FTA
FINANCE & TREASURY ASSOCIATION

XVA

ISSUE SNAPSHOT

RELATED TERMS

CVA: CREDIT VALUE ADJUSTMENT
DVA: DEBT VALUE ADJUSTMENT
FVA: FUNDING VALUE ADJUSTMENT
KVA: CAPITAL VALUE ADJUSTMENT
COLVA: COLATERALISATION VALUE ADJUSTMENT
MVA: MARGIN VALUE ADJUSTMENT
CSA: CREDIT SUPPORT ANNEXURE

WHAT IS XVA?

XVA stands for "X-Value Adjustment" and is an umbrella term for different valuation adjustments to derivative contracts. Banks' balance sheets have been impacted by these adjustments to fair value measurement and pricing in their trading books.

WHY IS XVA IMPORTANT FOR TREASURERS?

XVA impacts the pricing Banks are willing to give corporates on derivative contracts as trading desks are now having these charges levied on the positions that are created when dealing with corporates.

WILL THIS HAVE A POSITIVE OR NEGATIVE IMPACT?

On balance, XVA will increase the cost of executing derivatives. Longer dated, more volatile derivatives such as Cross Currency Swaps will attract larger XVA charges. Presently, the application of XVA differs by bank in Australia and competitive pressures are also limiting the impact in some instances.

Calculating the impact is very complex, as the adjustments are calculated on a portfolio basis. The tenor, instruments, and extent to which your existing portfolio with any one counterparty is in- or out-of-the-money will impact on the mathematical calculation of the XVA adjustments for an incremental trade.

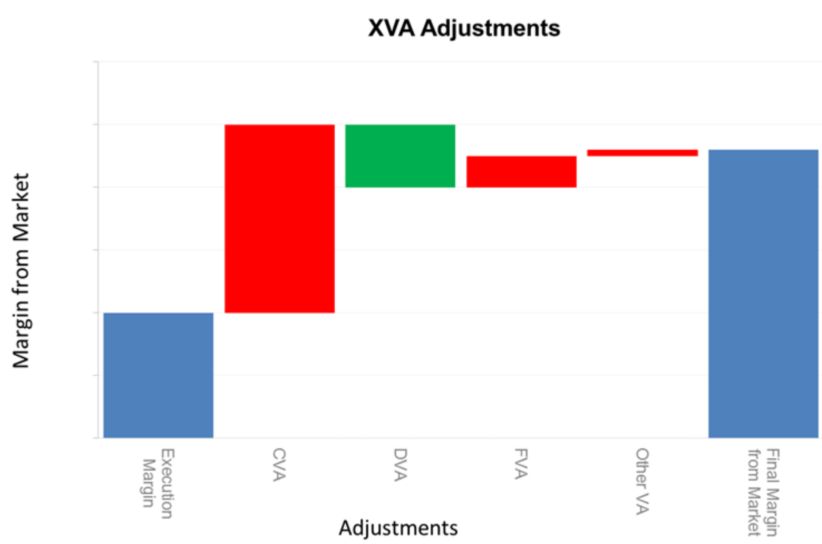
HOW CAN THE IMPACT BE REDUCED?

By executing Credit Support Annexures (CSA) to your ISDAs, you will be able to negate much of the impact of the XVA component exposures.

WHEN DID THIS BECOME AN ISSUE?

The Global Financial Crisis was instrumental to the development of thinking around the true cost of holding derivatives. Corporate and bank defaults, coupled with corresponding market-driven increased bank funding costs were a significant contributor to the development of the relevant methodologies. Furthermore, regulators requiring banks to hold more capital following the GFC has also evolved thinking as both the cost and the volume of capital required to be held has increased throughout the banking system.

IFRS 13 Fair Value Measurement introduced the requirement to measure amd report both CVA and DVA where applicable, which are two components of XVA.



Copyright © 2017 The Finance & Treasury Association Limited | ABN: 70 006 509 655