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The Role Of Foreign Exchange Risk Management On Performance Management Of Exporting Firms In Developing Countries: A Case Study Of Uganda's Exporting Firms

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Abstract

This study examined the role of foreign exchange risk management (FERM) on performance management of exporting firms in developing countries taking Uganda as the case study. The conceptual framework relating to FERM attributes (currency risk assessment and currency risk management strategies) and the indicators of performance (profitability and sales growth) were constructed. A cross section and descriptive research design was adopted using a representative sample of 51 exporting firms and the population was drawn using Krejcie and Morgan (1970) method of sample selection. Proportionate stratified sampling and simple random sampling techniques were used to select from manufacturing and agro processing exporting firms. SPSS was used to analyze the data which was presented in tables and graphs. Spearman's rank correlation coefficient was used to determine the relationship between FERM and performance of the exporting firms and the regression analysis was used to predict the financial performance of the exporting firms. The findings indicate a moderate applicability level of FERM, low level of financial performance and a significant positive relation between FERM and performance of exporting firms. The researcher recommends that exporting firms should constantly assess their exposure to foreign exchange risk, which can guide them towards a suitable currency risk management. The study concentrated on foreign exchange risk management and performance of exporting company in Uganda. Similar studies can be carried out in Rwanda by analysing multinationals and banking sector.

Keywords: Foreign exchange, risk management, performance

1. Introduction

The experience with the exchange rates has in many ways differed from what was anticipated in 1973 when the major industrialized countries abandoned the effort to keep the values of their currencies fixed. There is a wide spread feeling that exchange rates have turned out to be more volatile than they were expected to be, than they should be and perhaps than they need to be (Frankel 1995). Exchange rate volatility creates special problem for international business activity (exporting and importing) because it creates a special kind of risk (foreign exchange risk). When business deals are arranged for the future, they are complicated by the increased risk of exchange rate changes (Evans Taylor &Holzman, 1985).

Uganda has experienced deterioration in terms of trade of which deprecation in exchange rate is one of the contributing factors. The Uganda shilling depreciated against the US dollar during most of the periods (1991-2013) and the trend may continue in the coming years (IFEM, 2004). This depreciation has got a great impact on the export performance.

Exporters expressed their concern over the exchange rate fluctuations in the year (2012) saying if the trend continues their industry will generally be affected in 2013 (National Bank of Uganda 2012). The Uganda shillings depreciated against the US dollar by over shs. 400/= leading to quarterly variations of 2200Shs, 2600Shs and 2900Shs in the first, second and third quarter respectively. This depreciation squeezed profitability in the export sector due to the fact that all exports are in foreign currency and sometimes on credit terms. Such receivable are either having a loss index or gain, which has a great impact on the cash flow forecasts.

When exporting firms quote the price of their goods in a foreign currency, they want to be sure of the receiving sufficient returns in their own currency to cover the costs of production and generate a reasonable profit. If in the meantime, the value of their own currency appreciates/ depreciates in terms of the other currency; they stand to make a loss on the transaction.

To guard against this inconsistence exporting firms develop strategies to either eliminate or reduce this currency risk, which is the major aim of foreign exchange risk management (Dawson &Rodney, 2002). Foreign Exchange Risk Management (FERM) is the process of measuring or assessing currency risk and then developing strategies to manage the risk. It deals with the systematic management of the risk of loss from exchange rate movements on international transactions. FERM minimizes quarter-to-quarter or year-to-year earning fluctuations stemming from currency fluctuations (Shapiro, 2003).

