Northern Exposure: Hedging In Canada.

We're constantly looking for opportunities to promote our clients' respective businesses by identifying needs and leveraging the many services BOK Financial offers.

To that end, we encourage each team member to have a strong understanding of what other departments do within the bank. By doing so, we work to help our clients generate new streams of revenue and give them the confidence they demand out of a financial partner.

A prime example of this can be found in our relationship with a dynamic energy infrastructure company based in Houston, Texas.

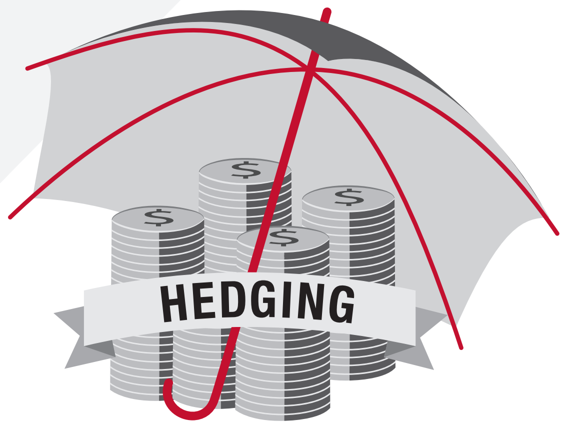
BOK Financial began working with this company in 1996, funding a small-scale rail terminal project. As their business grew, so did our partnership with them. In 2012, they started doing contract work in Canada and we quickly saw an opportunity to help them manage their international currency exposure with our FX services.

See, when it comes to doing business in another country, there are plenty of strategic considerations that must be taken into account. Cultural differences. Legal and regulatory policies. Government permits. Labor laws. The list goes on. However, there's one item in particular that has to hold the coveted top spot of concern; your exposure to fluctuating currency exchange.

In 2013, our client took on an even larger project, designing and building a major rail terminal in Canada. The Canadian receivables were forecasted to be significant once the terminal became operational. Great news from a revenue production point-of-view. However, somewhat concerning from a currency exchange perspective. Would the Canadian Dollar (CAD) maintain its current value, or would it fall and prove detrimental to our client's cash flow when converting to US Dollars (USD) back home?

Our goal was to get a known result by locking in a fixed exchange rate to cover any downside loss should the CAD drop in value. This is called hedging. Not to be confused with a hedge fund.

Hedging is more like insurance against the unknown. By initially securing a fixed rate, you won't be at risk of potentially losing money on future exchanges should the local currency be devalued against the USD.



Understanding that our client was able to forecast their receivables and wished to hedge quarterly, we devised several different strategies to best help protect their revenue's value. Ultimately, we landed on five option structures commonly known as Collars for five different periods. This structure consists to two separate FX options expiring at the same time—a CAD call, the right to buy Canadian Dollars, and a CAD put, the right to sell Canadian Dollars.

Here's how it worked:
Client purchased five separate option structures. The cost for the five option structures was CAD 508,000 or USD 462,280.

Each structure consisted of the client purchasing a CAD/USD put—again, the right to sell CAD at a given rate—at 0.91 and selling a CAD/USD call at 0.93. The puts afforded them the protection against a lower CAD/USD rate. The sale of the calls is a common way to lessen the expense of the structure versus buying straight puts.

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When the options expired there could have been three scenarios:

1— If the CAD went up in value and the market was above 0.93, then BOK Financial would have exercised the right to buy (the client would be selling) at 0.93.

2— If the CAD remained stable and the market was between 0.91 and 0.93, then the option structure would expire worthless and client would have been able to sell at market.

3— If the CAD went down in value (what we were hoping to insure against) and was below 0.91, then the client would exercise the right to sell at 0.91.

So, how did it play out? Over the course of the next five quarters, the CAD lost value against the USD. The client exercised their right to sell at 0.91 instead of selling at market value at that time. In total, our client hedged $37.5 million CAD of exposure.

DEC 31, 2014

Client sold at
0.9100
instead of market
0.8635

a difference of USD
$348,750

MAR 31, 2015

Client sold at
0.9100
instead of market
0.7880

a difference of USD
$915,000

JUNE 30, 2015

Client sold at
0.9100
instead of market
0.8040

a difference of USD
$795,000

SEPT 30, 2015

Client sold at
0.9100
instead of market
0.7500

a difference of USD
$1,200,000

DEC 31, 2015

Client sold at
0.9100
instead of market
0.7240

a difference of USD
$1,395,000

TOTAL PROTECTION
$4,653,750

In summary, by purchasing the five separate options for $462,280 the client was able to insure their USD receivables to the tune of approximately $4.6 million USD by being proactive and employing option strategies to mitigate what would have been an adverse movement in the currency, at the time of conversion.

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