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### **Case Study A: Hedging Within an Existing Capital Structure**

#### **Situation:**

- Company was reviewing interest rate risk hedging alternatives given impending hedge maturities and current yield curve
- Company was receiving ideas from multiple sources, including banks and board members

#### **Key Management Questions/Goals**

- How should we think about the fixed/floating ratio?
- Does our existing hedge documentation allow for long-dated swaps?
- How do we ensure ideal hedge accounting treatment of the various alternatives?

#### **Chatham's Approach**

- Crafted "accounting friendly" hedging alternatives that met the business objectives
- Performed analysis to evaluate impact of different rate environments on cash interest expense under each alternative
- Educated treasury and reporting staff on relevant issues & assisted in creation of board presentation materials
- Assisted in ISDA documentation review & negotiation with banks and client's counsel

#### **The Results**

- Board reviewed and approved half of a 2-part hedging alternative
- Relying on guidance provided by Chatham on accounting issues, board tabled part 2 for the time being
- Chatham led \$2bb hedging execution through process involving all 10 relationship banks
- Savings on execution were over **30x** Chatham's fees

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## Case Study B: Merger of a Public Company with a Private Firm

### Situation:

- Private company acquiring a public corporation via refinancing of existing debt
- Financing contingent on shareholder vote scheduled to take place in three months
- Target had existing swaps in liability position facing member of new lending group
- Acquirer found then-current interest rate environment attractive and wanted to protect against rising rates

### Key Management Questions/Goals

- Determine how to settle existing swaps without a cash outlay at deal closing
- Facilitate a potential IPO exit down the road
- Comply with covenants of new financing
- If possible, lock-in prevailing interest rates

### Chatham's Approach

- Explored multiple hedging alternatives including deal-contingent structure
- Explained accounting implications of forward-starting swap in a changing capital structure
- Assessed potential breakage costs of hedge alternatives in the event deal didn't close
- Negotiated trade to embed existing liability into an off-market swap at entity level
- Orchestrated a competitive auction to efficiently execute remaining new hedges

### The Results

- Scenario analysis made clear best strategy: compromise between locking attractive rates and limiting exposure in case deal didn't close
- Acquirer hedged a percentage of total debt prior to closing and modified existing swaps to mirror new capital structure at deal close
- Hedge accounting avoided earnings volatility to comply with covenants and facilitate IPO
- Competitive process saved the acquirer **3 times Chatham's fee**

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## **Case Study C: Hedging for Multinational Company**

### **Situation:**

- Software company with contracts in different geographies, each denominated in the local currency
- Complicated legal structure made it difficult to differentiate between economic and accounting transactions among entities
- Lender demanded that interest payments be tied to a USD index despite the loan being denominated in CAD (the company's reporting currency)

### **Key Management Questions/Goals**

- What is the optimal way to address the mismatch between CAD cash flows and payments based on a USD interest rate index?
- What is the real FX exposure?
- What hedging alternatives are available that fit the company's practical constraints?

### **Chatham's Approach**

- Explained the concept of a quanto swap to address the mismatch between index and currency
- Modeled main cash flows to uncover true FX exposure versus the reporting currency
- Analysis uncovered that once foreign cash flows were netted the real exposure was primarily between USD-CAD
- Although many exotic products could be considered, recommended a vanilla instrument to hedge the primary FX exposure

### **The Results**

- Clear understanding of real exposure led company to tailor approach and select most optimal and efficient instruments for each risk
- CAD interest rate swaps for the senior debt (denominated in CAD) fixed interest rate risk
- Quanto swap for the mezzanine debt (denominated in CAD but based on USD LIBOR) to eliminate index mismatch
- Currency forward contracts hedge the primary FX exposure

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## **Case Study D: Restructuring In a Developed Economy**

### **Situation:**

- Capital re-structuring of a Canadian company
- Due to its massive size, a substantial portion of the debt package was denominated in USD to facilitate market clearing
- Business plan favored a larger percentage of fixed rate debt than lenders could provide

### **Key Management Questions/Goals**

- What is the best way to address the mismatch between cash flows and interest payments?
- What is the optimal way to fix more of the debt at a fair price?
- For a deal of this size, are there any other capital markets risks that should worry the consortium?

### **Chatham's Approach**

- Explained how to synthetically create debt denominated in CAD to eliminate mismatch
- Isolated hedge provider compensation within derivatives pricing structure and pre-negotiated execution levels with bank group as a spread over the inter-bank market
- Quantified proposed bank compensation in USD for consortium to review and approve
- Injected transparency into documentation negotiation by highlighting potentially onerous terms in ISDA Schedule

### **The Results**

- Consortium eliminated cash flow mismatch with a cross-currency swap to convert USD debt to CAD
- Chatham achieved high pricing efficiency during execution despite large transaction size relative to the market - each bp (0.01%) was worth USD 1mm
- Chatham & counsel negotiated out some of the unfavorable ISDA provisions
- Cross-currency swap has kept company debt service stable despite recent CAD depreciation versus USD

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## **Case Study E: Emerging Markets Acquisition**

### **Situation:**

- Company in a competitive bid to acquire a retail store chain in Eastern Europe
- Deal appeared attractive in local currency, but uncertain when translated into USD
- Hedging seemed unattractive because forward rates reflected deep depreciation of the local currency

### **Key Management Questions/Goals**

- What is the most cost-effective way to hedge?
- What are the likely key drivers of the local currency?
- What is the expected maximum exposure if the deal is not hedged?

### **Chatham's Approach**

- Explored hedging structures including forwards, various option structures, and inflation-linked instruments
- Researched the country's macroeconomic data and correlation with currency movements against USD
- Assisted in modeling pro-forma financial statements using real forward rates (i.e. inflation adjusted rates)
- Quantified expected range of terminal value in USD if the acquisition was not hedged

### **The Results**

- Hedging alternatives failed to meet business objectives – the implied cost of hedging would have made the deal unattractive
- Inflation identified as the major threat for that country's economy
- Armed with a quantitative measure of anticipated currency exposure and an understanding of the local economy's key levers, sponsor made an informed and risk-adjusted bid

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## **Case Study F: Entering an Emerging Market**

### **Situation:**

- Company was evaluating entering a developing market in which it had limited experience
- The country does not have a freely convertible currency for repatriation back to USD

### **Key Management Questions/Goals**

- How do we move funds into and out of the country in an efficient manner?
- What type of hedging strategy should we pursue given the nature of our investments and the country itself?
- How will we track & manage all of our currency hedging positions?

### **Chatham's Approach**

- Tapped deep network of market expertise to pin-point currency convertibility issues and determine liquidity constraints on various hedging alternatives
- Provided education on various hedging strategies, taking into consideration country and investment specifics
- Crafted a process wherein Company & Chatham worked closely together to ensure proper management of positions
- Customized website created for tracking and valuation needs

### **The Results**

- Executed over 20 hedging transactions to reduce volatility associated with investments and repatriations
- Employed combination of on-shore and off-shore transactions to achieve optimal pricing
- Company has been able to manage and report on positions without adding incremental staff or systems cost

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