LKA

TRANSACTIONS & ENGAGEMENTS

Global Infrastructure Fund Risk Management

Developing a multi-currency risk management framework for an international renewable infrastructure investment platform

Independent Treasury, Hedging & Capital Markets Adviser

EXECUTIVE SUMMARY

LKA's principal advised a European-based renewable infrastructure investment manager investing in renewable energy projects across **Africa, Asia and Latin America**.

The investment platform operated across multiple currencies and jurisdictions. Investor capital and distributions were denominated principally in EUR, while underlying investments and project revenues could be denominated in USD, local currency, or local currency indexed to USD or EUR. Investments also progressed through different stages of the project lifecycle, from development and construction through refinancing and eventual exit.

This created financial risks at several levels of the investment structure rather than simply within individual project companies.

THE CHALLENGE

The investment manager required a comprehensive framework for identifying, evaluating and managing **foreign exchange, interest-rate and associated financial risks across a geographically diverse portfolio of infrastructure investments**.

A central issue was determining not simply whether an exposure should be hedged, but **what should be hedged, when, for how long, using which instrument and at what level of the investment structure**.

The underlying markets varied considerably. Some jurisdictions had developed derivative markets, while others offered limited liquidity or relatively short hedge tenors. Long-dated hedging could be available only at a substantial premium, while credit constraints could make conventional long-term FX hedging impractical.

The investment strategy created a further complication. Projects could subsequently refinance or be sold. A hedge designed solely around the contractual maturity of an investment could therefore leave the fund with substantial breakage costs if the underlying investment was refinanced or exited earlier than anticipated.

Liquidity was equally important. Conventional rolling FX forwards could generate collateral requirements and cash drag, potentially affecting fund returns and creating liquidity requirements quite separate from the underlying investment.

LKA PERSPECTIVE

The advisory work developed a practical risk-management methodology linking **hedging strategy to the underlying investment strategy** rather than treating derivatives as standalone financial products.

The framework considered whether exposures were most appropriately managed at **fund, holding-company or individual project level**, taking account of counterparty credit quality, collateral requirements, regulatory and capital-control restrictions, liquidity, operational flexibility and the ability to restructure or terminate hedges following refinancing or disposal.

Particular attention was given to the relationship between **hedge tenor, credit cost and potential breakage exposure**.

Rather than automatically seeking the longest available hedge, alternative approaches included mandatory breaks, sculpting hedge profiles around anticipated refinancing dates, shorter rolling strategies and option-based structures. The framework specifically recognised the ability of options to provide long-term protection while reducing the potentially substantial breakage exposure associated with conventional long-dated forward contracts.

Counterparty strategy was also incorporated into the framework, including the establishment of appropriate derivative facilities, early engagement with potential hedge providers and competitive pricing processes. This was particularly important where local market depth, counterparty appetite or available tenor could materially constrain the theoretical hedging strategy.

A structured pre-investment assessment was developed covering matters including **currency convertibility, capital controls, availability of hard currency, local derivative-market liquidity, interest-rate exposure, security and ranking, counterparty capacity and the ability to transfer funds between different levels of the investment structure.**

Scenario analysis was also developed to assess potential hedge breakage under different exchange-rate, interest-rate, credit and refinancing assumptions, including mandatory breaks and cash flows sculpted around anticipated refinancing.

COMMERCIAL OUTCOME

The work established a structured methodology through which financial risk could be considered **as part of the investment decision itself**, rather than only once an individual project approached financial close.

It provided a consistent framework for evaluating FX and interest-rate exposures across substantially different markets while retaining sufficient flexibility to accommodate the characteristics of individual investments and jurisdictions.

Importantly, the work moved beyond policy development into practical implementation.

The framework subsequently supported the development and implementation of pay-as-you-go FX option structures with tenors extending beyond 20 years, providing long-term currency protection while addressing the credit, liquidity and breakage-cost challenges associated with conventional long-dated FX hedging.

The result was a risk-management approach capable of operating across the full investment lifecycle — **from initial investment assessment and construction through refinancing, long-term ownership and eventual exit.**

About Lionel Kruger & Associates

Lionel Kruger & Associates provides independent treasury, project finance and capital markets advisory services across infrastructure, energy, mining and industrial sectors.

LKA advises sponsors, investors and borrowers independently of financing banks and derivative counterparties, with particular expertise in interest-rate, foreign-exchange and commodity risk management.

Career Note: This engagement was undertaken by Lionel Kruger prior to the establishment of Lionel Kruger & Associates Limited. It forms part of his personal professional advisory track record, which continues through the firm's current infrastructure, treasury and capital markets advisory engagements.