Front page

/ Bringing stability to uncertainty:

How finance teams can prepare & forecast for 2020

October Report 2019

Roomex

It has been over three years since the United Kingdom voted to leave the European Union, and by now, you may be tired of hearing about the speculative outcomes of Brexit. Since there's been another extension to January 2020, more confusion, delays, and uncertainty are on the horizon, making it even more critical to plan for the likely impacts to your business.

A "deal" Brexit would mean the United Kingdom (UK) will leave the EU with a trade deal in place, while a "no-deal" Brexit would mean the UK would leave without any formal agreements regarding trade with its closest neighbours. This "no-deal" scenario could have huge impacts on the UK's economy, including a potential seismic shift in the country's currency.

The uncertainty surrounding the UK's departure from the EU has C-level executives wondering what these changes could mean for their companies. Most businesses and media outlets are focusing heavily on the operational challenges that Brexit presents – how to physically move the imports/ exports between the EU and UK. But another huge issue is being overlooked, the potential volatility and fluctuation in sterling.

As many companies approach the end of the 2019 financial year and shore up budgets for 2020, it is important that both management and finance teams alike are thinking about the impact currency changes could have on their forecasts. But this isn't just important when thinking about 2020 budgets, these changes could potentially have knock-on impacts to your 3 and 5-year financial plans.

Who is this guide for?

This guide is intended for financial decision makers in companies that trade internationally between the UK and EU countries, including:

- **Business Owners**
- **CEOs/Managing Directors**
- **CFOs/Financial Planners**
- **Finance Teams**

What you'll learn

This guide is intended to outline ways to financially prepare and forecast for your business post-Brexit. We have suggested tactics that can be implemented to help reduce your company's risk in the event of large fluctuations in the pound.

This guide will also take a deeper look at accurate forecasting with simple tips to make sure you are getting the most precise picture of your company's future. Beyond your budgets for next year, these tools can be used to better forecast long-term financial projections in the aftermath of the UK leaving the EU.

Table of Contents

Prepare: Controlling Currency to Reduce Risk

Since the UK referendum to leave the European Union was officially passed in June of 2016, the GBP has experienced a significant devaluing and periods of high volatility. In August of this year, it hit a 2-year low, with expectations that it could fall even further in the event of a “hard” or “no-deal” Brexit. Though much of the media attention is focused on trade deals and what the UK import/export market will look like after Brexit, this uncertainty around the pound poses a more immediate and potentially greater risk to business operations. This is especially true for companies that operate between the EU and UK.

In the next sections, we will discuss how your finance team **can** mitigate the risk associated with a volatile GBP.

1. Natural hedging – Riding the wave

If Brexit is a storm, and the fluctuations in the pound are the unusually erratic waves; a natural hedge is riding out those swells.

This kind of hedging is probably the simplest way for companies to reduce their currency risk and involves the company capitalising on their normal operating procedures by reducing their exchange risk as much as possible. For example, if your company relies on a large amount of revenue from the UK market, natural hedging would entail moving the majority of your cost base into the UK, thus reducing the price you pay on the exchange.

As the pound goes up or down depending on the latest political changes and subsequent economy changes, the price you pay for raw materials, labour, and overheads, moves in line with the rates of the market. This allows you to keep your margins as consistent as possible and helps avoid potential surprises when forecasting the year's revenues.

Natural hedging can look different depending on the structure and industry that your company operates in. For some companies, it may be as simple as trying to source a greater percentage of raw materials from the UK market. For others, it may mean moving their entire manufacturing operations into the UK. However, it's important to assess the financial benefit in total to your company before making any decisions about using a natural hedge to protect against volatility.
Unlike conventional hedging methods, natural hedging allows you to easily reduce your risk without the need to purchase complex financial products. Though this could mean a large shift in the operational side of your business, it's a fairly straightforward way and sometimes an easy option for companies to implement.

2. Purchasing financial instruments – Stabilising the ship

If we're still likening Brexit to a storm, the purchasing of financial instruments is essentially buying a bigger ship to try and stabilise yourself as much as possible against the current changes.

By purchasing one of these financial products, you can lock in the rate of the pound, so that a large devaluation has the least amount of impact on your profit margins. The two simplest forms of these products are spot and forward transactions. A spot trade would involve selling the company's sterling at the current market rate and typically takes place within two days of a deal being agreed upon between your company and the financial institution.

Another relatively simple option is a forward foreign exchange contract. In these types of contracts, you agree a fixed rate with the bank for a specified amount of time. Most banks will have a maximum time period for forward contracts, typically no more than 12 months. Though this option protects against negative movements in sterling, it does not allow your company to benefit if there is a positive movement in the currency.

If your company is interested in options that allow for greater flexibility in this regard, two other instruments: a foreign exchange option or participating forward might be suitable. Each of these financial instruments are more expensive and can potentially pose a greater risk if not constructed properly, so should be closely assessed before being decided upon.

