FOREX CASE STUDIES

Market Turbulence in the Past Decade in the Words of Traders

Simon Kostrava

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Author: Simon Kostrava

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1. Forex case studies

There is much turbulence in today's financial markets. Numerous political and nonpolitical events impact currency rates, equity and bond prices. Some events can have a really broad and strong influence and change the value of your holdings, or even zero them.

Although we do not want to see a financial Armageddon, we should to be prepared. There is no better way of preparing than by looking into history. In my opinion, events are not repeated in the same way, but to know the mistakes of the past can help you to adapt to the future.

We have chosen three case studies from the last decade to show you what can happen on the markets.

We cover and describe the history of the Swiss National Bank (SNB) and its attempt to cease strengthening the Swiss franc, followed by its approach that resulted in a sudden market crash. A crash that erased almost USD 1 billion from financial

markets and left many participants in debt or bankruptcy.

Next, we explore the recent story of the Brexit referendum, the result of which was surprising to many participants. However, it has not led to severe losses, as banks and brokerages were able to learn a lesson from the year-old incident with the Swiss franc.

As a bonus, we write up the history of Slovakia entering the eurozone. Replacing the Slovak koruna with the euro brought about unusual situations, which suggest illegal actions relating to insider trading. This part of an otherwise successful story concerning Slovakia's entry into the eurozone is not widely known.

All three stories are written not only in a factual way, but also in the words of direct participants. In other words, traders with whom we spoke in an attempt to reconstruct what people on the trading floor of banks and brokerages thought in relation to the aforementioned events. How were they prepared for such unexpected events and how did they react in the moments immediately after they

happened?

At the end of the book, we offer you some advice about current currency markets. Can we see patterns similar to above-mentioned events? Could another currency experience an SNB-type crash? Will another country vote to leave the European Union (EU)? Can the fixing rate of another currency entering the eurozone be manipulated?

2. How the Swiss National Bank ruined the party (twice)

2.1 Safe haven

When you think about a currency that can withstand any crisis, only one springs to mind. The US dollar. The king of currencies. Sometimes, however, you want to have two currency options with security. So, if you think a bit more, you will conclude that the second best currency option in a crisis is the Swiss franc.

Switzerland, a country of secret bank accounts and solid bankers. A country of neutrality throughout history. No wars and a persistent tendency to remain on good terms with everyone everywhere.

So, your second choice is clear. In a time of crisis, when other currencies weaken, the Swiss franc will definitely hold or even increase its value.

Of course, a strong Swiss franc can sometimes make people in Switzerland, especially in the SNB, nervous. Exporters are first in line when it comes to being unsatisfied. And, in a country that is well

known around the world thanks to its watch manufacturers, you can be sure that their voice is clearly heard. A strong franc kills the economy and subsequently employment. You can bet your money that the Swiss Government and the SNB will sometimes listen to those voices.

The first such attempt of note was in 1978 when, after years of strengthening, the SNB decided to set a CHF/DEM floor at the rate CHF 80 for DEM 100 (or CHF 0.8 for DEM 1).

This floor led to a weaker currency situation for Switzerland, while, as a secondary effect, it also brought about inflationary tendencies in the economy. The SNB abandoned this floor in 1982. In other words, it took four years before they realized that they cannot compete with market forces. Unfortunately, they did not learn from that. And if you don't learn from your own mistakes, you can bet that you will repeat them in future.

2.2 When interventions do not work

As usual in times of crisis, people on forex markets tend to move to safe havens: namely, the US dollar, the Japanese yen and the Swiss franc. One year that was special in this regard was 2008, when the mortgage crisis in the USA escalated and Lehman Brothers filed for bankruptcy protection on September 15. The world was full of financial problems.

The Swiss franc highlighted what people do when they think about a safe haven on the currencies market. The shift in the CHF/EUR rate – from CHF 1.60 for EUR 1 to CHF 1.45 for EUR 1 – in the course of the turbulent 2008 was not surprising.

However, those in the SNB and in Switzerland's exporting industries were not celebrating. This move could cause big problems for them, so the SNB decided to intervene. This intervention started in March 2009 in the form of buying euros and US dollars against the Swiss franc. The supply of Swiss francs on the markets was abnormally high, which should have led to a weakening of the Swiss franc. Unfortunately, the world economic outlook was so

bleak that demand for the Swiss franc as a safe haven was also abnormal. And, even with the SNB's overwhelming desire to weak Swiss currency, market power was stronger. The Swiss franc continued to weaken and moved to levels below the CHF 1.30 for EUR 1 rate.

Graph – CHF/EUR exchange rate 01.04.2007 to 08.31.2011

(source: European Central Bank)

The SNB was in an unenvious position. Its foreign reserves ballooned to over CHF 200 billion as a result of interventions on forex markets. However, due to the continuing strengthening of Swiss francs, the loss on foreign currency reserves ballooned too, to the tune of CHF 26.5 billion in 2010 and another CHF 11.7 billion in the first half of 2011.

These losses were negatively regard by the Swiss public, while calls for the resignation of the head of the SNB, Philipp Hildebrand, grew louder and louder. In the years before 2010, the SNB used to divide its profits between the state and the regions of Switzerland. However, for 2010 and 2011, no promises were made regarding any financial reallocation from the SNB.

The intervention was too weak to stop the Swiss franc from strengthening.

2.3 The SNB ruins the party for the first time

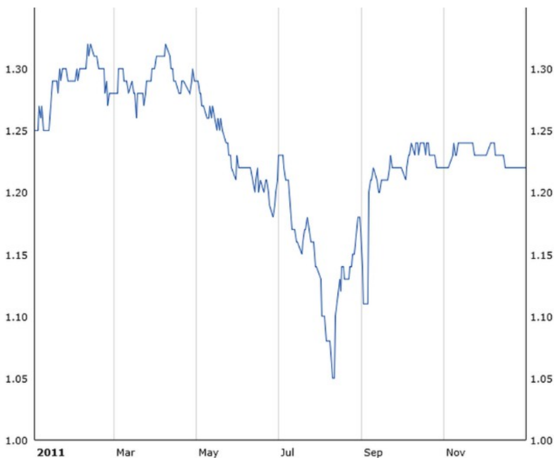
The strengthening of the Swiss franc continued at a much faster pace in 2011. During the summer months of 2011, the rate of the Swiss franc against the euro dropped below 1.1000. That rate was alarming for the SNB. Forex interventions did not work, nor did verbal interventions.

On September 6, 2011, minutes before 9.00 GMT, the SNB published its announcement that the current value of the franc was a threat to the Swiss economy. The SNB subsequently set the floor on the CHF/EUR exchange rate at CHF 1.2000 for EUR 1. The SNB also announced that it was prepared to buy foreign currency in unlimited quantities and defend the floor with the utmost determination.

This safe haven ceased to be. Currency traders saw the rate immediately move from CHF 1.0950 for EUR 1 to CHF 1.2000 for EUR 1. A 9.5% move is pretty wild, given that, on currency markets, anything more than 1% is considered as a sharp move. Several bank traders were caught out with big losses, along with many retail traders. However, with an average margin of around 5%, most of them

were able to cover their recorded losses.

Graph – CHF/EUR exchange rate 01.01.2011 to 12.31.2011



(source: European Central Bank)

TradeFloor view:

There was an interesting story behind the main fact that the SNB enforced the floor on the CHF/EUR rate.

According to the newspapers, which obtained information from a political opposition party, which in turn obtained information from a source in the SNB, in August, Kashya Hildebrand, the wife of the SNB head, made a CHF 60,000 profit on a currency transaction involving a CHF/USD pair. She had bought the US dollars just a few days before the floor was introduced.

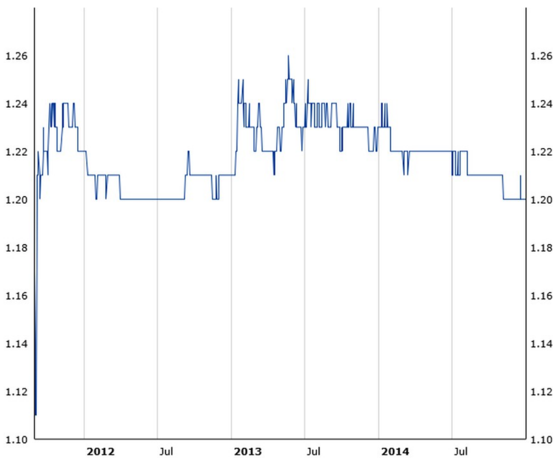
The transaction was reported by Mr. Hildebrand to the compliance department in the SNB. When later asked about the transaction, he argued that his wife had a strong personality. Mrs. Hildebrand had her own art shop and regularly bought US dollars for her company. The timing of this conversion was very lucky and she personally identified a weakness in the US dollar at that time. It is very hard to decide whether Mrs. Hildebrand is generally a skillful currency trader, whether she had a case of pure luck or whether she received some information beforehand.

