FX risk management rated important by financial executives, but new study says only half have a process to manage it

TORONTO, April 17, 2013 – The vast majority (90%) of financial executives surveyed rated foreign exchange (FX) management as an important consideration in their business, according to a new survey by the Canadian Financial Executives Research Foundation (CFERF). However, almost half of organizations participating in the survey indicated they did not have a policy or formal process/procedure in place to manage FX risks, according to the study, which was sponsored by CIBC.

"This would suggest that some organizations could benefit from a more structured approach to managing their FX risk," said Michael Conway, Chief Executive and National President of Financial Executives International Canada. "This is proving even more important as Canadian companies are moving into foreign markets to generate growth."

The *Foreign exchange risk management: Perspectives from financial executives* report is based on the results of an online survey that took place between November 26, 2012 and January 3, 2013, and was expanded with insights gathered during an executive research forum that included participants in Montreal, Toronto and Calgary on November 28, 2012.

To Mr. Conway's point, managing foreign currency risk is no longer simply a case of guarding against changes between the U.S. and Canadian dollar. In fact, 42% of Canadian financial executives surveyed said that they are now doing business in fast-growing emerging markets, where currencies can be volatile or under strict government controls.

FX risk can negatively affect cash flow and profitability both in the short and long term. Changes of more than 5% in the value of the Canadian currency relative to the U.S. dollar are commonplace over any typical 60-day period. Viewed over the longer term, the Canadian dollar has broken out of a narrow, stable trading band with the U.S. that prevailed from 1994 until 2007. The financial crisis of 2008 resulted in three years of extreme currency volatility, and risk.

"The swings in the U.S.-Canada currencies became very extreme," said Mary Mulqueen, Managing Director of Foreign Exchange Sales with CIBC. "So companies that aren't addressing risk management would have experienced that in a major way and would be feeling it now. 78% of our exports are still to the U.S. and even for those companies that are expanding into Asia, most of their trade is denominated in U.S. dollars. We expect that to change and evolve over time, but currently the U.S. dollar is the key counterparty currency for Canada."

Responsibility for managing FX risk generally lies near the top of Canadian businesses. In the majority of cases, the CFO, VP of finance or treasurer has direct responsibility for controlling FX risk and many of those executives report directly to a board committee charged with monitoring the business' foreign exchange exposure.

Canadian companies take a "do no harm" approach to FX risk management, borne out by the stated goals of their FX hedging programs. Hedges are not created as speculative bets with the hope or

expectation of windfall gains out of currency fluctuations, but are created instead to protect against short-term changes in exchange rates, provide certainty for purchases and/or sales and short-term cash flows in home currencies or neutralize the balance sheet impact on working capital and long term capital.

Organizations employ a sophisticated range of processes to mitigate exchange rate impacts, such as diversifying their foreign currency holdings, adjusting selling prices in response to exchange rate volatility, borrowing in foreign currencies and limiting longer term contractual arrangements to lessen the impact of currency fluctuations.

"Canadian businesses need to address the risks that come with failing to insure against possible foreign exchange shifts," Mr. Conway said. "Those include the potential for lower revenue and profits, loss of market competitiveness, the potential for higher interest costs and debt levels in a foreign market and the uncertainty that comes with controlled or managed currencies."

Currency fluctuations are a serious concern for one in four of the survey respondents. Negative effects range from a loss of competitiveness in a foreign market to shrinking profit and sales to a reduction in reinvestment in the parent company.

Companies need to see rewards as well as the risks with foreign exchange. As the participants in the Executive Research Forum and survey respondents highlighted, Canadian businesses are tackling the issues around foreign currencies with increasing sophistication.

"FX in the form of foreign currency transactions, i.e. payables and receivables, is an integral part of more and more Canadian businesses today," said Ms. Mulqueen. "As a result, FX is getting a much higher profile, whether it be from the news media or just internally, as businesses have to rely on global connections to survive and thrive. The focus on emerging markets like Latin America and Asia has opened up new opportunities for Canada as these countries seek natural resources for industrial and infrastructure development. Foreign exchange can materially impact businesses' competitive advantage or put them at a real disadvantage if they aren't aware of their risks or don't handle them effectively because that impact goes directly to the bottom line."

Click here to view the full report.

About the Canadian Financial Executives Research Foundation
CFERF is the non-profit research institute of FEI Canada. The foundation's mandate is to advance the profession and practices of financial management through research. CFERF undertakes objective research projects relevant to the needs of Canada's senior financial executives in working toward the advancement of corporate efficiency in Canada.

About Financial Executives International Canada
FEI Canada is the all-industry professional membership association for senior financial executives. With 11 chapters across Canada and more than 1,800 members, it provides professional development, thought leadership and advocacy services to its members. The association membership, which consists

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