FOREIGN EXCHANGE RISK MANAGEMENT AND FINANCIAL PERFORMANCE OF IMPORT FIRMS IN NAKAWA URBAN COUNCIL

BY

SHALLONE NAMANYA BATTE

12/U/297/GMBA/PE

A DISSERTATION SUBMITTED TO THE GRADUATE SCHOOL IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTERS DEGREE IN BUSINESS ADMINISTRATION OF KYAMBOGO UNIVERSITY

DECEMBER, 2014

DECLARATION

I, **Shallone Namanya Batte**, do hereby declare that this dissertation is my original work and has, to the best of my knowledge, not been submitted for any degree award to any other University before.

SHALLONE NAMANYA BATTE _____

(Student) **Signature**

Date: 30/12/2014

APPROVAL

This is to certify that this dissertation has been submitted for examination in partial fulfillment for the award of Masters in Business administration with our approval as University Supervisors.

Academic Supervisor:

DR MARY MAURICE MUKOKOMA

Signature

Date: 30/12/2014

MR. MASIMENGO TADEO

(Supervisor)

Signature

Date: 30/12/2014

DEDICATION

This work is a tribute to my family members for their patience, understanding and love to cause possibilities

ACKNOWLEDGEMENT

I would like to acknowledge the following persons whose contributions facilitated the completion of this project.

First and foremost, I thank the Almighty God for the gift of life and for giving me the skills, knowledge and energy to be able to complete this paper.

Great thanks go to family members for their continuous support financially towards the completion of this report with out forgetting my academic supervisors

I also recognize the valuable work done by the organizations who participated in providing the right information that was used in this study. May God bless you all

TABLE OF CONTENTS

LIST OF TABLES

LIST OF ACRONYMS

COSO	:	Committee of Sponsoring Organizations of the Tread way
ERM	:	enterprise resource management
FX	:	Foreign Exchange
KACITA	:	Kampala city trading association
SWOT	:	Strengths-weaknesses-opportunities threats
VaR	:	Value at risk

ABSTRACT

The objective of the study was to establish the effect of foreign exchange risk management on performance of import firms. The study employed a case study design and sampled a total of 59 import firms out of the 70 import firms that were targeted under KACITA in Nakawa Urban Council. The study employed a questionnaire as a major tool for data collection and data was analysed using SPSS as a tool for analysis. Correlation was made using Pearson correlation to obtain the results.

The study found out that foreign exchange rate risk management has a positive impact on profitability, market share and the total sales volume of import firms. There is evidence of significantly positive linear relationship between foreign exchange risk management, and performance of import firms. A p-value $0.005<0.05$ indicates that there is a correlation between foreign risk identification and the performance of import firms. The p-value $0.045<0.05$ implies that there is a correlation between foreign exchange risk measurement and profitability, sales volume and market share hence firms' performance. The p-value $0.03<0.05$ means that there exists a strong relationship between foreign exchange risk mitigation measures and performance of import firm. The study also found out that majority of the import firms that were sample respond to foreign exchange risk with a risk management policy plan, often use forwards, futures, money market contracts, options and swaps for hedging in the order of merit.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This chapter consists of the background of the study, statement of the problem, purpose of the study, objectives, definition of key terms, the scope of the study, justification, significance of the study, and theoretical/conceptual frame work .

1.1 Background to the study

Foreign exchange risk (also known as FX risk, exchange rate risk or currency risk) is a financial risk that exists when a financial transaction is denominated in a currency other than that of the base currency of the company (Shapiro, 2007). Foreign exchange risk also exists when the foreign subsidiary of a firm maintains financial statements in a currency other than the reporting currency of the consolidated entity. The risk is that there may be an adverse movement in the exchange rate of the denomination currency in relation to the base currency before the date when the transaction is completed (Levi, Maurice, 2005). Investors and businesses exporting or importing goods and services or making foreign investments have an exchange rate risk which can have severe financial consequences; but steps can be taken to manage (reduce) the risk (Eiteman, David K. 2009).

The foreign exchange risk usually affects businesses that export and/or import, but it can also affect investors making international investments. For example, in a situation where money must be converted to another currency to make a certain investment, then any changes in the currency exchange rate causes that investment's value to either decrease or increase when the investment is sold and converted back into the original currency.

According to the Uganda Export Promotion Board (2012), the import firms face two kinds of foreign exchange risks. The first is the risk of depreciation of the foreign currency in which an importer has invoiced the import contract. If the currency depreciates the importer would receive more money in the home currency. The second is the risk of appreciation of the foreign currency in which the importer holds a due. This would affect the importer's product making it more expensive at home country. The overall long term impact of exchange rate movements is determined by a number of complex linkages and time lags making it difficult to isolate (Uganda Trade Review, 2005). Foreign exchange risk is the degree to which a company is at risk from exchange rate changes. It refers to a change in the value of the company due to an exchange rate change. Foreign exchange risk is a risk that the currency of a country in which it does business will decide to value relative to have a foreign currency. It is also a risk that domestic currency value of cash flows denominated in foreign currency may change because of variations in foreign exchange rate. Foreign exchange fluctuations expose companies to foreign exchange risk, (Abor, 2005), moreover, this coupled with the different firm characteristics have a bearing on the degree of foreign exchange risk management in terms of policy.and techniques, and consequently on the performance of import firms. Foreign exchange risk management according to Abor (2005) is hedging against risk through a number of techniques, (payments netting, prepayment, leading & lagging, hedging with derivatives, forward and futures contracts, currency options and currency swaps).

According to Bank of Uganda Publications (2004), Risk management is described as the performance of activities designed to minimize the negative impact (cost) of uncertainty (risk) regarding possible losses. It is a systematic process for the identification and evaluation of pure loss exposure faced by an organization or an individual and for the selection and implementation of the most appropriate techniques for treating such exposure. The process involves; identification, measurement, and management of the risk. The objectives of risk management

include; minimizing foreign exchange losses, to reduce the volatility of cash flows, to protect earnings fluctuations, to increase profitability and to ensure survival of the firm (Fatemi, 2000).

Exchange rate volatility creates a risky business environment in which there are uncertainties about future profits and payments. These are especially exacerbated in countries where financial instruments for hedging against foreign exchange risk are not developed, which is the case in many developing countries including Uganda (World Bank & MTTI, 2006).

1.2 Statement of the problem

Changes in exchange rates induce changes in the value of a firm's assets, liabilities and cash flows, especially when these are denominated in a foreign currency. In situations where foreign currency is predominantly used over the local currency, the local firms stand at a risk of devaluation of their assets since they sometimes lose a lot of money to buy foreign currency and the fluctuations in the currency markets have continued to have an impact on the outgoing import payments and incoming export funds of import firms. For example, there many currencies that are used by import firms in Uganda in their import transactions, and they include; US Dollars, Euros, British Pound, Japanese Yen, South African Rand. However, the US Dollar is the most predominantly used currency. The exchange rate between the US Dollars and the Uganda shilling has been fluctuating centrally to the Budgeted plans, 2009/2010, 2010/2011, 2011/2012, & 2012/2013), this is a source of foreign exchange risks for the import firms (Bank of Uganda Report, 2013).

Despite the various mitigating measures like currency risk transfer, currency risk reduction, currency risk retention and using several derivatives like options, futures and swaps as hedging techniques against risk, the import firms in Uganda continue to decry poor currency performance of the Uganda shillings (UGX) on the money market which has persistently continued to affect

the import firms' performance and marginalized the foreign exchange risk with its associated challenges (Bank of Uganda Publications, 2004).

It is upon this background that the researcher conducted a study basing on the variables that determine the effect of foreign exchange risk management on the financial performance of import firms.

1.3 Objectives of the study

The general objective

To establish the effect of foreign exchange risk management on the financial performance of import firms

1.4 The specific objectives

The study was guided by the following objects;

i. To investigate the effect of foreign exchange risk identification on the financial performance of import firms in Nakawa Urban Council.
ii. To determine the effect of foreign exchange risk measurement techniques on the financial performance of import firms in Nakawa Urban Council.
iii. To examine the effects of foreign exchange risk mitigations on the financial performance of import firms in Nakawa Urban Council.

1.5 Research questions

The researcher explored the following research questions;

i. What are the effects of foreign exchange risk identification on the financial performance of import firms in Nakawa Urban Council?
ii. What are the foreign exchange risk measurement techniques on the financial performance

of import firms in Nakawa Urban Council?

iii. What are the effects of foreign exchange risk mitigation on the financial performance of import firm in Nakawa urban Council?

1.6 Scope of the study

1.6.1 Subject scope

The study focused on the effect of foreign exchange risk management on financial performance of import firms under KACITA. Specifically the study explored whether foreign exchange risk identification, risk measurement and risk mitigation have an effect on sales volume, profitability and market share of import firms.

1.6.2 Geographical scope

The study was carried out on import firms in Nakawa Urban Council under KACITA. These firms were targeted because they are under one umbrella organization, KACITA and therefore have more standardized procedures for recording their business transactions. Given the fact that their organization is responsible for agitating for fair business policies from government, these firms were more inclined to provide in-depth information on their performance challenges resulting from foreign exchange exposure.

1.6.3 Time scope.

The study covered the period between 2010-2014 when Uganda' currency the shilling become very unstable against major foreign currencies such as the dollar and the pound starling. KACITA annual reports (2012-2013) also indicated that import firms under her oversight experienced issues significant performance challenges due to foreign exchange instability. Therefore the researcher considered data from the firms with this time period.

1.7 Significance of study

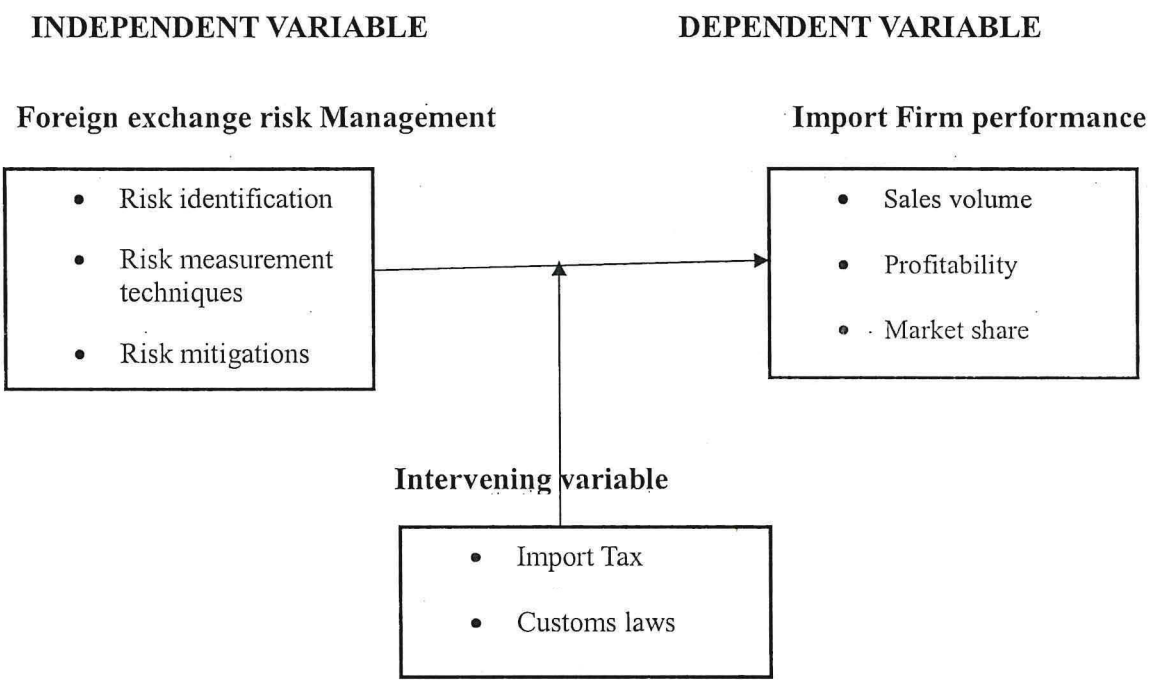
The study has improved the knowledge base on the contribution of active currency risk management practices and human capital components within the currency market on the performance of import firms. Investors and practitioners may use the findings to adopt optimal business plans for competitive performance in term of profits and sales volume.

