



# MANAGING TRADE PAYMENTS AND FX IN GLOBAL MARKETS

Middle Eastern Economies

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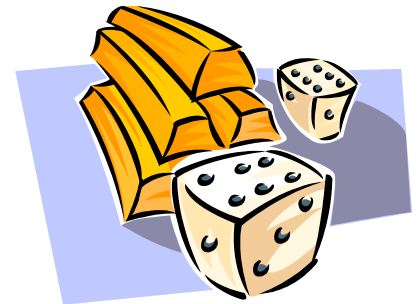
# Domestic Business becomes Global Business

- ❑ Global integration of supply chain
- ❑ Market Diversification, finding the strong economy
- ❑ Determine best vendor within global marketplace
- ❑ Reduce trade deficit



# Risks in International Trade

- ❑ Can I trust my overseas vendor / customer?
- ❑ When will I receive payment? Before or after shipment?
- ❑ Am I guaranteed to receive what I ordered?
- ❑ What currency will I pay / receive in?
- ❑ How stable / volatile is the market?



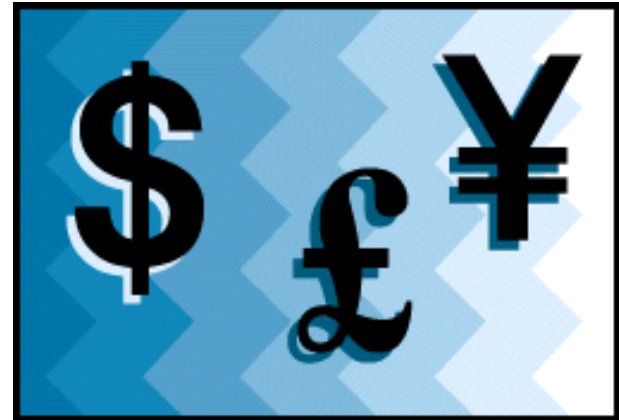
# Why pay in foreign currency?

## Benefits

- Pay “true” price of product
- Control the payment
- Incentive to supplier
- Price Stability

## Disadvantages

- Unavailability of funds
- USD cost instability



# Why export in foreign currency?

## Advantages

- Offer stable price to customer
- Expand market share
- Tailor sale to customer needs
- Possible gains in exchange
- Control of hedge



## Disadvantages

- Determining invoice rate
- Possible loss in exchange without hedge

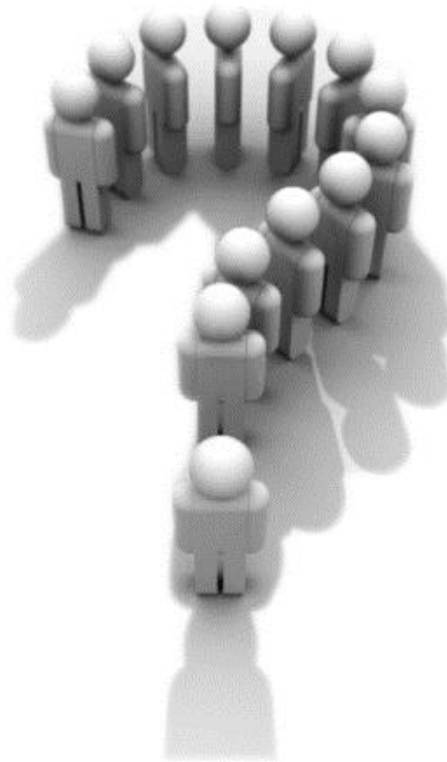
# Current Market Trends

- Central Bank Intervention
  - ▣ Trend in central banks trading their currency to make to give their country a boost to exports
- Low interest rates
  - ▣ Historically low rates aimed at boosting borrowing
- Slow recovery
  - ▣ Jobless claims are still very high in US and Europe.
  - ▣ Many economies' GDP remains low
- Political Uncertainty
  - ▣ US talks in resolving potential Syrian conflict allowed for USD depreciation (USD rises with political instability)



# KYC / Compliance

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# Wire Transfers - Travel Rule

## Transparency in payments

- Complete disclosure of ordering party and beneficiary information
- IBAN
- BSA
- OFAC Checks





# Mechanics of Currency Movement

1. Customer currency request
2. Bank sells funds
3. Customer provides payment instructions
4. Bank sends SWIFT message to their foreign correspondent requesting them to send the funds to beneficiary's bank

Note: Currency is always held in its home country.

