# 2017 FORECASTS

**The purpose of this document is to provide a view of what may happen over the course of 2017 in the banking and financial markets. We also evaluate how the 2016 forecasts turned out!**

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

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## 1. 2017 Forecasts

**I ended last year's forecast with what could best be described as a plea:**

**"PLEASE, PLEASE, PLEASE START TO FOCUS ON FOREIGN EXCHANGE MANAGEMENT IN A FORMAL AND STRUCTURED WAY**. The amount of value wasted in this space is huge and favourable trends of the past two years may reverse in 2016, especially for Sterling".

If ever a piece of free advice was worth thousands, this was it. And against a backdrop of most banks forecasting a move only towards EUR/GBP0.75

**2017 considerations**

1. **REFINANCE WITH A LOT OF YOUR FOCUS ON THE QUALITY OF THE DOCUMENTATION – NEEDS TO SEE YOU THROUGH A SLOWDOWN**
2. **Check out non-Bank sources of finance, especially if you are a SME**
3. **Formalise Foreign Exchange policies at Board level and then draw up and update quarterly strategies thereafter**
4. **DO with your debt management this year what you should have done with your Foreign Exchange last year.**

### 2017 Detailed Forecasts

- Firstly, I think that it has the potential to be the most volatile year since 2008, mainly due to the political uncertainty. So, the plea this year is simple: GET THE BASICS RIGHT. This isn't a year to be undertaking "mad stuff"
- Getting the basics right means looking at the commercial risks and desired outcomes and putting the appropriate strategies in place….from the start of the year
- There's an almost universal view that USD will have a good year against EUR and while I am inclined to agree that the first half of the year could be good for the US (as European outlook is somewhat ropey given the various elections), can it be sustained? A break through parity looks on and if (as I think) the new president introduces a low rate of tax to bring home cash from abroad, this will drive demand for USD up and also give a one-off boost to the economy if some of that works its way into the pockets of US citizens
- The narrow 2016 high/low range of circa 10% in EUR/USD will not be repeated and will be wider than that so this is not the year for complacency in managing such exposures
- Where to for GBP? Maybe the question is "Where to for GB?". Brexit will be a huge influencer
- Will they trigger Article 50 by Q1? What about the Supreme Court decision? View seems to be that it will reaffirm the High Court ruling…which could mean a challenge of some sort from the Leave side…which, I think, must be to the European Court of Justice (irony of ironies). All of this

would point to a delay in the trigger. But something tells me that they are hell bent on triggering it asap and just might find a way around it. So, I am going with view that Q1 trigger will proceed

- And thereafter? Won't be pretty. Even within the UK. Mrs May has trouble keeping the Tories together, Labour is also split down the centre. Who is the saviour? Won't be Blair. Could Miliband the Defeated return? Probably not. UK election? Certainly on the cards….but in the middle of an 18-month negotiation period (as Mr Barnier has stated it is). Would not be wise. More likely in 2018 if negotiations do not go well
- Impact on EUR/GBP will be a lot of shorter, sharper moves: 3%-5% moves in 2-3 week periods. High/low range likely to be narrower than 2016 (28%) but more than the average of prior 6 years (10%)
- On the interest rate front I think that it is time to start polishing off the debt management strategies. This could become very important if we were to get caught in a pincer movement here: rates increasing while Brexit has a negative impact on Irish economic growth. And although the immediate upward pressure on rates is low, sustained inflation growth, especially in Germany, could see a change in that dynamic. AND WATCH THE PROPORTIONATE EFFECT OF RATE HIKES WHEN COMING OFF LOW LEVELS. A move in official rates of 2% will double the cost of debt of many borrowers. And fixed rates (which is what we are concerned about) will increase 6-9 months before any rise in short-term rates
- And if we get what is perceived as a "premature" hike in Eurozone rates due to German pressures in the middle of Brexit negotiations, the clamour for a discussion around an Irish exit vote (or "retIRE" as I call it!) will increase. A convergence of this with a wobbly government situation (highly likely) could lead to a lot of uncertainty here
- In the short-term the Irish economy could get a one-off boost from the settlement of the overcharging of trackers. 15,000 trackers at EUR20k each is EUR1 billion!! Will add fuel to property market?
- But it will also cause significant dissatisfaction YET AGAIN with the banking sector. The question as to whether criminal charges could be advanced over the tracker issue is a serious and real one. It is difficult to see the overcharging as anything other than organised and systematic given both the scale of it across the sector and the manner in which banks (some more than others) have fought it. I expect someone to go this route, especially someone that lost their home as a result of it. Won't be a lot of sympathy for banks in this space ("As you sow, so shall you reap") and it also could appeal to some politicians to support (it's a vote getter I suspect)
- Uncertainty tends to lead to a more difficult banking environment. And I think that it will be made worse by a real emergence of 2017 of the non-bank lending sector, especially for SMEs. This allied to the possible negative ramifications of the tracker issue (which really does need to be resolved) will make it a difficult year for banks to hit lending targets. And having recently seen at first hand the total inflexibility in documentation content adopted by one of the main banks in dealing with a very good quality SME credit, I suspect that if SMEs can get broadly similar pricing from non-banks, they will be given a shot at new borrowing. Will be interesting to see if Credit Unions are permitted to offer mortgages to use their surplus EUR8bn. Expect significant lobbying from banking sector to avoid this
- Inflation will be another story for 2017 I believe, especially if oil continues to creep up (and it has a potential knock-on effect on interest rates)
- FINTECH will be the other major development. The move to increased use of mobile technology from recording transactions to the use of electronic wallets is now unstoppable. The drive to integrate processes and use data for better management of finances and other metrics has momentum. So, last year's prediction of the move to increased systemisation, Straight Through Processing, etc. was good if just ahead of the curve. I think this year will see major initiatives across the board in this space.

