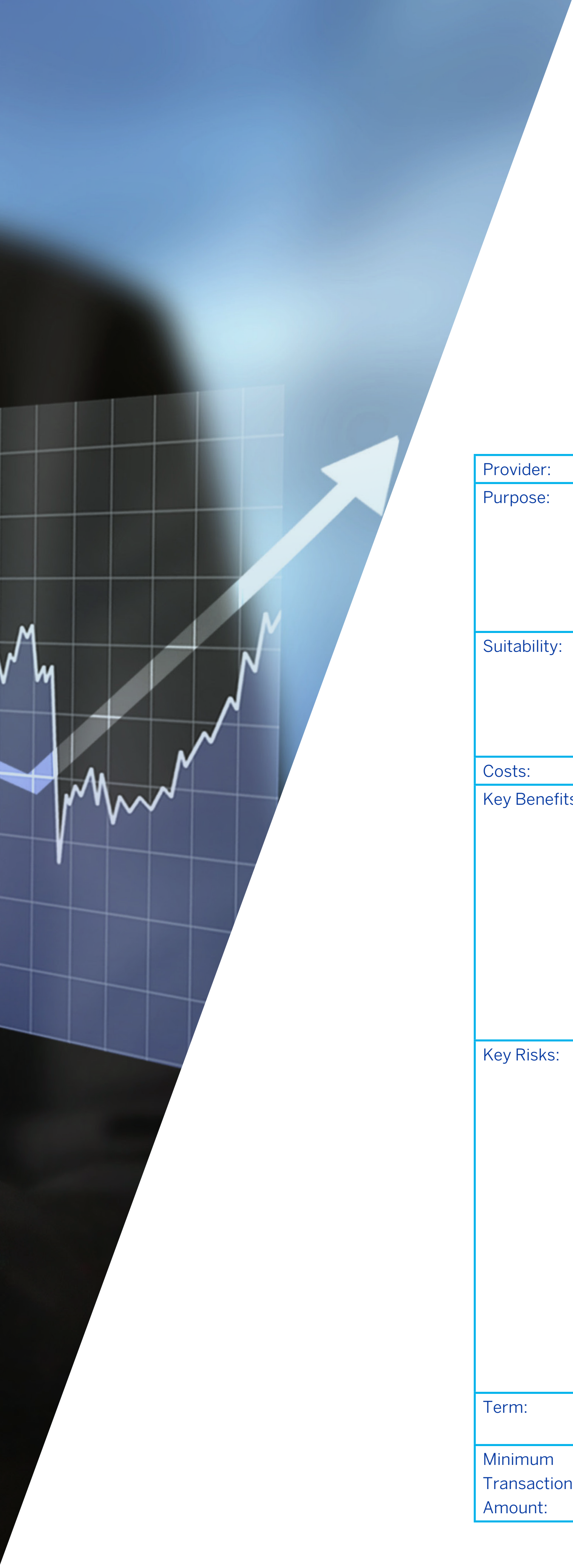
Foreign Exchange

Non-deliverable Forward Transaction

Standard Bank IT CAN BE™


35%
15%
search



Foreign Exchange Non-Deliverable Forward Transaction (NDF) Summary

Provider:	The Standard Bank (Mauritius) Limited ("SBMU").
Purpose:	A foreign exchange Non-Deliverable Forward Transaction ("NDF") is a cash-settled foreign exchange transaction. It is designed to assist in reducing foreign exchange risk in situations where physical delivery of the underlying currencies is not required and/or in markets where physical delivery is not possible.
Suitability:	An NDF may be suitable if you have a good understanding of foreign exchange markets and have a commercial need to manage currency risk associated with a particular currency pair. It should not be used for speculative purposes.
Costs:	There are no up-front costs associated with an NDF.
Key Benefits:	• **Protection** – An NDF provides you with protection against unfavourable exchange rate movements. • **Coverage** – NDF's are available for a broad range of currencies. • **Managing Risk** – Where exchange restrictions do not allow physical delivery of currency, NDF's provide a means of mitigating foreign exchange risk. • **Flexibility** – The maturity date and the notional amount can be tailored to meet your particular needs.
Key Risks:	• **Opportunity loss** – You will not receive the benefit of favourable exchange rate movements. • **Variation/Early Termination** – You can adjust or terminate an NDF early upon prior agreement with SBMU, but there may be a cost if you do so. • **Counterparty and operational risk** – SBMU has performance obligations under an NDF. You need to assess SBMU's ability to meet those obligations. • **Fixing Risk** – NDF's fix against official rates (see Appendix A attached hereto). It is possible that the official rates do not reflect at which rate one will actually be able to transact in the deliverable foreign exchange market.
Term:	Usually 1 month to 1 year (other terms may be available on request).
Minimum Transaction Amount:	The minimum notional amount of an NDF is normally USD100 000 or the local currency equivalent.

