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BEYOND BREXIT

CONTRIBUTORS

Owen Lock

Cheickna Moulaye

Tom Harrison

Xinran Liu

Ross McKenzie

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FOREWARD

The trade landscape post-Brexit: what's happening?

The UK has had a turbulent year; having voted to leave the European Union and seeing much political unrest with the prime minister resigning. The process has been anything but straightforward, as a formal exit did not start until Theresa May decided to trigger Article 50. This has meant that the two-years provided for negotiations has now commenced.

Due to the time it will take to exit the EU, there should not be any short shocks. A big fear is that of trade and how companies in the UK will be treated. This may have impacts on legal contracts and free movement of persons. However, we see that many SME's will actually hedge out the risk of the uncertain environment. If required; offices may be set up in the EU but this will all become clearer as negotiations progress. We see that it is important to understand how the land lies with the Euro; which is feeling this strain already.

Brexit Report from Trade Finance Global

The following report contains a few feature articles on some of the impacts we have seen following Brexit, and how political agendas, international relations, and foreign exchange volatility has shaped and could change Great Britain.

SME CONFIDENCE IN THE AFTERMATH OF BREXIT

SETTING THE LANDSCAPE POST-BREXIT FOR SMES

OWEN LOCK

The vote by the people of Britain to leave the EU single market on Thursday 23rd June 2016 had substantial implications for SMEs in the United Kingdom. Business Confidence measures across all platforms dropped to lows which had not been seen since the aftermath of the financial crisis in 2008.

In the immediate aftermath, the pound's value plummeted overnight (subsequently stabilising at a lower price on foreign exchange markets). The mechanisms through which Brexit has impacted the economy can be primarily attributed to two broad categories; uncertainty – particularly with regard to regulation (for example, passporting rights in Financial markets and free movement rights in the aviation sector), and the weaker value of the pound, and its subsequent impact on export markets, input prices and inflation. However, a sound understanding of the current economic climate in the UK must also be understood against the upward trajectory of fuel prices, and the wider environment of political uncertainty which has been a prominent feature of western economies in the past 12 months.

This post shall refer to the results of business confidence surveys issued by Lloyds, the ICAEW, and the FSB from Q1 and Q2 2017 to identify current sector trends, challenges facing SMEs in the UK, and the strategies being adopted to counter these.

Challenges facing SMEs in the aftermath of Brexit

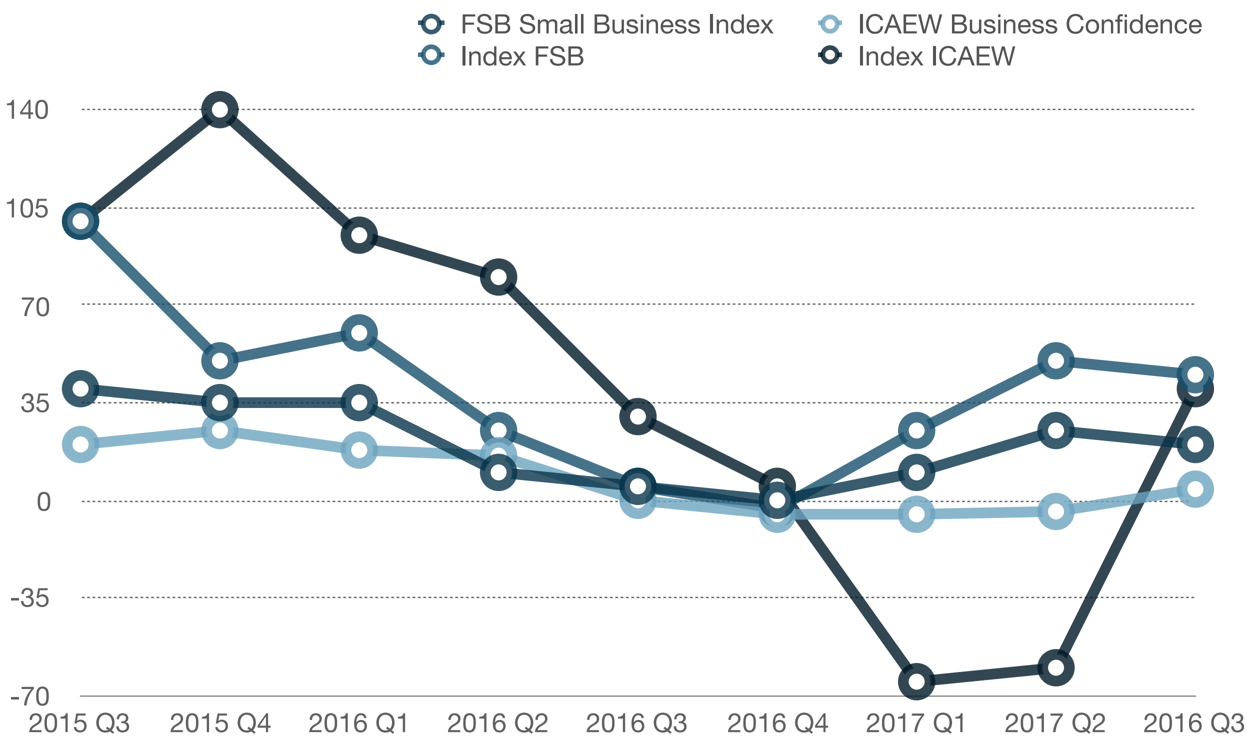

Figure 1: *data source - ICAEW and FSB Q2 business confidence surveys*[1]

[1] ICAEW and FSB Business Confidence Survey, 2016, 2017

Although the decline in confidence among SMEs following Brexit was nowhere near the scale of the collapse following the financial crisis in 2008, the results are nonetheless significant. The extent of pessimism following the election can be seen by the deterioration in confidence from Q1 to Q2 2016 in the graph above, most evident in the indexed versions of the FSB and ICAEW surveys (Q2 2015 = 100). The Lloyds survey demonstrates similar results in this period, with the banks business confidence index dropping from +38% to +12% over the course of the immediate period following the EU referendum. Although there has been some inconsistency between the forecasts of the FSB, Lloyds and ICAEW confidence index' in the aftermath of the election, all now have indicators at a similar level to before the referendum (Lloyds' index has subsequently recovered to +24% this quarter)[2].

A continued issue surrounding Brexit for the majority of SMEs is the high level of economic uncertainty which surrounds the Brexit negotiations. Departure from the EU single market poses problems for UK sectors which rely on EU regulation to service the European market. The most notable example of this is in Financial Services, where London has previously been the hub of choice for the majority of major international banks to service European clients. However, concerns over regulation post-Brexit has caused companies such as Morgan Stanley and JP Morgan to relocate staff to locations within the EU such as Frankfurt and Dublin, leading to expectations of falling rates of new hires within financial services in the UK (according to the ICAEW survey).

The greatest impact of Brexit in the short term is likely to continue to be felt through the devaluation of sterling. Figure 2 shows the devaluation of sterling in the aftermath of Brexit, with the British pound currently trading at approximately 90% of its value prior to the EU referendum against both the dollar and the euro. The weaker pound has directly impacted sectors who rely on imports from abroad in their business, with input prices rising as a result. These rising input prices, combined with increasing commodity prices (particularly in fuel markets) and persistent low interest rates set by the Bank of England has subsequently created inflationary pressure, with CPI currently standing at 2.7% - near to the upper limit of the Bank of England's target range of 1-3%[3]. This inflation has increased the cost of living for consumers, at a time where wage growth stands at less than 1% per annum (as shall be referred to in the next section), resulting in profitability being increasingly difficult to maintain for sectors which are consumer-facing. This cocktail of conditions can explain the subdued conditions in the services sector, with growth declining from 0.8% in Q4 2016 to just 0.3% in Q1 2017. The most challenging conditions as a result of the depreciation can be found in the Retail sector, where rising input costs, combined with fierce price competition and falling consumer spending power have eroded profit margins. It is therefore no surprise that the FSB survey has SME confidence within retail at a lower level than any other sector (-9%).

