

Managing Currency Volatility in Emerging Markets



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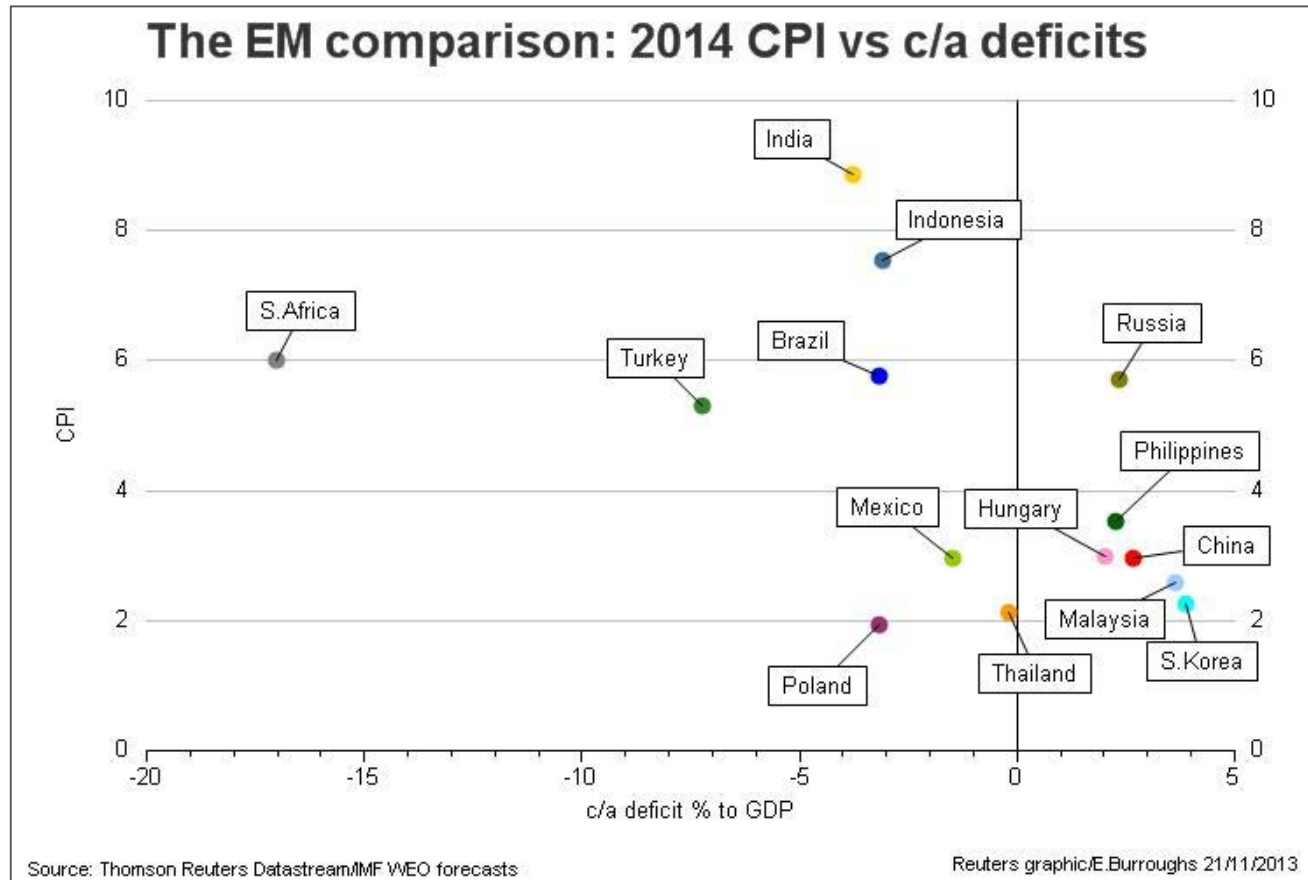


