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**Saizeriya and the Use of Foreign  
Currency Coupon Swaps: Was This  
for Hedging or Speculation?**

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# **Saizeriya and the Use of Foreign Currency Coupon Swaps: Was This for Hedging or Speculation?**

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## Case Assumptions:

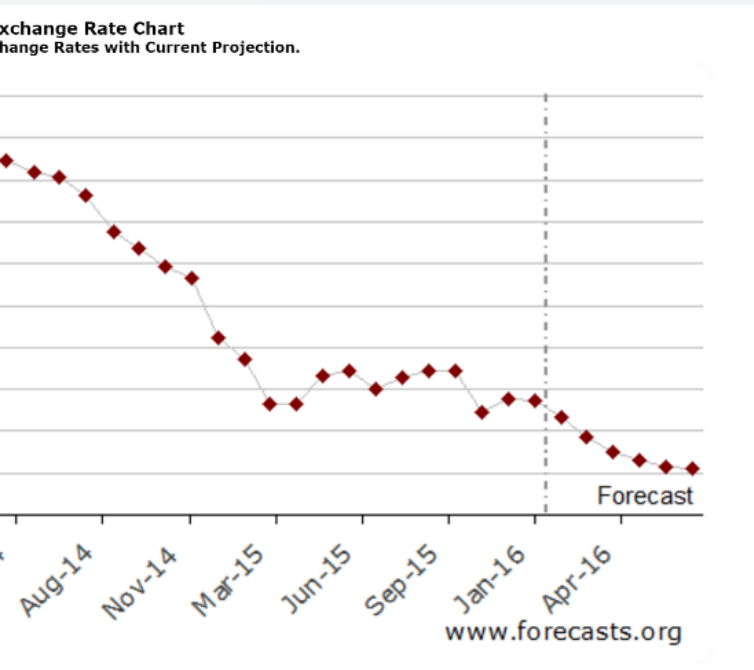
- There is NO budget constraint.
- You are the CFO and you are the rule maker.
- WACC is 12%.
- You utilize the current market rates of interest for borrowing or lending.
- The forecast of the Euro is based on the current economic and financial conditions.
- You have bought 5 Airbus each costing €46MM to be paid entirely in € in 6 months.

Nancy Diaz-Quinones



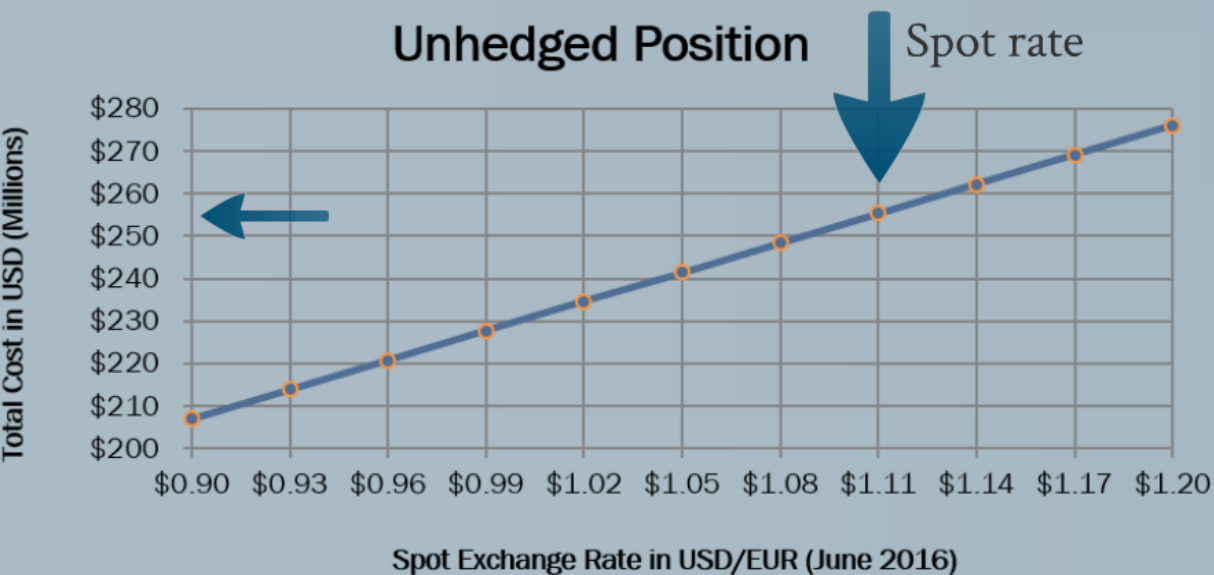
# Current Market Rate Assumptions:

