



CONSEQUENCE
PRIVATE WEALTH

The Brexit Factor

Three trading days have passed since the Brexit result. Our sense now is that although capital losses in specific UK sectors such as banks and construction are likely to continue through the week, global markets are not headed towards a repeat of a 2007/2008 event, with central banks prepared to assist with a wider economic fallout. The initial shock and sharp negative market reaction is understandable given that a Remain vote had been generally priced in. The JSE All Share equity index finished Monday at 50 087, down 3% yesterday, our financial sector being particularly affected. There are however signs of a recovery this morning here and in London with Asian markets and US futures positive. Gold rallied Friday and Monday as a perceived safer haven but has dropped off this morning as markets rebound.

At this point our markets are simply mirroring global volatility and that may continue for some time. Our client portfolios are well diversified and are relatively steady compared to global indices. Our offshore clients are overwhelmingly invested in portfolios denominated in USD and have benefitted somewhat from GBP weakness although the underlying asset weaknesses will have had an impact.

The true long term effects on our economy obviously remain unclear. Direct trade with the UK makes up 3.7% of SA global trade, they being notable importers particularly of our platinum and agricultural goods. The UK is also a major direct investor in our economy and financial markets. Will these links be affected by uncertainty over the UK's current international trade deals? Brexit has certainly highlighted the central role of multinational trade agreements. Free marketers question their true significance but trade will move where governments create paths of least resistance.

Crucial now will be the outcome of negotiations on the UK remaining within the European Economic Area (EEA) or 'single market' as it is known. The EU may withhold ongoing membership on the principle of retaining open borders, an issue which the Brexit camp campaigned on. Could the alternative possibly be an emboldened and more competitive UK setting out to re-negotiate on its own around the globe and ultimately reaping greater dividends? Our feeling is that trade between our two nations will continue on as before, negotiations notwithstanding, but the truth is that none of us can predict the long term consequences of this event.

Legend has it that British PM Harold MacMillan, when asked by a young journalist what was most likely to blow his government off course, answered "events, dear boy, events". The quote may be apocryphal but it endures because we sense in it a simple truth; that despite our best laid plans, unforeseen events which can blow a great many things off course are inevitable. For the South African investor, "events" now seem to come thicker and faster than ever. We lurch groggily from one crisis event to another; Marikana to Nkandla to Grexit to Chinese Yuan devaluation to Nenegate to Junk Status to Brexit to who knows what. (Trump?)

The real question for us is whether we allow these events, now instantly magnified in the digital information age, to influence our plans and strategies. How far off course do we allow ourselves to be

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blown? To us the answer is straightforward; geo-political swings and roundabouts must always be considered at the tactical level, but seldom should they influence longer term strategic goals.

Brexit again spurs short term uncertainty and volatility - an opportunity for our preferred fund managers to take advantage of mispricing. Their strategies remain consistent: identify quality assets and tactically acquire them at or less than what they judge to be fair value when others feel compelled to sell. Yes, their trade relations now look uncertain but has the UK suddenly become an investor's nightmare? Hardly. As George Osborne pointed out yesterday, the UK boasts record employment levels, consistently robust growth since 2008 and a budget deficit forecast to be below 3% of national income in 2016.

At times like these we often reflect on the high quality of fund managers produced here in South Africa (the best of these used by us as offshore managers). Perhaps our own turbulent history has delivered unusually patient strategists willing to look through the noise and seek opportunities. Staying on the quotes theme:

"The investment industry never ceases to amaze me. We all understand that we are managing long-term retirement capital. We all understand that it is the long term that matters. And yet the collective temptation to focus myopically on the short term seems irresistible. If one believes that financial markets misprice assets, then one should expect, not just tolerate, periods of underperformance (as long as the fund manager has a demonstrable track record of delivering over the long term). Perversely, this groundswell of short-termism is ultimately helpful to our cause. More short-termism means there will be more mispriced assets out there for the patient, long-term investor to profit from." -Coronation Fund Managers CIO, Karl Leinberger

"We're bottom-up investors and..as this event approaches we've been looking at all of our companies and saying, "To what extent does a Brexit vote either way present a risk or an opportunity for businesses that we own?" and we have not really found it to be a material driver of any of the businesses. As you know, we have a global outlook – a global portfolio – and even those companies that we hold in the U.K. may be U.K. listed but they tend to be multinationals so they're very unlikely to be impacted by even the direst of Brexit outcomes." – Orbis (Allan Gray) Director for UK Business, Dan Brocklebank

So we ask our clients to remain calm and stick to their long term investment strategies. Events continue to dominate the news but not our strategic planning for clients.

Please phone us on 021 674 2222 or email info@consequence.co.za for further information.

This document should not be construed as financial advice, please contact us or your financial advisor for further information before making investment decisions.

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