The research has also contributed to the knowledge of foreign exchange exposure and risk management. The practices of Ugandan firms in relation foreign exchange risk management have been brought to the fore. This will motivate more firms to give due attention to foreign exchange risk management and adopt more effective techniques to help salvage themselves from the increasing foreign exchange exposure as the effects are becoming a global phenomenon. The financial institutions will gain from this as they design foreign exchange rate exposure management products for the Ugandan Market.

The study findings will stimulate more research on the subject of foreign exchange risk as the capital markets activities and trading pick up in Uganda (more firms being listed). The findings may also augment the limited body of empirical literature on exchange rate exposure of firms in Sub Saharan Africa. The results of this study may serve a useful guide to corporate managers, financial managers and investors on the degree of foreign exchange exposure and the need to effectively manage firm exposure.

1.8 CONCEPTUAL FRAME WORK

The diagram below gives a graphical conceptual representation of the variables of study and how they relate to each other. The independent variable was Foreign exchange risk Management practices while the dependent variable was financial performance of import firms. The moderating variables were the import tax and customs laws in business environment in which import firms operate.



***Source: Shapiro (2006) and* Stewart, (2007).**

The above conceptual frame work is based on Shapiro (2006) and Stewart (2007) theories

Of according to Stewart (2007), the business environment the world over is full of risks. Flybjerg (2008) and Minshkin (2001) indicate that these risks increase if the business is on the stock market. The value of a company's profitability increases as the stock prices rises. Frequent

appreciation of a foreign currency against local currency makes it difficult to retain local customers because of high prices of imported input that tend to affect prices of their final products sold locally. This therefore implies that a company's profitability fluctuates because of fluctuations in currency being translated into fluctuating prices But If these risks are not effectively anticipated and prepared for they can significantly lower profitability of business. Therefore, Shapiro (2006) advises that businesses should prepare for and control these risks through risk assessment and mitigation strategies so that their sales, market share and profitability are not affected. Becker (2003) adds that risk management practices should be backed by good managerial skills and entrepreneurial intellectual capability. The success of risk management practices finally depend on the customs laws and import taxes.

1.9 Definitions of key terms

This section presents an operational definition of key terms. The terms are defined the way they are used in the study.

Business Risk: According to Shapiro (2007), A risk is a condition in which the decision maker in a business is able to estimate the likelihood of a threat resulting from certain actions, conditions, alternatives or outcomes.

Risk management:

As indicated by Becker (2003) Risk management are practices or actions used by a business to prevent, control or deal with the uncertainties.

Foreign exchange risk:

Based on Shapiro (2007), a Foreign exchange risk is the likelihood a business will be negatively affected by changes in exchange rates. The business operates at a loss due to an adverse movement in exchange rates. This is also known as "currency risk" or "exchange-rate risk".

Risk identification:

Stewart, (2007) indicates that Risk identification are practices by the firms to identify risk factors That are likely to have greater effect on profitability

Risk measurement techniques:

These are techniques used by the firm to ascertain the magnitude and other potential negative effects that are likely to result from certain business risks

Risk mitigations:

Based on Pickford (2000) views, Risk mitigations are business management practices that a firm implements to stop risks from adversely affecting the profitability and other operations of a firm.

Profitability

According to Stewart, (2007), Profitability is the extent to which a firm achieves success in its objectives of increasing sales volume and market share. It is also the extent to which the firm is able to prevent failures and the uncertainty in achieving the overall objective of the firm. This eventually the ultimate test of the effectiveness of foreign exchange risk management practices. This normally achieved through increased sales volume, or total amount of sales and increased market share, the proportion of the total market controlled by the firm.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

Under this chapter, the researcher reviewed related literature about foreign exchange risk management. This chapter mainly included secondary data that was got from text books, journals, magazines, news papers and organizational records like annual reports about foreign exchange risk management and the performance of import firms.

2.1 Overview of Foreign Exchange Risk Management

According to Featherson, Littlefield & Mwangi (2006), foreign exchange risk arises when fluctuation in the relative values of currencies affects the competitive position or viability of an organization. Firms are exposed to foreign exchange risk if the results of their projects depend on future exchange rates and if exchange rate changes cannot be fully anticipated. Generally, companies are exposed to, Transaction exposure, Economic exposure and Translation exposure (El-Masry, 2006; Salifu et al, 2007).

Transaction risk occurs where the value of the existing obligations are worsened by movements in the foreign exchange rates. Transactional exposure arises from future cash flows such as trade contracts and also occurs where the value of existing obligations are affected by changes in foreign exchange rates. Economic risk relates to adverse impact on entity /income for both domestic and foreign operations because of sharp, unexpected change in exchange rate. Operational exposure occurs where the market position of a firm changes as a result of the effect of exchange rate changes on competition, prices and demand (El-Masry, 2006). Translation risk is also related to assets or income derived from offshore enterprise. Translation exposure occurs through currency mismatch and it is related to assets or income derived from offshore enterprise

(Madura, 2003). Contingency exposure occurs from possible revaluations arising from future liabilities. The total or economic exposure of a firm refers to all exchange rate effects through all the four of foreign exchange rate risk (El-Masry, 2006).

The risk of channels undesirable changes in the company's value resulting from unexpected changes in the real exchange rates is presented for companies across both domestic and international markets. Choi and Kim (2003) in their analysis showed that both internationally involved companies and companies with only domestic operations are exposed to foreign exchange risk in the long run. The present research, however, concerns only those companies that are at least to some degree involved in international operations.

Considering the nature of operating exposure it is obvious that it has the greatest consequences for a company's development and growth compared to other types of exposure. Glaum (1990) highlighted the concept of operating exposure as the prior foreign exchange exposure academic concept. The results of the survey of the British Times 1000 corporations conducted by Belk and Edelshain (2000) revealed that operating exposure is also important for practitioners since the majority of the companies defined this particular exposure as the most significant in the total foreign exchange rate exposure. However, despite the fact that the companies recognize that they are highly vulnerable to the elements of operational exposure, several studies witnessed that in their practice the companies mostly manage transaction and translation exposures (Lessard 1986, Hakkarainen et al 2000, Bodnar et. al 2009). The most obvious explanation of this is that the broad scope of the operating exposure makes it impossible to measure it only via analysis of the companies' financial accounts and statements. Therefore difficulties in quantification and prediction of operating exposure due to many uncertain elements make it difficult to choose the exchange rates represent one of the major sources of macroeconomic risk for a nonfinancial company. In the long run exchange rate changes influence a company's volume of foreign trade,

the costs of foreign purchases; alter its domestic and international competitive profile and the structure of foreign markets in which the company operates. These changes have a large impact on small and internationally oriented economies (Bodnar and mbusa Gentry 2003).

Therefore difficulties in quantification and prediction of operating exposure due to many uncertain elements make it difficult to choose the appropriate management tools to manage it. Furthermore, management of the long-term exposure to currency fluctuations is costly and time consuming. It would definitely require a great deal of the company's resources in order to gather the necessary information for the analysis, which means that management of the operating exposure would be impossible for the companies restricted in their resources. Belk and Edelshain (2007) pointed out that insufficient knowledge of the phenomenon also prevents managers from considering all possible alternatives and make them concentrate on exposures that can be assessed ex post. Lessard (2006) emphasized, that not all managers realize the fact that management of the operating exposure is already incorporated into the operational decisions of the company.

In Uganda, the forex annual report (2009) revealed low multi-currency spreads and limited human capital agenda. The first half of 2010 had low sales volumes and profitability levels which further threatens financial distress on business existence and expansion of forex bureaus. Other Stakeholders like BOU and the forex association have partly addressed the unpredictable currency rates and human capacity. Despite management effort for firm-specific human capacity and forex risk control, forex bureaus are highly characterized with low financial performance yet adhered to sales and profit objective. Inadequate practice of foreign exchange risk management and shortcomings in human capital could have a possible direct relationship on the performance of forex bureaus. Oxelheim (1984) defines foreign exchange risk as the risk of change (gain or loss) in the company's future economic value due change of foreign exchange rates. It is

manifested by exposure, the degree to which a company performance is affected by exchange rate changes. Thus, Shapiro (2006) suggests adherence to foreign exchange risk management, which involves currency assessment (identification and quantification) and designed counter-strategies against foreign exchange risk.

Mutebile E. (2011) stated that Uganda Shilling (UGX) per US Dollar is undervalued and further depreciation will be counterproductive. According to Uganda Export promotion Board (2003), an importer's vulnerability to foreign exchange risk depends on the currency mix and competitive structure. Risk may be greater on account of currency mix if the importer imports from more than one country. A balance of outflows and inflows of different currencies has to be achieved in order to minimize risk. As for the competitive structure, the particular industry in which the importer is operating may also be prone to currency risks. More competition in the industry will expose the importer to currency 9 risks due to price sensitivity. According to El-Masry & Omneya, (2007), foreign exchange exposure is the sensitivity of changes in the real domestic currency value of assets, liabilities or operating incomes to unanticipated changes in exchange rate. Organizations can choose to do nothing about their exposure and accept the consequences of variations in currency values or the possibility that their governments may impose restrictions on the availability or transfer of foreign currency, they can "hedge against their exposure", that is they can purchase a financial instrument that will protect the organization against the consequences of those adverse movements in foreign exchange rates. They can also adopt partial hedging, but this is after a careful review of the risk (Featherson et al., 2006).

According to Bank of Uganda Publications (2004), Risk management is described as the performance of activities designed to minimize the negative impact (cost) of uncertainty (risk) regarding possible losses. It is a systematic process for the identification and evaluation of pure loss exposure faced by an organization or an individual and for the selection and implementation

of the most appropriate techniques for treating such exposure .The process involves; identification, measurement, and management of the risk. The objectives of risk management include; minimizing foreign exchange losses, to reduce the volatility of cash flows, to protect earnings fluctuations, to increase profitability and to ensure survival of the firm (Fatemi, 2000).

2.2 risk Identification and Performance

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. Failure to clearly understand or notice the existence of a certain risk will retard the performance of the imports firm.

Businesses that trades internationally or have operations overseas are likely to be exposed to foreign exchange risk arising from volatility in the currency markets. The most common cause of foreign exchange exposure arises from having to make overseas payments for your imports priced in a foreign currency or receiving foreign currency receipts for your exports. However, exposure can also arise from: Foreign currency borrowing/deposits, overseas subsidiaries. Assets located overseas. The impact that exchange rate fluctuations have on profitability and the general performance will vary but in many cases it can be significant and suppress the performance of indigenous firms if the financial strategies are not dealt with.

Evans et al., (1985) and Shapiro (2006) state that currency risk identification and assessment and strategies will mitigate foreign exchange risk in exposed firms. Barney (2001) relates trade experience and valuable training to focus on profits while Becker (1993) agree that managerial skills, advanced education, knowledge and intellectual capability have key strategic contributions to firm performance in any business environment. Performance can be viewed in financial perspective through profitability and sales volume or growth. Gopinathan (2009a) and James

(2009) emphasized profits/sales affect performance of import firms and their ratio analysis can be performed from financial statements to measure organizational performance.

Lock in to fixed rates – as soon as you become aware of a need to exchange foreign exchange at a future date, you can fix the exchange rate by booking a forward exchange contract. This approach provides certainty but you could suffer an opportunity loss if rates subsequently move in your favour and you are obliged to transact at the forward contract rate.
Use flexible products – a currency option will offer you the potential for upside benefit if rates move in your favour – like a spot deal, but will provide protection against adverse rate movements – like a forward contract. For this flexibility, we will normally charge a premium although there are a range of alternative structured option products available where an up front premium is not required.

