Transforming Brocade’s FX Hedging Program

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Brocade Business Background

• Brocade is the leader in data center fabric networking solutions

• Founded in 1995 / IPO in 1999 / NASDAQ: BRCD

• The Company is headquartered in San Jose, CA and operates worldwide with 4,200 employees generating $2.2 billion in revenue

• Operating expenses at international subsidiaries create most of the Company’s foreign currency exposures

• All worldwide treasury activities are centralized and managed out of the headquarters in San Jose, CA
Transforming Treasury

• Why transforming?
  ➢ Vision
    ➢ Value
    ➢ Insight
  ➢ Current state and course of business not aligned to Vision
    ➢ Clear definition of end-state and key attributes
    ➢ Roadmap
  ➢ Talent Management
    ➢ Develop
    ➢ Retain and attract talent

• How to transform?
  ➢ Connect
    ➢ Internal
    ➢ External
  ➢ Execution Roadmap
    ➢ Basics under control
    ➢ Step-by-step
  ➢ Benchmarking and best practices
Transforming Foreign Currency Hedging
Applying Transformation Principles to FX Hedging

- Vision
  - Value
    - Manage vs. transact
    - Full end-to-end ownership and control
    - Delivery measured by metrics
    - Drive changes
  - Insight
    - Full visibility on currency exposures and income statement impact
    - Alternative evaluations
    - Management reporting vs. reporting numbers
    - Strategic and business intimacy
Brocade FX Risk Management
Before transformation

Past
- Lack of Treasury leadership in guiding corporate FX hedging activities
- Lack of visibility on FX exposures, in addition sub-optimal hedging programs
- System limitations related to processing FX transactions and hedging activities
- FX hedging activities were isolated from rest of the business, and lacked of management support

Basic Hedging program to minimize FX fluctuation
Brocade FX Risk Management
After transformation

- Full control on FX rates and clear Treasury leadership in all FX hedging activities
- Clear visibility on FX exposures and variances, excellent variance reporting, and optimal hedging programs
- ERP System enabled for FX transactions and systematic processes
- Cross-functional coordination and executive support on hedge programs

Optimal FX risk management to minimize earnings impact
Brocade FX Risk Management
FX Hedging Transformation Roadmap

- Stagnant Hedging
- Full Control on FX Rates
- Full visibility
- System Strategy
- Dynamic hedging
- Optimal Hedging
Brocade FX Risk Management
FX Hedging Transformation Roadmap

Stagnant Hedging

Full Control on FX Rates

Full visibility

System Strategy

Dynamic hedging

Optimal Hedging
Brocade FX Risk Management
Full Control on FX Rates for Planning and Quoting

Challenge
• Lack of visibility and control on FX quotes / transactions
• No control on FX plan / forecast rates
• Lack of efficient hedging performance measurement reporting

Solution
• Treasury set quarterly quote rates and monthly accounting rates
• Treasury set annual plan rates
• Constant dollar FX variance reporting

Execution
• Treasury loads quarterly rates into Oracle and Sharepoint
• Treasury aligns hedging activities to planning cycle
• Use plan rates as benchmark for variance analysis

Benefits
• Full control on FX transactions rates
• Full control on FX planning / forecast rates
• Benchmark enabled for transparency
Brocade FX Risk Management

Re-engineered FX business controls and processes

**Past**

- **Financial Planning**
  - Oracle
    - Monthly rates
  - Oanda.com
  - Wall Street Journal
  - Bank websites
  - Customer decides
  - Other sources
  - Manual download
  - Email requests
  - Manual upload/download

- **Sales force**
  - BMI
    - Multi-currency Pricing table
    - Manual upload/download
    - Monthly feed
  - Oracle
    - Treasury via Bloomberg

**Now**

- **BMI**
  - Sales force
    - Quarterly feed
- **Oracle**
  - Treasury via Bloomberg
  - Monthly feed
  - Annual reset
  - Financial Planning
  - Past
- **Hyperion**
  - Treasury - Sole source and full control on all FX rates

**AFP® Annual Conference**

11/5/2013
Brocade FX Risk Management
Alignment of hedging to planning

Past

Now

Hedging coincides with FP&A Annual Planning cycle

AFP® Annual Conference

11/5/2013
Brocade FX Risk Management
New programs to enable foreign currency businesses

Challenge
- System limitations
- Manual workarounds for transacting in foreign currencies

Solution
- Enable FX quoting functionality in the systems
- Revamp processes
- Setup polices
- Lend expertise and guidance to sales and deals desk.

