Growing a business

How to reduce the impact of FX changes

If you're trading in the international marketplace as an importer, exporter or both and invoice in a foreign currency, then foreign exchange (FX) fluctuations will affect the Canadian dollars you pay or receive.

As an exporter you may receive more (or less) Canadian dollars for your exports, as an importer you may pay less (or more) for your imports.

Any strong movement affecting either currency, in any direction, would have significant consequences on your profit margins.

What influences exchange rates?

The first step towards protecting your business against FX fluctuations is understanding what factors influence exchange rates. Regularly keep track of what's happening in the international markets. Check the RBC Economics page for;

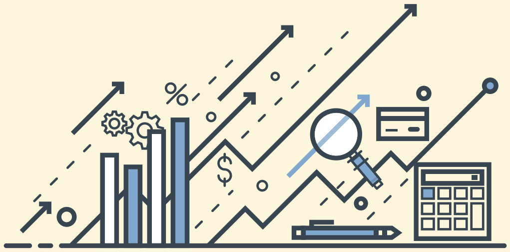
- Economic policies in the countries you're exporting to, such as interest rate changes and quantitative easing.
- Economic factors such as increases in inflation or strong economic growth.
- What's happening at home, such as rising debt levels in Canada or interest rate changes.

Keep this fundamental principle in mind: a strong Canadian dollar is great for importers, whereas a low Canadian dollar benefits exporters. If you're dealing in both, the trick is to strike a balance between the profits being made from each. Our foreign exchange solutions can help you to manage your global transactions in real time.

Key payment decisions

How you're paid are key factors in reducing the risk of FX fluctuations. As an importer, you'll need to decide whether to lock in an exchange rate when ordering from your supplier, or when you pay them. As an exporter, will you charge for your goods in Canadian dollars or the foreign currency where they're being sent? Your customers will also be interested in getting the best possible exchange rate on their purchases.

We can help you to improve your foreign currency cash flows by maximizing the value of your receivables and minimizing the cost of your payables.



Managing foreign exchange

Once you've obtained a better understanding of FX fluctuations and have set up your payables and receivables accordingly it's time to look at how to manage foreign exchange.

You'll need to:

- Decide what methods you'll use to counteract FX movements, for example quote in Canadian dollars, set up a letter of credit or have payments wired to you immediately
- Assign the best method to each market or customer you trade with
- Note your targeted rates or goals for exchanging currencies
- Follow through with your strategy and then review it as market conditions change

Visit the International Banking section of our website to help your business go global while reducing FX risks.

Hedging

Entering financial contracts that protect against expected or unexpected changes in currency exchange rates is known as hedging.

For example, if you manufacture clothing, you could sell a container-load of T-shirts to an overseas buyer who will pay for them when they are delivered in one months' time. You can fix the exchange rate now for the transaction taking place later and so secure the profit margin you will make on the deal.

Other methods of reducing the risk of FX fluctuations include:

- Spot trading – this involves the purchase or sale of a foreign currency 'on the spot.' There's immediate delivery of the FX, so it's the opposite of setting a future date.
- Setting up forward contracts – this is locking in a fixed exchange rate and settling at a future point in time. Forward contracts can be used for any expiry date within one year and with any amount of foreign currency.

We can help you facilitate spot transactions and forward contracts through our foreign exchange solutions. Remember that currency hedging is designed to protect your profits only, not to speculate on foreign exchange markets.

Summary

The internet's a wonderful resource for not only monitoring foreign exchange, but for educating yourself in all areas of international currency. Understanding how foreign exchange works, and constantly monitoring it, will ensure you're in the best position possible to reduce the risk of it impacting on your profits. Remember too, that at RBC we're committed to helping Canadian businesses succeed in the international marketplace. We've got product and service solutions available in each region of the world, including reducing FX risks, so get in touch with us and find out how we can help you.

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