SYZ WEALTH MANAGEMENT

SPOTLIGHT

24 June 2016

OUR CONVICTIONS AFTER THE "LEAVE" VOTE

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The decision of the UK people to exit the European Union raises many questions for the short and medium term outlook. On the economic side, the immediate impact should be contained to the British economy, which will probably suffer from a dry up in investment spending and is likely to suffer a contraction in its GDP in the months to come. The direct economic impact on the rest of the world, including continental Europe, is likely to be limited, although central banks will be on their guard to ensure that financial market volatility does not translate into a slowdown in credit distribution to the real economy. Therefore, going forward, the global economic outlook remains similar to that of the previous months: an environment of slow but positive growth driven by domestic demand in the US and Europe, and slightly rising inflation fuelled by commodity prices. However, risks to the growth outlook remain tilted to the downside given the loss of momentum in the US economy and the potential for financial market volatility to weigh on credit distribution channels.

In Europe, the main risk going forward is the political uncertainty that the UK vote triggers. The Pandora's box of popular referendums on EU membership has been opened and European election calendar features national elections in all of the five largest Euro area economies in the next 18 months. Each one of them could be an occasion for anti-European parties to strengthen their positions or even get close to power in the wake of the UK example.

This general framework of subdued growth and political risk will remain for a while but the volatility triggered on financial markets by the UK results probably opens opportunities as all segments of financial markets are being dragged down. While bearing in mind that several risks or uncertainties will remain for a while, today's large movements can be used to tactically adjust portfolio exposure by taking advantage of valuations cheapened by risk-aversion.

In this context, our main convictions are:

- In the high-quality government bond space, US TIPS (Inflation Linked) bonds are now the clear favoured choice: inflation breakeven have dropped this morning and, in a context of positive growth and upward trending inflation, offer upside potential that would result in an outperformance of TIPS over fixed rate bonds. This environment is also supportive for gold.
- In the FX space, the downward moves of the GBP and, to a lesser extent, of the EUR, are not expected to extend further. We would expect a rebound in those two currencies against the USD in the near future. The reaction of the CHF is relatively muted today. In CHF portfolio, we would advise to reduce further or cut EUR exposure. Note also that we are now considering put options on EURCHF as a relatively cheap hedge against additional political turmoil and possible concerns about European Union disintegration
- In equity markets, stock picking opportunities in European markets have certainly arisen in the broad-based sell off. US equity markets may decline within this risk off environment but shall fundamentally be little impacted by Brexit-related developments and therefore remain, in relative terms, attractive. The same can be said for Japanese markets, especially if the JPY retreats from its high reached this morning.

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