THE STORY OF CHF OR HOW TO LOSE YOUR SLEEP AND MONEY BY IGNORING THE FOREIGN CURRENCY RISK

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This paper represents an empiric research how The Central Bank of Switzerland gave up on sustaining the minimum exchange rate for CHF, as a result of a dramatic movement in the history of the FX market. The decision has equally affected companies or families that got loans (usually in another currency than their incomes). Due to the troubles that reached social dimensions in some ECE countries, we decided that it is worth making an academic X-ray upon the way the specialists succeeded in transmitting their experiences to the others. The lessons from history should be learnt, it is the scientists’ duty to use their ability to get into the essence of the phenomena and to reveal the conclusions to the ones around.

Keywords: currency risk, Swiss Franc, double-entry accountancy, moral hazard, loans.

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1. Introduction

The concern for finance and accounting was born together with the subsistence economy within the primitive commune, some of the drawings in the ancient caves being nothing more than early forms of “calculations”: how many animals were hunted and eaten, how many skins were skinned and how many clothes resulted, as Dragan argued (2008).

Together with the developing economy, the “art of calculations keeping” was also developed, the turning point being represented by the mathematic model elaborated by the Franciscan monk Luca Bartolomeo di Borgia more than 500 years ago. Starting from here, the finance and accounting became irreplaceable, without any other alternatives, being in the same time science and art in following the existence and the movement of the capitals.

Even from the medieval period, the Venetian traders began to feel the need of a double entry evidence of the business in foreign currencies they were dealing with other citadels. Just for diminishing the foreign exchange risk and also the risk of cash transportation, they improved the bill of exchange (ital. cambio = change) as an exchange and debts transferring instrument, for thus to permanently benefit from the necessary money support.

According to Dunlop (1985), in 1494, namely 2 years after the discovery of America by Columb, Friar Luca Pacioli Bartolomeo di Borgia was writing and offering to the mankind, for a whole eternity, the work Summa de Arithmetica, Geometrica, Proportioni et Proportionalita (All about Mathematics, Geometry and Proportions).

He was not 50 yet, when the complex work was published in Venice, in which Luca Pacioli was warning the traders that “nobody will go to bed at night, before the debt is equalled by the credit”. Some of us will understand now that, his advice was that nobody remain with unpaid debts, as the debts create troubles and fights. Unfortunately, some of the today’s people did not understand this advice come from the Resurrection age and got indebted over their refund limit and accepted risks unknown to them. This way, we would like to link the history of sciences and the father of accounting on one hand and the way in which, after one half of a millennium, by not admitting or ignoring the foreign currency risk on purpose, lead some of us to higher debts than the ability to pay back.

2. Some Crises Induced by the CHF Exchange Rate

Any person that would like to get informed, may generate, online, variation graphs for the CHF towards another currency, thus acknowledging that, its ups and downs towards the main reference currencies in the world (US Dollar, Euro but also towards the currencies of the Central and Eastern Europe countries) are not small at all. On the opposite, they are quite steep, fact that should worry the
supervisors in the Central Bank, that should have known that the commercial banks action pro cyclical, namely they are interested by the immediate profits and do not think about the long term risks.

We will make an analysis upon the history of the crises caused by the variation of the Euro against the Franc and of the US dollar against the Franc, starting from 1985 and going up to 2008, when the great financial crisis started, not being yet overcome.

The Banking Crisis and the Stock Market Crisis in USA, between 1985 - 1987

The first important appreciation of the Franc towards Euro happened after 1985, when the biggest crisis of the USA banks burst out, after the "Black Thursday" in 1929, as an effect of the banking de-regulation in America of the ‘80s. Consequently, the local saving cooperatives got into more complex financial products that they did not quite control, trying to compete the big American banks, the consequence being that, starting from 1985, many of them were subject to bankruptcy and vanished.

Two years later, in 1987, there followed another crisis on Wall Street, when, on the 19th of October 1987, the Industrial Dow Jones index and also the shares of the biggest American companies fell down with 22%, bringing the negative effects like a genuine tsunami also over the European and Japanese stock markets. In other words, there was a crisis of the CHF/USD rate, out of which the economists and the bankers should have learnt something.

