ISSN: 2308-5096(P) ISSN 2311-620X (O)
[International Journal of Ethics in Social Sciences
Vol.3, No. 1, June 2015]

Foreign Exchange Risk Management In Banks : A Comparative Study of Some Selected Banks In Bangladesh

Md. Matiur Rahman[1]

Md. Mukitul Hoque[2]

Abstract

This paper investigates how Conventional and Islamic banks in Bangladesh manage their foreign exchange risk and compares the results to theoretical findings and to previous empirical research. The information incorporated in this report is collected both from the primary sources and as well as from the secondary sources. Data directly from the practical field is called primary source of data. Although Information is mainly collected from different published articles, journals, brochures, published documents of Bangladesh Bank and web sites. The study finds significant differences in the foreign exchange risk management policies, guidelines of Bangladesh Bank, Management oversight notably in the choice of various types of exposure to cover and in the hedging instruments used. Consistent with previous research, forwards and netting are the most used instruments and transaction exposure is the most managed foreign exchange risk. Surprisingly, translation and economic exposures are not well identified and managed mainly because firms believe it is unnecessary or too compels. Finally, firms hedge their exposure but never fully due to high cost of hedging. The researchers believe this report inspires to increase the performance and management of these respected Banks.

Keywords: *Foreign exchange, Foreign Exchange Risk, Perception, Guidelines for Managing Risk,*

1.1 Introduction

1 Probationary Officer, Islami Bank Bangladesh Ltd, Head Office Complex Corporate Branch, Contact: +8801627524820, Email: matiur.rahman@yahoo.com

2 Research Assistant, Center for Research on Islamic Management and Business, and Studying MBA under Korean Government Scholarship Program (KGSP) 2015, Contact: +8801715698689, +8801671641018, Email: mukithoque007@yahoo.com

Foreign exchange refers to the financial transaction where currency value of one country is traded into another country's currency. The whole process gets done by a network of various financial institutions like banks, investors and governments. The exchange rate varies according to the value of each country's currency which is based on the health of that particular country's economy. Any individual or company engaged in overseas business should be aware of the risks of currency fluctuations. Customers without commercial contracts expressed in domestic currency (or fixed by an agreed rate of exchange) are fully exposed to what is known as an exchange risk. Exchange risk may arise because of exchange rate movements in the period from the original commercial contract, to the time of settlement of the domestic equivalent of the foreign currency amount. Foreign exchange risk management is designed to preserve the value of currency inflows, investments and loans, while enabling international businesses to compete abroad. Although it is impossible to eliminate all risks, negative exchange outcomes can be anticipated and managed effectively by individuals and corporate entities. Businesses do so by becoming familiar with the typical foreign exchange risks, demanding hard currency, diversifying properly and employing hedging strategies.

No countries of the world can produce all their necessary commodities and services. So it has to buy the commodities and services which it can not produce or produce insufficiently from other countries. On the other hand countries producing commodities and services excess of their necessity export a portion of it to other countries. The activities of buying and selling or of exchange of commodities and services between two different countries are done by banks. So Banks play the important role of financial intermediation and are key to international financial stability, they need to operate in a safe and sound manner, and hold capital and reserves sufficient to protect against the risks that arise in their business.

1.2 Objective of the Study

The main objective of this study is to analyze the comparative status of some banks regarding foreign exchange risk management. In order to achieve the main objective, the specific objectives are as follows:

- To identify various types of foreign exchange risk.
- To find out foreign exchange risk management techniques.
- To compare foreign exchange risk among conventional banks and Islamic banks in Bangladesh.

2. Literature Review

Many researchers have made their research upon foreign exchange risk management; most of them show their key findings and their main objective on this selected area. A general concern in the FX risk management in the organization is whether management should be centralized or decentralized. Prindl (1976) recommends a centralized risk management system. Because in the risk point of view it incur lower cost but it has some disadvantage too like lack of autonomy in some units. Most studies tend to show that FX risk is considered an important risk to manage. Marshal (1999) finds that FX is the most important financial activities in large firms and banks of British, America and Asia.