The devaluation of the pound combined with positive economic performance in the global economy has also been important in creating opportunities in the export sector. A devaluation in the pound improves the competitiveness of UK goods in global markets, with the fallout from this visible in the Lloyds Q2 2017 survey result that 29% of firms anticipate higher total exports in the next 6 months. This export-led growth can help explain the upturn in fortunes for the UK manufacturing sector, in which the FSB confidence indictor currently

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[2] Lloyds Business Banking Confidence Index (http://www.lloydsbankinggroup.com/Media/Press-Releases/2016-press-releases/lloyds-bank/business-confidence-at-highest-level-since-march/)

[3] Consumer Price Index, ONS (https://www.ons.gov.uk/economy/inflationandpriceindices)

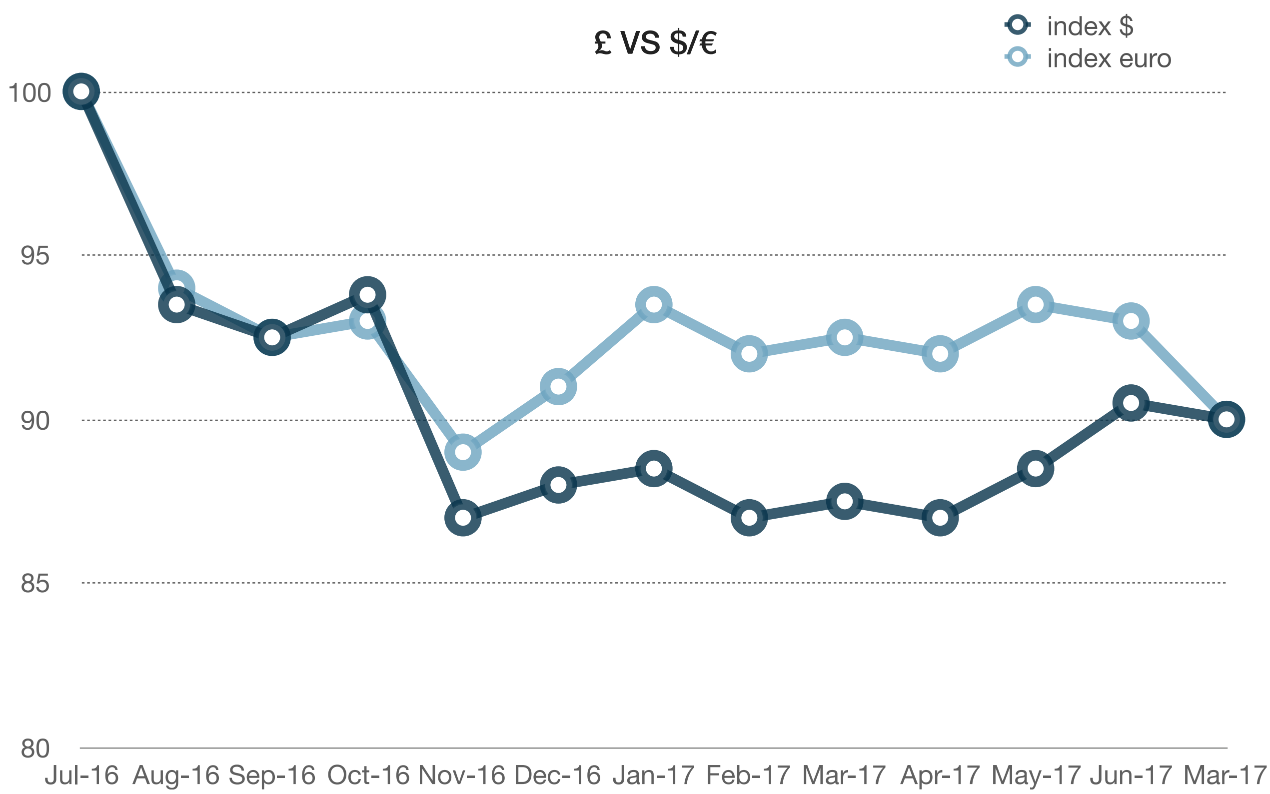

Figure 2: *data source - x-rates.com*

stands at +38% (a result which indicates a large proportion of firms anticipate improved performance in the next 12 months).

Current strategies adopted by SMEs

In the face of rising input costs due to a weaker pound and rising fuel prices, combined with low consumer confidence, many consumer-facing SMEs are looking to maintain profit margins by controlling labour costs. The FSB Q2 survey[4] found that SMEs on average only intend to increase wages by 1.6% in the coming year, with real wages anticipated to fall for the first time since 2013. This strategy is having an inverse effect on consumer confidence (the GfK NOP consumer confidence index[5] registered -7 in April), with the retail sector in particular negatively impacted as a result of consumers having less income to spend on discretionary goods. An increasing number of SMEs are also passing on price increases to consumers, although once more for competitive sectors such as retail the options to do so are somewhat limited. One challenge that persistent growth through low unemployment has created for SMEs is maintaining strong levels of productivity. The strategy to consistently invest in personnel, rather than high tech machinery, has resulted in the UK falling behind global competitors in the US, Germany and France on productivity ratings, and with strong growth in the domestic tech sector, this may be an avenue that SMEs may wish to consider in the immediate future to maintain an efficient cost structure.

A number of sectors are also experiencing positive levels of capital investment, particularly within IT. This has been aided by excellent conditions within domestic credit markets, with 74% of applications for credit among

[4] FSB Voice of Small Business Index, Q2 2017 (http://www.fsb.org.uk/docs/default-source/fsb-org-uk/fsb-sbi-q2-2017-final.pdf)

[5] GfK NOP Consumer Confidence Index (researchbriefings.files.parliament.uk/documents/CBP-7959/CBP-7959.pdf)

SMEs accepted this quarter according to the FSB survey. Furthermore, 46% of these credit extensions were at low rates of 4% or less. The positive state of the credit market for SMEs can be attributed to the increasing diversification of financing methods, as SMEs increasingly opt for asset-based finance methods such as invoice financing, rather than traditional bank loans.

Summary

With a high level of uncertainty likely to persist in the UK economy for the duration of 2017, efficient cost structures would appear to be the key avenue to maintaining profitability. Hedging against volatility risk in commodity markets would appear to be a sensible strategy for many, particularly in sectors with high levels of price competition such as transport. There remains a risk of further movement of the pound against the dollar and more notably the euro, with major political events such as the progression of Brexit negotiations and the German general election likely to impact on FOREX markets. Subsequently, SMEs with cost structures highly dependent on international trade may wish to mitigate some risk in this area. However, the greatest political risks for 2017 in the form of the UK and French national elections have already been negotiated with positive outcomes for market stability. ■

Owen Lock

T: @owen.lock7

Economics graduate from the University of Warwick

UNCERTAINTY: THE WATCHWORD OF BREXIT

THE STATE OF POLITICS AND BUSINESS POST BREXIT

CHEICKNA MOULAYE

On 29th March 2017, Theresa May triggered Article 50 and irrevocably executed the will of the British people to exit the European Union. In order to strengthen her majority and be able to negotiate a better Brexit deal for Great Britain, Theresa May called for an early Snap Election which was approved by the parliament. However, the outcome of the election was not the one that was expected by May, as the Tories lost their majority which weakened Great Britain's negotiating power right at the beginning of the Brexit negotiations in European Parliament.

A month after the reception of Theresa May's letter expressing the will of the British people by the European council, its president Donald Tusk convened the members of the council in order to, according to Mr Tusk, "adopt the EU's draft guidelines for Brexit negotiations".

