

HEDGING OF CURRENCY RISKS OF NON-FINANCIAL ORGANIZATIONS

IRYNA STROHANAVA, LUDMILA STEFANOVICH
Polotsk State University, Belarus

The article discusses the essence of the hedging method, its role in the management of foreign exchange risks of exporters (importers), provides theoretical definitions of hedging instruments and the hedging process.

Task formulation. In the context of the deepening process of internationalization of the world economy and the transition to globalization of the world economy, the problems of professional risk management and operational accounting of risk factors are of paramount importance for financial market participants.

Among the risks that have the most devastating impact on the financial performance of a country's economy, it is necessary to highlight currency risks associated with changes in exchange rates.

The volatility of the foreign exchange market has a negative impact on the activities of enterprises participating in foreign economic activity, reduces the financial result of their work in the event of adverse changes in the exchange rate.

Currency risk is a probabilistic category. In some cases it is not possible to forecast and predict the trend of the foreign exchange rate for a long period. The exchange rate dynamics is influenced by many different factors - from the decisions of Central banks to the behavior of prices in world commodity markets.

The result of an effective currency risk management is the reduction of losses due to changes in world currency rates, the reduction in the uncertainty of future financial flows, ensuring more efficient financial management and reducing profit fluctuations.

Solving the problem of minimizing the currency risks of non-financial organizations predetermines the need to solve the following tasks:

1) to review existing approaches and principles of currency risk management by non-financial organizations;

2) to expand the use of currency risk hedging instruments in an expanding financial market.

Main body. Hedging in the world practice has long been used to optimize currency risks, the number and variety of methods and tools with which hedging is performed [3, 5].

Derivatives market in its present form began to develop actively with the emergence of the need for hedging floating exchange rates introduced at the Jamaican currency conference in 1976. Before the principles of the Jamaican monetary system were proclaimed, exchange rates were fixed, implying no currency risk in international economic relations [1].

In turn, the need for hedging foreign exchange risk was the reason for the active development of derivative instruments in the foreign exchange market, which led to the spread of hedging techniques and speculative operations with derivative financial instruments (hereinafter DFIs).

We will investigate the essence, mechanism, strategies and instruments of hedging foreign exchange risks on the basis of foreign experience [5, 6].

Hedging transactions (hedging) are forward transactions closed in order to prevent possible losses as a result of changes in prices and rates of commodity, currency, stock and exchange markets. They are closed not for speculative purposes, but in order to minimize the risk.

We emphasize that the hedging operation involves making two transactions. One transaction is a common forward transaction and the subject of the economy assumes the obligation to perform some actions in the future at a fixed price in the present. The other is a transaction with DFIs, by means of which an economic entity protects itself from adverse price (exchange rate) changes of the financial asset, with respect to which it assumed forward liabilities. In addition, it should be noted that for market participants price (exchange) risks are important not only for the concluded forward transactions, in which they are obliged to perform future actions for the purchase/sale of the asset. Price (exchange rate) risks are a significant factor for them in planning future actions. In this case, through the conclusion of a transaction with a derivative instrument, the producer or consumer of the goods is able to fix an acceptable level of future price of the goods, thereby protecting their plans from the risk of price (exchange) changes.

On the other hand, the hedging operation does not always imply the compulsory and simultaneous conclusion of both transactions: a forward transaction with a commodity subject to currency risk and a derivative transaction for the future delivery of that commodity.

Therefore, we can state that the derivative instruments, in addition to their stated above main purpose to fix the future price, there is one more additional purpose - to hedge an unfavorable development of the price situation (exchange rate volatility) in the derivatives market.

An important point here is that the presence in the economy of the futures market (the market of the basic DFI asset) and the derivatives market of the DFI, absolutely different from the point of view of their functioning mechanisms, leads to the emergence of a hedging phenomenon, in the course of which the results of two transactions - a forward transaction with the underlying asset and transactions with DFI are balanced.

The economic concept of hedging is the process of concluding new transactions and establishing relations between transactions to ensure the necessary netting aimed at reducing financial (currency) risk. The hedging operation is to find a quantitative relationship between the changes in the prices of the hedged asset in its two different markets: primary and secondary. This relationship has an objective economic character, because in different markets of the same asset, price changes are on average closely related.