The risk identification process begins with the team compiling the project's risk events. The identification process will vary, depending on the nature of the project and the risk management skills of the team members, but most identification processes begin with an examination of issues and concerns created by the project development team. These issues and concerns can be derived from an examination of the project description, work breakdown structure, cost estimate, design and construction schedule, procurement plan, or general risk checklists. A number of documents and tools are available to support the risk identification process. It is therefore upon the risk checklists that the management team can design mitigation measures and ensure performance of the firm.

Brainstorming

When objectives are stated clearly and understood by the participants, a brainstorming session drawing on the creativity of the participants can be used to generate a list of risks. In a well

facilitated brainstorming session, the participants are collaborators, comprising a team that works together to articulate the risks that may be known by some in the group. In the session, risks that are known unknowns may emerge, and perhaps even some risks that were previously unknown unknowns may become known. Facilitating a brainstorming session takes special leadership skills, and, in some organizations, members of the internal audit and ERM staff have been trained and certified to conduct risk brainstorming sessions. In addition to well trained facilitators, the participants need to understand the ERM framework and how the brainstorming session fits into the ERM process. However, a failure in the brainstorming process will negatively influence the foreign exchange risk which will therefore affect the general performance of import firms since it will lead to unknown risks Gopinathan et al (2009).

SWOT Analysis

SWOT (strengths-weaknesses-opportunities threats) analysis is a technique often used in the formulation of strategy. The strengths and weaknesses are internal to the company and include the company's culture, structure, and financial and human resources. The major strengths of the company combine to form the core competencies that provide the basis for the company to achieve a competitive advantage. The opportunities and threats consist of variables outside the company and typically are not under the control of senior management in the short run, such as the broad spectrum of political, societal, environmental, and industry risks.

Facilitated Workshops

After the information is completed and collected, a cross-functional management team from the unit or from several units might participate in a facilitated workshop to discuss it. Again, using voting software, the various risks can be ranked to arrive at a consensus of the top five to 10, for example. As noted previously, using interactive voting software allows the individuals to identify

and rank the risks anonymously without fear of reprisal should their superior be a member of the group (Holton, 2003).

Risk Questionnaires and Risk Surveys

A risk questionnaire that includes a series of questions on both internal and external events can also be used effectively to identify risks. For the external area, questions might be directed at political and social risk, regulatory risk, industry risk, economic risk, environmental risk, competition risk, and so forth. Questions on the internal perspective might address risk relating to customers, creditors/investors, suppliers, operations, products, production processes, facilities, information systems, and so on. Questionnaires are valuable because they can help a company think through its own risks by providing a list of questions around certain risks. The disadvantage of questionnaires is that they usually are not linked to strategy (Holton, 2003).

Scenario Analysis

Scenario analysis is a particularly useful technique in identifying strategic risks where the situation is less defined and "what-if" questions should be explored. Essentially, this technique is one way to uncover risks where the event is high impact/low probability. In this process, "Managers invent and then consider, in depth, several varied stories of equally plausible futures. The stories are carefully researched, full of relevant detail, oriented toward real-life decisions, and designed (one hopes) to bring forward surprises and unexpected leaps of understanding (Deloitte, 2006).

Using Technology

The risk identification process can also utilize the company's existing technology infrastructure. For example, most organizations utilize an intranet in their management processes. The group responsible for a company's ERM process can encourage units to place their best risk practices on the ERM site. Risk checklists, anecdotes, and best practices on the intranet serve as

stimulation and motivation for operating management to think seriously about risks in their unit. Also, tools that have been found particularly useful to various units can be catalogued. As new projects are launched, business managers are encouraged to consult the risk management group's intranet site (Holton, 2003).

Interviews and Self-Assessment

This technique combines two different processes. First, each individual of the organizational or operating units is given a template with instructions to list the key strategies and/or objectives within his or her area of responsibility and the risks that could impede the achievement of the objectives. Each unit is also asked to assess its risk management capability using practical framework categories such as those contained in the ERM framework from the Committee of Sponsoring Organizations of the Tread way Commission (COSO).

Other Techniques

Other possible approaches for identifying risks include value chain analysis, system design review, process analysis, and benchmarking with other similar as well as dissimilar organizations. Also, external consultants can add value in the risk identification process by bringing in knowledge from other companies and industries and by challenging the company's list of identified risks.

In conclusion, the identification of the possible risk is very instrumental in the simplicity of the mitigation measures. The technicality in the identification of the risks determines the simplicity in mitigation and the reverse is true. Therefore, in order to minimize the foreign exchange risk effectively, the risk identification team should be too technical that they have all the possible skills of risk identification and create possible mitigation measures in relation to achieving performance because mitigation measure are never static but varies from organization to the other and base on the nature of the risk and the organizational goals (Choi and Kim, 2003)

2.3 Risk Measurement and Performance

According to Moosa, (2004), financial risk is most commonly measured in terms of the variance or standard deviation of a variable such as percentage returns or rates of change. In foreign exchange, a relevant factor would be the rate of change of the spot exchange rate between currencies. Variance represents exchange rate risk by the spread of exchange rates, whereas standard deviation represents exchange rate risk by the amount exchange rates deviate, on average, from the mean exchange rate in a probability distribution. A higher standard deviation would signal a greater currency risk. Economists have criticized the accuracy of standard deviation as a risk indicator for its uniform treatment of deviations, be they positive or negative, and for automatically squaring deviation values. Alternatives such as average absolute deviation and Sem-ivariance have been advanced for measuring financial risk.

Practitioners have advanced and regulators have accepted a financial risk management technique called value at risk (VaR), which examines the tail end of a distribution of returns for changes in exchange rates to highlight the outcomes with the worst returns. Banks in Europe have been authorized by the Bank for International Settlements to employ VaR models of their own design in establishing capital requirements for given levels of market risk. Using the VaR model helps risk managers determine the amount that could be lost on an investment portfolio over a certain period of time with a given probability of changes in exchange rates (Moosa, 2003). VaR typically is the risk measure of choice for FX managers and risk departments because it expresses a portfolio's risks in a coherent and logical manner. It is expressed in real profit-and loss terms and can directly tell a risk manager the potential risks inherent in a portfolio based on varying degrees of statistical confidence. VaR traditionally is measured in the following three ways:

- Historical simulation
- Variance/covariance (parametric)
- Monte Carlo simulation

Each method produces a statistical measurement of VaR that is calculated using an historical data assumption to give a level of confidence that is determined from the historical price action. Each method differs in complexity and has advantages and disadvantages. Historical simulation assumes that the past is a good predictor of the future and that the volatility of the analyzed currencies will remain stable, within the parameters observed in the past. It uses real historical data and therefore importantly does not assume that the returns are normally distributed. It is, however, computationally intensive and completely dependent on historical price movements, and therefore it can seriously underestimate "tail risk." (Tail risk is a measurement of the probability of an event occurring at the extremes of a given distribution, the reasons for this will be explained later in this article.) Historical simulation is also dependent on the quality and depth of the input data, which can be problematic for emerging market currencies. Variance/covariance, sometimes known as parametric VaR, is computationally easier because historical data is used to calculate the standard deviation of the changes of risk factors and the correlations between them.

The measurement and management of foreign exchange (FX) risk, particularly in emerging market portfolios, often is not fully understood. The Bank of International Settlements has proposed a "shorthand" method and a "simulation" method to measure FX risk. Essentially shorthand risk measurement refers to an outright notional expression of risk, loosely measured by some form of leverage calculation, and simulation risk refers to a simulation of the possible impact on a foreign exchange portfolio by measuring historical price action to give some degree of insight into potential profit-and-loss scenarios based on this price action. This approach commonly is referred to as Value-at-Risk (VAR) analysis.

Measuring currency risk may show difficult, at least with regards to translation and economic risk (Van Deventer, Imai, and Mesler, 2004; Holton, 2003). At present, a widely used method is

the value-at-risk (VaR) model. Broadly, value at risk is defined as the maximum loss for a given exposure over a given time horizon with z% confidence. However, most Ugandan firms have tendency of poor records management that they do not document their past records and by the time they realize a risk, the firm will have made a great lose. This means that the technique of measurement of the magnitude of the risk is very instrumental in determining performance.

Kirt (2008) whose study showd foreign exchange risk management is about wealth value in a firm through cost effective and innovative techniques of currency risk control. Import firms were able to identify that foreign exchange risk as a problem to their business profit and sales turnover.

2.3.1 Value-at-Risk Calculation

Value-at-risk method employs the historical simulation approach of data of transaction cash flows and simulation. Kirt (2008) says the value at risk is potential losses over a certain time horizon using a certain confidence level or probability hence error margin. This method is widely used in transaction risk measurement by regression modeling. For economic exposure, Van .D et al., (2004) and Kirt C. (2008) insist that Value-at-Risk model measures actual and potential loss of portfolio under a certain probability or confidence interval (z%). Economic risk is also the sum of translation and transaction exposure. The present value of a company is measured from changes in future operating cash flows caused by environmental unexpected changes in currency exchange rates. The analysis of economic exposure assesses dynamic exchange rates on a company's own operations in future position relative to other companies.

The VaR methodology can be used to measure a variety of types of risk, helping firms in their risk management. However, the VaR does not define what happens to the exposure for the (100 – z) % point of confidence, i.e., the worst case scenario. Since the VaR model does not define the maximum loss with 100 percent confidence, firms often set operational limits, such as nominal

amounts or stop loss orders, in addition to VaR limits, to reach the highest possible coverage (Papaioannou and Gatzonas, 2002).

The VaR measure of exchange rate risk is used by firms to estimate the riskiness of a foreign exchange position resulting from a firm's activities, including the foreign exchange position of its treasury, over a certain time period under normal conditions (Holton, 2003). The VaR calculation depends on 3 parameters:

- The holding period, i.e., the length of time over which the foreign exchange position is planned to be held. The typical holding period is 1 day.
- The confidence level at which the estimate is planned to be made. The usual confidence levels are 99 percent and 95 percent.
- The unit of currency to be used for the denomination of the VaR.

Assuming a holding period of x days and a confidence level of y%, the VaR measures what will be the maximum loss (i.e., the decrease in the market value of a foreign exchange position) over x days, if the x-days period is not one of the (100-y)% x-days periods that are the worst under normal conditions. Thus, if the foreign exchange position has a 1-day VaR of $10 million at the 99 percent confidence level, the firm should expect that, with a probability of 99 percent, the value of this position will decrease by no more than $10 million during 1 day, provided that usual conditions will prevail over that 1 day. In other words, the firm should expect that the value of its foreign exchange rate position will decrease by no more than $10 million on 99 out of 100 usual trading days or by more than $10 million on 1 out of every 100 usual trading days.

2.3.2 The Historical Simulation Method of Calculation

The historical simulation is the simplest method of calculation that involves running the firm's current foreign exchange position across a set of historical exchange rate changes to yield a distribution of losses in the value of the foreign exchange position, say 1,000, and then

computing a percentile (the VaR). Thus, assuming a 99 percent confidence level and a 1-day holding period, the VaR could be computed by sorting in ascending order the 1,000 daily losses and taking the 11th largest loss out of the 1,000 (since the confidence level implies that 1 percent of losses – 10 losses –should exceed the VaR). The main benefit of this method is that it does not assume a normal distribution of currency returns, as it is well documented that these returns are not normal but rather leptokurtic. Its shortcomings, however, are that this calculation requires a large database and is computationally intensive.

