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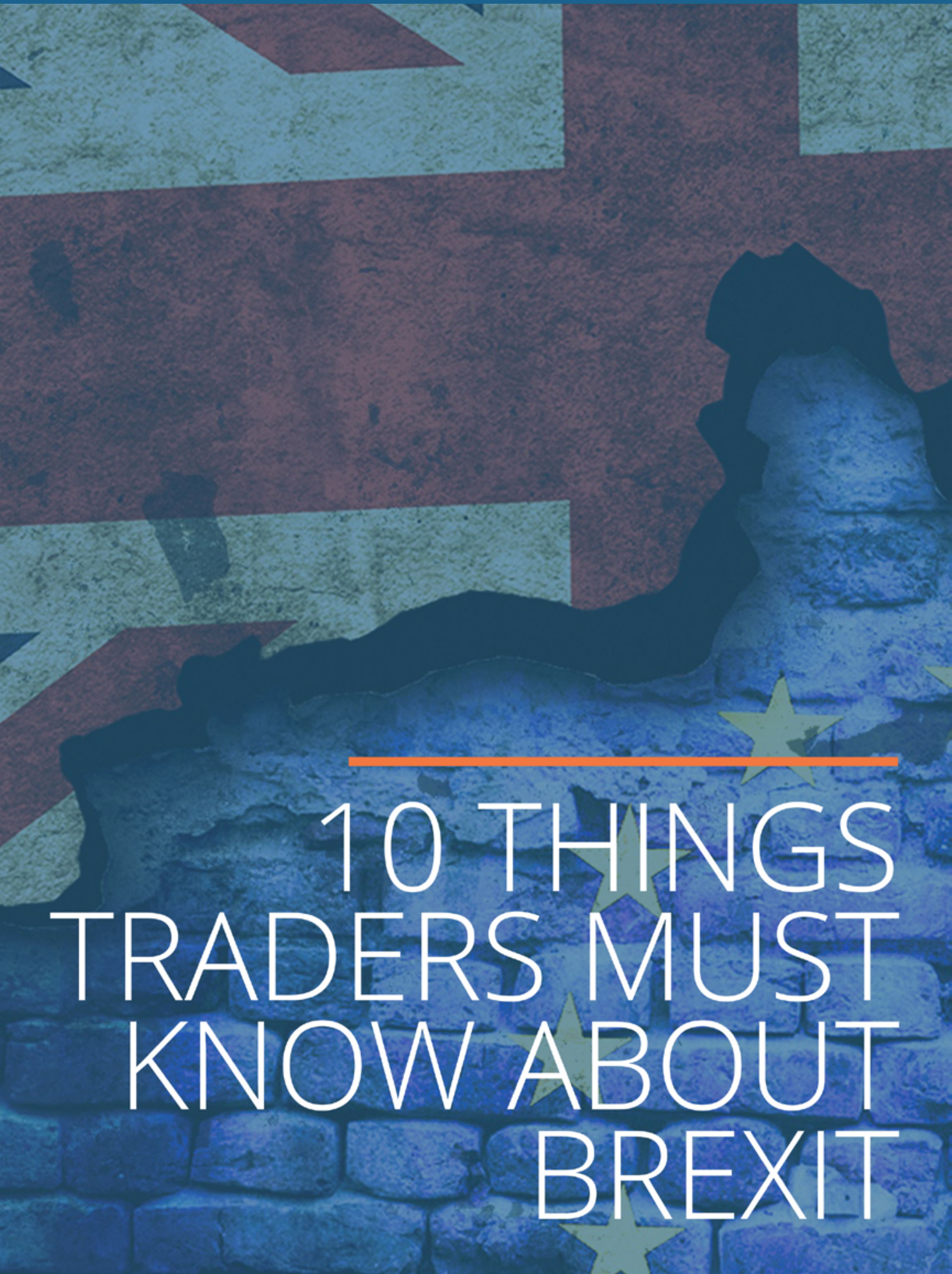


10 THINGS TRADERS MUST KNOW ABOUT BREXIT

THE BLACKWELL ADVANTAGE

BLACKWELL GLOBAL

Blackwell Global is a global brokerage, aiming to be the most trusted financial service provider. We are committed to transparency, integrity and service excellence.

Founded in 2010, we now have global presence in over 90 countries, with main offices in the separately regulated markets of Australia, Cyprus, New Zealand and the United Kingdom.

We believe that sound investment and trading decisions begin with a strong grounding in financial education. Our goal is to make this available to everyone - and this free eBook is part of that commitment.