The Crisis in Asia, Russia and Brazil between 1997-1998

The Swiss Franc remained strong after the America’s ‘80s crisis, fluctuating around 1,5 CHF for an American Dollar for the following 10 years, period after which it got stronger and stronger during the period of crisis in Asia, in 1997. The crisis was spread in Russia and Brasil in 1998, thus lowering the dollar’s rate under 1,2 CHF, in 1998 – 1998. Still, in the following 5 years, there followed a shocking depreciation of the Franc, that subtly increased to from 1,2 to 1,8 CHF for one dollar and also towards the European currency at that time, ECU - the Grandfather of the today’s EURO.

The dot.com Crisis from 2000

In 2000-2002, however there burst out a new crisis, the one named dot.com, having as an effect a decrease of the NASDAQ INDEX with 78% in 2002.

Predictably, there followed a new important strengthening/appreciation of the Franc: the rate decreased from 1,8 to 1,1 Francs for 1 Dollar in 2006.

In what the Euro/CHF rate concerns, this decreased from 1,6 in 2000 to 1,4 Francs in 2003. In the next years, there followed a new depreciation of the Franc, together with the economy stabilization, the rate towards Euro increasing from 1,4 to 1,7 Francs in 2008, before the financial crisis began, when, as we all know, there followed a steep appreciation.

What we would like to highlight by a simple empiric research of the phenomenon called the volatility of the exchange rate CHF towards RON, but also towards other currencies of some countries we carefully watched, such as Hungary, Poland, Croatia, is that some have learnt almost nothing from the past mistakes.

What should we learn from this short, but troubled history of the CHF rate? That that the Franc was never peaceful/quiet, that it has always made victims among the ones that were longing for it in its weak moments, while it was ruining their plans when it was getting stronger overnight.

3. Some Effects of the Wrong Management of the Exchange Rate Risk

When they granted loans in Swiss Francs, in 2007 and 2008, the 11 banks that developed operations in Romania, benefited from the fact that the interest rates for this currency were lower than the ones in Euro, without considering the ones in RON that were even prohibitive. From this temporary circumstances, there benefited 2 categories of people: the first category, of the greedy ones or of the FX speculators, that wanted to borrow as much money as possible for low interest rates, to exchange them in other currencies and to lend or place it for higher interest rates, thus achieving easy profits. On the other hand, the second category were the ones that had just only one solution for...
getting loans from the banks as their salaries were too low to access even a modest loan in EURO or RON. Both categories were wrong, because they did not listen to the warning coming from the friar monk Luca Pacioli and went to bed too early, before their debts were covered by current or future sure incomes.

After the crisis in 2008 burst out, the CHF rate exploded, but, on the other hand, also the reference interest rates steeply decreased, for all currencies: both in EURO, in RON and also in CHF. EURIBOR, the index for EURO, reached close to 0, more exactly 0,05% in present, while LIBOR for CHF reached negative levels, of almost – 1%, after The Central Bank of Switzerland has recently decreased the reference interest rate to – 0,75%, once they gave up on the fixed exchange rate that determined the sudden appreciation, with 20%, of the CHF.

As the cost of the loans in Swiss Francs is calculated depending on the LIBOR index for CHF plus a fixed margin and being adjusted once in 3 or 6 months, the banks will apply negative interest rates for their clients in Romania.

What does this mean? For example, if a loan has a fixed margin of 5% plus LIBOR CHF (-1%), then the interest rate will be 4%.

Yet, for the moment, when we are elaborating this paper, the 11 banks in Romania apply the old value of the LIBOR index, valid for the end of 2014, of approximately 0%, and keep the clients' interest rates high. But even so, the interests paid by the Romanians with loans in CHF are currently higher even than the ones in RON.

For example, in OTP Bank, the bank that introduced the loans in CHF in Romania for the first time, the interest rate for the mortgage loans in CHF raises to 6,3%, this being, in fact, the fixed margin of the bank, and the LIBOR index being 0.

At Raiffeisen Bank, that has almost 9.000 loans in Francs, amounting 360 million EURO, the average interest for these loans is of 6%.