Both parts, the EU and Great Britain, agreed on the fact that talks should last until 2019 but in the meanwhile, Brexit's effects on the economy are starting to become apparent.

Uncertainty: The watchword of Brexit

According to the national chairman of the Federation of Small Businesses Mike Cherry, "not enough attention is being paid to the plight of SMEs in the Brexit negotiations". Indeed, the export-based SMEs might need the most a safe and facilitating deal between the two sides because of all the uncertainty surrounding the triggering of Article 50.

Even though only 10% of them export directly to the EU according to the Department for Business, Energy & Industrial Strategy, the FSB is aware that export-based SMEs have a greater chance to be affected by the adversity post-Brexit, and that they "need the Government to enhance specific support for small exporters to reach new customers and to negotiate ambitious UK-specific trade deals with large and emerging markets."

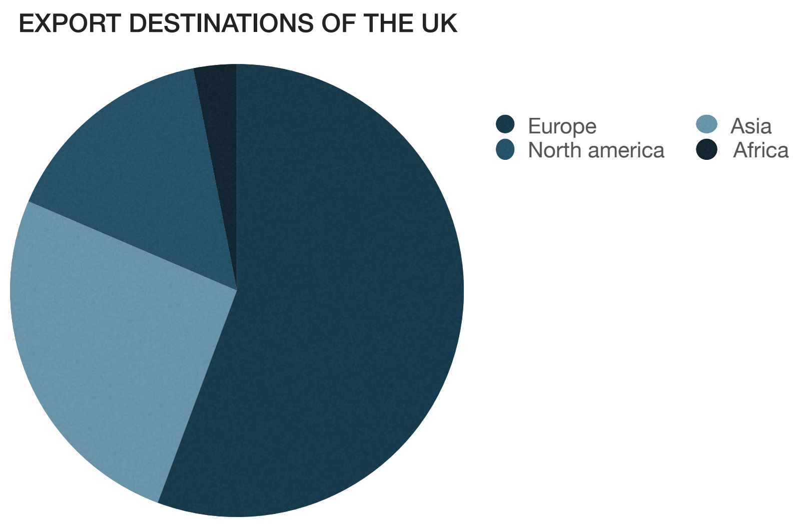

Figure 1: *Export Destinations of the UK. Source: [Atlas]*

Great Britain always had a particular relationship with the EU as it wasn't part of the monetary union (euro) and the Schengen area. However, having access to the single European market at no cost was and is still something essential for the British economy as more than half of its commercial partners are within European borders.

The growing uncertainty around the Brexit may cause important industrial groups and multinational companies to outsource and therefore could create a "domino effect" on SMEs due to the connected structure of the economy. The spokesperson of the FSB, Louise Stewart, stated in an interview for the French website latribune.fr following the 2016 vote that "small companies often depend on big companies to survive. With the current uncertainty, it is possible that small businesses might be weakened"[6].

In addition of the effect seen above, Brexit might cause a "brain drain" out of Great Britain. According to the ONS, 2.2 millions of UK workers are EU nationals which is around 7% of the total working population and a Deloitte study found that 47% of the highly skilled workers EU nationals are considering leaving the country due to the actual climate of uncertainty[7]. A study from Deloitte raises that the contribution of non UK national on the British economy and even on its society and therefore shows how Brexit could have consequences beyond the monetary and economic sector.

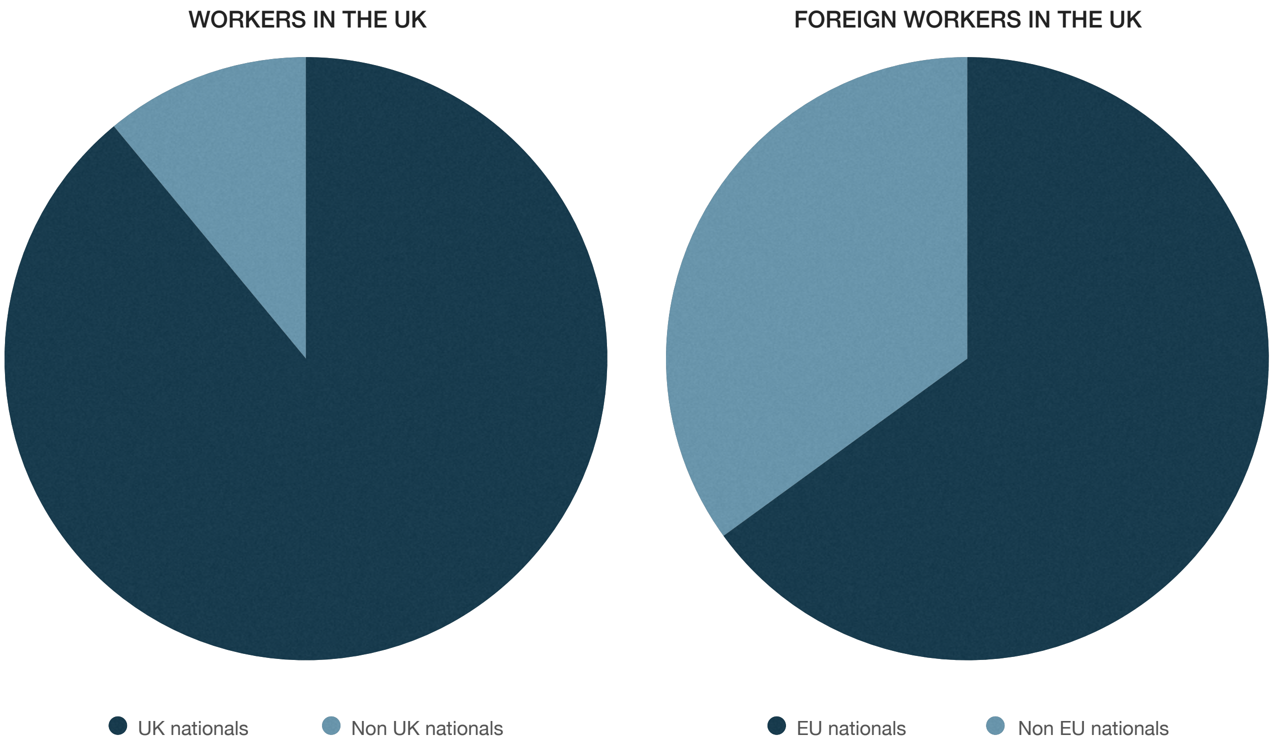

Figure 3: *ONS Data on Workers in the UK and Foreign Workers in the EU, Source: BBC*

[6] La Tribune Interview: http://www.latribune.fr/economie/international/brexit-les-interets-des-pme-britanniques-ont-ete-oublies-582115.html

[7] Office for National Statistics: http://www.bbc.com/news/uk-politics-39576112

Finally, even though the overall collapse of the pound since June 2016 has balanced the SMEs uncertainty surrounding the Brexit, it is still there because of the rarity of the situation as Dr Angus Armstrong, the director of the French national institute of social and economic research mentions; “Never a country as big as the UK exited such a union. In other words, there’s no precedents which allows us to draw lessons.”

With those uncertainties remaining, confidence is mixed but there's a real danger that the needs of SMEs will be overlooked during the negotiations. ■

Cheickna Moulaye

Cheickna is an economics graduate from the University Paris 1 Panthéon-Sorbonne.

CORBYN VS. MAY

THE ATTITUDE OF THE 2017 LABOUR & CONSERVATIVE MANIFESTOS TOWARDS GLOBAL TRADE AND BUSINESS FINANCE

TOM HARRISON

Brexit will fundamentally change the UK's conditions of trade with the other 27 EU Member States, and with over 60 countries with which the EU has preferential trade agreements… Minimising disruption to trade between the UK and the EU-27 after Brexit is crucial to the UK's future prosperity.