2.3.3 The Variance – Covariance Model

The variance – covariance model assumes that (1) the change in the value of a firm's total foreign exchange position is a linear combination of all the changes in the values of individual foreign exchange positions, so that also the total currency return is linearly dependent on all individual currency returns; and (2) the currency returns are jointly normally distributed. Thus, for a 99 percent confidence level, the VaR can be calculated as: VaR= -Vp (Mp + 2.33 Sp) where Vp is the initial value (in currency units) of the foreign exchange position Mp is the mean of the currency return on the firm's total foreign exchange position, which is a weighted average of individual foreign exchange position Sp is the standard deviation of the currency return on the firm's total foreign exchange position, which is the standard deviation of the weighted transformation of the variance-covariance matrix of individual foreign exchange positions (note that the latter includes the correlations of individual foreign exchange positions). While the variance-covariance model allows for a quick calculation, its drawbacks include the restrictive assumptions of a normal distribution of currency returns and a linear combination of the total foreign exchange position. Note, however, that the normality assumption could be relaxed (Longin, 2001). When a non-normal distribution is used instead, the computational cost would be higher due to the additional estimation of the confidence interval for the loss exceeding the VaR.

2.3.4 Monte Carlo Simulation

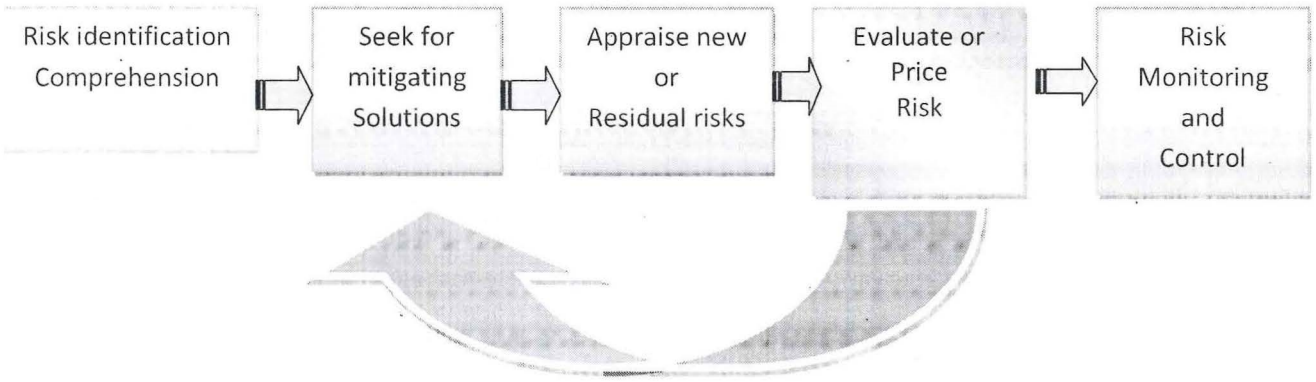
Monte Carlo simulation usually involves principal components analysis of the variance covariance model, followed by random simulation of the components. While its main advantages include; its ability to handle any underlying distribution and to more accurately assess the VaR when non-linear currency factors are present in the foreign exchange position (e.g., options), its serious drawback is the computationally intensive process.

2.4 risk Mitigation and Performance

The globalization of business generates foreign currency risks. This process is irreversible and critical to the survival of most industries and businesses. The "globalization process" affords enormous opportunities to diversify business risk, generate economies of scale and capture additional market share. Companies can no longer state "Our company deals only in US dollars" since this approach is not sustainable in global trade. It is estimated that 40% of all international trade is denominated in foreign currency. Trillions per day move through the foreign exchange markets. Political factors determine that not all currencies are convertible. Commercial trade is full of challenges, many of which may be overcome by utilizing the options available in this section.

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. These are control techniques to mitigate exchange risk exposure. Shapiro (2006) categorizes as hedging strategies by currency risk transfer, reduction and risk retention.

The Risk Management Process



Adapted from (Steele, 1992): approaching risk management as an iterative process

Risk identification

The greater burden of risk identification varies basing on the nature of the organization

Seek for mitigating solutions

This stage involves identifying several techniques to deal with risks and what possible solutions should be applied to overcome risks

New or residual risk

At this stage we identify the rate at which risks emerge or occur in the project. We should be able to determine whether there are new emerging risks in the project in relation to the past risks.

Evaluate or pricing risk

Involves evaluating risks and risk interactions to assess the range of possible outcomes. It is primarily concerned with determining which risk events warrant a response.

Risk monitoring and control

Involves defining enhancement steps for opportunities and responses to threats. Responses to threats generally fall into one of the following categories; risk avoidance, risk reduction, risk

transfer and risk retention. Usually, the way risks are monitor and controlled highly influence the performance of the firm. Firms with a strong monitoring and control techniques towards the existing risks perform better.

2.4.1 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). This is when consequences of foreign exchange risk are shifted to a counterparty by contractual acceptance. Various authors and studies explain risk transfer contracts without impact to risk levels. These include forward contracts, currency futures, money market hedge, currency swaps, currency options and diversification. Organizations that easily accept the risk usual perform poorly since most of their resources are spent in paying for the risk. This is different from those from transfer the risk to other parties mainly for import firms, the risk can be passed on to the customers inform of high prices so that the burden does not cause a detriment on their performance as a firm.

2.4.1.1 Forward contract

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. Principally, a forward contract involves pre-selling or buying a particular amount of currency at a specified rate now for future delivery. Currency forwards stop exchange rate risk for company's receivables or payables. Giddy and Dufey (2000) notes forward deals with specific currency amount and specified rate now, avoids exposure upon delivery at maturity date despite locked future gains.

2.4.1.2 Currency future

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.

It is a commitment to deliver a specific amount of a specified currency at a specified date for an agreed price incorporated in the contract. Futures perform like forwards but differ by marketability, any time liquidity, standard size, flexibility and economy by commission. In contrast, Van Horne (2002) assures stable cash flows with flexible but standardized currency futures where specific currency volume(s) with independent rates are delivered on future specified date (s) or periodic intervals.

2.4.1.3 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.

This is the borrowing of transaction currency amount, immediately convert the loan into the company's operating currency and then repay foreign currency loan within a cash settlement date with the proceeds of a particular transaction. The difference between the money market hedge and the forward hedge is that the cost of money market hedge is determined by different interest rates rather than a forward rate quotation. Eiteman et al., (2007) relates money market hedge with differential interest rates by converting cheap foreign loans into operating currency for gainful transactions to repay using proceeds before settlement date.

2.4.1.4 Currency swap

According to Van Horne, (2002), 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 Sun et al., (2003) adds currency swap where counterparties exchange equal initial principal of two different currencies by spot rate and comparative advantage. Though a costly third party offsets default risk. In general terms, a currency swap is when two parties, usually between a bank and a company to exchange payments denominated in one currency for payments denominated in another. The usual aim to replace cash flows scheduled in an undesired currency with flows in a desired currency to raise capital in currencies of no significant revenues. Having raised the capital however, the company may wish to swap its repayment into a currency in which it has future operating revenues.

2.4.1.5 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. Is a derivative instrument where the owner has the right but not the obligation to exchange money denominated in one currency into another currency at a pre-agreed exchange rate on a specified date. It thus avoids potential exposure as counterparties have free and open choice to trade currency amount at specified rate before expiry date. Ross et al, (2005) states the holder may buy a call option while a writer may sell a put option. The rule is to hedge expected foreign currency cash flows with forwards, and uncertain foreign cash flows with options.

2.4.1.6 Diversification

According to Belk, Bidgood & Duangploy (2003) 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). Currency diversification is the spreading of your investment across different global currencies such as sterling pound, yen and the Euro. Belk et al., (1993) identifies with diversification as a defensive reaction where exposure is mitigated by spreading risk or currency assets into several portfolios or currency outlay. It is due to comparative advantages of stronger currencies. Uganda's forex bureaus do diversify to remittance services and may involve shifting markets or service lines. Diversification eases currency conversion and minimizes forex risks by extra flexibility to switch currencies.

2.4.1.7 International borrowing

International borrowing is used to minimize adverse foreign exchange risk by borrowing a weakening currency. If borrowing is spread across many currencies, it is unlikely that they will appreciate at the same hence low risk level. Borrowing can be done coincidentally with money market hedge methods.

2.4.2 Currency Risk Reduction

According to (Bartram, September 2013) these are methods to reduce the likelihood and severity of foreign exchange risk exposure. A firm can opt to lead or lag, net off, match cash flows and invoice in stable hard currency. Leading and lagging - An additional operating technique that can be used by companies is leading and lagging foreign currency receipts and payments. Leading reduces exposure by prepaying in soft currency and the practice of lagging is about accumulating accruals till the sales quote favours the creditor. The effect of hard currency payables is low hence timing controls exposure. A company would l lead soft currency receivables and lag hard

currency receivables to avoid loss from depreciation and benefit from appreciation of the hard currency respectively

2.4.2.1 Netting

The strategy of netting applies when the company and its branches net off intra-organizational currency flows at the end of each period and hence hedging. This saves a company branch or subsidiaries by balancing receivables against payables in a two-way intra organization flow. The net balance is the only exposure to hedge hence risk saving. For example a UGX 20 million branch transfer to the main company owing 40 million. A net-off UGX 20 million, rather than the corporation's UGX 60 million transaction is only exposed. Netting further saves transfer and commission costs in the two-way flow in the same currency.

2.4.2.2 Matching

Timing benefits another tool called matching. This is a technique similar to netting where a company strives to match its currency outflows by its anticipated currency outflows with amount and timing. Here outflows suitably paired with inflows of same expected currency amount. Firms produce a benefit in the form of spread-saving (Bartram, September 2013). For example a firm anticipating receipts in a specific currency may match it with an arranged outflow of the same currency hence natural matching. Parallel matching can be used whereby a company tries to match cash flows in currencies that move closely together over time.

2.4.2.3 Currency invoicing

By using the strategy of hedging through the choice of invoice currency, a company can shift share or diversify the exchange risk to avoid exchange risk anymore. It has merely shifted from the dealer to the buyer to share exposure for example invoicing half of the bill in home currency and the remaining half in the currency of the buyer. The risk is then halved when a chosen invoice currency is presented at the same time as the sales quote or sales contract. Dominant

substantial market power can use this method as, Oi et al., (2004) favours currency invoicing in both stable currency and sales quote. A depreciating currency will maximize profits hence hedge against gross loss.

2.4.3 Currency Risk Retention

This is an organizational retention of funds to offset unexpected foreign exchange risk where mitigating cost outweighs perceived benefit. According to Shapiro (2006), some firms are risk neutral to foreign exchange changes in the long run. This calls for investment in higher returns to exceed loss or risk potential overtime.

Bradley and Mole (2002) notes that foreign exchange risk management is a financial function and thus affects the firm's financial position. Volatile exchange rates do reduce cash flows and profitability of any firm. Belk (2002) states the aim of foreign exchange risk management as limiting volatile forex exposure on the firm's financial performance whereas Shapiro (2006) describes performance in terms of higher profit margin, sales growth and overall liquidity of firm. This relates how currency risk assessment stimulates financial objectives.

Forex managers can implement mitigation measures as competitive advantage to stabilize financial performance in dynamic currency markets for example foreign fixed deposits earn interest with a saved principal. It depends on other currency capabilities, real-time economic quotes and reliable payment by wires or online offers of cross-currency deals. Evans et al, (2005) notes efficient cash control promotes profitability by incorporating exposure into the firm's operational and long term planning. Secured profits and cost control will arrest possible financial distress of forex related firms like forex bureaus.

For optimal financial performance, forex risk management needs to be specific to strategies and high efficiency of market information to select ideal tools for sales and profits. Handling

currency fluctuation with risk management strategies is befitting in today`s enormous size of the forex market of speed and liquidity unlike other markets. Losses exist, but profits are even higher. But just like any other speculative trade, enlarged risks come along with probability for a higher profit/loss. Regardless of forex rate changes, profits or losses prevail with caution of the rate spread. This is consequently translated into the firms` performance through documentary evidence namely statement of comprehensive income and financial position. In the end currencies inventory is converted into the local currency (Bartram, September 2013).

