

Currency risk and the strong franc

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Currency management is one of the most important tasks of a Basel treasury. Roche reports its results in Swiss francs, Novartis in US dollars, while a large share of their revenues is earned in US dollars, euros, Japanese yen and emerging market currencies. Since a significant part of the costs of both groups is incurred in francs, a strengthening of the franc compresses margins, and for Roche it also reduces reported revenues and profits. The groups hedge their transactional exposures to a certain extent, usually with forward contracts and options for periods of a few months, but they do not attempt to hedge the long-term translation exposure that results from converting foreign earnings into the reporting currency. In their reporting, they present growth rates at constant exchange rates in addition to growth rates in francs.¹

The strength of the franc has been a recurring theme of Swiss economic history, which Part D, Chapter II has traced for the chemical industry. In the period after the financial crisis of 2008, the franc appreciated strongly as investors sought a safe haven. On 6 September 2011 the Swiss National Bank introduced a minimum exchange rate of CHF 1.20 per euro, which it defended through large foreign exchange purchases. On 15 January 2015, the National Bank abandoned the floor without warning, causing the franc to appreciate by about 20 per cent against the euro within minutes before settling at a somewhat lower level.²

For the pharmaceutical groups, the removal of the floor had immediate effects on reported results and margins, since the franc value of foreign sales fell while Swiss costs remained unchanged. The companies had not hedged against such a sudden change and had little reason to do so, because the National Bank had repeatedly declared its commitment to the floor. Their operating businesses nevertheless proved resilient, since a large share of their costs was also incurred abroad. Research and production in Basel became more expensive in international comparison, a fact that fed

into the long-term decisions on the location of activities. Several companies in Switzerland, including the pharmaceutical groups, reviewed their cost bases in the following years.³

1 Notes

1. On the currency exposures of Roche and Novartis, their hedging policies and the presentation of growth rates at constant exchange rates, see the financial risk management sections and the financial reviews in the annual reports of both groups. To be verified. ↩
2. On the minimum exchange rate of CHF 1.20 per euro introduced by the Swiss National Bank on 6 September 2011 and abandoned on 15 January 2015, see the press releases of the Swiss National Bank and its annual reports 2011 and 2015. On the earlier history of franc management, see Part D, Chapter II. To be verified. ↩
3. On the effects of the removal of the minimum exchange rate on the reported results and cost structures of Roche and Novartis, see their annual reports 2015 and 2016 and the analyses of the Swiss National Bank and of economic research institutes. To be verified. ↩

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