TCX

The Currency Exchange Fund

IfTI, June 20, 2018

I. Introduction: Currency Risk, Its Consequences, and Remedies
II. TCX: Concept, Principles, Capacity & Performance
III. How Can TCX Support Export Financing?
IV. Remaining barriers

I. Currency Risk and Its Consequences,

- Currency risk occurs when external savings finance domestic investment.
- Traditional development finance puts currency risk on (poor) borrowers (by denominating debt in hard-currencies), who are less able to manage the risk.
- Hard currency financing obscures macro risks and – combined with short-horizons and incentive/principle-agent problems contributes to poor investments and over-indebtedness.

➔ **This results in unnecessary high micro and macro vulnerabilities and reduces development potential & effectiveness**.

Increasing Policy Demand For Sustainable Local Currency Finance & Better FX Risk Management

> Development banks are urged to take on the currency risk of projects that are desperately needed to fill Asia's infrastructure shortfall
>
> *Norbert Kloppenburg, Member of KfW Executive Board, May 2016*

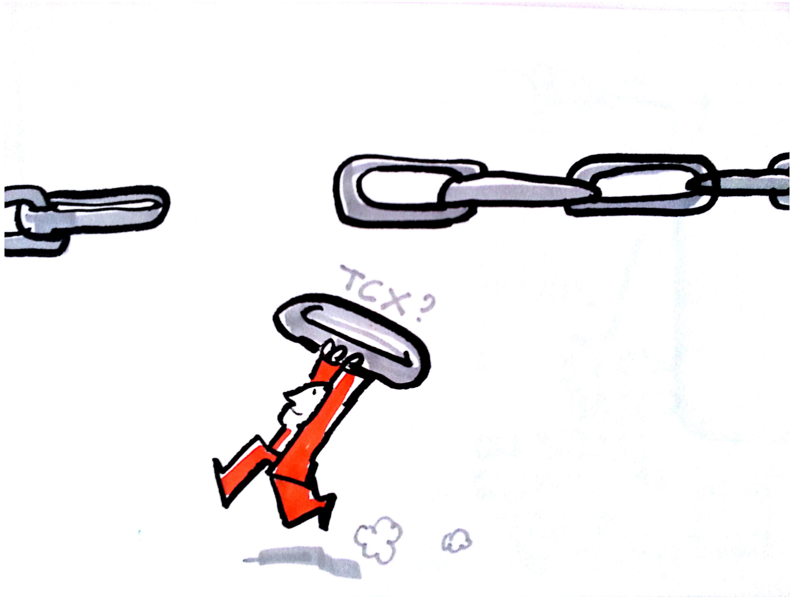
> While still small in comparison to development banks' foreign currency financing, local currency will evolve into an increasingly important financing mode
>
> *Asian Development Bank, 2016 AGM*

> Exchange rate risk is the most material risk for bonds issued to date in SSA, (...) because it is effectively unmanageable.
>
> *Overseas Development Institute, 2015*

> Yes we want you to invest, but no, we do not want you to invest in dollars. The mismatch on our country's balance sheet is unbearable and a risk to development.
>
> *Ken Ofori-Atta, Minister of Finance, Ghana. addressing the G-20, June 2017*

> I did a lot of infrastructure development in my life, to fund them with foreign currency is madness. OK? Madness.
>
> *Tidjane Thiam, CEO Credit Suisse, Oct 2015*

I. Currency Risk and Remedies



- Promote local savings (trust in banking system, low inflation, etc).
- Grow local markets, institutions, and capacity.
- Promote local currency based development lending
- Create hedging opportunities

➔ TCX is missing link

II. TCX

- Mandated to promote local currency financing and improve the allocation and management of currency risk.
- Active in about 80 OECD DAC markets, offering cross currency swaps with a range of tenors (including 15 years or longer) and notional amounts (including upwards of US$100m)

