



# Hedging SDR Exposure



**BNP PARIBAS**  
CORPORATE & INSTITUTIONAL BANKING

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## 1. What is SDR?

## 2. Hedging Ideas

- **Forward**
- **Vanilla Option**
- **Collar (Risk Reversal)**

## 3. Potential impact of inclusion of Chinese Renminbi in SDR



## What are Special Drawing Rights (SDR)?

- The SDR is an international reserve asset, created by the IMF in 1969 to supplement its member countries' official reserves
- Its value is based on a basket of four key international currencies, and SDRs can be exchanged for freely usable currencies
- As of March 17, 2015, 204 billion SDRs were created and allocated to members (equivalent to about \$280 billion)

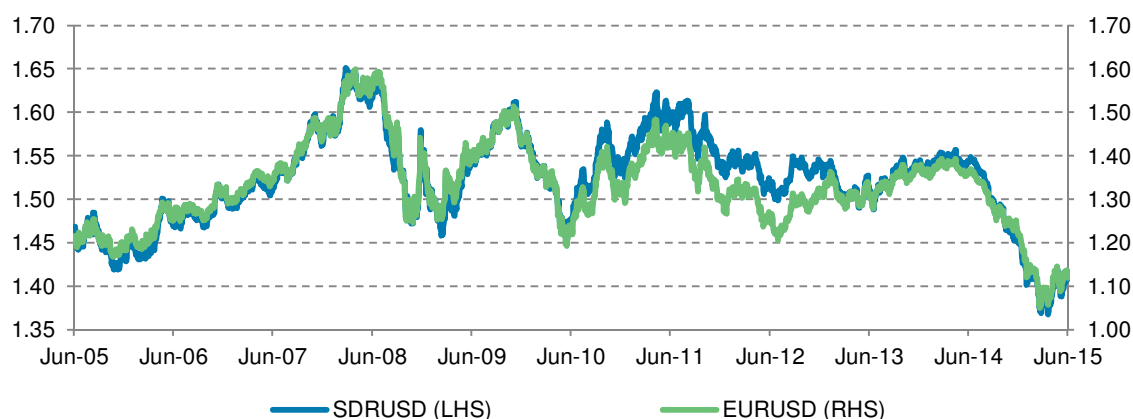
## Other Key Facts

- The allocation of SDRs for IMF members is proportional to their standing in the organization based on their share of the global economy
- While SDRs cannot be used to purchase goods and services directly, countries can exchange them amongst themselves
- Once SDRs have been added to a country's official reserves, these can be exchanged for hard currencies such as the USD, EUR, JPY or GBP through voluntary trading arrangements with other IMF member countries
- The basket composition is reviewed every five years by the Executive Board, or earlier if the IMF finds changed circumstances warrant an earlier review, to ensure that it reflects the relative importance of currencies in the world's trading and financial systems
- ***The next review is currently scheduled to take place by the end of 2015***

## Current Value of 1 SDR

Currency	Weight
USD	0.6600 (41.9%)
EUR	0.4230 (37.4%)
JPY	12.1000 (9.4%)
GBP	0.1110 (11.3%)

## Historic SDRUSD vs EURUSD Chart



Source: BNP Paribas, Bloomberg, IMF, CIEC



# 1 - Forward

## Product Details

### Forward

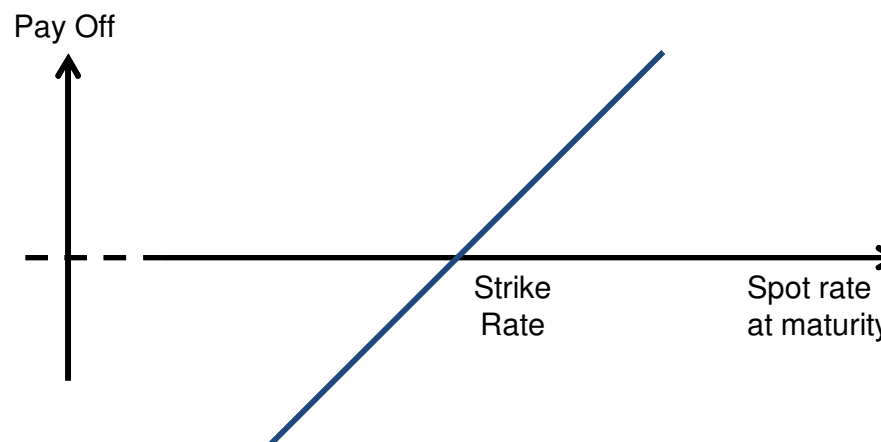
A Forward provides the customer with a guaranteed worst-case hedge rate.