*Customer* ➡ *Local Bank* ➡ *Foreign Correspondent Bank* ➡  
➡ *Beneficiary Bank* ➡ *Foreign Beneficiary!*

# Avoiding Fraudulent Transactions

## Common Scenarios in International Transactions

- Check in, foreign wire out
- Foreign vendor suddenly changes wiring instructions
- Foreign vendor falsifies shipment
- Additional tax or freight fees to be paid via wire
- Email hacking, financial information request
- Online banking transactions – require RSA token
- Your long, lost uncle died in Africa with millions.....

# POP QUIZ!!!

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Immediately after depositing a check drawn on a foreign bank, it's accurate to assume that the funds are available for use???

# Middle Eastern Market

## Middle East Economy consists of:

Bahrain, Cyprus, Gaza, Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Northern Cyprus, Oman, Palestine, Qatar, Saudi Arabia, Syria, United Arab Emirates and Yemen.

Turkey: border of EU and ME





# Geographies and Challenges

## □ Geography & People

- Middle east population is over 190 million
- Gulf Cooperation Council (GCC) - Cooperation of 6 member states to advance collectively in economic growth, education, scientific research and culture
  - Accounts for 20% of ME population and more than 60% of GDP
  - GCC Countries: UAE, Saudi Arabia, Bahrain, Oman, Qatar and Kuwait
  - GCC Currencies / Oil price pegged to USD

## □ Banking Environment

- Payment industry is young and undeveloped outside of the GCC.
- Level of development varies greatly by country.
- Most transactions still executed in Cash.
- Number of Annual Non-Cash transactions per capita: US=352, UAE=20, Saudi Arabia=9.5, Jordan=3



# Islamic Banking

- Sharia - Islamic law and jurisprudence, Sharia rules are derived from the *Quran* and the *Sunnah* (the practices and traditions of the Prophet Muhammad), governing all economic, political, social and cultural aspects.
- All contracts and transactions involving Islamic banks should be **Sharia-compliant**.
- **Core elements** are the prohibition of interest, speculation, gambling, uncertainty, alcohol, pork, unjust enrichment and other unethical purposes.
- Money has **no intrinsic value** and is just a medium of exchange as well as a way of defining value.
- Money is **not a commodity** which can be bought, sold, borrowed or lent and should not be an income-generating asset in itself and trading in debt is prohibited.
- Islamic Finance is commonly thought “**interest-free banking**” and mainly “**asset-based**”
- Approx. 500 Islamic banks in more than 55 countries, whose Sharia-compliant assets can be roughly estimated with USD 700 billions.
- Highest concentration of Islamic banking activities can be found in the Gulf-Region (GCC-Countries) and the Islamic countries in Asia (notably Malaysia and Indonesia).

# US-Middle East Trade Statistics

## Saudi Arabia

- Saudi Arabia is currently the 12<sup>th</sup> largest goods trading partner with \$73 BN total in total trade
  - ▣ 2012 Imports: \$55 BN
  - ▣ 2012 Exports: \$18BN
  - ▣ Trade Deficit: \$37 BN
- Largest import groups from Saudi Arabia are: Oil (46.2 billion), Organic Chemicals, Fertilizers, and Steel





# Trade Statistics con't...

## ISRAEL



- Israel is currently the 26<sup>th</sup> largest goods trading partner with \$36Bn total in total trade of goods.
  - ▣ 2012 Imports: \$22Bn
  - ▣ 2012 Exports: \$14Bn
  - ▣ Trade Deficit: \$8Bn
- Largest import groups from Israel are: Precious Stones, Pharmaceuticals, Electric machinery, Medical Equipment



