28 June 2023

Corporate Sales
Markets & Securities Services,
HSBC India

Product Disclosure Statement – Sell FX Forward

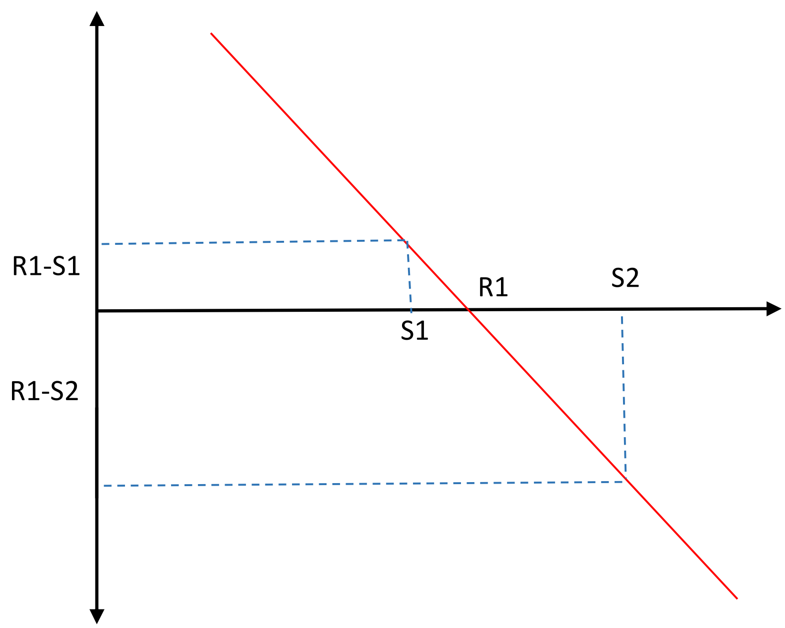
1. Background

A company (hereafter referred as XYZ) has future receivables denominated in foreign currency (USD). Hence, XYZ will be exposed to the FX risk in case INR appreciates against USD on the payment date. If XYZ wants to protect itself from INR appreciation from current levels, it can achieve this hedge objective by selling a vanilla USDINR forward.

2. Product Description – Sell USDINR Forward

A plain vanilla USDINR forward (sell) obliges the contract holder to sell USD against INR at a certain predefined rate (R1).

The payoff of this hedge can be explained via the following pay off diagram -



We now explain this further with an example of an indicative trade.

3. Indicative Trade details

Trade Date:	28-Jun-2023
Indicative Notional	USD 10,000,000.00 (10.00M)
USD/INR Contract Rate (R1)	83.5
Maturity date	30-Jun-2024

XYZ sells USD/INR 10.00M @ 83.5 value dated 30-Jun-2024

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Payoff

Irrespective of spot USD/INR on maturity, XYZ sells USD 10.00M against INR on maturity date.

If USD/INR spot on delivery (S1) is below 83.5 (R1), XYZ sells USD 10.00M against INR on delivery at 83.5, and if XYZ wants to net-settle the contract, they will make a profit of INR (83.5-S1) per USD on maturity date.

If USD/INR spot on delivery (S2) is above 83.5 (R1), XYZ sells USD 10.00M against INR on delivery at 83.5, and if XYZ wants to net-settle the contract, they will make a loss of INR (83.5-S2) per USD on maturity date.

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4. Risk Disclosure Statement

1. Rationale

XYZ is entering into this transaction to hedge its USD receivables at a fixed rate in order to protect itself from potential future INR appreciation against the USD.

2. Risk Factors

XYZ is obliged to sell USD against INR at the Contract Rate for the Notional Amount, which would lead to a loss versus the Spot Rate prevailing on the maturity date if the Spot Rate is above the contract rate on the respective maturity date.

3. Scenario Analysis –

Disclaimer:
The following analysis is produced for illustrative purposes only, and does not reflect a complete analysis of all possible opportunity gain and loss scenarios that may arise under the actual hedge structure. No representation or warranty is made by HSBC that any scenario shown below can be duplicated under the actual structure. Actual results may vary from the results shown below, and variations may be material. The scenario analysis only illustrates potential outcomes on expiration dates and is not considered a reflection of the mark-to-market value nor the exit cost which depends on additional market factors (see sections on 'Building Blocks of the Transaction & Factors impacting pricing', 'Sensitivity Analysis', 'Valuations and Mark to Market' and 'Exit Costs on Early Termination'). The exit cost of the product can fluctuate either upward or downward due to changes in prevailing market conditions. Accordingly, if the hedge structure set out herein is unwound prior to its stated maturity, you may sustain a loss which may well exceed the amount you receive under the said structure.

While the above structure is a hedge for USD receivables, should XYZ decide to net settle the hedge at market levels instead of accepting the USD receivables for settlement of the underlying exposure on the delivery date there would be a net cash flow based on the then prevailing spot rate at the time of net settlement. Refer a few illustrative scenarios below -

Scenario 1 –

Assume a scenario where USD/INR spot is at 100.20 on delivery. There is a loss of INR -167,000,000.00 in this scenario as XYZ would be selling USDINR at a value lesser than the market spot rate.

Scenario 2 –

Assume a scenario where USD/INR spot is at 66.80 on delivery. XYZ would in this scenario be able to sell the USDINR at 83.5, a value higher than the market spot rate hence making a profit of INR 167,000,000.00 on the hedge.