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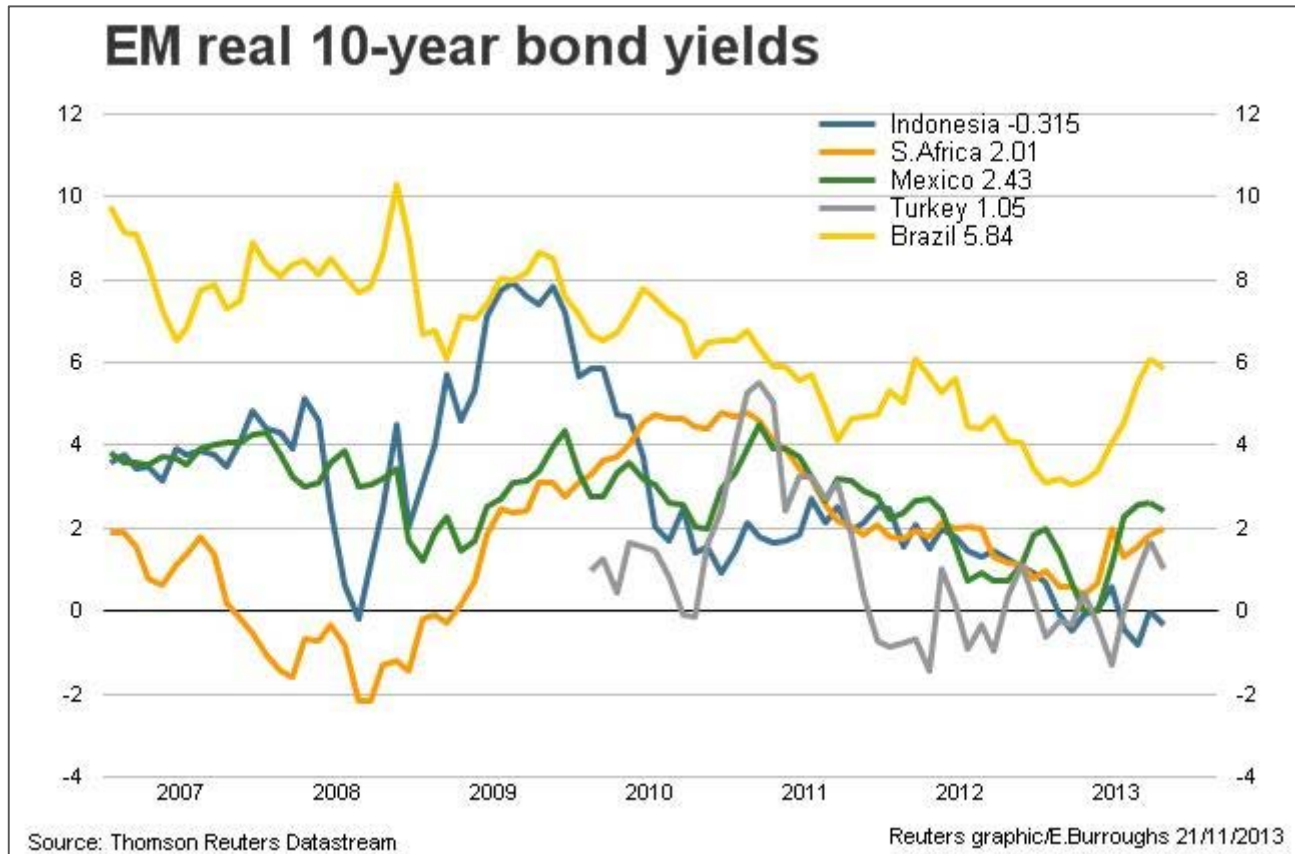
