Literature review of foreign exchange essay

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Foreign exchange exposure is very crucial now a days as cross border trade is increasing day byway at a very fast pace. But it is also regarded as very complex. There is a dearth of good literature on this subject, especially in India. Some of the studies identified in this area areas follow; Bengt Pramborg, in this study, ―Foreign Exchange Risk Management by Swedish and Korean Non Financial Firms: A Comparative Survey‖, 2002, makes a comparison of hedging practices of Swedish and Korean Firms. The evidence suggests that Korean firms are more concerned about fluctuations in their cash flows whereas Swedish firms focus on accounting numbers.

The Foreign exchange trading history started in 1875 with the birth of the gold standard monetary. Prior to 1875, countries primarily used gold and silver as a form of international payment. Payment using gold and silver were hampered by their devaluation according to external factors such as an increase in the discovery of new deposits, which would lead to a change in supply and demand. This factor would change the Foreign exchange trading history forever. The aim of the implementation of the gold standard was to guarantee any currency, to set amount of gold. Currency was now backed by gold, measured in ounces. Countries needed large gold reserves to back the demand for currency. This new Bretton Woods monetary system defined the new Foreign exchange market history: * A new method of obtaining a fixed foreign exchange rate. * The gold standard to be replaced with the US Dollar as the ultimate exchange currency. * The US Dollar to be the only currency backed by gold.

* The inception of three international authorities to guard over all foreign transactions. “ According to Julian Walmsley, author of The Foreign Exchange

and Money Markets Guide” although foreign exchange has existed since before biblical times, a formal global market for foreign exchange did not develop until the 1800s with cable transfers taking place between London and New York. 2. 2 Foreign Exchange Trade in Bangladesh

Two issues are investigated that may justify intervention in the foreign exchange market. One is the exchange market pressure and the other is exchange rate pass-through. We find that the exchange rate pass-through effect is high and statistically significant for Bangladesh—87 percent for international price, 95 percent for Indian price. This indicates that a change in international or Indian prices will almost completely translate into a change in domestic prices. Therefore, any depreciation of the taka will lead to an increase in inflation in Bangladesh The results of an error correction model (ECM) suggest that there is a long-run unidirectional causality from exports to growth in Bangladesh.

“ Murshed (2000) finds that an increase in remittance by Taka 1 would result in an increase in national income by Tk 3. 33.” Remittance constitutes an important source of foreign exchange for the poor countries, which have substantial development impact as can be understood from micro and macro point of view. From macro frontier; remittances are used to make import payments and are used for productive investment by the government (Salim, 1992).

“ World Bank (Ali, 1981) identified overseas achieving a favorable balance of payments and as well as creating a new resources base for the country.” In Bangladesh, a significant portion of overseas earnings is spent for

consumption purposes, acquisition of assets, investment in trade and business and to finance import of capital goods. It will positively affects the socio economic condition of migrant families. Some of the early studies (Salim, 1992 and Matin, 1994) focused on the macroeconomic impact of overseas remittances in Bangladesh. Giles and Williams (2000a, 2000b) provide an excellent literature review of the ELG hypothesis until the late 1990s. We are investigating consequence of export (X), import (M) and remittances (R) on GDP growth in Bangladesh. No other previous studies looked at ELG with remittance as a variable.