January Review and Outlook

The purpose of this document is to provide a review of what we have seen and experienced in the financial markets over the past few weeks. We hope that it provides you with some meaningful insight.

PLEASE NOTE THAT NONE OF THE CONTENTS OF THIS REVIEW CONSTITUTES ADVICE. READERS SHOULD TAKE PROFESSIONAL ADVICE BEFORE UNDERTAKING ANY RISK MANAGEMENT ACTIONS.

www.treasurysolutions.ie

021 4919794

2/3/2017

1. Monthly Review

Busy month both on the markets and at the coalface here.

Re the former, the markets are trying to adjust to the consequences of the Trump election and Brexit process…but it's too early yet for trends to emerge. In fact, in the short term, the trend may be no trend but volatility and rang-trading…. which, in turn, won't last forever as traders need volatility to make money.

On the latter, the year has kicked off where last year finished i.e. more debt work with the first term sheet of the year just about finished ((€100m+ deal). However, the other trend has been the attempt to finalise documentation around two sub-€10m loans which have run into the New Year and the incredibly slow reaction and poor service of banks in this space. In one of the deals (with an Irish bank), there are three legal teams involved: the borrower's, the bank's own legal department and a third firm that the bank has outsourced legal work to (mainly on the security front). This for a loan under €5m. And the borrower pays all parties legal fees. There are ways to reduce both risk and cost in this area provided your strategy is right from the offset. Please note this.

Also, looks like some more High Court work looms on the expert witness front as activity increases in that space.

FX management is creeping on to the agenda with Brexit now accepted as a reality – we shall see if it becomes formalized at Board level. We expect that banks who lend to exporters to demand this in the coming months as they review 2016 accounts with their accompanying foreign exchange losses. Advice is to do it before being asked to do it.

Finally, debt management is also coming back on the radar. In my opinion, if one is considering a 5-year fixing there is probably 25-50bp (€2,500-€5,000 on every €1m borrowed)) up for grabs in just getting the basics right before we look at how the hedging might look. Money for jam as I say…don't leave it behind.

Courses

I will be giving my Banking and Finance Outlook courses again in Dublin on March 6th in conjunction with the Institute of Chartered Accountants. The update for medium to large companies will be in the morning (9.30 to 12.00) while the SME update will be in the afternoon (2.00 to 4.30). If anyone missed the December updates get in touch or check out the CPD section of the website of the Institute www.charteredaccountants.ie

Thoughts for the month

Ascertain if your bank is ready to fix interest rates if you so require. If not, sort it out now. Be careful on documentation in this area.

If you plan to refinance, allow plenty of time especially if you require the funds to close a project. Tactics in this space are crucial and can save significant money if adopted and implemented correctly.

Enterprise Week

I have been asked to give updates on Banking and Brexit as part of Enterprise Week by several Local Enterprise Offices ("LEO"). Current dates are:

March 7th Wicklow LEO (morning)
March 8th Cork Chamber/Cork City LEO (afternoon)
March 9th Kilkenny LEO (morning)
March 10th South Cork LEO (morning).

Details will be on the websites of the respective LEOs.

Alliances

Having already started to partner with Treasury Delta (www.treasurydelta.com) in their cash management product, expect announcements with two further service providers in the near-term as we strive to ensure that you are in a position to take advantage of the technological changes that are both imminent and advantageous to you.

Email me at johnfinn@treasurysolutions.ie with any queries on what services we can provide.
Tweet at @JohnTSFinn

2. Foreign Exchange ("FX")

Table 1. Overall FX trends in 2017 (and comparative data)

	31/01/17	02/01/17	2017 high	2017 low	Range %	2017 avge	2016 avge	2015 avge
EUR/GBP	0.8583	0.8516	0.8853	0.8446	4.82%	0.8609	0.8192	0.7263
EUR/USD	1.0795	1.0457	1.0828	1.0339	4.73%	1.0627	1.1066	1.1099
EUR/JPY	121.78	122.87	123.72	120.51	2.66%	122.32	120.29	134.32
EUR/AUD	1.4228	1.4542	1.464	1.4024	4.39%	1.4263	1.4845	1.4777

- First key point to note here is the move in the average rates (as they are a better indicator of medium-term trends). GBP in 2017 is 18% on average weaker than the 2015 full year figure. USD was largely unchanged last year although I have warned in my 2017 forecasts against such a trend continuing and the year-to-date trend backs that up with USD almost 4% stronger.
- Second point to note is the high/low volatility in the month was almost 5% for GBP and USD versus EUR which is quite high against a backdrop of 12-month ranges of 10% and 15% respectively for the years 2009-2015.