Technical analysis is of higher role to have higher sales in any forex related firm. This should be complemented with practical statistical tests and routines. There is need for knowledge of the exit point of the currency market at profit targets. Limit orders let the currency investors stop further trading and leave the market at preset profit objectives. By creating a disciplined trading methodology, limit orders allow the traders to fix a limit of the profits which they want to make, and then exit the market. Also, they are free from the work of continuous monitoring the market sitting in front of their computers all day.

Stop/loss commands also follow the same motive as that of the limit orders, by allowing the investors to set an exit point for a loss. By limiting your losses to a preset position, Stop/loss orders help forex investors control their risk conditions. Under normal situations, management of forex risk should strategically align to objectives for value addition to serve shareholders' interests. Accurate placing of stop and limit orders calls for risk takers.

Mitigating strategies can be appropriately structured against forex risk by focusing on one key currency business than currency markets as Allayanis et al., (2001) notes risk averse behaviors of firms.

UFBAMBRA (2010) states currency volumes in the descending order are the US Dollar, UK Pound Sterling, Euro, Kenya Shilling and the South African Rand. This serves to stabilize the

earnings to limit probable insolvency. The investor`s stop and limit orders determines the amount of risk level hence it is advisable to place your stop/loss orders far from normal market price as changes can trigger the order. Limit orders also reflect a rational hope of expected profits based on market's trading activity. The forex rate should not be overexposed nor too close to market. Stop-loss and limit orders can lower an investor's exposure to risk by a large proportion.

A dynamic business environment will always explain the financial performance of firms.
This is important for strategic reasons of competitive sustainability. A collection of human capital input will enhance business success in sales and profit. Garavan et al (2001) cites a resource based view where Human capital unites individual abilities, skills, training, education, and experience in their performance of fruitful output through decisions and cost effective techniques.

Foreign exchange risk management strategies require education and on job training for highly skilled technical and managerial employees. Kenyon (2000) suggests that key successful forex trading involves understanding of other risks like liquidity risk and cash risk. Firm employees aim at financial profits by cost control and risk adjustment hence need for loyalty and commitment to specific skills. It is quite ideal that exchange risk control should precede exposure for informed financial decisions. Forex bureaus need specific skills and applications to enable positive net present values through management by objectives, financial plans and stable reserve fund. Therefore forex dealers should appreciate basic currency trading, chart movements, indicators and interpretation. There is limited or no human sphere of influence and wisdom for currency exchange behavior because most knowledgeable traders can no absolute prediction. As such, forex traders are advised to benefit from designed strategies to reduce exposure. Currency markets are highly unpredictable and tentative in nature, as any currency may fluctuate to becoming very expensive or very cheap in relation to other.

Forex risk management calls for collective application of analytical skills prompt knowledge and experience in a highly efficient currency market. Forex risk management and human capital rely on basics behind an investment, and understanding behind the major market trading. This is the ideal way for higher turnover and profitable currency trading. Skilled technical analysis and good money management skills are the basic essentials to trade well. Analyze the market and create a position, establishing rational stop loss and profit taking levels.

According to Kizza Caroline (2009), Uganda`s case is unique as the employees of forex bureaus have various training and educational background. This diversity can be positive or otherwise depending on how they appreciate forex trade and risk management. Though human capital is a competitive advantage, generally organizations need understand its nature and value to add corporate value through currency risk assessment and counter strategies. It is therefore ideal that costs of employing human capital and currency risk techniques should be less compared to costs of currency risk management. This can be critical in face of today`s globalization and knowledge economies.

CHAPTER THREE

METHODOLOGY

3.1 introduction

This chapter contains the research design, study population, sampling design, sample size, sample area, data collection instruments, reliability and validity of data, sources of data, study variables, data collection procedures, data processing and analysis and limitations to the study.

3.2 study design

A case study research design was used to get an in depth understanding of the effect of foreign exchange risk management and the financial performance of the import firms in Nakawa Urban council. The type of research was quantitative. Quantitative research methods were used because they enable a structured statistical measurement of variables (Trochim, 2006). Data was collected using a questionnaire. Quantitative data was analyzed Using statistical methods. A case study method was employed because of its strength in allowing the researcher to concentrate on a specific situation and to identify, the various interactive issues affecting the research problem (Bell, 2004).

3.3 Study population

The study population included all proprietors and managers of import firms located in Nakawa Urban Council under the oversight KACITA. KACITA (2013) records indicated that a total of 35 import firms were located and operated in the Nakawa area. Therefore, the population had a total of 70 proprietors and managers. Therefore, the target population included 70 respondents who either serviced as proprietors or managers of the firms.

3.4 Sample size and sample size determination

The Krejcie and Morgan (1970) guide was used to determine sample size. For a population of 70 Krejcie and Morgan (1970) suggest sample of 59 respondents. Therefore, a total of 59 respondents were selected from the firms. The respondents were in categories of Executives (proprietors), Senior Managers and Finance. The table below gives a summary of respondents and the nature of information they provided.

Table 3.1: Summary of Category of Respondents

Category	N	s	Sampling Strategy	Data
1. Proprietors	35	26	Purposive	Quantitative (questionnaires)
2.Administrators	35	33	Stratified random	Quantitative (questionnaires)
Total	**70**	**59**		

As indicted in the table above out of 59 respondents, 26 were the actual owners (proprietors) of the business and served as firm executes, while 33 were administrative managers sometimes serving as operations managers. In the category of administrative managers, Senior and Finance managers were included. Respondents were selected from import firms that were highly affected by foreign exchange risks since they deal with foreign currency.

The researcher purposively selected executives from the firms. This was because the study requires the knowledge of foreign exchange risk management meaning that only those employees have knowledge of managing foreign exchange risk were selected and allowed to

participate in the study. Business administrators were selected using stratified random sampling. This was done in order to give them

3.5 Sources of data

Sources of data were classified into primary sources and secondary sources. Primary data involved first hand information that was got from the respondents by use of structured questionnaires and interviews that were self administered to the members of KACITA in Nakawa Urban Council. Secondary data comprised second hand information that involved reviewing of related literature from text books, journals, news papers, web articles and other related literature like the KACITA records on foreign exchange risk.

3.6 Data Collection Instruments

Structured Questionnaire

One instrument, a structured questionnaire was used to collect data. According to Mellenbergh, G.J. (2008), a questionnaire is a research instrument consisting of a series of questions and other prompts for the purpose of gathering information from respondents. The researcher designed structured questionnaires to successfully extract information from the targeted population. The questionnaires were professionally drafted in a way that they included both the open and closed ended questions. The researcher used these questionnaires because they are easy to be administered and they take limited time.

3.7 Reliability and validity of the Instrument

3.7.1 Validity of the Instrument

In order to collect reliable and valid data, the researcher ensured that valid instruments are used. Instruments were also made easy to complete so that respondents were motivated to provide honest responses. Arya et al. (2002), say that a data collection instrument is valid when it

actually measures what it claims to measure. In this research, content valid of the instruments was measured. Bell (2004), affirms that respondents are more likely to honestly complete and return questionnaires they perceive as having relevant content. Therefore, the researcher ensured that all items in the questionnaire had face validity. The words that were used in both instruments were simple clear and related to the research problem. Besides, the instruments were made easy to complete and the total time needed to complete both instruments was limited to about 10 minutes. Furthermore, the questionnaire used simple to understand questions in order to avoid ambiguity and misinterpretation of items by respondents. Additionally, the statements were kept simple in order to avoid any response biases by leading the respondents to agree or disagree with the statement.

Finally, the layout of the questionnaire was condensed in two pages so that multiple pages would not act as a de-motivator for the respondents to comply with the surveys' most important requirement; the willingness of the respondents to respond in a motivated and genuine manner.

With regard to content validity the supervisor, evaluated the questionnaire for its content validity. As recommended by Amin (2005), items that were found to be ambiguous and those judged inappropriate were either eliminated or adjusted. In the content validity test, the validity of each item were evaluated on a scale for which 1 = relevant, 2 = quite relevant 3 = somehow relevant and 4 = not relevant.

The validity of the instrument was tested using the Content Validity Index (CVI). The CVI was measured using the formula:

$$\text{Content Validity Index (CVI)} = \frac{\text{Number of items declared valid}}{\text{Total number of items}}$$

The findings are shown in the table below.

Table 3.2: Content validity index (CVI) of the Questionnaire

Expert(assessor)	Content validity index
Supervisor	0.84

As indicated in Table 3.2, the CVI for the instruments were above 0.80, indicating that the items in the instrument actually measured the study variables. This value was in agreement with Mugenda (2003), who recommended that for an instrument to be valid for research purposes, its content validity index has to be 0.8 and above.

3.7.2 Reliability of Instruments

When an instrument is reliable, it yields consistent responses because it is interpreted well. If the desired variable is not measured reliably, the information obtained would not be correct and therefore not be reliable (Joppe, 2000). Pilot data was collected and used to measure and enhance the reliability of the questionnaire. Data from ten business administrors was collected and entered in the Statistical Package for Social Sciences (SPSS) version 17. A Cronbach alpha coefficient test of reliability was calculated .The variables with an alpha correlation coefficient of at least 0.7 were taken to be reliable (Ahuja, 2005).

Table 3.3: Reliability of the Instrument

Variable	Alpha coefficient
Risk Identification	0.72
Risk Measurement Techniques	0.89
Risk Mitigation	0.71
Firm Performance	0.78
Average	**0.77**

Source: Pilot data

Findings in table 3.3 above revealed that the alpha coefficients of the sub variables making the independent variable of foreign exchange risk management were; Risk identification= 0.724, risk measurement = 0.89, Risk mitigation = 0.71 and firm performance = 0.78. The alpha coefficient for the dependent variable, firm performance was 0.78. All Cronbach alpha coefficients were above 0.70 which indicated that the questionnaire was reliable enough to be used as a research instrument (Amin, 2005).

3.9 Data collection procedure

Primary data was collected using a questionnaire as the major instrument of data collection. These instruments were administered to the study population which included the import firms under KACITA. They were both closed and open ended questionnaires. It is the best instrument for getting qualitative data since they reflect the general opinion on the issues at stake in this research. For the case of quantitative data collection tool, the researcher used self administered questionnaire during data collection that constituted of both closed and open ended questions.

For the case of qualitative data collection tool, the researcher employed an interview whereby face to face questions were asked to the respondents and their responses were noted down by the researcher and research assistants.

3.12 data analysis

Data was analyzed using computer soft ware package known as SPSS and the output were exported to Microsoft word and excel for presentation. The researcher used frequency tables and graphs using percentages to present data about foreign exchange risk. Descriptive statistics were used to describe the population sample with results reflected in percentage and frequencies. The researcher finally used Pearson to analyze the correlation/relationship between the dependent and independent variables.

3.13 Ethical considerations

The researcher ensured that informed consent is adhered to, whereby the respondents participated in the study voluntarily after achieving an understanding of the relevance of the study and the risks involved.

The researcher ensured that the information obtained from the respondents is kept highly confidential and protected throughout its lifetime; and is only accessible to those authorized to access it in order to build trust and security that their privacy is protected.

The researcher ensured that respondents' right to privacy is maintained through seclusion from other people and their information kept from unwarranted publicity.

The researcher through an inquiry centered approach observed, classify the information obtained in categories using standards of measurement in order to interpret data and ensure an unbiased

inquiry. In order to ensure non-discrimination, the researcher treated individual participants equally with fairness irrespective of their race, sex, or any other form of discrimination.

3.15 Limitations of the study

The study is likely to be hampered by the following limitations:

The researcher faced by methodological problems as in interviewing respondents, who in any case were suspicious of ill motives by the researcher. However, an honest, intimate relationship was developed to overcome this.