II. TCX concept & principles

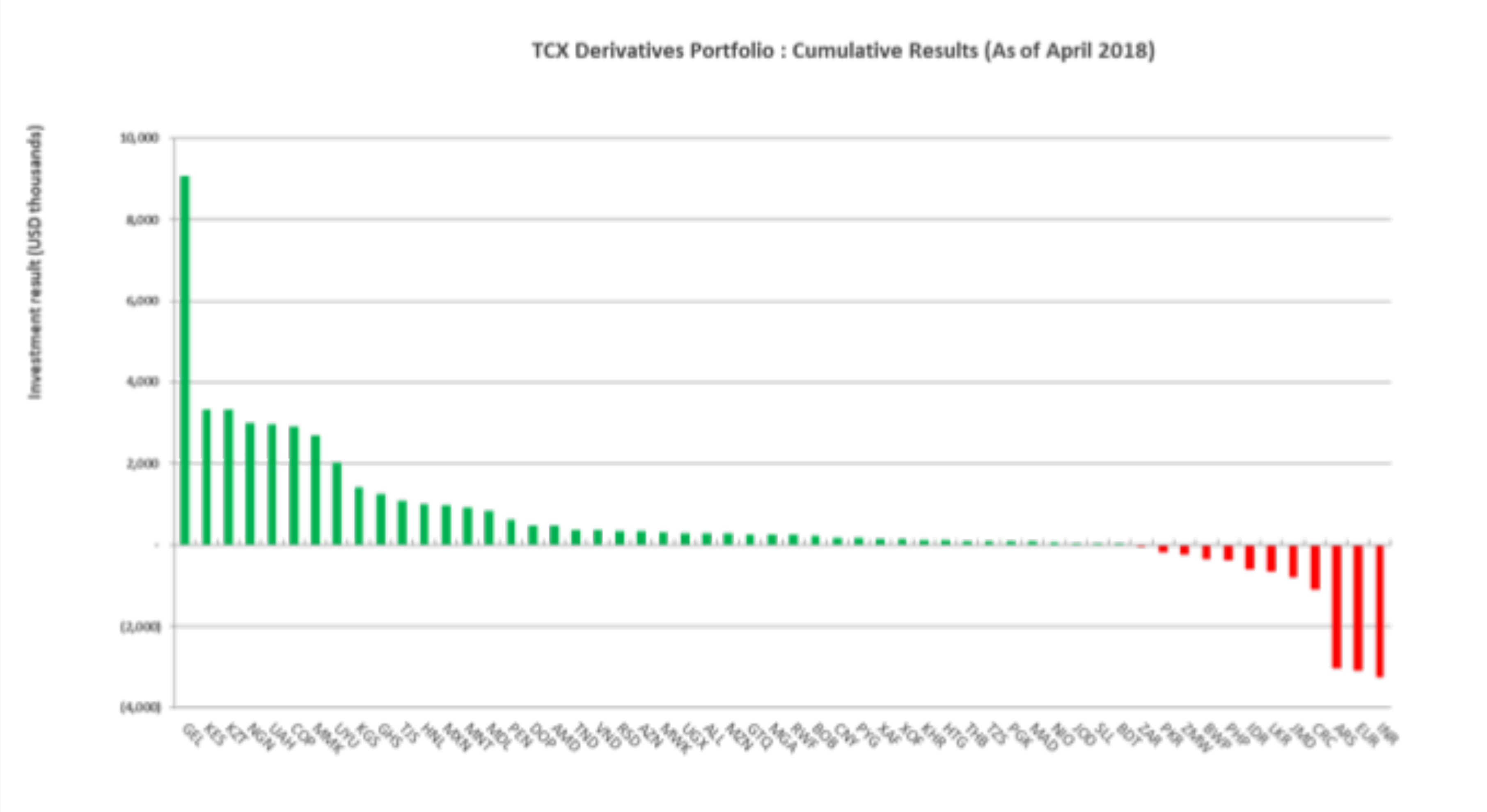
Concept

- Global pooling of currency risk
- Risk management based on geographic diversification
- Economies of scale and network

Business principles

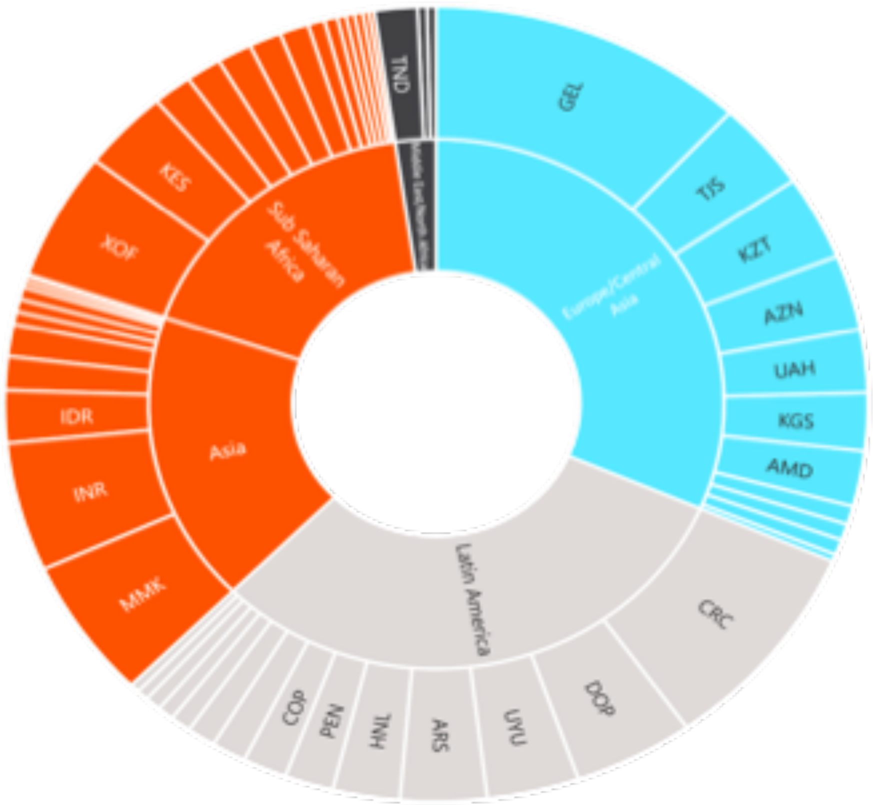
- Additionality
- Non-speculation
- Market/Risk-Reflective Pricing