3. Reducing reliance on the GBP – Getting out of the water

If worst comes to worst, there is also the option of evacuating during a big storm. But as is with many storms, there is a time to get out while you still can. Another option for companies to reduce their risk, is to reduce their reliance on the pound altogether.

For companies that operate in B2B sales or services, that may just entail invoicing your clients in euro instead of sterling. Though this may not be palatable for every client, it may be worth asking some of your UK clients, particularly those that export to the European Union. If your company operates in B2C sales, depending on your industry, you may also be able to increase prices to make up for negative movements in the pound. However, this should be done with careful consideration of your industry dynamics, competitors and individual brand.

Beyond trying to increase revenues in sterling, it may also be advantageous to consider market diversification. For certain companies, especially those with a heavy reliance on revenue from the UK market, this could be a critical move given the extreme uncertainty of what the UK's economy will look like after it leaves the EU.

Forecast: Tips to Avoid Surprises

Even if you have already forecasted the effects of Brexit on your business, it's important to continue to iterate on those forecasts as more information becomes available. Now that Brexit is around the corner, it's essential to make sure your forecasting is as up to date as possible and any new options to help mitigate risks to the business are evaluated.

When forecasting, your company is able to gain greater visibility into the areas where changes can be made. Understanding what products are driving the most profits, which markets will see the most revenue and what investments need to be made in the short term are all important factors to consider when assessing how Brexit will affect your company.

This next section will give you some best-practice tips on how to improve your forecasts in order to help lessen your company's exposure to risk.

1. Evaluate all of your options

Once an initial forecast for the upcoming year has been created, you should use that to help narrow down the options available to your company. Whether you're considering changing your import/export strategy, purchasing financial instruments to help bring stability to profit margins or just considering sourcing more raw materials from the UK, it's important that you go through the process of forecasting the scenario for each potential option.

This may seem like a lot of work, but it will allow you to evaluate the costs and benefits of potentially large changes to the business. In addition, this scenario forecasting can serve as valuable support when trying to get the backing of stakeholders.

2. Know when to leave the party

Just as important as trying to find solutions to decrease your risk in the wake of the UK leaving the EU, it's equally as important to understand the exact (or near exact) scenario in which it no longer makes sense for the company to be operating in the UK market. To do this, your forecasting should include a calculation of the exchange rate at which UK sales are no longer profitable for your business. This number can then be useful to understand how close or far away you are from needing an exit strategy for the market.

3. Get specific about costs

A good forecast comes from accurate numbers. And the best way to have accurate numbers is to have a firm grasp on not only your projected revenue, but on the likely expenses that will be incurred in the period. With the advent of new financial technology, it's now easier than ever to track what has been spent in previous periods and estimate the likelihood of the continuation of those costs.

There will always be some areas of your business where you can't fully itemise spend. But, when the economy is in flux, and businesses are in full cost saving mode, it's important to have a detailed view into all spend. One of the biggest areas of disorder is travel spend. For example, the majority of CFO's and Finance teams don't place controls around business travel- yet it can account for up to 10% of their total operating expenditure.

Roomex is the best tool in the industry to get full visibility into hotel spend, while shortening month's end close with a single invoice. Roomex helps businesses understand the key cost drivers behind their business travel spend. When you have the full view, broken down by internal reporting codes, CFOs have the data they need to make cost saving decisions. Learn more about ways Roomex can save your business money by getting in touch with one of our travel experts today.

Wrapping up

No matter what happens with Brexit, during this time of economic instability the pound will most likely fluctuate over the next few months. Though we don't know if this will be a positive or negative shift, now is the time to assess how it will affect you, if you have not yet done so. A clear plan of action will ensure that your company is prepared to face the uncertainty of the next 12-18 months.

These tips are a roadmap for getting started, but we recommend devising a plan by sitting down with your senior management team, financial advisors, investors, and other stakeholders to develop a comprehensive plan. In addition, many EU countries are offering government support for companies planning in advance of Brexit. We recommend reaching out to your local government agencies for further advice.

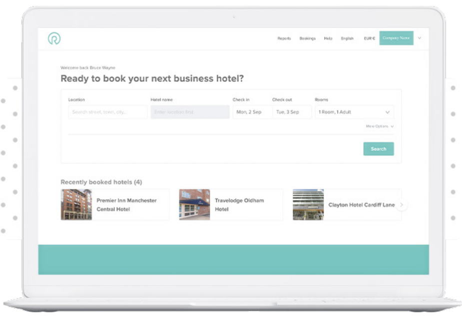
> When devising your Brexit plan, consult Roomex for your business travel needs and queries.

We are the free, B2B, self-service hotel management platform with expert support, offering cost savings, a simplified expense management system, a single monthly invoice and the best rates on all hotels globally.

In a world in flux, it can be difficult to forecast and stay on budget. With Roomex, you'll always get the best prices on business hotels globally, while keeping the entire company on budget thanks to our 100% accuracy on travel programmes.

Want to learn more?

Get in touch with one of our workforce travel experts today



Roomex

Contact:
+44 20 7183 7737
roomex.com
business@roomex.com