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GLOBAL CONSUMERS: BREXIT OFFERS SOME OPPORTUNITIES BUT RAISES CONCERNS ABOUT EU FUTURE

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In the aftermath of the Brexit vote, the consumer stocks that we invest in have been particularly volatile. There was a sharp sell-off after the vote, followed by a strong rebound across global markets. This rebound was likely due in part to the view that monetary policy around the world will remain particularly accommodative along with an evolving view that the impact of Brexit will be limited beyond the UK.

The situation remains fluid. The immediate fundamental impact has been a significant decline in the British pound and initial signs of a slowdown in the UK economy. Beyond these immediate effects, we are also looking at the possibility that the referendum may create additional fissures within the European Union. That would have a more material impact on global markets.

In search of perceived safety amid an uncertain global economic environment, investors are rewarding defensively positioned consumer staples stocks that also benefit from low interest rates. Consumer discretionary stocks are more mixed due to several factors, including a decline in consumer confidence, a drop in commercial real estate prices and demand, the weaker pound and euro, and expectations that unemployment could climb in post-Brexit Britain.

We are seeing signs of investor caution amid uncertainty about the near- and long-term consequences of an exit. Within our portfolio, our initial moves have been to limit direct investment in companies with the majority of their business in the UK. Our exposure to the country will come primarily from investments in multinationals that, in some cases, actually benefit from the weaker currency. However, I will be on the lookout for consumer discretionary stocks with good fundamentals that are getting punished by an overly cautious market.

The more pressing concern is not the UK's defection from the EU, in part because the UK leaves a fairly small footprint on global trade. Rather, I am focused on whether other EU countries will follow the UK's defection. Any breakdown of the EU would have far-reaching negative consequences and put further downward pressure on consumer discretionary stocks. While I am seeing no strong signs of an imminent breakup of the EU, the small possibility of it occurring is on our radar.

Given the uncertainty surrounding the global economy's strength and the late-cycle nature of the economic expansion since the global financial crisis, we continue to have more of the fund weighted toward consumer staples. While staples valuations have become somewhat rich, we are still finding selected opportunities within the sector that offer reasonable value. We like consumer-focused stocks that have idiosyncratic performance drivers that are ideally independent of the broader economy where possible. I continue to look for the right mix

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of offensive and defensive, and cyclical and non-cyclical stocks that I believe will perform well in a variety of market environments.

As our portfolio is global, I think it's worth noting that the U.S. has been a bright spot compared with the rest of the world. Consumer confidence is higher compared with Europe, and employment and wage growth are ticking upward. Housing demand and prices are also on the rise. I believe these factors are supportive of certain consumer discretionary and consumer staples stocks. My view is that the U.S. and high-quality U.S.-domiciled multinationals offer more favorable opportunities compared with European and emerging markets regions, where the risks seem comparatively higher.

However, caution in the U.S. is warranted. The country is in its eighth year of expansion, and if history is a guide, the prospects of an economic downturn have increased. Given the chance of further economic weakness in Europe and particularly in the UK, a more defensively positioned portfolio is prudent.

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