In comparison, the average interest rate for the mortgage loans in RON is 4,9% according to BNR, while the annual effective interest rate (DAE), that also includes the commissions, is of only 5,25%.

OTP Bank has recently announced, after the CHF crisis burst out due to the appreciation of this currency with almost 20%, that will reduce the interest rate with 1,5 p.p., but only for a limited period of 3 months. Which means that, the new interest rate will reach 4,8%, namely the level of the RON interest rate. In its turn, Raiffeisen Bank decided to adjust the interest rate for the CHF loans, but only with half p.p., thus it still remaining equal or even higher than the interest for the mortgage loans in RON.

The conclusion is clear: the banks should decrease the interest rates for the clients with loans in CHF even more, if they wish to have some good paying clients, considering that these are strongly affected by the devaluation of the RON towards the CHF with 20%.

In Romania, according to the NBR (Central Bank) data, the population has loans in CHF amounting approximately 10 billion RON, out of which 3,5 billion are loans for houses (35%), the rest being consumption loans and for other destinations. If we consider an average loan of 80.000 CHF, this means that, the Romanians still have 30.000 such loans more.

According to the data from the Credit Bureau, the delays of more than 30 days the people have for the CHF loans amount 1,6 billion RON (16% from the total CHF loans), in a significant decrease comparing with the 2,4 billion RON amounted the last year.

In comparison, the delays for the loans in EURO raise to 4,9 billion EURO towards a total volume of loans in EURO of 51,8 billion EURO, namely almost 10%.

The delays for the loans in RON are of 4,32 billion RON, towards a total volume of loans in national currency of 39,8 billion RON, namely 10,5%. This analysis shows us very clearly that, it is not the CHF that represents the currency with the highest non-performance rate, but the opposite.

4. The Analysis upon the Options of the Various CHF Loans "Stakeholders"

What would be the possibilities to diminish the negative effects of the CHF exchange rate increase towards RON?

Some say (the interested ones, namely the clients and they lawyers) that, a solution would be the loans’ conversion to RON, at the exchange rate that was valid at the date of signing the lending contract. The 11 banks that granted loans in CHF could thus lose 950 million EURO in this case, and this is why they do not accept this solution and either NBR, that supervises the security of the entire banking system, in which, if some are allowed to get sick, there is the risk for the rest to get contaminated.
The value in RON of the 75,000 loans in CHF is currently of 2 billion RON. The most of the loans can be found in Bancpost (32%), Volksbank (24%), Piraeus Bank (20%), Raiffeisen Bank (11%), Banca Romaneasca (7%) and OTP Bank (2%), while the rest of 4% are with the other 5 banks.

Hence, NBR does not agree with applying an administrative measure, by issuing law, for solving the problem of the CHF loans but with finding individual solutions, negotiated between the banks and the clients. The Ministry of Finance stated that they support the NBR’s opinion for this issue, opinion that, otherwise, we also share.

Just that, as predictable, these individual solutions are difficult to agree and take time for being accomplished, not to mention the ongoing lawsuits on this subject, that meaning the prolongation of the agony and crisis. Fact that allows the politicians to continue this days to sustain adopting the laws for conversion at a convenient rate for the clients, most probably just for populist reasons.

Sharing the burden between the bank and the client.

This would mean a conversion of the ongoing loans for a rate of approximately 3 RON for a CHF, rate placed somewhere in the middle, between the rate of 2 RON at the moment of granting the loans, in 2007 – 2008, and the one that exceeds 4 RON for a CHF, in present. The Romanian Banks Association (ARB), specified that the bankers cannot agree with the conversion at another rate than the current one for the day when the conversion is done, according to the European Directive regarding the loans. In the Directive, there is clearly stipulated that, the exchange rate for the conversion is the one valid for the day the conversion is done. In addition, it is said that, “the states can make changes, but as long as they do not apply retroactively”. The parliamentarians however wish that the low is applied also for the ongoing loans, as just this way the law can be helpful for the clients.

Among the other solutions that may be tried is the so-called “electo-rate”, by which the banks will support the new Governmental program for loans restructuring, that aims to reduce the monthly instalments for a period of 2 years. This is accomplished by granting fiscal loans in the guise of a salary tax exemption, but only for the ones with monthly incomes under 2200 RON.