# Trade Statistics con't...



## Turkey

- United States' 21<sup>st</sup> largest goods export market
- World's 17<sup>th</sup> largest economy
- Top exports to Turkey are: Aircrafts, Iron and Steel, Oil, Cotton, and Machinery.
  - ▣ 2012 Imports: \$ 6BN
  - ▣ 2012 Exports: \$12BN
  - ▣ Trade Surplus: \$ 6BN
- Largest import groups from Turkey are: Vehicles, Machinery, Iron and Steel, Stone Plaster and Cement. Agriculture products like fruit and vegetables.



# Trade Statistics con't...



## UAE

- Federation of seven emirates Abu Dhabi, Dubai, Sharjah, Ajman, Umm Al-Qaiwain, Fujairah, and Ras Al-Khaima founded in 1971
- Over the last 38 years, the UAE has developed into the second largest economy in the Arab world
- Primary export market is Japan
- 34<sup>th</sup> largest goods trading partner with the USA, \$24BN in trade
  - ▣ 2012 Imports: \$ 2BN
  - ▣ 2012 Exports: \$22BN
  - ▣ Trade Surplus: \$20BN
- Largest import groups from UAE are: Aluminum, Oil, Iron and Steel, Precious Stones (diamonds)



# A Snapshot of the Currencies

USD/ILS 3.6445

Israeli Shekel

USD/KWD\*\*\* 0.2850

Kuwaiti Dinar

USD/AED\*\* 3.6660

United Arab Emirates Dirham

USD/BHD\*\* 0.3760

Bahraini Dinar

USD/TRY 2.028

Turkish Lira

USD/SAR\*\* 3.7501

Saudi Arabian Riyal

USD/QAR\*\* 3.6400

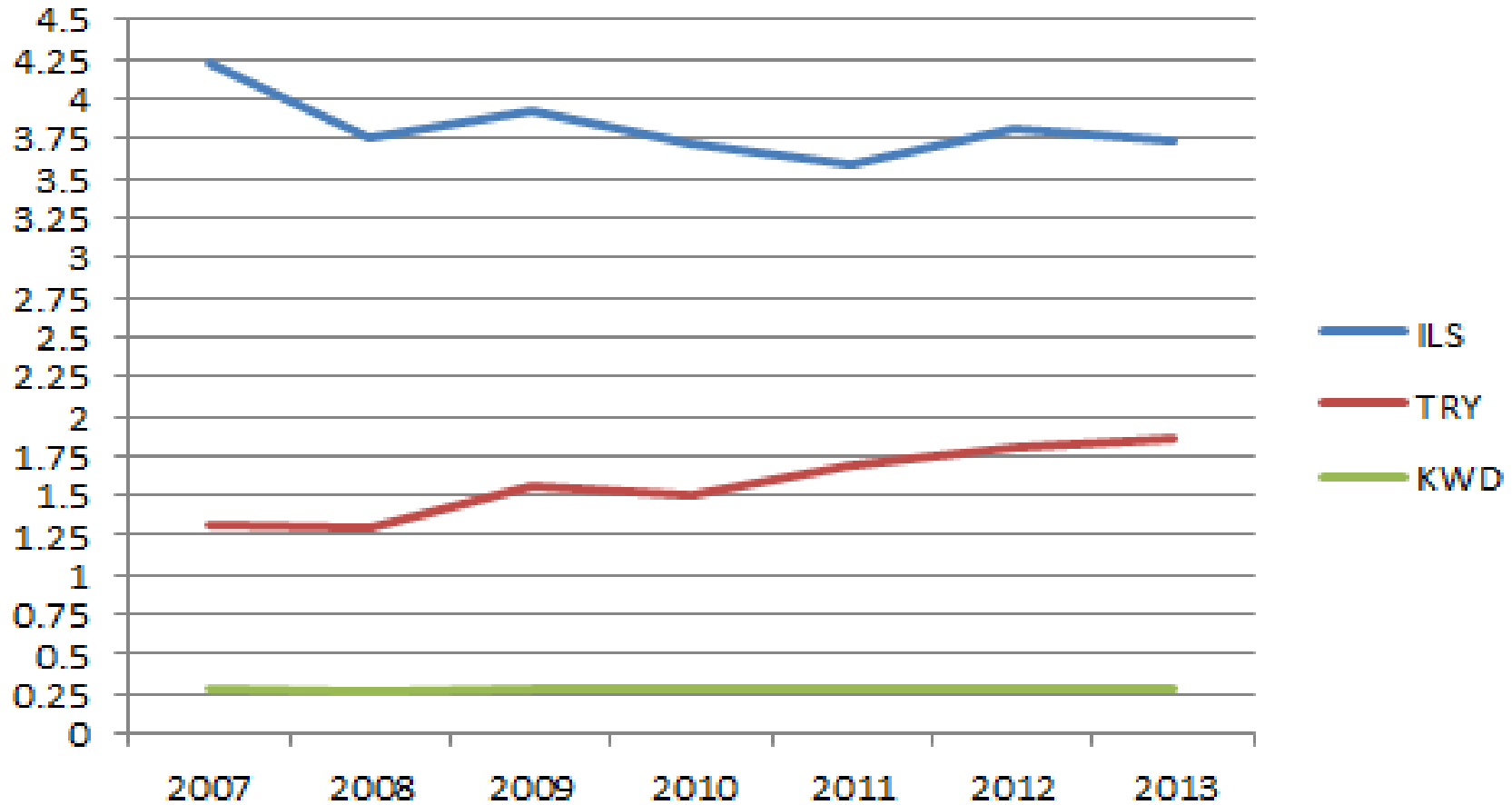
Qatari Riyal



\*\* Pegged to USD

\*\*\* Pegged to basket of currencies

# 5-Year Historical Chart of ILS, TRY, KWD



# POP QUIZ!!!

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What is the currency of  