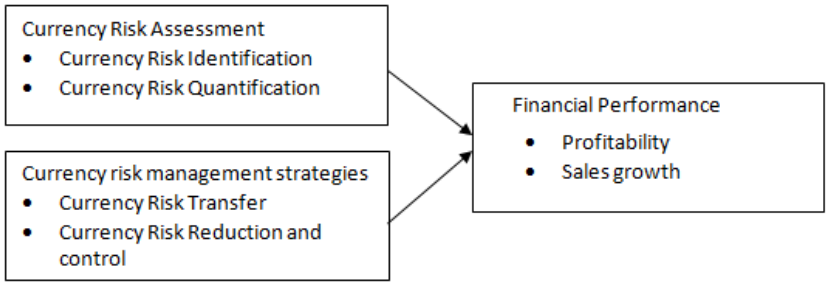
It looks forward to future cash flows and seeks to ensure that their value will be maintained when they occur. In other words it becomes an insurance against a decline in these cash flows (Evans et al, 1985). With foreign exchange risk management, the exporter's main goal is to ensure that proceeds from sales are not lower than the expected.

2. Theoretical And Conceptual Framework Of FERM And Performance

The conceptual framework was developed from of extensive review on existing literature. The model explains the relationship between the variables under study. It describes Foreign Exchange Risk management and financial performance.

2.1 The Conceptual Model

Foreign Exchange Risk Management (FERM) and Financial Performance

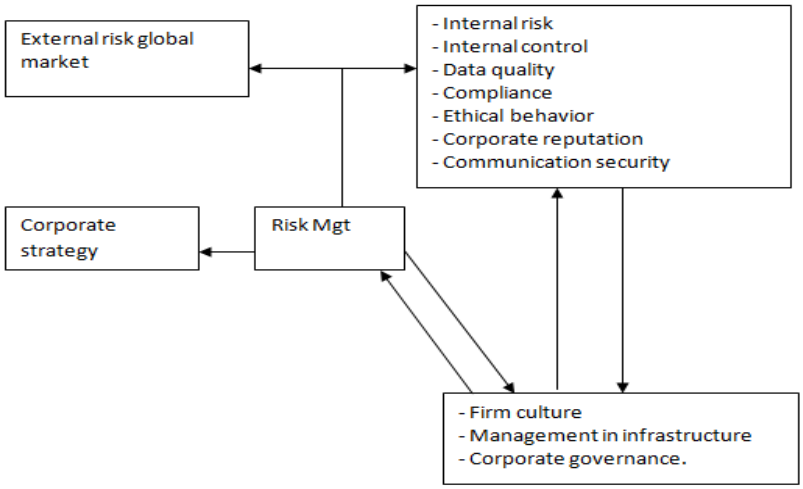


Firms should identify and quantify their exposure to currency risk, which is a basis for a suitable currency risk management strategy (Shapiro, 2003). According to Brain (2000) there is a variety of currency risk management strategies namely currency risk transfer, currency risk reduction and control or currency risk retention. The financial performance of export ventures can be examined basing on profitability and sales growth (Lages&Mantgomery,, 2004, Eatwell, 1971). Allayannis (2001), revealed a relationship between FERM and financial performance by noting that exporting firms that carry out Foreign exchange Risk management have been attaining higher returns than other firms.

2.2 Risk Management

According to international standards organization (ISO) 31000 risks is defined as the uncertainty on objectives whether positive or negative. Risk management is considered as the identification, assessment and prioritization of risks followed by a coordinated and economical application of resources to minimise monitor and control the probability and impact of unfortunate events.

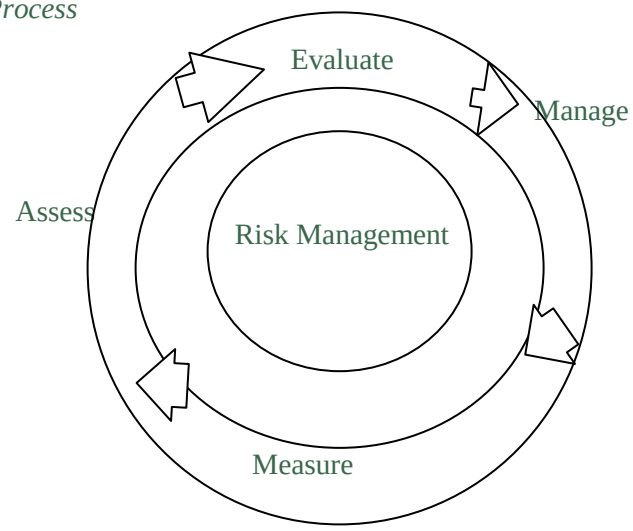
Risk Management Model



Source: Bentley university

According to John Alzak (2007) risk management is the identifying of risks, assessing the impact on the business of a security incident that occurs and making the right financial decision about how to deal with the result of the assessment. Risk management is an on going process which involves a number of stages. According to John Alzak (2007) risk management is a cycle that is composed of the following:

Risk Management Process



Source: John Alzak (2007)

2.3 Foreign Exchange Depreciation And Appreciation

This describes the movement of the exchange rate induced by market fluctuations. Currency appreciation this is when the value of the local currency increases with the respect to the foreign currency. And currency depreciation is when the value of the local currency loses value with respect to the foreign currency. These changes are driven by changes in demand and supply which also depends on the country's exports, imports, international financial transactions and speculations on foreign exchange market.

2.4 Foreign Exchange Risk Management

There has been little study on Foreign Exchange Risk Management and financial performance of exporting firm in developing courtiers. The literature reviewed in the study is cited mainly from studies carried out in developed countries in relation to its applicability in developing countries.

Exporting firms are businesses involved in international trade that is business activity, which extends beyond national boundaries (Taggert& McDermott (2000). Firms involved in international trade are subject to foreign exchange risk arising from payables and receivables in foreign currencies (Bradley & Moles, 2002). In international business two national currencies are naturally involved; the currency of the buyer and the

currency of the seller. One characteristic that distinguishes the international from the domestic transaction is the need to agree on which currency will be used (Evans et al, 1985).

2.5 Currency Risk Assessment

A firm must first define the exposure to loss from foreign exchange and decide whether it will attempt itself against the possibility of loss from exposure created by transactions denominated in other than domestic currency (Pritaman, Shomek&Singal, 2003).

2.6 Currency Risk Identification

According to Giddy and Dufey (2002), the first step in management of foreign exchange risk is to acknowledge that such currency risk does exist and managing it is in the interest of the firm. Firms should identify the nature and magnitude of foreign exchange exposure.

2.7 Currency Risk Quantification

After identification of the nature of exposure the second step is to quantity and gauges the impact of exchange rate changes by determining the amount or value at risk (Giddy &Defey 2002). Firms need to carry out exchange rate forecasts and determine the expected gain or loss; which must be compared with the predetermined goal. As might be expected, forecasts will be prepared for the currencies relevant to the firm's current and projected exposures and those currencies in which the firm has major operations.

2.8 Currency Risk Management Strategies

Due to volatility in exchange rates exporting firms have actively and creatively developed foreign exchange risk management strategies (Belk, 1998). Once a firm has identified and quantified its exposure to foreign exchange risk and determined the expected foreign exchange gain or loss, and concluded that it is not acceptable, it must take action. This action can be basically through the use of any currency risk management strategies under currency risk transfer, currency risk reduction and control or currency risk retention.

Currency risk transfer: Risk transfer means causing another party to accept the risk, typically by contract. In management of foreign exchange risk, this is through the concepts of hedging, insuring and diversification (Brian, 2000).

Forward contracts: Kakuru (2003) asserted that a forward contract involves an arrangement between two parties to exchange currencies or any other commodities at a future date and at a price determined today. The contract is based on a future price that is agreed in advance.

Currency futures: According to Van Horne (2002), the purpose of currency futures is to fix an exchange rate to avoid alterations in the future cash flows of the firm. A futures contract is essentially a standardized forward contract that is traded in an organized exchange.

Money market hedge: This is an alternative to a forward market hedge. It involves simultaneous borrowing or lending in two different currencies to lock in the home currency value of future foreign currency cash flows (Shapiro, 2003). In using a money market hedge, the company is expecting to receive income or make a payment in a foreign currency at a future date and intends to exchange it in domestic currency.

Swap contract: A swap is a contract between two counter parties who agree to exchange a stream of payments over an agreed period. The principle amount is exchanged, usually at a rate of exchange agreed upon in advance (Van Horne, 2002).