Graph 1. EUR/GBP – two year trend

- Since the Brexit vote and the initial market shock which saw the rate move by 7p in matter of days and second trading jump in October due to the "flash crash", EUR/GBP seems to have tightened up into a range between EUR/GBP0.84 and EUR/GBP0.90.

- With the UK, Supreme Court voting 8-3 requiring the UK government to invoke Article 50 with a vote in parliament, it is going to be passed and Article 50 could be triggered as early as March 8th
- So, the markets have moved into the "acceptance" phase now i.e. it IS going to happen so the questions are how quickly and what is the deal?
- Our view on the former is that a framework agreement is all that can be agreed in the 2 year period post Article 50 being triggered and probably a 6 year period thereafter before all necessary actions are taken
- No idea how the latter will play out although I have already started to work with companies on putting arrangements in place to beef up their UK presence in preparation for an expectation of a higher level of "on the ground" activity there.

Graph 2. EUR/USD – two year trend

- First thing to notice here is how much more volatile this rate has generally been (see 2015) compared to GBP although the 2016 volatility was a lot less pronounced
- President Trump has called for a weaker dollar (to help US exports)… but there was also an interest rate hike in December
- So, his call probably took the momentum out of the move below EUR/USD1.06 for now
- His policies would suggest short-term economic gain and that with rate hikes would support the dollar
- However, if he continues to be (or appears to be) volatile in his own policy implementation, the markets tend to look on uncertainty as a reason to sell a currency
- Regardless, we suggest that the 2017 range in EUR/USD is unlikely to be as narrow as 2016's 10%
- And we also suggest to exporters to USD-denominated countries that ongoing USD strength is NOT a guarantee. Beware complacency.

3. Interest Rates

Table 2. 2017 trends in interest rates (with some 2016 comparatives

	31/01/17	02/01/17	2017 high	2017 low	2016 high	2016 low
3-m euribor	-0.3280%	-0.3180%	-0.3180%	-0.3290%	-0.1320%	-0.3280%
EUR 3-year	-0.0700%	-0.1180%	-0.0700%	-0.1400%	0.0595%	-0.2743%
3-m libor	0.3559%	0.3725%	0.3729%	0.3552%	0.5929%	0.3621%
GBP 3-year	0.8119%	0.6983%	0.8473%	0.6691%	0.9935%	0.3663%
USD 3-year	1.6900%	1.6400%	1.7530%	1.5710%	1.7758%	0.6827%

Graph 3. 3-m Euribor - two year trend

- Rate continue to fall due to QE
- Borrowers losing money on new loans due to failure of documentation to adopt this basis
- Not forecast to move materially for now.

Graph 4. EUR 3-year Fixed Rates - two year trend

- This seems to have bottomed out but remains negative (before credit spreads)

Graph 5. 3-m Libor – two year trend

- Rate fell after Base Rate cut post Brexit vote and after a blip has settled back again.

Graph 6. UK 3-year Fixed Rates – two year trend

- The post-Brexit fall has reversed in the past few weeks and this rate looks like it has bottomed out
- Watch inflation trends in the UK (see Section 5).

Graph 7. USD 3-year Fixed Rates – two year trend

- This is what starts to happen once rates begin to rise. This rate has more than doubled in the space of 6 months and will, in all probability, continue this trend in 2017.