To find out more about Blackwell Global, please visit: www.blackwellglobal.com

MAKING SENSE OF BREXIT

FOREWORD

We are now living in a post-Brexit world. What this means for the UK economy over the long-term is still unclear - but if the referendum has taught us one lesson, it's that we are in an age of high unpredictability.

This uncertainty has real ramifications for financial traders. We all know that the markets become anxious and volatile when unexpected events come to pass. Brexit certainly falls into this category - and with that in mind, we thought we would create an eBook explaining how you can navigate the markets successfully in the coming months.

Best of luck

Patrick Latchford
CEO, Blackwell Global Investments (UK) Limited

ONE: WHAT IS BREXIT?

Brexit is a term that has been impossible to avoid over the last few months, with the phrase appearing in almost every bulletin and newspaper article, or so it seems. But what does this overworked abbreviation actually mean for traders and the markets?

In this eBook we will look behind the curtain and discuss what Brexit really means for traders, what they need to know and be prepared for.

In its simplest terms Brexit was the catch phrase adopted by the media to describe the referendum on EU membership, held in the UK on the 23rd of June 2016. The referendum had been promised by the then UK Prime Minister David Cameron, as part of his Conservative party's 2015 election manifesto. Mr Cameron won that election but "lost" the referendum, having elected to back the remain campaign.

As we now know it was the leave campaign that emerged victorious. That victory has turned Westminster politics on its head and shaken the European Union establishment to its core. Despite months of campaigning prior to the referendum there are still many questions which are unanswered and many more which were not considered, or perhaps not even thought of before the vote.

Markets mispriced the referendum and its outcome. Of that there can be no doubt. We need only to look at the sharp rally in the GBP USD exchange rates on the evening of the 23rd June, ahead of the first results, to confirm that fact. But even the most accomplished forecaster could not have predicted the political turmoil that followed. That turmoil could well continue across the normally quiet (politically speaking) summer months, here in the UK.

The UK has a new Prime Minister, after what effectively amounted to an uncontested scrum. It is quite possible that we will also see a new leader of the opposition, as well as a new figure at the head of the UK Independence Party (who were prime movers in the leave campaign's success). It is often said that markets dislike uncertainty but with the political landscape shifting under our feet like quicksand, there has been little political certainty since the referendum results were announced.

So why did the UK vote to leave the European Union and what will happen next? There has been much hand wringing as to why the UK voted to leave the EU after four decades of membership. Issues such as immigration, the economy, perceived rule from Brussels, by unelected bureaucrats and European courts, were all behind the leave vote.

However for many voters the main issue was the perceived lack of tangible, personal benefits from EU membership. As far as much of the UK populace is concerned membership of the European Union has not been a success for them.

TWO: WHEN WILL BREXIT HAPPEN?

The timetable for Brexit has been clouded by the political fallout from the referendum.

Not least the election of a new Conservative party leader and UK premier. David Cameron made it clear that he would not start the Brexit process and that it was a matter for his successor. We now know that this is Theresa May MP, who served as Home Secretary under Mr. Cameron's administration. Theresa May was of course a member of the remain campaign. Once again the political ground has moved significantly under our feet.

European politicians and civil servants expressed their displeasure with the "deferred" UK timetable but at the same time confirmed that there can be no preliminary discussions with the UK until it invokes article 50 of the Lisbon treaty, which is effectively the official notification that a member state intends to leave the EU.

Even if Theresa May decides to invoke article 50 soon after taking office, no one is quite certain exactly how long the process of extricating the UK from the European Union will take, as this will be a test case for this procedure.

That said, there is a notional two year deadline within article 50. However, the practicalities of undoing forty years of membership, treaties, rules and arrangements, between Britain and the rest of Europe, may well mean that the process takes much longer. Philip Hammond MP, the new Chancellor of the Exchequer, was quoted as saying the process may take as long as six years to complete.

THREE:
WILL THE UK 'LEAVE'?

This is an interesting question. The referendum result clearly showed that a majority of the UK's citizens wanted to leave the European Union. However the result is not considered to be legally binding on the UK government. Meaning that in theory at least, the government could choose to ignore or set aside the result.

There have been precedents elsewhere in Europe for such behaviour. For example in Holland and France in the late spring of 2005. Both countries held referenda on a new EU constitution. In each the case there was a "no vote". Those results were not binding on national governments however. Ultimately the new EU constitution was ratified, regardless of the French and Dutch voters objections.

