Par Forward

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

Par forward is an agreement to exchange a series of cash flows over time from one currency to another currency with all exchanges occurring at the same exchange rate. Therefore, a Par Forward is a series of forward contracts with different settlement date (at same interval) and all such contracts having same notional amount and a common exchange rate.

Illustration:
A user may have a series of receipts/payments in foreign currency where INR is domestic currency and user wishes to hedge all these series of receipts/payment at the same rate, user sells/buys Par Forward Contract respectively.

Considering the underlying exposure for the above illustration is USD receivable/payable. User is exposed to the risk of INR appreciation/depreciation against USD resulting in lower INR receipts/higher INR cost respectively and also exposed to currency fluctuation resulting in different exchange rate on different dates of receivable/payable. Par forward will act as a hedge against USDINR spot rate going lower/higher and ensure same exchange rate for all the future receipts/payments which are being hedged through Par forward.

Building Blocks:

The building blocks of this Par forward are as below:

a. Spot Fx rate
b. FX forward premium
c. Time to maturity
d. Discounting curve

Costs and fees, including break-up and details

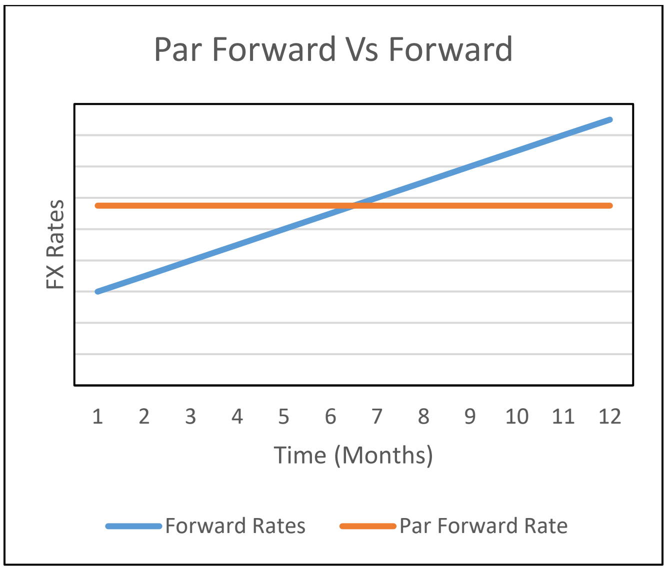
The par forward cost consists of market cost which is determined through a financial model taking above building blocks as input parameters and the price is dependent on Bid/Offer spread of the spot rate, forward rate, discounting curve, along with administrative costs and transaction handling charges.

An illustration of how the product works

User sells USD/INR Par forward contract for each month end maturity for next 12 months.

User will get to exchange the USD receivable on month end dates for the next 12 months at the agreed rate as per par forward contract irrespective of the market rate at the time of conversion.

Pay-off profile:



Impact Analysis

Impact Analysis for first settlement date

Product: Sell USD/INR Par Forward Spot at the time of deal: 74 Maturity - Month end for next 12 months Par Forward Rate - 75			
Spot at Expiry	Sell price if Unhedged	Net Sell Price	Forward Payoff
73	73	75	2
74	74	75	1
75	75	75	0
76	76	75	-1
77	77	75	-2

Benefits

Under this transaction, user will get the benefit of fixing future cash flows and also get the single exchange rate for all maturities. User is hedged against the adverse currency fluctuations in future.

Risks

(1) User is fixing its receivable/payable rate in case of an exporter/importer respectively. Market rates can be better at maturity date (i.e USDINR rate being higher/lower compared to rate at which forward contract was entered into)
(2) 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