The independent investigation into this transaction reported that the trade was delicate, but did not breach any SNB guidelines.

2.4 Three and half years of "stability"

After the rather surprising move of the SNB, markets and forex traders tried to learn how to live with it. At the beginning, there was a fear that the SNB would move the floor further up in a near-future run on the market, where the Swiss franc might even fall to the CHF 1.2400 for EUR 1 level. Meanwhile, other market participants tried to fight the SNB regarding its utmost determination to keep the floor intact. The SNB and its officials repeatedly stated: "The SNB will keep the floor with the utmost determination." These officials gave no indication of any movement or that it would cancel the floor in the near or distant future. Many forex traders, therefore, adapted to the prevailing situation. Sometimes they tried to fight with the SNB, other times they allowed the franc to reach higher levels. The CHF/EUR rate traded in a narrow range between 1.2000 and 1.2500, depending on which rumor prevailed. There was a little volatility, which coincided with a regular quarterly meeting of the SNB, but, as time passed, even this event was neglected.

Graph – CHF/EUR exchange rate 08.31.2011 to 12.31.2014



(source: European Central Bank)

TradeFloor view:

Well, the free float finished on the CHF/EUR pair, or at least the one that should have led to increasing the value of the Swiss franc. We had to adapt to it. When we tried to reach 1.2000, the SNB appeared on the markets and carried out many trades in millions and

millions of US dollars or euros. 1.2000 was secured with big orders overnight and the daily service of SNB trading desks.

Our clients decided to pursue a simple strategy: selling CHF/EUR put options with strikes on 1.2000 at the start, then later with even higher strikes, as volatility substantially decreased in the following days. The idea was very simple. The SNB were to keep 1.2000 at any costs, so if you were trading on a margin, i.e., a premium for an option at the full amount, even a small one, would have given you nice interest on the margin. So you deposited your money on nice interest and the risk you took seemed very small.

Margin requirements fall down with a decrease in volatility. So you would have been able to sell EUR 1,000,000 put options and Swiss franc call options with a maturity of three months with just a margin of EUR 10,000. Just 1%. With a premium of 0.20%, you would have got on option amount worth EUR 2,000. So let's compare earnings of EUR 2,000 against your EUR 10,000 margin, and you have nice 20% profit over three months.

If your strike was some pips above 1.2000 and your option expired, you just swapped it and waited until the rate was at your strike. With a general feeling that the floor would be kept by the SNB forever, it seemed like perpetuum mobile for profit with low risk. Now, everybody knows that the risk was underestimated. However, during these days, every retail trader was doing the same. Selling CHF/EUR put options and waiting.

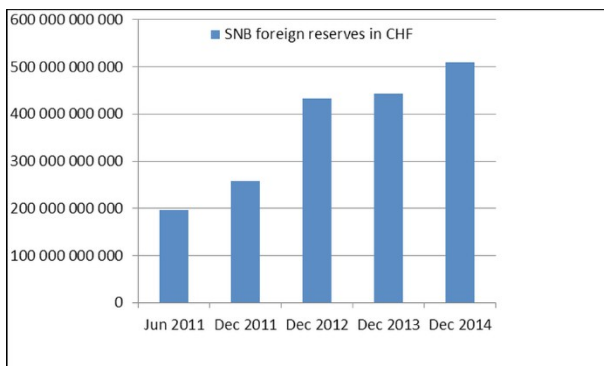
What was important to watch was the eurozone, in case of any possible nervousness there or any emerging crisis. And, believe me, there were lots of those during those three years, when the Swiss franc had a tendency to move to the floor. Any crisis meant running towards safe havens: the US dollar, the Japanese yen and the Swiss franc. However, the Swiss franc was limited by the floor at 1.2000 and the SNB was very strict in keeping it.

The SNB was on guard every single second. Verbally, it reiterated its utmost determination to keep the floor at 1.200, and, in the real world, it was able to sell any amount of Swiss Francs it wanted to. It is

always easy for the SNB to depreciate the Swiss currency. Metaphorically, it owns the printers and can print any amount it wishes. If it tried to do the opposite, i.e., to keep the Swiss franc strong, it would definitely have failed in its battle with the markets as it did (does) not have infinite amounts of foreign currencies. The only infinite supply it had was its supply of Swiss francs.

On the other hand, with many interventions, SNB foreign reserves rose very quickly. They more than doubled during these three years. Whenever some kind of crisis, either big or small, emerged, which was often the case with weak eurozone politics, the SNB had to intervene with large amounts involved. It sold the franc and bought euros and US dollars. It tried to invest its foreign reserves in the bonds of robust countries, like Germany; however, its supply was not infinite. The interest rates of bonds collapsed due to the overwhelming demand for them, as well as the unstable political environment. The job of the SNB started to get harder as it began to encounter problems in investing in foreign reserves at reasonable prices.

Graph – SNB foreign reserves in CHF



(source: Swiss National Bank)

2.5 The SNB ruins the party for the second time

The situation in the eurozone in December 2014 was very nervous. Speculation about European Central Bank actions, to be announced at its next regular meeting on January 22, 2015, was rife. The general feeling was that the European Central Bank would announce quantitative easing, which the expected result that it would further weaken the euro and subsequently apply pressure so as to strengthen the Swiss franc.

Meanwhile, the SNB, at a regular meeting on December 14, 2014, introduced negative interest rates on deposits in order to support the CHF/EUR floor. However, this move did not prevent the Swiss franc from strengthening. As a decision about quantitative easing in the eurozone was in sight, the euro weakened more and more, such that pressure on the Swiss franc started to be very strong.

During the first days of January, the chairman of the SNB, Thomas Jordan, described the floor as absolutely central, while the vice chairman of the SNB, Jean-Pierre Danthine, stated on Monday, January 12, 2015, that the floor would remain the

cornerstone of SNB policy.

TradeFloor view:

The big bang happened on January 15, 2015, in the morning. Just a few days before, SNB officials reiterated that they would keep the floor at 1.2000 with the utmost determination. Markets stayed in their typically stable mood when the rate was a little bit over 1.2000. However, the situation in the eurozone was nervous. Even in such circumstances, nobody expected any drastic action regarding SNB policy. If it had bought billions in foreign currencies in the last three years to keep the floor intact, why would they not buy another billion in the following month?

At 09.30 local time, all Reuters and Bloomberg screens went red with the breaking announcement from the SNB. The floor at 1.2000 was canceled immediately. The interest rate on Swiss franc deposits was lowered to -0.75% from -0.25%.

Markets went crazy. Everybody was trying to get a price for EUR/CHF, but nobody was willing to quote anything. After 10 minutes of frenzy, everybody realized that the market for CHF/EUR did not exist.

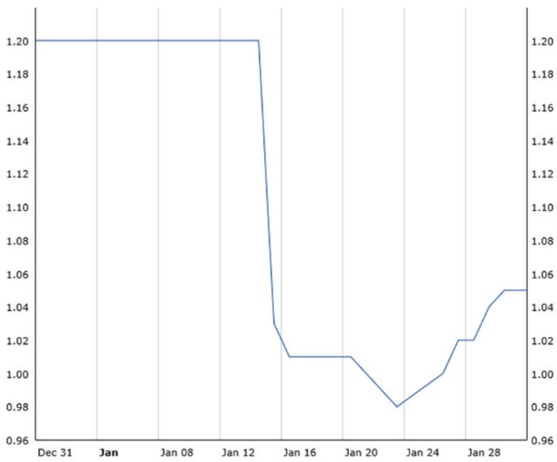
Remaining calm and quiet, everybody was in a waiting mode.