Saudi Arabia???

# FX Basics



# Overview of Foreign Exchange

- Largest financial market in the world.
- Approximately \$4 trillion dollars (USD) are traded daily.
- Supply and demand market with currencies traded 24-hours, six days a week.
- On average, exchange rates change every *4.8 seconds*.





# Standard Exchange Rate Format

**EUR/USD**  
**1.3315**  
**0.7510**

**GBP/USD**  
**1.5815**  
**0.6323**

**AUD/USD**  
**0.9273**  
**1.0783**

**NZD/USD**  
**0.8148**  
**1.2273**

**USD/CAD**  
**1.0310**  
**0.9699**

**USD/CHF**  
**0.9286**  
**1.0768**

**USD/JPY**  
**0.9923**  
**1.0077**

**USD/CNY**  
**6.1082**  
**0.1637**

# What factors affect exchange rates?

- Political
- Market Psychology
- Economic



*The Yin and Yang of the Currency Markets*



# Economics....

## Interbank Interest Rates

- Relative Growth & Relative Interest Rates
- Return to conventional fundamental that drives currency values



### World Interest Rates

|             |       |
|-------------|-------|
| US          | 0.25% |
| Japan       | 0.10% |
| EU          | 0.50% |
| G. Britain  | 0.50% |
| Switzerland | 0.00% |
| Canada      | 1.00% |
| Australia   | 2.50% |
| N. Zealand  | 2.50% |
| China       | 6.00% |

# POP QUIZ!!!

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What is the major  
economic factor affecting  
exchange rates???

# Market Players

Who is affected by the foreign exchange market?

