World First
SME Global Trade Barometer
Q3 2016
An uncertain business landscape for SMEs

2016 has been characterised by political and economic uncertainty. The UK’s decision to leave the EU, terror attacks across Western Europe, an embittered US election campaign and China’s slowdown have all caused volatility across financial markets and have had a considerable impact on how UK SMEs trading internationally have been able to manage their business.

In the third edition of World First’s Global Trade Barometer, we shine a light on international trading trends of UK SMEs over the third quarter of 2016. By analysing data from a sample of World First’s corporate clients, supported by the findings of an independent survey of 679 decision-makers at UK SMEs, the attitudes of the UK’s mini-multinationals are brought to life during an exceptional and extraordinary period in the UK.

In this edition of Barometer, we focus on the following:

- International transfers and most traded currencies
- Hedging strategies deployed by SMEs
- Sterling volatility following the result of the UK’s EU referendum and appointment of a new Conservative government
- Dollar volatility in the lead up to one of the most anticipated US elections in history

UK SMEs transfer on average £38,000 each month in Q3 – same as Q2

Through a politically eventful summer, UK SMEs continued to trade internationally at similar levels as before to the EU referendum.

Research conducted for World First by YouGov shows that the average UK SME made foreign currency transfers of £38,000 in a typical month across July to September. This is the same level as that recorded in Q2 and slightly down from Q1, an average of £39,000.

When, if ever, was the last time your business made a foreign currency transfer?

- 13% Within the last week
- 6% 1–2 weeks
- 6% 2–4 weeks
- 5% 1–3 months
- 2% 3–6 months
- 2% 6 months to 1 year
- 9% Longer than a year ago
- 11% Don’t know
- 47% Never

- There’s been a slight decrease in the share of SMEs trading internationally with 47% admitting to not making any foreign currency transfers in the average month compared to 40% in Q2.
- Focusing on medium sized business in our sample, however, shows a significant increase in value of international trades. The average medium sized business made foreign currency transfers of £74,000 in Q3 compared to just £59,000 in Q2 suggesting a bounce back in international trading from more established businesses.
- The number of SMEs making foreign currency transfers has been steadily declining over the year with 30% of businesses having done so at least once in the last three months, down slightly from 31% across Q2 and 33% in Q1.
Euro and Dollar trading bounces back post Brexit vote

Q2 saw a sharp drop in euro and dollar trading as businesses held back in the lead up to the EU Referendum. Following the result, euro trading has picked up slightly with 37% identifying it as the most common currency traded in the last three months compared to 30% in Q2. Nevertheless, euro trading has failed to get back to its initial popularity in Q1 when 49% of SMEs listed it as their most traded currency. Similarly, World First data shows payments reaching the European Union fell more sharply than those reaching the rest of the world (-11.8% vs. -3.2% respectively) in Q3.

Likewise, 28% listed the dollar as the most traded currency of the last three months compared with 24% in Q2. This is still someway from the levels during Q1 which hovered just above 36%.

Previous favourites Norway suffered a fall in payments reaching their shores, with over 28% fewer UK businesses sending funds across the North Sea. Compared to Q2 Canada was spared from the sharpest of declines, but still saw payments fall by a more modest 3.2%. Similarly, New Zealand saw the number of payments fall by 6% in Q3 from Q2’s levels.

Emerging markets had a far more favourable quarter. Payments to Zimbabwe, Peru and Vietnam all grew by double-digit percentages, with eastern European destinations also faring well: Romania, Estonia, Latvia and Slovenia all saw inflows increase.
Looming threat of elections and rate hike plays on UK SMEs trading with the US

The fall in the pound following the EU referendum has been persistent and far-reaching. Companies that benefit from a weaker domestic currency (primarily exporters) now have the opportunity to sell their goods and services overseas with either a wider profit margin, or at a far more competitive price against domestic equivalents. In Q3, UK-based SMEs’ use of GBP-buying forward contracts rose by 13%, showing the readiness of SMEs to lock-in rates for an extended period picked up sharply following the EU referendum.

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The same can’t be said for USD-buyers who, in Q3, shortened the maturity of forward contracts sharply, falling from over 90 working days per contract to below 70 days - a fall of over 25%. The shorter length of these contracts is significant, as it shows that the majority of USD-buyers will be wholly unhedged beyond the Christmas period, ahead of which there are two significant events that could have long-lasting and meaningful impacts on the USD: the Presidential election on November 8th and what’s expected to be the first Federal Reserve rate hike in 12 months this December.

