Çakmak Alert | Banking and Finance

EASING OF LIMITATIONS ON FOREIGN CURRENCY DERIVATIVE TRANSACTIONS

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Author: Devrim Ergun

In April, in an attempt to offset the volatility and risk in the global markets triggered by the COVID-19 pandemic, the Turkish Banking Regulatory and Supervision Agency ("BRSA") and the Capital Markets Board of Turkey ("CMB") had tightened their limits on foreign currency swap, forward, option and other derivatives transactions (where the parties swap Turkish Lira and foreign currency) ("FX Derivatives Transactions")[1]. As a step towards normalization, on 25 September 2020, the BRSA relaxed the tightened measures it introduced on local banks ("Banks") in April. As of writing, the CMB has not yet made an announcement on the matter and it is unclear whether similar easing measures will be made available to Capital Markets Institutions (defined below).

For context, the BRSA has maintained a tight policy towards FX Derivatives Transactions following heavy fluctuation in the value of the Turkish Lira in 2018 and has consequently introduced a number of measures restricting Banks engaging in such activity[2] (cumulatively, "BRSA Imposed FX Derivatives Limitations"). With its announcement in April, the CMB began imposing similar restrictions on institutions which are regulated by the CMB[3] ("Capital Markets Institutions") that take part in FX Derivatives Transactions ("CMB Imposed FX Derivatives Limitations" and together with BRSA Imposed FX Derivatives Limitations, "FX Derivatives Limitations").

[1] Please refer to our Alert dated 14 April 2020 available at http://www.cakmak.av.tr/articles/Banking_Finance/41250012.pdf for further details.

[2] BRSA Press Release dated 13 August 2018
BRSA Press Release dated 15 August 2018
BRSA Press Release dated 17 August 2018
BRSA Press Release dated 8 September 2018
BRSA Press Release dated 17 September 2018
BRSA Letter to the Banks Association of Turkey dated 19 September 2018
BRSA Press Release dated 18 December 2019
BRSA Press Release dated 9 February 2020
BRSA Press Release dated 12 April 2020

[3] The Capital Markets Law No. 6362 specifies capital markets institutions as: (i) investment firms, (ii) collective investment schemes, (iii) independent audit firms, appraisal firms and credit rating agencies that are active in the capital markets, (iv) portfolio management companies, (v) mortgage finance institutions, (vi) housing finance and asset finance funds, (vii) asset leasing companies, (viii) central clearing institutions, (ix) central depository institutions, (x) trade repositories and (xi) other capital market institutions falling under the regulation of the CMB.

The most recent changes to the BRSA Imposed FX Derivatives Limitations specify that, for FX Derivatives Transactions between Banks and non-resident counterparties:

(a) if at settlement a Bank receives Turkish Lira, the previously imposed volumetric threshold of 1% of the Bank's regulatory capital, has now been revised as 10%;

(b) if at settlement a Bank provides Turkish Lira; new volumetric thresholds shall be 2% for transactions with seven days remaining until settlement, 5% for transactions with thirty days remaining until settlement and 20% for transactions with one year remaining until settlement, whereas such thresholds had been previously determined as 1%, 2% and 10%, respectively; and

(c) all other previously announced BRSA Imposed FX Derivatives Limitations shall remain unchanged.

Following these developments, the FX Derivatives Limitations can be summarized as follows:

Pursuant to the BRSA Imposed Derivatives Limitations, FX Derivatives Transactions between Banks and non-resident counterparties shall be subject to the following restrictions:

(1) Where at settlement a Bank receives Turkish Lira; the total notional amount of FX Derivatives Transactions may not exceed %**10** of the Bank's most recently calculated regulatory capital (delta values may be taken into consideration for options transactions), and if any excess exists, further such FX Derivatives Transactions may not be executed and any such FX Derivatives transactions may not be renewed;

(2) Where at settlement a Bank provides Turkish Lira; depending on the settlement date of the FX Derivatives Transactions, their total notional amount may not exceed certain ratios based on the Bank's most recently calculated regulatory capital (delta values must be taken into consideration for options transactions) as follows: (i) **2%** for transactions with seven days remaining until settlement, (ii) **5%** for transactions with thirty days remaining until settlement and (iii) **20%** for transactions with one year remaining until settlement. Furthermore, for purposes of the calculation above, the effective date shall be taken into consideration for FX Derivatives Transactions where the effective date is after the transaction date. If any excess exists, further such FX Derivatives Transactions may not be executed within the maturity ranges with limit breaches;

(3) Banks' transactions with their consolidated non-resident credit and financial institution affiliates are exempt from the FX Derivatives Limitations;

(4) The above ratios must be calculated daily, on a solo and consolidated basis; and

(5) Any early settlement or extension of the original maturity date (for whatever reason) of any transaction falling within the scope of the BRSA Imposed FX Derivatives Limitations shall be subject to the prior written consent of the BRSA.

As of writing, the CMB Imposed FX Derivatives Limitations remain unchanged and accordingly, FX Derivatives Transactions between Capital Markets Institutions and non-resident counterparties are subject to the following restrictions:

(6) Where at settlement a Capital Markets Institution receives Turkish Lira; the total notional amount of FX Derivatives Transactions may not exceed 10% of the Capital Markets Institution's capital calculated at the end of the preceding month pursuant to applicable capital adequacy calculation laws, and if any excess exists, further such FX Derivatives Transactions may not be executed and any such FX Derivatives transactions may not be renewed;

(7) Where at settlement a Capital Markets Institution provides Turkish Lira; depending on the settlement date of the FX Derivatives Transactions, their total notional amount may not exceed (on any day) certain ratios based on the Capital Markets Institution's capital (as calculated in (6) above): (i) 2% for transactions with seven days remaining until settlement, (ii) 5% for transactions with thirty days remaining until settlement and (iii) 20% for transactions with one year remaining until settlement;

(8) The above ratios must be calculated on a daily basis; and

(9) Any early settlement or extension of the original maturity date (for whatever reason) of any transaction falling within the scope of the CMB Imposed FX Derivatives Limitations shall be subject to the prior written consent of the CMB.

Çakmak Avukatlık Ortaklığı

Piyade Sokak, No. 18
C Blok, Kat:3, 06550
Çankaya, Ankara - Turkey

T +90 312 442 4680

Zorlu Center, D Lobisi, T3 Katı,
Daire 356, Levazım Mahallesi,
Koru Sokak No:2 34340
Beşiktaş İstanbul - Turkey

T +90 212 939 7560