

Principal Only Swap (POS) - FCY to INR

This Product Disclosure Statement is in reference to RBI Circular dated 16.09.2021, Master Direction – Reserve Bank of India (Market-makers in OTC Derivatives) Directions, 2021.

This document contains standard information about the product which may enable the user to determine if the product will meet its hedging needs and to facilitate comparison with other products.

Features

A Principal Only Swap (POS) is a type of currency swap under which two parties exchange only principal cash flows in two different currencies at maturity at a spot reference rate decided at the initiation of the swap. FCY to INR POS is an effective instrument to convert the principal portion of FCY Liability to an INR Liability. Here, the currency risk on the principal is hedged but currency risk and interest rate risk (if any) on the coupon remains open. User pays agreed hedge cost at pre-defined intervals over the tenor of the swap and not at the maturity of the transaction unlike forward premium. In this swap transaction, the user pays hedge cost but does not receive any cash flows in exchange in the interim. The exchange of principal cash flow happens as per amortization schedule.

Illustration:

For a liability in USD where INR is domestic currency, user enters into USD to INR POS to pay a fixed amount of INR and receive a fixed amount of USD on principal amortization dates and pays a cost for the same.

The underlying exposure for this product is a USD liability. User is exposed to risk of USD appreciation against INR resulting in higher INR cost. The USD to INR POS acts as a hedge and converts USD liability (principal only) to INR liability (principal only). Under this product, user pays hedge cost for shifting from a low interest rate liability (USD) to a high interest rate liability (INR).

Building Blocks:

The building blocks of this swap are as below:

- a. FCYINR Spot rate
- b. Overnight (FCY Rate) Curve
- c. Overnight SOFR Curve
- d. Modified MIFOR curve
- e. USDINR FX Swap
- f. FCYUSD cross currency basis curve
- g. Tenor of the swap

Costs and fees, including break-up and details

The derivative cost consists of market cost which is determined through a financial model taking above building blocks as input parameters and the price is dependent on Bid/Offer spread of the FCYINR spot rate, overnight FCY rate curve, overnight SOFR rate curve, Modified MIFOR curve, USDINR Fx swap, FCYUSD cross currency basis curve rate along with administrative costs; Capital charge and transaction handling charges

An illustration of how the product works

User receives under the swap agreement: 0.00% p.a. on USD notional

User pays under the swap agreement: 5.00 % p.a. on INR notional

Coupon settlement frequency: Quarterly

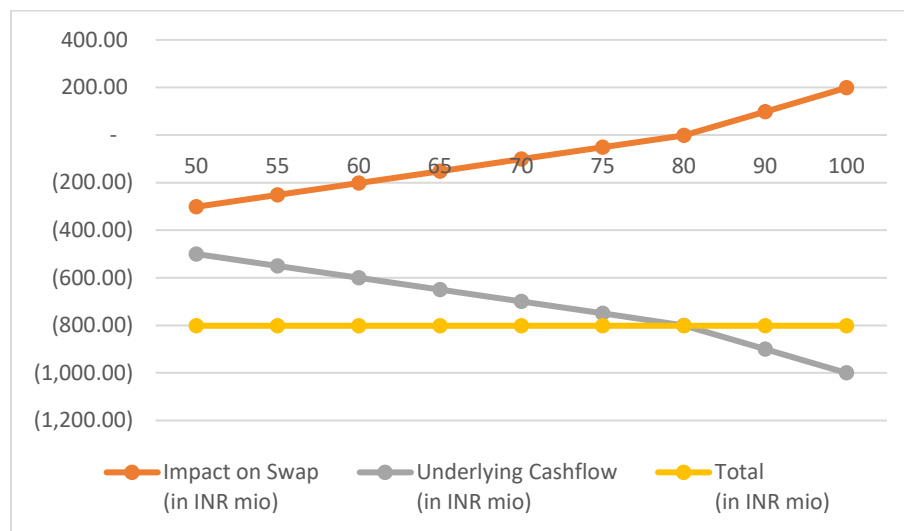
Tenure of swap: 2.5 yrs

Amortization: As per schedule given below

Start Date	End Date	Applicable USD Notional	USD Amortization on End date	USD coupon	Applicable INR Notional	INR Amortization on End date	INR coupon
28-Dec-21	28-Mar-22	10,000,000.00	1,000,000.00	-	750,000,000.00	75,000,000.00	9,246,575.34
28-Mar-22	28-Jun-22	9,000,000.00	1,000,000.00	-	675,000,000.00	75,000,000.00	8,506,849.32
28-Jun-22	28-Sep-22	8,000,000.00	1,000,000.00	-	600,000,000.00	75,000,000.00	7,561,643.84
28-Sep-22	28-Dec-22	7,000,000.00	1,000,000.00	-	525,000,000.00	75,000,000.00	6,544,520.55
28-Dec-22	28-Mar-23	6,000,000.00	1,000,000.00	-	450,000,000.00	75,000,000.00	5,547,945.21
28-Mar-23	28-Jun-23	5,000,000.00	1,000,000.00	-	375,000,000.00	75,000,000.00	4,726,027.40
28-Jun-23	28-Sep-23	4,000,000.00	1,000,000.00	-	300,000,000.00	75,000,000.00	3,780,821.92
28-Sep-23	28-Dec-23	3,000,000.00	1,000,000.00	-	225,000,000.00	75,000,000.00	2,804,794.52
28-Dec-23	28-Mar-24	2,000,000.00	1,000,000.00	-	150,000,000.00	75,000,000.00	1,869,863.01
28-Mar-24	28-Jun-24	1,000,000.00	1,000,000.00	-	75,000,000.00	75,000,000.00	945,205.48

This derivative transaction allows user to convert a USD Liability to an INR liability. Under this transaction, user undertakes to pay INR coupon and receive nil USD coupon on the respective exchange dates. In addition to this coupon exchange, users on both sides exchange principal cash flows on respective amortization/maturity dates.

Pay-off profile:



Impact Analysis

[USD/INR] Level	Impact on Swap (in INR mio)	Underlying Cashflow (in INR mio)	Total (in INR mio)
50	(301.53)	(500.00)	(801.53)
55	(251.53)	(550.00)	(801.53)
60	(201.53)	(600.00)	(801.53)
65	(151.53)	(650.00)	(801.53)
70	(101.53)	(700.00)	(801.53)
75	(51.53)	(750.00)	(801.53)
80	(1.53)	(800.00)	(801.53)
90	98.47	(900.00)	(801.53)
100	198.47	(1,000.00)	(801.53)

Benefits

This structure insulates the user from any adverse currency risk arising from spot movement on FCY based principal exposure. The user with foreign currency liability can convert it to INR liability by paying the hedging cost over the tenor of the transaction.

Risks

- (1) The user may lose from principal exchange risk arising from FCY depreciation/INR appreciation
- (2) The user is still exposed to interest obligation risks (if any)
- (3) Liquidity risk
- (4) Bid-offer spreads in case of unwind



The terms and conditions applicable for booking/termination will be guided by deal term sheet/sanction letter/ISDA document.