer good value, is now the key for investors.

## The Marketplace

- UK votes to leave the European Union; sterling depreciates
- Political backlash from referendum result
- Pessimism in global equity markets following UK vote
- Fresh record lows for government bond yields
- Flight to safe-haven assets sees gold rally

## Market Focus

### UK

- The UK population on Thursday voted to leave the European Union: 51.9% voted to leave with a turnout of 72%, translating into a winning margin of 1,269,501 votes.
- Early-week increases of the Sterling against the US dollar were eroded on Friday in reaction to the vote, with sterling falling just over 8% on the day. The pound dipped below USD 1.33 intraday to its lowest level since 1985, before rallying slightly to a fall of 4.7% over the week. At time of writing it has fallen by a further 3.3% to reach USD 1.32.
- Bank of England governor Mark Carney announced that “all necessary steps”, including a potential GBP 250bn injection of cheap loans, would be taken to ensure financial and monetary stability.
- Political fallout following the event saw Prime Minister David Cameron announce his resignation by October. Meanwhile a revolt within the Labour party against leader Jeremy Corbyn has resulted in 12 members of the shadow cabinet resigning by the time of writing. Finally, Scottish National Party leader Nicola Sturgeon stated that a second Scottish independence referendum “is on the table” following 62% of Scottish voters wishing to remain in the EU.

### Global

- Developed equity markets reacted negatively to the result in the UK. Prior to Friday, markets experienced gains resulting from increasing confidence in a ‘remain’ result: with UK, continental Europe, US and Japanese equities rising 5.3%, 2.1%, 5.6% and 3.8% respectively up to the close on Thursday. Widespread shock from the referendum result proceeded to trigger a risk-off surge: the same markets’ weekly returns trimmed down to 2.1%, -0.7%, -1.6% and -3.7% respectively.
- Bank stocks were hit particularly hard, with the Euro Stoxx 600 Banks index falling 14.5% on Friday, and a further 6.9% at time of writing on Monday morning.
- Investors sought the relative safety of government bonds. At Friday’s close, 10Y German bund yields (-0.051%), 10Y UK gilts (1.082%) and US 10Y Treasuries (1.561%) all reached record lows.

### Commodities

- Gold was a major beneficiary of the result of Thursday’s referendum, rising by 4.69% on Friday and 1.3% for the week.
- US Brent crude fell 1.5% over the week, including a 4.9% fall on Friday, ending the week at USD 48.41 per barrel.

*James Klempster, CFA & Oliver Bickley*

Asset Class/Region	Currency	Currency returns			
		Week ending 24 June 2016	Month to date	YTD 2016	12 months
<b>Developed Market Equities</b>					
United States	USD	-1.6%	-2.7%	0.4%	-1.9%
United Kingdom	GBP	2.1%	-1.0%	0.8%	-7.1%
Continental Europe	EUR	-0.7%	-6.6%	-10.0%	-16.0%
Japan	JPY	-3.7%	-12.7%	-21.4%	-26.8%
Asia Pacific (ex Japan)	USD	-0.2%	-1.2%	-0.9%	-15.4%
Australia	AUD	-1.0%	-4.9%	-1.5%	-5.7%
Global	USD	-1.6%	-3.8%	-2.1%	-8.1%
<b>Emerging Market Equities</b>					
Emerging Europe	USD	-0.8%	-2.4%	7.9%	-14.7%
Emerging Asia	USD	-0.4%	-0.8%	-1.4%	-17.2%
Emerging Latin America	USD	1.6%	4.9%	18.1%	-14.6%
BRICs	USD	0.7%	-0.2%	0.5%	-22.1%
MENA countries	USD	0.6%	1.6%	0.1%	-18.8%
South Africa	USD	2.6%	3.9%	11.6%	-18.8%
India	USD	-2.1%	-1.6%	0.1%	-8.3%
Global Emerging Markets	USD	0.1%	0.2%	2.5%	-16.9%
<b>Bonds</b>					
US Treasuries	USD	0.2%	1.7%	5.1%	6.4%
US Treasuries (inflation protected)	USD	0.4%	1.4%	5.8%	4.0%
US Corporate (investment grade)	USD	0.2%	1.4%	6.8%	7.1%
US High Yield	USD	0.5%	0.7%	8.9%	0.8%
UK Gilts	GBP	0.8%	3.5%	9.5%	12.9%
UK Corporate (investment grade)	GBP	-0.5%	1.2%	5.7%	7.6%
Euro Government Bonds	EUR	0.3%	0.9%	4.3%	7.3%
Euro Corporate (investment grade)	EUR	-0.2%	0.4%	3.5%	4.4%
Euro High Yield	EUR	-0.7%	-1.2%	3.0%	1.7%
Japanese Government	JPY	0.7%	1.2%	7.5%	9.8%
Australian Government	AUD	0.5%	1.8%	6.0%	8.6%
Global Government Bonds	USD	0.2%	3.0%	9.9%	11.3%
Global Bonds	USD	0.0%	2.0%	7.8%	8.2%
Global Convertible Bonds	USD	-0.9%	-1.5%	-1.3%	-4.2%
Emerging Market Bonds	USD	0.9%	2.5%	10.0%	10.2%



Asset Class/Region	Currency	Currency returns			
		Week ending 24 June 2016	Month to date	YTD 2016	12 months
<b>Property</b>					
US Property Securities	USD	-0.1%	2.2%	8.0%	15.0%
Australian Property Securities	AUD	-0.9%	-0.1%	11.2%	10.7%
Asia Property Securities	USD	-0.3%	-2.1%	-1.5%	-11.4%
Global Property Securities	USD	-0.7%	-0.2%	4.8%	3.6%
<b>Currencies</b>					
Euro	USD	-1.4%	0.0%	2.4%	-0.8%
UK Pound Sterling	USD	-4.7%	-5.5%	-7.2%	-12.9%
Japanese Yen	USD	1.9%	8.3%	17.7%	21.2%
Australian Dollar	USD	1.0%	3.3%	2.5%	-3.0%
South African Rand	USD	-0.1%	3.6%	2.0%	-19.9%
Swiss Franc	USD	-1.4%	2.1%	3.0%	-4.0%
Chinese Yuan	USD	-0.6%	-0.6%	-1.9%	-6.3%
<b>Commodities &amp; Alternatives</b>					
Commodities	USD	-1.6%	0.7%	9.1%	-17.1%
Agricultural Commodities	USD	-4.8%	-0.4%	5.0%	-3.6%
Oil	USD	-1.5%	-2.6%	29.9%	-23.8%
Gold	USD	1.3%	8.2%	23.9%	11.9%
Hedge funds	USD	0.5%	0.4%	-0.8%	-6.6%

For more information, please contact your adviser or alternatively contact:

**Financial Partners Ltd.**  
泛柏資產管理有限公司  
Unit 01 - 03  
24/F, Kinwick Centre 32  
Hollywood Road  
Central, Hong Kong

Tel +852 2827 1199  
Fax +852 2827 0270  
[client.services@f-p.hk](mailto:client.services@f-p.hk)  
[www.f-p.hk](http://www.f-p.hk)

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