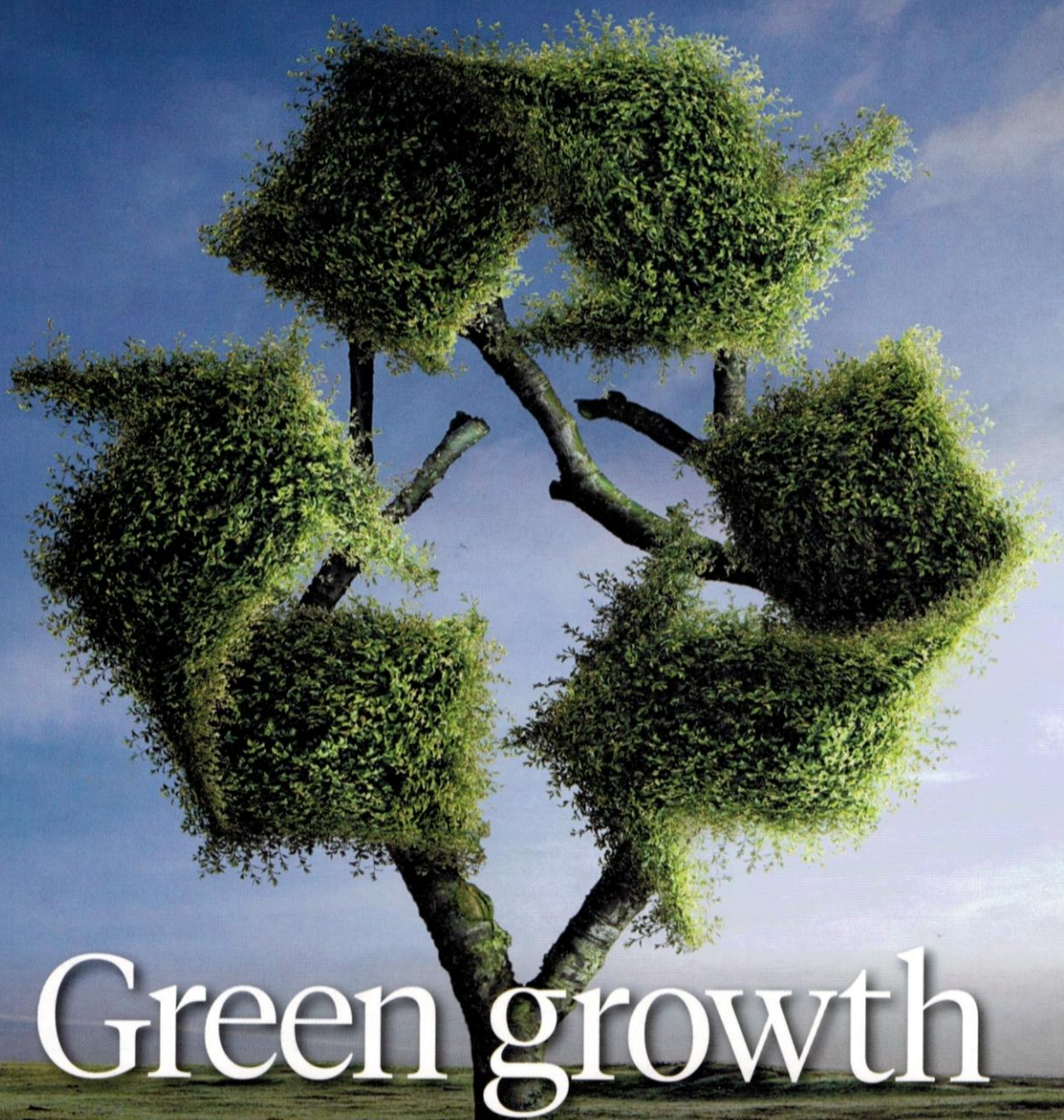


fund strategy

INVESTMENT INSIGHT FOR FUND SELECTORS



Green growth

The ethical investment market is set to boom – 28

Fund manager profile

M&G's Jamie Horvat is seeking to turn around the fortunes of the Global Basics fund – 14

Behind The Numbers

Lipper's Jake Moeller asks, how bad is the closet tracker problem? – 18

Investment Committee

Our experts expect volatile markets in the run-up to the EU referendum – 36

MORE INSIDE

- › Platforms
- › Square Mile
- › Investment Trusts

What does EU referendum mean for markets?

