Economic and Market Insights

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What You Need to Know: Yes, the European Union Referendum Vote Can Affect Your Investments

U.S. investors may think of the European Union (EU) referendum as a temporary economic flap across the Atlantic, but Britain's decision to keep or revoke its EU membership on June 23rd could affect your investment portfolio -- especially if you have exposure to international stocks or mutual funds. Commerce Chief Economist Scott Colbert, CFA, skips the political rhetoric and gets straight to this event's impact on you.

Q. What is the background on the European Union referendum?

A. At stake is Britain's continued membership in the European Union, the economic and political alliance the United Kingdom (UK) shares today with 27 other European countries, as well as the fallout a departure might have on the financial markets, global business trade and the longer term tenure of the EU as a whole. Headline writers call a British "exit" from the EU a "Brexit."

Q. Which way is the vote predicted to go?

A. Even British pollsters recognize the "knife-edge" referendum is too close to call with any authority – to exit or remain. Perhaps in recent days there has been a slight anecdotal tilt toward staying.

Q. As a U.S. investor, why should I care about this?

A. Britain is a major contributor to the EU and the EU's status as the third-largest economy in the world makes this decision important. A British vote to leave has significant implications for Europe, financial markets and investors worldwide. Just the run-up to the vote has recently influenced the Federal Reserve to leave short-term rates unchanged and added to financial market volatility.

Q. What happens if the UK elects to leave?

A. An "out" vote will most likely weigh negatively on global economic growth and add to market turbulence this summer. Few know exactly how much of this event is already priced into the financial markets, but in general, one could expect that the pound and the euro likely will weaken relative to other major currencies, which probably would have a downward effect on most stocks and a positive effect on government bonds and gold. We'd note some of this has already occurred. Just the certainty of knowing the vote, in or out, could afford a bit more stability and perhaps a relief rally for "risk-type" assets.

Q. What would the UK departure do to the EU?

A. Britain would still interact with its trading partners under rules yet to be determined by a two-year negotiation phase after any member country departs. One extreme interpretation is that a British exit will be the first step in eventual disintegration of the union. We doubt that to be the case. While we do not want to trivialize this, or the fact that the markets will focus on whatever the markets like to focus on, our guess is that this will largely be forgotten as the markets find something else to dwell on. Think Greece, Crimea and the recent near obsession with the price of a barrel of oil.

Q. What happens if the UK elects to remain?

A. It would likely be a financial market relief rally and then business as usual with less fluctuation in exchange rates for the euro and pound. London remains a major financial gateway, the biggest and busiest in Europe and rivaling Wall Street as a center of international trading in stocks, bonds, currencies and commodities. The European bloc of like-minded countries would maintain their influence as a united group on the world stage.

Q. Is there anything to do to my portfolio at this point?

A. Just be mentally prepared for possible market fluctuations so you are not compelled to short-circuit your asset allocations for a temporarily bumpy international market. Just remember U.S. markets had a 10.5% correction back in the first quarter and we've already recovered. We believe any market disruption due to a Brexit will eventually be reclaimed as the markets recognize its relatively slow and, in the long run, minimal impact on day-to-day global financial life. Although this is certainly an economic development worth watching, stick to your investment plan and do not get distracted by this event over the long term.

Takeaways:

- Be prepared for plenty of economic media coverage when the Brexit decision is announced June 23rd.
- Recognize that global and U.S. markets already have been volatile and might surprisingly calm down once the certainty of the event is over and the dust settles from any decision.
- Talk to your investment advisor and rebalance to your investment portfolio allocations if markets become distorted.