Currency option: According to Brian (2000) an option is an agreement between two counter parties. Giving the option the buyer or holder, the right but not the obligation, either to buy or sell a quantity of an item at fixed price, on or before a specified date in the future.

Diversification: According to Belk, Bidgood&Duangploy (1993) diversification is an important strategy to react against exchange rate changes, which affect the performance of many firms**.** Many companies such as Japanese auto producers are now seeking flexibility in production location, in part to be able to respond to large and persistent exchange rate changes that make production much cheaper in one location than another. Some of the diversification policies include; shifting of markets for output, shifting sources of supply, shifting product lines and production facilities as a defensive reaction to adverse exchange rate changes (Giddy &Defey, 2002).

3. Research Methodology

Across- section study design was used. This was combined with descriptive. Correlation and regression studies to establish the relationship between foreign exchange risk management and performance of exporting firms. Study units ware chosen using proportionate stratified sampling and simple random sampling to ensure that it comprises the entire firm's representation. Financial managers constituted of appropriate respondents because they are the ones who make decisions regarding foreign exchange risk management and are responsible for preparing

The population comprised of all manufacturing and agro processing exporting firms in Uganda. The study was drawn from two sectors of agriculture and manufacturing. The population consisted of more than 70 exporting firms, was determined Using Krejcie& Morgan (1970) to determine 51 firms.

Spearman's correlation was used to establish the relationship between FERM and performance and multiple regression analysis was used to determine the contribution of FERM on the dependent variable. Chi square tests, t-tests were used to examine the variability of foreign exchange risk management on the performance in the exporting industry.

4. Results Of The Study

Different constructs were used to establish the management of foreign exchange risk by exporting firms namely currency risk assessment and currency risk management strategies. Currency risk assessment was measured by two components of currency risk identification and currency risk quantification while currency risk management strategies were divided into currency risk transfer, currency risk reduction and control and currency risk retention. Frequencies, percentages and chi-square tests were used to establish the management of foreign exchange risk by exporting firms.

4.1 Currency Risk Identification

Currency risk identification is the first step in the process of managing foreign exchange risk. Respondents were asked to rate the following statements regarding the level of currency risk identification and Table 1 below shows their responses

Table 1: Response on Currency Risk Identification

			Manufacturing		**Agro processing**	
	Freq.	**Percent**	**Freq.**	**%**	**Freq.**	**%**
Not sure	8	15.7	6	26.1	2	7.1
Agree	37	72.5	16	69.6	21	75
Strongly agree	6	11.8	1	4.3	5	17.9
Total	**51**	**100.0**	**23**	**100.0**	**28**	**100.0**
Chi-squareX2 =12.56,d.f=4,p=0.000						

Source: Primary Data

X2 is the Chi-square d.f is the degree of freedom and P is the probability of success.

Most of the manufacturing exporters (74%) had a significant positive perception about foreign exchange risk identification compared to 26.1% who were not sure while about 93% of the agro processing exporters had a significant positive perception on foreign exchange risk identification compared to 7.1% who were not sure. This implies that exporters in the agro processing sector identify currency risk more than manufacturing exporters.

4.2 Currency Risk Quantification

Respondents were asked to rate the following statements regarding forecasting future foreign currency cash flows and whether they measure and report their exposure to foreign exchange risk. The findings are depicted in Table 2 and 3 below.

Table 2: Response on Future Foreign Currency Cash Flow Forecasts

	SA		**A**		**NS**		**D**		**SD**	
	Freq	**%**	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**
Monthly	2	3.9	25	49.1	3	5.9	18	35.3	3	5.9
Manufacturing	-	-	10	43.5	1	4.3	11	47.8	1	4.3
Agro processing	2	7.1	15	53.6	2	7.1	7	25.0	2	7.1
X^2=9.21,d.f=12,p=0.321										
Quarterly	1	2.0	13	25.3	4	7.8	31	60.8	2	3.9
Manufacturing	-	-	5	21.7	1	4.3	15	65.2	2	8.7
Agro processing	1	3.6	8	28.6	3	10.7	16	57.1	-	-
X^2=8.03,d.f=12,p=0.438										
Semi Annually	1	2.0	12	23.5	4	7.8	31	60.8	3	5.9
Manufacturing	-	-	5	21.7	1	4.3	15	65.2	2	8.7
Agro processing	1	3.6	7	25.0	3	10.7	16	7.1	1	3.6
X^2=10.65,d.f=12,p=0.218										
Annually	3	5.9	17	33.3	4	7.8	24	47.1	3	5.9
Manufacturing	1	4.3	8	34.8	1	4.3	12	52.2	1	4.3
Agro processing	2	7.1	9	32.1	3	10.7	12	42.9	2	7.1
X^2=11.32,d.f=16,p=0625										