Let’s understand the situation for the countries around.

The clients in Hungary are obliged to refund the loans at the selling exchange rate the bank practices. As against, the clients in Romania, may reimburse the instalments in the foreign currency in which the loan was granted, meaning in CHF directly, currency that they can buy from any exchange office and not being obliged to buy the foreign currency right from the bank they got the loan from.

In Hungary, starting with the 1st of February 2015, the automatic conversion of the loans in various currencies (such as CHF, EURO or Japanese Yens) to the national currency (Forint-HUF) began, according to the laws that were adopted by the Hungarian Parliament by the end of last year (2014).

The authors of the current paper analyzed in which conditions the conversion is done and what The European Central Bank’s opinion towards this measure is. This measure that was toughly criticized last year, but now, could become a model also for other countries in the area, including Romania, where the Parliament debates a law project regarding the conversion of the foreign currency loans into RON.

First of all, it must be highlighted that in Hungary, the conversion is not done at the date when the loans are granted, as some politicians and banks' clients' lawyers erroneously try to accredit.

According to the legislation adopted by the Hungarian Parliament, the conversion of the loans from foreign currency into HUF will be done at a fixed rate, set by the Central Bank of Hungary on the 7th of November 2014, rate that is actually more advantageous than the current one for the CHF, that appreciated with 21% in January 2015.

On the other hand, the law of Hungary also sets some limits for the interests that will be applied to the loans, after their conversion into HUF. Thus, the interest margin of the loans in HUF (plus the local market index, BUBOR at 3 months, the equivalent of the Romanian ROBOR), will remain the same with the one applied to the old foreign currency loans, but not to exceed 4,5 p.p for the mortgage loans and 6,6 p.p. for the consumption loans with mortgage collaterals. The law stipulates that the interest for the loans (formed of these maximum margins plus BUBOR at 3 month) to be the maximum cost of these (The Annual Effective Interest - DAE), that means that, for the banks that practice additional commissions, apart from the interest, this should be accordingly decreased.

In other words, the maximum interest that the banks in Hungary will be able to apply to a mortgage loan in HUF is of 4,5% plus BUBOR at 3 months or of 6,5% plus BUBOR at 3 months, for the
concerning the juridical phenomenon, not before ascertaining one more time that, what we call today debtor must pay back the nominal received amount, regardless its variation. The authors of the current 1864, it is stipulated in what the lending concerns, the “nominalism principle”, according to which the disadvantage, this way breaking the fairness and trustfulness principle.

As the current example of Hungary, that is very often recallable, is not quite suitable for the Romanian realities. Why? Because, over 50% from the CHF loans from Hungary were granted to the local authorities. The States’ interest in solving the problem was obvious, and the way in which the State (the central budget) solved the State’s problem (the local budget) was its decision.

In Poland, the Central Bank is suspected to have artificially strengthened the rate of the local currency towards CHF for making the duty of reimbursement more bearable. The unexpected decision of the National Bank of Switzerland to eliminate the minimum level of the exchange rate EURO-CHF, led to a depreciation with 22% of the Polish Zloty towards the Franc, fact that caused difficulties for the approximately 575.000 families in Poland that have loans in Francs. The protests organized in many cities by the owners of loans in CHF became a political issue in Poland, where, this year, Parliamentary elections will take place. The Polish Government works at a series of plans for converting the populations’ mortgage loans in CHF to Zloty, while the costs of this operation will be bear by the banks and not by the State budget.

According to the authors’ of this work opinion, a law to refer and apply back would be totally unconstitutional and would also trespass the European Directive regarding the loans, as it would create an unbalance towards other currencies, that, in time, also had or might register dramatic rate variations.

Thus, it would generate the so called moral hazard, as it is not moral that a solidarity fund or all the contributors in one country to pay part of the personal use good that some of the banks’ clients got CHF loans for.