As a consequence there is a school of thought which suggests that the new UK Government could actually try and negotiate further concessions from other European countries and the Brussels hierarchy, which could allow the UK to remain in the EU.

Examples of such concessions could include the ability for the UK to further restrict freedom of movement and to control its own borders. Or to exempt itself from the rulings the European court of human rights, whilst retaining access to the single market. Building on the concessions won by David Cameron in early 2016.

If such a package of concessions could be negotiated, then the UK government might feel that remaining in the EU, on improved terms, would represent a better outcome for the country, than withdrawing completely. Whilst this would prove controversial to say the least it's not impossible for such a scenario to unfold. Plus, some legal experts have suggested that the UK parliament itself would need to vote in favour of enabling article 50 before it could be enacted. It is by no means certain that a majority of UK MPs would in fact vote for this.

FOUR: BREXIT'S IMPACT ON TRADE?

Clearly a withdrawal from the European Union and more importantly the single market would have an effect on UK trade and the wider economy.

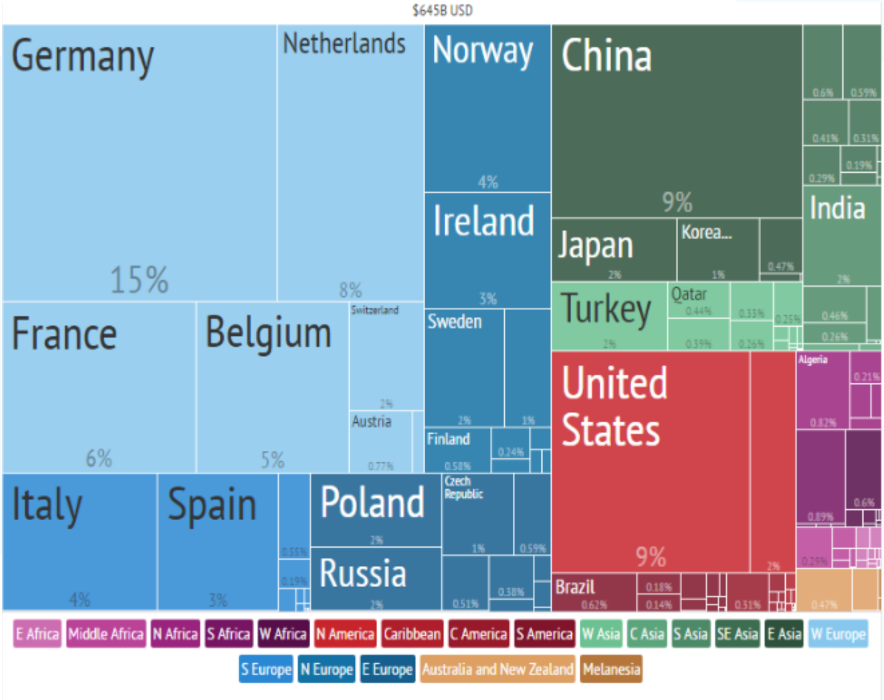
However figures suggest that the equation is not as one sided as some would have us believe.

For example according to data from the Harvard University atlas of economic complexity the UK is the third largest export market for German goods and services, accounting for 7% of all German exports.

We are also Italy's third largest export market, with the UK taking 6% of their exports. The UK is joint third as far as destinations for French exports are concerned and so on.

The graphic below shows UK imports during 2014, which are ranked by the percentage of total imports and their country of origin.

UK IMPORTS BY SOURCE AS PERCENTAGE OF TOTAL UK IMPORTS (SOURCE: HARVARD UNIVERSITY ATLAS OF ECONOMIC COMPLEXITY)



Given the scale of UK Imports from other EU members it's clear that for all of their hard ball posturing over prospective UK exit terms, there are plenty of vested interests in their own economies to be considered in any negotiation. It's of course unlikely that the UK will get an easy ride from its EU peers in those discussions.

At least not at the outset, as the powers that be try to send a message to any other would be "exiteers" within Europe. But it seems possible to us that a more pragmatic EU approach may begin to emerge over time. Looking at UK exports the picture is also very interesting post the referendum. True, as a country the UK does export significant amounts of goods and services into the EU. But our largest single trading partner on this basis is the USA, which accounts for some 11% of UK export trade.

