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# Managing Liability Price Risks & Cross Border Payments

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## Capital Markets Update: Themes for 2008



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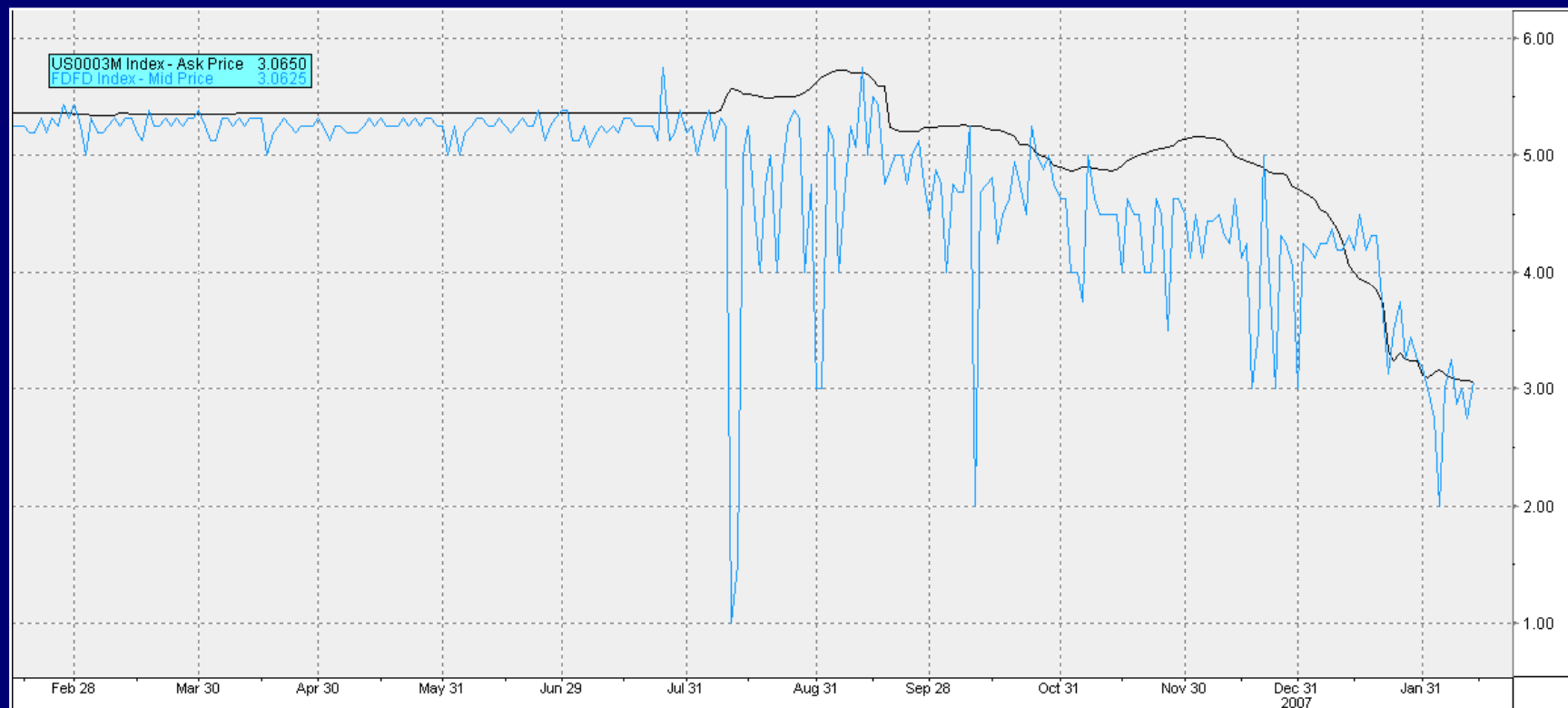