The riddles posed by a possible vote for Brexit are hard for our experts to answer at this stage, but they expect markets to be volatile in the run-up

COMMITTEE CHAIRMAN



Laura Suter
Editor,
Fund Strategy

Prime minister David Cameron's announcement last month of the date of the EU referendum sounded the starting gun on the Brexit debate, which had until then been on the periphery for many in the industry.

The 23 June deadline put the debate centre stage and since then much rhetoric has been spouted from both sides.

While both the "leave" and "stay" campaigns are promising economic nirvana for their camp, and inevitable financial ruin for the opposing view, the data to actually back up these claims seems lacking.

Analysis by Capital Economics of the economic impact of the referendum shows that there will, obviously, be winners and losers in either scenario. But it finds that the net result of leaving the European Union or staying in will not be dramatic either way.

While that may be true, it will not stop markets reacting to the uncertainty. At the time of going to press the outcome looks very uncertain, and if the British public remain split as the date gets nearer markets are likely to get very twitchy.

Sterling has clearly borne the brunt of the indecision so far, which has a knock-on effect on those firms relying on imports and exports.

However, much as with the General Election last year, the Greek crisis and the subsequent China fallout, these wobbles will remain a short-term problem that is likely to be no more than a small blip in any long-term investor's portfolio.



James Calder
Head of research
City Asset Management

As a topic for discussion, Brexit will be staple fodder for anyone commenting on financial markets in the months running up to the referendum in June. My view is that the rights or wrongs of either side of the debate are a personal matter and should be left as such.

However, its impact on markets, particularly the UK, should be assessed. I am unlikely to have any insight on this and would revert to consensus in that we will see, and have seen, sterling weaken. I agree with having a relatively short run-up to the referendum as it avoids a prolonged period of nervousness.

With regard to what we are doing with our portfolios the short answer is nothing. I am usually in the 'we'd rather be doing something' camp as opposed to the 'head in the sand' camp but in this case waiting to see where the chips fall is in my view the best course.

If the result is to stay then it would be business as usual. If it appears that the vote-to-leave camp have attracted substantial support then our view on UK equities, first and foremost, would need to be assessed before the referendum.



Jonathan Davis
Managing director
Jonathan Davis Wealth Mgmt

According to much punditry the recent run on the pound was because either Boris Johnson declared for Brexit or the polls suggest higher than ever numbers supporting it.

Well, I say the pound run has nothing to do with any of this. The fact is sterling rose in the past two economic upcycles – the DotCom boom to 2001 and the lending boom to 2007 – and both times it then crashed in the ensuing recessions.

We have had a third upcycle this century that ended last spring/summer, in which sterling peaked again. We are in potential recession for the third time. The pound is acting entirely normally and is bursting because it's bursting. Nothing to do with Brexit.

In the same vein, I expect Brexit to have zero effect on asset classes, before, during or after the referendum. Individual companies' shares and corporate bond prices may be affected, but not shares or corporate bonds in general. Nor commodities, government bonds or property.

It is a huge 'Herring Rouge' that Brexit will, of itself, hit asset classes. Invest in diversified funds as normal.



Peter Lowman
Chief investment officer
Investment Quorum

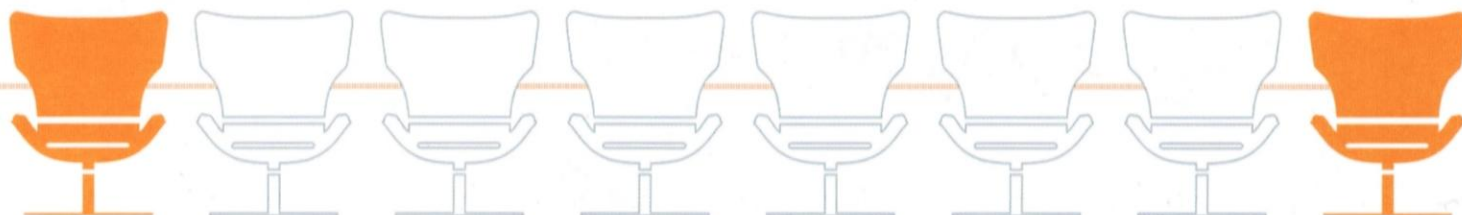
The Brexit effect can already be observed in financial markets. Sterling has felt the force of uncertainties surrounding the vote, with some large institutions predicting it could fall a further 20 per cent if the UK votes to leave the EU.

The effects from a "no" vote are equally visible, but less easy to quantify. At present, while it's a close call, the general consensus is that the country will vote to stay in. However, polls can be unpredictable and sentiment can turn quickly.