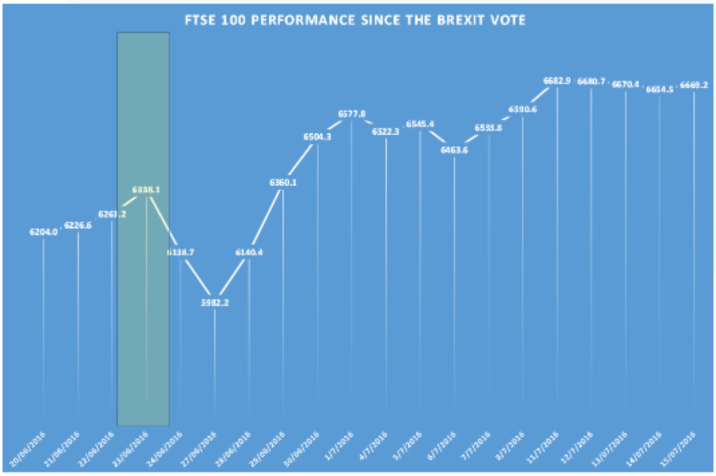
Much has been made of the sharp and sustained decline in the sterling exchange rate versus the USD since the referendum. And indeed cable, as that rate is known, has moved to 30 year lows against the US currency. However that 10% plus decline in the value of sterling will of course make UK exports that much cheaper to buyers of UK goods and services paying in dollars, euros or indeed any other currency that has appreciated against the pound in this period.

Against that of course imports to Britain from those countries will effectively be dearer to UK buyers. However the UK has an export led economy and many of the commodities that make up a large proportion of our imports have experienced substantial price declines in recent years. Largely due to concerns about a slowdown in the global economy and the strength of the US dollar.

Economic growth forecasts for the UK have been trimmed since the referendum. But in truth growth forecasts were under threat well before the Brexit vote, because of those global economic concerns. Whilst the UK cannot be complacent we should not be overly pessimistic about the economic outlook either. In the medium term if the UK can successfully negotiate some form of continuing access to the European single market then so much the better.

FIVE: BREXIT & UK STOCK MARKET

UK stock markets have also moved sharply - initially to the downside - in the aftermath of the referendum. The FTSE 100 index broke below the psychologically important 6000 level, before going on to test at 5800, from where it has rallied sharply to within 110 points of its 52 week high (as at the time of writing).



The index has been helped by weaker sterling exchange rates as discussed above. Many FTSE 100 companies are exporters, who earn the majority of their revenues from abroad.

In fact, leading investment banks have calculated that up to 75% of FTSE 100 revenues are earned outside of the UK. Much of that money is also generated away from the European Union. In a recent research paper a leading US investment bank noted that UK companies with large overseas exposure were the third best performing group year to date, when compared to more than 20 other assets classes and international stock groupings.

True, certain sectors within the UK, such as Banks and Property have been and to some extent remain under pressure. But if we chart the performance of the FTSE 350 UK Banking sector index against that of its European peers, We find they have effectively moved in lockstep over much of the last 12 months. Suggesting that the issues facing the Banking sector are regional, if not global in nature, rather than a purely UK problem (see chart below).

SIX:
CHEAPER UK BORROWING

UK government bonds or gilts as they are known have appreciated in the wake of the referendum result. Such bonds are effectively UK government IOUs. The initial demand for these securities could be viewed as a post referendum flight to safety by investors.

We note however that in a recent sale or auction of new ten year bonds, the UK government raised £2.25 billion, at a record low interest rate of just 0.91%. The demand for these new bonds was for more than twice the amount issued.

Investors would normally expect to receive a higher interest rate or premium on such bonds, if they perceive any risk at all of not being repaid. That not does appear to be a concern in this instance.

Furthermore at its first meeting post the referendum, the Bank of England's Monetary Policy Committee, which sets key UK interest rates, took no action. Voting eight-to-one to leave UK interest rates unchanged at 0.50%. Despite the expectation of many in the market for at least a 0.25% cut. Attention now moves to the August meeting at which we might see the introduction of additional monetary stimulus, or QE as it's more widely known.

SEVEN: IMPACT ON EU MEMBERS

One of the most debated items in the run up to the UK's referendum vote was the amount of money contributed to the EU from the UK treasury. Various figures were put forward, including the now infamous £350 million per week. Of course whilst Britain is a net contributor to the EU it has also benefited from EU payments, grants and funding. The UK's net contribution to the EU, in 2015, was in the order of £8.5 billion whilst our gross contribution was some £13 billion.