(HL Paper 129)[8]

This is the opening of a recent House of Lords paper concerning Brexit and trade. It is clear that the next two years will be a vitally important period of British history as the Article 50 talks are carried out, uncoupling the UK from the European Union. With the recent snap election, Brexit features prominently in both the Labour and Conservative manifestos.

One particularly pressing area of policy that must be addressed is international trade policy. By definition, the UK must change its international trade policy post-Brexit as it will no longer be a part of EU trade agreements. This article looks at the attitude of Corbyn and May towards international trade as outlined in their respective manifestos.

Trade Relationships with Europe

As shown in Figures 1 and 2, for the beginning of 2017 (January to April), 52% of UK imports and 47% of UK exports have been with the EU. Negotiations that result in a break down of the UK-EU relationship could be extremely damaging for UK trade due to the likely high tariff and non-tariff barriers that would come into force.

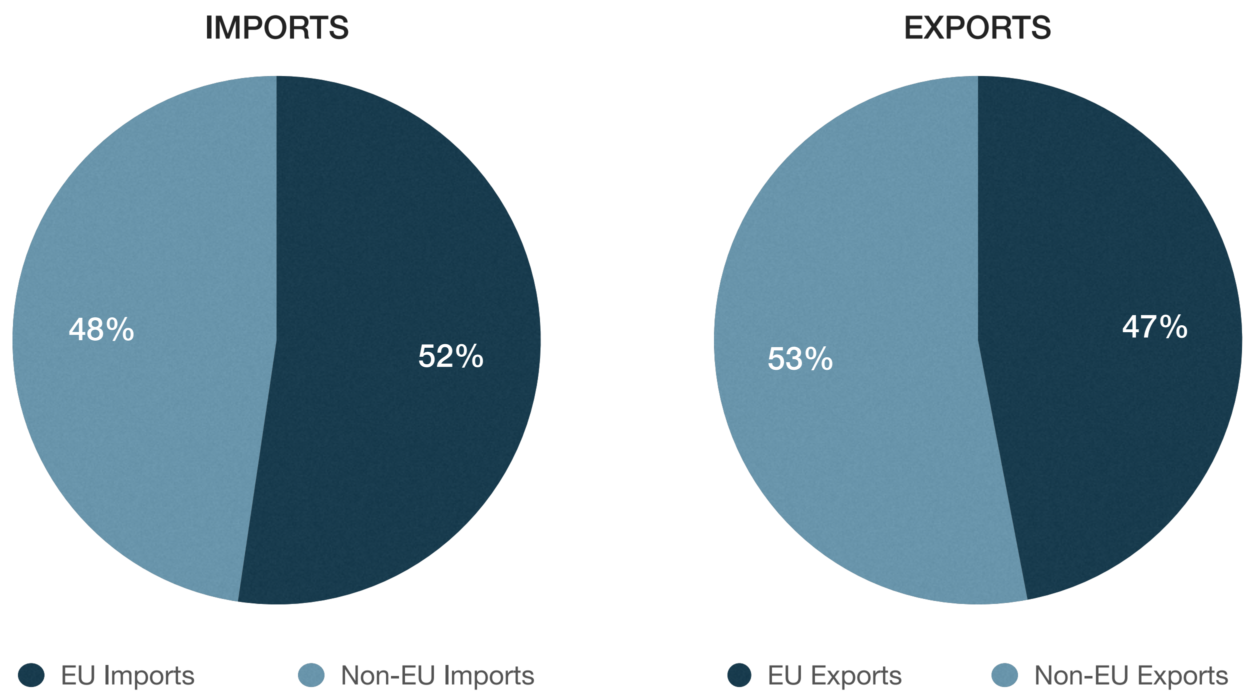

Figure 1 & 2: *Proportion of the UK's Imports & Exports to the EU vs. Non-EU countries (Year to Date 2017)*

[8] House of Lords - EU Paper (https://www.publications.parliament.uk/pa/ld201617/ldselect/ldeucom/129/12903.htm)

Both parties outline clear intentions for maintaining a good trade relationship. The Conservatives state that "while we are leaving the European Union, we are not leaving Europe". The UK will still be a European country and will still be on close terms with their former partners. Despite this, however, the Conservatives do make it clear that they view 'no deal' as a better outcome of the Brexit talks than a bad deal. Whilst ministers claim that this result is unlikely, if no deal is agreed upon then the World Trade Organisation rules would come into force; an outcome that many claim would be damaging to the UK economy[9].

Labour go further in their desire to remain close to the EU stating that they plan to scrap the Conservative's Brexit White Paper and replace it with negotiating priorities that place "a strong emphasis on retaining the benefits of the Single Market and the Customs Union". In contrast to the Conservative's position, Labour also state that no deal is the worst possible outcome of the Brexit talks.

The Conservatives more hard-line approach to the negotiations could well be a tactic that recognises the value that the UK brings to the EU in the form of its trade deficits. For example, the UK has a £13.95 billion deficit in the trade of cars with the EU, £10.85 billion of which is with Germany. Compromising this relationship would be harmful to both UK and European businesses and therefore undesirable for both sides[10].

An Opportunity for New Relationships

Once the UK has completed its departure from the EU it will no longer be bound under EU trade legislation. This means that it will not be prohibited from making individual trade deals with non-EU countries or trade areas. However, the EU trade deals it has been a part of will also no longer apply. Therefore, it will be necessary for the ruling party to establish new relationships with the rest of the world. Because of this both parties place a large emphasis on this topic in their manifestos.

Again both parties take a similar position, outlining their desire to establish the UK as a global economy. The Conservatives believe that "the UK must seize the unique opportunities it has to forge a new set of trade and investment relationships around the world, building a global, outward looking Britain". This support for global trade liberalisation is emphasised in their Brexit White Paper.

Labour outlines a slightly more reserved position indicating that "the UK's future prosperity depends on minimising tariff and non-tariff barriers that prevent us from exporting and creating the jobs and economic growth we need". Whilst it is not as deep a commitment as the Conservative's free trade ambitions, it is still a clear indication that they would strive for strong trade agreements across the globe.

The Effect on Small & Medium-Sized Enterprises (SMEs)

Making up 99% of businesses, 60% of private sector employees, and 47% of business turnover, SMEs constitute a vital part of the UK economy. The figure below indicates the extent to which SMEs account for UK private sector employment and turnover in two of the key exporting industries. In both cases they generate a large proportion of jobs and revenue for the UK economy.

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[9] **Blitz, J.** (2017) 'The danger of no Brexit deal to UK economy', *Financial Times*, [Available at: https://www.ft.com/content/9a1109a0-452c-11e7-8d27-59b4dd6296b8?mhq5j=e1]

[10] Office for National Statistics - https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/timeseries/l7d7