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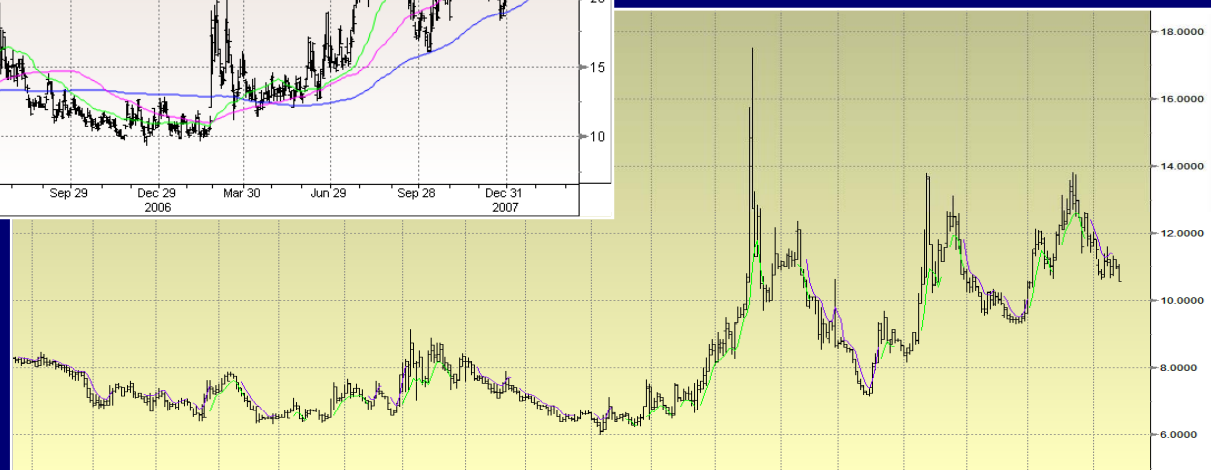
# Liquidity & Funding Concerns

- Market remains over-leveraged
- Derivative 'wrappers' make it hard to identify potential risks
- Are Monoline Insurers the next sub-prime, only larger?
- Libor spread over Fed Funds target remains a risk
- US deficits funded primarily via US fixed income markets



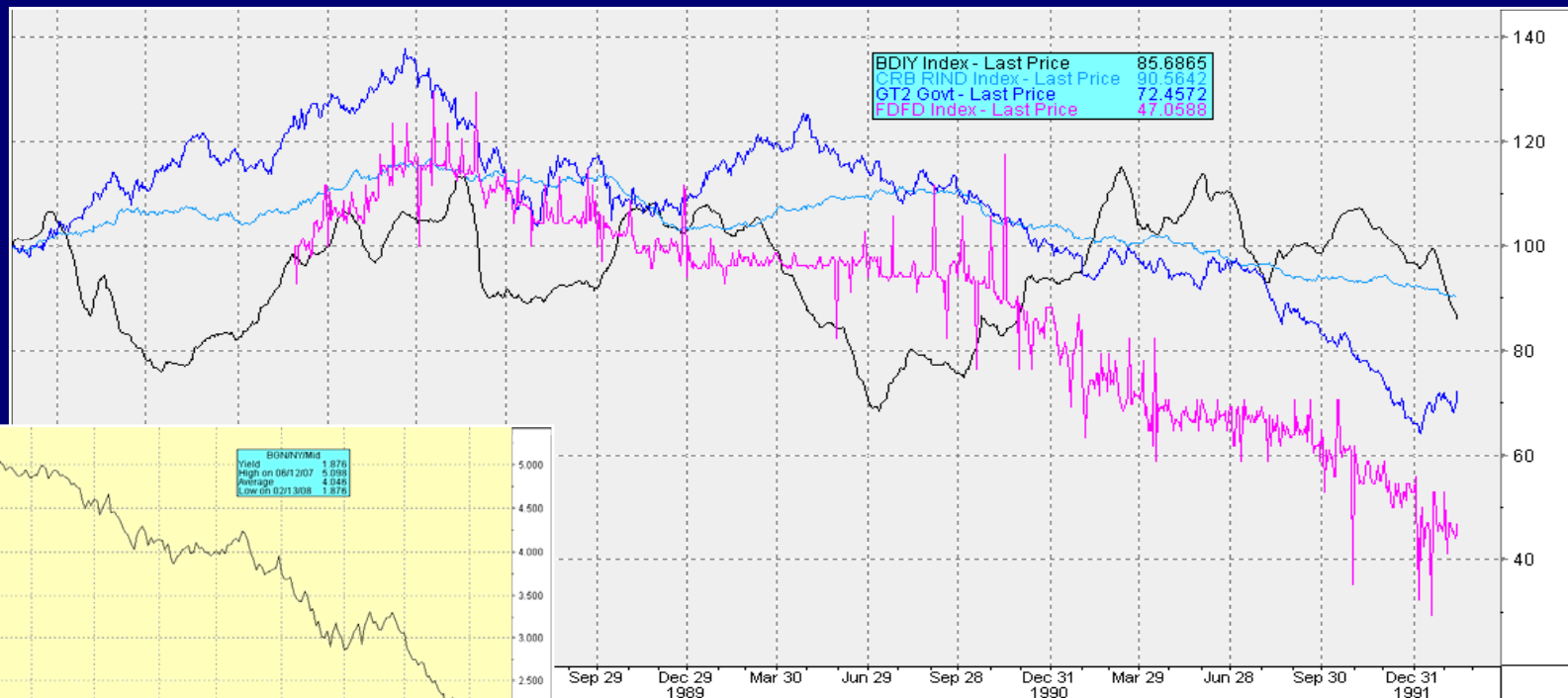
# Increase in Financial Markets Volatility