Non-Deliverable **Forward Transactions – FAQ's**

1. What is an NDF?

An NDF is an agreement between a client and SBMU that can be used to protect against unfavourable exchange rate movements. It operates in the same way a foreign exchange forward transaction does in the sense that it is an agreement to buy or sell currencies at a specific forward price. The difference, however, is that it is a cash-settled transaction, meaning that there is no exchange of currencies between the client and SBMU at maturity, but rather a cash settlement in an agreed currency of what the contract is worth at maturity.

An NDF can be used to manage the currency risk associated with:

- exporting and/or importing goods;
- investing and/or borrowing amounts denominated in a foreign currency;
- repatriating profits denominated in a foreign currency;
- converting dividends denominated in foreign currency denominated; and/or
- settling other foreign currency contractual arrangements.

It is particularly useful where a forward physical exchange of currencies is not required or in cases where a central bank of a relevant jurisdiction limits access to foreign currency in its domestic cash markets. An NDF should only be used where there is a commercial need to manage currency risk. It should not be used for speculative purposes.

2. How do NDFs work?

The following items form the key components of an NDF contract:

- The amount of foreign currency in respect of which currency protection is sought in terms of the transaction (the "**notional amount**");
- The two currencies involved (the "**settlement currency**" and the "**non-deliverable currency**");
- The **maturity date** on which cash settlement will occur;
- The relevant foreign exchange rate at which the currency protection is fixed (the "**contract rate**") to be provided by SBMU; and
- The date at which the relevant spot foreign exchange rate for the relevant currency pair (the "**fixing rate**") which is to be determined by SBMU (the "**fixing date**") in order to determine which party will pay the other the relevant cash-settlement amount.

More information on how these rates are determined is set out in the questions that follow.

The best way to understand an NDF is by way of example:

Let's assume:

- The Reference Currency is Kenyan shilling ("KES"), being the non-deliverable currency; and
- The Settlement Currency is United States dollars ("USD"), being the currency in which settlement will take place.

If the client is concerned about KES weakening against USD, then it should enter into an NDF where it elects to sell KES and purchase USD on the maturity date. Alternatively, if the client is concerned about the KES strengthening against USD, then it should enter into an NDF where it elects to purchase KES and sell USD on the maturity date.

In each of the cases above, there are three possible outcomes at maturity:

- If the contract rate is more favourable for the client than the fixing rate, SBMU will pay the client the difference in the Settlement Currency;
- If the contract rate is less favourable for the client than the fixing rate, the client will pay SBMU the difference in the Settlement Currency; or
- If the contract rate is equal to the fixing rate, there will be no settlement by either party at maturity.

3. How does SBMU determine a contract rate?

SBMU takes into account several factors when determining this rate. These include:

- the currency pair;
- the maturity date;
- inter-bank foreign exchange rates;
- the notional amount;
- market volatility; and
- inter-bank interest rates of the jurisdictions of the currencies for part of the currency pair.

Note that the contract rate does not represent a forecast that SBMUhas made, nor is it a guarantee of future exchange rates in the deliverable market.

4. How does SBMU determine the fixing rate?

The **fixing rate** for a particular currency pair is sourced from an independent market rate provider used by the financial markets industry. Generally the rate is published on a Reuters reference page or a Central Bank webpage.

The **fixing date** is the date on which the fixing rate is determined and is usually two business days before the maturity date. In situations where an NDF is required against ZAR or EUR rather than USD, SBMU will specify the way in which the fixing rate will be determined.

5. How does SBMU determine the cash settlement amount?

SBMU calculates the cash settlement amount using the notional amount, the contract rate and the fixing rate.
The **cash settlement amount** will be the difference between **the contract settlement currency amount** and the **fixing settlement currency amount**, where:
contract settlement currency amount = notional amount converted at the contract rate and;
Fixing settlement currency amount = notional amount converted at the fixing rate.