Execution
- Create new FX approval processes
- Treasury involved in order approval
- Treasury sets quarterly rates

Benefits
- Executive support
- Automated approach
- Scalable processes
- Cross-functional coordination
Brocade FX Risk Management
Established automated and structured FX business cycle

FX Management

- Sales Engagement
  - Sales Training
  - Engagement Rules
- FP&A Analyses
  - $ based margin analyses
- Revenue Accounting
  - $ analyses
- Collection
  - Currency bank a/c
- Invoicing
  - FC invoicing
- PO/Order Admin
  - Automatic validation
- Quote
  - Automatic from BMI
- Opportunity Mgmt
  - SFDC - $ based
- Pricing
  - Quarterly Currency Rates
- Discount / Deal Desk
  - $ based process
- Credit
  - $ Based process
- Support
  - Training
- Hedge Analysis
- FX Forecasts
- FX Rates
- FX settlement
- Re-class FX hedge
- Approval

Association for Financial Professionals
Annual Conference

11/5/2013
Brocade FX Risk Management
FX Hedging Transformation Roadmap

- **Stagnant Hedging**
- **Full Control on FX Rates**
- **Full visibility**
- **System Strategy**
- **Dynamic hedging**
- **Optimal Hedging**
Brocade FX Risk Management
Full visibility on BS and IS FX exposure

**Challenge**
- Significant Income Statement Volatility
- No accurate forecast and always surprises
- No active management of exposures

**Solution**
- Efficient FX variance reconciliation
- Rigid exposure reporting & natural hedge mechanism
- FX transaction and reporting rules
- Move hedge gain/loss into the operating line

**Execution**
- Created Full FX variance analysis and recon process
- Align FX invoicing to FX settlement timing to minimize FX variance
- Implemented system to enable more accurate Hedge accounting and reporting.

**Benefits**
- Full visibility on FX variances
- Reduce millions of dollars of income statement impact
- Reduce BS FX volatility and forecast variance
- Better align Hedge g/l to business exposure
Brocade FX Risk Management
Streamlined exposure reporting and management processes

<table>
<thead>
<tr>
<th>Key Stakeholder</th>
<th>Monthly</th>
<th>Quarterly</th>
<th>Annually</th>
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<tbody>
<tr>
<td>FX Risk Committee</td>
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<td>Hedging proposal &amp; KPI</td>
<td>FX Hedging Strategy and Policy Update</td>
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<td>BS Exposure Reporting &amp; hedging recommendation</td>
<td>CF Exposure reporting &amp; hedging recommendation</td>
<td>FX strategy Proposal</td>
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<td>FX variance forecast (m2 &amp; m3)</td>
<td>Variance analysis in Close binder review</td>
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<td>Hedge Accounting &amp; FX Risk/Hedge Disclosure</td>
<td>Annual FAS52 review</td>
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<td>Tax</td>
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<td>Manual Tax reserve table in Foreign Currency. Hedging memo and FX breakdown</td>
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<td>GL Accounting</td>
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<td>Revaluation GL account list update</td>
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<td>Order Management</td>
<td>FX rates update</td>
<td>FX rate update and BMI FX quote report</td>
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<td>International Controllership</td>
<td>Hedging Progress bill settlements &amp; recording</td>
<td>IC policy governed settlements</td>
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Brocade FX Risk Management
Full visibility on FX exposures and variances

Actual FX Gain / (Loss)  
July 2013

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<tr>
<th>Currency</th>
<th>Interco</th>
<th>Cash</th>
<th>Receivables</th>
<th>Payables</th>
<th>Accrued Tax</th>
<th>VAT</th>
<th>Tax Reserve (Manual)</th>
<th>VAT Adjustment</th>
<th>Grand Total</th>
<th>Total European Exposure</th>
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<td>275,701</td>
<td>287,434</td>
<td>(5,902)</td>
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<td>CAD</td>
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<td>82,983</td>
<td>(878,420)</td>
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<td>27,269</td>
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<td>CNY</td>
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<td>CZK</td>
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<td>97,747</td>
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<td>DKK</td>
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<td>JPY</td>
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<td>354,043</td>
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<td>675</td>
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<td>MXN</td>
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<td>16,951</td>
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<td>7,948</td>
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<td>SAR</td>
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<td>(55,917)</td>
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<tr>
<td>SEK</td>
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<td>(9,003)</td>
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<td>TWD</td>
<td>20,522,992</td>
<td>1,947,065</td>
<td>(16,447,372)</td>
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<td>(1,302,689)</td>
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</tr>
</tbody>
</table>

De-emphasize high balance but less volatile currencies
Brocade FX Risk Management
Reduced FX income statement impact

