

# [Currency and interest rate swap: a case study](https://assignbuster.com/currency-and-interest-rate-swap-a-case-study/)

[Business](https://assignbuster.com/essay-subjects/business/)

In essence, It will be clearly noted that the fixed-to-fixed currency swaps provide another form of arbitrage which can influence long-term forward exchange pricing. This paper will discuss how the violation of the traditionally covered arbitrage pricing activity is always practiced by the international currency and the interest charge swap markets who are reported to be inappropriately placing the prices, the interest rate swap market is found to be providing some kind of arbitrages which actually affects the long term forward exchange pricing process.

The application of both the urinary and the Interest rate swaps providing a market for the bonds and contracts In the International market will be critically analyzed and discussed In this paper. INTRODUCTION A swap is always defined as an agreement made between two parties with an intention of exchanging a particular good, this good may be something of money value, we find under this agreement one party is always willing to make some payments for the good while the other one intends to purchase basing on some interests that are to be gained.

In this case we find that as from the year 2000 the swaps has been reporting a umber of growth this coming up as a result their outstanding amount of the swaps In the market (Price and Henderson, 2009). The growth of the swaps In the market, we find that there has also been an increment In the marketing of the long-term forward currency contracts: this Includes other major currencies found In the International mar et. K I Norte tans paper wall KICK at ten Importance AT legal tender Ana rate swap in the determination of the long term forward exchange rates.

Statement of the Problem Interest Considering the economic factors, it can be noted that in sass national economy as actually growing at the desired economic growth rate which facilitated opening of more commercial banks in anticipation of earning normal profits by the investors. For instance, even after the worst economic depression of the years 2000 to 2002; the overall economic growth continues to thrive which witnessed the decrease in unemployment rates, little interest rates as well as declining rate of inflation (Price and Henderson, 2009).

However, it should be noted that the problems experienced by the commercial banks in sass were either indirectly or directly related to the instabilities of banking environmental challenges of the sass. For instance, in the sass the exchange rates floated thus leading to main currencies being volatile. Further there were several peripheral economic shocks such as changing interest rates due to inflation aspects as well as lack of clear monetary policies which led to escalating price levels; the later was mainly caused by the policies adopted and effects of oil embargoes of the sass.

These failures engaged many organizations to engage in the long term forward exchange contracts Aims The aim of study is to shed more light on the issue of interest rate and currency swaps as a mode of financing in the foreign exchange market, the paper also aims at discussing the types and importance of swapping in the attaining of the organizations objectives.

This will essentially facilitate the stability in the financial rates offered by the different financial organizations world wide and therefore lead to the facilitation of increased profit margins and rise in the growth rates of the world economies. \_ObJectives The overall objective of this research work is to find out whether interest rate and urinary swaps play a key role in achieving firm’s objectives with regards to the force marketing in Australia. Other objectives will include; finding out the various swapping approaches to be used in organizations.

The specific objectives include the following; To describe the operational environment of swapping as a mode of financing To identify the drivers that lead to firms to carry out the interest rate and currency swaps 10 analyze Ana critically evaluate ten currency swapping In a Tore market \_Research\_ \_Questions\_ Based on the objectives of this study research queries will include the following: Does interest rate and currency swaps play a key function in attaining organizations goals or objectives? What are the different ways of interest rate and currency used in the fore market?

The importance of using the currency swaps in an organization? How can the management evaluate the interest rate and currency swaps put in place and rate them as effective or non effective? What are the appropriate remedies for ensuring that a successful swapping is carried out \_Benefits of conducting the research \_ This research will not only benefit foreign exchange market but it will be applicable o all those organizations who wish to engage in the interest rate and currency swap financing globally.

It will provide focus and insight to the management on how the swapping is practiced and how it enables the organization achieve its goals \_Limitations of the study\_ Because this is an investigative study more time will be essential to carry out the exploration so as to find the pertinent information that will reveal the issue of interest rate and currency swaps as a key force to achieving results in an organization.

Also another limitation is that of availability of funds because the study ill require the researcher to reach to a wider population through interviewing many respondents. LITERATURE REVIEW \_Swaps\_ Swaps are regarded as a mode of financing that was formed as a result of problems that used to come hand in hand with various types of loans such as the parallel and back to back loans, this was back in the year 2000 and so on. This swap financing carried a number of advantages such as the intermediaries are given an opening to nave unmatched positions In swap Tallying.

I en swap Tallying has also led to the growth of the liquid markets through which we find that the totes for the swaps are availed on a daily basis (Price and Henderson, 2009). As this goes then we find those using the swap financing are required to know to know the techniques of equivocation that exist in this type of financing.

Research indicates that swap financing operates under the principle of exchanging cash flows whose values are said to be equal as at the time of implements the swap financing. Types of Swaps \_ Research shows that there exist two main types of swap financing and they are the currency swap and the interest rate swap. Under the interest rate swap financing it squires that the exchange of the net cash flow under transaction should be based on the fixed and floating interest rate borrowings, through this we find that it has two borrowers whereby one borrower gives out a debt at a fixed rate and exchanging the periodic net payments with the other borrower presenting a debt on a floating rate (Price and Henderson, 2009).

On the other side a currency swap entails the exchanging of net cash flows basing on the debts provided that are dominating the market in diverse currencies, under this type we find that the exchange takes place when the values in the exchange are at he initiation and maturity stage working under the same exchange rate. When these types of swaps are combined we find that they lead to the exchanging of values in different currencies that have interest rates that are fixed or floating (Price and Henderson, 2009).

Research indicates that in a fixed to fixed currency swap is a type of swap financing that is normally agreed upon on a foreign exchange rates that are applied basing on the date of closure governing the initiation and maturity and also the time of the payment of the net interest while the fixed periodic net payments are normally achieved through negotiations between the parties, this negotiation is done basing on the differences that occur in existing varieties of currencies that are present at closure time, in this case the provisions made will actually be given the net payment as this happens to the fixed to fixed currency we find that the foreign borrowing that is full hedged does not require any counter partying the reason for this is that the process of borrowing is usually made straight into the targeted currency whereby the principals of exchange are always put in the required exchange using the available exchange rates. After transacting then the paying of the coupons and the returning of the principals are fully protected using the forwarding market. Research indicates that the currency swap usually provides a differing series of cash flow while the fully protected currency borrowing only needs suitable forward exchange quotations. \_Advantages of using the currency swaps \_ Elastically This currency swap financing allows the exploitation of the target markets that borrow by the organizations transacting.

The research methodologies applied here included both qualitative and quantitative research techniques that involved the use of the interviews and the administration of the questionnaires. These were regarded as the best methodologies to be used because of the fact that they gave the respondents an occasion to answer about their point of view or perception on the current currency swap and how its application in he business organizations can be of great benefit in increasing the profit margins.

This study necessitated the identification of the main the methods used to reduce risks affecting the international currency and the interest rate swap markets.

The researcher therefore mainly concentrated on the issues concerning the currency swap financing and how best it can be applied by organizations in there attempt to boost there profitability levels in the exchange market. The reason for choosing both open and closed questionnaires to be administered is that it will give the informants chance to answer freely to set of questionnaires that will be administered to them during the study. \_Methodology Used, Process and Statistical Technique\_ The facts and figures that were collected regarding the question under siege were collected using the analysis of the information from the secondary sources.