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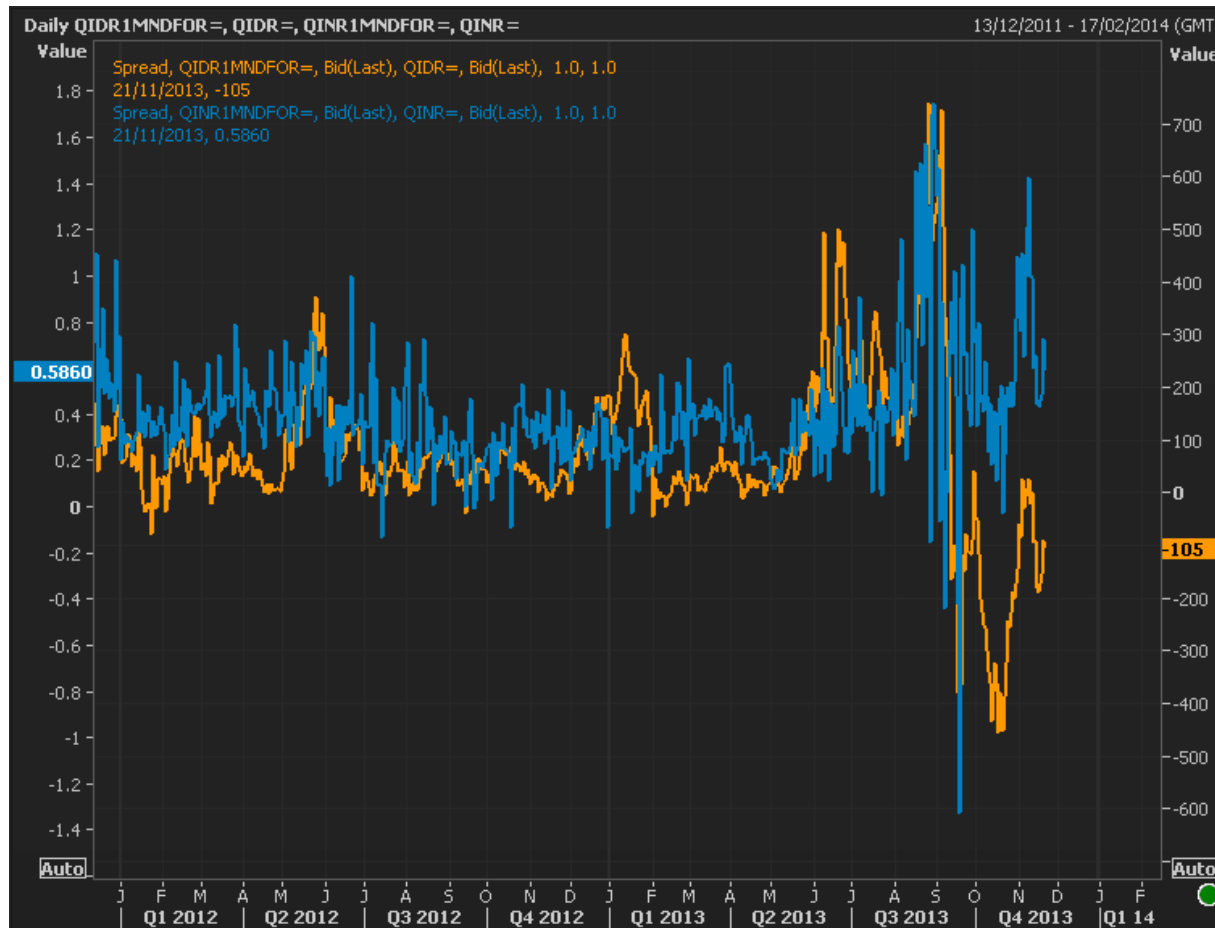
The Fragile Five