Reduced FX Gain/(Loss) / PL volatility

Program formalized

Foreign currency Gain/(Loss) '000's


(8,000) (6,000) (4,000) (2,000) - 2,000 4,000 6,000 8,000
Brocade FX Risk Management
FX Hedging Transformation Roadmap

- Stagnant Hedging
- Full Control on FX Rates
- Full visibility
- System Strategy
- Dynamic hedging
- Optimal Hedging
Brocade FX Risk Management
System Implementation

**Challenge**
- Sparse systems and manual processes
- Time consuming processes related to hedge trading, settlement, reporting and auditing

**Solution**
- Automate FX rates feed to Oracle
- Automate FX processes from trading & settlement, to hedge accounting and reporting

**Execution**
- Automate FX rates feed using Bloomberg FX data license
- Implement FXall for trading & settlement
- Implement Reval for hedge docs, MTM & reporting

**Results**
- Streamlined processes
- Time reduction in MTM valuations and journal entries
- Reduction in audit time and efforts
Brocade FX Risk Management
System Strategy

- **Oracle / Hyperion**
  - FX rates fed from Bloomberg
  - Automatic FX business quote and approval
  - FX Exposure / Variance analysis reports

- **FXall**
  - Multi-bank pricing on spot, forwards and options
  - Template based batch trading
  - Automatic settlement and reporting

- **Reval**
  - Post-trade activities including hedge documentation, MTM valuation, hedge effectiveness testing, hedge accounting and reporting
  - Risk management
    - Exposure capture with multi-level structure
    - Stress-testing
    - Scenario analysis
    - Hypothetical strategy
Brocade FX Systems

Brocade FX Exposure System
Balance Sheet and Cash Flow Hedging

<table>
<thead>
<tr>
<th>FX Rate Feed</th>
<th>Bloomberg Data License FX Rates</th>
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</thead>
<tbody>
<tr>
<td>Exposure Resource</td>
<td>Oracle FX Trail Balance Cash/Tax/Interco/AR/AP</td>
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<tr>
<td>Exposure Resource</td>
<td>VAT Recon</td>
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<tr>
<td>Exposure Resource</td>
<td>Tax Fin 48 Recon</td>
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<tr>
<td>Business Object / Hyperion Actual Opex in FX</td>
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<tr>
<td>Treasury Balance Sheet Exposure / Variance Tracking</td>
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<tr>
<td>Treasury Cash Flow Forecast / Variance Tracking</td>
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<tr>
<td>Trading</td>
<td>FXAll Trading and Settlement</td>
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<tr>
<td>Post-trade</td>
<td>Reval Risk Management / Hedge Accounting</td>
</tr>
</tbody>
</table>

Note: Brocade has 45 legal entities - by policy all international subsidiaries are local currency functional except Swiss and Luxembourg holding entities. All Interco transactions are in their local currency except India and China. Therefore most of FX exposures are with Swiss and very small percent is with US for legacy FX exposures via acquisitions.

Legend:
- FX system
- Manual
- Excel
- ERP System

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Brocade FX Risk Management

FX Hedging Transformation Roadmap

Stagnant Hedging

Full Control on FX Rates

Full visibility

System Strategy

Dynamic hedging

Optimal Hedging
Brocade FX Risk Management
Dynamic Hedging

Challenge
• Stagnant hedging program
• No express views on the FX market fluctuations
• Inflexible hedging strategies resulting in FX losses

Solution
• Evaluation of tools & assessment on market trends
• Ensure hedge accounting qualification
• Implement Option strategy for CHF, EUR & JPY
• Dynamic hedging

Execution
• Scenario testing in Bloomberg and Reval
• Present PL analysis to executives
• Propose low budget / risk strategy
• Track performance against benchmark

Benefits
• Additional $2M net benefits realized by buying options instead of forwards
• Seize profit opportunities under risk management guideline
Brocade FX Risk Management

Dynamic hedging

- Various strategies based on analysis on currency characters
  - INR NDF forward rates advantage
  - CHF overbought in 2011
  - JPY overbought in 2012
  - EUR fluctuations in 2013
- Alternative strategies using Options
  - Pass hedge accounting test by running hypothetical portfolio in Reval
  - Gain FX Risk Committee support with profit / loss analysis
- Repositioned certain hedge positions
  - Sell and Buy at different levels on EUR fluctuations
  - Enter into forwards at more favorable levels, and de-designate option hedges
- Recommend flexible hedging ratios and time horizons
- Benchmark with banks and peers
Brocade FX Risk Management
FX Hedging Transformation Roadmap

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