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An Empirical Study on the Various Risks in Foreign Exchange Market and its Impact in Global Business Transactions

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ABSTRACT
Today's business world is growing rapidly at a faster pace. After the emergence of globalization the business market is become global and the business transactions have become more complicated. Numerous traders, different countries, varied currencies, unique products, innovations etc. have become a vital source for the emergence of foreign exchange market to be more popular in the recent trends. The ICT (Information, Communication and Technology) Revolution has motivated a wide number of traders across the globe to do business globally. There is no business without risks. In finance we term risk with investment as 'higher the risk, higher the return'. And hence it has become necessary to deeply analyze any new business proposals before investing in it. Since 2014 with the exception of 2017, India's economy has been the world's fastest growing major economy, surpassing China. Hence many countries across the globe are being attracted by India and FDI's have increased in the recent years. Many new business ventures have increased and hence the role of risk in business is become very crucial and important element for every international trader involved in business transactions across various countries. Here the author in this paper has tried to bring the outcome of various risks associated in international business transactions and how it affects the foreign and domestic companies in business. Indian currency value fluctuates everyday with the change in the macro economic factors. All business dealings in India are focused in order to appreciate the value of INR in comparison to other currencies. Central bank of every country monitors this function in every country.

KEYWORDS: *international trade, exposure, foreign currencies, globalization, forex market, exchange rate*

1. INTRODUCTION
The foreign exchange market (Forex, FX, or currency market) is a global decentralized or over-the-counter (OTC) market where the trading of currencies takes place. Forex market has the ultimate power to determine the foreign exchange rates for every currency. It includes all aspects of buying, selling and exchanging currencies at current or decided prices. It is termed as an OTC market because unlike Stock market there is no central association or authority to decide the terms and conditions involved in trading of currencies. Due to decentralized market the traders face high risk in their foreign business transactions. Forex market is the biggest market in the world and it functions 24/7 due to its massive business transactions in currencies.

2. Participants in the Forex market
The main participants in the forex market are as follows;

- **Commercial Banks**:

The main participant in the foreign exchange market are the huge Commercial banks who act as a core player in the market. The commercial banks connect the international banks to help in the cash flows from one country to another.

- **Foreign Exchange Brokers**:

These brokers' on-behalf of the traders undertake the activity of buying and selling of currencies. They work for a commission.

- **Central banks**:

The Central Banks play a vital role in the Forex market. Reserve Bank of India is the central bank in India. Central Banks are government agencies and they function on their national currencies in order to maintain a healthy economic atmosphere, balance exports and imports, prevent inflation, and stimulate growth in their economies. Central banks play a very crucial role and they are important players in the forex market. Central banks are responsible for forex rate fixing. Central banks tries to stabilize and increase the demand of their nation's currency and they take many actions to accomplish this tasks.

- **MNCs**:

The Multinational Corporations play a key role in the development of an economy and for attracting new investments in foreign currencies. They help a developing host country by rising investment, income and employment in its economy. They contribute to the faster process of growth and development of the nation through transfer of technology, finance and modern management.

- **Individuals and Small Businesses**:

The small traders also build high business transactions in a country. These businesses do trading in bulk of small/cheaper products but at the same time they contribute a major income for an economy's growth and development. Small businesses also make use of forex market to aid execution of commercial or investment transactions. The foreign wants of these small business players are usually tiny and they account for only a fraction of all foreign exchange transactions. Though they are very important participants in the market. Some of these participants use the market to hedge currency risk. Hedgers normally use various techniques to cover their risk in currency fluctuations. For instance, importers and exporters occupied in foreign trade may have open positions in numerous foreign currencies. They may therefore get affected if there is a variation in the value of foreign currency. As a result, to safeguard themselves against these losses, hedgers undertake opposite positions in the market. Therefore if there is an adverse fluctuation in their original position, it is offset or compensated by an opposite movement in their hedged positions. Their profits and losses and therefore equalized and hence they get stability in the operations of their business.