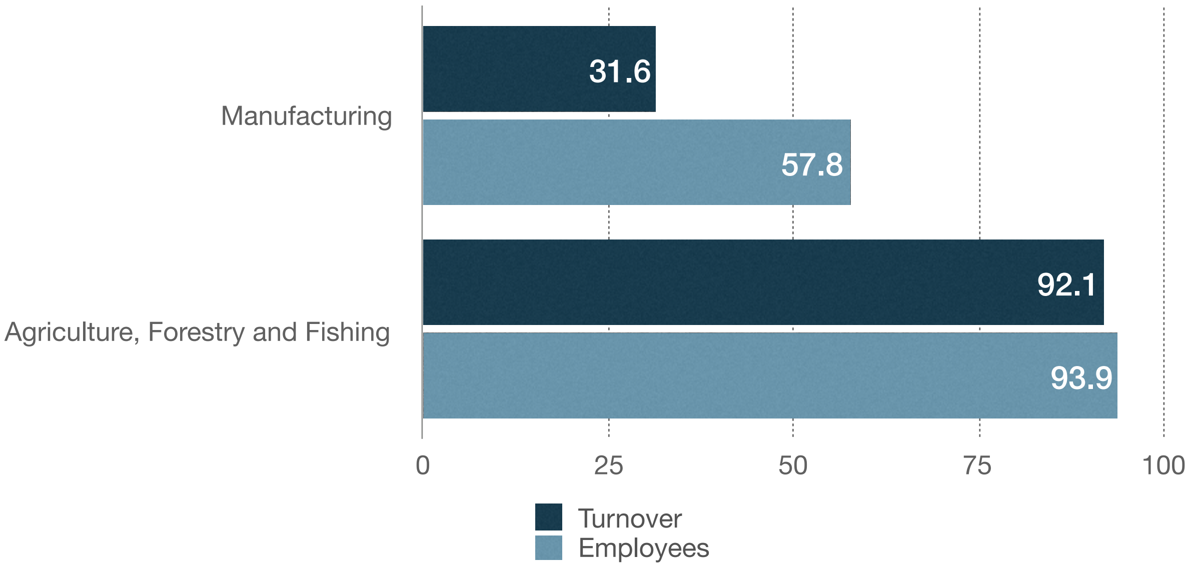

***Figure 4**: SME Turnover & Number of Employees as a Percentage of All UK Private Sector Businesses*

Both parties appear to be cognisant of the importance of SMEs to the strength of the economy and therefore both discuss the importance of policies and trade agreements that encourage these businesses.

The Conservative manifesto states that it is the party of the the entrepreneur: “We understand that small businesses are the wellspring of growth”. Whilst they are not as explicit as Labour in outlining a desire to protect the interests of SMEs in the Brexit negotiations, they do state that they will be seeking a comprehensive free trade and customs agreement. Furthermore, they propose to enact a Great Repeal Bill which will include the conversion of EU law into UK law. This bill is particularly reassuring for SMEs who export to EU countries as it will allow for them to “go about life knowing that the rules have not changed overnight.”

Labour state that they will “champion the export interests of SMEs” and “support their market access needs” when negotiating new trade agreements. Moreover, they propose to develop an “export incentive scheme for SMEs based on international best practice”, and to “ring-fence Tradeshow Access Programme grants to help SMEs reach new customers around the world”.

Export Finance

Whilst attracting less coverage within the manifesto than the areas discussed above, both parties show an understanding of the importance of export finance for facilitating trade.

The Conservatives[11] state that they will “put UK Export Finance… at the heart of the UK’s trade promotion proposition” ensuring that “no viable UK export fails for lack of finance or insurance”. And Labour “will use the full range of export credit, finance, insurance and trade promotion tools to boost British exports and support priority industrial sectors.”[12]

[11] Conservative Manifesto - https://www.conservatives.com/manifesto

[12] http://www.labour.org.uk/page/-/Images/manifesto-2017/Labour%20Manifesto%202017.pdf

Summary

In summary, in terms of trade the Labour and Conservative manifestos are more similar than would perhaps be expected. The Conservatives outline a slightly more aggressive approach to the Article 50 talks, and a greater desire to establish free trade agreements with non-EU countries, however, Labour are more explicit in their support for SMEs and in ensuring that they arrive at trade terms which are suitable to these types of businesses. ■

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Data

https://www.gov.uk/government/statistics/business-population-estimates-2016

https://www.uktradeinfo.com/Pages/Home.aspx

Tom Harrison

MSc in International Business at the University of Birmingham

CHINA'S RELATIONSHIP WITH BRITAIN POST BREXIT

XINRAN LU

On June 24th 2016, The final outcome of the British referendum came out as a total shock - the 43 years of "marriage" between British and the EU were officially over. There was temporary chaos in overseas financial market: The Hong Kong Hang Seng Index fell below 6%, while the Nikkei 225 index fell below 8%, and so did the Chinese stock market.

Now, one year later, after Theresa May barely survived her first parliamentary test, the road to Brexit can hardly take on this harsh approach. One year later, we look at where the relationship between China and Britain has gone - what is the impact of Brexit on bilateral trade?

Historic trade between China and UK

HEATING UP THE RELATIONSHIP

With the continuous development of Chinese-British economic relationship, the trade relationship between China and UK is heating up. As for the exporter to the UK and importer from the UK, China has become the second largest and fourth largest UK trade partners respectively, when compared to other countries and regions. Also, compared to other EU countries, the UK has now become the third largest importer from China, and the second largest exporter to China. However, the Brexit negotiations are still in progress, so it might have a both favourable and adverse effects on Chinese-British trade.

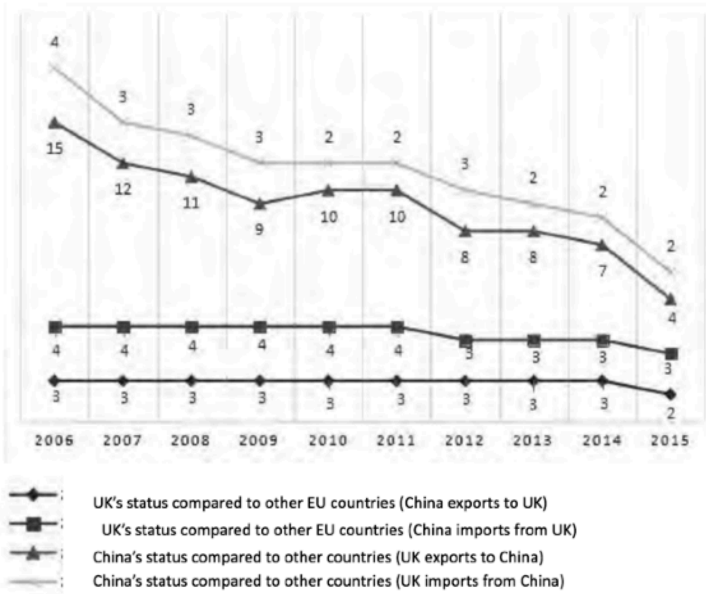


Figure 1*: Import and Export stats between China and the UK*

In recent years, the UK's import and export volume of China's goods trade has been increasing year by year, from $ 41.83 billion in 2006 and $ 6.04 billion in 2006 respectively, to $62.98 billion and $27.63 billion in 2015 respectively. To put it in percentage terms, it was an increase of 50.6% and 358% respectively. For UK, the volume of exports to China has increased by more than the increase in imports, net exports of goods declined year by year, from $ 520 billion in 2011 to $ 354 million in 2015.

How can Brexit be a propeller to China-UK trade relationship?

After the referendum in Britain, in early October 2016, Chinese ambassador to Britain Liu Xiaoming proposed that China and Britain should sign a free trade agreement. British International Trade Minister Liam Fox expressed support for free trade agreement between China and UK[13]. He believed that such trade will bring great opportunities to the UK. Before Brexit, EU is Britain's largest trading partner. After it, Europe's market share in the EU may be reduced due to higher EU trade market access conditions.

Brexit: a double-edged sword

A POSITIVE SIDE

Brexit could be a double-edged sword for the relationship between China and UK. Britain has been one of the ideal destinations for China's foreign investment in recent years. For Chinese companies, Britain's attraction is not limited to the UK's own market of 65 million people, but also a portal to the EU market. After Brexit, Chinese companies will need to reconsider this strategy and make the appropriate adjustments. The positive side is that after leaving the EU, the United Kingdom will be able to establish a closer economic and trade cooperation with China. On the one hand, the depreciation of the pound may lead to an increase in Chinese imports from the UK at a lower cost. This may also ease the negative impact of reduced exports to the EU market.

