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U.K. voters approve “Brexit,” triggering uncertainty

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U.K. voters have decided that Great Britain should leave the European Union (EU), capping a high-stakes, emotionally charged debate.

Market volatility in the immediate aftermath of the Brexit vote is to be expected, as investors often fixate on global macro events at the expense of longer-term economic trends and market fundamentals.

Despite the vote, favorable economic indicators suggest that Europe is on an improving growth path, while European equity valuations represent attractive long-term investment opportunities.

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By a margin of 52% to 48%, U.K. voters have decided that Great Britain should leave the European Union (EU). This result capped a high-stakes, emotionally charged debate between those who believe EU membership confers the benefits of economic strength and free trade against those who favor greater national sovereignty and independence from the EU.

The closeness of the vote was not surprising, as a number of public opinion polls had shown the race between the “leave” and “stay” camps as statistically too close to call, up until the night before the referendum. British Prime Minister David Cameron, who spearheaded the effort to keep the U.K. within the EU fold, acknowledged what for him was a difficult outcome and said the will of the British people “must be respected.” Meanwhile, Nigel Farage, the leader of the U.K. Independent party and a long-time opponent of the EU, proclaimed, “June 23rd will go down in history as our independence day.”

The result puts Europe in uncharted territory, as no country has ever left the EU before. What is certain, though, is that changes will not occur overnight. The British government must invoke Article 50 of the Lisbon Treaty before the exit process can begin, and the timing of that step has yet to be determined. Once Article 50 is invoked, the government has two years to complete the withdrawal. (An extension beyond two years is possible but would require the unanimous consent of the 27 other members of the EU.) The bottom line is that it will take several years for all of the necessary negotiations and agreements to be crafted and implemented before “Brexit” is realized. Over time, economies and markets will have an opportunity to adjust to new realities—a process whose ultimate outcomes no one can predict now.

A significant post-vote challenge will be heightened political uncertainty, both within the U.K. and for the EU as a whole. Prime Minister Cameron has announced that he will step down by October, setting the stage for elections in which Brexit supporters could assume leadership of the government. In other European countries—notably Spain, where a June 26 general election is

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scheduled—there are factions that want to leave the EU and may now seek to capitalize on any “leave” momentum from the Brexit result. While not necessarily poised for major victories, a growing chorus of “Eurosceptics” has prompted core EU members such as France to consider closer integration of the union as a defense mechanism. France has also vowed to impose harsh terms on the U.K. should it choose to leave the EU, thereby creating a disincentive for other potential defectors.

How are markets responding?

Not surprisingly, initial market reaction to Brexit has been negative. U.K. and Eurozone stocks are down sharply today, as are the British pound and the euro. U.S. stock futures pointed to steep opening losses, while Treasuries and other safe-haven assets have benefited from a flight to quality amid the anxiety.

That said, short-term volatility is inevitable whenever markets fixate on the uncertainty surrounding global macro events and developments at the expense of longer-term economic trends and market fundamentals. Despite the vote, there are favorable economic indicators suggesting that Europe is on an improving growth path, while European equity valuations represent attractive investment opportunities. As always, we think investors are best served by remaining patient, diversified, and focused on the long term.

TIAA’s perspective on short-term market volatility

- Despite the potential for market volatility, investors should avoid making sudden changes to their portfolios in response to short-term market events.
- A sound approach is to adhere to a long-term investment plan that is tailored to individual investment objectives and risk tolerance.
- If you have concerns about whether your investments are still appropriate for your long-term needs, please consult a financial advisor.