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- Spot Rate: \$1.11/€ (WSJ)
  - Forecast Rate (6 mo): \$1.00/€
  - 6 Mo Forward Rate: \$1.12/€ (Investing.com)
  - Risk Free U.S. Investment Rate: 1.84% (Bloomberg)
  - Risk Free Europe (France 10 year Government bond) Investment Rate: 0.59% (Bloomberg)
  - Commercial Borrowing Rate: 4.56% (LIBOR + inflation + additional risk)
- Vanessa Bryan

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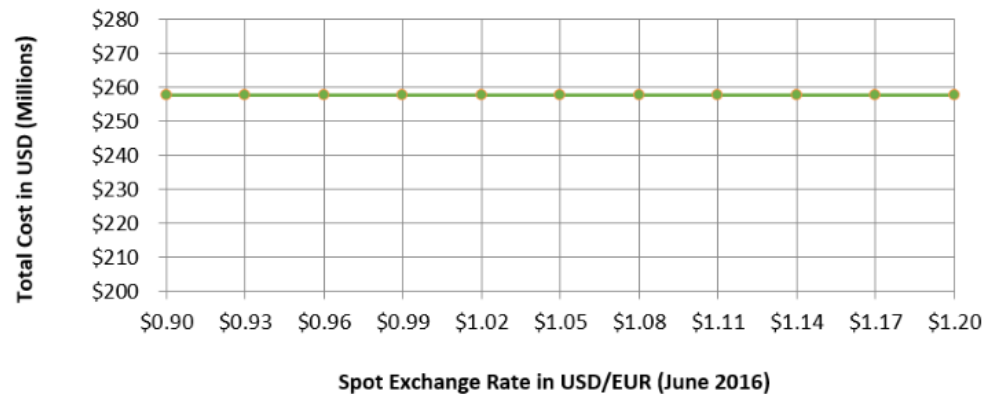


- This strategy is the one with the maximum risk. It represents the greatest potential benefits if the dollar strengthens, and the greatest potential cost if the dollar weakens.
- Many firms consider it to be currency speculation.
- Total cost at Spot Rate: \$255.3MM
- Total Cost at \$1.00/€: \$230MM
- Total Cost at \$1.20/€: \$276MM

Yenny Passanante

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## Full Forward Contract Hedge



A forward hedge involves a forward contract and source of funds to fulfill that contract

It is booked at the spot rate of exchange existing on the booking date

Total Cost at Spot Rate \$255.3

Total Cost at Forward Rate \$257.6

Fully eliminate currency exposure by locking in the exchange rate

The difference is recorded as a foreign exchange loss

Cristobal Lopez

# Forwards VS Futures contracts

## Forwards

- A forward contract is a private transaction (unregulated)
- Forwards are customized to meet the user's special needs
- Forwards have credit risk