Loderer and Pichler (2000) made a similar survey but for Swiss organization. They obtain as main reasons for managing currency risk guaranteeing the cash flow, reducing financing cost, preventing losses, and reducing taxes.

Bodnar, Marston and Hayt (1999) find that many firms take into account their market view when choosing a risk management strategy. About 10% of firms in their sample altered either the size or the timing of hedges that they made because of their market view.

Froot and al (1994) shows that there is no general framework for managing economic exposure. This appears difficult. Shapiro (1998) argues that Translation risk should not be managed because it is purely an accounting concept. He used qualitative data for his research. For hedging Batten et al (1993) find that most of the companies or organizations use forwards option and currency swaps.

According to Bodnar and Gebhart (1998), German and US companies use derivatives primarily to manage foreign exchange risk. They also show the reasons to use it and that is variability in cash flows.

Marshal (1999) also shows that economic exposure varies across countries with Asian firms paying most attention to this kind of exposure.

4. Findings and Analysis

Part one of chapter four discusses about those findings which we avails from our fields from several Islamic and Conventional Banks and in part two we discusses over the comparison between Islamic and Conventional Banks foreign exchange risk and their technique. Here, we are going to shows how Islamic Banks and Conventional deals with their risks and techniques which are restricted by Bangladesh Bank.

4.1 Perception of Bankers Regarding Banks Foreign Exchange Risk

Table 4.1: Perception of Bankers Regarding Banks Foreign ExchangeRisk

Types of risk	Very Low (%)		Low (%)		Neutral (%)		High (%)		Very High (%)		WAS		Ranks	
	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Exchange Rate Risk	0	0	10	10	20	10	40	30	30	50	3.5	4.2	1.5th	1st
Interest Rate Risk	0	0	20	20	30	30	30	30	20	20	3.5	3.5	1.5th	2nd
Settlement Risk	0	0	30	20	20	40	40	20	10	20	3.3	3.4	4th	3rd
Sovereign Risk	0	10	30	30	10	20	50	10	10	30	3.4	3.2	3rd	4th

Source: Field Survey 2014

Note: WAS stands for weighted average score; it is calculated using weights as follows;
Very low=1, low=2, neutral=3, high=4, very high=5

In order to get the perceptions of bankers regarding various types of foreign exchange risks of respected banks, ten (10) bankers have been interviewed, their responses have been tabulated in 4.1 which shows that exchange rate risks gains 1st place in conventional banks where Islamic Banks achieved first place in Exchange rate risk with average score 4.2 and 3.5 respectively, and both in conventional and Islamic risks followed by interest rate risk, settlement risk, sovereign risk with average score 3.5.3.4, 3.2 and 3.5, 3.4 and 3.2 consistently.

4.2 Options Of Bankers Regarding Risk Management Oversight

Table :

Management	Never	Seldom	Sometimes	Often	Always	WAS	Ranks

Oversight	(%)		(%)		(%)		(%)		(%)		(%)		(%)	
	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
The management at divisional level monitors risk	0	0	20	40	30	20	40	30	10	10	3.4	3.1	4th	4.5th
The Board of Director performs the responsibility of the main risk oversight	0	0	20	10	40	30	10	30	30	30	3.5	3.8	3rd	1.5th
Branch level officials supervise risk	0	0	20	30	50	40	20	20	10	10	3.2	3.1	5th	4.5th
The Executive Committee monitors risk	0	0	10	10	30	20	40	50	20	20	3.7	3.8	2nd	1.5th
The Audit Committee oversee all the activities of banking operations	0	0	10	1	20	30	50	40	20	20	3.8	3.4	1st	3rd

