



Cross-Currency Carry Leakage – Operating Project Debt

SCENARIO TYPE	Project Finance – Operating Phase
ASSET CLASS	Infrastructure / Energy / Transport
RISK FOCUS	Cross-currency basis and carry leakage in long-dated offshore debt
PRIMARY OFFER	Hedge Rebuild™
RELEVANT SERVICES	Hedge Rebuild™ · Synthetic funding optimisation · Cross-currency restructuring · CSA renegotiation

THE SITUATION

The financing made sense at the time. Offshore debt was materially cheaper than domestic funding. Long tenor. Attractive fixed rates. Strong appetite from international lenders looking to deploy capital into stable Australian infrastructure.

EUR, USD, or JPY debt was raised against an asset generating AUD revenues. Currency risk was addressed using long-dated cross-currency swaps arranged at or near financial close. The offshore debt was treated internally as synthetic AUD funding. The economics were assumed to be locked.

The hedge was executed, documented, and put in the drawer.

Years later, the asset is operational. Revenues are stable. Covenants are being met. The financing is no longer front of mind. But the cost of that offshore funding is quietly higher than anyone expected.

HOW THE TRAP FORMS

Cross-currency leakage rarely shows up as a single moment of failure. It starts as background noise.

Interest expense runs a little above model. Treasury attributes it to basis volatility. Asset management assumes it will normalise. Boards focus on operating performance rather than liability mechanics.

FX basis widens and stays wider than expected. Reset timing between debt, swaps, and settlements does not line up cleanly. Margin requirements on long-dated cross-currency swaps become more volatile.

The project is still hedged. FX risk is neutralised in principle. But the all-in AUD cost drifts. What was meant to be cheap offshore funding becomes persistently expensive synthetic AUD debt – and no one is quite sure why.

WHAT TYPICALLY BREAKS

The headline rate was never the real cost

The project approved offshore debt based on nominal coupons. The true cost sits in the cross-currency conversion: interest rate differentials, cross-currency basis, dealer margin, and tenor premium. Those components are opaque at close and very visible later.

Collateral is a silent drain

Long-dated cross-currency swaps generate significant margin volatility. Liquidity that should support operations, distributions, or reserve buffers becomes trapped supporting derivative mechanics under one-sided CSAs.

Tenor mismatch removes flexibility

Projects often lock 15–20 year cross-currency swaps. But assets rarely keep the same debt that long. Refinancing, partial prepayments, and asset sales all become expensive because exiting long-dated swaps crystallises large mark-to-market costs.

Bank solutions preserve bank economics

The default response offered by banks – roll, extend, or replace existing swaps – preserves dealer margin, re-locks funding spreads at current market levels, and fixes accounting optics while worsening underlying economics.

THE STRUCTURAL INSIGHT

The starting point is not how do we hedge FX better. It is: what problem are we actually trying to solve now?

Projects often do not need 15–20 year FX locks. They need controlled exposure over realistic refinancing horizons. Replacing monolithic cross-currency swaps with layered or rolling structures can materially reduce cost without increasing risk.

Vanilla cross-currency swaps bundle together FX conversion, interest rate transformation, and funding intermediation. Unbundling these allows each component to be priced more efficiently – the economic hedge remains, the leakage reduces.

Any redesigned structure should make future refinancing, asset sale, or debt repricing easier. Shorter tenors, cancellable layers, and modular hedging matter more than theoretical neatness.

INTENDED OUTCOMES

- ▶ Carry discipline restored – offshore funding behaves as intended, not as a persistent drag on project economics.
- ▶ Liquidity stability – collateral volatility becomes manageable and predictable rather than episodic and disruptive.
- ▶ Funding cost drivers made explicit rather than buried in swap mechanics – boards and ICs can understand and explain outcomes.
- ▶ Optionality recovered – refinancing, prepayment, or asset sale decisions are no longer hostage to derivative break costs.
- ▶ Governance clarity – the capital structure tells a coherent story that survives scrutiny from lenders, auditors, and future buyers.

WHERE THIS APPLIES

Most relevant where offshore debt was raised for pricing or tenor reasons; long-dated cross-currency swaps were used; refinancing or asset rotation is a realistic future path; and collateral volatility has become noticeable.

Less relevant where debt is short-dated or naturally currency-matched, physical revenues offset foreign currency liabilities, or FX exposure is intentionally retained as part of the investment thesis.

TYPICAL ENGAGEMENT PATH

Hedge Rebuild™ – Cross-currency restructuring and synthetic funding optimisation. Secondary: CSA renegotiation, counterparty consolidation, collateral diagnostic. Scope confirmed following a focused diagnostic review.

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Illustrative scenario based on common operating-phase project finance patterns. Details have been anonymised. Outcomes depend on hedge structure, counterparty documentation, market conditions, and accounting constraints. Not investment advice.