II. TCX: Global Diversification

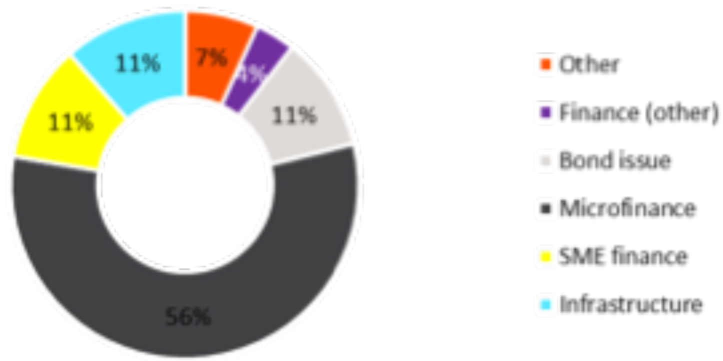


II. TCX: Global Diversification

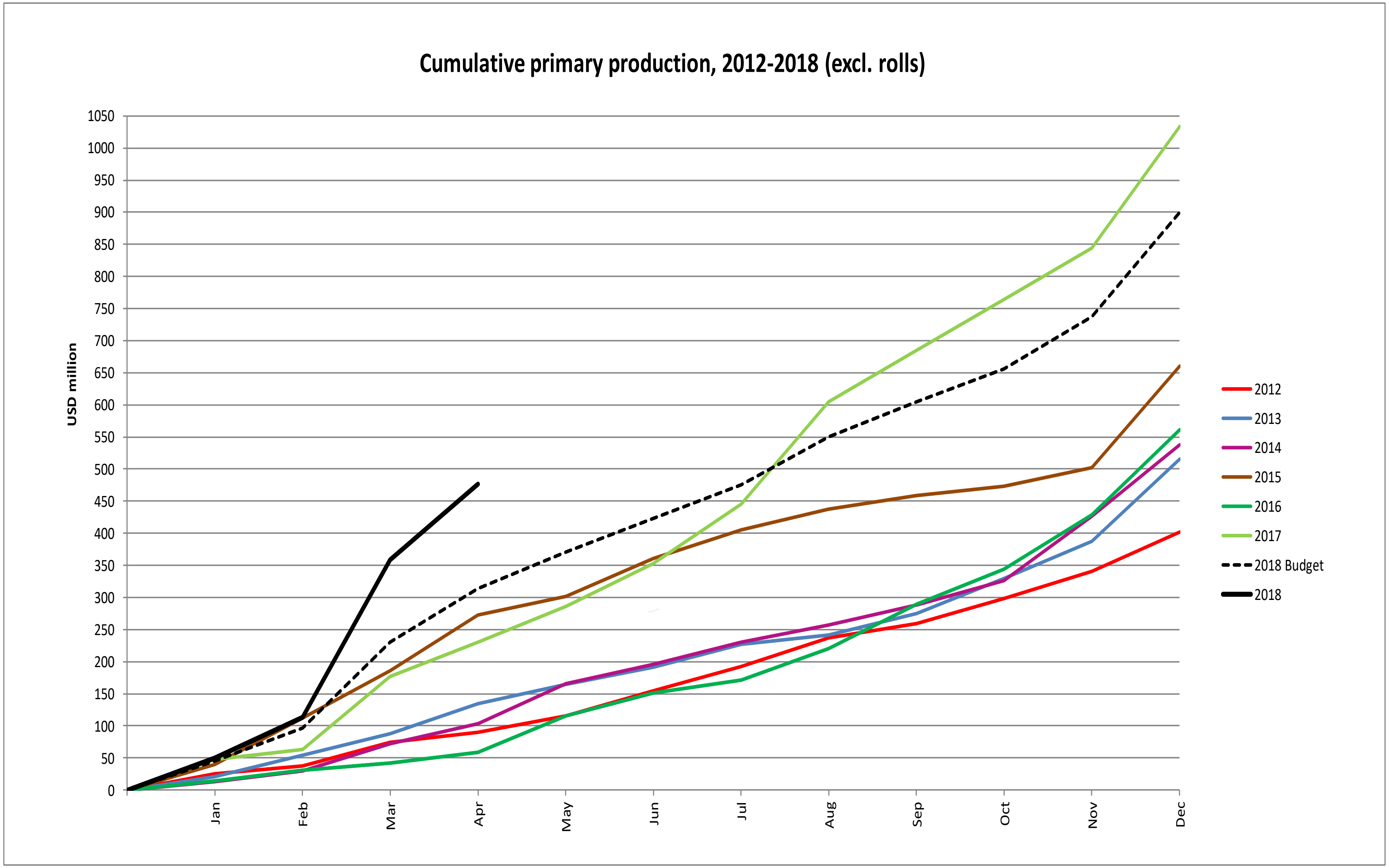
Primary Portfolio: currency diversification
(% of gross outstandings)



