A

s you may know, various foreign timeshare and fractional resorts with domestically based management companies collect funds annually from their members, usually during the months of December through February.

In most instances, the majority of the resorts’ expenses are paid in foreign currencies, while virtually 100 percent of the revenue is received in dollars. In Mexico for instance, if the peso strengthens against the dollar, it could cause the resort to exceed its operating budget, which is not a good thing in today’s fragile economy—possibly causing a dues increase or special assessment.

Over the years, many resorts have been fortunate that the peso or other currencies have been weak against the dollar, so the budgeting process has not been seriously impacted. Now, however, with increased global volatility and debt problems in Greece, Italy, and Spain, the movements of the dollar in the world markets—and against the Mexican peso in particular—are different. Therefore, resorts may want to consider engaging in proactive risk mitigation such as entering into foreign exchange (F/X) hedge contracts.¹

The end results are to “hedge” against any possible losses due to volatility in the markets and help protect the corpus of funds for their sole purpose—to prudently operate the resort for the entire year.

The Business Scenario
Here’s an example. At one resort, when the annual maintenance fees are received, the funds are turned over to our advisory group for investment in a series of laddered, FDIC-insured CDs that we place with banks around the country. CDs are scheduled to mature serially, in line with anticipated expenses for operating (monthly) and reserves (in concert with an exclusive “Needs-Based Analysis” and review of the reserve study). [NOTE: CDs referred to herein are specifically delineated as the resorts operating funds. Its reserve funds, which are also invested with The March Group in CDs and other relatively safe vehicles, are not part of this discussion.]

The members’ funds flow into Wells Fargo Advisors through a liquid FDIC Insured “Operating Account” maintained at Wells Fargo Advisors, and maturing proceeds of the CDs come back into that same account for disbursement, either via ACH, On-Line BillPay, or printed checks. In the past, many resorts would transfer funds as needed to their foreign destination (i.e., Mexico), in dollars for conversion to a foreign currency (i.e. pesos). This was time-consuming, expensive, and fraught with potential problems and risks.

The FX hedging program involves the resort entering into a series of foreign exchange hedge contracts, in which Wells Fargo Bank, at the direction of The March Group, delivers foreign currency to your corresponding foreign bank. At a certain future date, the funds from the proceeds of maturing CDs will be transferred from the Wells Fargo Advisors Operating Account to Wells Fargo Bank, the purpose of which is to service/pay for the FX contracts.

Second, some principles and assumptions:
1. Each December, the resort enters into a series of 12 monthly FX hedge contracts that mature serially from January through December. The maturities of the FX contracts and the CDs coincide and lock in an exchange rate.
2. In many resorts, the Board of Director’s fiduciary responsibility to its members requires that all bank CDs or other investments be considered safe, or insured by the FDIC.
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3. The amount of each monthly contract is typically based on the total operating expenses for the year divided by twelve.

4. Wells Fargo Bank requires collateral in the form of cash and/or pledged CDs which are held in a separate account at The March Group in a total amount not less than the exposure represented by the market risk of outstanding FX contracts. The pledged CDs are liquidated as the FX contracts come due and as exposure reduces, Wells Fargo Bank can release any excess collateral back to the operating account.

5. Some resorts also have U.S.-based expenses for which they will need to use some dollar funds. The resort is free to withdraw funds from the Wells Fargo Bank Direct Deposit Account and non-pledged CDs. This provides the operating flexibility it needs.

Finally, a hedge can be structured to place a ceiling on the resort’s cost of acquiring the needed foreign currency, while leaving open the opportunity to share in the portion of a favorable exchange rate move.

You can also see that as we can set the maturity dates of each contract to coincide with the maturity of the corresponding CD, we have a series of appropriate investments and a virtual self-liquidating system, which is what we seek to do.

If there are excess dollars available each month, these funds would be used to pay the resort’s dollar expenses and/or be reinvested, just as they are now.

I believe this is a unique, innovative, simple, and cost effective solution—as well as a proactive way to help resorts and associations “cover their assets.”

Endnote

1. Futures trading, which is speculative and volatile and involves a high degree of risk, is only appropriate for the risk capital portion of a portfolio. Foreign exchange trading is not suitable for all clients.

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