

June 24, 2016 has become a U.K. Independence Day after a historic vote last night on Brexit. Contrary to what polls and bookmakers thought would happen, Britons voted yesterday to bid adieu to the European Union, terminating their membership after 40 years.

We were not surprised the polls would get a vote wrong, however, it did surprise us that bookmakers, who set odds of a “Leave” vote at an astounding 9/2, would have missed this outcome.

If a “Remain” vote meant a short-term “risk-on” trade the opposite has clearly turned out to be true as well. The U.S. futures market open limit down at 5% but quickly recovered and the S&P is trading less than 2% down as I write. Europeans and Asians were less fortunate with the Japanese Nikkei 225 trading down 8%, German DAX down 6.5%, and the broad European Stoxx 600 losing 14% taking it 40% below its 52-week high after the U.K. vote.

The biggest impact of the vote will be political contagion across Europe. The Dutch and other European nations are already calling on referendum votes to leave the EU and the die has been cast. I do not think the EU or the currency known as the Euro will exist 5 years from now.

The dislocation specific to the U.S. should be short-term as the U.S. is now the world’s safe haven. This will drive U.S. Treasury yields lower and U.S. high quality, large cap stocks should see a lot of buying buoying prices.

We have been holding gold as a hedge in certain portfolios and the yellow metal jumped 5% to a 2-year high. We are also seeing buying in some of the defensive stocks in our Dividend Equity strategy, specifically Verizon.

Looking beyond the immediate impact of the Brexit vote, it is very likely that the U.K. will lead Europe into a recession that will impact China and Japan (already in a recession) and spread to negatively impact the U.S. economy as well. Central Bank bazooka’s were already prepared to shoot whatever ammunition they still hold but with rates already near zero or negative in many instances, they are shooting mostly blanks. Asset purchases will accelerate by Central Banks but I find it unlikely they can keep recessions at bay.

The other impact this vote has involves the U.S. election in November. The U.K. vote was very much populist driven which turned out to be far more powerful than pollsters thought. The Donald is the king of populism and his potential presidency will receive a boost starting today.

We will keep you posted as additional information emerges.