The researcher was limited by financial constraints to cover cost of paying research assistants transportation, typing, and printing among others. The researcher solicited for funding from parents, relatives and friends

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF FINDINGS

4.1 Introduction

This chapter presents and explains analysis of the study findings. Results include descriptive and Inferential statistics for measurable relationships according to the study objectives below:

i) To investigate the effect of foreign exchange risk identification on the financial performance of import firms in Nakawa Urban Council.

ii) To determine the effect of foreign exchange risk measurement techniques on the financial performance of import firms in Nakawa Urban Council.

iii) To examine the effects of foreign exchange risk mitigations on the financial performance of import firms in Nakawa Urban Council.

4.2 demographic characteristics of the respondents

Table 4.1 below shows frequency distribution by age of the respondents as shown below;

Table 4.1: respondents' Age Characteristics

Age	Frequency	Percent (%)
18-25	14	23.7
25.5-30	15	25.4
30.5-35	14	23.7
35.5-40	12	20.3
40.5 plus	4	6.8
Total	**59**	**100.0**

Source: primary data

Table 4.1 above shows 23.7%(n=14) are aged between 18-25, 25.4%(n=15) are aged between 25.5-30, 23.7%(n=14) are aged 30.5-35, 20.3%(n=12) are aged between 35.5-40, whilst 6.8%(n=4) were aged between 40.5 and above. The responses in the above table 4.1 show that

the import firms are dominated the active and risk taking youth. This implies that the active youth and middle aged have majority influence in managerial role with most full time commitment towards foreign risk management in import firms.

Table 4.2: Gender of the Respondents

Gender	Frequency	Percent (%)
Male	38	64.4
Female	21	35.6
Total	**59**	**100.0**

Source: primary data

Table 4.2 above shows 664.4% (n=38) males outweigh the 35.8% (n=21) females by managerial respondents. Therefore, responses were male dominated to show limited female presence in managerial decision making when it comes to import firms' initiatives to address foreign exchange risk management hence they prefer employing males than females.

Table 4.3 highest level of education of the respondents

Level of education	Frequency	Percent (%)
Certificate	2	3.4
Diploma	16	27.1
Degree	29	49.2
Masters	12	20.3
Total	**59**	**100.0**

Source: primary data

Table 4.3 above shows only 3.4% (n=2) held a certificate in different disciplines, 27.1% (n=16) held at least a diploma in different fields, 49.2% (n=29) had at least a degree in different fields whilst 20.3% (n=12) held at least masters. Results for highest education attainment show about

69.5 percent (n=41) held at least a Bachelor degree while 30.5 percent shared lesser qualifications. This statistics above imply that the employees of the import firms are educated with reasonable knowledge of managing foreign exchange risk.

Table 4.4: the Departments of Attachment

Departments	Frequency	Percent (%)
Production	5	8.5
Sales and marketing	17	28.8
Human resource management	11	18.6
Accounting and finance	26	44.1
Total	**59**	**100.0**

Source: primary data

Table 4.4 above shows that 8.5% (n=5) belong to the production department, 28.8% (n=17) from the marketing and sales department, 18.6% (n=11) from the human resource management whilst 44.1% (n=26) were from the accounting and finance department. A higher percentage of about 41.1% (n=26) out of 59 respondents were from the accounting and finance department with a key experience on the foreign currency exchange rate.

Table 4.5: Period of Service

Period of service	Frequency	Percent (%)
0-2 Years	12	20.3
3-5 years	28	47.5
6 years plus	19	32.2
Total	**59**	**100.0**

Source: primary data

The results in table 4.5 above indicate that 20.3% (n=12) had served in import firms' operation for 2 years, 47.5% (n=28) had served in import firms for at least 3-5 years, 32.2% (n=19) had served in the import firms for at least 6 years and above. The results in Table 4.5 above show

that 79.7% (n=47) who dominated the study had worked with the import firms for at least 3 years. This implies that the study population was dominated by highly experienced respondents and so the responses were based on an experienced point of view. This also implies considerable firm-specific experience in top management and could contribute to a high level of foreign exchange risk management for import firms in KACITA.

Table 4.8 :Legal Status of The Company

Legal status	Frequency	Percent (%)
Sole proprietorship	15	25.4
Partnership	27	45.8
Limited company	17	28.8
Total	**59**	**100.0**

Source: primary data

Table 4.8 above shows frequency distribution graded by legal status of the companies that were involved in the study. 25.4% (n=15) were registered as sole proprietorship, 45.8% (n=27) were registered under partnership whilst 28.8% (n=17) are limited companies.

Table 4.9: Currency Frequently Quoted For Import Transactions

Currency frequently quoted for import transactions	Frequency	Percent (%)
US Dollar	34	57.6
UGX	14	23.7
Euro	4	6.8
Pound Sterling	4	6.8
Japanese yen	3	5.1
Total	**59**	**100.0**

Source: primary data

During the study, the respondents were asked about the dominant currency they frequently quote for import transactions, 57.6% (n=34) frequently quote US Dollar for import transactions, 23.7% (n=14) frequently quote UGX (Uganda shillings) for import transactions, 6.8% (n=4) frequently quote Euro for import transactions, 6.8% (n=4) frequently quote pound sterling for import transactions, whilst 5.1% (n=3) frequently quote Japanese Yen which was shown the least currency option quoted for import transactions. The results in Table 4.9 show that about 76.7% of the import firms frequently quote US Dollar for import transactions implying that majority of the import firms are vulnerable to foreign exchange risks.

4.3 risk Identification and Performance

Respondents were asked to indicate the techniques used to identify risks for their business. The results are shown in table 4.10 bellow,

Table 4.10 Techniques of Risk Identification

Techniques of risk identification	Frequency	Percent (%)
SWOT analysis	7	11.9
Facilitated workshops	9	15.3
Risk questionnaires and risk surveys	6	10.2
Scenario analysis	10	16.9
Using technology	14	23.7
Interviews and self-assessment	4	6.8
We use a process analysis	5	8.5
We do benchmarking with similar organizations	4	6.8
Total	**59**	**100.0**

Source: primary data

Results in Table 4.10 above show that import firms use several techniques in identifying foreign exchange risks and they include; 11.9% (n=7) reported the use of SWOT analysis in identifying foreign exchange risks, 15.3% (n=9) reported the use of facilitated workshops in identifying foreign exchange risks: after the information is completed and collected, a cross-functional management team from the unit or from several units might participate in a facilitated workshop to discuss it, 10.2% (n=6) use risk questionnaires and risk surveys, a risk questionnaire that includes a series of questions on both internal and external events can also be used effectively to identify risks, 16.9% (n=10) use scenario analysis in identifying foreign exchange risk. It is a particularly useful technique in identifying strategic risks where the situation is less defined and "what-if" questions should be explored, 23.7% (n=14) use technology in identifying foreign exchange risk such as Risk checklists, anecdotes, and best practices on the intranet serve as stimulation and motivation for operating management to think seriously about risks in their unit, 6.8% (n=4) use interviews and self-assessment, 8.5% (n=5) use a process analysis, whilst 6.8% (n=4) use benchmarking with similar organizations in identifying foreign exchange risks.

The results in the table 4.10 above show that the methods and techniques used in identifying foreign exchange risks vary from import firm to another. However, they share in come most of the techniques like brainstorming,. use a process analysis, scenario analysis, risk questionnaires and risk surveys are all implemented to identify foreign exchange risks.

Table 4.11: foreign Exchange Risk Identification and Performance of Import Firms

Foreign risk identification and performance	Frequency	Percent (%)
Poor risk identification affects the profits/sales volume	6	10.2
Performance is viewed in profitability perspective	15	25.4
RI has a key strategic contribution on performance of firm	13	22.0
The impact of exchange rate fluctuation suppresses performance	15	25.4
Poor risk identification retards firms' performance	10	16.9
Total	**59**	**100.0**

Source: primary data

The results in table 4.11 above show that 10.2% (n=6) reported that poor foreign exchange risk identification by the import firm with highly influence the profitability and sales volume of the firm. 25.4% (n=15) believed that the existing relationship is that performance of any organization or firm is measured and viewed in a profitability perspective, implying that poor identification of the foreign exchange risk management is reflected in a poor organizational performance in form of low profit margin. 22.0% (n=13) show that risk identification has a key strategic contribution on the performance of the firm especially in the long run. This was followed by 25.4% (n=15) who show that the impact of exchange rate fluctuation suppresses performance as per table 4.11 above. The same table shows that poor risk identification retards organizational performance with about 16.9% (n=10). The result in the table reveals an observed significant positive relationship between foreign exchange risk identification and performance. This substantive relationship implies a better currency risk assessment and strategies is a likely observation for better financial performance. It eventually enhances sales volume and profitability.

4.4 foreign Exchange Risk Measurement and Organizational Performance

In foreign exchange, a relevant factor would be the rate of change of the spot exchange rate between currencies. The study was intended to examine where there is any relationship between Foreign exchange risk measurement and organizational performance the responses are summarized as in tables 4.12 and 4.13 below;

Table 4.12: foreign exchange risk measurement techniques used by import firms

Risk measurement techniques	Frequency	Percent (%)
Value-at-risk model that measures potential loss	14	23.7
Historical simulation	19	32.2
The variance-covariance model	14	23.7
Monte Carlo simulation	12	20.3
Total	**59**	**100.0**

Source: primary data

Results in Table 4.12 above show the techniques of measuring foreign exchange risk with account of 23.7% (n=14) value at risk model employs the historical simulation approach of data of transaction cash flows and simulation, 32.2% (n=19) Historical simulation technique assumes that the past is a good predictor of the future and that the volatility of the analyzed currencies will remain stable, within the parameters observed in the past. This is followed by Variance/covariance (parametric) 23.7% (n=14), whilst 20.3% (n=12) Monte Carlo simulation that usually involves principal components analysis of the variance covariance model, followed by random simulation of the components. The results in table 4.12 above is dominated by 32.2% (n=19) because it was show that the historical simulation is the simplest method of foreign risk calculation that involves running the firm's current foreign exchange position across a set of historical exchange rate changes to yield a distribution of losses in the value of the foreign exchange position

The historical simulation is the simplest method of calculation that involves running the firm's current foreign exchange position across a set of historical exchange rate changes to yield a distribution of losses in the value of the foreign exchange position.

Table 4.13: foreign exchange risk measurement and performance

Risk measurement and firm's performance	Frequency	Percent (%)
Value -at-risk method exposes the risk and scares imports	4	6.8
Risk measurement retards import volume and reduces profits	18	30.5
Risk measurement improves import firms profits in long run	12	20.3
Risk measurement improves on the firms yields/sales volume	10	16.9
a general relationship is the increase in profitability, sales volume and market share	15	25.4
Total	**59**	**100.0**

Source: primary data

Table 4.13 above shows that 6.8% (n=4) value –at-risk method expanses the risk and scares import firms to take risky purchases/imports of certain goods which are sometimes profitable, this is followed by 30.5% (n=18) risk measurement retards import volume and reduces profitability, 20.3% (n=12) risk measurement improves firms' profits in long run, 16.9% (n=10) reported that risk measurement improves on the firms' yields/sales volume, whilst 25.4% (n=15) a general relationship is the increase in profitability, sales volume and market share. Table 4.13 above imply that risk measurement has got a strong relationship with the firms' performance

because the present value of a company is measured from changes in future operating cash flows caused by environmental unexpected changes in currency exchange rates.

