Information on currency swaps

This fact sheet contains general information on currency swaps traded through Danske Bank.

Currency swaps may be traded in an OTC transaction with Danske Bank as the counterparty.

What are currency swaps?
A swap is an agreement between two parties to swap payments in different currencies.

These are some of the ways a currency swap can used:

- to pay a fixed rate of interest in one currency and receive a fixed rate of interest in another currency;
- to receive a fixed rate of interest in one currency and pay a floating rate of interest in another currency;
- to pay a floating rate of interest in one currency and receive a floating rate of interest in another currency.

The latter type is the most frequently used currency swap and is referred to as a base swap.

In principle, a base swap is embedded in all currency swaps. A currency swap in which Part A e.g. pays a fixed rate of interest in DKK and receives a floating rate of interest in USD consists of:

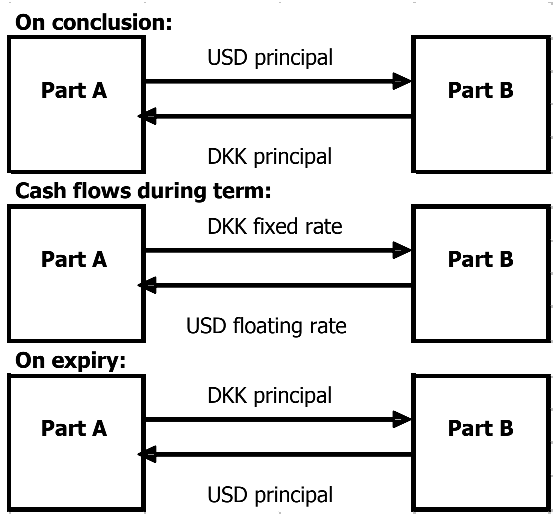
- an interest rate swap in DKK in which the fixed-rate payment is offset by the floating-rate payment;
- a base swap in DKK/USD in which the floating-rate payment in one currency is offset by the floating-rate payment in another currency.

See the fact sheet on interest rate swaps for more information.

On the conclusion of a currency swap, the amount of the principal (notional amount) is determined on the basis of the exchange rate of the relevant currencies at the date the swap transaction is set up. The notional amounts are exchanged initially and finally at the effective date and the termination date respectively. The notional amounts will then be used to calculate interest rate payments throughout the term of the swap.

When entering into an agreement to trade a currency swap, you determine the effective date, the termination date, the principal, including any repayment profile, and the payment frequency of interest payments.

The fixed rate of a currency swap reflects the market rate for the selected term while the floating rate is determined relative to a reference rate at a given date (interest-reset date). Interest payments may be agreed that do not correspond to the interest rate level at the time the transaction is set up. This would then be offset by an upfront payment at the time the transaction is set up. The party in whose favour the rates have been fixed will pay the upfront amount to the other party.



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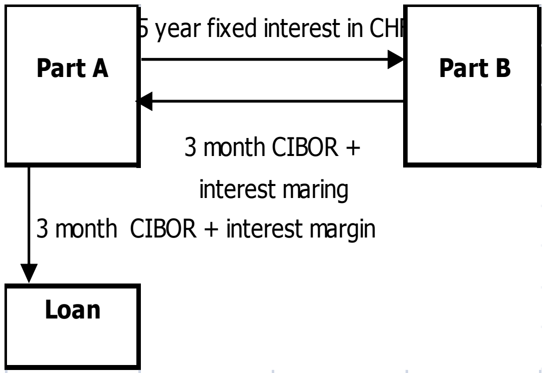
Using currency swaps
Here is an example of how currency swaps can be used.

Converting loans into another currency
A cross currency swap can be used to convert a loan into another currency. That way, physical debt rescheduling can be avoided.

In the example, Part A has raised a loan with a maturity of five years. The interest rate is floating and fixed every three months. Part A has an single interest payment every three months equal to the CIBOR rate plus a loan margin.



