

Would you agree to buy a property without knowing what it is going to cost you?

Probably not. Yet this is what many people do when buying their dream home overseas if they have not considered how they are going to buy the foreign currency needed to pay for it.

Exchange rates play an important role in the purchase of your new home as they determine how much foreign currency, such as Euros and US Dollars, your Pounds sterling will buy. Obviously, you will want to pay the least and buy your property for the cheapest price you can. Therefore you should aim to obtain the greatest amount of foreign currency for every single Pound you spend.

This document is intended to help you understand the various methods available to you to best manage your currency transaction. We will show you how simple buying an overseas property can be and how exchange rates should be seen as an opportunity rather than something to be feared.

SCENARIO – BUYING A NEW BUILD PROPERTY

Many 'new build' properties are purchased 'off plan' and require a series of foreign currency payments to be paid in stages during the build. This may spread out over 12 months or more. Consequently, there will be many weeks or months in between the dates when each staged payment is required and this extended timeframe exposes you to currency risk; the risk that the exchange rate may move adversely against you within the period between you agreeing to buy the property and needing to pay for it.

If we assume the measure of 'success' in buying your overseas property is determined by:

- 1) How little you pay for it
- 2) How simple and risk free your solution is

To be successful, you will need to overcome this common 'time lag' problem. The following example will help demonstrate how this can be achieved.

If we take a new property in Spain as an example, the table below outlines a typical payment schedule:

Property Price	Stage Payments	Quantity	Payment Date
EUR 300,000	10% deposit	EUR 30,000	3/03/04
	25% 1st payment	EUR 75,000	3/06/04
	25% 2nd payment	EUR 75,000	3/09/04
	40% final payment	EUR 120,000	3/12/04
TOTAL	100% payment	EUR 300,000	9 month period

As each staged payment will be required in Euros, you will need to exchange your British Pounds sterling into Euros before the designated payment date. Therefore, the exchange rate achieved will determine the amount of Pounds sterling you need to pay to buy the required quantity of Euros.

Given the near two year timeframe and inherent uncertainty, you will be pleased to hear there are various ways in which you can buy your currency and pay for your dream home. You choose the plan that suits you best.

LOW RISK STRATEGY – BUY THE CURRENCY UP FRONT

If you want to know all your costs up front, then this may be the solution for you. To reduce the ongoing exchange rate risk, this strategy involves the immediate purchase of the full EUR 300,000 on a spot contract. The 10% deposit needed for the first payment, amounting to EUR 30,000, would be immediately transferred to Spain and the remaining EUR 270,000 balance would be held in a transaction account with Halo Financial or another Euro designated account of your choice. The Euros required for each subsequent stage payments can be debited from your account as and when required.

Key features

- + Simple and effective in eliminating currency risk
- + All costs are known at the outset
- All Sterling funds must be available from the outset
- Funds could be better invested elsewhere as EU & US interest rates are comparatively low.

If these last two points strike a chord with you, an alternative strategy might be preferred.

HIGH RISK STRATEGY – IGNORE STRATEGIES AND EXCHANGE YOUR FUNDS AT THE LAST MINUTE

This is a common course of action for overseas property buyers; unaware of the risks that exchange rate fluctuations bring. Sadly this inaction often costs them a lot of money. This, higher risk, strategy, involves buying the Euros needed to pay for each staged payment on spot contracts as and when the payments are required.

The Pounds sterling / Euro (GBP/EUR) chart below illustrates how volatile exchange rates can be. The jagged line represents the exchange rate over the course of a 12 month period and the boxes detail when your payment would be required and how much you would need to pay.



The information contained in the above chart is not intended as a solicitation for funds nor a recommendation to trade. Halo Financial Ltd accept no liability whatsoever for any loss or damages suffered through an act or omission taken as a result of reading or interpreting any of the information contained in or related to this chart or document.

Remember that, in this example, each staged payment is required in Euros, so you would need to exchange your British Pounds into Euros by the designated payment dates. Therefore, the exchange rate available on each payment date will determine the amount of Pounds sterling you need to pay to buy the required quantity of Euros.

The table below illustrates this point:

Property Price	Stage Payments	Quantity	Prevailing Floating Exchange Rate	Pounds Sterling Cost
EUR 300,000	10% deposit	EUR 30,000	1.4995	£ 20,067
	30% 1st payment	EUR 75,000	1.5058	£ 49,807
	30% 2nd payment	EUR 75,000	1.4723	£ 50,940
	30% final payment	EUR 120,000	1.4447	£ 83,062
TOTAL	100% payment	EUR 300,000	-	£ 203,876

- + You need outlay no money on each payment until the last minute
- You do not know how much the property will cost until you have made all your payments and added up the costs.
- + The exchange rate may continually move in your favour over the 9 month period in which you make your payments.
- But they rarely do for this length of time.