- The current economic cycle has been founded in (a) abundant liquidity due to historically low global interest rates and (b) the absence of financial market volatility
- This up-tick typically signals an imminent end to the current cycle/trend
- Observed and implied volatility is starting to pick-up across financial markets



# Anticipated Slowdown in Global Growth

- Baltic Freight starting to turn lower
- Aggressive FOMC easing
- Commodity prices remain high
- Global housing markets cooling
- US consumer expected to spend less
- US economic growth expected to be minimal and possibly negative



\*Graph Source: Bloomberg



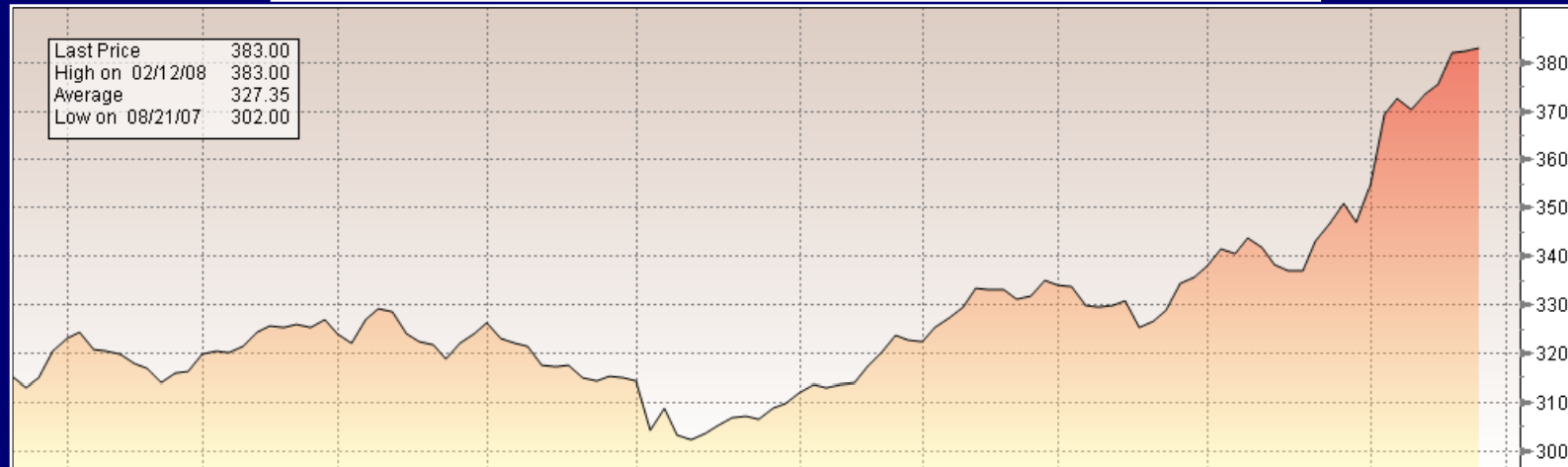
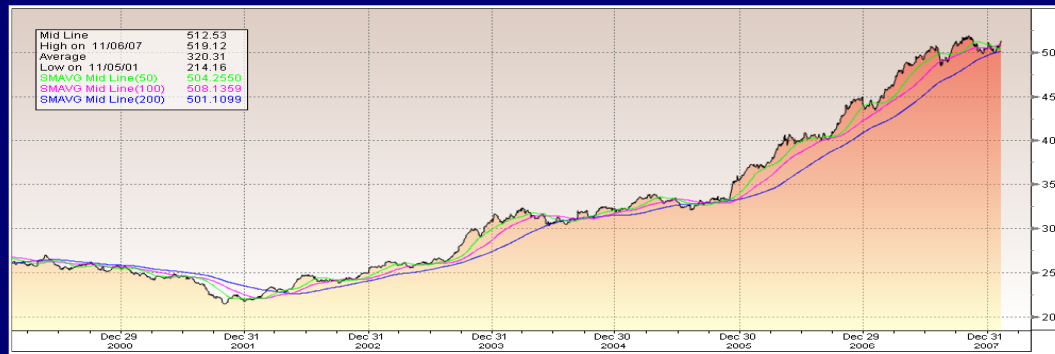
# Global Equity Weakness