4.5 Risk mitigation strategies and performance

Table 4.14 : Risk mitigation strategies

Risk mitigation strategies	Frequency	Percent (%)
Risk avoidance	24	40.7
Currency risk transfer	17	28.8
Currency risk retention	10	16.9
Currency risk reduction	8	13.6
Total	**59**	**100.0**

Source: primary data

Table 4.14 above shows that there are various risk mitigation strategies employed by import firms in mitigating foreign exchange risks, the results in the table shown that 40.7% (n=24) use risk avoidance as a dominant strategy of risk mitigation, followed by 28.8% (n=17) who reported risk transfer, 16.9% (n=10) risk retention and the least strategy was risk reduction as shown by 13.6% (n=8). A high frequency count of about 40.7% (n=24) and 28.8% (n=17) risk transfer imply that many import firms try to either avoid the risk or transfer the burden of risk to other parties such as forward contract, currency futures, forward market hedge, currency swap, currency option, diversification, and international borrowing.

Table 4.15: Foreign exchange risk management and performance

Relationship between foreign risk management and organizational performance of import firms	Frequency	Percent
When FX currency goes down, import firms report low profits	9	15.3
When curacy is high, market share goes down	19	32.2
When controlling risk, some items are left out, low sales volume.	15	25.4
Risk mitigation lowers sales volume, profitability, market share	16	27.1
Total	**59**	**100.0**

Source: primary data

Table 4.15 shows 15.3% (n=9) reported that when foreign exchange currency goes down, import firms report low profitability, low market share, low sales and hence poor performance of the firm, 32.2% (n=19) show that when currency is high, market share goes down because the purchase and importation of certain commodities is minimized, 25.4% (n=15) reported that when controlling foreign exchange risks, import firms are forced to minimize the imports that require foreign currency use and import only those that may accept domestic currency, in this way, the firms' total sales volume goes down which is finally witnessed in form of poor performance of the firm, 27.1% (n=16) risk mitigation lowers sales volume, profitability, market share and the general performance of the firm. Volatile exchange rates do reduce cash flows and profitability of any firm

4.6 Pearson Correlation Analysis

Table 4.16 correlation between foreign exchange risk management and performance

Correlations

		Foreign risk Identification	Risk Measurement	Risk Mitigation
Foreign risk identification and performance	Pearson Correlation	1.000	.861	.671
	Sig. (2-tailed)	.	005	.001
	N	59	59	59
Risk measurement Techniques	Pearson Correlation	.861	1.000	.671
	Sig. (2-tailed)	.005		.045
	N	59	59	59
Risk mitigation strategies	Pearson Correlation	.98	.671	1.000
	Sig. (2-tailed)	.003	.045	.
	N	59	59	59

Source: primary data

Table 16 shows a p-value 0.005<0.05 meaning that there is a correlation between foreign risk identification and the performance of import firms. The p-value 0.045<0.05 implies that there is a correlation between foreign exchange risk measurement and profitability, sales volume and market share hence firms' performance. The p-value 0.03<0.05 means that there exists a strong relationship between foreign exchange risk mitigation measures and performance of import firm implying that effectiveness in risk mitigation will increase the total sales volume, market share as well as the profitability of import firms.

In conclusion, foreign exchange rate risk management has a positive impact on profitability, market share and the total sales volume of import firms. There is evidence of significantly positive linear relationship between foreign exchange risk management, and performance of import firms.

CHAPTER FIVE

DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

In this chapter, conclusions are drawn from the discussed results and findings from previous chapter. The purpose of the study was to establish the effect of foreign exchange risk management on performance of import firms with keen interest in firms under KACITA. Future areas of research thereby suggested. The generated findings here are related to the prevailing literature as per the conceptual framework.

5.2 Discussion

The presented findings are discussed according to research objectives and questions as shown below:-

5.2.1 Risk identification and performance

The results in the table 4.10 above show that there is an existence of correlation between foreign exchange risk identification and the performance of import firms in terms of sale volume, market share and profitability. The findings of the study revealed that the methods and techniques used in identifying foreign exchange risks vary from import firm to another. However, they share income most of the techniques like brainstorming, use a process analysis, scenario analysis, risk questionnaires and risk surveys are all implemented to identify foreign exchange risks. This is in agreement with Giddy and Dufey (2002) who argued that 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. Failure to clearly understand or notice the existence of a certain risk will retard the performance of the imports firm. Businesses that trades internationally or have operations overseas are likely to be exposed to foreign exchange risk arising from volatility in the currency markets. The most common cause of foreign exchange exposure arises from having to make

overseas payments for your imports priced in a foreign currency or receiving foreign currency receipts for your exports. However, exposure can also arise from: Foreign currency borrowing/deposits, overseas subsidiaries. It is also in collaboration with the work of Evans et al., (1985) and Shapiro (2006) who stated that currency risk identification and assessment and strategies will mitigate foreign exchange risk in exposed firms. Barney (2001) relates trade experience and valuable training to focus on profits while Becker (1993) agree that managerial skills, advanced education, knowledge and intellectual capability have key strategic contributions to firm performance in any business environment.

5.2.2 Risk measurement and performance

The results in Table 4.13 shows that 6.8% (n=4) use a value- at- risk method which expanses the risk and scares import firms to take risky purchases/imports of certain goods which are sometimes profitable in return, the total sales, market share and profitability of the import firm reduces tremendously, this is followed by 30.5% (n=18) risk measurement retards import volume and reduces profitability, 20.3% (n=12) risk measurement improves firms' profits in long run, 16.9% (n=10) reported that risk measurement improves on the firms' yields/sales volume, whilst 25.4% (n=15) a general relationship is the increase in profitability, sales volume and market share. Table 4.13 above imply that risk measurement has got a strong relationship with the firms' performance because the present value of a company is measured from changes in future operating cash flows caused by environmental unexpected changes in currency exchange rates.

The collective role of currency risk measurement and strategies has got a strong positive relationship to performance of import firms. This confirms that improvement of foreign exchange risk management in import firms will result into improved financial performance and inadequacies of foreign exchange risk management will cause low financial performance.

The results of the study findings are in agreement with Moosa, (2003) who argued that financial risk is most commonly measured in terms of the variance or standard deviation of a variable such

as percentage returns or rates of change. In foreign exchange, a relevant factor would be the rate of change of the spot exchange rate between currencies. This is also in agreement with Kirt (2008) whose study show foreign exchange risk management is about wealth value in a firm through cost effective and innovative techniques of currency risk control. Import firms were able to identify that foreign exchange risk as a problem to their business profit and sales turnover. This is consistent with studies by Taggert and McDermott (2000) who argued foreign exchange risk is inevitable in import related firms. This is because foreign exchange risk is the dominant financial risk affecting their book value and transactions. The nature of import business holds international currencies as diversified inventory against the unpredictable foreign exchange rates hence active application of currency risk assessment and counter strategies for business survival. Relatedly, Evan et al., (1985) asserted foreign exchange risk management as the outright solution. In addition, it is possible to earn higher profits and sales in currency trade regardless of currency appreciation and depreciation. Basing on the findings in table 4.13 in chapter four of this paper, import firms should work hard to effectively measure the magnitude of foreign risk. Gopinathan (2009a) and James (2009) emphasized profits/sales affect performance and their ratio analysis can be performed from financial statements to measure performance. The results in this table consolidates works by Giddy & Dufey (2002) who asserted that import firms should quantify and report currency risk exposure to determine wealth through loss or profits.

5.2.3 Risk Mitigation and Performance

The findings in Table 4.14 shows that there are various risk mitigation strategies employed by import firms in mitigating foreign exchange risks, risk avoidance as a dominant strategy of risk mitigation, risk reduction, transfer risks and the least strategy was risk retention. A high frequency count of about 40.7% (n=24) risk transfer imply that many import firms try to either avoid the risk or transfer the burden of risk to other parties such as forward contract, currency futures, forward market hedge, currency swap, currency option, diversification, and international

borrowing. This is in agreement with Bradley and Mole (2002) who notes that foreign exchange risk management is a financial function and thus affects the firm`s financial position. Volatile exchange rates do reduce cash flows and profitability of any firm. Belk (2002) states the aim of foreign exchange risk management as limiting volatile forex exposure on the firm's financial performance whereas Shapiro (2006) describes performance in terms of higher profit margin, sales growth and overall liquidity of firm. This relates how currency risk assessment stimulates financial objectives.

5.3 Conclusions

According to the preceding discussions, the following are the conclusions:-

Results show that existence of human capital practices and foreign exchange risk management in import firms. This study provides unique findings on the relationships between foreign exchange risk management, risk identification, risk mitigation and financial performance. There is evidence of significantly positive linear relationship between foreign exchange risk management, and the financial performance of import firms under KACITA, in Nakawa division, Kampala. The risk identification process begins with the team compiling the project's risk events.

The identification process will vary, depending on the nature of the project and the risk management skills of the team members, but most identification processes begin with an examination of issues and concerns created by the project development team. The survey reveals that foreign exchange risk management practices are more valued and applied by management of import firms compared to another other local business that transacts locally using domestic currency. Adoption of currency risk assessment tools is thus aimed to immediately identify, quantify and mitigate effects of foreign exchange risk for sales volume, market share and profit margin from currency spreads. Foreign exchange risk management shows a significantly stronger positive association and predictive contribution to financial performance. In addition, both risk identification, risk measurement and foreign exchange risk mitigation measures had a joint

positive and moderate effect on performance of import firms hence a call for more investment if the import firms are to improves their market share which will improve their total sales volume and so the profitability that will enhance their performance. This further closes the literature gap between foreign exchange risk management and organizational performance in the local context. Both independent variables contribute to target performance in market share, sales volume and profits margin (profitability).

Stock prices and exchange rate are positively related. Frequent appreciation of a foreign currency against local currency makes it difficult to retain local customers because of high prices of imported input that tend to affect prices of their final products sold locally. This therefore implies that a company's profitability fluctuates because of fluctuations in currency being translated into fluctuating prices.

Foreign exchange risk arises when fluctuation in the relative values of currencies affects the competitive position or viability of an organization. Import firms. are exposed to foreign exchange risk if the results of their projects depend on future exchange rates and if exchange rate changes cannot be fully anticipated. Generally, companies are exposed to, transaction exposure, economic exposure and translation exposure

5.4 Recommendations

With findings and conclusion, the following recommendations are presented to management of import firm under KACITA with reference to needful on the improvement in foreign exchange risk management import firms should enforce a foreign exchange risk management plans, operational manuals and framework, which evidently shows the what and how of currency risk identification, assessment, measurement and mitigation procedures and implementation of currency risk management strategies.

Necessary changes should prompt import firms for market efficiency to prevail in a dynamic business and knowledge environment. Identification, monitoring, measurement, evaluation and mitigations should be periodic for opportunities to improve the performance of import firms.

Import firms' management should opt for cost effective risk management strategies for more significant positive relationship between foreign exchange risk management, and the performance of import firms. It would be profitable strategy to adopt them only when possible their costs are low because investment gains are small relative to the firm's size. The gross margin per unit transaction is still meager due to small spreads. Currency risk retention should be used if losses and gains are high during currency fluctuations.

Import firms should network and share their concerns with member firms in the import association and stakeholders in the line ministry like BOU, KACITA, MOF and others who can help them especially in the regulation of monitory policies.

5.5 Areas of Further Research

With a low performance of correlation between foreign exchange risk identification techniques in the study, the researcher suggests that a cross sectional study should be conducted to examine relationship between foreign exchange risk management techniques and organizational performance of import firms.

References

Amin, M.A. (2005). *Social Science Research: Conception, Methodology and Analysis*. Kampala

Abor, J. (2005), *Managing foreign exchange risk among Ghanaian firms*. Journal of Risk Finance volume 6 number 4, pp.306-318.

Allayannis, G., Ihrig, J. and Weston, J.P., 2001, *"Exchange-Rate Hedging: Financial Management*. Vol. 26 No.3.

Allayannis, G., J. Ihrig, and J. Weston, 2001, *"Exchange-Rate Hedging: Financial vs. Operational Strategies."* American Economic Review Papers and Proceedings, Vol. 91 (2), pp. 391–395.

Bank of Uganda (2013). *Bureaux and inter-bank transactions*, Kampala: Research Department.