Source: Field Survey 2014

Table 4.2 shows that out of six aspects regarding foreign exchange risks management oversight in conventional banks The Board of Director performs the responsibility of the main risk oversight and The Executive Committee monitors risk occupy the 1st position where in Islamic banks The Audit Committee oversee all the activities of banking operations stands for 1st place with WAS 3.8 achieved by both of them. And in Islamic banks The management at divisional level monitors risk, The Board of Director performs the responsibility of the main risk oversight, Branch level officials supervise risk, The Executive Committee monitors risk with was 3.4, 3.5, 3.2, 3.7and Conventional Banks oversight have been followed by The Audit Committee oversee all the activities of banking operations, The management at divisional level monitors risk, Branch level officials supervise risk with WAS 3.4, 3.1, 3.1.

4.3 Options Regarding Using of Techniques For Managing Risk

The following table shows that…..

Techniques	Never	Seldom	Neutral	Average	Highly	WAS	Ranks

	(%)		(%)		(%)		Used (%)		Used (%)		(%)		(%)	
	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Diversification	0	0	0	10	40	20	50	40	10	30	3.7	3.9	2nd	1.5th
Derivatives	0	0	20	30	30	30	40	30	10	10	3.4	3.2	3rd	3rd
Currency SWAPs	0	0	0	10	20	20	40	40	40	30	4.2	3.9	1st	1.5th

Source: Field Survey 2014

Table 4.3 shows that among five techniques for managing RiskDiversification and Currency SWAPs achieve first place with WAS 3.9 where in Islamic Banks Currency SWAPs achieved first place with WAS 4.2 and in Islamic Banks are being followed by Diversification and Derivatives with WAS 3.7 and 3.4 respectively. In conventional banks Derivatives with WAS 3.2.

4.4 Operations Regarding Using of Bangladesh Bank Guidelines For Managing Risk

The following table shows that…..

Issues	Not followed at all (%)		Frequently followed (%)		Neutral (%)		Average followed (%)		Highly followed (%)		WAS (%)		Ranks (%)	
	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Dealing limit	0	0	10	10	10	30	30	20	50	40	4.2	3.9	2nd	2nd
Mandatory Leave	0	0	0	0	10	20	20	20	70	60	4.6	4.4	1st	1st
Position Reconciliation	0	0	20	10	10	0	10	20	60	50	4.1	2.6	3rd	3rd
Valuations	60	80	30	20	10	0	0	0	0	0	1.5	1.2	4.5th	5th
Internal Audit	50	60	50	40	0	0	0	0	0	0	1.5	1.4	4.5th	4th

Source: Field Survey 2014

Table 4.4 shows that among five guidelines restricted by Bangladesh Bank where both in Islamic Banks and Conventional Banks Mandatory Leave gets the 1st position with WAS 4.6 and 4.4 respectively and in Islamic Banks and Conventional Banks followed by Dealing Limit , Position Reconciliation, Valuations and Internal Audit with4.2, 4.1, 1.5, 1.5 and 3.9, 2.6, 1.4, 1.2 respectively.

4.5 awareness of The Bank's Personnel Regarding Various Types of Risk of The Bank And Measurement Level

The following table shows that awareness of different types of risk faced by respondents

Types of risk	**Islamic**	**%**	**Mean**	**SD**	**Convention**	**%**	**Mean**	**SD**

	Banks				**al Banks**			
Credit Risk/ Investment Risk	7	100	1.00	.000	7	100	1.00	.000
Liquidity Risk	6	85.7	1.14	.378	7	100	1.00	.000
Interest Rate Risk	2	28.6	1.71	.488	7	100	1.00	.000
Foreign Exchange/ Currency Risk	6	85.7	1.14	.378	7	100	1.00	.000
Performance/ Operational Risk	7	100	1.00	.000	7	100	1.00	.000
Environmental Risk	5	71.4			7	100	1.00	.000
Rate of Return Risk	6	85.7	1.14	.378	7	100	1.00	.000
Shari'a non-compliance Risk	6	85.7	1.14	.378	2	28.6	1.71	.488
Price risk	2	28.6	1.71	.488		100	1.00	.000