n=51

Source: Primary Data

Results in Table 2 above show that there were no significant differences among the manufacturing and agro processing exporting firms regarding currency risk quantification through future foreign currency cash flow forecasts (p-values>0.05). Most exporters (53%) carry out future foreign currency cash flow forecasts monthly. However, exporters in agro processing sector (60.7%) forecasts foreign currency cash flow monthly and more often than those in the manufacturing sector (53.5%). Very few exporters forecast future foreign currency cash flow on quarterly, semi annual and on annual basis. This meant that exporters carry out currency risk quantification through currency forecasts but on a monthly basis.

4.3 Currency Risk Transfer

Currency risk transfer is another construct of Foreign Exchange Risk Management Respondents were asked to rate the following statement regarding the use of currency risk transfer and Table 3 below reveals the findings:

Table 3: Response on Use of Currency Risk Transfer Technique

	SA		**A**		**NS**		**D**		**SD**	
	Freq	**%**	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**	**Freq**	**%**
Forward Contract (FC)Combined	**2**	**3.9**	**30**	**58.8**	**7**	**13.7**	**12**	**23.5**	**-**	**-**
Manufacturing	-	-	10	43.5	4	17.4	9	39.1	-	-
Agro processing	2	7.1	20	71.4	3	10.7	3	10.7	-	-
X^2=23.12,d.f=2,p=0.416										
Currency Future(CF)	**1**	**2.0**	**12**	**23.5**	**11**	**21.6**	**27**	**52.9**	**-**	**-**
Manufacturing	-	-	3	13.0	5	21.7	15	65.2	-	-
Agro processing	2	3.6	9	32.1	6	21.4	12	42.9	-	-
X^2=32,d.f=4,p=0.280										
Currency Options(CO)	**2**	**3.9**	**12**	**23.5**	**11**	**21.6**	**26**	**51**	**-**	**-**
Manufacturing	-	-	5	21.7	3	13.0	15	65.2	-	-
Agro processing	2	7.0	7	25.0	8	28.6	11	39.3	-	-
X2=12.67,d.f=4,p=0.724										

Insurance contract(IC)	-	-	3	5.9	7	13.7	40	78.4	1	2.0
Manufacturing	-	-	1	4.3	4	17.4	18	78.3	-	-
Agro processing	-	-	2	7.1	3	10.7	22	78.6	1	3.6
X^2=21.00,d.f=4,p=0.182										
Swap Contract(SC)	**1**	**2**	**11**	**21.6**	**10**	**19.6**	**27**	**52.9**	**1**	**2.0**
Manufacturing	-	-	5	21.7	6	26.1	12	52.2	-	-
Agro processing	1	3.6	6	21.4	4	14.3	15	53.6	1	3.6
X^2=16.46,d.f=4,p=0.357										
Money Market Hedge	**4**	**7.8**	**12**	**23.5**	**4**	**7.8**	**30**	**58.9**	**1**	**2**
Manufacturing	-	-	7	30.4	1	4.3	15	65.2	-	-
Agro processing	4	14.3	5	17.9	3	10.7	15	53.6	1	3.6
X^2=19.00,d.f=4,p=0.821										
Diversification(DC)	**-**	**-**	**-**	**-**	**4**	**7.8**	**44**	**86.3**	**3**	**5.9**
Manufacturing	-	-	-	-	2	8.7	20	87.7	2	7.1
Agro processing	-	-	-	-	2	7.1	24	85.7	2	7.1
X^2=24.12,d.f=2,p=0.071 n=51										