Bank of Uganda, foreign exchange market operations "an over view of Bank of Uganda policies and procedures", presentations to the East African central Banking course (7th July 2004).

Bell, J. (2004). *Doing Your Research Project: A Guide for First-time Researchers in Education and Social Science* (3rd ed.). New York: McGraw-Hill House.

Barney, J. (1991). *Firm resource and sustained competitive advantage*. Journal of Management, 17, 99-120. doi: 10.1177 /014920639101700108

Bartram, Söhnke M.; Burns, Natasha; Helwege, Jean (September 2013). *"Foreign Currency Exposure and Hedging: Evidence from Foreign Acquisitions".* Quarterly Journal of Finance.

Becker, G.S. (1993). *Human capital*. Chicago: University of Chicago Press.

Belk, P.A, Bidgood, V.H., & Doungploy, O. (1993). *Comparative analysis of UK & US firms* (Research Series No. 13), Loughborough University Business School.

Belk, P.A. (2002). *Managing strategic exchange risks exposures*. Evidence from UK firms.

Belk, P.A., & Glaum, M., (1990). *The management of foreign exchange risk in UK multinationals.* An Empirical Investigation, 21, 3-33.

Bodnar, G. and Gebhardt, G., 1998, *Derivatives Usage in Risk Management by U.S. and German Non-Financial Firms:* A Comparative Survey. NBER Working Paper No 6705, Cambridge, Massachusetts: NBER (August).

Bradeley, K., & Moles, P. (2002). *Managing strategic exchange risks exposures*. Managing

Choi, J. J., and A. M. Prasad (1995), "*Exchange Risk Sensitivity and its Determinants*: A Firm and Industry Analysis of U.S. Multinationals," Financial Management, Vol.24, No. 3, pp. 77-88.

Deloitte & Touche LLP, *The Risk Intelligent Enterprise*: ERM Done Right, Deloitte development LLC, 2006.

Don Hosfstrand (2006). *Foreign Exchange Rates and Their Impact on Trade,* Investment and Profitability in the APEC Region, Occasional Paper No. 145.

Dufey, G and Giddy, H (1995), *Management of corporate Foreign Exchange Risk.* International Accounting and Finance Handbook.

Evans, T.G., Taylor, M.E., & Holzmann, O. (1985*). International accounting and reporting*.(2nd ed.). New York: Macmillan Publishing.

El-Masry, AA., & Omneya, A S. (2007).*Exchange rate exposure ;do size and foreign operations matter?.*Managerial Finance volume 33 number 9,pp 741-765.

El-Masry, A A. (2006).*The exchange rate exposure of UK nonfinancial companies:* industry level analysis Managerial Finance volume 32 number 2, pp.115-136.

Featherson, Littlefield & Mwangi (2006). *Foriegn Exchange Management* .Microfinance

Fatemi, A and Glaum, M (2000), *Risk Management Practices of German Firms* International

Flybjerg, B. (2008). *An International Comparison of National Products and the Purchasing Power of Currencies:* A Study of the United States, the United Kingdom, France, Germany, and Italy (Paris: Organization for European Economic Cooperation).

Garavan, T., Morley, M., Gunnigle, P., & Collins, E. (2001). *The role of human resource management.* Journal of European Industrial Training, 25, 48-68.

Kenyon, A. (1990). *Currency risk & business management. Unpublished manuscript*, Oxford University, Oxford, United Kingdom.

Kiiza, C. (2009, October). *From The Secretariat,* Forex News, 10, 5.

Kipchirchir, D.T. (2008) *Foreign Exchange Risk Management Practices*: A Survey of Motor Vehicle Industry in Kenya, Unpublished MBA Project, University of Nairobi.

Kirt C. B. (2008). *Multinational finance.* New Jersey: John Wiley & Sons Ltd.

Krejcie, R.V., & Morgan, D.W. (1970). *Determining sample size for research activities. Educational and Psychological Measurement*, 30, 607-610.

Levi, Maurice D. (2005). *International Finance, 4th Edition.* New York, NY: Routledge.ISBN 978-0-41 530900-4.

Longin, F.M., 2001, "Beyond the VaR," *The Journal of Derivatives*, pp. 36-48 (Summer).

Madura,J., (1989) , *International Financial Management, 2nd ex.'s Paul, Minnesota* : West Publishing Company

Mellenbergh, G.J. (2008), *Tests and Questionnaires:* Chapter 10: Construction and Administration. In H.J. Ader & G.J. Mellenbergh (Eds.)(With Constructions By D.J Hand), Advising On Research Methods: A Consultant's Companion (Pp. 211—2360). Huizen, The Netherlands: Johannes Van Kessel Publishing.

Moffett, Michael H.; Stonehill, Arthur I.; Eiteman, David. K. (2009). *Fundamentals of Multinational Finance, 3rd Edition.* Boston, MA: Addison-Wesley. ISBN 978-0-32-154164-2.

Mugenda Olive, M. and Mugenda Abel, G. (2003). *Research Methods: Quantitative and Qualitative Approaches*. Nairobi: Acts Press Kenya

Mutebile, E. (2011 January). Currency crisis. *Statement on the Exchange Rate,* Kampala: Bank of Uganda Press.

Oi, H., Otani, A., & Shirota, T. (2004). *The Choice of invoice currency in international trade:* Implications for the Internationalization of the Yen. 27-63

Papaioannou, M., and Gatzonas, E. K., 2002, *Assessing Market and Credit Risk of CountryFunds: A Value-at-Risk Analysis.* In J. Jay Choi and Michael R. Powers (eds), Global Risk Management: Financial, Operational and Insurance Strategies, International Finance Review, 3, Amsterdam: Elsevier Science, pp. 61-79.

Ross, S.,, Westerfield, R., & Jaffe, J. (2005). *Corporate Finance (7th ed.).* Irwin:McGraw- Hill.

Shapiro, A.C. (2007), *Multinational Financial Management*, 9th ed, Willey, New York.

Steve Johnson (2010), *New world currency index launch,* Published: October 24 2010 12:07 Last updated: October 24 2010 12:07, United Kingdom.

Sun, T., Sundaresan, S., & Wang, C. (1993). *An empirical investigation. Journal of Financial Economics,* 34, 132.

Uganda Forex Bureau and Money Remitters Association (2010, December). Members, Retrieved March 09, 2011, from http://www.ugandaforex.com/members.html.University, Oxford, United Kingdom.

Van Deventer, D.R., K. Imai, and M. Mesler, 2004, *Advanced Financial Risk Management*: Tools and Techniques for Integrated Credit Risk and Interest. Rate Risk Management, (Hoboken,New Jersey: Wiley).

Van Horne, J.C. (2002). *Financial Management and Policy.* Singapore: Pearson Education.

versus Operational Strategies", AEA Papers and Proceedings, may, pp. 391 – 395.

Wainer, H., & Braun, H.I. (1998), *Test Validity. Hilldale*, NJ. Lawrence Earlbaum Associates.

APPENDIX 1 QUESTIONNAIRE

KYAMBOGO UNIVERSITY

Dear Respondent,

I am Shallone Namanya Batte, a student of Kyambogo University, pursuing a degree of masters in business administration of Kyambogo University. I am conducting a study on foreign exchange risk management and performance of import firms. This study will help policy makers, management and other stakeholders understand the relationship between foreign exchange risk management and import firms performance.

In order to accomplish this study, I am kindly requesting you to complete this questionnaire. The information provided will be treated with utmost confidentiality.

Thank you for participating and making this study a success.

Researcher; Shallone Namanya Batte

Tel. 0715647295

Instructions

- **Kindly tick the most appropriate option**

SECTIONS A: DEMOGRAPHIC CHERACTERISTICS OF THE RESPONDENTS

1) In which age bracket do you fall?

18-25 ☐ 25.5-30 ☐ 30.5-35 ☐ 35.5-40 ☐ 40.5 and above ☐

2) Please kindly state your gender

Male ☐ Female ☐

4) What level of education have you attained?

Certificate ☐ Diploma ☐ Degree ☐ Masters ☐

Others, specify .....

5) Please state the department you work with in the organization.

.....

6) For how long have you served?

0-2 years ☐ 3-5 years ☐ 6 years and above ☐

7). State which category best describes the legal status of this company.

Sole proprietorship		
Partnership		
Limited company		

Other specify .....

8) Which currency are your import transactions frequently quoted in?

US $(Dollars)		
Pound sterling		
Euro		
Japanese yen		

Other specify .....

Section B: Risk identification and performance

9) What are the techniques of risk identification on the performance of import firms in Nakawa Urban Council? **(Please tick the commonly used techniques).**

Brainstorming	
SWOT analysis	
Facilitated workshops	
Risk questionnaires and risk surveys	
Scenario Analysis	

Using Technology	
Interviews and Self-Assessment	
We use a process analysis	
We do benchmarking with other similar as well as dissimilar organizations	

Others, specify.....

Give reasons why you prefer using the above techniques?

.....

.....

.....

.....

10) How does foreign exchange risk identification impact on the sales volume and profitability of the import firms?

Poor risk identification affects the Profits/sales volume of the import firms which later reflects poor organizational performance.	
Performance can be viewed in financial perspective through profitability and sales volume or growth	
Risk identification, managerial skills, advanced education, knowledge and intellectual capability have key strategic contributions to firm performance in any business environment	
The impact that exchange rate fluctuations have on profitability and the general performance will vary but in many cases it can be significant and suppress the performance of indigenous firms if the financial strategies are not dealt with.	
Failure to clearly understand or notice the existence of a certain risk will retard the performance of the imports firm.	

Others, specify .....

Section C: Risk measurement and performance

11) What are those foreign exchange risk measurement techniques that impact on the performance of import firms in Nakawa Urban Council? **(Please tick the commonly used).**

Value-at-Risk model measures actual and potential loss of portfolio under a certain probability or confidence interval (z %).	
The historical simulation is the simplest method of calculation	
The variance - covariance model assumes	
Monte Carlo simulation	

Others, specify.....

Give reasons why you prefer using the above techniques?

.....

.....

.....

.....

12) In your own opinion, what is the relationship between risk measurement and the performance of import firms?

.....

.....

.....

Section D: Risk mitigation and performance

13) What are the foreign exchange risk mitigation measures?

Risk avoidance	
Currency risk transfer	
Currency risk retention	
Currency risk reduction	

Others specify .....

14) Is there any relationship between foreign exchange risk management and organizational performance of import firm?

Please indicate the relationship in the table below;

Risk identification	**Sale volume**	**Profitability**	**Market share**
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
Risk measurement	**Sale volume**	**Profitability**	**Market share**
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
Risk mitigation	**Sale volume**	**Profitability**	**Market share**
	.....	.....	.....

	.....	.....	.....
	.....	.....	.....
	.....	.....	.....
	.....	.....	.....

Others, specify.....

15) Give reasons for your answers in question 14 above

.....

.....

.....

.....End.....

KYAMBOGO UNIVERSITY

GRADUATE SCHOOL

CERTIFICATE OF CORRECTION OF THESIS

Department ..... Faculty .....

Degree .....

Candidate's No. ..... Signature .....

Registration No: .....

Title of Thesis/Dissertation .....

.....

.....

.....

DECLARATION BY SUPERVISOR OF CORRECTIONS

I have received the required six bound copies of the above named thesis (including the original). I have examined these copies and I certify that the corrections have been made as instructed by the Board of Examiners of this Faculty.

NAME: ..... SIGNATURE .....

(SUPERVISOR OF CORRECTIONS)

DATE .....

NAME ..... SIGNATURE .....

(HEAD OF DEPARTMENT)

DATE .....

NAME ..... SIGNATURE .....

(DEAN FACULTY/SCHOOL

DATE .....

NAME ..... SIGNATURE .....

(DEAN GRADUATE SCHOOL)