Internationalization & Export Management (IEM 6CFU)

Financial risks of Internationalization

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Financial risks

Risks connected to the variability of market process of financial activities (exchange rates, commodity prices, interest rates)

Market risks

<u>It's a two way risk</u>

- Firms need to protect from unfavourable variation
- But also to to consider the opportunity cost of any hedging
- The aim is transforming unpredictable events in calculated risks

Currency risks

Three main forms:

- **Transaction risk:** exchange variation impacts the debts owed to and by companies in foreign currency;
- **Translation risk:** The variation in the exchange rate also impacts the actual countervalue of the financial statement items related to transactions in foreign currency;
- **Economic risk:** the exchange variation may impact the company's competitive position in a given market

➡ Countervalue effect
Currency flow effect

Hedging instruments

Traditional instruments

a. Invoicing in reporting currency
b. Insurance
c. Currency basket
d. the establishment of an eschange cap and/or an exchange floor

Derivatives

a. Currency future
b. Currency option
c. Currency swap

What is the variation feared by European importers?

What is the variation feared by the European exporters?

Price risks

It’s connected to the volatility of commodity prices

Three main forms:

- **Transaction risk:** possibility that an increase (decrease) in the commodities’ quotations might force the buyer (seller) to pay (collect) an amount greater (less) than that estimated
- **Replacement risk:** possibility that an increase in prices might shift demand towards replacement products;
- **Competitive risk:** possibility that the increase (decrease) in prices might be to the disadvantage of a company but not its competitors that purchased (sold) at more affordable prices.

Hedging instruments

Real instruments

a. Agreement at a fix price
b. speculative inventory

Financial instruments

a. Cap and floor
b. Collar
c. Commodity option
d. Commodity future
e. …..

What are the factors affecting the possibility to develop speculative inventory?