Citi arranges 10-year Cross-currency Swap for Caribbean Nation Lowering Cost and Risk

Case Study

The Challenge

In 2010, a Caribbean nation borrowed CNY484 million (US$78 million equivalent) from the China Exim Bank in order to finance infrastructure projects on the island. As is customary with such transactions, the facility was denominated in Chinese Yuan. However, because this government's revenues were in U.S. dollars, there was an inherent currency exposure due to fluctuations in the value of the Yuan versus the U.S. dollar.

As a result of such fluctuations, the cost of the loan could rise or fall depending on the relative strength of either currency at the time of repayment. During a routine review of the Government's financial needs and overall risk management, a review of this exposure was conducted with an eye toward mitigating risk by affixing the exchange rate between the two currencies, as well as fixing the interest rate in U.S. dollars.

The Solution

Citi worked with the Government to convert the debt synthetically from Chinese Yuan to U.S. dollars, which it could readily access. Citi arranged a simple 10-year cross-currency swap with full exchange of remaining balances at year 10, which is a longer term than the typical five- to seven-year tenor. Hedges would take place as disbursements were completed, eliminating exposure until that time.

By arranging a fixed-rate facility in U.S. dollars, the Government was able to take advantage of a lower price than what they normally would have had access to in the market. Citi's approach and original solution have provided this sovereign nation with a successful solution for their currency exposure to the Chinese Yuan.

The Result

As a result of Citi's 10-year cross-currency swap, this Caribbean nation now has certainty for the next 10 years around the overall cost of its Chinese facility. Because the Yuan has appreciated relative to the U.S. dollar since the inception of the facility, the cost of the underlying loan has risen. However, the hedge set up by Citi has enabled the Government to fix their costs, which has proven to be a tremendous benefit.

A further benefit is that the Government now has greater flexibility in terms of financing options in the future. If there is an opportunity to access funding in a cheaper currency or at a cheaper rate, even if that funding is not in U.S. dollars, the Government now has the ability to swap those funds synthetically in U.S. dollars. This solution offers an effective roadmap for other sovereign governments.

Since the completion of this facility, the Caribbean nation has successfully financed its infrastructure projects, allowing the Government to move forward with public transportation improvements.

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