TRANSACTIONS & ENGAGEMENTS

Interest Rate Risk Management

Independent Treasury, Hedging & Capital Markets Adviser

East African Energy Group - USD Interest Rate Hedging

EXECUTIVE SUMMARY

Lionel Kruger & Associates was appointed to advise two operating subsidiaries of a privately owned East African energy group on the interest-rate risk arising from two separate USD 50 million floating-rate facilities, creating an aggregate USD 100 million exposure.

The mandate covered hedge strategy, product selection, market testing, counterparty engagement and execution. The work was undertaken during the rapid tightening of US monetary policy in 2022-23, when the cost of protecting floating-rate USD debt had become a material commercial issue.

Following execution, LKA also supported the group with the associated hedge-accounting work.

COMMERCIAL CONTEXT

The facilities referenced six-month SOFR and exposed the borrowers to the risk of further increases in USD interest rates. Management was apprised of the available hedging alternatives, including swaps, caps and collar structures, and the relative implications of each.

Following this assessment, LKA recommended the use of an interest-rate cap. This would establish a ceiling on borrowing costs while allowing the borrowers to retain the benefit of lower floating rates should the interest-rate cycle reverse.

Access to competitively priced derivatives was a central consideration. Pricing obtained from the domestic market demonstrated a substantial premium for option-based protection. One indication for a 5% SOFR cap was USD 775,000 on a USD 50 million facility.

SCOPE OF ENGAGEMENT

- Assessment of the underlying USD interest-rate exposure
- Analysis of swaps, caps, floors and collars across alternative tenors
- Evaluation of the trade-off between protection, participation and upfront premium
- Structuring of the hedge to reflect the amortising debt profile
- Independent sourcing and comparison of hedge-provider pricing
- Support with counterparty onboarding, negotiation and hedge execution
- Subsequent hedge-accounting support

COMMERCIAL OUTCOME

The recommended strategy used an amortising 5% interest-rate cap referenced to six-month SOFR. This protected the borrowers against further increases above the agreed strike while preserving the economic benefit of lower floating rates below the cap.

Competitive procurement produced pricing from the selected bank of approximately USD 92,000 per USD 50 million facility. This compared with materially higher alternatives available during the process, including the USD 775,000 domestic-market indication noted above.

The mandate therefore demonstrated that hedge-provider selection and market access can be as important as the choice of instrument itself. Independent price discovery materially improved the economics of the risk-management programme without compromising the client's desired protection.

WHY THE ENGAGEMENT MATTERED

For African corporates borrowing in hard currency, the decision is not simply whether to hedge. Counterparty access, product liquidity, credit appetite, documentation and pricing can materially affect the cost and practical availability of protection.

The engagement illustrates LKA's ability to combine treasury strategy with detailed derivatives structuring, competitive execution and post-trade accounting support - providing continuity from the initial risk decision through to implementation.

TRANSACTION SNAPSHOT

- Sector: Energy
- Region: East Africa
- Facilities: Two separate USD 50 million facilities
- Aggregate exposure: USD 100 million
- Reference rate: Six-month SOFR
- Selected protection: 5% amortising interest-rate cap
- Selected-bank indication: approximately USD 92,000 per USD 50 million facility
- Additional scope: Hedge-accounting support

Confidentiality Note: The client and counterparties have been anonymised. Transaction characteristics and pricing are presented to illustrate the nature and outcome of the advisory engagement.