If the UK does leave the EU completely then that net contribution will no longer flow into EU coffers - meaning that the remaining member states will have to pick up the shortfall. It's also possible that budget contributions for the remaining members will rise further going forward. As potential future members of the EU, such as Serbia, FYR Macedonia, Albania and Turkey have developing economies and are therefore likely to be substantial recipients of EU funding for some time, before they can make a financial contribution to it.

There is also a certain amount of political risk for other EU member states arising from a Brexit. Populist anti-EU parties are making gains across the continent. Whilst there is not yet the ground swell of opinion that was seen in the UK, the European establishment will ignore this discontent at their peril. A recent set of inconclusive elections in Spain (the second within a year, despite an economic recovery of sorts) and a forthcoming constitutional referendum in Italy, all point to the fact that the status quo of European politics is open to challenge.

EIGHT: TRADING BREXIT

As we have discussed UK markets moved significantly in the immediate aftermath of the referendum, initially to the downside in most instances. But following that initial period of volatility there has been a recovery. The UK's currency has moved off of its 30 year lows versus the US dollar and back above US$1.30, as some of the political uncertainty in the UK has dissipated. The FTSE 100 index has also recently traded at 11 month highs, benefiting from lower sterling exchange rates. Even the domestic focused FTSE 250 index has recovered the majority of its post referendum losses. We have also seen M&A (Merger and Acquisition) activity return as foreign buyers bid for UK companies, which they perceive to be good value following sterling's recent decline.

Of course we are just a few weeks into an exit process that is likely last for several years and which could take considerably longer to achieve. During that process there will almost certainly be additional periods of volatility. Particularly around key moments such as the enacting of article 50, or the UK commencing negotiations over access to the single market.

Let’s not forget the possibility that the Scottish National Party (SNP) could muddy the waters further. If they try and force a second referendum on Scottish independence, that would be an unwelcome distraction and one that would once again increase levels of uncertainty around the Brexit process.

On the plus side, positive influences would come in the form of any conciliatory signals from Brussels over trade and wider Brexit negotiations and any better than expected UK economic data. Particularly if that data was also better relative to that emanating from the Eurozone.

NINE: WHAT TO WATCH

Weaker sterling exchange rates particularly against the US dollar are currently viewed as a positive for the FTSE 100 index. That relationship could change in the short term, if for instance the pound made and sustained new lows against the US dollar. But as was the case with the initial post referendum move, once the dust settled, we could well see export led sectors and indices in the UK make good gains once more.

The markets real opinion of sterling and sterling based assets can be derived from the performance of UK government bonds - the prices of which have risen and yields (or interest rates paid) have fallen to record lows post referendum. Whilst the appetite for UK gilts (government bonds) persists we can infer that institutional investors remain broadly positive in their outlook for the UK. The Bank of England's almost unanimous decision at its July meeting to leave interest rates unchanged also implies that the outlook for the UK economy is not as dire as was suggested in the days immediately after the referendum.

Many of the issues brought to the fore after the leave vote, such as the potential for slower rates of economic growth in Britain and concerns over the UK banking sector, pre-dated the referendum. Up until which they had largely been ignored by the markets. The leave vote has forced investors to recognise these inconvenient truths. But as we noted earlier these are not localised UK problems, rather they are regional if not global issues and they need to be judged against the wider economic backdrop. As such they will require international, rather than purely domestic solutions.

Gold could be an ongoing hedge against uncertainty and further sterling weakness. The price of Gold has risen by more than 12% since the start of June as the prospects for a rise in US interest rates in 2016 receded. Post-Brexit uncertainty added some additional momentum to that rally. By opening a position in Gold investors are taking a view on the dollar, effectively backing or selling the dollar versus their own base currency. In the current climate, as the US dollar has rallied, so has Gold.

TEN: CHOOSE BLACKWELL GLOBAL

The implications of the UK's vote to leave the EU are clearly profound. But such momentous events inevitably create trading opportunities for investors. Blackwell Global is dedicated to helping you make the most of those opportunities.

Founded in 2010, Blackwell Global was established to offer brokerage solutions for private and institutional clients. Blackwell Global is a Straight Through Processing or STP broker who provide their clients with superior liquidity and price feeds from top international banks. These are offered alongside 24-hour technical support, market research tools, educational materials, professional partnership programmes and fully integrated trading platforms.

We offer access to multiple asset classes including more than 60 currency pairs, precious metals and other contracts for differences. As a global broker, we are always striving to achieve excellence in our customer service, as well as developing innovative technology to support our customers needs.

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