The ramifications of these actions could be significant in the early months of 2017. As hedging contracts expire, wholesalers, retailers and those who import from the US will have to revert to spot rates. In many cases this will be detrimental to margins and introduce price pressures to the UK consumer, potentially becoming the catalyst for a wave of ‘cost-push’ inflation in the first six months of 2017.

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World First data shows trades taking advantage of the weak pound rose sharply in Q3 in the wake of referendum-induced currency volatility

Popularity of hedging USD rates forward falls in anticipation of the November Presidential elections

SMEs favour shorter USD hedges in Q3, covering the period ending Christmas but no further

What does the expert say?

Jeremy Cook, Chief Economist at World First: “The pound’s weakness will be a boon to exporters in the UK and our data shows they’re willing to take advantage of this. The sharp rise of hedging contracts securing a rate for the pound shows that even if the weakness in the pound is short-lived, SMEs can continue to reap the rewards for an extended period. On the other hand, the reluctance of firms to hedge forward the dollar for a material period of time shows that SMEs are more hesitant ahead of the potential paradigm-shifting dollar volatility that could ensue if Trump ascends to the White House in 2017.”
Sterling dive hurt SMEs but confidence picks up

- A growing number of SMEs are feeling the impact of falling sterling with 28% experiencing the negative impact of exchange rate movements in Q3, up from 23% in Q2.
- 38% of businesses admitted to being worried about currency volatility, down from 46% in Q2, though not quite reaching the levels of Q1 where only 31% indicated worries.
- Still, a quarter of business (23%) responded that currency volatility has impacted business investment decisions similar to 24% in Q2.

SMEs expect volatility is here to stay

- Three quarters (72%) expect sterling to be volatile all the way into the new year, similar to Q2 (77%) and a significant increase from Q1 (55%).
- Business confidence in managing currency volatility remains steady with 75% feeling confident compared to 74% in Q3.

To what extent do you agree or disagree with the following statements?

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly agree</th>
<th>Tend to agree</th>
<th>Tend to disagree</th>
<th>Strongly disagree</th>
<th>Don't know</th>
<th>Net: Agree</th>
<th>Net: Disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>My business has felt the negative impact of exchange rate movements in the last quarter (i.e. from July to the end of September 2016)</td>
<td>15%</td>
<td>28%</td>
<td>25%</td>
<td>15%</td>
<td>57%</td>
<td>17%</td>
<td>28%</td>
</tr>
<tr>
<td>Currency volatility in the last quarter (i.e. from July to the end of September 2016) has impacted my business’ investment decisions to support development and growth</td>
<td>16%</td>
<td>25%</td>
<td>21%</td>
<td>18%</td>
<td>59%</td>
<td>8%</td>
<td>28%</td>
</tr>
<tr>
<td>I am worried about currency volatility and the impact it could have on my business</td>
<td>14%</td>
<td>38%</td>
<td>47%</td>
<td>13%</td>
<td>52%</td>
<td>25%</td>
<td>25%</td>
</tr>
<tr>
<td>Having an effective currency strategy is important to the success of my business</td>
<td>19%</td>
<td>25%</td>
<td>25%</td>
<td>26%</td>
<td>52%</td>
<td>9%</td>
<td>20%</td>
</tr>
<tr>
<td>The outcome of the EU referendum vote has been positive for my business’ future prospects</td>
<td>27%</td>
<td>25%</td>
<td>25%</td>
<td>23%</td>
<td>49%</td>
<td>18%</td>
<td>25%</td>
</tr>
</tbody>
</table>

What does the expert say?

Jeremy Cook, Chief Economist at World First: “Calling 2016 an eventful year politically and economically would be a bit of an understatement and SMEs have certainly felt the impact that momentous events like Brexit and an unpredictable US election have had on currency volatility. With sterling tumbling over Q3, it is unsurprising that many businesses have felt the need to alter their investment decisions.