By adopting this strategy, you remain uncertain as to what the property will ultimately cost and run a far higher risk than is necessary. After all, would you agree to buy a property at home without knowing what it is going to cost you until the completion date?

RISK MANAGEMENT STRATEGY – BUY THE CURRENCY ON A FORWARD BASIS (PERHAPS THE BEST OF BOTH WORLDS)

Forward contracts are beneficial as they allow you to:

- Manage your currency risk
- Identify the Pounds sterling cost of your property from the outset
- Keep you cash rich by not tying up large quantities of your money

In many ways they are perfect for overseas property buying as they offer a simple, risk free means of buying foreign currency.

Forward contracts enable you to fix an exchange rate at the outset for delivery and settlement of your foreign currency at an agreed date in the future. As it is fixed, the exchange rate is therefore not subject to rampant currency fluctuations so you can budget for future staged payments so much easier as you know your commitment in Pounds from the start.

In addition, a forward contract can be agreed and an exchange rate fixed without the need to pay for the contract in full, in advance. In fact, a major advantage of forward contracts is that the immediate payment of a small deposit equal to 10% of the amount you wish to buy, can fix an exchange rate against the full payment value, with the 90% balance payable upon the contracts completion. For example, if you need to buy £100,000 of currency, all you will need to send us is a £10,000 deposit immediately and £90,000 at an agreed date in the future.

The Pounds sterling / Euro (GBP/EUR) chart below illustrates how a forward contract can iron out currency volatility:



The information contained in the above chart is not intended as a solicitation for funds nor a recommendation to trade. Halo Financial Ltd accept no liability whatsoever for any loss or damages suffered through an act or omission taken as a result of reading or interpreting any of the information contained in or related to this chart or document.

In the above example, the deposit, as requested by the estate agent, lawyer or builder, was paid immediately on a spot contract at an exchange rate in March. The balance of the contract was purchased on a forward contract to fix the exchange rate and protect it against any deterioration in its value. You will notice that the subsequent staged payments required over the next 9 months were purchased against the fixed exchange rate rather than at the prevailing market exchange rate, which had deteriorated significantly.

The financial savings from this risk management strategy versus the high risk alternative, is outlined in the table below:

Property Price	Stage Payments	Quantity	Prevailing Floating Exchange Rate	Pounds Sterling Cost	Fixed Forward Exchange Rate	Pounds Sterling Cost	Saving
300,000	10% deposit	30,000	1.4995	£ 20,067	1.4995	£20,067	£ 0
	25% 1st payment	75,000	1.5058	£ 49,807	1.4900	£50,336	- £ 529
	25% 2nd payment	75,000	1.4723	£ 50,940	1.4810	£50,641	£ 299
	40% final payment	120,000	1.4447	£ 83,062	1.4720	£81,522	£ 1,540
TOTAL	100% payment	300,000	-	£ 203,876		£202,566	£ 1,310

Not only can forward contracts save you money, they also reduce the administration and worry often associated with currency buying. These contracts are very flexible, allowing smaller sums of money to be drawn down within the contract period whenever you require them. Indeed, should you experience any delay in the construction of your property or should it be completed earlier than anticipated, your contract can be amended to reflect this.

Foreign exchange therefore has a very direct impact on the price you pay for your property. Generally the longer the timeframe the greater the extent of a currency's volatility. However, it is worth noting that, in time of increased exchange rate volatility, shorter timeframes can be equally affected. Should you be buying a resale property and be faced with a 30 day completion window (indeed it is not uncommon for conveyancing periods to be upwards of two months), do not make the mistake of assuming you will be unaffected. Risks remain – risks that could prove very expensive if not considered and managed early.

OUTCOME

The above generic example helps to explain the importance of foreign exchange within the process of buying an overseas property. They also show that when you buy and the means you use to buy your currency will have an impact on your overall costs and cash flow. The confidence needed to manage the risks comes from knowledge and guidance – we hope we have given you a head start. However, your circumstances are unique and so the solution that best suits you is likely to be unique as well. We recommend you contact us for a personal consultation to discuss your individual requirement.

GETTING STARTED

For further information on how we can help and to enquire about account opening documentation, please contact the private client team on:

t: +44 (0) 20 7350 5474

e: help@halofinancial.com

w: www.halofinancial.com/gettingstarted