**LAST POINT TO NOTE (PLEASE!!):**
**WHEN EVALUATING HOW TO MANAGE ANY OF THE ABOVE, YOU NEED TO LOOK AT THE "VALUE AT RISK" IN THE CONTEXT OF INCURRING COSTS TO MANAGE SAME. SO, FOR EXAMPLE, ASSUME THAT WHEN INTEREST RATES START TO INCREASE THAT THE AMOUNT AT RISK IS 5% (1% FOR 5 YEARS) OR EUR50,000 FOR EVERY EUR1MILLION BORROWED. ON THE CURRENCY, FRONT A 5% FIGURE IS THE MINIMUM YOU SHOULD USE. AND AS FOR REFINANCING….. WELL YOU GET IT WRONG THIS TIME IT COULD COST YOUR BUSINESS. I DON'T** EXPECT TO **SEE A LOT OF COMPASSION OUT THERE** FOR TROUBLED BORROWERS FROM LENDERS**, ESPECIALLY AS BANK BALANCE SHEETS ARE NOW REPAIRED.**

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

## 2. 2016 Forecasts and Outcomes

| Forecast | Outcome |
|---|---|
| On balance would expect Dollar to remain strong versus Euro. | Correct |
| However, Brexit is a real risk, much larger than being priced by the markets. We forecast EUR/GBP0.800 being hit in 2016. | Hit EUR/GBP by end Q1 2016 |
| No change to the negative deposit rates outlook | Correct |
| Bank margins may begin to top out again at the upper end of the market. | I believe this to be the case |
| If you have bank facilities maturing in the next 24 months, I would refinance in 2016 and preferably in H1. I think the volatility that could arise in the broad sense during the year added to the regulatory pressures could make it more difficult to get borrower-friendly deal. | This remains a 2017 priority for those that did not refi in 2016 |
| Of course, the growth of non-bank providers will probably mean that there will be a notable casualty in that space at some point...... and watch the backlash from the banking sector over the lack of regulation in the shadow banking sector as a result. | Keep watching! |
| There is going to be a liquidity squeeze/event at some point relating to bonds. But will be a jolt in this space in 2016. | General view that liquidity is tight but no crisis of this nature yet |
| I recommended at the December 2015 market outlook session that Corporates start using technology better and focus on cash management technology. I think we will see more of this. With an evolving banking landscape this area requires more effort and tighter processes and efficiencies. But will it gain the momentum it deserves? | Not enough momentum yet but see 2017 predictions |
| **Economic policy of the next government here is crucial, especial for indigenous companies**. It is not easy to grow as a SME here and there are a number of initiatives that could be undertaken. But the fascination with big business will remain. | Increasing evidence that bank debt availability is getting tougher to secure on good terms. |
| **Corporation tax take will hold up here for another year or two so there is a real risk that this is just wasted**. The next government really needs to plough some of that into the development of Irish companies on a sustainable and outside of Dublin. **But the gap between the East and the rest will grow**. | Correct on both tax take and gap between East and Rest |
| UK has a problem with Brexit. **Exporters to the UK ignore at your peril**. Oil prices will remain low for 2016. | Good Brexit call. Oil had a recovery to around $50 per barrel but that is less |

| | |
|---|---|
| | than half the rate of over 2 years ago |
| Stock markets are due a large correction. | Hasn't happened yet…might keep away from the equity stuff! |
| POLITICS WILL CONTINUE TO BE VERY IMPORTANT… WHICH IS WHERE IT GETS TRICKY FROM A FORECASTING PERSPECTIVE. NO IDEA HOW IRISH ELECTION WILL PAN OUT. | Brutally honest I suppose - the minority government nature of the outcome highlights the fragility of same |

# 3. Foreign Exchange ("FX")

## 2016 trends in FX rates

| | 31/12/16 | 01/01/16 | 2016 high | 2016 low | Range % | 2016 avge | 2015 avge | diff |
|---|---|---|---|---|---|---|---|---|
| EUR/GBP | 0.8518 | 0.7351 | 0.9365 | 0.7308 | 28.15% | 0.8192 | 0.7263 | 12.79% |
| EUR/USD | 1.0513 | 1.0858 | 1.1614 | 1.035 | 12.21% | 1.1066 | 1.1099 | -0.30% |
| EUR/JPY | 123.32 | 130.45 | 132.25 | 109.46 | 20.82% | 120.29 | 134.32 | -10.45% |
| EUR/AUD | 1.4298 | 1.4907 | 1.6244 | 1.4068 | 15.47% | 1.4845 | 1.4777 | 0.46% |

# 4. Interest Rates

## 2016 trends in interest rates

| | 31/12/16 | 31/12/15 | 2016 high | 2016 low |
|---|---|---|---|---|
| 3-m euribor | -0.3190% | -0.1310% | -0.1320% | -0.3190% |
| EUR 3-year | -0.1070% | 0.5600% | 0.0595% | -0.2743% |
| 3-m libor | 0.3666% | 0.5804% | 0.5929% | 0.3621% |
| GBP 3-year | 0.6756% | 1.2938% | 1.2938% | 0.3715% |
| USD 3-year | 1.6542% | 1.3807% | 1.7758% | 0.7454% |