Report to the
GAVI Alliance Board
16-17 November 2011

Subject:	**GAVI Alliance Currency Hedging Policy**
Report of:	Barry Greene, MD, Finance and Operations
Authored by:	Barry Greene and Fabrice Dutin
Agenda item:	16e
Category:	For Decision
Strategic goal:	Alliance operations

Section A: Overview

1. Purpose of the report

1.1 This paper presents the proposed GAVI policy on currency hedging; no such policy currently exists.

2. Recommendations

2.1 On 28 October 2011, the Audit and Finance Committee recommended to the Board that it approve the Currency Hedging Policy.

3. Executive summary

3.1 GAVI receives contributions and other inflows in a variety of currencies, while its outflows – for programme and business plan expenditures – are incurred mainly in US dollars, with minor components in euros and Swiss francs.

3.2 Arising from these transactions, at any given time GAVI may have future cash flows denominated in various currencies that will be converted to their value in another currency at the time of receipt or disbursement, to meet business needs. Because of foreign exchange rate fluctuations, that value is subject to change over time and this creates the risk of potential reductions in value to GAVI .

3.3 Currency hedging instruments can reduce that risk (usually for up to two years forward) and, by reducing volatility, enhance the reliability of financial forecasts used to inform decision making. The proposed policy specifies paramaters for currency hedging through which GAVI can manage the risk.

3.4 GAVI cannot totally eliminate the risk because its contractually agreed or expected cash flows extend beyond the two year period over which currency hedging is usually feasible. Furthermore, even within a two-year forward period, the expected amounts and timing of cashflows may be subject to change. Accordingly, the Policy does not require that 100% of the exposure to exchange rate fluctuations be hedged. That also allows GAVI limited opportunity to gain or lose from the future evolution of exchange rates.

4. Context

4.1 See Section 3.

5. Next steps

5.1 Should the Board approve the Policy, the Secretariat will proceed with its implementation and commence reporting thereon to the Audit and Finance Committee in 2012.

6. Conclusions

The Audit and Finance Committee and the Secretariat request the Board to consider the Policy for approval.

Section B: Implications

7. Impact on countries

7.1 Provides greater predictability of amounts available for programme funding.

8. Impact on GAVI Stakeholders

8.1 Reduces volatility in the US-dollar valuation of donor contributions in other currencies.

9. Impact on the Business Plan / Budget / Programme Financing

9.1 Provides greater predictability the US-dollar values of non-US dollar elements included in programme funding and budgetary amounts.

10. Risk implications and mitigations

10.1 Reduces GAVI's exposure to the risk of decreases in the value of future net cash inflows due to exchange rate fluctuations and reduces volatility in financial forecasting.

11. Legal or governance implications

11.1 None

12. Consultation

12.1 GAVI Audit and Finance Committee; Secretariat Legal and Investments teams.

13. Gender implications / issues

13.1 None

14. Implications for the Secretariat

Additional activity within the Finance team.

Annex 1

GAVI Alliance Currency Hedging Policy

1. Purpose and scope

1.1 The purpose of this Currency Hedging Policy is to define how the GAVI Alliance ("GAVI") manages the risk to which it is exposed as a result of fluctuations in foreign currency exchange rates.

1.2 GAVI receives contributions and other inflows in a variety of currencies. GAVI's programme expenditures (for vaccine purchases and cash grants) are incurred almost entirely in US dollars, with some in Euros; business plan expenditures (for staff costs, office facilities and other services) are incurred mainly in US dollars and Swiss francs.

1.3 Arising from these transactions, at any given time GAVI may have future cash inflows (e.g. contributions) and outflows (e.g. for vaccine purchases and business plan expenses) denominated in currencies that will be converted to another currency at the time of receipt or disbursement, to meet business needs.

1.4 Because foreign exchange rates fluctuate, the value in a given currency of future cash flows denominated in another currency will vary over time, resulting in increases or decreases in that value, to which GAVI is exposed. These variations may be substantial, especially in periods of high exchange rate volatility.