Source: Field Survey 2014

The following table shows that level of awareness of respondents as regards various risks The analysis of the table 1(a) reveals that there are differences between Islamic Banks and

Types of risk	Highly Aware		Only Aware		Neutral		Unaware		Not at all aware		Mean		SD	
	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Credit Risk/ Investment Risk	100	100									5	5	.00	.00
Liquidity Risk	7	100	28.6								4.71	5	.488	.00
Interest Rate Risk	14.3	100							71.4		1.67	5	1.63	.00
Foreign Exchange/ Currency Risk	71.4	100	14.3						14.3		4.29	5	1.49	.00
Performance/ Operational Risk	71.4	100	14.3						14.3		4.29	5	1.49	.00
Environmental Risk	42.9	100	42.9						14.3		4.00	5	1.21	.00
Rate of Return Risk	42.9	100	42.9						28.6		4.00	5	1.21	.00
Shari'a non-compliance Risk	42.9		57.1						71.4		1.00	1.86	.535	1.46
Price Risk	14.3	100									1.67	5	1.63	.00
Average														

Source: Field Survey 2014

Conventional Banks as regards the awareness of different types of risks. As regards the awareness of Credit/Investment risk and Performance of the Operational risk, there is no difference between Islamic Banks and Conventional Banks. But as regards the other types of risks there is variation between Islamic Banks and Conventional Banks. The highest variation has been observed in case of Shariah non-compliance risk and Interest rate risk followed by Price Risk and Environmental risk. In case of other risks the variation of awareness has been observed at 14.3%.The analysis of table 1(b) reveals that there are also variations as regards the level of awareness of the various risks between Islamic Banks and Conventional Banks. In case of Islamic Banks, 100% respondents have been highly aware as regards Credit/ Investment risk, 71.4% respondents have been highly aware of Liquidity risk, Foreign exchange/Currency risk and Performance/operational risk. Only 42.9% respondents have been highly aware Environmental risk, Rate of return risk and Shariah non-compliance risk. Only 14.3% respondents have been highly aware of Interest risk and Price risk. But, in case of conventional banks, 100% respondents have been highly aware of all types of risk shown in the table excepting Shariah non-compliance risk about which no respondents is highly aware.

4.6 Concernedness About The Various Types of Risk

The following table shows that concernedness of the respondents regarding various types of risks

Types of risk	Highly Aware		Only Concerned		Neutral		Not Concerned		Not at all Concerned		Mean		SD	
	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	Conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Credit Risk/ Investment Risk	100	100									5	5	1.134	.000
Liquidity Risk	71.4	71.4	28.6								4.71	4.71	1.46	.488
Interest Rate Risk		100	14.3				14.3		71.4		1.57	5	.787	.000
Foreign Exchange/ Currency Risk	14.3	28.6	28.6		57.1	28.6					4.14	4	1.49	.816
Performance/ Operational Risk		28.6	71.4			71.4			28.6		3.57	3.57	.787	.976
Environmental Risk	71.4	28.6	14.3						14.3		3.14	4.29	1.464	.488
Rate of Return Risk	71.4	57.1	14.3		14.3	14.3					4.29	4.43	1.49	.787
Shari'a non-compliance Risk		28.6			14.3				57.1		4.57	2.14	.787	1.954
Price Risk		28.6									1.40	4.29	.894	.488

Source: Field Survey 2014

The concerns of the various types of risks also varies between Islamic Banks and Conventional Banks as shown in table 2 .In case of Islamic Banks, 100% respondents have been highly concerned as regards Credit/Investment risk; 71.4% respondents have been highly concerned as regards liquidity risk, Environmental risk and Rate of return risk each. Only 14.3% respondents are highly concerned about Foreign exchange risk. But in case of

Conventional banks 100% respondents have been highly concerned as regards Credit risk and Interest risk each. 71.4% respondents and 57.1% respondents have been highly concerned regarding liquidity risk and rate of return risk respectively. Only 28.6% respondents have been highly concerned about Foreign exchange/Currency risk, Performance risk, and Environmental risk and Price risk each.