Refer payoff table below for some more scenarios -

USD/INR spot on delivery	XYZ sells USD 10.00 M at	Gain to XYZ (INR)*
100.20	83.5	-167,000,000.00
91.85	83.5	-83,500,000.00
75.15	83.5	83,500,000.00
66.80	83.5	167,000,000.00

*The above analysis assumes the spot rate for net settlement to be the same as the spot rate at the time of delivery

4. Building Blocks of the Transaction & Factors impacting Pricing

The execution of this transaction involves accessing markets for spot USD/INR and USD/INR forwards. On having entered into this transaction -

a. XYZ is selling USD against INR

- The lower the spot the lower is the forward rate and vice versa

b. XYZ is receiving the USD/INR forward premium

- The lower the forward premium the lower is the forward rate and vice versa

5. Sensitivity Analysis

The transaction is sensitive to the market parameters such as but not limited to those mentioned above in the ‘Building Blocks’ section. We explain as to how the change in the market factors mentioned in the ‘Building Blocks’ section would impact the transaction -

- USD/INR Spot rate: If INR depreciates against USD from current levels; it will adversely impact the transaction (i.e. the Mark to Market will be impacted negatively).
- USD/INR Forward Premium: If USD/INR forward premium moves higher, it will adversely impact the transaction (i.e. the Mark to Market will be impacted negatively).

6. Valuations and Mark to Market

The Mark-to Market of the structure and future valuations will be impacted by changes in the variables as highlighted in the ‘Building Blocks’ and ‘Sensitivity Analysis’ sections.

The valuation of the structure can be ascertained from the MTM updates the bank is willing to provide. These MTM updates can be provided upon specific request and/or the same can be provided periodically based on your specific requirements/requests.

7. Exit costs on Early Termination

In case XYZ decides to do an Early Termination of this Transaction there could be Exit costs (or gains) based on market factors as highlighted in the ‘Building Blocks’ and ‘Sensitivity Analysis’ sections. Thus there could be scenarios where there could be a net cash payout (after accounting for the initial option premium paid) by XYZ on Early Termination. Estimates of Exit costs can be provided upon specific request.

What is an exit cost?
An exit cost is a cost that XYZ might incur should XYZ wish to terminate the hedge prior to its scheduled end date for any reason

How are exit costs calculated?
When XYZ enters into a derivative transaction with us, the price proposed at the time is impacted by the initial mark-to-market value of the trade i.e. the current market value (based on market factors as highlighted in the ‘Building Blocks’ and ‘Sensitivity Analysis’ sections) as well as the cost [to us of entering into] hedging

positions expected to cover the term of the hedge to maturity. Should XYZ request to terminate the hedge prior to maturity, these same factors (all of which fluctuate due to changes in market and liquidity conditions) will be considered in order to determine the cost of closing out the transaction on the day of the request.

To illustrate what exit costs might be in the event of changes to the spot rate, please see the table below. Note that we have not considered changes to any other market factors (such as changes in Forward Premium) in this illustration.

Movement vs Spot on Trade Date	Spot reference on Exit	Illustrated Exit Cost (Rs))
+10%	90.20	67,000,000.00
+20%	98.40	149,000,000.00
+30%	106.60	231,000,000.00

The above numbers should only be taken as a simplified illustration, based only on changes in the spot exchange rate and on a limited number of scenarios. Actual exit cost is very likely to be different due to changes in the other market factors as described in the 'Building Blocks' section and the difference may be substantial.

In addition, there is a risk that market liquidity may diminish or become unavailable for this type of transaction at the time of close-out, which would increase further the exit cost as interbank trading spreads may have increased.

Therefore, depending on the market conditions at the time of early close-out the exit costs of early terminating the product could result in substantial loss for XYZ.

8. Underlying Exposure

Receivables of USD 10.00M

Disclaimer:
Please note that these levels are indicative, and are based on current market conditions, and are therefore subject to change. The levels are purely indicative and are meant for discussion purposes only. The above structure is subject to availability of limits and execution of appropriate documentation by the company.

Acknowledgement

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The Client has read this term sheet in detail and has clearly understood the risks and payoffs of this transaction as highlighted in the term sheet, the nature and extent of its exposure to risk and to loss as well as the consequences of the transaction. The Client is aware that the transaction entered into by it is subject to the applicable regulations issued by the Reserve Bank of India (RBI). These regulations are also supplemented by the guidelines issued by the Foreign Exchange Dealer's Association of India (FEDAI) (including around product permissibility), as amended from time to time. The Client's decision to enter into this hedging transaction is based on its own independent assessment and it has not relied on any advice given by HSBC. The Client confirms that they have on hand a valid underlying exposure and they are duly authorized to execute the transaction. Further the Client confirms that the above transaction is in line with its board approvals and the approved risk management policy of the Client. The Client also confirms that it follows prudent accounting and disclosure norms.

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Disclaimer

This document is intended as an outline only of the product(s) described herein and does not purport to list or summarise all of the terms and conditions of a particular transaction, nor to identify or define all or any of the risks that would be associated with the purchase or sale of such product(s). Prior to making an investment decision, you should conduct such investigation and analysis regarding the product(s) described herein as you deem appropriate and to the extent you deem necessary obtain independent advice from competent legal, financial, tax, accounting and other professionals, to enable you to understand and recognise fully the legal, financial, tax

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