Then, around 10.00, half an hour after "Francogeddon", as somebody quickly started to call it on social networks, the first quotes showed up. Approximately CHF 1.0100 for EUR 1. The news spread like wildfire. Typically, EUR/CHF was quoted with a two-pip spread (0.0002), but we now saw a one-figure spread instead (0.0100). Next, new quotes showed that the fall of the euro against the Swiss franc was continuing. 0.9800, 0.9600... 0.8700 and, finally, 0.8500. Then the market went back a little bit to 0.9500. Still, the move meant that the Swiss franc had strengthened by almost 30%.

In the following hours, risk managers started to calculate how much we had lost, how much our clients had lost. Any given stop-loss was fulfilled at a much lower rate than the rate put in the order.

That day was worse than anything we had experienced in the past and everybody hopes that we will never experience it again.

Graph – CHF/EUR exchange rate 12.31.2014 to 01.31.2015



(source: European Central Bank)

2.6 Counting the losses

The days following “Francogeddon” were very sad on the financial markets. From all sides of the markets and industry, you only heard about the losses.

This move caught almost everybody unprepared. As the SNB head said: “The decision has been a surprise for the markets; you cannot do it in any other way.” Later he added that the SNB came to the conclusion that the CHF/EUR floor was not a sustainable policy.

Counting the losses could now start. At first, equity markets in Switzerland took a big hit, with stock prices falling by over 15%. At the same time, big exporters in Switzerland announced that their profits for the relevant quarter would be substantially lowered by the strength of the Swiss franc, while the outlook for them looked worse as it all depended on this currency’s future movements.

Then there was the typical retail forex trader. It did not matter whether he had a stop-loss order in place or not, his losses were around 30% of the notional amount of his positions. With a margin requirement at the level of 2% from the notional, he immediately

owed his brokers 28% of his previous positions.

Next in line were the retail brokers, who called their clients to cover their margins and debts. However, the responses were very poor. So now it was their turn to adjust their expected profitability and outlooks. Legal departments got a free hand in dealing with retail debts. Losses in the brokerage industry were estimated at approximately USD 1 billion.

Big banks had their share of losses too. However, as trading positions were not calculated with particularly small margin requirements, losses were not as crucial as they were for retail brokers and retail traders.

Last in the line of losers was the general population in Poland and Hungary. As interest rates on the Polish zloty and the Hungarian forint were always way above the rates for the Swiss franc in Switzerland, the popular move by banks was to offer mortgages in Swiss francs. You borrowed them at the Swiss interest rate, immediately exchanged them into your domestic currency (zloty or forint) and then bought your apartment or house. In future,

you would have to convert your installment from zlotys or forints back to Swiss francs every single month. You were happy with lower interest rates. But this only worked if the Swiss franc, your funding currency, stayed unchanged or weakened over time. Once it started to strengthen, your funding costs and installments rose. Yes, this is exactly what happened. The Swiss franc was 25% stronger than before, your house in terms of your mortgage immediately cost you 25% more than it did the day before. The problem in Poland and Hungary was so big that even the respective governments had to deal with it, typically by trying to transfer costs to the banks.

TradeFloor view:

The days following January 15, 2015, were hard to swallow. First of all, losses had to be calculated. We have to decide when to stop our Swiss franc positions, whether to wait for some improvement or stop them immediately. That is a purely trading decision. The hard decision when you are in uncharted territory, but the decision you, as the trader, has to be able to do.

Then there was an internal review of our trading practices. Every big unexpected loss means that a bank or a broker or any institution wants to learn something from it. That's because the clever guys are the only ones who never repeat their mistakes. Secondly, a bank usually investigates whether there was some noncompliance issue, such as fraud or deception in terms of whether everybody kept within the trading limits that are always in place. Any breaking of the rules leads to the immediate firing of the responsible persons, after which a new set of rules is introduced. In this particular case, the focus was on other currencies, which had floor or similar forex limits in place. The Czech crown and the Danish krone were suspects in this case. New limits on trading with these currencies were set. But only stupid ones, which would repeat the loss and the situation with the Swiss franc on other currencies.

The Swiss franc later went a little bit back and currently trades around CHF 1.0900 for EUR 1. So, banks and traders who, in a hurry, closed positions immediately on January 15, 2015, lost three times more than they would have lost if they had kept their

position open. But that is always the problem when you face big losses and insufficient collateral. You have to make decisions and you do not have the time to let things evolve in some way.

The Swiss franc case was very costly for many forex traders and I would say that forex trading will never be the same as before.

3. Brexit: how a bad idea turned into a market crash

3.1 How the bad idea happened

Political situations always impact the markets. Whatever is said, thought or done in the name of politics can have a great influence on currency and equity prices. The British pound is no exception.

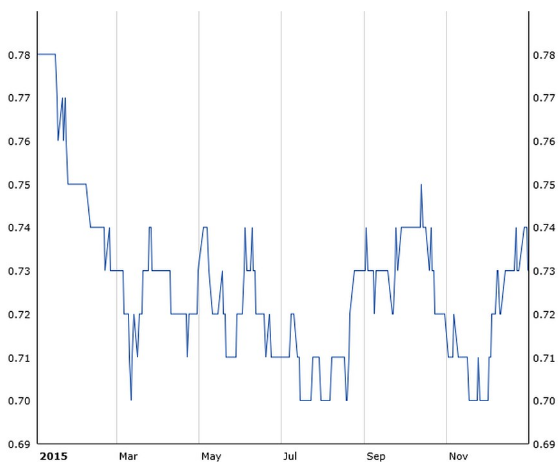
When David Cameron, the former UK Prime Minister, spoke about a referendum regarding membership of the EU, everybody thought it was just a political gesture to gain more votes. He needed to take the wind out of the opposition by calling for a renegotiation of the UK's agreement with the EU. And, while his attempt was very successful, some people still believed he would not call a referendum any time soon, even if he were to win an election in 2015.

However, David Cameron kept his promise and, after his surprising return to 10 Downing Street in 2015, on February 22, 2016, he announced the date when a referendum about the UK leaving or staying in the EU would take place.

GBP/EUR and GBP/USD are two of most traded currency pairs in the world. Any nervousness about the British pound has an impact on global currency and financial markets.

The British pound was relatively strong against the euro in the second half of 2015. However, as the final decision about the referendum drew closer, the pound started to weaken substantially.

Graph – GBP/EUR exchange rate 01.01.2015 to 12.31.2015



(source: European Central Bank)

TradeFloor view:

In December 2015, the GBP/EUR rate was at the level of GBP 0.7000 for EUR 1. From that day onwards, the pound started to weaken. It finished the year at GBP 0.7370 for EUR 1, which was 5% down on what is was in mid-December. 5% in forex trading is a hell of a move. Such a move in December, where every trader tries to get his P/L at the right numbers, can kill your mood. If you are not on the right side of the market with your positions, you can finish the year in the red or under the budget mark. And you can be sure that

underperforming will not be forgotten next February when bonuses are paid.

The problem with the UK referendum was that lot of people still doubted it would really happen. I saw a lot of traders who believed that, with the positive interest rate differential between the British pound and the euro, as well as a good outlook for the British economy, GBP/EUR would break the 0.7000 level. The 0.7000 level was a big psychological barrier. Not just because it was a nice, rounded number, but also because we had not seen this level in the last five years. The breaking of the 0.7000 level would mean that the crisis for Britain was over and its economy was flourishing (at least compared to the eurozone).

Unfortunately, politics decided otherwise. What started as a good move to gain voters turned into a series of events that changed the direction of the markets. We saw the first signs in December 2015.

January and February simply confirmed what we saw in December. The pound fell further to a level around GBP 0.7700 for EUR 1 in mid-February. That is a 10% weakening against what it was in mid-December. 10% in two months, what a move. It could have

earned you lot of a money or lost you a lot very quickly, depending on whether you were clever enough to have had the right position.

After the SNB events in January 2015, trading limits and margin requirements were set very strictly. So, even a 10% move did not cause the bankruptcy of any brokerage or trader. Everybody knew at that time that moves could be very quick and very steep.

Monday, February 22, 2016 was just another day for the already steep weakening of the British pound. In seconds, we moved 50 pips (or 0.0050), while three days later the rate was 0.7900. Another 2.2% weakening against the level from Friday, 19 February.