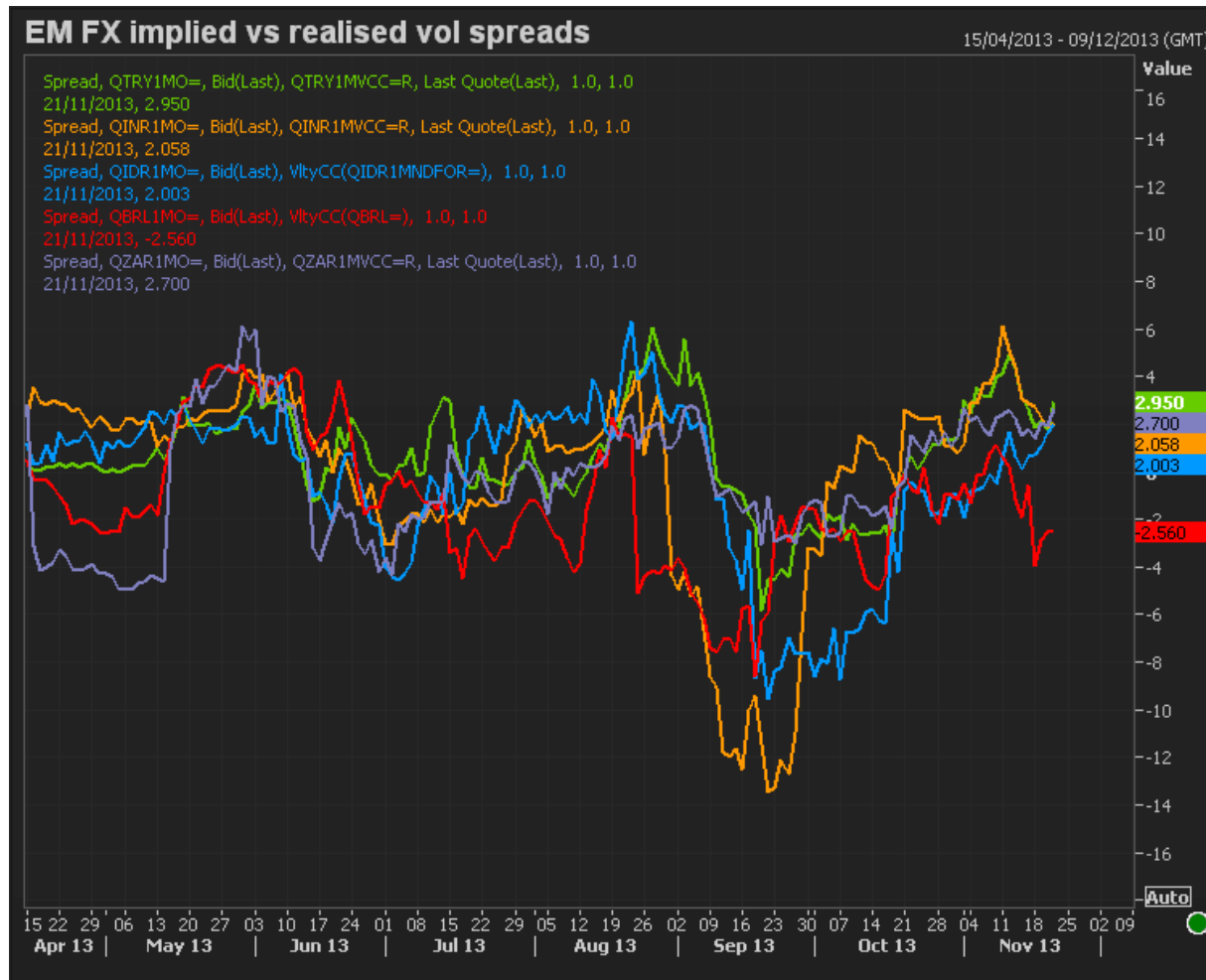
EM real yields show vulnerabilities



EM FX liquidity still problematic



Paying vol premiums for protection





Hedging Emerging Market Currencies - *Increased Volatility and Challenges*

Damian Glendinning
President, ACT(S)

Singapore, 3rd December 2013

AGENDA



- Are Emerging Markets different?
 - Key requirements for a successful programme
 - Technical issues in some emerging markets
- Where is the real volatility?
 - Does not depend on EM/DM status
- Issues with new regulations
 - Could make emerging markets even more difficult
- Potential Solutions
 - Reduce the need for hedging?
- Conclusions