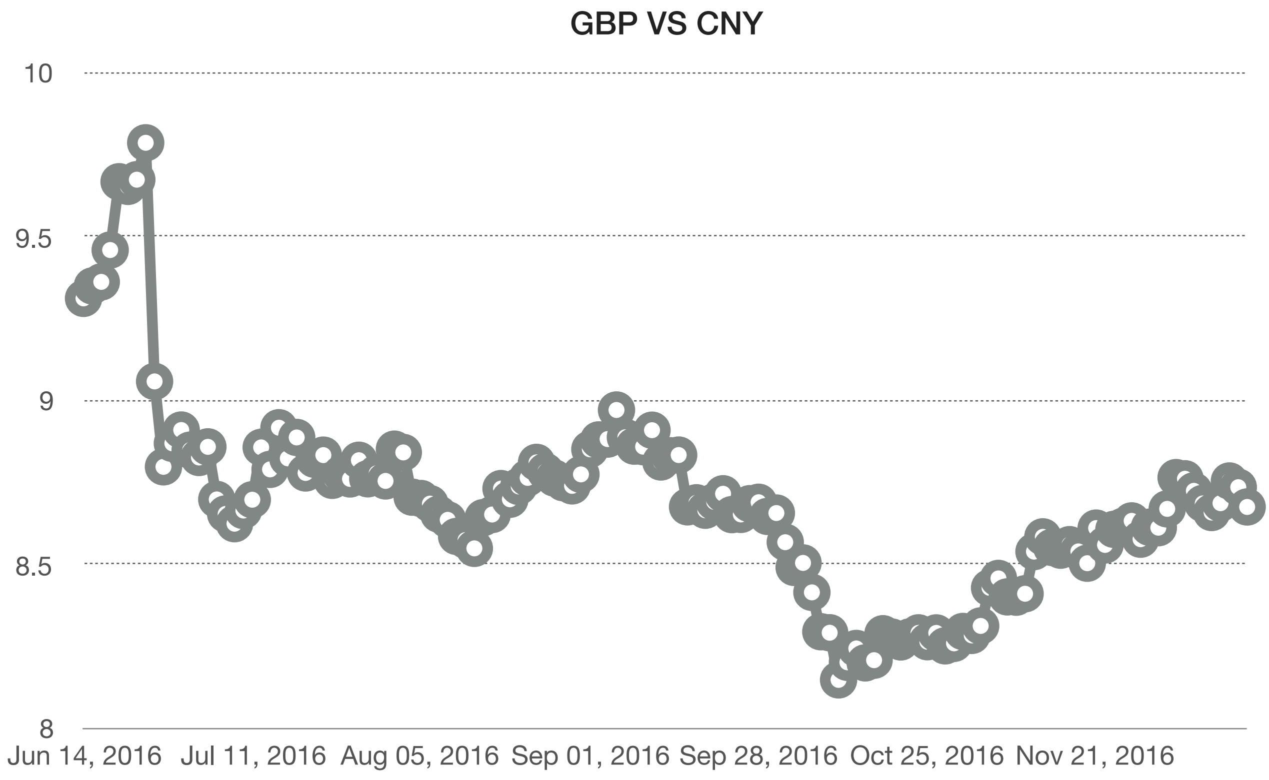


***Figure 2**: GBP versus RMB June 2016 - Nov 2016*

[13] Financial Times (https://www.ft.com/content/71f43baa-96e9-11e6-a80e-bcd69f323a8b%22%20%5Cl%20%22comments)

We can see from Figure 2, that from the day of referendum, the exchange rate between Pound and RMB fell from 9.8 to 8.77 in June. In the next few months, the exchange rate was in a volatile decline. In October 31st, 2016, the exchange rate fell to the lowest point 8.24 in 10 years. In November it increased significantly, but exchange rates between Pound and RMB has not been able to return to the level before the referendum.

A NEGATIVE SIDE

The negative side might be that after Brexit, Chinese enterprises would need to meet the criteria of both Britain and EU standards when exporting, which add inevitable complexity. Although the British Standards Association (BSI) issued a statement that the United Kingdom will continue to follow the EU standards, in practice, the British standard are most likely to be adjusted[14]. If the standards change, it would result in higher costs for Chinese enterprises.

Also, uncertainty in the UK has led to a reduction of investment in the oil industry, an increase in operating costs for oil companies, and heightened trade risk in the Scottish region, which is detrimental to the UK's exports to China. Brexit will increase investment in UK energy infrastructure and new projects are likely to be postponed. The UK will further reduce investment into the oil industry, which reduces British oil exports to China. As for the oil industry operating costs, the depreciation of the pound will decrease the operating costs in the short term, but in the long term, it may incur more costs due to the uncertain political environment.

Summary

The impact of Brexit could bring both opportunities and challenges for China and the UK. Brexit will enhance the cooperation between China and the UK in economic and trade fields, achieving a mutual benefit for both sides. As one of the core developed economies in the EU, Britain had played an important "stabilizer" role in economic and trade relations between China and the EU. After Brexit, the trade relationship between the EU and China will be more fragile and unstable in the face of economic crisis and other negative impacts. ■

Xinran Liu

T: @leahlxr

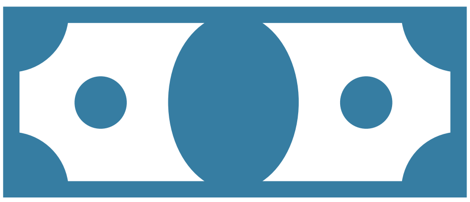
Xinran Liu is currently studying MSc Financial Economics in University of Birmingham,

[14] British Standards Association Statement (https://www.ft.com/content/71f43baa-96e9-11e6-a80e-bcd69f323a8b%22%20%5Cl%20%22comments)

BREXIT'S AFFECT ON THE CURRENCY MARKET

"POLITICS IS THE NEW ECONOMICS"

Ross McKenzie



With the more commonly known Forex Market operating with an average of $5.2 Trillion dollars exchanged per day, what role has Brexit played since the announcement (some 13 months previous at the time of writing).

Why would Brexit Affect the Currency Market?

Volatility creates margins in which money is made in the financial markets. The more volatile in a market, the more room there is for traders to profit.

The Forex markets are well-known for volatility, which is why it attracts such a large portion of global investment.

Another important aspect of the forex market is the fact that it is largely focused on the short-term. This means when uncertainty is introduced, the result is mass-sell off, which then of course leads to a sharp decline in the price of the currency.

George Soros, seen as one of the most successful investors in the world, explains Brexit's importance well in his famous quote "Volatility is greatest at turning points, diminishing as a new trend becomes established".

Brexit was indeed a huge turning point with its implementation affecting all aspects of the macro economy – for more information on what Brexit meant for trade finance, see Trade Finance Global's "Brexit and the EU Referendum"

Because today's monetary system involves fiat currencies – intrinsically worthless paper, backed by governing bodies; uncertainty surrounding currencies can cause further volatility. This often pushes more investment toward commodities with an intrinsic value such as gold. Gold's reaction to the Brexit announcement is explained in our article "Gold's performance in 2017".

To put it simply, because Britain and its operations were so well intertwined with European legislation and the Single Market, the prospect of a complicated departure triggered by the starting of Article 50 caused (and continues to) great uncertainty surrounding both the Pound and the Economy.

"Politics is the New Economics"

Writing for Business Insider UK, Will Martin brought to light research carried out by HSBC, in which they found it was politics, not economics that drove large fluctuations in the global currency markets. Forex analysts at the bank have included Brexit in their examples of currency-fluctuating political events, and said that the reactions of the markets to the election of Donald Trump "cemented their belief".