- Anticipated slowdown in global growth weighing on stocks
- Significant write-downs in the financial sector
- Remaining uncertainty regarding further write-downs, Monoline Insurers



# Higher Commodity Prices?

- How much will a slowdown in US growth affect global growth, and ultimately, global commodity prices?
- Some argue global growth is less dependent on the US, and that strong EM growth will keep demand for commodities high
- With 10% of the world's population, the US consumes 60-70% of the world's resources



# USD to Remain Under Pressure

- USD remains overvalued and will continue its depreciation against Asian currencies
- Funding concerns, FOMC easing and US deficits will continue to keep the USD down
- USD is close to the bottom of the PPP +/- 20% band against G7 currencies
- Carry, liquidity and equity prices continue to drive price action



## Changes in Hedge Accounting – FAS 133 & 157

- **Upcoming changes in FAS 133 effectiveness testing**
  - Shortcut method for interest rate derivatives will be tougher
  - Potential amendments to DIG Issue G20
- **FAS 157 and fair market valuations for derivatives**
  - Counterparty risk (CDS Spreads have widened)



## Contacts

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## Expansion in Cross Border Payments

- \$35 billion – global estimate of payments related to FX\*
- Cross border payments are estimated to represent approximately 8% of total payments\*\*
- Volume of international trade doubled in 1995-2005 time period\*\*

\* Treasury Strategies, Inc. research

\*\*www.epaynews.com, 2006

# Why are Cross Border Payments Needed?

- **If you have retail customers**
  - Over-the-counter retail FX payments
  - Worker remittance payments
  
- **If you act as a payment agent for the government**
  - Pension disbursements to pensioners living abroad
  - Tax collection and refund payments
  - Government outlays to overseas contractors
  - Scholarships or stipends to students studying abroad
  
- **If you service corporate clients that invest and maintain operations in foreign countries, or import and export goods and services**
  - Vendor or supplier payments
  - Royalty payments
  - International payroll
  - Trade related payments
  - Dividend and interest payments

# FX Payments

**FX payment applications provide the ability to affect cross border payments without having to maintain multiple in-country accounts.**

- Reduce number of local accounts maintained and fund from one or more centralized accounts
- Save costs by consolidating accounts and respective reconciliation efforts
- Automate and streamline payables processes regardless of payment type
- Improve working capital and eliminate FX risks associated with idle balances
- Improve efficiency via streamlined process of FX dealing, settlement and payment
- Enhance current services offered to client base (Financial Institutions)
- FX revenue opportunity to offset diminishing fees and float revenues (Financial Institutions)

# FX Payments – Client Segmentation

- **Large Corporates – Over \$5B in revenue**
  - Separate A/P and treasury departments
  - With MNC's, international subsidiaries initiate payments
  - Moving towards centralized payment and currency management
  
- **Small and Middle Market Corporates - \$10M to \$5B in revenue**
  - May have separate A/P and treasury departments
  - Growing international payment needs
  
- **Financial Institutions**
  - Some have no international branches and presence
  - May have limited or no trading desks and respective nostro account network

## FX Payments – Key Corporate Needs

- Ease of access – single platform, single sign on
- Ease of use – payments initiated from repetitive templates
- Bulk payment upload features
- Leverage investments in back-end systems to achieve STP
- Transaction level reporting to facilitate reconciliation
- Flexibility to centralize or decentralize respective processes
- Visibility and control with regards to FX and payment execution
- Currencies offered and rate types (ex. real time, benchmark and fixed rates)
- Payment types supported (wire, draft, ACH)
- Trade types supported (spot, same / next day and forwards)
- Ability to aggregate multiple payments in one FX contract
- Customer service
- Advisory services

## FX Payments – Key Financial Institution Needs

- Ease of access at branch level
- Flexibility in product attributes
- Potential for white label offering
- Revenue sharing
- Customer service
- Advisory services



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