## Indirectly

- All consumers

## Directly

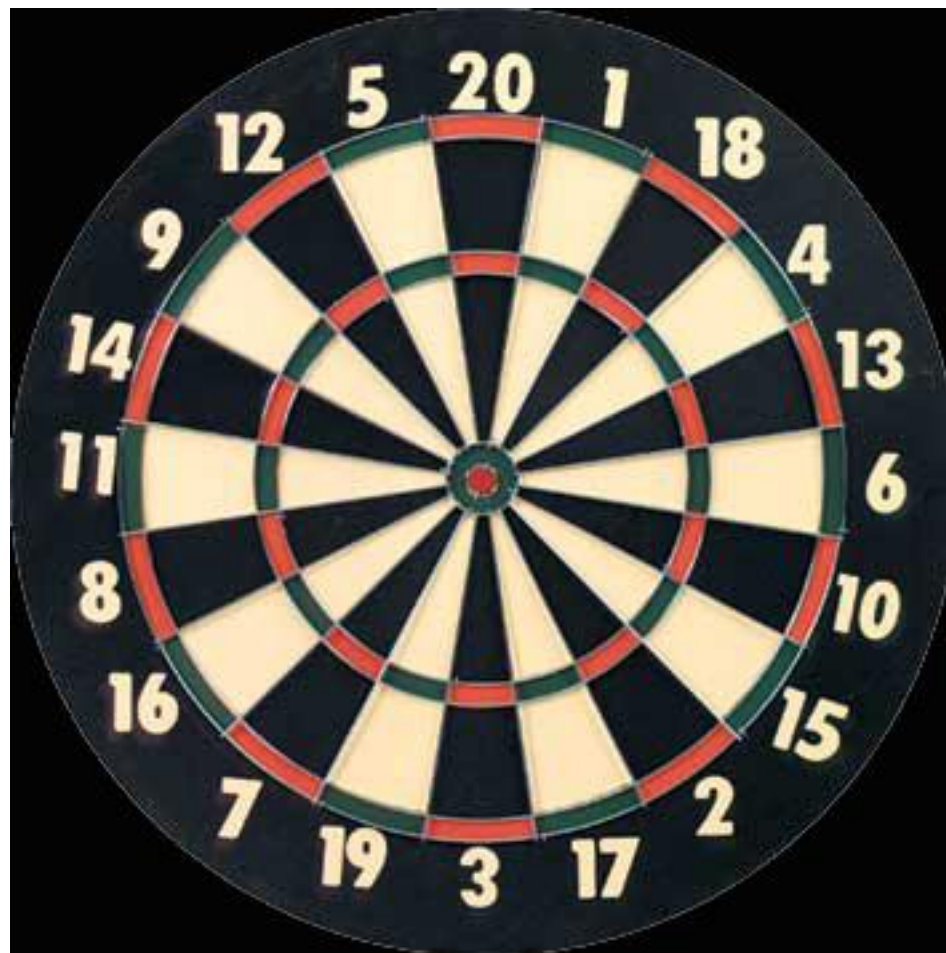
- Banks
- Importers and Exporters
- Traders and Investors
- Governments



