

# The Currency Exchange Fund

May 2008



# Why TCX?

# The Local Currency Challenge

## Often, the market status quo does not allow for long-term local-currency financing

- International long-term emerging-market debt financiers are unwilling to assume market risks (currency risk and interest rate risk), and appropriate hedging products are not available
- Local financiers are unable to provide long-term debt due to lack of appropriate funding options

## Result:

- Borrowers with assets generating long-term local-currency revenues must choose between two “second-best” options: long-term hard-currency liabilities (currency mismatch) or short-term local-currency liabilities (maturity mismatch)

# The TCX Solution

- Global partnership of international long-term investors in emerging markets, such as:

AFD / Proparco

COFIDES

DEG / KfW

EBRD

EFSE

FMO

Norfund

Oikocredit

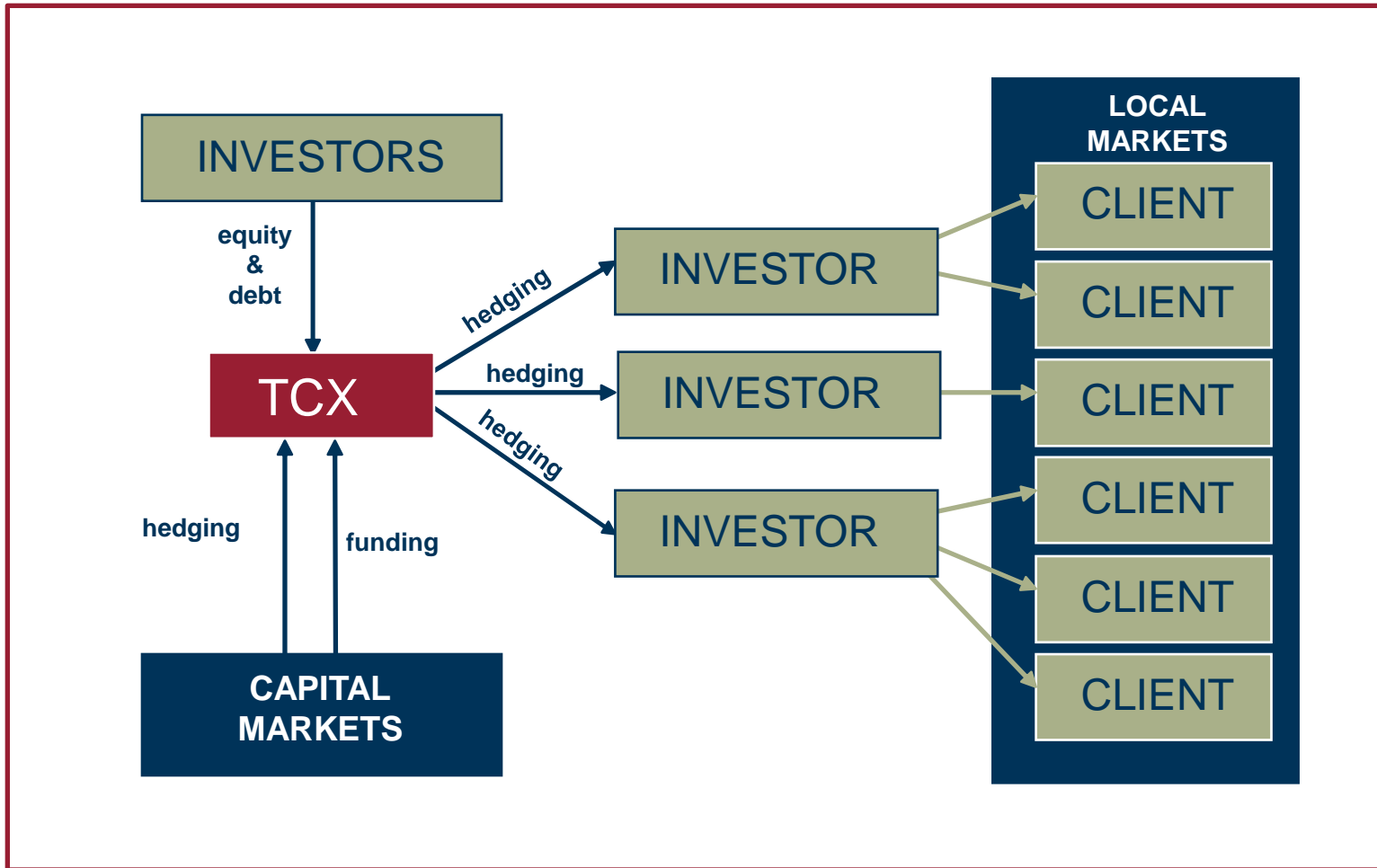
- EUR 50m first-loss tranche provided by the Dutch Government
- Based on the concept of broad market risk diversification
  - up to 75% risk reduction from individual currency exposure due to portfolio effect.
- Structured to obtain a high-quality rating (AA- or better), TCX acts as a swap counterparty to investors who, in turn, provide their products in local currency rather than USD/EUR
- TCX aims to maximize local capital markets participation

# TCX Investors



# The TCX Model

# TCX Business Concept



# TCX Capital and Risk Structure

## Current capitalization

- Share capital: USD 394 million
- Subordinated loan: USD 100 million
- Subordinated convertible loan: EUR 50 million

## Conservative risk management

- Tier 1 capital ratio minimum of 15%
- Tier 1 + Tier 2 capital ratio minimum of 21%
- Tight risk concentration limits
- Independent risk manager
- Liquidation trigger event to ensure orderly liquidation process at capital ratio below 14%

# TCX Commercial Concept

## Coverage

- All DAC 2006 countries
- For floating-rate products, maturity is unlimited
- For fixed-rate products, maturity is limited to 150% of the longest-maturity liquid benchmark available in the market
- At present, the single-currency limit is about USD 230 million
- Transactions limited to hedging real exposures – no speculation

## Pricing

- Pricing is market-based and referenced to local benchmarks
  - No distortion of markets
- Additionality
  - No competition with commercial banks

# TCX Products

## Offshore Products

- Non-Deliverable Cross-Currency Swaps and Forwards

## Onshore Products

- Agency Cash Management Services
- Deliverable Cross-Currency Swaps and Forwards

Approved Southeast European Benchmarks		
ALL	Albanian Lek	3-month, 6-month, and 1-year T-bills
BAM	Bosnia-Herzegovina Mark	EUR swap curve with risk premium
MDL	Moldova Leu	1-month, 3-month, 6-month, and 12-month CHIBID and CHIBOR averages
MKD	Macedonia Denar	3-month and 6-month T-bills
RSD	Serbian Dinar	1-month, 3-month, and 6-month BELIBOR

# Development Impact

## Removal of currency and interest-rate mismatches

- Reduced market risk leads to lower business risk, which leads to lower credit risk, which leads to a lower cost of funds
- Local currency funding for key sectors, such as manufacturing, finance, and infrastructure
- Reduced impact of currency shocks on the local economy

## Active development of the local capital market and financial sector

- Development of high-quality long-term asset classes, such as fixed-term loans, mortgages, and leasing
- Extension of local yield curves



# Conclusion

# Principles and Success Factors

## TCX Principles

- Additionality
- Partnership
- Commercial pricing

## TCX Success Factors

- TCX investors
- Geographical diversification effect
- Robust financial structure
- Management capability

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