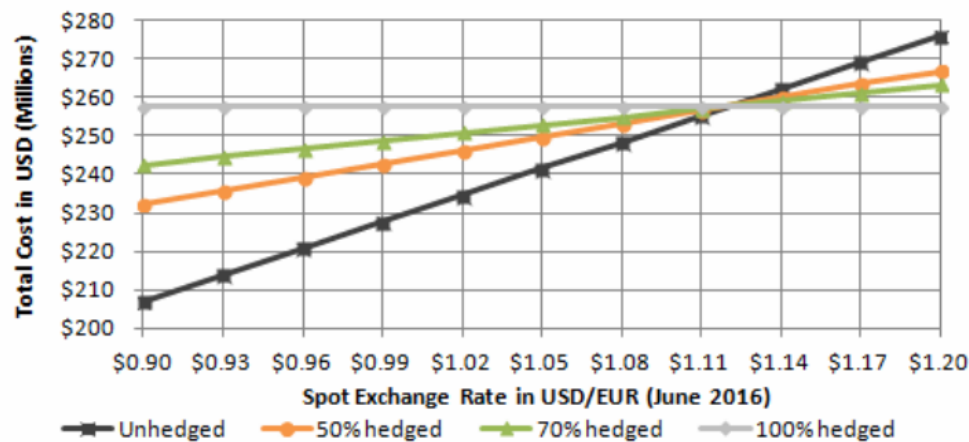
## Futures

- Takes place on an organized exchange where all of the contract's terms and conditions, except price, are formalized
- Prices change daily in the marketplace and are marked to market on a daily basis
- Regulated at the federal government level. The regulation is there to ensure that no manipulation occurs, that trades are reported in a timely manner and that the professionals in the market are qualified and honest.



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### Partial Forward Hedge



Covers only part of the total exposure leaving the remaining exposure uncovered

There are a few objective methods available for determining the proper balance

Total potential exposure is still unlimited although it is highly unlikely to occur.

#### 50%-50% Scenario

Best: \$243.8 million @ \$1.00/€

Worst: \$266.8 million @ \$1.20 /€

#### 70%-30% Scenario

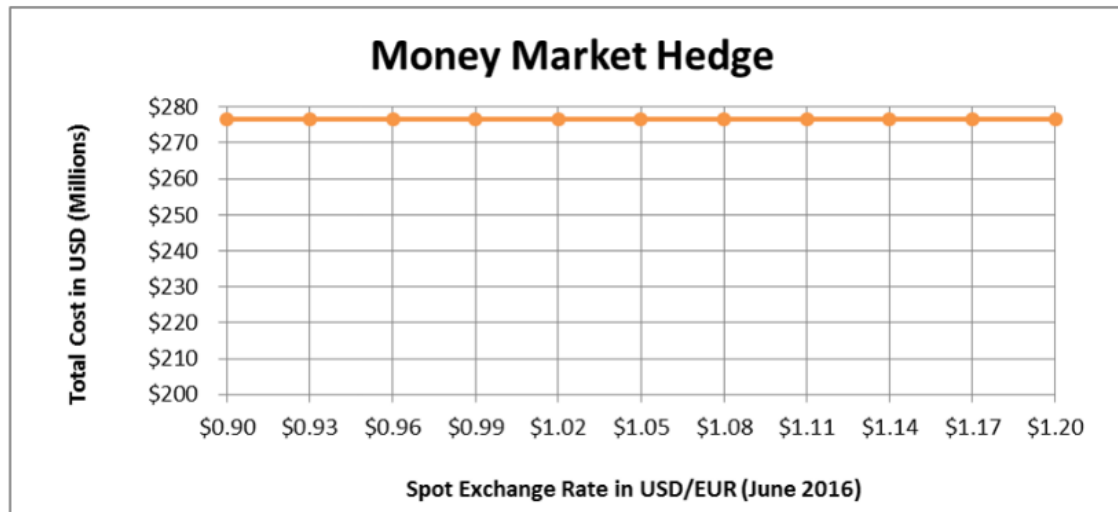
Best: \$249.3 million @ \$1.00 /€

Worst: \$263.1 million @ \$1.20 /€

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## Obtain in dollars now & hold them until payment is due



- Dollar to Euro spot rate= 1.11
- Spirit Airlines will need 257.6 million dollars= 230 million Euros, today to purchase 5 planes
- Each plane will cost 46 million Euros or 51.52 million dollars(what we will pay with)
- Almost as risky at remaining uncovered, specially if the dollar depreciates in 6 months
- (Reason 1) High debt on balance sheet, potentially affects stock value of company
- (Reason 2) Borrowing interest rate makes this option not feasible