4. Oil

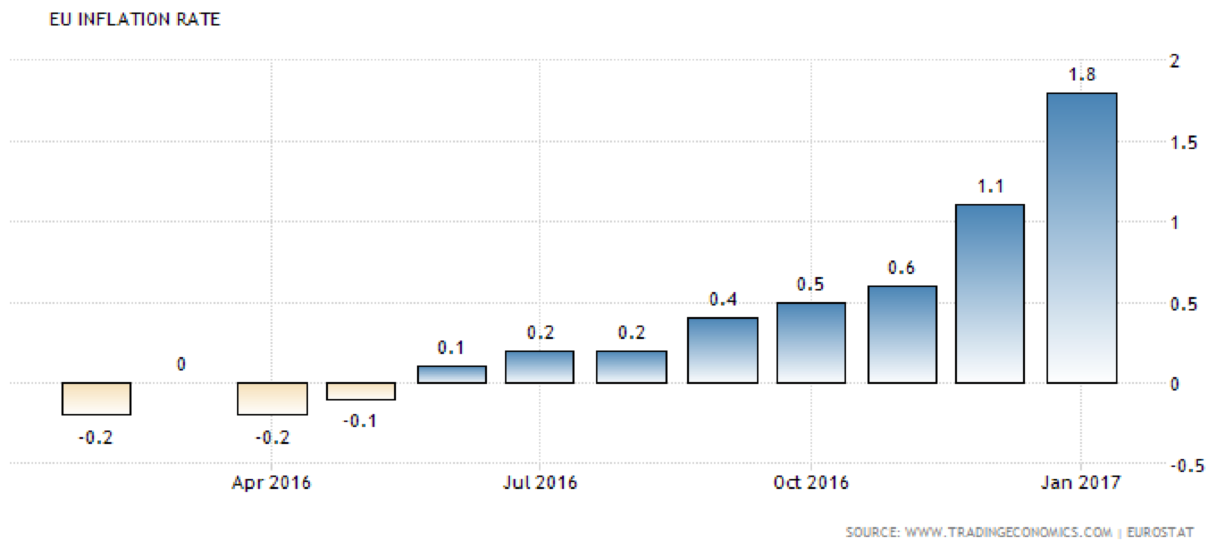
Graph 8. Brent Crude – two year trend

- Price holding up post OPEC decision to reduce production.

5. Feature of the month – Inflation

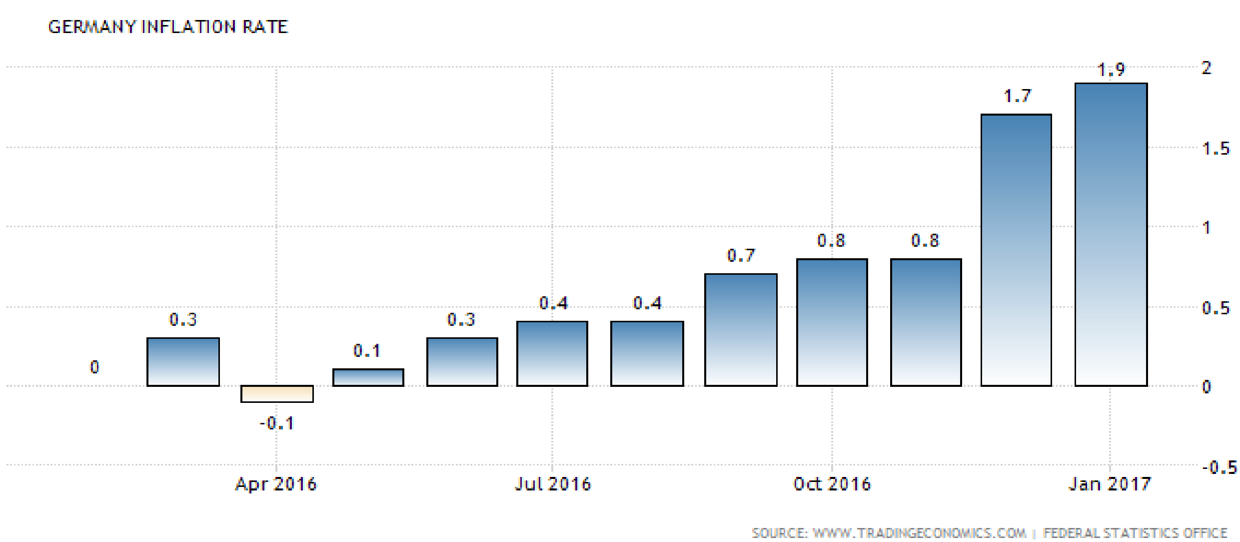
- Need to watch this as it is a driver of both interest rate expectations and wage growth/competitiveness

Graph 9. EU inflation



- Jump in Eurozone inflation over the past few months (above) but real pressure will come from Germany (see below)

Graph 10. German inflation



Graph 11. UK inflation

- UK inflation is actually lower than in the Eurozone notwithstanding the expected price pressure on imports as a result of weak GBP (the UK is a net importer)
- However we believe that this has been protected both through hedging by UK companies and UK importers taking some pain…which is not sustainable in the medium-term.