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When entering into the currency swap, Part A and Part B agree that Part A will pay a fixed quarterly interest rate in CHF for five years to Part B. By way of consideration, Part B pays the CIBOR rate plus a loan margin. On entering into the currency swap, Part A has refinanced the floating-rate payment obligation in DKK into a fixed-rate payment obligation in CHF.

On the effective date of the currency swap, Part A will receive the agreed principal in CHF and pay the principal in DKK to Part B, on the basis of the prevailing CHF/DKK exchange rate at the date the swap is set up.

If Part A does not wish to receive the notional amount in CHF, the amount will be exchanged into DKK on behalf of Part A, who will subsequently pay the sum to Part B. The currency exchange will be effected at the bank's ordinary exchange rate for buying and selling plus a client margin.

A flexible instrument

A currency swap may be adjusted to suit individual needs. Examples of parameters that can be agreed at the establishment of the transaction include:

- the day-count convention for the fixed interest rate;
  The day-count convention determines the payment resulting from the price fixed by the parties. In other words, there is a difference between calculating the payment on the basis of a 360-day interest year and calculating it using the actual number of days in the calendar year.

- the frequency for determining the floating rate and whether interest should be paid in advance or in arrears;

- the frequency for payment of the fixed and the floating rate;

- the settlement profile.
  This may be a so-called bullet profile, for which the notional amount is not written down during the term of the transaction. An

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alternative is a serial profile, for which the principal is written down by equal amounts during the term. However, the settlement profile may also be fixed individually.

Pricing currency swaps

The basic principle of determining the price of currency swaps is that the values of the two cash flows should be identical so that the transaction has no market value when it is entered into.

If one of the cash flows of the currency swap relates to a floating rate, the floating rate during the term is of course unknown. However, using the structure of the yield curve at the time the transaction is set up, you can estimate how the floating rate will develop.

If one of the cash flows of the currency swap relates to a fixed rate, the fixed rate will reflect the market rate for the selected term.

After the floating and fixed rates have been fixed, a client margin is added to the transaction, which results in a negative market value at the time the transaction is entered into, corresponding to the present value of the client margin during the entire term of the transaction.

Term

The term of a currency swap varies from one currency to another, but is typically up to 30 years.

If a transaction is terminated prior its scheduled maturity, the market value may be negative. The party to whom the transaction has a negative market value must compensate the other party by an amount equal to the absolute value of the negative market value.

Risk factors

Under the executive order on risk-labelling of investment products, this product type is in the "RED" category.
The "Red" category consists of: "Investment products involving a risk of losing more than the amount invested, or product types which are difficult to understand".

The risk-labelling categories defined by the Danish Financial Supervisory Authority ("DFSA") can be found at www.danskebank.dk/risikomaerkning [(in Danish only)].
The risk-labelling system should not form the exclusive decision-making basis of an investment. It is only intended as a supplement to the information you should obtain before making an investment or to the advice you receive from the bank after defining your investment profile.

The risk of a cross currency swap relates to the future development in short and long-term interest rates and exchange-rate fluctuations between the two currencies.
The greatest risk for a payer of fixed interest in a currency swap is a general decline in short and long-term interest rates, which would increase the present value of the future payment obligation. The opposite applies when interest rates go up.

In the example where Part A enters into a currency swap to reschedule a floating-rate

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payment obligation in DKK to a fixed-rate payment obligation in CHF the risk relates to CHF appreciating by a wider margin than DKK. The greatest risk to Part A, however, is a combination of falling CHF interest rates and that the exchange rate of CHF appreciates by a wider margin than DKK.

Collateral
When you enter into transactions with Danske Bank as the counterparty, we may require that you provide collateral.

Special market conditions
Under special market conditions, it may be difficult or impossible to close a position; for example if, during periods of frequent price fluctuations, prices rise or fall to such an extent that we are unable to provide a price.

Tax
The tax treatment of gains or losses on currency swaps depends on whether you are a private individual or a company.

Due to the complex nature of this area, we recommend that you consult an accountant or other professional adviser to clarify the tax and accounting consequences to you of engaging in such trading.

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