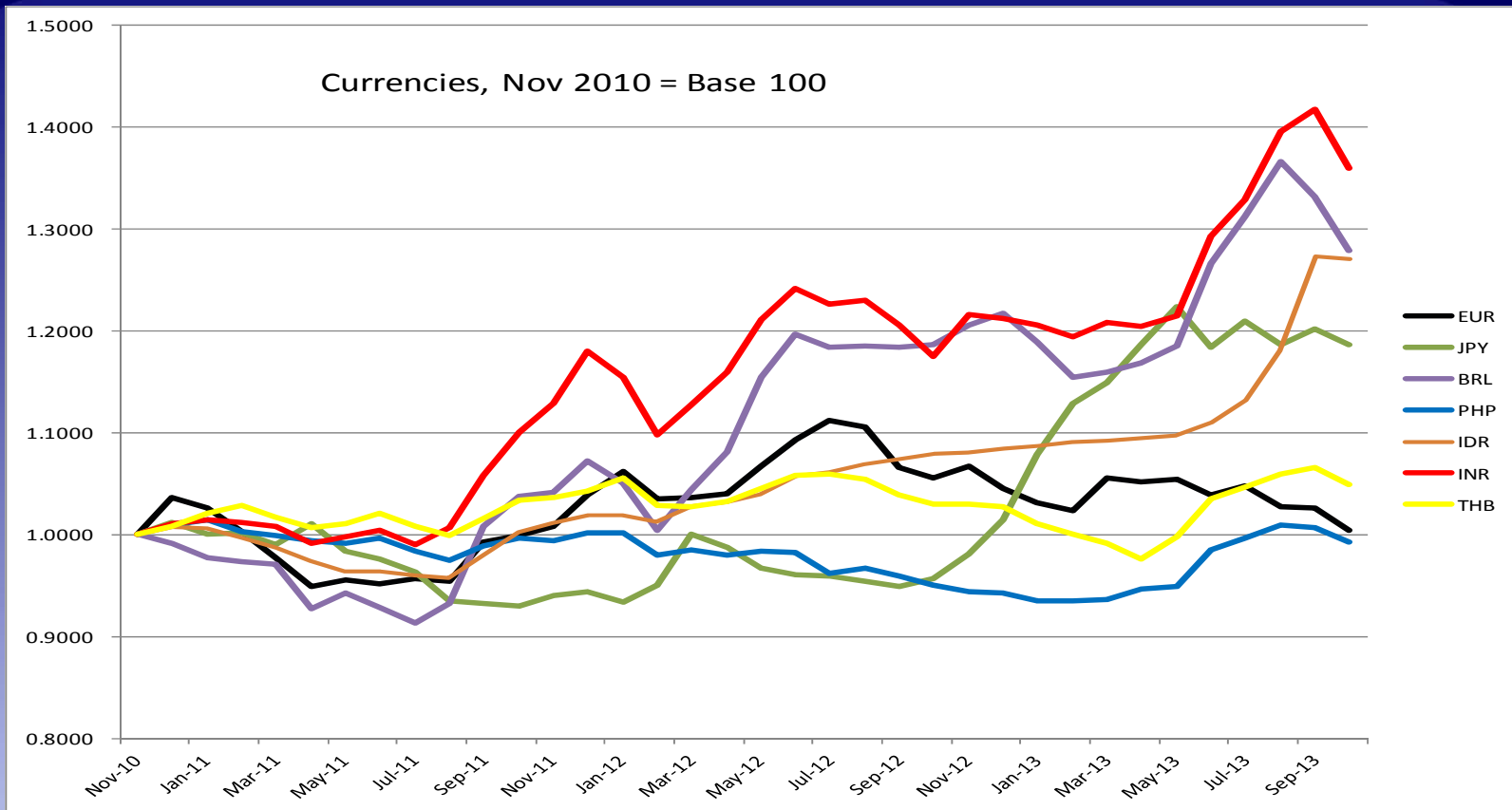
EMERGING MARKETS - DIFFERENCES



- The principles of hedging are the same as for DM:
 - Need a clear understanding of the business
 - How are currency variations passed on to customers – and when?
 - Clear policy on what will be hedged – do not invent as you go along
 - Educate management – for them, currency risk is not symmetrical!
 - EM currencies are not necessarily more volatile
- Differences for EM:
 - Often have exchange controls
 - This can lead to using NDFs
 - Result: lower liquidity, significant basis risk vs spot settlement
 - Can be difficult to predict when payment will be made
 - Cost is frequently higher

BUT NOT ALL EMERGING MARKETS ARE THE SAME !

CURRENCY VOLATILITY – DM VS EM



- Volatility is not necessarily linked to EM status!

ISSUES WITH NEW REGULATIONS



- Possibly, increased cost for all hedging activities
 - Regulations not yet certain
 - Different rules in different countries
- Major issues for NDFs:
 - Will be centrally cleared – reduces liquidity and possibly size
 - Will be very difficult to fully match trades
 - Volcker rule will prevent banks from providing unmatched positions
 - Issues with finding benchmarks – LIBOR etc
- Alternative onshore markets
 - Often very illiquid
 - Have constraints on delivery dates, documentation etc
- Some currencies cannot be hedged: VEF, ARS

SOLUTIONS:



- Clear policy is essential
 - Decide percentages to hedge
 - Evaluate cost of hedging versus risk
 - Make sure management understands the trade-offs
- Currencies which are expensive to hedge:
 - Explore local borrowing or factoring to expedite settlement
 - If amounts cannot be remitted, consider capitalisation
 - Explore local manufacturing to create offsetting exposures
- To avoid:
 - Doing business in home currency, to avoid FX risk
 - It comes back in the form of a credit exposure

DON'T WAIT FOR THE CRISIS TO PREPARE!



CONCLUSION



- Currency risk has to be managed
 - A policy is required
- The solutions vary
 - They depend on the business – and the currency being hedged
- The policies must be in place before a crisis occurs!
- The new financial regulations will cause problems
 - For all currencies, but even more for EM hedging via NDFs
- It may be necessary to consider different alternatives
- *And don't forget to communicate:*
 - Currency gains come from good management by the business
 - Currency losses are the fault of the treasurer



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QUESTIONS

Thank you all for your participation

**This webinar will be available shortly at
www.treasurytoday.com**