

The Brexit Referendum: What's at Stake?

The so-called Brexit Referendum -- which will ask British citizens to decide whether they want the United Kingdom to remain a part of the European Union (EU) or to cut ties and go its own way -- will come up for vote on June 23. At stake are weighty economic and political issues that could also impact the global financial markets.

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For the UK, an Economic "In" or "Out" Debate

UK citizens who favor getting out of the European Union cite economic reasons as their main concern. "Out" supporters, weary of funding past bailouts of other Eurozone member governments and wary of potential economic burdens in the future, believe leaving the EU would be in their nation's best interest. Those in favor of staying the course suggest the opposite: that leaving the EU could seriously undermine the UK's economy and force the government to renegotiate its trade and investment relationships with EU member countries.¹ Each side has economic data to support its position.

The Macroeconomic Fallout

The overall economic impact of Brexit -- for the UK and the EU -- is difficult to quantify. While the UK accounts for just one-sixth of the EU economy, of the 28 member nations it is the second largest net contributor to the EU's operating budget, accounting for 5.8% of total expenditures, second only to Germany.² Yet because there are several unknowns and so many channels through which Brexit could potentially impact the economy, no comprehensive macroeconomic estimates have been established. Of the studies that have been published thus far, the majority find the impact on the UK would generally be negative and significant, while the impact on the rest of the EU would be smaller.²

Beyond Economics

There are other ways in which Brexit is already affecting the UK and the rest of the EU nations that may not be captured by any macroeconomic models:

Uncertainty -- For the UK, studies show that many businesses are concerned about the uncertainty surrounding the impending referendum. Once the votes are tallied -- and if the UK opts to leave the EU -- the process of establishing new relationships within the EU will likely be prolonged and generate new levels of concern.

Demographics -- As of the first quarter of 2015, approximately 1.9 million workers from EU countries were employed in the UK.³ Similarly, some 1.26 million UK

citizens are currently living and working throughout the Eurozone.¹ What a UK vote to leave the EU would mean for these populations is still unclear.

Political contagion -- Some of the tensions giving rise to the Brexit vote in the UK also exists to varying degrees in other EU member nations. If the UK leaves, reestablishes itself as an independent economic entity, and is seen to have succeeded, it could set a precedent for other EU members to try the same.

Should Investors Worry?

As the UK and the rest of Europe brace for the Brexit vote, Wall Street is also mulling the impact an "Out" vote could potentially have on the financial markets.

Some analysts argue that the risk surrounding the UK's potential secession from the EU has already been priced into stocks. Still, some fallout is to be expected if the UK does opt to leave the EU. The impact will likely be most prominently observed over the longer term as the macroeconomic impact of the shift plays out.

Uncertainty has already eroded the value of the British pound, which has been trading at historically low levels against the dollar in recent months.⁴ Similarly, investors should watch the movement of the euro in the days and weeks ahead as well as the stocks of companies with large exposure to the UK and/or Europe.

Which market sectors could be affected most by Brexit? Market watchers say British stocks and the banking sector in particular could be hurt by a potential slowdown in economic activity -- i.e., business investment and consumer spending -- at least in the short term. Yet such an eventuality could be a plus for U.S. financial sector stocks that compete directly with UK banks.

Generally, U.S. investment markets could be exposed to increased volatility as a result of Brexit. U.S. corporate investment into Britain totaled \$588 billion in 2014, more than double the amount invested into South America, the Middle East, and Africa combined.⁵

With much at stake, investors should maintain a close watch over their portfolios -- and stay in close contact with their financial advisors -- in the weeks ahead as events across the pond unfold.

¹ *Time*, "[These 5 Facts Explain the Debate Over Brexit](#)," February 4, 2016.

² Global Counsel, "[BREXIT: The impact on the UK and the EU](#)," June 2015.

³ The Migration Observatory at the University of Oxford, "[Briefing: EU Migration to and from the UK](#)," May 10, 2015.

⁴ TD Ameritrade, "[Trading the Brexit: Will U.S. Markets Feel an Impact?](#)" May 23, 2016.

⁵MarketWatch, "[Why U.S. investors should fear a 'Brexit'](#) " February 25, 2016.