Source: Primary Data

Results in Table 3 above indicate that there were no significant differences among exporting firms in regard to use of currency risk transfer techniques (p-values>0.05. Most of the exporters (62.7%) use forward contracts as a risk transfer technique unlike 25.5% who use currency future, 27.4% that use currency option, 5.9% who use insurance contracts, 23.6% who use swap contracts, 31.3%who use money market hedge and non (0%) use diversification as a risk transfer technique. Comparing exporters in the manufacturing and agro processing sector, 78.5% of the agro processing exporters use forward contracts compared to 43.5% of the manufacturing exporters.

4.4 Currency Risk Reduction And Control

Currency risk reduction and control is an attribute of Foreign Exchange Risk Management. Respondents were asked to rate the following statements regarding the use of currency risk educational and control techniques as shown in the Table 4 below

Table 4: Response on use of Currency Risk Reduction and Control Techniques

Leading	1	2.0	13	25.5	1	2.0	34	66.7	2	3.9
Manufacture	1	4.3	5	26.1	1	4.3	14	60.9	1	4.3
Agro processing	-	-	7	25.0	-	-	20	71.4	1	3.6
X2 = 26.23,d.f.= 4, p =0.182										
Lagging	1	2.0	12	23.5	1	2.0	34	66.7	3	5.9
Manufacturing	1	4.3	5	21.7	-	-	16	69.6	1	4.3
Agro processing	-	-	7	25.0	1	3.6	18	64.3	2	7.1
X2 = 24.23, d.f = 2, p = 0.064										
Matching	3	5.9	30	58.8	-	-	17	33.3	1	2.0
Manufacturing	-	-	13	56.5	-	-	10	43.5	-	-
Agro processing	3	10.7	17	60.7	-	-	7	25.0	1	36
X2 = 18.21, d.f = 4, p = 0.052										

Source: Primary data

Results form Table 4 above show that there were no significant differences among exporting firms towards the use of currency risk reduction and control strategies (p-values>0.05). Exporters in both sectors (64.7%) preferred the use of matching technique to leading and lagging (27.5% and 25.5) respectively. Agro processing exporters high preferred the matching strategy as indicated by 71.4%than the manufacturing exporters with 56.5%.

4.5 Currency Risk Retention

The study was interested in finding out whether exporting firms may decide to adopt currency risk retention strategy as a way of managing foreign exchange risk and the results are shown in Table 5below.

Table 5: Response on use Currency Risk Retention strategy

	Combined		Manufacturing		Agro Processing	
	Freq.	**Percent**	**Freq.**	**Percent**	**Freq**	**Percent**
Strongly Disagree	1	2.0	1	4.3	-	-
Disagree	39	76.4	18	78.3	21	75
Agree	11	21.6	4	17.4	7	25.0
Total	51	100.0	23	100.0	28	100.0
X2 = 23.65, d.f = 0.26						

Source: Primary Data

Results in Table 5above indicate that there was significant difference among exporting firms in regard to use of currency risk retention strategy (p-value<0.05). Most of the exporters (78.4%) denied the use of currency risk retention strategy to manage foreign exchange risk compared to 21.6% who had a positive response. Comparing both sector, 82.6% of the agro processing exporters denied the use currency risk retention, compares to 75% of manufacturing exporters. 17.4% of the exporters in the manufacturing sector and 25% of exporters in the agro processing had a positive response towards the use of currency risk retention strategy to manage foreign exchange risk. The findings above clearly show that exporters in both sectors do not adopt a risk retention strategy toward Foreign Exchange Risk.

