BARCLAYS COMMERCIAL

FAIR EXCHANGE.

A GUIDE TO PROTECTING YOUR BUSINESS AGAINST FX FLUCTUATIONS.

TURNING THE CORNER

HIGH LEVELS OF VOLATILITY AND RAPID ECONOMIC CHANGE CAN CAUSE ANXIETY AS YOU FACE THE EFFECTS OF CIRCUMSTANCES WHICH ARE OUT OF YOUR CONTROL. HOWEVER, FX IS AN AREA WHERE YOU CAN TAKE PRACTICAL STEPS TO TAKE CONTROL AND MITIGATE RISKS. WE UNDERSTAND THAT IT'S DIFFICULT TO KNOW HOW TO MANAGE YOUR FX EXPOSURE, ESPECIALLY IF YOU'RE IMPORTING OR EXPORTING. HERE WE GIVE YOU PRACTICAL HINTS AND TIPS TO MAKE IT EASIER FOR YOU.

Market conditions have changed dramatically in recent months and continue to do so on a daily basis. Fluctuations in foreign exchange markets have had a significant impact on both importers and exporters – importers have seen an increase in their costs whereas exporters have seen an equal and opposite benefit.

SO WHAT CAN YOU DO TO PROTECT YOUR BUSINESS IN THESE CHALLENGING TIMES?

Before you can begin to manage your foreign exchange exposure, you need to understand the foreign exchange risk your business is facing:

- **What proportion of your business relates to imports or exports?**
- **Which currencies are involved and what is the timing of the payments?**
- **Are your payables and receivables in the same currency?**
- **What effect would an adverse move in foreign currency markets have on your balance sheet?**
- **Is the level of overseas business likely to change? Are you looking at new buyers/suppliers in new markets?**

Once you have understood the risks, it will help you to identify your business needs and appropriate solutions. On the following pages there are some options available to you for managing your foreign exchange risk.

1. BUY OR SELL YOUR CURRENCY IN THE SPOT MARKET.

The amount of currency or sterling required, the exchange rate and the value date are all fixed on the day the deal is done. Deals are normally settled ‘value spot’ i.e. the exchange of currency takes place two working days after the exchange rate has been agreed.

The benefit of this option is that it provides you with the ability to take advantage of favourable currency market movements. However, it can also be a high risk strategy as it doesn’t provide any protection against adverse rate movements and negative market conditions. If FX rates move the wrong way, it may have a significant impact on your business resulting in your profit being reduced or, in a worse case scenario, a loss-making year.

The level of your exposure and competitive nature of your business will help you determine if this option is suitable.

2. FIX YOUR FOREIGN EXCHANGE RATE USING A FORWARD EXCHANGE CONTRACT.

If you have identified key transactions in your business cycle where FX rates could fluctuate, it may be worth considering achieving certainty of exchange rates at a future date by booking a forward exchange contract.

A forward exchange contract is a contract between you and Barclays for the sale or purchase of a specific amount of currency at a specified exchange rate, for settlement on a future date or between two future dates.

This approach eliminates the exchange rate risk and provides a fixed rate to cover your exposure. However, it may be worth considering the level of exposure you are prepared to commit to as this option could also mean that you're not able to take advantage if rates subsequently move in your favour, as you are obliged to transact at the forward exchange contract rate.

3. USE A FLEXIBLE SOLUTION.

Your business strategy may favour a more flexible approach to FX. A currency option offers you this flexible means of obtaining protection against adverse exchange rate movements – like a forward exchange contract – whilst at the same time allowing you to take advantage if rates move in your favour – like a spot deal. These solutions may incur a premium and it may be worth exploring alternative structured solutions which offer similar protection and the potential to participate in favourable spot rates to a predetermined point. Barclays Commercial Bank can share with you a range of solutions to support you in developing an appropriate strategy for your business.

HOW IT WORKS.

To give you an idea of the various options available to you, let's take the example of a company that imports goods and pays for them in US Dollars.

Company scenario:

- **The company places an order on 2nd January with their supplier to buy USD1,000,000 worth of goods. They agree that payment will take place in 3 months time**
- **The customer will pay for the goods from their sterling account**
- **The GBP/USD exchange rate at the time of the order (i.e. 2nd January) = 1.50**
- **The 3 month forward rate at the time of the order = 1.47**
- **The company's budget rate (the rate at which their product remains profitable) = 1.45**

The foreign currency markets are volatile with GBP/USD rate having hit a low of 1.45 and high of 1.55 in the previous month. Furthermore, economic reports published on 2nd January forecast that sterling will depreciate over the next 3 months i.e. the GBP/USD exchange rate will be lower than 1.50. If this materialises, the importer will have to pay more if they do not protect their foreign exchange exposure.

In view of the forecasts, market volatility and the need to ensure they do not go below their budget rate, the importer decides to use a combination of spot, forward exchange contract and currency option* as follows:

1. **To cover 25% using a forward contract at GBP/USD 1.47**
2. **To cover 50% using a flexible solution e.g. a currency option,* also at GBP/USD 1.47**
3. **To transact the remaining 25% on a 'spot' basis**

This solution gives them protection on 75% of their foreign currency exposure i.e. 25% forward contract and 50% flexible solution which ensures that they stay above their budget rate. It also provides them with 75% flexibility i.e. 25% spot and 50% flexible solution, so they can take advantage if sterling appreciates and the GBP/USD exchange rate moves in their favour.**

MORE INFORMATION ONLINE.

- Latest sterling developments
- Interest and exchange rates
- A short form to register for free financial news bulletins

If you would like to discuss any of these options further, please contact your local Barclays Commercial Bank Relationship Team or visit www.barclayscommercial.com

* May incur a premium. **Note that this solution is one of many available and some businesses may decide to protect more, less or all of their FX. Please speak to your local Barclays Commercial Bank Relationship Team for more information.