The main difference between hedging and other types of transactions is that its purpose is not to gain an additional profit, but to reduce the risk of potential losses. This difference reveals the main goal of hedging – to achieve the optimal risk structure, that is, the optimal balance between the advantages of hedging and its value.

In the process of risks hedging, it is necessary to compare the cost of the hedge with the amount of the reduced possible losses on risk. In combination with each other these two indicators form the effectiveness of risks hedging.

When hedging, it is important to accurately select the hedging objectives in order to correctly determine its effectiveness. In general, the effectiveness of a hedge is determined by the ratio of the actual financial result to the planned result.

The process of currency risks hedging can be described by the following sequence of steps:

1) making a decision to hedge: whether or not to carry out a hedging operation (risk assessment in comparison with possible costs);

2) determination of the hedging objectives, the hedging object;

3) data collection: the amount of currency reflected in the balance sheet, future currency transactions, etc.;

4) the development of a currency risk hedging plan (search for someone who will hedge foreign exchange risk, organize internal control and process, implement a currency hedging strategy of an established or unidentified type);

5) accounting of the hedging transaction and analysis of the results (eligibility, documentation and verification, fair market value, profit/loss accounting for transactions of an unidentified type, special hedge accounting for transactions of a specified type).

It should be noted that certain risks are inherent in hedging. We emphasize that the main risk of hedging is the risk associated with a change in the base price. There always exists the risk of a change in the base price, because the prices of real and futures markets do not differ significantly.

Another risk is a systemic risk, that is, the risk associated with sudden changes in external factors (legal framework, introduction of new tax rates, duties, etc.).

The main DFIs of the derivatives market, designed to hedge currency risks, can be currency forwards, currency futures, currency options and swaps.

The unifying beginning of the whole variety of hedging tools for currency risks is their key properties: their value changes when the basic variable changes, no investments are required to purchase them, or minor initial investments are required, payments on these instruments are made in the future.

In the course of studying the characteristics of the main DFIs, the dual nature of market relations in a derivative financial instrument is specified [2–8].

Since any market instrument is an agreement of at least two parties, a market participant who tries to save his capital must be opposed by another market participant who agrees to risk his capital in the hope of earning income from this market instrument. As a result the derivative tool is both an instrument for keeping capital intact, and an instrument for its multiplication. Otherwise, the derivative could not appear on the market.

A distinctive feature of **DFIs** is that the moment of the performance of obligations under the contract is separated from the time of its conclusion by a certain period of time, i.e. they are fixed-term.

For large companies and commercial banks the **DFIs** market is transformed into a market where the received profit serves as a hedge (protection) of the company's total target profit.

Thus, the purpose of the hedge is to eliminate the uncertainty of future cash flows (both negative and positive), which will allow you to have a comprehensive idea of future income and expenses arising in the course of financial or commercial activities.

Economics

We consider it expedient to give our own definition of the concept of "hedging instruments" which is based on the conducted research.

Hedging instrument is a derivative financial instrument used to optimize the price risk of the underlying asset under the assumed and planned commitments with maximum possible efficiency according to the developed hedging strategy which allows you to receive additional profit when it is implemented (under certain conditions).

Hedging, as a risk minimization technique, has a number of obvious advantages in comparison with other techniques:

- futures contracts on the basis of which hedging is performed, fix the price level of the underlying asset, and allow not to forecast the change in the value of the underlying asset, but to fix it at an acceptable level;

- on the basis of the information that futures contracts contain, it is easy to be up to speed on the demand and supply for these or other assets and thus be insured against losses.

A new definition of hedging is proposed, which includes the following main distinctive features:

- 1) it is an independent type of economic relations, based on the use of hedging instruments;
- 2) it provides greater objective predictability of the future financial flows (distinguishes the hedging process from other risk management techniques);
- 3) it optimizes the risks of the main business activity of a business entity (distinguishes hedging from speculation and arbitrage, which also use derivative financial instruments);
- 4) it takes into account the assumptions about possible changes in the risk factor in the future with a view to effecting effective hedging.

Hedging is an independent type of economic relations with respect to optimization of price risk for accepted and planned liabilities through the use of hedging instruments with the greatest possible efficiency.

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