Table 6: T-Test of Foreign Exchange Risk Management

	Sector	**N**	**Mean**	**F**	**Sig**	**T**	**Df**	**Sig. (-.)**
Risk Identification	Manufacturing Agriculture	23 28	3.7826 4.1071	.838	.365	-2.275	49	.0135
Risk Quantification	Manufacturing Agriculture	23 28	2.8261 3.0000	.407	.407	-.287	49	.102
Forward Contracts	Manufacture Agriculture	23 28	3.0435 3.7500	5.286	5.286	-3.003	49	.002
Currency Future	Manufacturing Agriculture	23 28	2.4783 2.9643	2.948	2.948	-1.996	49	.026
Currency Option	Manufacturing Agriculture	23 28	2.5652 3.0000	.123	.123	-1.676	49	.05
Swap Contracts	Manufacturing Agriculture	23 28	2.2609 2.2143	.017	.017	.280	49	.03905

Money Market Hedge	Manufacturing Agriculture	23 28	2.6957 3.0000	2.065	2.065	-.677	49	.2505
Diversification	Manufacturing Agriculture	23 28	2.6522 3.5714	2.214	2.214	-1.129	49	.132
Leading	Manufacturing Agriculture	23 28	2.0435 2.0000	.059	.218 .726	.410	49	.342 .252
Lagging	Manufacturing Agriculture	23 28	2.6522 2.4643	1.557	.658	.205	49	.4195
Matching	Manufacturing Agriculture	23 28	2.5217 2.4643	.124	.676	-1.233	49	.112
Risk Retention	Manufacturing Agriculture	23 28	3.1304 3.5000	.198	.143	-1.240	49	.1105

Source: Primary Data

Results in the t-test Table 6 above indicate that there were difference in currency risk identification, us of forward contracts, currency futures, currency options, and insurance contracts among the manufacturing and agro processing exporters (t-sig. Values<0.05). This implied that manufacturing and agro processing exporters differed significantly I their perceptions in regard to currency risk identification and use of forward contracts, currency futures, currency options and insurance contracts. t-test Table 6 above further reveals that there were no differences in perceptions of the manufacturing and agro processing exporters in regard to currency risk qualification and use of swap contracts, money market hedge, diversification, leading, lagging, matching and risk retention (t-sig. Values> 0.05).this implies that exporters had similar perceptions in regard to currency risk quantification, use of swap contracts, money market hedge, diversification, leading, lagging, matching and risk retention as currency risk management strategies.

4.6 Relationship Between FERM And Performance Of Exporting Firms

The degree of relationship was determined by Spearman correlation coefficient and the predictability of performance of exporting firms was determined through regression analysis.

Spearman Correlation Coefficient

Spearman correlation coefficient was used to determine the degree of relationship between FERM and performance. The relationship was established by running independent variables against the dependent variable that is Currency risk assessment (CRA), currency risk transfer (CRT), currency risk reduction and

control (CRRC) and currency risk retention (CRR) against Gross Profit Margin (GPM), Net Profit Margin (NPM), Selling General and Administration expenses to sales (SG & A) and Sales Growth (SG) as shown in Table 10 below.

Table 7: Spearman Correlation Matrix

Variable	1	2	3	4	5	6	7	8
CRA (1)	1.000							
CRT (2)	-.216	1.000						
CRRC(3)	-.083	.063	1.000					
CRR(4)	.406	-.479	..28	1.000				
GPM(5)	.404**	.347**	.341**	.406	.1,000			
NPM(6)	.415**	.407**	.390**	.318**	.321**	1,000		
SG & A (7)	.207**	.432**	.342**	.311**	.474**	.231**	1.000	
SG (8)	.351**	.388**	.388**	.307**	.363**	.267	-.350**	1.000

**. Correlation coefficient significant at 0.01 levels (2-tailed)

Table 7 above reveals that there was a positive and significant relationship between currency risk assessment and Gross profit margin (r = 0.405; p-value<0.01, net profit margin (0.415; p-value<0.01, selling general and administrative expenses to sales (r=0.2.7; p-value<0.01) and sales growth (r=0.315; p-value<0.01) of exporting firms in Uganda. This implied that as exporting firms carried out an assessment of their exposure to currency risk, a higher gross profit margin, net profit margin and sales growth was realized while selling, general and administrative expenses to sales reduced.