3.2 The days before Brexit

The date of the referendum, when the UK would vote to either leave or stay in the EU, was set for Thursday, June 6, 2016. The British pound reacted appropriately. Until the beginning of April, the GBP/EUR currency rate moved to GBP 0.8100 for EUR 1. Then the pound started to strengthen when there was a general belief that the UK would stay in the EU.

However, polls from different agencies showed that the result would be very close. Meanwhile, betting companies, in their odds, showed a probability of over 80% for a referendum result to remain.

Volatility on the GBP/EUR market decreased during May, while we saw levels around 0.7600 at the beginning of June. Then doubts started to grow as the decision day got closer. Polls showed that more and more people would likely choose to leave, although betting companies' probabilities for a decision to remain were very high.

The general sentiment was hard to read and the pound started to depreciate in the days before the referendum. In the first days of June, the pound fell

to 0.7900 from 0.7600, which equated to another 5%.

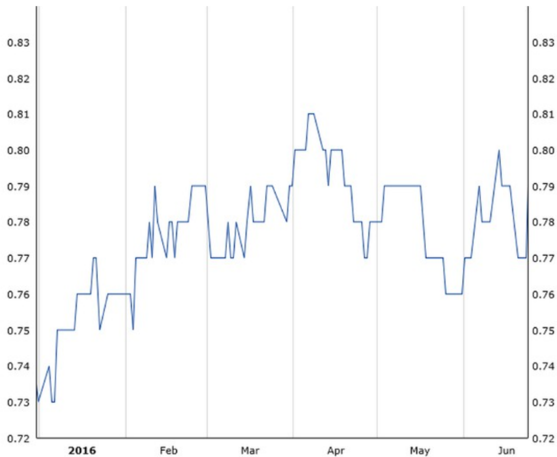
One thing was sure, the result could cause a very big movement on several markets, not just those of the pound. Having learned their lesson in January 2015 when the SNB canceled its floor on EUR/CHF, brokerages did not want to repeat the same mistake again.

In early June, they drastically increased the margin requirement for all currency pairs, with the main increase for pairs involving the pound. Before 2015, we were used to margins of around 1 or 2%, whereas, after the SNB bloodbath, margin requirements started to rise. In days before the UK referendum, brokerages asked for margins as high as 20% for GBP/EUR and GBP/USD currency pairs. A surprising result could cause a really big fall for the pound, while brokerages would not be able to afford another major loss a few months after they had lost almost USD 1 billion as a result of the SNB crash.

The fortnight before the UK referendum brought further strengthening of the pound. The rate on June

15, 2016 was GBP 0.7900 for EUR 1, while June 22, 2016, EUR 1 was worth GBP 0.7700. The general market feeling in the City of London was that the UK would remain in the EU.

Graph – GBP/EUR exchange rate 01.01.2016 to 06.23.2016



(source: European Central Bank)

TradeFloor view:

The general feeling among traders in spring 2016 was that the UK would vote to remain. We started to follow bookmakers' odds on a daily basis, as we thought that they would know more than we did. They saw real inflows from the general public. In the event that the attitude of folk in the UK started to favor leaving the EU, the subsequent inflow of stakes in this regard was expected to force bookmakers to decrease the odds for "leave".

When bookmakers stayed put with their odds and continued to indicate a probability of around 75% for "remain", nobody was afraid to trade with the British pound. Everyone waited for the pound to strengthen.

In early June, the situation changed dramatically. More and more polls by different outlets showed that the result would be very close or even that the "leave" campaign was slightly ahead. Nervousness was in the air. The main recommendation from risk management was to stay put regarding the day of the referendum and only maintain minimum positions in the days ahead.

The only thing that calmed us down was the strong

position of bookmakers, who still kept the odds for "remain" very low. There were only two possible explanations for this. Either they had their own polls with quite different results than the published polls, or they were not seeing any inflow from people on the "leave" side. Bettors were probably overly sure that result would be to "remain".

3.3 D-Day

TradeFloor view:

On Wednesday, the day before the referendum, the mood was pretty nervous in dealing rooms. There was a rumor that the biggest banks and hedge funds would run their own exit polls during referendum, which, according to the law, could not be published, as well as ruin their trading, according to them.

If that rumor was true, then, according to the GBP/EUR rate on referendum day, we could have estimated the final result.

The trading strategy for Thursday, June 23, 2016, was to follow the rest of the markets and jump on the wave if a clear direction was obvious.

As bookmakers still kept their low odds for "remain", financial markets were silent – nervous, but silent. Some traders started to build up small pound positions in advance.

D-Day – June 23, 2016 – started very calmly. Any polls that hedge funds commissioned would not have received any reasonable numbers sooner than early afternoon. When the British pound started to gain a

little over lunchtime, the mood was very good. The small move from GBP 0.7700 to GBP 0.7630 for EUR 1 was celebrated as confirmation of a "remain" result.

A lot of London banks and hedge funds decided to run night shifts just in case the results were published in the early hours. After a promising afternoon and evening, nobody doubted that the night shift would be easy.

A lot of traders with small pound positions went home for the night to get some sleep.

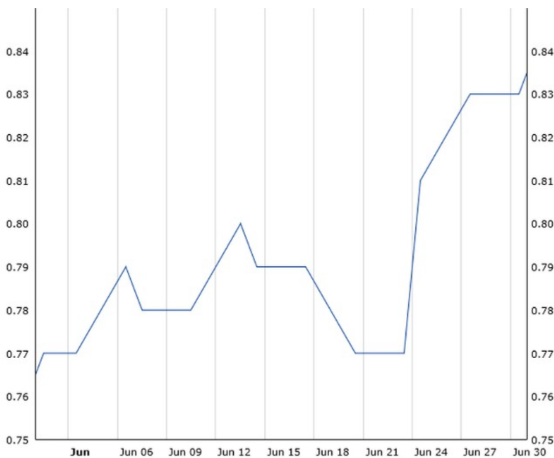
The craziness started just before midnight. Exit polls published by TV stations showed that the result would be close or even that "leave" would prevail. These polls changed everything.

The pound immediately dropped by 2.5% to GBP 0.7800 for EUR 1, with the drop getting bigger and bigger every minute. In the morning, we stayed at GBP 0.8185 for EUR 1. That was a 7% fall in value.

Friday was very nervous, with the GBP/EUR rate moving sideways a few times in wide two-figure ranges (0.8000 to 0.8200). "Leave" was inevitable and the markets reacted appropriately.

The only hope was that any pound position that had been open the day before, which was really low value or even had a 7% drop in value, would not cause any significant hole in banks' or brokerages' balance sheet.

Graph – GBP/EUR exchange rate 06.01.2016 to 06.30.2016



(source: European Central Bank)

The results of the referendum were rather surprising. Not for the public, but for politicians and financial markets. Even on the day of referendum, almost nobody on the financial markets expected that the will of the UK would be "leave".

The results were published on the morning of Friday, June 24, 2016. There were 17,410,472 votes for "leave" against 16,141,241 votes for "remain". That is, 51.89% to 48.11%. The UK had voted to leave the EU.

3.4 The days after Brexit

The week after the referendum, everybody realized that the process for leaving would be long. Politicians who backed the "leave" campaign were unwilling or unable to offer any subsequent plan for leaving. UK politics appeared very weak and to lack awareness.

Everybody on the markets realized that this instability in the UK could last for a few months, while the process for leaving the EU could last a few years.

In early July, the GBP/EUR fell to GBP 0.8600 for EUR 1. Then, after the leadership situation in the Conservative Party ended with the new Prime Minister Theresa May taking office, the pound gained a little bit to move to GBP 0.8300 for EUR 1.

However, during August, as the situation regarding the process of exiting the EU continued to lack clarity, the British pound fell further to levels greater than the rate of GBP 0.8700 for EUR 1.

TradeFloor view:

Days after the Brexit result were funny. Politicians from the "leave" campaign resigned one after another, while there was seemingly nobody capable of leading the UK.

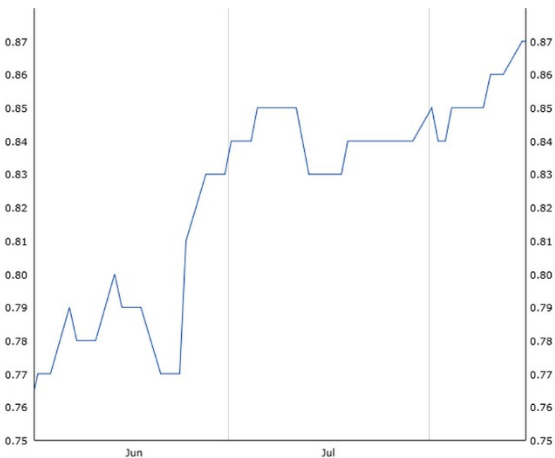
Trading in such a scenario was easy. You just sold the pound and waited. And, provided that nothing really bad in the eurozone did not happen in the meantime, you could use this strategy for a long while.