Primary portfolio: sector diversification
(% of gross outstandings)



II. TCX: Accelerating Demand



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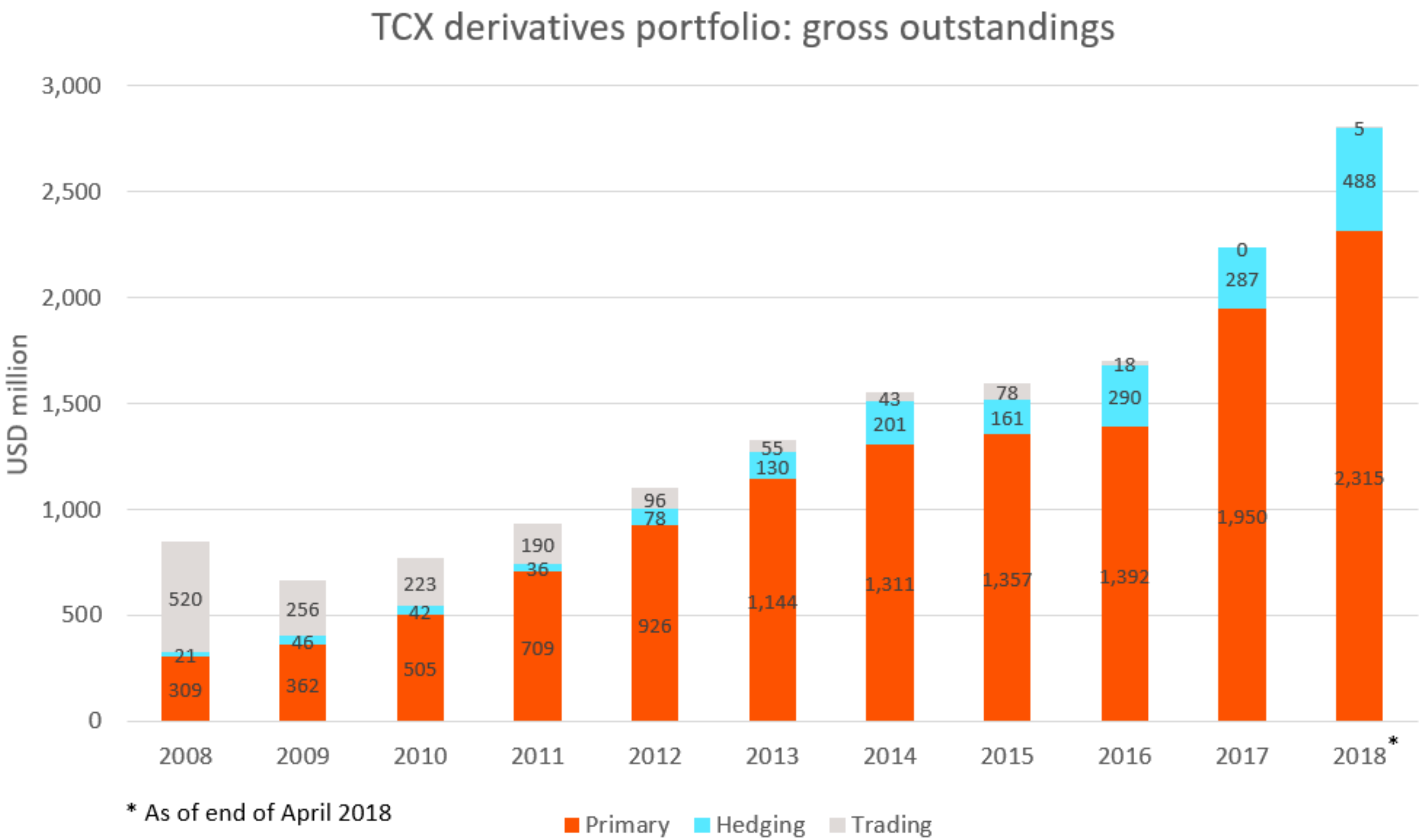
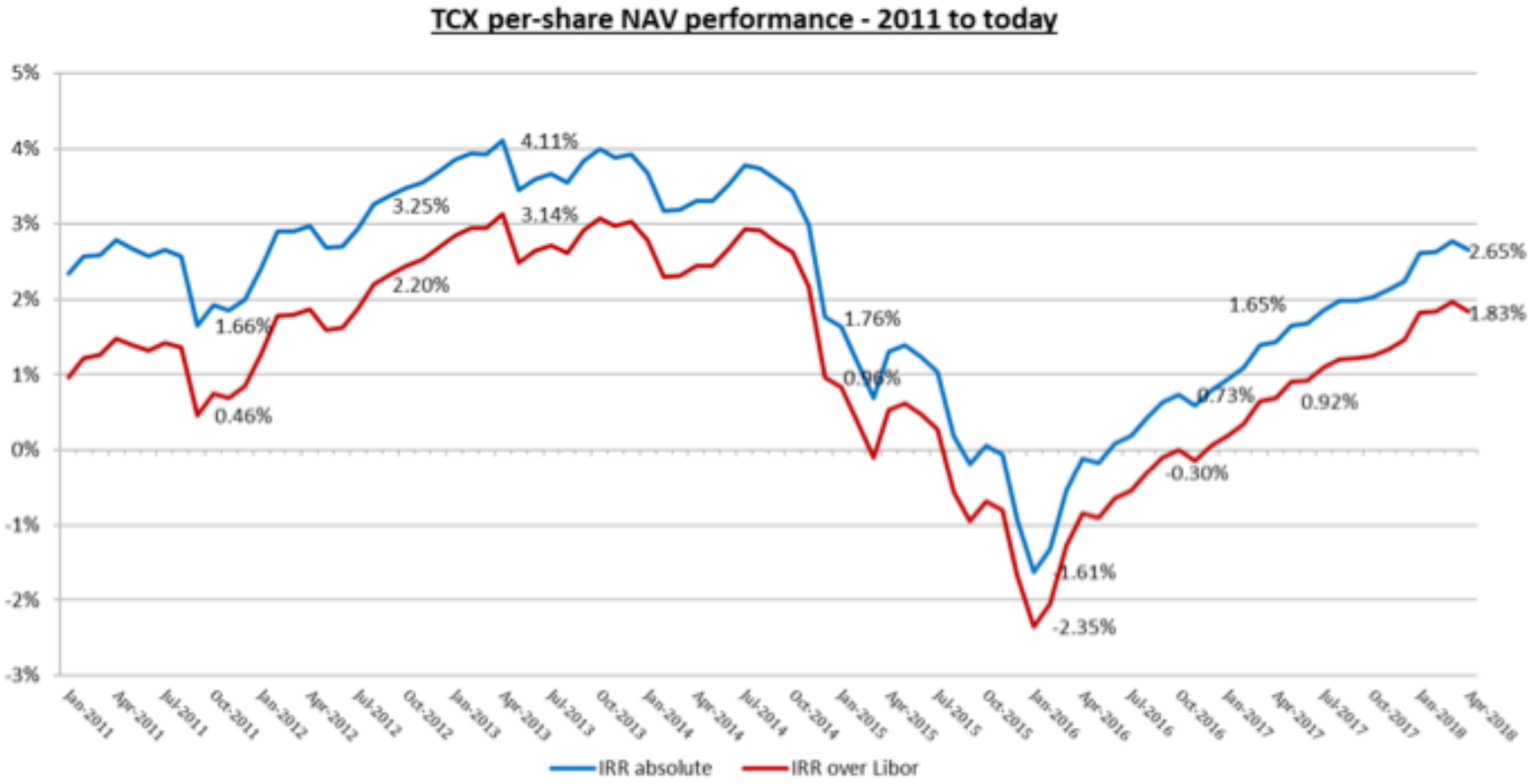
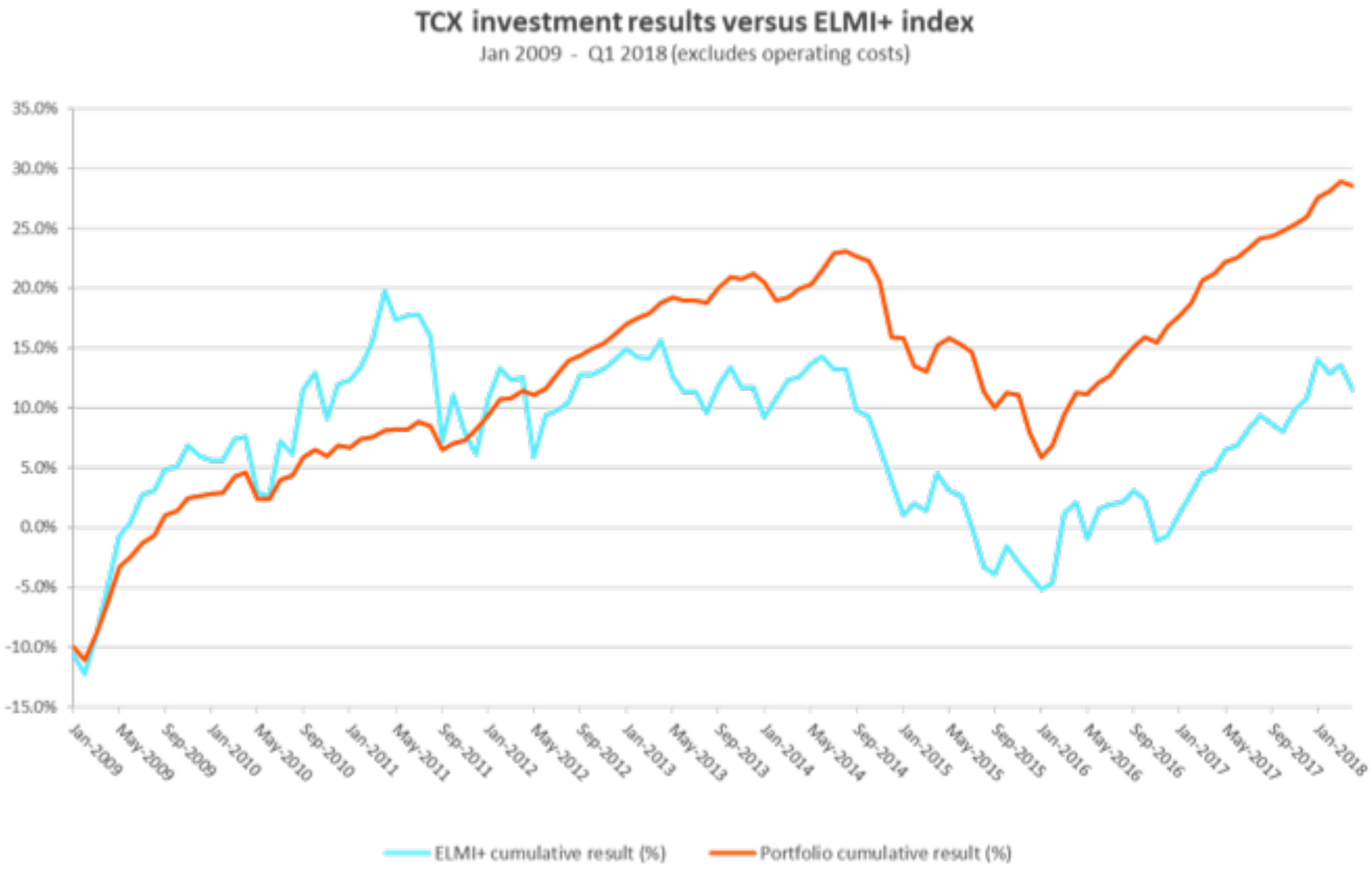