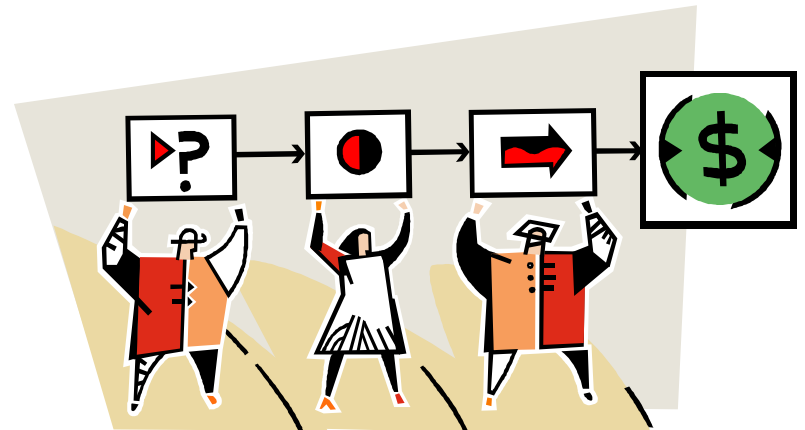
## 5 Year Volatility Trend

| *Based<br>on year-<br>end<br>rates | ‘07–‘08<br>% Change | ‘08–‘09<br>% Change | ‘09–‘10<br>% Change | ‘10–‘11<br>% Change | ‘11–‘12<br>% Change | Average<br>YOY<br>Volatility |
|------------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|------------------------------|
| <b>AUD</b>                         | <b>-18%</b>         | <b>26%</b>          | <b>14%</b>          | <b>0%</b>           | <b>2%</b>           | <b>5%</b>                    |
| <b>GBP</b>                         | <b>-27%</b>         | <b>11%</b>          | <b>-4%</b>          | <b>0%</b>           | <b>5%</b>           | <b>-15%</b>                  |
| <b>EUR</b>                         | <b>-4%</b>          | <b>2%</b>           | <b>-7%</b>          | <b>-3%</b>          | <b>2%</b>           | <b>-10%</b>                  |
| <b>CAD</b>                         | <b>-17%</b>         | <b>16%</b>          | <b>6%</b>           | <b>-2%</b>          | <b>3%</b>           | <b>9%</b>                    |
| <b>CHF</b>                         | <b>6%</b>           | <b>3%</b>           | <b>11%</b>          | <b>0%</b>           | <b>3%</b>           | <b>5%</b>                    |
| <b>JPY</b>                         | <b>26%</b>          | <b>5%</b>           | <b>15%</b>          | <b>5%</b>           | <b>-11%</b>         | <b>12%</b>                   |
| <b>CNY</b>                         | <b>0%</b>           | <b>0%</b>           | <b>4%</b>           | <b>4%</b>           | <b>1%</b>           | <b>2%</b>                    |
| <b>SGD</b>                         | <b>0%</b>           | <b>2%</b>           | <b>10%</b>          | <b>-1%</b>          | <b>-6%</b>          | <b>2%</b>                    |
| <b>NOK</b>                         | <b>-22%</b>         | <b>20%</b>          | <b>-2%</b>          | <b>-2%</b>          | <b>-8%</b>          | <b>-3%</b>                   |
| <b>SEK</b>                         | <b>-18%</b>         | <b>10%</b>          | <b>8%</b>           | <b>-2%</b>          | <b>6%</b>           | <b>9%</b>                    |
| <b>MXN</b>                         | <b>-19%</b>         | <b>7%</b>           | <b>2%</b>           | <b>-13%</b>         | <b>9%</b>           | <b>10%</b>                   |

# Forecasting Exchange Rates



# Risks and Solutions in Foreign Currency





# Risks in Multiple Currency

## ***Transaction Risk:***

Short term risk on foreign-denominated payables and receivables

## ***Translation Risk:***

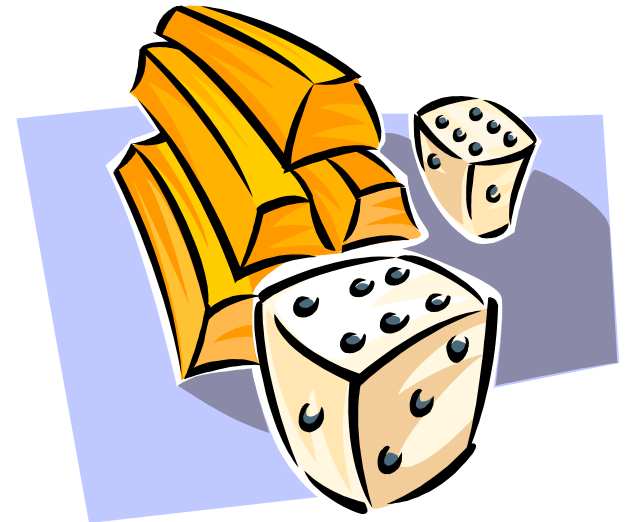
Longer term risk on foreign-denominated assets and liabilities (balance sheet conversion)

## ***Economic Risk:***

Business / competitive risk

# Risk Aversion Strategies

- Defining currency risk
- Quantifying financial impact
  - Worst case scenario
- Create corporate strategy
  - FX vs. USD
  - Spot vs. Forwards
  - Partial cover vs. full cover
- Use hedging tools



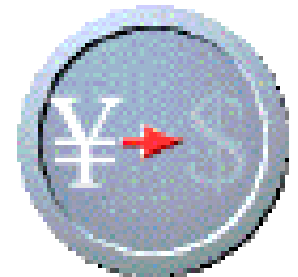
# EXAMPLE

A US company is importing widgets from a Chinese company. CNY is strengthening against USD.