Instability in politics means higher volatility on the markets. And that is an environment every trader likes. You cannot earn money on a stable, unchanged market. You need moves towards profit. Well, not 20% in one hour, but a few percent in a month is not bad.

The British pound looks like a promising currency from this point of view. The exiting process will bring about many turns and new events supporting the pound's volatility. What now looks like simple scenario – "sell the pound and wait" – can easily change one day.

Graph – GBP/EUR exchange rate 06.01.2016 to

08.15.2016



(source: European Central Bank)

All the events between announcing the referendum and the results, as well as the current unclear state regarding leaving the EU, have led to a sharp decrease in the value of the British pound. In one year, the pound lost over 24% against the euro (from GBP 0.7000 to GBP 0.8700 for EUR 1) and almost 20% against the US dollar (from USD 1.5500

to USD 1.3000 for GBP 1). Further instability and a long process for leaving the EU could lead to another decrease in the value of the pound as financial markets do not like uncertainty.

The UK referendum is a good example of how politics can influence financial markets and how hard it is to predict the outcome of political events.

The only good result that we can see in the events surrounding Brexit is in terms of the adaptability of financial institutions. They were able to withstand the unexpected Brexit result and not report any substantial trading losses. The lessons from the SNB crash were learned, while new limits and process were quickly adopted in a short time. The fall of 7% in one day had no substantial impact on balance sheets, with no unpaid debts left by retail traders on that day. Even the fall of 20% in a month was not critical for banks and brokerages around the world.

4. The Slovak koruna rate-fixing case

4.1 Slovakia on the road to the EU

Slovakia became a member of the EU in 2004. By signing the EU accession agreements, Slovakia undertook an obligation to enter the eurozone as well. Despite no specific timeline, there was a general opinion that entry to the eurozone ought to happen sooner rather than later. There was quite a difference between Slovakia and other Central European countries. The Czech Republic, Poland and Hungary have chosen to keep their national currency for the time being and are not clear about when they will enter the eurozone. As the obligation to enter the eurozone, which was also part of their respective accession agreement, does not carry any penalties, it remains their choice to pick the right time when to replace the koruna, zloty and forint, respectively, with the euro.

Slovakia was a different story. It is a small country that was established in 1993, after splitting from the Czechs, and underwent much political turbulence between 1993 and 1998. After pro-EU and right-

wing parties gained power in 1998, entering the EU was the main aim for everybody. And nobody doubted joining the eurozone either. A country with five million inhabitants and an economy that is dependent on exports, with Volkswagen and US Steel as the main drivers of economy growth, does not have many choices in terms of how to flourish. So adopting the euro was inevitable.

The Slovak koruna, Slovakia's national currency, was launched in 1999 at the rate of around SKK 42.000 for EUR 1. Let us move forward quickly. Despite several political disturbances, Slovakia experienced a decade of economic growth, which was reflected in the currency rate.

A quick tour of important events before moving onto the most interesting part of the story:

> April 16, 2003 – Slovakia signs the accession agreement with the EU, which includes an obligation to replace the Slovak koruna with the euro.
>
> July 16, 2003 – Slovakia adopted a national

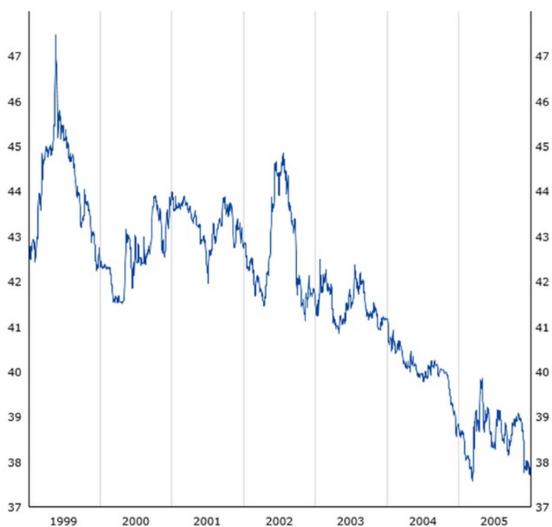
strategy for adopting the euro.

November 28, 2005 – Slovakia enters the European Exchange Rate Mechanism (ERM) II.

The ERM II is a currency stabilization system, where participating countries bind themselves together by maintaining currency rates in the range of +/- 15% from central parity. The ERM II serves as a stabilization mechanism and is compulsory for every country that would like to adopt the euro. Every country should be in the ERM II at least two years before the date of eurozone entry. By entering the ERM II, Slovakia showed its utmost determination to replace the koruna with the euro in the near future.

Graph – SKK/EUR exchange rate 01.04.1999 to

01.01.2006



(source: European Central Bank)

Central parity at the time of entering the ERM II was set at SKK 38.455 for EUR 1. The range of fluctuation in the ERM II was, therefore, set at SKK 32.686 to SKK 44.2233 for EUR 1. The Slovak

National Bank undertook a commitment to use all necessary tools to keep the EUR/SKK exchange rate in the set range.

The exchange rate can reflect overall economy performance. In seven years, the Slovak koruna moved from SKK 42 for EUR 1 to SKK 38 for EUR 1. A 10% improvement is a never bad thing.

TradeFloor view:

1998 was a pretty volatile year for the Slovak crown. In November, it dropped like a stone. And, as the exchange rate fell to SKK 47 for EUR 1, interest rates skyrocketed to 100%. A common liquidity crisis had come to Slovakia.

The situation much improved in the spring of 1999. Interest rates went back to normal levels, first to 20% and then lower to single digits, which meant it was an ideal time for currency speculators. As the country moved closer to the EU and subsequently to the eurozone, with a positive interest rate differential between the Slovak koruna and the euro, the only thing that currency traders had to keep in mind was having enough margin to cope with a negative shock. I just pushed as many forwards as possible, or as

much as my risk managers and margin allowed. I just kept it and swapped it for longer and longer periods of time. The interest rate differential brought me additional profit, and I just sat and waited and calculated the profit.

Of course, there were also hard times, such as when the Slovak koruna fell back to 45 from 42, usually due to some stupid political dispute. But clever margin management lets me sleep peacefully, even during such times.

The Slovak koruna had firmed up by 10% in seven years, which is not much. But, if you add the interest rate differential I pocketed during those seven years, and with the margin requirement around 10%, which meant I slept well, even in volatile times, I was able to triple my initial investment.

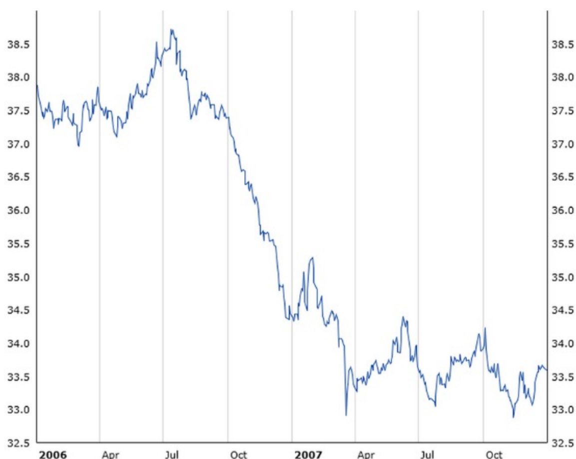
Overall, this was like the good old days, when all your trading strategy was about was to exploit the positive interest rate differential and Slovakia's convergence with the EU.

4.2 Once in the EU and the ERM II, the future is bright

In June 2006, general elections took place in Slovakia. After eight years of a conservative right-wing government, the leftist party Smer won, which made the markets nervous. In the pre-election campaign, Smer often attacked the right-wing government over reservations about politics towards the EU and joining the eurozone. Therefore, the markets reacted strictly based on election results. The SKK/EUR rate fell from SKK 37.00 to SKK 38.50 for EUR 1. The Slovak Central Bank decided to act quickly, calling a meeting with government officials, Prime Minister Robert Fico and the Minister of Finance, Jan Pociatek (remember this name, as it will crop up again in a surprising way). The common resolution of the Slovak Central Bank and the government after the meeting was to declare they were committed to doing as much as possible in the process of joining the eurozone.