Therefore, H1- "There is a variation as to the awareness and concernedness of the various risks by the Islamic Banks and Conventional Banks" has been proved in our study.

4.7 Use of Various Risk Management Techniques

The following table shows that use of risk management techniques

Techniques	**Islamic Banks**	**%**	**Mean**	**SD**	**Conventional Banks**	**%**	**Mean**	**SD**
Credit Ratings	7	100	1.00	.000	7	100	1.00	.000
Gap Analysis	5	71.4	1.29	.488	5	71.4	1.29	.488
Scenario Analysis	5	71.4	1.29	.488	7	100	1.00	.000
Duration Analysis	6	85.7	1.14	.378	2	28.6	1.71	.488
Maturity Matching	3	42.9	1.71	.488	7	100	1.00	.488
Earning at risk	2	28.6	1.29	.488	2	28.6		.000
Value at risk	5	71.4	2.00	.000	7	100	1.00	.000
Simulation techniques	4		1.29	.488	7	100	2.00	.000
Stress testing	5	71.4	2.00	.000	5	71	1.29	.488
Risk adjusted return on capital	1	14.38	1.29	.488	7	100	1.00	.000
Internal Based rating system	7	100	1.86	.378	7	100	1.29	.488
Credit Scoring	6	85.7	2.00	.000	7	100	1.00	.000
Credit committees	6	85.7	1.14	1.14	7	100	1.00	.000

Source: Field Survey 2014

Table 4(a) presents the picture of use of risk management techniques in the sample banks. The table depicts that 100% respondents of both the banks have used credit ratings and Interest based rating systems. In case of Islamic Banks 85.7% respondents have used duration analysis, credit scoring and credit scoring committee techniques each. Again, 71.4% respondents have used GAP analysis, Scenario analysis, Value at risk, Stress testing techniques each. In case of Conventional Banks 100% respondents have used Scenario analysis, Maturity matching, Value at risk, Simulation techniques, Risk adjusted return on capital, Interest based rating, Credit scoring and Credit committee techniques each. Again, 71.4% respondents have followed GAP analysis and Stress testing techniques each. Therefore, it can be said that both the Islamic Banks and Conventional Banks used traditional techniques and as well as advanced techniques while measuring risk in their banks.

Therefore, it can be said that -"There is a variation between the Conventional and Islamic banks in the understanding of risk and risk management and its practice" has also been proved in the study.

4.9 Awareness of The Risk Mitigation Approaches &Measurement level

The following table shows that risk mitigation approaches

Approach	**Islamic Banks**	%	**Mean**	**SD**	**Conventional Banks**	%	**Mean**	**SD**
Risk may be avoided	6	85.7	1.14	.378	2	28.6	1.71	.488
Risk may be retained	2	28.6	1.71	.488	7	100	2.00	.00
Risk may be transferred	3	42.9	1.57	.535	7	100	2.00	.00
Risk may be shared	3	42.9	1.57	.535	7	100	2.00	.00
Risk may be reduced	7	100	1.00	.000	7	100	1.00	.00

Source: Field Survey 2014

Table 5(a) presents the picture of use of risk mitigation approaches in the sample banks. The table depicts that In case of Islamic Banks 100% respondents have agreed about risk reduction. 85.7% respondents have agreed to avoid risk and 42.9% have agreed to use the approach of risk mitigation namely; Risk transferring and risk sharing. Only 28.6% respondents have agreed for risk retention technique. In case of Conventional Banks all the respondents have agreed for risk Retention, Transferring, Sharing and Risk reduction techniques. Only 28.6% respondents have agreed for risk avoidance techniques for risk mitigation. Therefore, it can be said from the above findings that Islamic Banks have been using the approaches as mentioned in Table 5(a) to lesser extent to mitigate risk of their banks than that of Conventional Banks.