* As of end of April 2018

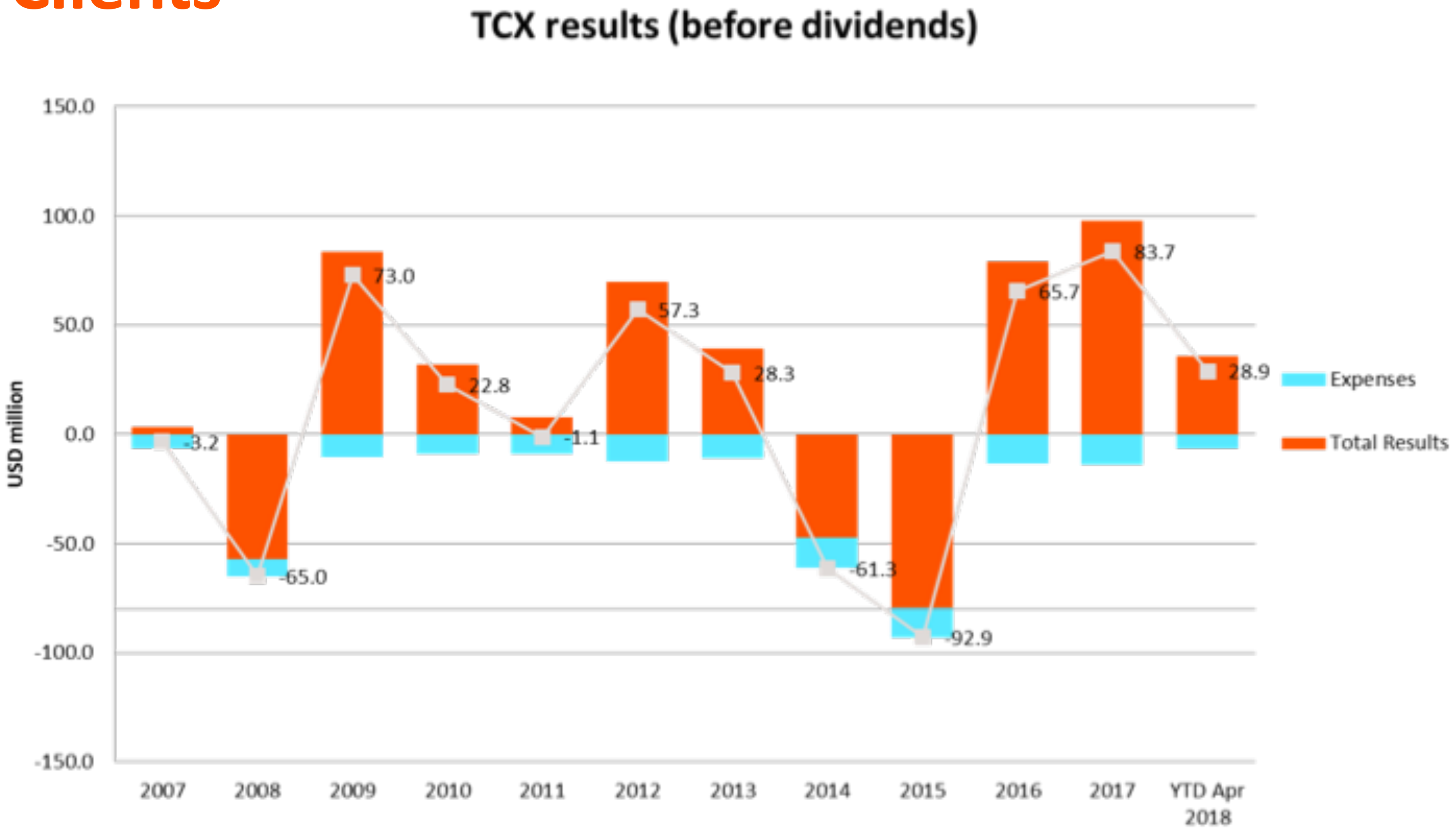
II. TCX: Sustainability



II. TCX: Portfolio vs ELMI index

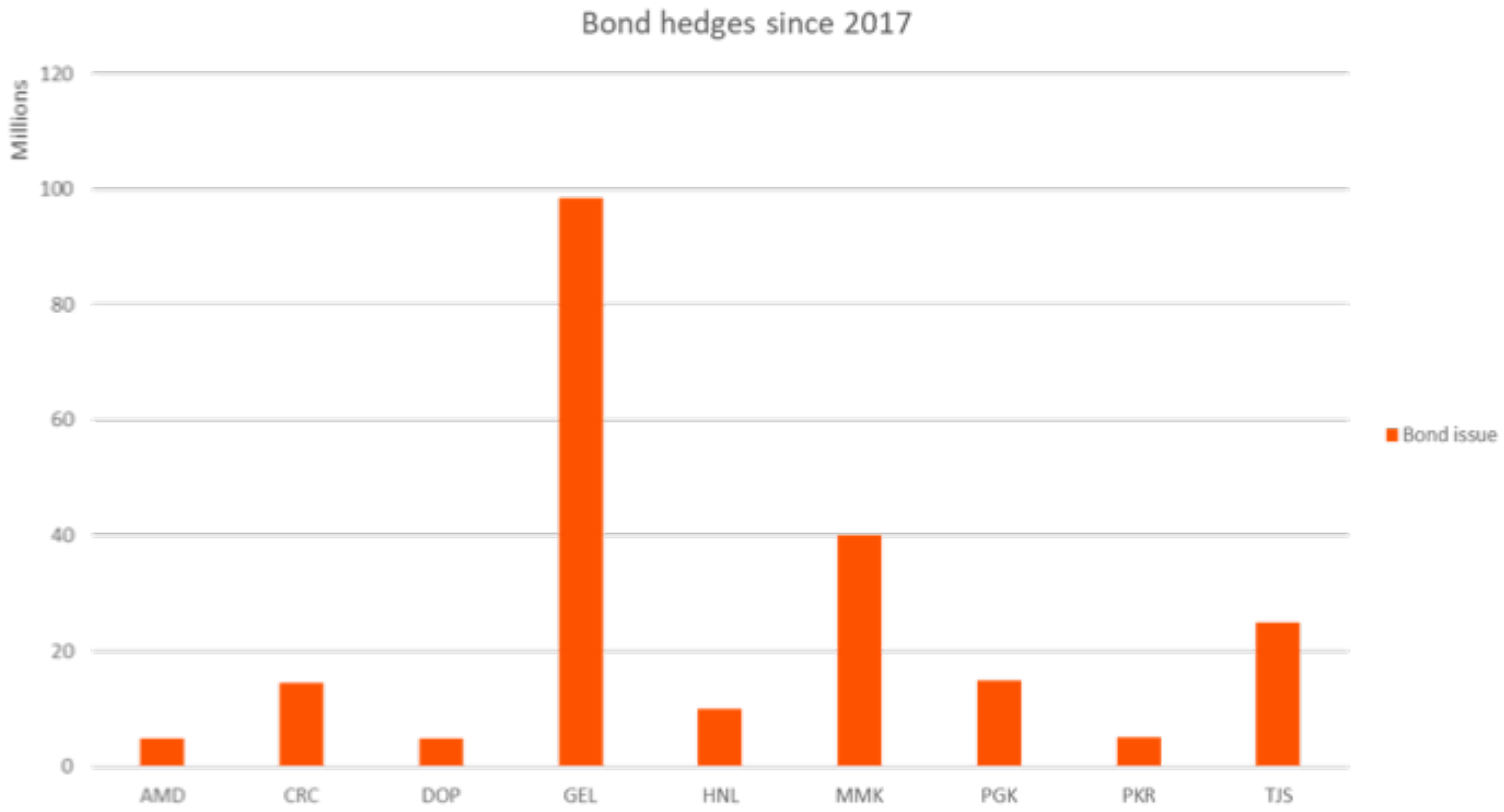


II. TCX: Absorbing Shocks for Shareholders & Clients



II. TCX: Creating markets

- Bond issuance activity



II. TCX: Strategy 2016-20

Grow

- Volume of hedged local currency investments.
- Hedging Capacity
- Coverage: Sierra Leone, Ukraine, Pakistan, Myanmar, Serbia ➔ 100% DAC List
- Currency risk markets

Innovate

- 15 year tenor, or more (i.e. India)
- Deliverable swaps on-shore
- Integrate into comprehensive solutions (Global De-risking Facility for Solar PV, SIDS IRENA initiative, ASEAN FX Hedging Facility)

Advocate

- "**Local currency financing improves MICRO + MACRO sustainability and development**." @ UN Sustainable Development Agenda, G20 Sustainable Infra, EU Sustainable World Action Plan + Blended Finance, OECD DAC, MDB & DFI boards.
- Notion "**hard-currency funding is anti-mission"** is gaining traction
- Conferences, webinars bi weekly, OPEDs

III. How TCX Works with ECAs

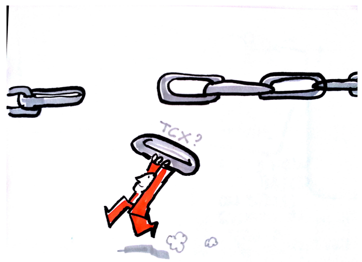
III. How Can TCX Support Export Finance?

Local currency funding and more accessible hedging/insurance tools improve risk allocation and reduce default risks. Improved resilience may widen the reach of ECAs. TCX covers most low and middle income countries which Berne Union members have described as “neutral to hard”.

- TCX supports Lenders in EXPORT FUNDING transactions in local currencies.