Nevertheless, it’s not over yet and as we head into a fraught US election which could bring up more surprises, UK SMEs need to brace themselves for a bumpy road ahead. We’ve seen the pound fall against the dollar by record amounts over the past few months, and for businesses without the right foreign exchange protection this can add a lot of pressure on margins.”
Conclusion

The events of 2016 have taken their toll on the currency market — and as a result — on UK SMEs trading or looking to trade overseas. A weak pound has made importing goods and services up to 20% more expensive over the last three months following the EU referendum result and many businesses are having to revisit deals with overseas suppliers. As evidenced in World First’s transactional data, payments internationally have fallen as a whole in Q3 and in particular payments to the European Union.

SMEs have rushed to protect themselves with our data showing a willingness to lock in rates in Q3 as they anticipate further volatility ahead.

The fallout from the EU referendum has not been the only thing for SMEs to contend with as the lead up to a US election pitting Hillary Clinton against Donald Trump, coupled with the likelihood of a rate hike by the US Federal Reserve in 2016, has led to a good run for the dollar which is great for UK exports to the US but costly for any businesses importing from the region.

With UK imports from the US totalling $44.6bn, any further strength in the dollar could have a significant impact not just on UK businesses, but on the economy as a whole and it is likely that the higher cost of importing goods will be fed directly back to the consumer in Q4 2016 and Q1 2017. Now more than ever, businesses need to be savvy, actively managing their currency strategies so they are not caught out by currency volatility — which for the near term, is here to stay.

Following the EU Referendum on June 23rd, sterling has fallen against the dollar to record lows

Research Methodology

All figures, unless otherwise stated, are from YouGov Plc. Total sample size was 679 senior decision makers in small/medium British businesses. Fieldwork was undertaken between 3rd October and 6th October 2016. The survey was carried out online. The figures have been weighted and are representative of all British business sizes.

World First data on client contracts was collated between 1st July 2016 and 30th September 2016 and refers to UK corporate desk clients only.

Respondent breakdown by average transfer amount

<table>
<thead>
<tr>
<th>Average Transfer Amount</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than £10,000</td>
<td>34%</td>
</tr>
<tr>
<td>£10,000 - £19,999</td>
<td>10%</td>
</tr>
<tr>
<td>£20,000 - £39,999</td>
<td>7%</td>
</tr>
<tr>
<td>£40,000 - £59,999</td>
<td>4%</td>
</tr>
<tr>
<td>£60,000 - £79,999</td>
<td>3%</td>
</tr>
<tr>
<td>£80,000 - £99,999</td>
<td>2%</td>
</tr>
<tr>
<td>£100,000 - £124,999</td>
<td>5%</td>
</tr>
<tr>
<td>£125,000 - £149,999</td>
<td>0%</td>
</tr>
<tr>
<td>£150,000 - £199,999</td>
<td>0%</td>
</tr>
<tr>
<td>£200,000 - £249,999</td>
<td>0%</td>
</tr>
<tr>
<td>£250,000 - £299,999</td>
<td>0%</td>
</tr>
<tr>
<td>£300,000 or more</td>
<td>3%</td>
</tr>
<tr>
<td>Don’t know</td>
<td>31%</td>
</tr>
</tbody>
</table>

Notes

Forward Contract

A forward contract is a contract to exchange a specific amount of one currency for another on a future date, at a predetermined rate. A deposit is normally required for forward contracts.

Hedging

To hedge or hedging is to manage the risk of future currency movements.

FX

In this report, ‘FX’, ‘foreign exchange’ and ‘foreign currency transfers’ refer to the buying/selling of international money (including the payment of international money).
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World First is market-leading, award-winning, rapidly-growing international FinTech business. Expert in international currencies and money transfer, World First combines specialist knowledge of foreign exchange markets with technological innovation to help individuals and businesses manage cross border currency payments quickly, securely and transparently. A specialist alternative to traditional banks’ generalist approach, World First has successfully exchanged more than £45bn for over 105,000 individuals and businesses since 2004. World First’s corporate and e-commerce desks enable SMEs and online marketplace traders to expand internationally via a specialist and personalised service proposition and bespoke technology. We call these businesses ‘mini-multinationals’.

World First employs c.550 people across 6 international offices of London, Amsterdam, Sydney, Austin, Singapore and Hong Kong with plans for further expansion into new countries. World First has strategic partnerships with over 20 businesses including Virgin Money, Harrods Bank, News Corp and Le Figaro. World First has licences to service clients in over 45 countries.

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