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CEO: More demand for interest rate swaps

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PETALING JAYA: There is an increasing demand for interest rate swaps (IRS) from corporate clients given the present low interest rate environment.

According to chief executive officer of Alliance Investment Bank Bhd and head of financial markets of Alliance Bank Malaysia Bhd Sachi Ratnajoothy, IRS appeal to customers that have long-term floating rate loans that are subject to the fluctuations of the benchmark interest rate.

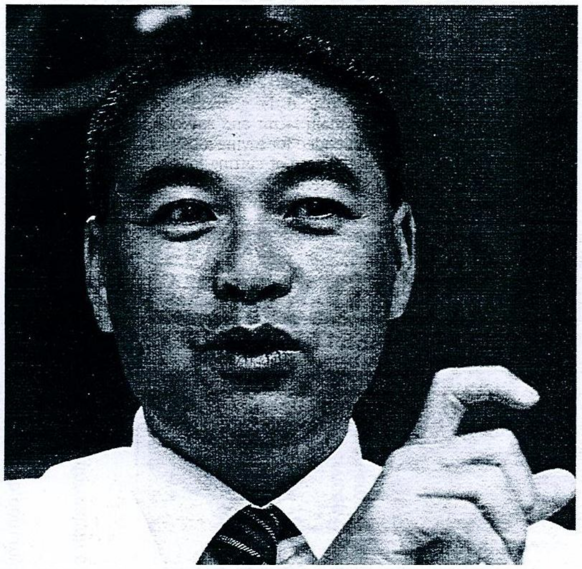
"We have many inquiries on this and the bank is looking to provide them such solutions," she said in an email reply to *StarBiz*.

IRS is essentially a tool for businesses with long-term non-fixed rate loans to transfer the interest rate risk to the financial markets via intermediaries such as banks.

Citi Malaysia head of sales and structuring Angeline Ong said businesses "locked in" or "fixed" their cost of borrowing by undertaking a pay-fixed IRS, which was an alternative to tapping the bond markets or refinancing into fixed rate loans.

"The 'overlaying' of such IRS enables businesses to better manage their liability profiles without altering the underlying loans," Ratnajoothy said, adding that the rising demand was driven by the increasing awareness on the need to mitigate uncertainty related to the cost of financing, which could cripple future cashflows.

Similarly, foreign exchange (forex) hedge is also an instrument that helps to mitigate the impact of the currency market volatility.



Lee Kok Kwan ... By hedging forex risks, businesses and individuals could lock in one's cost

A business owner can hedge his exposure to a foreign currency receivable or payable from the unpredictable swings in the forex markets by entering into a hedge mechanism with a bank to lock in a pre-agreed rate for a future date.

Such forex contracts usually attract companies involved in international trade and require huge amount of foreign currencies for the business.

CIMB Group deputy chief executive officer and treasurer Lee Kok Kwan said without managing forex exposure and locking in forex levels forward, one could not be certain of the actual revenue or costs in ringgit terms until the moment they did the exchange.

By hedging forex risks, businesses and individuals could lock in one's cost or preserve one's margin of future forex receipts or payments in current ringgit terms, he said.

Alliance's Ratnajoothy said forex volatility increased substantially last year due to the subprime crisis. If they were importers, they had to deal with the additional risk of paying too much for raw materials while exporters risked receiving too little in sales proceeds, which both lead to profit margins squeeze, she said.

OCBC Bank (M) Bhd head of treasury Gan Kok Kim said by utilising IRS and forex hedging products, business owners could limit their risk exposure while having the peace of mind to focus on growing the business as those risks were transferred to intermediaries like banks.

Although IRS and forex hedging could become a disadvantage to companies, depending on the direction of the interest rate and currencies, they offered a form of certainty in terms of cash flow management, he said.

Lee of CIMB said every business should identify and quantify such risks and decide how to manage them.

"Companies and individuals should focus on how much losses or reduced revenue they can stomach in ringgit terms from their overseas sales, or escalation in costs from imports, or from rising interest rate cost on floating rate loans," he said.

Not hedging was also a form of speculation and "a bet in itself" because businesses were betting that the forex levels did not move against them before they needed to convert, or that interest rates did not increase during the loan tenure, Lee said.

"It is never a binary decision of either hedging 100% or not at all. Prudence will likely dictate that businesses and individuals should hedge some and it is a question of degree," Lee added.