Apart the moral hazard, we also appeal to other juridical arguments and, as neutral analysts, we try to balance the facts from as many positions as possible. If we think that, the contractual clause regarding the foreign currency risk was not negotiated, the signed contract being a pre-formulated standard contract, we have to face an unequal juridical position to the bank’s interests advantage and the clients’ disadvantage, the latter representing the weaker contracting party. Thus, the foreign currency risk materializes in the fact that the bank obtains an unjust income to the client’s disadvantage, this way breaking the fairness and trustfulness principle.

On the other hand, it is significant that, in the Art. 1578 from the Romanian Civil Code from 1864, it is stipulated in what the lending concerns, the “nominalism principle”, according to which the debtor must pay back the nominal received amount, regardless its variation. The authors of the current paper, not being professional jurists, prefer to leave aside the area of the empiric researches concerning the juridical phenomenon, not before ascertaining one more time that, what we call today
Foreign exchange rate risk management also existed 500 years before, being called by Luca Pacioli "the necessity to equal the debit with the credit". Also, 150 years ago, it was called by the Romanian Civil Code, the principle of nominalism, namely, of paying back to the creditor the borrowed amount, in the same currency of the loan, regardless the variation of its value, you, the debtor, assuming the entire loss.

Regardless the historical times we refer to, one thing is still unchanged: traders were traders and, even from the Medieval times until today, the creditor, the one who granted money for an interest (even as an admitted, legal activity) targeted a single scope, namely to make profit. The debtors were always forced to pay more (meaning to pay back the loan and also high interests), because they needed money they did not have. This aspect is understandable but, what is more difficult to be understood is why we do not learn from the past mistakes. Why some lend either more than they can pay back, or get amounts in a foreign currency that they do not know and that is inaccessible to them, being different from the currency of their own incomes, thus getting to ignore the foreign currency risk.

If we are to summarize everything into a single conclusion, this would be that, although the risk management is considered to be a relatively young science in its historical dimension, academically recognized under this name only by the seventh decade of the last century, this (the science of the risk management, in general and of the foreign exchange rate, in particular) crossed the entire history, as we have shown all along this paper. As Treapăt affirms (2011: pp. 9-13) "While in the last century, by the '70s, the risk was a notion mainly associated with the natural sciences and less with the financial and insurance theories, in the last years, the concept of risk gained importance among the decision factors in the business world. The loans crisis...starting with the second half of 2008, covered almost the entire planet, due to the contamination effect. This contamination was possible due to the existing strong economic bonds and financial interdependencies caused by the mutual exposures to risk that the main investment and commercial banks in the world, assumed."

5. Conclusion:

The unexpected (for some) decision of the National Bank of Switzerland to eliminate the minimum level of the EURO/CHF exchange rate, caused important financial losses for many persons, mainly for the families that borrowed for buying a house. It is regrettable today, in the era of the online information, that there still exist victims of the lack of information. What is there left to do in such a situation? The authors of the present work consider that, at least us, the ones activating in the academic environment have a mission, namely to analyze the phenomena, the facts in their historical evolution and to state opinions and optimisation proposals concerning the foreign exchange rate risk management to the decision makers (the regulation institutions and for financial-banking supervision, Parliament, Government, banks, etc) but also to our students, the tomorrow’s professionals, and to all that by reading this paper, will be better informed and consequently will have the chance not to make the same mistakes again.

Opportunities and Proposals for Avoiding the Unpleasant Situations Generated by the Foreign Exchange Rate Risk in Future:

1. Transposing the recent Directive of the European Parliament and of EU Council, no. 17/2014 regarding the loan contracts into the Romanian Legislation, represents a very good opportunity to legislate in this field. We have in view that, this Directive regulates, in its Chapter no. 9, art. 23, the loans in foreign currency, and imposes to the member states to adopt a proper regulation frame, that to allow "limiting the foreign exchange rate risk the client is exposed to, as a result of the credit contract", by converting the loan into an alternative currency or by establishing another mechanism for adapting the contract, applicable only in future.

2. All the banks must inform their clients in written, by announcements in the banks' offices, by information messages and even by the letters they send to the clients on different occasions, that signing a loan contract in a certain currency, is a matter that is exclusively linked to the parties’ wish (the debtor and the creditor), and once a loan in a foreign currency is contracted, both the borrower and the bank may stand a lot of negative consequences, result of the foreign exchange rate risk. In the current case, the CHF increased, the consumer being the one that had to stand the foreign exchange rate risk, but the evolution of the exchange rate is not influenced by any of the contracting parties, and tomorrow or just anytime, the bank may be the one to lose.

