Finlabo Market Update

27th June 2016

Brexit: Financial markets scenario

Against all the polls and all market expectations, the British people have voted to leave the European Union last Thursday.

Markets have reacted strongly, especially because in previous days agents were discounting the opposite referendum result. The reference European index, the Eurostoxx, lost more than 10% during the trading hours of Friday and GBP retreated to 30-year lows. In terms of commodities, it was registered a strong appreciation of precious metals, especially gold, which advanced about 5% last Friday on fly to quality.

So far, for those who followed our previous portfolio advices, the current scenario should not be devastating. The hedging levels of our funds have remained around 50%, which means 20-25% in terms of Beta Adjusted and exposure to US Dollar, Franco and precious metals have contributed positively.

However, the main question is… **what happens now?**

We believe this is the start of a high volatility period and the time and intensity of this phase will directly depend on two factors: First, the evolution of negotiations between UK and Europe will and second, the policy measures that Eurozone leaders will adopt and the potential political contagion that could derive from the British decision.

Regarding the first factor, there is not much to be said. The most probable scenario is that one in which the UK will be able to negotiate an agreement similar to the Swedish or Norwegian one. There are still two years' time, which should assure a positive output.

Still, it is natural to think that UK request of having access to the European market will be addressed on the measure they will be able to offer a counterpart. Furthermore, the key topic of the agreement will be related to the financial services passport, which is a pillar of British economy.

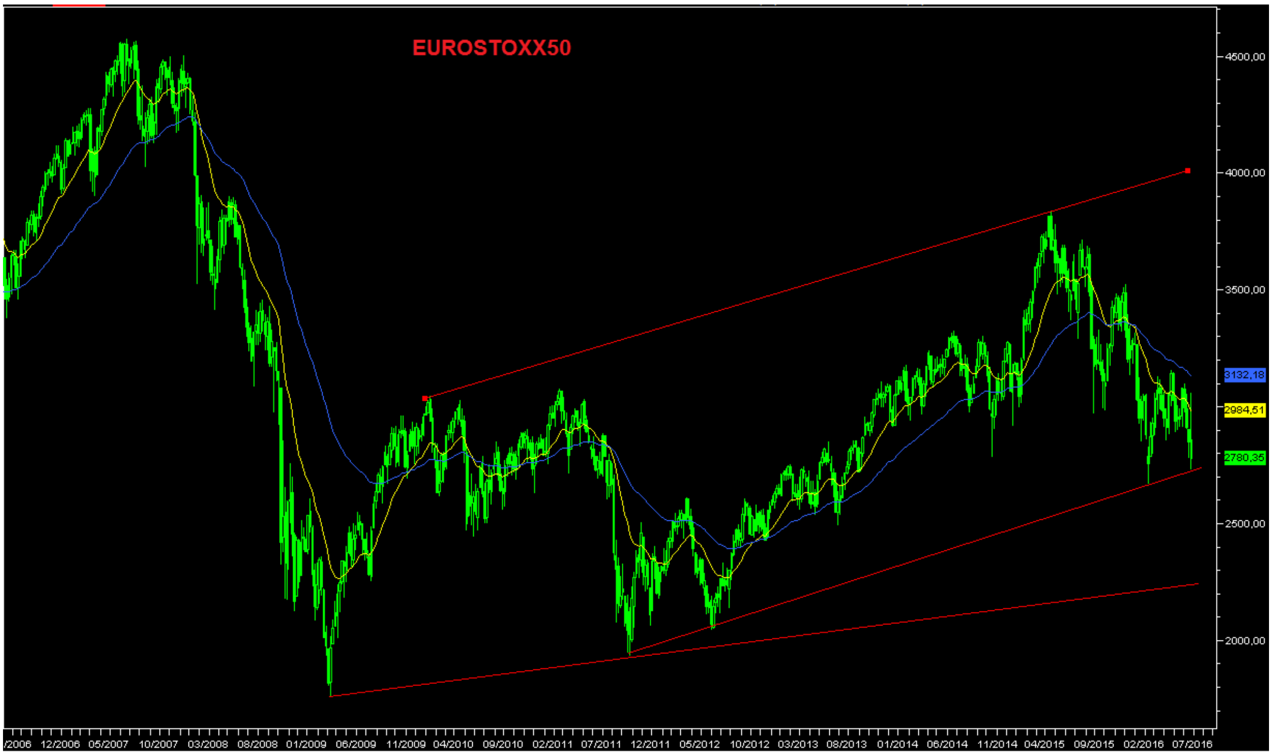
We expect that in the short and midterm foreign investments on the UK will decrease importantly. In this sense, recent depreciations of GBP could mark the beginning of a very negative trend for this currency as UK's current balanced is on deficit (around -5%). The winners could be Ireland and Luxembourg, which could serve as refuge of many financial institutions willing to keep the European passport.

Regarding the second factor, the readings are even more complicated. Populist parties, (with non-orthodox programmes and a non-euro approach) are gaining strength on the European political scene: This is the case of Le Pen in France and Wilders in Deutschland, which are already proposing to replicate UK's referendum on their countries.

In Italy, local elections showed that a Grillo-Meloni-Salvini coalition may be possible, which could add uncertainty to the European scenario. In the case of Spain, last Sunday Rajoy's center-right People's Party (PP) emerged on elections but fell short of a majority, leaving Spain at risk of another political stalemate.

Consequently, we consider the biggest current risks for European markets are not economical but political. This explains why Italian and Spanish markets have retreated even more than UK stocks in the last days. **We hold a defensive approach, keeping mid/high hedging levels although short upward corrections are feasible.**

Technical View: European Stocks



On Friday, Eurostoxx found support on the mid-term trend line around 2750 points. Today the index migrates to 2720. If risk perception continues, next trading days could take the index to 2300 points (next support level).

Disclaimer

FINLABO MARKET UPDATE IS PUBLISHED BY FINLABO RESEARCH, THE RESEARCH TEAM OF FINLABO SIM SPA
The information contained in this document is for general information purposes only. The information is provided by Finlabo and while we endeavor to obtain information from valid sources, we make no representations or warranties of any kind, express or implied, about the completeness, accuracy, reliability, suitability or availability with respect to the information. This report and its content is copyright of Finlabo Sim. All rights reserved. Any redistribution or reproduction of part or all of the contents in any form is prohibited.