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A Study on Financial Risk Management

[1]A. Anitha, [2] K. Manisha

[1]Asst. Prof., Dept. of MBA, Santhiram Engineering College, Nandyal
[2]Student of MBA, Santhiram Engineering College, Nandyal
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ABSTRACT:

The idea behind using risk management practices is to protect businesses from being vulnerable. Many business risk management plans may focus on keeping the company viable and reducing financial risks.

A financial risk management process is a series of steps undertaken to identify potential financial risks, assess their severity, and identify how they can be managed.

Financial risk management is a function within organizations that aims to detect, manage, and hedge exposure to various risks stemming from the use of financial services

REVIEW OF LITERATURE:

Risk management is an important part of planning for businesses. The process of risk management is designed to reduce or eliminate the risk of certain kinds of events happening or having an impact on the business.

Financial risk management is the practice of protecting economic value in a firm by managing exposure to financial risk - principally operational risk, credit risk and market risk, with more specific variants as listed aside.

Risk management is a process for identifying, assessing, and prioritizing risks of different kinds. Once the risks are identified, the risk manager will create a plan to minimize or eliminate the impact of negative events. A variety of strategies is available, depending on the type of risk and the type of business. There are a number of risk management standards, including those developed by the Project Management Institute, the International Organization for Standardization (ISO), the National Institute of Science and Technology.

RISK RETURN ANALYSIS:

All investment has some risk. Investment in shares of companies has its own risk or uncertainty; these risks arise out of variability of yields and uncertainty of appreciation or depreciation of share prices, losses of liquidity etc. The risk over time can be represented by the variance of the returns.

Principles of risk management:

- Create value - resources expended to mitigate risk should generally exceed the consequence of inaction, or (as in value engineering), the gain should exceed the pain
- Be an integral part of organizational processes
- Be part of decision making

- Explicitly address uncertainty and assumptions
- Be systematic and structured
- Be based on the best available information

NEED FOR THE STUDY:

The buying and selling of foreign currency and other debt instruments by businesses, individuals and governments happens in the foreign exchange market. Apart from being very competitive, this market is also the largest and most liquid market in the world as well as in India. It constantly undergoes changes and innovations, which can either be beneficial to a country or expose them to greater risks. The management of foreign exchange market becomes necessary in order to mitigate and avoid the risks the need of the study is to know the foreign exchange risk and factors creating risk in foreign exchange transactions and the technique used for managing that risk.

OBJECTIVES OF THE STUDY:

- To study the foreign exchange risk at Aurobindo Pharma Ltd.
- To analyze the revenues of the company when the exchange rates fluctuates.
- To analyze income statement to find out the revenue when the dollars are converted into INR
- To study the methodology of risk management adopted by the company

RESEARCH METHODOLOGY

Primary data:

Data used in research originally obtained through the direct efforts of the Researcher through surveys, interviews and direct observation. Primary data is more costly to obtain than secondary data, which is obtained through published Sources, but it is also more current and more relevant to the research project.

Secondary data:

The data has been collected from the various secondary sources like text books, journals, internet, and newspapers.

The research methodology adopted for the study is

Tools: • Tables

• Graphs

Techniques: • Hedging

LIMITATIONS OF THE STUDY:

- The study is confined just to foreign exchange risk but not the total risk.
- The analysis of this study is mainly done on the basis of secondary data of the company.
- Time was a major constraint for knowing the entire process in depth.
- The analysis made on the basis of secondary data

DATA ANALYSIS AND INTERPRETATION:

Hedge: Aurobindo Pharma Ltd is having receivables of USD 20571 on 25th Dec 2021 is exposed to the risk of dollar depreciation.

As on 10 Aug 2022

underlying	RBI reference rate Rs
1 $	61.13

	Spot (10 Aug 2022)	Futures (25 Dec 2021)
Today	61.13	62.25

Now on 25th Dec the dollar might have appreciated or depreciated.

Assuming both the situations:

Dollar appreciated (25th Dec)	Dollar depreciated (25th Dec)
USD/INR spot: 63 DEC Futures: 63.15	USD/INR Spot: 62 Dec futures: 62.15

Buy future contract :63.15 profit/loss= (62.25-63.15)*20571 loss=18513.9	Buy future contract :62.15 profit/loss= (62.25-62.15)*20571 profit=2057.1
Receivables in spot =(63*20571) =1295973	Receivables in spot =(62*20571) =1275402
Net receivables=(1295973-18513.9) =1277459.1	Net receivables=(1275402+2057.1) =1277459.1

So if rupee moves either way corporate is hedged against currency fluctuations Receivables not hedge in case the exporter didn't hedge his receivables and kept his position open then the consequences would be

Dollar appreciated (25 Dec)	Dollar depreciated (25 Dec)
USD/INR Spot: 63	USD/INR Spot: 62
Receivables in spot =1295973	Receivables in spot =1275402
Profit =(63-62.25)*20571 =15428.25	Loss=(62-62.25)*20571 =(5142.75)

Interpretation: Thus if the exporter didn't hedge his position, he would gain in case of dollar appreciation RS.15428.25 but would inure more losses Rs.5142.75 in case of rupee appreciation. Hence, it is always advisable to hedge the foreign exchange risks.

FINDINGS

1. High fluctuations in value of currency in short period of time is found. From the financial year 2020-22 there is a huge depreciation in the value of INR i.e. from Rs.50 to Rs.60.
2. Total revenues are decreased from Rs. 5996.34 crores at Rs.60 to Rs.5896.401 crores at Rs.59 when the average exchange rate is at Rs.60 in the Fy 2022.
3. Total revenues are decreased from Rs. 5205.78 Rs.54 to 5109.377 at Rs.53 crores. If the Exchange rate had fixed @ Rs.54, the revenues would have been same in thaw FY 2021.
4. The revenue received from Europe is decreased from Rs. 2178 cr to Rs.1573 cr for the year 2020-22. The revenue received from India is also decreased from Rs. 3481 cr to Rs. 3482 cr from first quarter to fourth quarter.

SUGGESTIONS

1. The exporters are faced either risk of rupee appreciation or importers are faced with that of dollar appreciation. So they hedge their risk by taking the opposite position in the futures market and restrict their losses

2. To overcome these problem exporters should make good governance by making available superior human, social and business infrastructure even if the tax rates are high. As a result good governance helps in lower the costs of operations and lowers the aggregate costs of doing business. 3. To improve rupee viability and preserve profits, exporters need to be efficient and productive and bring down aggregate rupee cost.

CONCLUSION

After the detailed study on foreign exchange risk management of Aurobindo Pharma Ltd it is concluded that the company is using VaR (Value at Risk) and Hedging techniques for minimizing foreign exchange risk. To improve rupee viability and preserve profits, exporters need to be efficient and productive and bring down aggregate rupee cost.

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