



Currency risk management in your business

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Agenda

Relevance of currency risk

Types and cases

Risk management approach

Q&A

What is currency risk?

Currency risk = Exchange rate risk =
= Foreign exchange risk = FX risk = FX exposure



A potential loss arising from an unexpected change in the price of one currency in relation to another.

Scope: currency risk is widespread

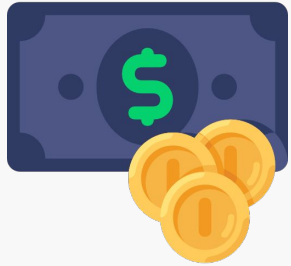


Foreign sales by S&P 500 companies were 43.2% in 2016.



57% of total Lithuanian import & export (€26.7 bn) was conducted with non-eurozone countries in 2016.

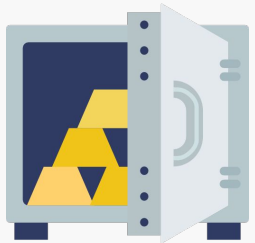
Impact: things happen in the market



2017: EUR/USD **+14%** throughout the year.



2016: GBP/EUR **-11%** in 2 weeks in 2016 after Brexit referendum.



2015: EUR/CHF **-16%** in 1 day after Swiss National Bank decision.

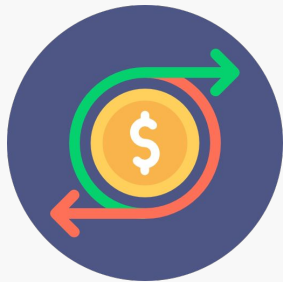
Scope **×** impact **=** relevance

Types of FX risk



(today's topic)

Transactional



Translational



Economic



Source: [International Monetary Fund](#)

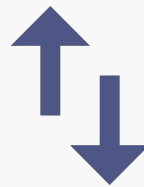
Transactional risk: common cases



Importers that need to pay suppliers in foreign currencies



Exporters that sell their products in foreign currencies



Combination of the above

Approach

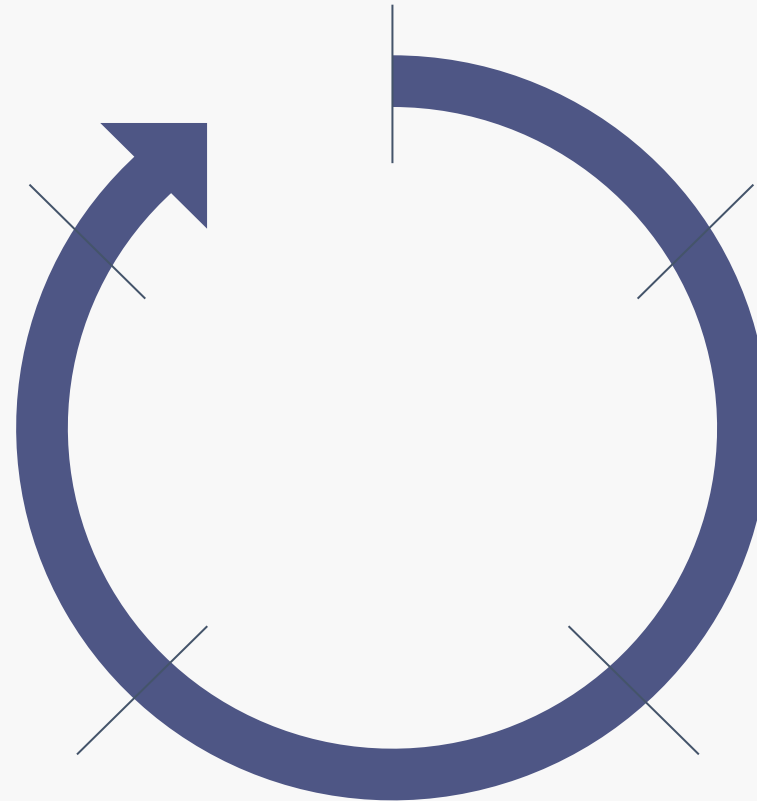
1. Quantify exposures

2. Assess your risk tolerance

3. Evaluate options

4. Develop a strategy

5. Implement your plan



1. Quantify exposures



Key is to understand where exposures arise.

Take into account everything that is not denominated in your base currency.

How do you know you have covered everything?

- Sometimes you don't...

Common items

 Inflows	Outflows 
Sales	Purchase of raw materials
Dividends	Purchase of equipment
Disposals	Business trip expenses
	Marketing & IT costs
	Acquisitions

2. Assess your risk tolerance

Plug the numbers into a simplified profit & loss statement:

P&L statement (forecast)	
Sales	1,000,000
Cost of sales	700,000
Expenses	200,000
P&L	100,000

FX exposure
500,000
0
0

-1%	-5%	-10%
995,000	975,000	950,000
700,000	700,000	700,000
200,000	200,000	200,000
95,000	75,000	50,000
-5%	-25%	-50%

When would it start hurting?

3. Evaluate options

Available risk management strategies:

1. Convert at spot rates (“do nothing”)
2. Pass on the risk to the other party
3. Internal matching of costs and revenues
4. Hedging with derivatives (e.g. forward contracts)

Case study: BMW



Challenge

- BWM, headquartered in Germany, sold only ~20% of cars in its home market.
- Negative effect from currencies over 5 years was €2.4 bn.
- Retail price increases were ruled out.



Solution

- Use a “natural hedge” by:
 - Moving production facilities (to China, India, Mexico, US).
 - Purchasing more in its main markets.
- Use financial hedges for the remaining exposures.

4. Develop a strategy

1

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2

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3

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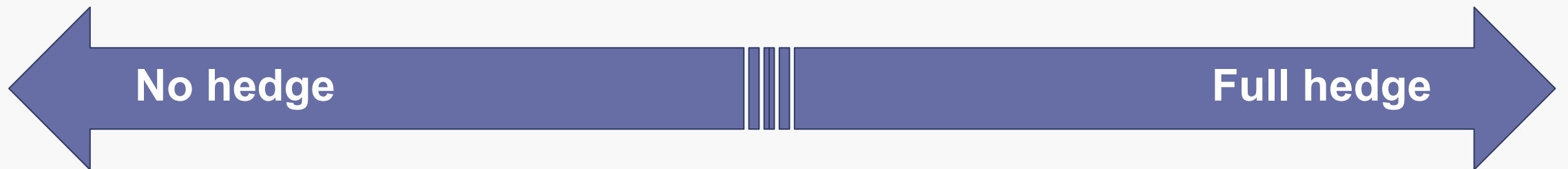
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Objectives

Priorities

Thresholds

Responsibilities



Case study: Apple Inc.



Net Sales by Operating Segment:	2017
Americas	\$ 96,600
Europe	54,938
Greater China	44,764
Japan	17,733
Rest of Asia Pacific	15,199
Total net sales	<u>\$ 229,234</u>

“The Company is a net receiver of currencies other than the U.S. dollar. Accordingly, changes in exchange rates, and in particular a strengthening of the U.S. dollar, will negatively affect the Company’s net sales and gross margins.”

“The Company uses derivative instruments, such as foreign currency forward and option contracts, to hedge certain exposures to fluctuations in foreign currency exchange rates.”

Source: [SEC](#)

Top mistakes by companies

- ① Downplaying exposures
- ② Maintaining the status quo “because we have always done it this way”
- ③ Taking a view on the direction of currencies
- ④ Lack of alignment between finance and senior management

“ The one unchangeable certainty is that
nothing is certain or unchangeable ”



J.F. Kennedy



Contacts

Get in touch if and when you need assistance or advice



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