Graph – SKK/EUR exchange rate 01.01.2006 to

12.31.2007



(source: European Central Bank)

As you can see from the graph above, since that time, the Slovak koruna has never again experienced weakness. Its journey towards the eurozone was definitely sealed. 2006 ended with a rate of SKK 34.50 for EUR 1, which represented more than a 10% improvement. Such a move was unprecedented. Markets were absolutely sure that

Slovakia would adopt the euro at a much stronger level. This conviction was supported by the Slovak Central Bank once again on March 19, 2007, when it moved central parity in the ERM II from SKK 38.455 to SKK 35.4424 for EUR 1, while the fluctuation range was set between SKK 30.126 and SKK 40.7588 for EUR 1.

As we know, Slovakia was required to stay in the ERM II for at least two years before joining the eurozone. Only one question remained unanswered: what would be the rate between the Slovak koruna and the euro at time of entry?

And that was the million dollar question, as reality later confirmed.

TradeFloor view:

2006 and 2007 were again great years for Slovak koruna traders. I still miss those times, as no other Central European currency is able to repeat this story. Around the time of the elections, almost everybody knew that a change of government was inevitable. So, even with a great interest rate

differential between the Slovak koruna and the euro, we decided to close part of our EUR/SKK positions. The events that unfolded after the elections gave us a green light. There were two hard months when you could not be sure where the rate would be in the morning. The news was coming up with different opinions from different leaders and we did not know which direction would prevail. Finally, in September, everything cleared. And, even if you did not start to buy the Slovak koruna right away after that central bank/ government meeting, you could still start anytime you decided. Nobody doubted that everything was now decided.

There was a small surprise when, in March 2007, the central bank moved parity to 35.4424, even when the market was more than SKK 1 lower than parity itself. However, that was just a small break in a long positive run of events.

All the talk among traders during these days turned to a final fixing rate. Guesses, bets and tips about where the rate would finally end up circulated every hour of every day. Anybody who guessed correctly would earn a lot. Really, a lot.

Also, all the Slovak koruna traders knew that, once the Slovak koruna ceased to exist, their place as market makers would be lost. On the one hand, this was good news for the country and its economy; on the other hand, it posed a big threat for the future of a small group of currency traders in Slovak banks.

The importance of getting the final fixing of SKK/EUR right increased every day. It was the last chance to hit the jackpot on the market you knew the best.

4.3 Setting the final rate

2008 was a one-way street for the Slovak koruna. The date for Slovakia's entry into the eurozone was set for January 1, 2009, with the Slovak koruna ceasing to exist on December 31, 2008. The final exchange rate had to be set in advance as replacing the koruna with the euro could not be done without any technical preparation. The common expectation was that the conversion rate would be set at least six months ahead of January 1, 2009.

TradeFloor view:

There is a special place for 2008 in the memory of every Slovak koruna trader. The start was very quick, nobody doubted that the rate should be somewhere below the current parity of SKK 35.4424 for EUR 1. Where exactly would it be? Guesses varied between 35.4424 and 30.000. Some optimists even thought it would be slightly lower. Most bets between traders were at 30.000. A nice round number, which would help people to recalculate next year's prices back into korunas.

So, all the trades pointed to strengthening. Everybody was selling euros and buying korunas, hoping for a

final profit on the koruna. It was simply repeating what you had done for the last eight years, but now with bigger amounts in anticipation of hitting the jackpot.

Extraordinary events happened in May. On the afternoon of Monday, May 26, 2008, we saw that clients' activity had picked up. On the following day, this activity continued. Clients who were usually quiet were now calling like crazy. They wanted to know what the biggest amounts were, which they could use on the current margin they had. They tried to squeeze out as much as possible. The EUR/SKK rate started to fall quickly; however, that did not distract clients from adding to their positions. Even rates under 31.000 were right for them, which was very unusual. When we got a call from highly ranked state official asking about the possibility of the EUR/SKK forward and maximum amounts he could use, we knew something had already been decided.

Recalling these days in my mind and the talks I had with other traders in the days after, everybody remembers the unusual activity on the Slovak koruna. No official statement, but certain clients, who were

generally connected to state officials, started to make a lot of EUR/SKK trades. No rate was bad for them; the only question was how much they could trade.

The truth was revealed after four days of frenzy. On May 29, 2008, the Slovak Central Bank officially announced that the European Central Bank had accepted its proposal as of Tuesday, May 20, 2008, about moving central parity for SKK/EUR from 35.4424 to 30.126.

Now it was time for the winners to count their profits. With the unusual spike in activity on Monday, everybody knew that somebody had spilt the beans before the official announcement was made. And that somebody definitely hit the jackpot.

Graph – SKK/EUR exchange rate 05.20.2008 to

06.01.2008

(source: European Central Bank)

The new central parity between the Slovak koruna and the euro was officially adopted as the final exchange rate between the currencies when Slovakia entered into the eurozone. As confirmed by the EU on July 8, 2008, 30.126 would be the official conversion rate on January 1, 2009.

Later on, new facts about the process of setting the new central parity and the exchange rate between the Slovak koruna and the euro emerged. Let us check these facts in precise chronological order:

> Tuesday, May 20, 2008 – Slovakia's Ministry of Finance, together with the Slovak Central Bank, asked ECOFIN and the European Central Bank for a change in central parity from 35.4424 to 30.126.
>
> Thursday, May 22, 2008 – Slovak Prime Minister Robert Fico met Czech Prime Minister Miroslav Topolanek in Prague. Later, in a news interview, Topolanek recalled that Fico spoke about the very good EUR/SKK rate negotiated with the European Central Bank.
>
> Saturday May 24 and Sunday May 25, 2008 – The Formula One Grand Prix in Monaco took place. This may seem a little bit off-topic, but this annual event in Monaco brings together oligarchs from Europe and possibly beyond, businessmen, the aristocracy and auto racing fans. Furthermore, a number of

Slovak businessmen moor their yachts in Monaco’s harbor and use them during the period of the Formula One event. You probably know how this kind of thing appeals to people like this. You can watch fast cars speeding around as track while sat in nice surroundings and talking with those around you. Slovak newspapers found out that the Slovak Minister of Finance Jan Pociatek was also present in Monaco during the 2008 Formula One Grand Prix. To be more specific, he was there on a yacht belonging to one of the co-owners of the Slovak financial group J&T. (J&T, at that time, owned a bank with the same name, a number of realty projects and some industrial factories). The winner of the 2008 Grand Prix was Lewis Hamilton of the McLaren team. However, he was probably not the only big winner of the Monaco Grand Prix.

Monday, May 26 to Wednesday May 28, 2008 – Unusually significant activity on the

SKK/EUR market. Clients, both big and small, were selling euros and buying Slovak korunas in above-average amounts. Unfortunately, information about trading activity during this period has not been made public by the Slovak Central Bank. Market participants have spoken about high-profile state officials and local financial groups, such as J&T, conducting major trades on these days.

Thursday, May 29, 2008 – The official announcement from the Slovak Central Bank about the change in the central parity of the EUR/SKK rate. The new central parity was set at SKK 30.126 for EUR 1.

Tuesday, July 8, 2008 – The EU officially sets the conversion rate between the Slovak koruna and the euro at 30.126.

Thursday, January 1, 2009 – Slovakia officially enters the eurozone. The Slovak koruna ceases to exist at the rate of 30.126.

Slovak journalists did not let information about Minister of Finance Pociatek on the yacht of a local

tycoon during the Monaco Grand Prix fade from view. They questioned him and got funny answers, with Pociatek claiming that he never spoke about the rate on the yacht, nor did he spill the beans about the future rate. All he had talked about was the weather.

TradeFloor view:

The popular joke at this time was about the conversation between Pociatek, Minister of Finance, and Jakabovic, co-owner of the J&T financial group, on a yacht in Monte Carlo during the Formula One event.

Jakabovic: "What will be the weather be on Tuesday?"

Pociatek: "30.126 degrees Celsius."