1.5 Foreign exchange hedging instruments enable reduction of the risk of decreases in the value of future net cash inflows (usually for up to two years forward). This provides greater certainty of the value of future cash flows in the currency to which they will ultimately be converted.

1.6 This Policy defines how GAVI applies currency hedging.

2. Currency hedging goal statement

2.1 GAVI seeks to provide predictability of funding when it supports a country programme. To strengthen this predictability, GAVI shall apply currency hedging to reduce its exposure to potential decreases in the value of future net cash inflows due to exchange rate fluctuations.

3. Exposures to be hedged

3.1 GAVI's exposure to foreign exchange fluctuations shall be evaluated at least once every month by the Senior Treasury Manager. Hedging shall be effected for exposures to be hedged as quickly as is practicable and within one month of the evaluation, having regard to expectations for the near-term evolution of exchange rates. Speculative hedging shall not be undertaken.

3.2 To allow for any uncertainty in the amount of the cash flow expected from a particular transaction (or category of transactions) and also to retain limited opportunity for potential gains (as well as losses) from the evolution of exchange rates, less than 100% of the exposure may be hedged. Natural hedges resulting from the existence of inflows and outflows in the same currency that reduce net exposure shall be taken into account before using hedging instruments.

3.3 Each category of transaction shall be hedged as follows:

(a) Inflows due under contribution agreements: Between 75% and 100% of the exposure arising in the two years following the evaluation, having regard to prior experience and expectations in the conversion of contribution agreements to cash.

(b) Inflows expected from announced pledges: Between 60% and 100% of the exposure arising in the year following the evaluation and between 40% and 100% in the following year, subject to visibility on the amount and timing of inflows and having regard to prior experience and expectations in the conversion of pledges to contribution agreements.

(c) Programme expenditure (non-US dollar): Between 60% and 100% of the exposure arising in the two years following the evaluation, having regarding to the degree of confidence with which the cash flow amounts can be estimated.

(d) Business plan expenditure: Between 60% and 100% of the exposure from expenditure budgeted for the current calendar year, and for the next calendar year once budget estimates have been compiled for that year.

4. Hedging instruments and counterparties

4.1 Hedging instruments: The foreign exchange hedging instruments that are permitted to be used are limited to those specified in Schedule 1, Part A.

4.2 Approved counterparties: GAVI shall use as counterparties to foreign exchange hedging transactions only banks that have a credit rating not less than that specified in Schedule 1, Part B. GAVI's exposure to any one counterparty shall not exceed the amount specified in Schedule 1, Part C.

5. Roles and Responsibilities

5.1 The Senior Treasury Manager is responsible for managing GAVI's exposure to exchange rate fluctuations in accordance with this Policy.

5.2 Any exceptions made to the Policy shall be authorised by the Managing Director – Finance & Operations or the Senior Director – Finance and the justifying rationale shall be documented.

5.3 The Secretariat shall expand its internal control and financial reporting environment to encompass the currency hedging activities.

6. Monitoring and amendment

6.1 The Senior Director – Finance shall monitor the implementation of this Policy and report on the effectiveness of its implementation at least once a year to the Audit and Finance Committee, together with any proposals for revisions to the Policy. The report shall include details of hedge effectiveness, counterparty exposure and any exceptions made to the policy.

6.2 The Audit and Finance Committee is authorised to amend the matters specified in each Part of Schedule 1 and shall recommend to the Board for approval any other amendments it considers appropriate to the Policy, from time-to-time.

Schedule 1

Part A: Permitted hedging instruments
• Foreign exchange forward contracts • Foreign exchange option contracts
Part B: Credit rating of counterparties
• Not less than A+ or A1 as measured by at least two major credit rating agencies
Part C: Maximum exposure to any one counterparty
• US$ 50 million (or equivalent in other currencies)