If Britain were to vote to leave, then the immediate aftermath could be messy, with GDP suffering, constraints on further fiscal policy, weaker growth and a possible downgrading of our credit rating.

While it is unlikely that the Bank of England would follow Europe's example of adopting a negative interest rate, further rate cuts could not be ruled out. Admittedly, some of this negativity might be offset by the weaker pound and further QE.

Opportunities in the UK market will exist but it's a stockpicker's market and investors should be willing to hunt for undervalued or mispriced businesses.



Mike Deverell

Investment manager
Equilibrium Asset Mgmt

Depending on who you believe, markets are currently pricing in around a 40 per cent chance of the UK voting in favour of Brexit.

Sterling is likely to remain weak, which isn't necessarily bad for investments. Those UK companies that make most of their profits overseas would benefit from a weaker currency. Any overseas holdings in a portfolio would also be boosted.

Despite warnings that the UK's credit rating could be downgraded in the event of a 'leave' vote there has been no sign of a sell-off in UK gilts, which have instead benefited from their safe haven appeal. However, gilts could slide as we get closer to the referendum as they are looking expensive already.

The UK stockmarket may be particularly volatile in the run-up to the vote so it might be advisable to hold extra cash and take advantage of any dips. However, I'd be wary of missing out on a potential rally in the event of a definitive 'remain' vote.

In general, it would be unwise to make too big a call on the referendum. Diversification remains the best defence against uncertainty.



Tim Cockerill

Investment director
Rowan Dartington

This referendum's initiation had little to do with what's best for the country. I fear the discussions will focus on narrow issues that will obscure many aspects that should inform the debate.

Markets hate uncertainty and Brexit provides this in bucketloads: volatility can be expected.

The problem is no one knows what it would mean to leave the EU. Trade integration has developed over the past 40 years and the EU is the UK's largest trading partner. Questions such as 'will we have to renegotiate trade agreements with each country?', 'what happens to legal agreements such as patents?', 'would London's position as the pre-eminent financial centre in Europe be challenged?' can't be answered with any certainty.

The EU accounts for only about 13 per cent of revenues for the stockmarket, whereas it accounts for 50 per cent of UK trade. So in theory international large caps are likely to fare better than domestically-focused mid and small caps.

Sterling could weaken further if the "no" vote gains momentum, giving exports a competitive advantage.



John Husselbee

Head of multi-asset
Liontrust Asset Management

In the long run, political risk typically has little effect on the path of financial markets. That may be little compensation today, with investors' anxiety increasing over the uncertainty of the EU referendum.

The difficulty for voters is to know what the consequences of leaving would be. For starters, the unwinding sounds an unprecedented, daunting and costly prospect. Taking the approach of "crossing the bridge when we get there" will only increase anxiety.

The immediate impact on investments has been transmitted through the currency markets. Sterling's weakness was triggered by a further delay to the prospect of interest rate rises and exacerbated by high-profile politicians declaring for an exit.

Bond rating agencies and professional investors will no doubt be trawling through balance sheets at both the government and company level for downgrades. This will have implications at both sector and stock level.

Last year, capital expenditure was on hold prior to the general election, and it is beginning to feel like *deja vu*.

INDEPENDENT VIEW



Richard Carter

Fixed income
specialist
Quilter Cheviot

With the EU referendum confirmed for 23 June, the stage is set for four months of uncertainty and debate about what Brexit would mean. The polls are leaning towards staying in, but there are a large number of undecided voters.

The clear loser from the uncertainty will be sterling, and the currency has already reacted sharply, dipping below 1.40 versus the US Dollar. This is understandable as no one is quite sure what would happen were the UK to leave the EU, how easy it would be to renegotiate access to the single market and how multinational companies based here would react. Further falls in sterling are likely if the vote is close, with some investment banks forecasting 1.15 versus the Dollar if Brexit were to happen.

The impact on gilts so far has been limited and will probably remain so. Brexit is only one of many factors driving bond markets at the moment, with worries over China and a slowing global economy being the more dominant concerns. In terms of possible bond market hedges, though, index-linked gilts could do quite well if Brexit happens because a sharp fall in sterling will almost certainly give a strong boost to inflation.

UK equities have so far reacted with a shrug, and that makes perfect sense. While some domestic companies may be adversely affected, a large part of the FTSE 100 is made up of international businesses that receive much of their revenues from overseas and in foreign currency. A weak sterling may benefit them as it will increase the funds available to pay dividends, an important topic in equity markets at the moment.