Indicative Terms	
Currency Pair	SDRUSD
Spot Reference	1.4038
Client Direction	SDR Buyer USD Seller
Notional	SDR 35m (~50m USD Equivalent)
Expiry	1 Month from trade date
Delivery	Two business days following expiry
Strike Rate	1.4048

### Mechanics

At expiry:

- If SDRUSD Fixing Rate is above the Strike Rate, the Client receives the USD Cash Amount on the Delivery Date, calculated as follows:
  - $\text{SDR Notional} \times (\text{SDRUSD Fixing} - \text{Strike Rate})$
- If SDRUSD Fixing Rate is below the Strike Rate, the Client pays the USD Cash Amount on the Delivery Date, calculated as follows:
  - $\text{SDR Notional} \times (\text{Strike Rate} - \text{SDRUSD Fixing})$



## 2 – Vanilla Option

### Product Details

#### Vanilla Option

A vanilla option provides the customer with a guaranteed worst-case hedge rate as well as the possibility of participating in any favourable move in the underlying.

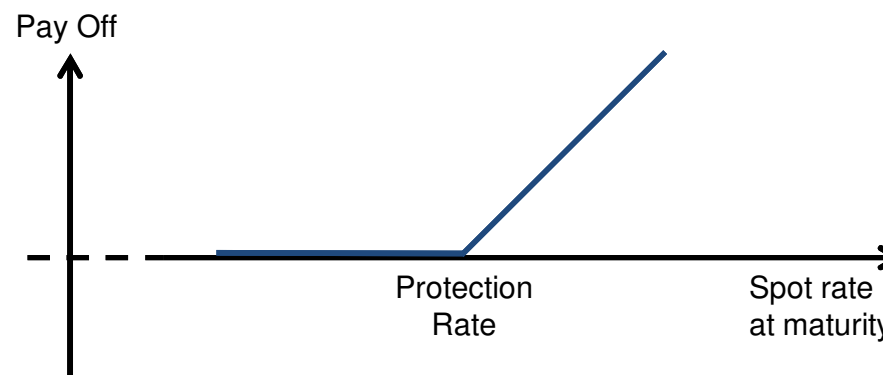
#### Mechanics

Client pays a premium amount upfront

At expiry:

- If SDRUSD Fixing Rate is above the Protection Rate, the Client receives the USD Cash Amount on the Delivery Date, calculated as follows:
  - $\text{SDR Notional} * \text{Max}[0, \text{SDRUSD Fixing} - \text{Protection rate}]$
- Otherwise there are no obligations for either party

Indicative Terms		
Currency Pair	SDRUSD	
Spot Reference	1.4038	
Client Direction	SDR Buyer USD Seller	
Notional	SDR 35m (~50m USD Equivalent)	
Expiry	1 Month from trade date	
Delivery	Two business days following expiry	
Forward	1.4048	
Protection Rate	1.4038	1.4250
Premium	0.75% (USD 375K)	0.25% (USD 125K)