£ vs € - The story so far

Predictions made pre-Brexit were not positive for the Pound. Because Britain's national debt is so high (1,682.8 billion, equivalent to 85.3% of GDP to be precise), if separation from the EU and the Single Market triggered a recession, the UK may default on its repayments. To avoid this, we will likely see expansionary monetary policy – usually the lowering of interest rates. Further detail on the outlook of the pound post-Brexit is available on our article "British Pound Outlook". In summary, expectations of the Pound's decline were based around negative expectations of the economy such as slowed growth and cost-push inflation. It also

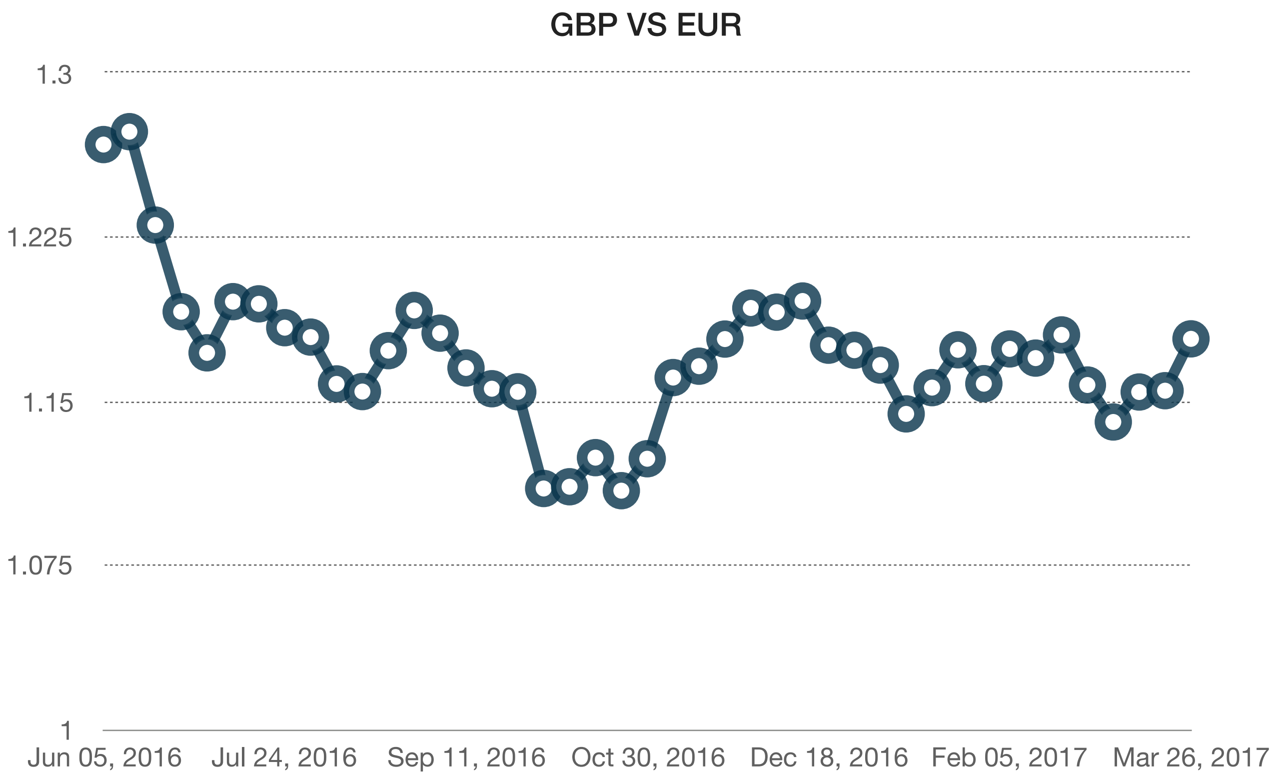


***Figure 1**: GBP vs EUR, Source: Financial Times*

highlights The Bank of England's Governor Mark Carney's announcement shortly after Brexit, warning that monetary easing is set to come into action.

With a lower rate of interest, we will see the pound traded less, leading to a lower performance over the Euro. This is shown in the below GBP/EUR graph.

GBP/EUR Since Brexit

In Figure 1, we see GBP/EUR levels fall significantly after Brexit, but more importantly, levels have remained deflated for the Pound sterling. Pre-Brexit saw the Pound at €1.30, then down to €1.09 four months down the line. A 16.15% fall in the Pound, with roughly half of that fall happening on the three days following the announced result.

The lowest it fell to was the Flash crash on 6th October, where the Pound fell 6.1% within minutes, but corrected itself soon after. This is believed to be algorithmic trading, which is the process of using computers that are specifically programmed to execute certain trade orders under specific conditions. According to Bloomberg, there were certain trades done in Asia during their trading hours, including the pound which were triggered by an algorithmic trade.

A weaker pound has had a real impact on many companies nationwide. Because imports became more expensive, we are seeing cost-push inflation in the economy. Cost-Push Inflation means that the general price level is pushed higher as producers/ suppliers have increased costs due to higher prices for inputs, which are passed onto the consumer.

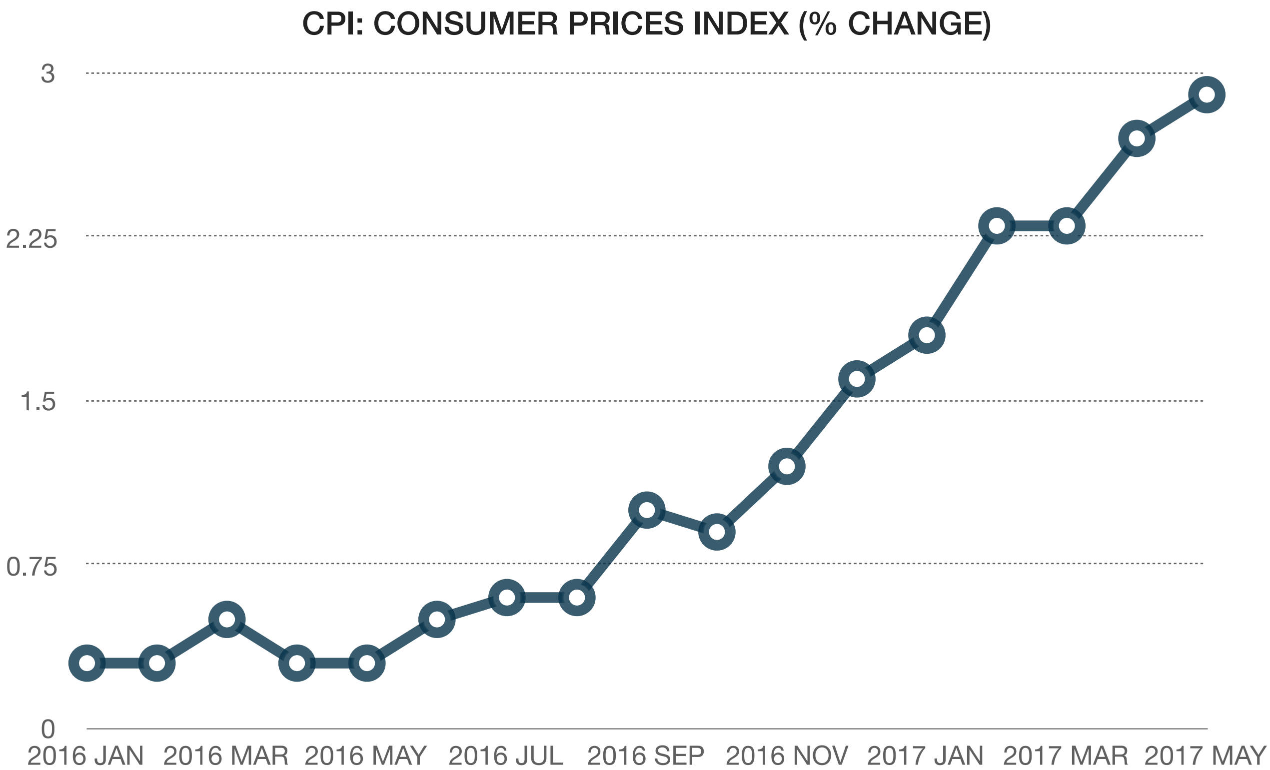


Figure 2: *British CPI % change January 2016 – May 2017.*

So not only are foreign prices increased, home prices are now also inflated meaning real trouble for many companies who not only depend on reasonably priced stock from the EU, but now have to charge the consumer more for their goods at home, which the consumer may not pay.