The investigation into the events surrounding the setting of a new central parity crumbled into sand. No prosecution by the police, no indictment and, therefore, no crime.

According to Slovak newspapers, local financial groups could have earned around EUR 35 million in those five days in May 2008.

Graph – SKK/EUR exchange rate 01.01.2007 to 12.31.2008

(source: European Central Bank)

TradeFloor view:

Everybody on the markets knew that what happened was not right. Someone had the information a few

days sooner than when it was officially announced. Someone hit the jackpot big time. In the USA, it is called "insider trading" and you can end up in jail for it. In Slovakia, nobody was indicted, nobody stood before the court, nobody was sentenced. Officially, no crime was committed.

Not only did the local oligarchs earn a big chunk of money. Some high-ranked state officials also took their share of the profits. A lot of cousins, brothers and nephews too.

4.4 What happened next?

The Slovak koruna is now history. Since 1999, Slovakia has adopted the euro as its domestic currency, which has definitely helped the country to attract many more foreign investments. Kia Motors and Jaguar are just two examples of how the euro has benefited the country. Slovakia still has its problems, but the standard of living is definitely higher than it was 10 years ago.

And what has happened to the participants in the EUR/SKK rate-fixing case?

Well, Prime Minister Robert Fico served out his term to 2006, then lost the elections in 2010. However, he was returned to power in the 2012 elections and is currently serving his third term as Prime Minister of Slovakia, which should last until the end of 2020.

The Minister of Finance Jan Pociatek stayed on in this role until 2006. In 2012, he became Minister of Transportation. He finished his career as a minister in 2016. Other cases of nontransparent business activity connected with the state were published by local newspapers. However, nobody has been

prosecuted by police.

The J&T financial group continues to flourish. It still owns the J&T Bank and is a part-owner of the highly successful industrial company EPH, as well as built up a number of exclusive Slovak and Czech real estate offices.

Graph – SKK/EUR exchange rate 01.01.1999 to 12.31.2008

(source: European Central Bank)

TradeFloor view:

Life as a trader started to get really hard from 2009 onwards. We lost our currency, we lost our edge on others. We lost our home market, where we had an information advantage. We tried to trade other currencies, but we did not have many chances against local banks.

A lot of traders were fired, with some moved to other countries. Generally, banks looked for ways in which to dispose of expensive dealing rooms. A lot of banks moved trading to mother companies in countries that still had its original domestic currency.

There was no reason to have forex traders in Slovakia with the euro if you have traders in Frankfurt or Vienna, where they also have the euro.

Times were nice with the Slovak koruna, but they have gone. Now it is time to look elsewhere. And we will see whether such spectacular events will also happen in other countries that join the eurozone in the future. Or whether this was just specific to Slovakia.

5. And what now?

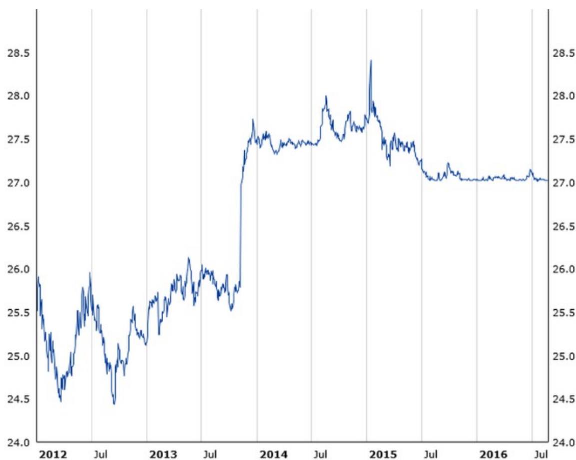
Is it possible that the events discussed above will be repeated on other currency markets in future? Yes, it is. Maybe not with such events in the same order, but definitely in a similar way.

5.1 Can the SNB crash be repeated elsewhere?

We have already suggested that there are two free-floating currencies in Europe that are not exactly free: the Danish kroner and the Czech crown. The latter is the most likely to go through a similar experience to that of the Swiss franc.

The Czech National Bank (CNB) set the same type of floor for the CZK/EUR rate as the SNB did in 2011 for the CHF/EUR rate. When the CNB did so in November 2013, it announced that rate should be at least CZK 27.000 for EUR 1.

Graph – CZK/EUR exchange rate 01.01.2012 to 08.25.2016



(source: European Central Bank)

A year and a half later, the floor movements of the Czech koruna were run mainly by rumors, which was a similar situation to what happened with the Swiss franc. Everybody was afraid that the CNB would move the floor higher or intervene in order to weaken Czech koruna even more. Indeed, at the beginning of 2015, the rate reached CZK 28.000 for EUR 1.

Then, after January 2015, the mood concerning the SNB events on the Czech koruna market changed dramatically. The fear of a sudden and abrupt removal of the floor on the CZK/EUR rate pushed

the Czech crown to CZK 27.020 for EUR 1, which was slightly above the floor kept and guarded by the CNB.

The situation lacked further clarity due to a change in the Board of Governors of the CNB. The President, who had the right to make board appointments on occasion, voiced his dislike of the current floor for the CZK/EUR rate. The markets, therefore, concluded that the new members would act very quickly and remove the floor at some point.

When the new CNB Board of Governors publicly voiced its opinion, it stated that it did not want to repeat the actions of the SNB in January 2015. However, it did not propose any other way by which to unload the floor, preferring instead to verbally prepare the markets that, in the first half of 2017, it would seriously consider removing the floor.

In other words, the markets should prepare themselves for a sudden cancellation of the floor. Even interest rate differential suggests that the floor would be removed in the short term.

Brokerages and banks were cautious enough to limit trades by clients on short maturities and amounts

with higher requirements for a margin. Indeed, a margin requirement of 15% and more is not unusual for the Czech koruna nowadays.

For retail traders, we recommend not maintaining any position regarding the Czech koruna at present. Although removal will happen in the future, predicting the date is impossible. We will all be surprised when it happens, but at least we can be prepared. Clever traders will stay away from the CZK/EUR and CZK/USD markets for a while.

As an aside, the SNB removed its floor after approximately three years and four months. The CNB set its floor in November 2013 and, if you add three years and four months, you arrive at March 2017. So be careful.

5.2 Surprising election results

The result of the Brexit referendum was something that almost nobody on the financial markets predicted in advance. Any political event in any country can impact at least on the domestic currency. But, if you are speaking about global events, which Brexit definitely was, then the impact can also be felt around the world and influence the movement of many currencies and stock exchanges.

It is now very hard to predict the public mood. Polls are not always right, as they simply follow specific voter patterns. Typically, they engage with the middle classes, while excluding lower classes or those living in villages. In turn, this can lead to very misleading findings.

Polls are not able to capture a sudden change in the public mood, which can occur immediately before actual voting begins. Polls need the time to be counted and published.

When reading polls, you should always check the number of people they asked and the time period when the questioning process took place. These two facts can help you in assessing the value of a poll in

relation to your decision.

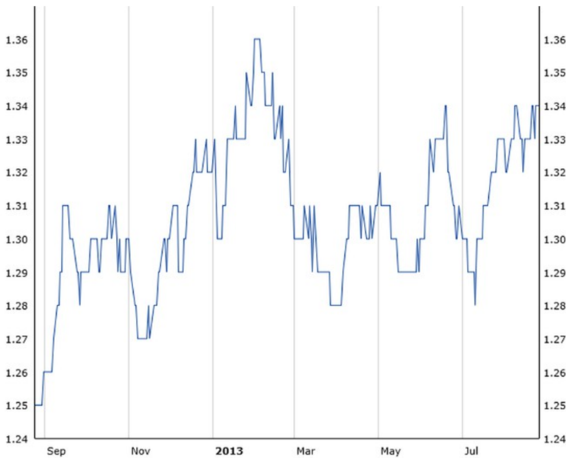
The result of the 2016 US presidential election could cause a surprise similar to Brexit. The Democrat contender Hillary Clinton is popular among the middle classes, while her Republican opponent Donald Trump lags behind in polls. However, he may still attract enough voters from all sides of the popular electorate. In other words, people who have never spoken with anyone from a polling agency, but people whose vote still counts.

An unexpected outcome in the US presidential election would deeply hit every market around the world. No free-floating currency would be safe from wild swings.

Just have a look at the USD/EUR rate during the 2012 US presidential election.

