TCorp Foreign Exchange Execution Framework

The TCorp Foreign Exchange Execution Framework (TCorp Execution Framework) provides guidance to Government Entities in relation to identifying and hedging foreign exchange (FX) risk, in accordance with TPP18-03 NSW Government Foreign Exchange Risk Policy.

This framework is designed to ensure that FX risk is identified and managed transparently, consistently, and at the lowest cost and/or risk to the State, by either:

i. Executing FX hedging transactions through TCorp; or

ii. Executing FX hedging transactions directly with '**TCorp's panel of service providers**' to ensure that Government Entities and the State obtain the best value; or

iii. Supporting and executing (where appropriate) FX transactions below the '**Threshold**'[1] through the Transactional Banking Platform to minimise related costs for immaterial transactions.

TCorp acts as an intermediary between Government Entities and service providers, thus it does not charge fees for executing FX hedging transactions. TCorp also receives preferential pricing due to its existing relationships with multiple service providers, its daily collateral management procedures[2], and access to wholesale rates based on the State's credit rating.

Steps for Government Entities to follow (see Table A – Process Summary):

Step 1: Identify Foreign Exchange Risk

Does your Government Entity:

- Buy or sell goods or services in foreign currency?
- Source goods or services from overseas or foreign companies?
- Own, otherwise control, or manage assets or liabilities denominated in foreign currencies?
- Have other income, such as royalties, interests, dividends etc. received in or affected by foreign currencies?

[1] The Threshold is defined in TPP 18-03 (NSW Government Foreign Exchange Risk Policy) as the face value amount of A$500,000 (or equivalent) or as otherwise agreed by Treasury.

[2] Where TCorp is not used as an intermediary, Government Entities will either have to manage collateral themselves or get a 'non-collateralised' price (this includes where TCorp's panel of service providers is used).

Step 2: Quantify the Direct and Indirect Foreign Exchange Risk

How much FX risk does or will your Government Entity have?

- Has your Government Entity made a commitment to complete a sale, purchase, or other government transaction (through contract or otherwise), either denominated in a foreign currency or A$, where goods and services are sourced outside of Australia (the Commitment)?
- Has a risk arisen:
  - due to a Commitment – **'Contracted Risk'**
    - e.g. purchasing US$100m per annum of medical consumables from the USA
  - prior to making a Commitment, but where a spending approval is obtained - **'Contingent Risk'**
    - e.g. a project and budget approval to make a significant purchase of equipment from overseas, or from a foreigner supplier, where the contract will not be signed for a number of months
    - where a **Contingent Risk** may occur, Government Entities should consult with Treasury (Treasury Relationship Leads) and TCorp to determine whether it is a '**Substantial Risk'**[3].
  - from making a Commitment denominated in A$, and/or where this spending is expected to continue to occur over future years – **'Embedded Risk'**
    - e.g. a Government Entity has a contract priced in A$ for medical consumables which are most likely sourced from the USA. The cost of the current contract may include an embedded or hidden premium for providing an A$ price for a US$ sourced product. Likewise, the cost of future contract renewals may be substantially higher due to FX movements.
  - from a balance sheet exposure of financial or non-financial assets to FX movements - **'Translation Risk'**
    - e.g. A Government Entity has an asset valued in A$ on its balance sheet, where this asset is inherently linked to a US$ market.
- What is the size of the exposure?
- Which foreign currency/ies is/are involved?
- What is the timing of the exposure and does it re-occur (e.g. monthly, annually or one-off)?

[3] Substantial Risk is defined in TPP 18-03 (NSW Government Foreign Exchange Risk Policy) as a risk considered by Treasury and TCorp to be substantial based on a range of factors, namely, size and nature of the exposure, duration and size of the procurement, frequency of the risk occurrence, timing and level of volatility of the foreign currency/ies to A$.

Step 3: Know your PAFA

What approval does your Government Entity have?

- General approval to transact FX hedging where the Government Entity chooses not to pay invoices in foreign currencies, through the Transactional Banking Platform, or State Owned Corporations through their approved banking platform, if less than the **Threshold**.
- Approval to transact FX hedging directly with TCorp's panel of service providers.
- Approval to manage FX with funds managers, where it is part of the Government Entity's approved investment strategy within the scope of its investment powers.