4.10 Awareness of Risk Mitigation Techniques & Measurement

The following table shows that awareness of respondents about risk mitigation techniques

Approach	**Islamic Banks**	%	**Mean**	**SD**	**Conventional Banks**	%	**Mean**	**SD**

Collateral Arrangement	7	100	1.00	.000	7	100	1.00	.000
Third party enhancement	6	85.7	1.14	378	5	71.4	1.29	.428
Loan loss reserves	5	71.4	1.29	.488	7	100		
On balance sheet netting	4	42.9	1.57	.535	5	71.4	1.00	
Guarantees	7	100	1.00	.000	7	100	1.29	.000
Parallel contracts	2	28.6	1.71	.488	7	100	1.00	.488
Over the Counter derivatives	6	85.7	2.00	.000	7	100	2.00	.000

Source: Field Survey 2014

The following table shows that awareness of respondents about risk mitigation techniques

Approach	Highly Used		Only Used		Neutral		Not-Used		Not at all Used		Mean		SD	
	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Collateral Arrangement	85.7	100	14.3								4.86	5.00	.378	.00
Third party enhancement	57.1	28.6	28.6	71.4					14.3		4.14	4.29	1.46	.488
Loan loss reserves	71.4	28.6		71.4					28.6		3.86	3.29	1.45	.488
On balance sheet netting	28.6		14.3			100			57.1		2.57	3.00	1.48	.000
Guarantees	100					100					5.00	5.00	.00	.000
Parallel contracts	28.6					100			71.4		1.86	1.86	1.14	1.46
Over the Counter derivatives	14.3					28.6			85.7	71.4	1.86	1.86		1.46

Source: Field Survey 2014

Table 6(a) depicts significance difference between the Islamic Banks and Conventional banks as regards the specific risk mitigation techniques. Results from the questionnaire suggests that Islamic Banks are less aware about following techniques compared to Conventional Banks, namely; Loan loss reserve, On balance Sheet netting, Parallel contracts, Over the counter derivatives. In addition, all the respondents of both the Islamic Banks and Conventional Banks have found aware of Collateral Agreement and Guarantees. However, Islamic Banks have found higher awareness only for the Third party enhancement compared to Conventional Banks by around 14.3%.

Even though table 6(a) suggests that Islamic Banks are less aware than Conventional Banks in terms of aware of the techniques for risk mitigation, table 6(b) depicts different results, the uses of different risk mitigation techniques have been found higher than that of Conventional Banks. As regards Islamic Banks, Guarantees has found highly used by all the banks. Collateral agreement, Loan loss reserves, Third party enhancement, Parallel contract and On balance sheet netting and Over the counter derivatives have been using by the Islamic Banks by 85.7%, 71.4%, 57.1%, 28.6% 28.6% and 14.3% respectively. As opposed regarding the Conventional Banks, all the respondents have said that collateral has highly been used for risk mitigation. However, 71.4% agreed that Third party enhancement and loan loss reserves have only used by the banks. In addition, all the respondents also opined that on balance sheet netting, Guarantees and Parallel contracts have neutral as to the use for the same purposes. The above findings suggest that Conventional banks fully concentrate on risk mitigation using Collateral, Third party enhancement and Loan loss reserve which has also marked as high usability by the Islamic Banks.

Therefore, it can be said that H4-"A positive relationship exists between risk management practices and understanding of risk; risk identification and mitigation" has also been proved in the study.

