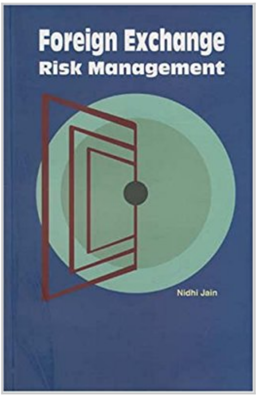


# Foreign Exchange Risk Management

*By Nidhi Jain*



**Foreign Exchange Risk Management** By Nidhi Jain

In the early 1990s, the foreign exchange (forex) market in India was in the initial stages of development and suffered from several shortcomings. The spot market, as well as forward market, lacked depth and liquidity. The market was skewed with a handful of public sector banks accounting for the bulk of merchant business, with foreign banks handling most of inter-bank business. The forward rates reflected demand and supply, rather than interest rate differentials, owing to lack of integration between the money and forex markets and also due to restrictions on borrowings/lendings in the international market. India's post-reforms period (1991 onward) has been marked by wide-ranging measures to widen and deepen the foreign exchange market. In line with the liberalization measures undertaken in other areas, various reform measures have been introduced in the foreign exchange market to make it liquid, vibrant, open, and market-determined. From a managed floating system under which the exchange rate was officially determined, the regime has passed through several phases to reach the present market-based system under which the exchange rate is determined by forces of demand and supply. With the introduction of market-determined exchange rate, companies have been exposed to risks of fluctuating rates which divert their attention from day-to-day corporate affairs. Management of risk associated with exchange rate is a new challenge for company managers. What is this risk? What are the perceptions of corporate managers about it? How to cope with it? These issues and solutions are discussed in Foreign Exchange Risk Management.

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