## 3 – Collar (Risk Reversal)

### Product Details

#### Collar (Risk Reversal)

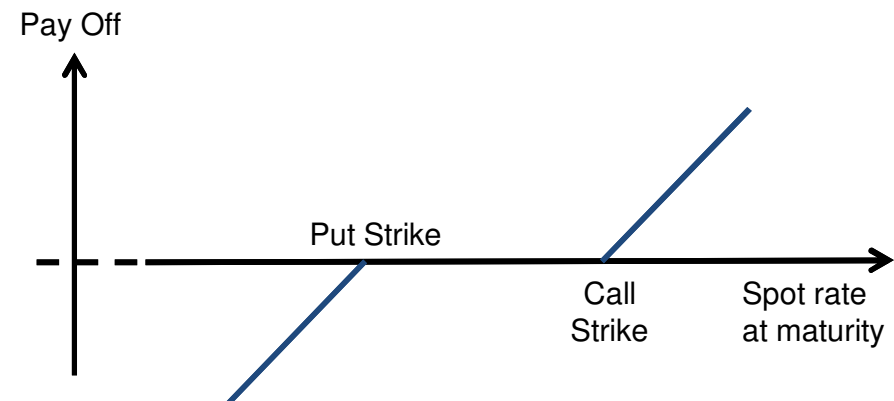
The Collar provides the customer with a guaranteed worst-case hedge rate as well as the possibility of participating in a favourable move in the underlying up/down to a predefined cap.

#### Mechanics

At expiry:

- If SDRUSD Fixing Rate is above the Call Strike, the Client receives the USD Cash Amount on the Delivery Date, calculated as follows:
  - $\text{SDR Notional} \times (\text{SDRUSD Fixing} - \text{Call Strike})$
- If SDRUSD Fixing Rate is at or below the Call Strike and above the Put Strike, there are no obligations for either party.
- If SDRUSD Fixing Rate is below the Put Strike, the Client pays the USD Cash Amount on the Delivery Date, calculated as follows:
  - $\text{SDR Notional} \times (\text{Put Strike} - \text{SDRUSD Fixing})$

Indicative Terms	
Currency Pair	SDRUSD
Spot Reference	1.4038
Client Direction	SDR Buyer USD Seller
Notional	SDR 35m (~50m USD Equivalent)
Expiry	1 Month from trade date
Delivery	Two business days following expiry
Forward	1.4048
Call Strike	1.4500
Put Strike	1.3760



# Potential impact of inclusion of Chinese Renminbi in SDR

Potential impact of inclusion of Chinese Renminbi in SDR

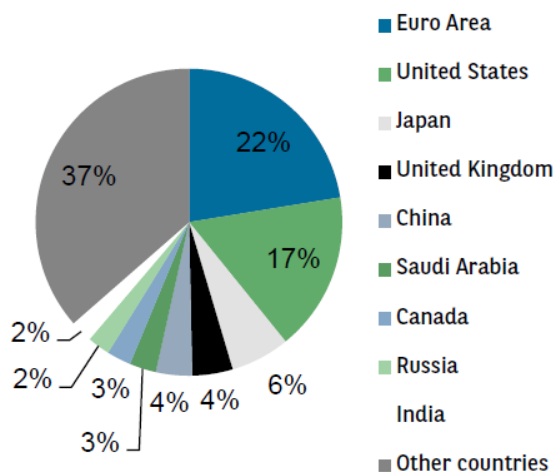
## Background

- China is transitioning to a “new normal” aimed at fostering safer but slower growth, with monetary easing and financial re-engineering being employed as the two main monetary policy tools to re-profile debt and smoothen the transition
- ...our assessment now is that the substantial real effective appreciation over the past year has brought the renminbi exchange rate to a level that **is no longer undervalued**. – IMF press release, May 26 2015
- PBOC to engineer a stable RMB ahead of SDR review (IMG board meeting in Oct 2015)

## RMB – October SDR inclusion?

- Voting required for SDR inclusion:
  - 70% majority, if China is deemed to have met both criteria of being a gateway (importance of the country's trade globally) and freely usable (widely used and widely traded) currency
  - 85% supermajority, otherwise
- Short-term flow impact on RMB will be limited. We believe the short-term impact on the RMB is more symbolic
  - Following SDR inclusion and near term political engagements, we expect the PBoC to become more willing to accommodate volatility in the RMB exchange rate and widen the daily trading band

## Percentage of voting rights in the IMF



## RMB Real Effective Exchange Rate



Source: BNP Paribas, Bloomberg, IMF, CIEC



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