No approval is required to transact FX hedging with TCorp.

Actions required

1. If you answered **'Yes'** to any of Step 1 and need help with Step 2 to explore cost savings and/or certainty, contact TCorp.

2. If you have a **Contracted Risk**, execute a hedge if the exposure amount is greater than the Threshold (unless advised otherwise by Treasury), no later than 3 business days after making the Commitment.

    a. Without a PAFA approval to transact FX hedging, contact TCorp.

    b. With a PAFA approval to transact FX hedging, execute either through TCorp or TCorp's panel of service providers.

If the exposure amount is below the Threshold, transact through the Transactional Banking Platform.

3. If you have a **Contingent Risk**, contact TCorp, TCorp will work with you and Treasury to determine whether it is a **Substantial Risk**.

    a. For **Contingent Risk** that is not deemed to be a **Substantial Risk**, there is no requirement to hedge the **Contingent Risk** (noting this will be re-assessed where certain changes occur e.g. increased probability, increased size, or it becomes a **Contracted Risk** greater than the Threshold).

    b. For **Contingent Risk** that is deemed to be a **Substantial Risk**, Government Entities will develop and update (where needed) a 'FX risk management plan' through consultation with TCorp and Treasury. This will be included in government submissions (e.g. ERC Submissions).

    c. Where FX hedging transactions are to be undertaken, the process for execution will be detailed in the FX risk management plan.

4. If you have an **Embedded Risk** above the **Threshold**, or wish to explore whether you may have an **Embedded Risk**, contact TCorp. TCorp will help you to compare the cost effectiveness of making a Commitment denominated in A$ versus foreign currency. This will involve obtaining quotes (where possible):

a. in A$ from the counterparty; and
b. in foreign currency from the supplier, together with an FX hedge quote from TCorp to compare to the A$ quote.

Where FX hedging transactions are to be undertaken:

a. Without a PAFA approval to transact FX hedging, contact TCorp.
b. With a PAFA approval to transact FX hedging, execute either through TCorp or TCorp’s panel of service providers.

5. If you have a **Translation Risk** above the **Threshold**, contact TCorp:

a. Government Entities will develop a ‘FX risk management plan’ through consultation with TCorp and Treasury.
b. Where FX hedging transactions are to be undertaken, the process for execution will be detailed in the FX risk management plan.

Contacts

For assistance, please contact:

- Relationship Leads, TCorp
- Relationship Leads, Treasury
- NSW Treasury’s Financial Risk Management team (frm@treasury.nsw.gov.au)

Table A – Process Summary

Type of FX risk/ Action required	Contracted Risk	Contingent Risk	Embedded Risk	Translation Risk
Purpose	FX risk arising from known exposure after making a Commitment	FX risk arising prior to making a Commitment but where a spending approval is obtained	FX risk arising from making a Commitment denominated in A$, and/or spending expected to continue over future years, where goods and services are sourced outside of Australia	FX risk arising from balance sheet exchange rate risk which is measured by the exposure of underlying assets or liabilities to exchange rate movements
Is the exposure greater than the Threshold or a Contingent Risk that is deemed to be a Substantial Risk?	**Yes** – Execute hedge pending your PAFA approval limits unless advised otherwise by Treasury **No** – No requirement to hedge	**Contact TCorp** TCorp will work with you and Treasury to determine whether it is a Substantial Risk. **If deemed a Substantial Risk** – Develop an FX risk management plan through consultation with TCorp and Treasury **If not deemed a Substantial Risk** – No requirement to hedge (noting this will be re-assessed where certain changes occur, e.g. increased probability, increased size, or it becomes a **Contracted Risk** greater than the Threshold)	**Yes** – Obtain different quotes (i.e. in A$ and in foreign currency coupled with an FX hedge quote from TCorp) (where possible) **No** – No requirement to obtain different quotes	**Yes –** Develop an FX risk management plan through consultation with TCorp and Treasury **No –** No requirement to hedge
Without PAFA approval	Contact TCorp	Contact TCorp	Contact TCorp	Contact TCorp
With PAFA approval	Execute through TCorp or TCorp's panel of service providers	Contact TCorp	Execute through TCorp or TCorp's panel of service providers	No further action required