- **Role of speculators in forex market**:

The retail market involves transactions made by smaller speculators and investors. Speculators are a group of traders who have no genuine requirement or need of any foreign currency. They only undertake the trading activity with a hope of making a small profit from it. The number of speculators rises a lot when the market sentiment is very high and every trader seems to be earning money in the Forex markets. Speculators usually do not have open positions in any currency for a very longer period. Their positions are for a short term and are only meant to make a short term profit. These transactions are carried out by the forex brokers who act as a mediator between the retail market and the interbank market. They mainly operate through forex platforms that offer tight spreads, spot execution and highly leveraged margin accounts.

3. Types of Forex exposure

The foreign exchange transactions are a bundle of varied currencies and hence the amount of risk involved in the transactions is very high. Hence it becomes necessary for every trader to understand the various risks associated in forex market that may affect their business transactions massively. The major three types of forex exposure are as follows;

a. Transaction exposure
b. Operating exposure
c. Translation exposure

A. Transaction Exposure

Definition: The Transaction Exposure is a one type of foreign exchange risk involved in the international trade which involves cross-currency transactions (multiple currencies). In other words, a risk that is faced by the company while doing business in international trade, the currency exchange rates may fluctuate before making the final settlement, and this is termed as a transaction exposure.

For example, If an Indian exporter has the receivable of \$5,00,00, due five months. Here in this case if the dollar value depreciates relative to the rupee, then the exporter will suffer the cash loss. But in the case of a payable of the same amount, the exporter gains if the dollar depreciates (decreases) relative to the rupee.

Thus, once the cross-currency contract has been agreed upon by the firms located in two different countries in two different currencies for the specific amount of goods and money, the contract value may vary with the fluctuations in the foreign exchange rates. This risk of fluctuation in the exchange currency rates is called the transaction exposure. The higher the time gap between the contract and the final settlement, the greater is the risk involved with the change in the foreign exchange rates. However, the companies could safeguard themselves against the transaction exposure through hedging techniques.

B. Operating Exposure

Definition: The Operating Exposure refers to the extent to which the firm's future cash flows get affected due to the alteration in the foreign exchange rates along with the price fluctuations. In other words, a risk that firm's revenue will be severely affected due to the substantial change in the exchange rate and the inflation rate is called as operating exposure.

Operating Exposure, like transaction exposure, also includes the actual or potential gain or loss, but the transaction exposure is specific in nature and deals with a particular transaction of the firm, while the operating exposure deals with certain macro level exposure whereas not only the firm under concern gets affected but rather the whole industry and the economy observes the change with the variation in the exchange rates and the inflation rate. Therefore the operating exposure affects the entire economy and is exposed to the foreign exchange risk.

Operating exposure is much broader as compared to transaction exposure. And in general it relates to the entire investment of the firm and if the exchange rate gets altered the overall value of the firm gets affected. The firm's value is constituted of the operating cash flows and the total assets the firm possesses.

C. Translation Exposure

Definition: The Translation Exposure or Accounting Exposure is the risk of loss experienced when stock, revenue, assets or liabilities denominated in foreign currency varies with the movement of the foreign exchange rates.

In other words, the translation exposure starts from the requirement and need of converting the subsidiary's assets and liabilities (operating in another country) denominated in foreign currency in the home currency of the parent company, at the time of arranging the consolidated profit and loss statement and the balance sheet. Thus, any modification in the foreign exchange rate will have a considerable impact on the financial statements.

If there is any alter made in the exchange rate over the previous accounting period, then the translation of the items denominated in the foreign currency will result in foreign exchange profits or losses, except if there is a tax implication on these items. The translation exposure is concerned with the accounted profits and the balance sheet values and it does not influence the overall value of the firm. Since the profits or losses suffered due to the translation of financial items has no big impact on the stock prices of the firm.

4. Conclusion

The global market today has motivated every trader doing business domestically to engage in international trade. Not all traders are educated and aware of the foreign transactions risks and hence many businesses face huge losses and are not traced anymore in the market. The era of globalization has brought immense contributions to our economy's growth and development. India is still developing and today we are become more competent to sustain in this global market against many developed nations like USA, Germany, and Russia etc. Thus the study can be concluded by saying that international business transactions on the whole sculpts a nation in a better way and enhances the standard of living of the people as a whole and hence the international traders much be well educated regarding the various business exposure or risks so as to sustain in the long-run.

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