4.11 Attitude of Management Towards Risk Management Practices

The following table shows that attitude of Management towards risk management practices

Types of risk	Highly Positive		Only Positive		Neutral		Negative		Highly negative		Mean		SD	
	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional	Islamic	conventional
Credit Risk/ Investment Risk	100	100									5.00	5.00	.000	.000
Liquidity Risk	100	57.1		14.3						28.6	5.00	3.71	.000	1.84
Interest Rate Risk	14.3	28.6		28.6		14.3			71.4	28.6	2.00	3.29	1.732	1.76
Foreign Exchange/ Currency Risk	42.6	28.6	14.3	42.4		28.6					4.13	4.00	.535	.816
Performance/ Operational Risk	85.7	28.6	57.1		14.3	57.1					4.71	3.67	.756	1.03

Source: Field Survey 2014

Refer to the table 7 Management attitude towards risk management seems favourable both in Islamic banks and Conventional Banks. As regards particular risk, a slight difference has been observed. All the respondents of Islamic Banks have shown highly positive attitude towards Credit risk and Liquidity risk; 85.7% respondents showed highly positive attitudes towards

Performance risk. Foreign exchange risk and Interest rate risk have been found highly positive by 42.4% and 14.3% respectively. As regards Conventional Banks, 100% respondents showed highly positive attitude towards Credit risk followed by Liquidity risk by 57%. Interest rate risk, Foreign Exchange Risk and Performance risk have found highly positive attitudes by the management by 28.6% respondents.

4.12 Major Problems Involved In Risk Management Practices And The Suggetions To Remove The Same

At this stage, our respondents were asked to mention the major problems in risk management practices and the suggestions for the removal of the same. Table 8 depicts the picture in this regards. The table reveals that Lack of qualified and experienced personnel ranks first as it is mentioned by 50% of the total respondents followed by Poor loan recovery problem which is mentioned by 30.77% respondent; followed by Lack of Market information as it is mentioned by 23.8% and the remaining problems namely- Capital inadequacy, Improper Credit identification and rating, Short term guideline from BB, Weak Liquidity management and Poor loan monitoring have ranked 6.6th each as mentioned by 15.38% respondents.

4.12 The Problems In Risk Management

The following shows that the Problems in risk management

Sl. No	Specific Problem	Frequency of the respondents	%
1.	Lack of market information	3	23.08%
2.	Capital inadequacy	2	15.38%
3.	Poor loan recovery	4	30.77%
4.	Improper Credit identification and rating	2	15.38%
5.	Short term guideline from BB	2	15.38%

The respondents have mentioned the following suggestions for the removal of above mentioned problems.

- Adequate market information needs to be available by setting Central Management Information System (MIS).
- Capital in adequacy of the banks should be met as far as possible by gathering more capital.
- Loan recovery should be strengthening by moral persuasion of the borrowers.

- Credit identification and rating system should be included by using modern techniques.
- Long term guideline should be provided by the Central Bank

5.1 Summary of The Study And Key Findings

On the basis of sample bankers' opinions the following (statistically significant results can be concluded:

1. Of the various types of foreign exchange risks faced by the selected banks, exchange rate risk, interest rate risk, settlement risk, and sovereign exchange risks are the major risks to the bankers.
2. Regarding foreign exchange risk management oversight, it is seen that the Board of director performs the responsibility of the main risk oversight, the Executive Committee monitors risk and the Audit Committee oversees all the activities of banking operations.
3. Regarding use of foreign exchange risk management techniques, it is found that internal rating system and risk adjusted rate of return on capital are important.

5.2 Recommendations

All things around us are changing at an accelerating rate. Today is not like yesterday and tomorrow will be different from today. Given the fast changing, dynamic global economy and the increasing pressure of globalization, liberalization, consolidation and disintermediation, it is essential that Islamic and Conventional Banks have a robust foreign exchange risk management policies and procedures that are sensitive to these changes. To improve the FOX management culture further, Islamic and Conventional Banks may adopt some of the industry best practices that are not practiced currently. These are Islamic and Conventional Banks should have a clear written lending guideline that focus lending policy of different Industry separately.