Exporting firms in Uganda had a significant and positive relationship between currency risk transfer strategies and gross profit margin (r=0.347; p-value < 0.01), net profit margin (r=0.407; p-value < 0.01), SG & A expenses to sales (r=0.342; p-value. < 0.01) and sales growth (r=0.388; p-value < 0.01) this implied that the use of currency risk transfer strategy influences the performance of exporting firms in Uganda. Hence proper use of currency risk transfer techniques is likely to protect gross profit margin, gross profit margin, net profit margin and sales growth and cut down their selling, general and administrative expenses to sales.

Exporting firms had a weak positive relationship currency risk retention and gross profit margin (r = 0.406; p-value < 0.01). net profit margin (r = 0.318; p- value < 0.01), SG & A expenses to sales (r = 0.406; p-value \, 0.01, and sales growth of exporting firms (r = 307; p- value < 0.01). This implied that there is a relationship between currency risk retention and financial performance of exporting firms but of a very low magnitude.

Therefore, when exporting firms decide to retain currency risk their gross profit margin, net profit margin and sales growth is likely to improve.

5. Discussion, Conclusions And Recommendations

Exporting firms identified that foreign exchange risk as a problem to their businesses. However, exporters in the agro processing sector identify foreign exchange risk more than manufacturing exporters. This is because Agriculture exporting firms mostly survive on exporting business and their exposure to exchange rate risk is high due to high levels of foreign currency sales compared to manufacturing exporting firms.

Results also indicate that exporting firms carry out currency risk quantification through forecasting foreign currency cash flows and measuring and reporting their exposure to foreign exchange risk on a monthly basis in order to asses how much value is exposed to foreign exchange risk. Findings on the adoption of currency risk management strategies reveal that exporting firms use all the different categories of currency risk transfer, currency risk reduction and control and currency risk retention strategies. Matching strategy is also a convenient currency risk management strategy to exporting firms because when the exchange rate of two currencies are positively correlated a firm can offset in long position in one currency with a short positioning the other (Flynn, 2003). Most of the firms denied the adoption of currency risk retention strategy towards foreign exchange risk.

The research results further revealed that exporting firms had similar perceptions in regard to currency risk quantification, use of currency risk management strategies namely swap contracts, money market hedge4, diversification, leading, lagging, matching and risk retention as currency risk management strategies. These findings are supported by Belk (2002) assertion that firms differ in their identification of foreign exchange risk but all need to quantify and ascertain how much value is exposed to foreign exchange risk. This helps them to choose van appropriate currency risk management strategy. Also, ideal use of currency risk management strategies may not be possible. Some of them may involve trade offs that are not acceptable to the organization or person making foreign exchange risk management decisions.

5.1 Conclusion

Exchange rate volatility has complicated the exporting business. Exporting firms adopt Foreign Exchange Risk Management as solution to these volatile exchange rates because of their impact on firm's financial performance. To most firms the objective of Foreign exchange risk management is to protect funds, which a company possesses or can expect in the near future. FERM is carried out purposively to minimize quarter-to-quarter or year-to-year earnings fluctuations stemming from currency movements.

5.2 Recommendations

Basing on the study findings, the following recommendations are suggested.

1. Exporting firms should develop a Foreign Exchange Risk Management framework, which clearly shows their currency risk assessment procedure and implementation of currency risk management strategies. This should be monitored and make adjustments as necessary.
2. An organized exposure management function is very necessary this will enable firms to:
   - To have a procedure which deals with Foreign Exchange Risk Management,
   - Involve operating departments in the FERM program
   - Identify people responsible for making FERM decisions
   - Have a FERM goal, which is fixed in writing and communicated to the responsible staff.
3. Exporting firms should emphasize the use of currency risk transfer strategies through hedging, insuring and diversification of foreign exchange risk. These are the most commonly recognized currency risk management strategies. With currency risk transfer strategies the risk is completely transferred.

5.3 Areas For Further Research

The study concentrated on foreign exchange risk management and financial performance of exporting firms however, a similar study can be carried out in Multinational corporations and the Banking sector because foreign exchange risk is identified as one area of risk created by their international operations.

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