6. What happens at maturity?

NDF's are cash-settled at maturity through a payment of a cash settlement amount. This means that at maturity, no exchange of the non-deliverable currency occurs.

7. Can I terminate an NDF before maturity?

The client may ask to terminate the NDF at any time up to and including the fixing date. SBMU may in its discretion provide the client with a termination quote and if the client accepts the termination quote, SBMU will cancel the NDF. SBMU's termination quote will incorporate the same variables (the contract rate, currencies, term, notional amount, fixing rate and maturity date) used when determining the contract rate. These will be adjusted for the prevailing market rates over the remaining term of the NDF. SBMU or the client, as determined by SBMU, will upon termination of the NDF pay an amount equal to the termination quote to the other.

8. Can I amend the maturity date?

At any time up to the fixing date, the client may ask SBMU to amend the maturity date of the client's transaction. SBMU will in the normal of course of business, but subject to its discretion, be able to quote a price to do this, as an adjustment to your existing contract rate. The extension quote takes into account the existing contract details, the exchange rate and the relevant market interest rates prevalent at that time (the "**forward margin**"). This forward margin will be expressed in exchange rate points and may be positive or negative. Where it is positive it will be added to your existing contract rate: where it is negative it will be subtracted. If you accept the extension SBMU will send you an amended confirmation.

9. Example trade: Illustration of cash flows

A multinational corporate client needs to hedge KES risk for 6 months' maturity. They have KES equivalent of USD1 million to hedge.

- Current USD/KES spot rate USD/KES105.00;
- The 6 month USDKES NDF contract rates are 114.00/116.00
- Here the corporate client concludes a 6 month NDF where they sell KES/buy USD at a contract rate of 116.00
  - That is, they sell KES116 million (buys USD1 million).

The below table highlights three scenario's with different fixing rates:

Scenario one	Scenario two	Scenario three
Customer Sells KES116 million Fixing rate: USD/KES110.00 Client Buys USD1,054,545.45	**Customer Sells KES116 million** Fixing rate: USD/KES116.00 Client Buys USD1 million	**Customer Sells KES116 million** Fixing rate: USD/KES120.00 Client Buys USD966,666.67
Single cash flow at maturity		
Client net pays USD54,545.45	Net – no cash flow	Client net receives USD33,333.33

In each case, the single USD cashflow represents the profit or loss on the deal. Just like a deliverable forward contract, the client has hedged his KES exposure at USD/KES116.00. The receipt or payment in USD via the NDF is offset by the loss or gain in USD/KES move.

Appendix A

The table below sets out information relevant to the fixing rates for a number of currencies The Standard Bank (Mauritius) Ltd can offer:

Currency	NDF Fixing Page
AOA (Angolan kwanza)	BNA auction rate (under "Venda" on www.bna.ao)
EGP (Egyptian pound)	FEMF reuters page 12.30PM Fix
ETB (Ethiopian birr)	Central Bank Transaction FX rate (avg of bid and offer on www.nbe.gov.et/market/dollarcurrencies.html)
GHS (Ghanaian cedi)	AFRICAFIX=TR Reuters page
KES (Kenyan shilling	AFRICAFIX=TR Reuters page
MGA (Madagascan ariary)	Central Bank Rate (under Cours du Mid on www.banque-centrale.mg/
MWK (Malawian Kwacha)	Central Bank public FX rate (average of bid and offer on www.rbm.mw)
MZN (Mozambique metical)	Central Bank FX rate (average of compra and venda on http://www.bancomoc.mz/fm_MercadosMMI.aspx?id=10)
NGN (Nigerian Naira)	NIFEX published by FMDQ
RWF (Rwandan franc)	Central Bank Transaction FX rate (avg of selling and buying on www.bnr.rw)
TZS (Tanzanian shilling)	Central Bank (USD selling rate / 100, on www.bot-tz.org
UGX (Ugandan shilling)	Mid CB rate on www.bou.or.ug (Midday Kampala)
ZMW (Zambian kwacha)	AFRICAFIX=TR Reuters page

Get in Touch:
Global Markets Sales Team
Telephone: +230 402 5047/5049
Email: MauritiusTreasuryFrontOffice@standardbank.mu