How the Dollar is affected?

Backed with a AAA rating, the United States Dollar is supported by the U.S Federal government, and is a world reserve currency.

Given the aforementioned increased volatility, and uncertainty surrounding the Pound and the Euro, it would be expected that investors fleeing away from the two uncertain currencies, would move toward the 'guaranteed' Dollar, which would then push up the price of the Dollar.

USD/EUR SINCE BREXIT

In the above we see the expected increase in the value of the dollar. From July of 2016, the sell-off of the pound lead many toward the more-stable dollar, resulting in the move from €0.878 on June 23rd, to €0.908 on July 26th. These effects then wore off, as the Pound sterling started to recover, and held a very slight upward trend. Donald Trump then won the Presidential election, after a long campaign in which he had expressed his

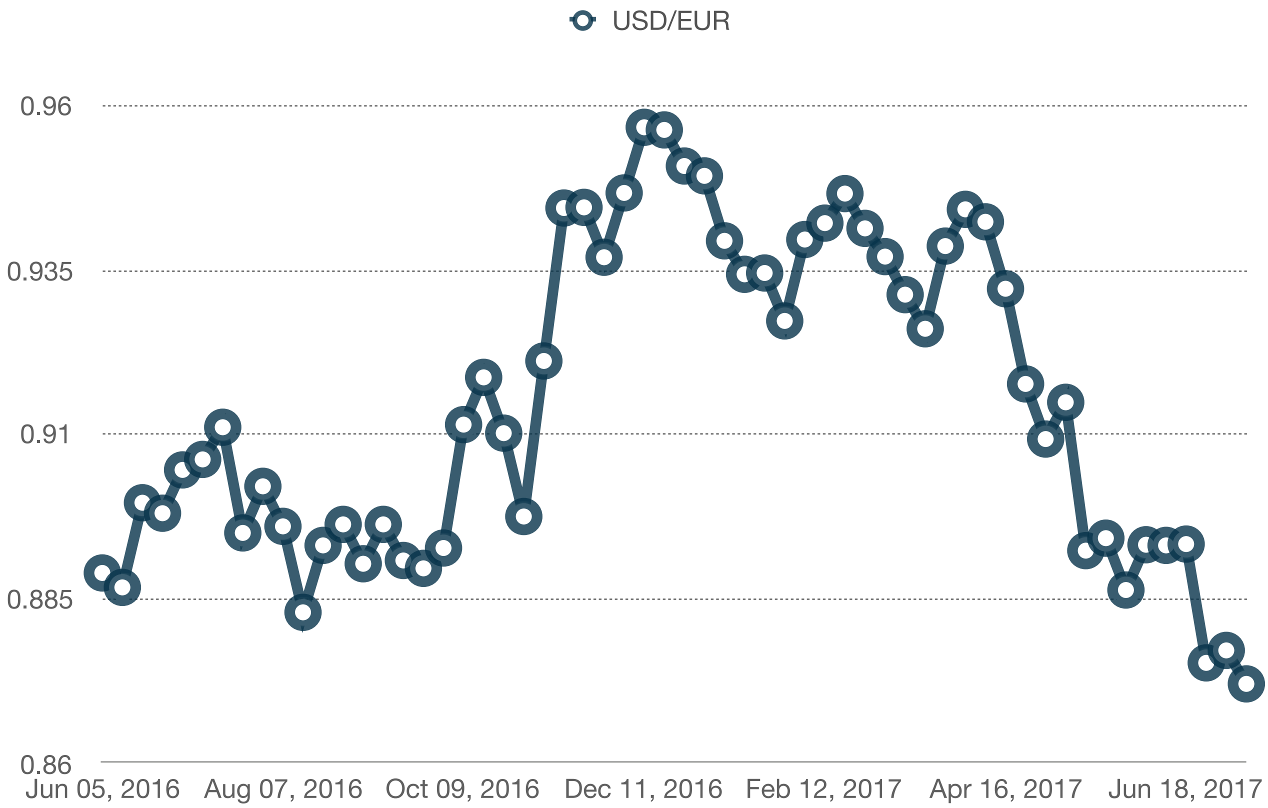


***Figure 3**: USD vs EUR since Brexit. Source: Financial Times*

intentions to deregulate the banks and business.

This is essentially a reverse of Brexit's effect on the Pound. Brexit caused probable business complications, leading to a fall in Investor confidence surrounding the UK/ Pound. Trump promised easier business, with less corporation tax to pay, which encouraged business and trade, leading to more interest in the USD, and thus, a higher price.

For more detail on Donald Trump's affect on the American Economy, see Trade Finance Global's 'Trump on the US Dollar'.

What to expect as Brexit unfolds…

Brexit has caused quite the storm in British Politics, after PM Theresa May called a snap election (see Snap Election) due to parliamentary turmoil, in the hopes for a larger majority. She did not get that. This complicates the process even further because the government has become less unified, and now includes coalition members the Democratic Unionist Party.

PM Theresa May will need the DUP's parliamentary support - without that she will not be able to pass bills through parliament as easily as before with her majority government. The DUP have been supportive so far.

This complication instils more uncertainty around the process of actually leaving the European Union. This then creates doubt around the British economy, which will inevitably result in less interest in the pound. That being said, British indicators have been relatively stable as of late, with Inflation at 2.7% (close to the 3% target), Unemployment at 4.5%, and GDP growth at a steady 2.3%.

If the above indicators can hold relatively stable, and Brexit negotiations go well, the currencies discussed will fluctuate, but hold a similar trend in the long run.

Summary

Complications with the negotiations, and the payment deals agreed to will play a major role in how investors react to the currency market. If the UK has to pay an exit bill, this large sum will affect confidence in the UK and affect the pound's value poorly. If this is accompanied by a poor trade deal, and dim new trade prospects, the results could be disastrous. However, only time will tell.

Keep a close eye on Brexit negotiations, the Pound Sterling, as well as what the EU has to say. Fluctuations are to be expected anyway, let alone at such a turbulent time. However, developments in Brexit's process, negative or positive, are sure to impact the currency markets greatly. ■

Ross McKenzie

Economics Graduate, interested in currency markets and macroeconomics.

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Trade Finance Global has supported clients with their trade and export needs for several years. Our teams are geographical and product experts in domestic and international trade.

Services

1. Trade Finance

Trade financing offers flexible financing which allows your business to improve cashflow, and support the procurement and sale of goods both domestically and internationally.

Trade finance can sit alongside existing financial and debtor arrangements.

2. Currency and risk mitigation

The recent depreciation of sterling has caused both challenges and opportunities for businesses. At TFG, we believe that planning alongside finance teams, hedging currency with the most appropriate financial tools, and highlighting the potential risks a business can face when it comes to long term payments can help save money and protect the business.

3. Letters of Credit

TFG helps companies access trade finance through Letters of Credit.

4. Invoice and Receivables Finance

TFG helps suppliers and buyers with the option to accelerate the payment of invoices, according to agreed payment terms. This can be done with our without recourse, for payment up to 100% of the value of the receivable.

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info@tradefinanceglobal.com