Price: CNY 100,000/widget      90 day payment terms

10/11   CNY 6.39 = 1 USD   \$15,650

01/12   CNY 6.30 = 1 USD   \$15,870



CNY Payment – importer pays \$220 per unit

# HEDGING

Elimination or reduction of risk through the use of forwards or options (derivatives). May sacrifice opportunity gain in order to reduce risk.

## *Why companies hedge?*

- Uncertainty about FX markets and forecasts
- Secure USD payable
- Risk aversion

## *Why companies don't hedge?*

- Misconceptions..., Hedging = Speculation
- Lack of understanding of risks and methods of hedging

# Hedging Tools

- Forward Contract: Contract to buy or sell a currency for a fixed rate and specific date(s) in the future.
- Option – Insurance against rising market (pay premium)
- Participating Forward: 50% forward contract; 50% option
- Zero Cost Collar: Range of rates set for future currency obligation

# When To Use Forwards

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- **Foreign cash flow is certain**
- **Known settlement date or range of dates**
- **Regular payments or receipts**
- **Need protection against declining USD (importer) or declining FX (exporter)**
- **Necessity to secure USD cost for forecasted income**

# Import Example

A US company is sourcing engine parts from a German supplier. The German co. does not accept USD and invoices only in EUR prices.

EUR is strengthening against USD. The company needs to order 400 units at EUR 250 per unit.

**EUR 100,000**

**90 day payment terms**

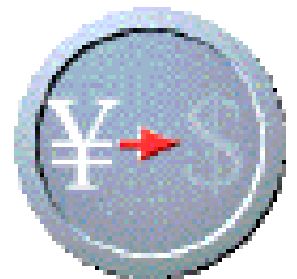
**Payment Order: 3/12 EUR/USD 1.32**

**USD 132,000 equivalent**

**Accts. Payable: 6/12 EUR/USD 1.35**

**USD 135,000 equivalent**

**- Transaction Risk: loss of \$3,000**



# Export Example

A US company is selling tractors to an agricultural firm in Canada. The Canadian company requests only CAD billing.

USD is strengthening against CAD. The US company is going to sell 5 units at CAD 25,000 per tractor. They need to protect the incoming payment.

**CAD 120,000**

**60 day payment terms**

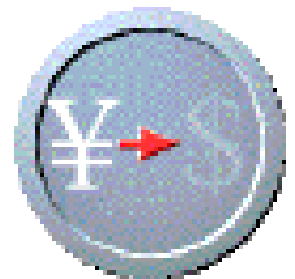
**Payment Order: 3/12 USD/CAD .98**

**USD 122,448.98 equivalent**

**Accts. Receivable: 5/12 USD/CAD 1.01**

**USD 118,811.89 equivalent**

**- Transaction Risk: loss of \$3,637**





# POP QUIZ!!!

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What are some hedging  
tools available to  
importers/exporters???

# Tips



- ❑ Be proactive, not reactive
- ❑ Be aware of market factors
- ❑ Use all tools available
- ❑ Prepare for markets to turn
- ❑ Don't panic



*As an international trader, you are playing a role in creating a stable, global economy!*

*NAMASTE*

**Tak**

**Xie xie**

**Merci**

**Grazie**

**Kamsa hamnida**

**Danke**

**Arigato**

**Gracias**

**Doje**

*Thank you!*

**Spasibo**

**Fulton International Group**

*Bringing our global reach to  
your local markets.*