Now, there is a part going to disclose which is every banker should follow their instructions and also their proper management guidelines as it proposed by central banks called Bangladesh Bank. And also from customers perspective we try our best what they should stands for the Bangladesh Bank regulations, all of these are going to discuss are given below in a consistent way.

Management Perspective:

- Build branch (SME, BDP, electronic) networks as fast as Central Bank approval and investment funds allow.

- In Islamic and Conventional Banks most of them are centralized. Decentralization of FOX management and approval authority may enhance the efficiency and effectiveness of loan appraisal process.
- Committee/ Board to ensure accountability. This system will not only ensure accountability of individual executives but also expedite the approval process.
- Management should more specific for every customer..
- Attitude of management towards risk management should more practices and explicates.
- Frequency of use foreign exchange risk management techniques more detailed to the bankers and also concern to the customers.
- Especially Management Committee should more concern on Foreign Exchange Risk Management techniques.

Bankers Perspective:

- Borrower selection should be more stringent to minimize risk associated with lending.
- It should adopt a credit grading system all facilities should be assigned a risk grade. In addition, the borrowers risk grades should be clearly stated on credit application.
- Bankers should more experienced and reliable
- Bankers should more aware and practicable about their guidelines and instructions
- They should more explicit on their responsibility which I faced a lot when I was in data collection process.
- They should more concern on their managing risk factor.
- Keep their customers about their market so that they can up to date.

5.5 Relevant Future Research

I have researched upon foreign exchange risk management field. In past many researcher have researched about this topics, but they had some deficiencies. To research in this topic we find lot of problems, limitations, prospects, various types risks are affecting banks, their probable solution. In future anyone can do his or her research work upon the risks, problems, prospects, and various techniques which are used to mitigate foreign exchange risks in conventional and Islamic bank.

References

Allayannis G and E Ofek, (Apr 2001)," Exchange rate exposure, hedging, and the use of foreign currency derivatives."*Journal of international money and finance*, Vol 20 no 2 273-296.

Bodnar G. and G. Gebhardt (1999), "Derivative uses by non financial firms in the US and Germany: A comparative survey, *Journal of international financial management and Accounting*.Vol. 10. No 3, 53-87.

Bodnar, G.R. Marston and G Hayt (1998)."Wharton 1998 survey of risk management by U.S. non financial firms." Financial management, winter Vol. 27, No.4

Breeden D, and S. Viswanathan (1996), "Why do firms hedge? An Asymmetric information model" Working paper, Duke University, NC 27708,

Froot K, D. Sharfstein, (dec 1993) and J .stein, Risk management: coordinating corporate investment and financial policies. The journal of finance Vol 48 no 5, 1629-1658.

Jacques L (1981) "Management of foreign exchange risk, a review article" *A journal of international business studies*, Vol 12 issue 1

LodererC and K Pichler. (2000)" firms do you know your currency exposure? Survey results" *Journal of empirical finance* 317 -344

Marshal A. P., (1999) Foreign exchange risks management in UK, USA and Asia pacific multinational companies" *journal of multinational financial management*. 185-211

Mayer's D and C W Smith (apr 1981). "On the corporate demand for insurance" *The journal of business* Vol 55, issue 2, 282-296

M Miller, (June 1958) "the cost of capital, corporation finance and the theory of investment," *The American economic review*, Vol 48 no 3 261-297

Prindl A. R. (1976): foreign exchange risk, John Wiley and sons,.

RadjaG., (1997) Principles of risk management and insurance, sixth edition, Addition Wesley.

Schmit J T and K Roth (Sep 1990). "Cost effectiveness of risk management Practice." *The journal of Risk and insurance*.Vol 57 issue 3,455-470.

Shapiro A.C (1977), "defining exchange risk "The journal of business Vol 50, issue 137-39

Smith C. W and R N Stultz (Dec 1998), "the determinants of firms hedging policy." *The journal of financial and quantitative analysis*, vsol 20, No. 4 391-405