

Brexit

Gambling: The sure way of getting nothing from something.

Wilson Mizner; American playwright, raconteur, and entrepreneur

As the UK's European Union referendum approaches we are often asked do we think the vote will be 'Yes' to remain part of the EU or 'No' it should leave?

This is a very important and pertinent question; and one which according to most headlines is dividing a nation and investment managers alike. Opinions have flooded in from every corner of society with each politician and commentator offering their support one way or the other. Even the Governor of the Bank of England, Head of the IMF and President Obama have weighed in for good measure. Early opinion polls were frustratingly undecided hailing the vote too close to call although more recently predicting the status quo being maintained. So what is TAM's view?

Interestingly we are also divided; we see arguments and benefits for both options; but believe it

impossible to predict what will actually happen on the day itself. Will it be another nail in the coffin of the European experiment or simply fade away as a distant memory akin to the Scottish referendum of last year where the silent majority voted with their heads rather than the more vocal minority ruled by their nationalist hearts? We or anyone else can't know for sure but if pushed for an answer this writer believes the latter will be the outcome, however TAM, as a portfolio manager, is sitting firmly on the fence.

We believe the question clients should be asking is; how are you positioning your portfolios in preparation for the vote? And here we have a firm view. Our mandate for every portfolio we manage is to focus on capital preservation when markets look uncertain (or more risky) and capital growth when we have a clearer view of the future. This is not always a straight forward task but our decision making process becomes simpler when we have more clarity such as the firm knowledge an important and potentially disruptive event is looming. To use an analogy; if we were sailing a ship through calm waters with blue skies above we look to add more sail whilst staying mindful that we may encounter an unexpected storm; but if we actually see that storm on the horizon it would be foolhardy not to slow down, batten down the hatches, and pass through it relatively unscathed. We are therefore preparing our portfolios in preparation of the storm by mitigating the risk from either result rather than 'betting' our clients portfolios on an uncertain outcome.

Traditional thinking suggests equity markets will rally following a 'yes' vote, else fall given the future uncertainty a 'no' vote would bring. We believe this assumption will probably hold true but will only be felt as a short-term reaction given much of the uncertainty is priced into equity markets already and not unduly affect portfolios. We are however maintaining a neutral to mild underweight equity exposure across our portfolios; and ensuring that this exposure is well diversified across sector, style and geography.

We are more concerned with currency risk. Sterling will undoubtedly feel the full brunt of the vote whatever the result. With a vote to leave the EU we would expect the pound, already under big selling pressures this year, to violently fall even further. This is a risk we fear and have made some notable changes to our currency exposures over the past months. In relation to our international exposure we have hedged out the currency risk entirely in some cases whilst in others only fifty percent so that we potentially gain or lose in equal measure whatever the vote. This neutralising strategy, we believe, will offer us the time to digest the result and then position portfolios accordingly.

A third area of concern is the physical property market. Our concern here is less the outlook for property – we retain a positive view – but rather the impact the current uncertainly has, and will have, on the liquidity within open-ended property funds. Remember it is near impossible to quickly sell an office building or shopping centre so any negative change in sentiment may cause serious liquidity problems for 'bricks and mortar' investment funds as redemptions overtake subscriptions. Indeed our fear led us to drastically reduce our overall exposure to the sector and more specifically to any single property fund last month. This proved very fortuitous given the pricing changes (resulting in on average 5% overnight falls in fund NAV) announced by the UK's largest property funds over the past weeks in response to increased investor redemptions.

In summary we are in capital preservation mode rather than seeking to add any undue risk or directional

bias to portfolios. We subscribe to the concept that volatility generates opportunity and believe this will be realised in the aftermath of the 'Brexit' vote. We therefore want our clients' portfolios to be in a position to fully benefit from these opportunities rather than feeling like the gambler who having bet it all on black, lost...

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