- TCX enhances currency risk resilience of Borrowers. Lender to manage counterparty risk?
- How to quantify and manage currency risk associated with EXPORT GUARANTEES? Uncertain cash-flows require optionality, which TCX does not offer. Which party is most suitable to carry the risk?

Client	Dutch Consortium
Currency	USD/CRC
Size	USD 27,150,000
Tenor	3 years
Product	Non-Deliverable Forward

- A consortium has been awarded the contract for the design and construction of Phase 2 of new container terminal in Moin, Costa Rica.
- The local subcontractors required payment in local currency. The consortium leader wanted to hedge the currency risk of these payments.
- Due to cooperation with TCX a Dutch Bank was able to successfully provide a hedge removing the currency exposure from the transaction.



THE GLOBAL SOLUTION FOR LOCAL CURRENCY

Client	Dutch Consultancy firm
Currency	USD/GHS
Size	USD 11,000,000
Tenor	5 years
Product	Non-Deliverable Forward

- A consultancy firm is bidding in an international tender for the provision of long term consultancy services to a parastatal active in logistics.
- The bidding documents indicate a preference for a party that would accept partial payment in Ghanaian cedi, as the parastatal concerned has limited USD income.
- The bidding documents included a price based on GHS, stating that the final price would have to be fixed pre signing date.

IV. REMAINING BARRIERS

- Cognitive barriers (last observation, simple model) lead to underpricing of risk.
- Insurance/hedging in high risk-countries (LDCs) is financially not accessible for the poor and SMEs.
- Short-termism of borrower representatives (manager, politicians). Local currency borrowing looks less attractive in short-term.
- Lenders have short-term performance targets and competitive pressures.
- Institutional inertia (example: OECD DAC rules to determine concessionality)

Solutions: Code of conduct for DFIs, consumer protection rules & prudential requirements, awareness building, shifting from HIPC to explicit or implicit subsidies?

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European Bank for Reconstruction and Development

KFW

FMO Entrepreneurial Development

European Investment Bank The EU bank

JBIC

DBSA Development Bank of Southern Africa

afd Agence Française de Développement

IFC International Finance Corporation World Bank Group

Banque Africaine de Développement / African Development Bank

OFID The OPEC Fund for International Development — Uniting against Poverty

bio Development through Investment

mfx Microfinance Currency Risk Solutions

COFIDES

OIKO CREDIT investing in people

Proparco Groupe Agence Française de Développement

EFSE European Fund for Southeast Europe

ASN BANK Voor de wereld van morgen

Oxfam Novib

Grameen Crédit Agricole Microfinance Foundation

BlueOrchard Impact Investment Managers

IDB Inter-American Development Bank

Ministry of Foreign Affairs of the Netherlands

Federal Ministry for Economic Cooperation and Development

Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety

Questions?

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