Graph – USD/EUR exchange rate 08.25.2012 to

08.25.2013



(source: European Central Bank)

The move from USD 1.2700 for EUR 1 to USD 1.3300 for EUR 1 is pretty big. It is possible that 5% could decide whether your year in forex is profitable or not, whether your investment in US dollars is earning money or whether you lost 5% on your house in the USA.

And be sure that, if the USD/EUR cross-rate moved

by 5%, then any emerging currency, for example, would move more than that. Furthermore, be absolutely clear that, when markets are moving at such a pace, it is very hard to stop-loss your position at a reasonable rate.

5.3 Who will be next to join the eurozone?

The eurozone is a live mechanism. Countries in Europe with open economies and strong export links to countries in the eurozone will always tend to eliminate currency risk.

Countries such as Slovakia have attracted a lot of interest from industrial companies willing to invest, thanks to the euro currency. The nonexistence of currency fluctuations helps investors precisely calculate future scenarios relevant to decisions about where to invest. Countries without the euro, such as the Czech Republic or Poland, are always at a disadvantage due to uncertainty about exchange rates. (Honestly, the currency rate is just one of many factors considered by foreign investors, along with taxes, justice, quality and accessibility of the workforce etc.)

When you recall how the Slovak koruna strengthened in the last decade prior to joining the eurozone, you will have a clearer idea about the market expectations regarding the currencies of other countries when they also decide to join the eurozone.

However, the final fixing rate is always a balance of two opposing powers. On the one hand, you have a population, which means that the stronger the rate at time of joining the eurozone, the richer they become. On the other hand, you also have exporting industrial companies in your country, which means that the stronger the rate at time of joining the eurozone, the weaker will be their position on common markets. In other words, these companies lose one of the key competitor advantages against companies that are not in the eurozone. A weakening domestic currency will always help domestic exporters, as their products will become much cheaper compared to those produced from a eurozone country.

When deciding on the fixing rate, you should balance these two powers in order that they satisfy each other.

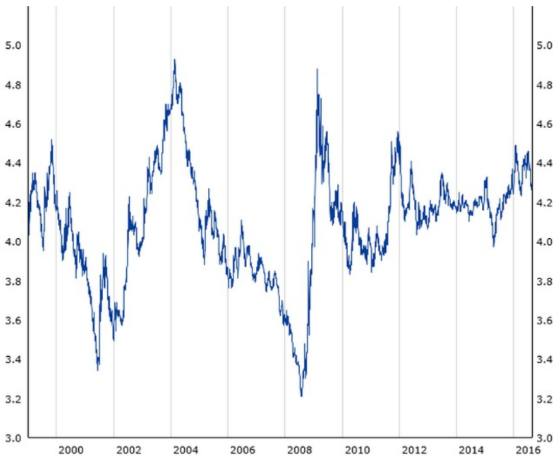
Let us now have a look at other Central European countries, which, in 2008, were also considered as candidates for eurozone entry. These countries had already signed an obligation to join at some future point. No time was specified, but it was absolutely

correct to assume that they would enter at some stage. Probably not now, though, given the difficult situation in the eurozone, thanks to Greece's problems and those faced by the EU overall due to Brexit. In five or 10 years, however, this situation will hopefully be different and the case for joining the eurozone will be clear and convincing.

5.4 Poland

Poland was the number one candidate. As a big country with a strong domestic demand, it was considered as a natural joiner.

Graph – PLN/EUR exchange rate 01.04.2009 to 08.25.2016



(source: European Central Bank)

You can clearly see that the strengthening of the

Polish zloty against the euro was much quicker and stronger than that seen in relation to the Slovak crown: from PLN 5.000 for EUR 1 to PLN 3.2000 for EUR 1. That is more than 50% over four years. Unfortunately, due to the Lehman Brothers' crisis in 2008 and the adverse effectives for emerging markets, which resulted in a sharp sell-off of local currencies, the rate almost returned to PLN 5.000 for EUR 1.

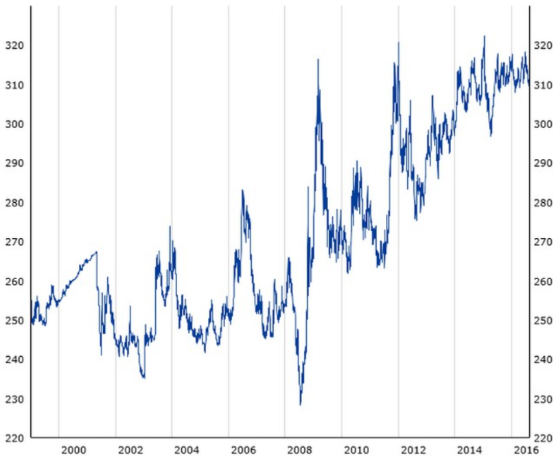
The zloty never again fell below 3.8000. It hardly breaks the rate of PLN 4.000 for EUR 1. The good news is that this currency does not react so wildly in times of crisis, but the story of the infinite strengthening of the zloty is over.

We can expect that, when an appropriate plan for joining the eurozone is set in the future, the zloty will strengthen again. However, guessing the entry rate would be very premature.

5.5 Hungary

The second possible candidate was Hungary.

Graph – HUF/EUR exchange rate 01.04.2009 to 08.25.2016



(source: European Central Bank)

We were able to observe a slight strengthening prior to 2008. Since the Lehman Brothers' crisis, however, there has been a period of continuous

weakening of the Hungarian forint, as the political class in Hungary fails to talk about possible entry and any plan to enter is far away. In turn, there has been a lot of a domestic economic and political problems, while the markets have also been affected.

The probability of joining the eurozone in a reasonable timeframe is very low. But, were it to happen at some point in the future, some kind of strength will probably emerge.

5.6 Czech republic

The third country considered to be a candidate for eurozone entry was Czech Republic.

Graph – CZK/EUR exchange rate 01.04.2009 to 08.25.2016

(source: European Central Bank)

The Czech koruna is like a mirror of the Slovak koruna, which is maybe due to the fact that the

Czech Republic used to be part of Czechoslovakia with Slovakia, or thanks to the country's economy. Although continuous strengthening stopped in 2008 (the year of the Lehman Brothers' crisis), the trend continued shortly after that period of time.

If the Czech Republic had not set the floor at a rate of CZK 27.000 for EUR 1, we would probably have seen the rate to be around CZK 20.000 for EUR 1.

Unfortunately, in the Czech Republic, joining the eurozone is not the story of the day. The political class in the country reject the idea of losing domestic currency and monetary policy. Even with strong export ties to its main economy partner, Germany, it does not consider the euro as a viable choice this time.

However, even without a plan to join the eurozone, the Czech koruna is likely to see strong strengthening once the Czech National Bank removes the floor and allows the koruna to free-float again.

6. Final remarks

Currency markets are too big to understand and can surprise anyone, even the most experienced traders.

Learning from history can help in understanding current and predicting future scenarios. Even if, as every trader knows, predictions are not very reliable, you should still adapt to new information, reassess your conclusions and be prepared for any possible eventuality. A good trader always knows his worst-case scenario.

Understanding historical patterns can help in deciding what to do in times of crisis. The three events that we described in this book should inform how you watch the markets in future, as you can be sure that similar (even if not the same) events will definitely happen.

I hope this book was, and will be, useful to you.

About the author

My name is Simon Kostrava and I have spent almost all my professional life at a dealing desk watching four screens with two eyes. As my professional life represents almost half of my entire life, I am not as young as it seems. I have spoken to a lot of investors, speculators and hedgers. Sometimes, I just listened; other times, I tried my best to help them or advise them. But there is never a better experience than when you invest and lose your own money.

With four screens on your desk, you sometimes need to a break from currency graphs and decide to switch to sport. Football, hockey, tennis, golf, horse racing or whatever sport you want to watch to get away from the financial markets. And when you get really into it, you always try to guess the winner of every match you see. One small step beyond and you're betting on outcomes. Financial trading is the same; you just speculate and try to be profitable. Well, that's not so easy these days.

Markets and sports. That is my life.

Other books by Simon Kostrava

Forex: How to Quickly Lose a Lot

By Simon Kostrava, published in 2016

The Betting Industry: Who Makes the Most Money and How?

By Simon Kostrava, published in 2016

You can follow Simon Kostrava on www.evilforex.com or on www.twitter.com/evilforex