3. Just for the above exposed reasons, all the players on the monetary and foreign currency market must know and apply the protection instruments towards the foreign exchange rate risk and to the interest rate risk. The foreign exchange risk and the interest rate risk action together as,
buying or selling foreign currency at term, generates foreign exchange rate risk (the correlation of the two kinds of risks is explained in the Annex no. 1), and placing the thus obtained capital, also generates the interest rate risk. For example, when a client buys foreign currency today for paying its future instalments that are due the following month/months, gives birth to foreign exchange rate risk. Placing this temporary available amount, until the due date, by granting a loan in foreign currency, generates the interest rate variation risk. We consider that risk cannot be entirely eliminated, but, limiting and covering the foreign exchange rate risk, implies both the diversification of the portfolio of assets and liabilities in foreign currency and also using certain techniques for reducing the risk, techniques that were developed on the derivatives market, by using some hedging instruments for compensating the risk. The derivate instruments action as FORWARD, FUTURES, OPTIONS, SWAP, FRA operations, that are used both as hedging instruments against the interest rates risk and also against the foreign exchange rate risk.

The authors of this paper know, from the banking practice, that these protection instruments against the risk were extremely little known and used before the methodological framework occurred in Romania (reason for which the notional represents under 10% from the banking assets volume before 2002). They began to be used more, starting with the issuing of the norms regarding the derivate financial instruments, as it is shown by Treapat (2011, pp. 39-40). As a consequence, the authors consider that, it is an obligation for every science person, professor, trainer freelancer or practician in the field of the management concerning the foreign exchange rate risk to promote, to inform the wide public about these protection instruments towards the risk:

- The hedging refers to the strategy that tries to minimize the exposure to the exchange rate fluctuation, this way minimizing the uncertainty of some transactions in foreign currency and giving stability to the incomes. In practice, this is achieved by using the futures and options contracts. When a client makes hedging for his or her exposure (the instalments and the unpaid interests), the objective is to minimize the uncertainty and not to maximize the profit out of the favourable variations of the exchange rate, but in return, it won’t expose the respective client to the potential loss generated by a unfavourable movement of the rate.

- The Forward contracts are actually hedging operations, by signing a sale-purchase contract for an amount in a certain currency against another currency, in future. For covering the foreign exchange rate risk, mostly all the banks offer the possibility of making transactions in foreign currency at term.

As it is practically demonstrated by Treapat (2013 pp. 106-112) in the case studies concerning the derivate instruments, the forward contract on exchange rate represents a flexible instrument of trading, offering the client the possibility to fix his or her own tenors, the level of the traded amounts and the entering moment on the foreign currency market.

The futures trading on the foreign currency market was possible both by granting a credit line dedicated to this product, and by making cash collaterals by the interested company such as a collateral deposit, meant to face the possible losses generated by the foreign exchange rate risk and that is granted to the client, at the moment the forward operation is settled.

The exchange rate (the price of the forward exchange contract) is determined according to the interests parity principle, adjusting the spot rate with the difference between the interest rates for the foreign currencies that are the object of the contract. This difference, that represents forward points or SWAP, may be positive (premium or bonus) or negative (discount).

- The SWAP involves performing the operations in the same time, without modifications for the two rates (spot and forward), as any change might mean a loss or a gain for the bank, depending on the trend of the change. At the beginning of such an operation, there exists a risk of the uncovered amount between spot and forward operations. The quotation made to the client is a sufficient one for the bank, the safety margins being quoted in a more relaxed manner. For the bank, a SWAP is a form of collateral loan, involving a relatively lower credit risk than in the case of lending internal funds. The SWAP operations are forward operations that allow placing some exceeding foreign currency amounts, but that can be performed only for the most important foreign currencies that are quoted both spot and forward. These operations require to the bank to adopt a careful behaviour when selecting the clients, mainly preferring the ones that have a high liquidity, reliable and with acceptable financial performance, thus being necessary the bank to fix exposure limits for each client.

- A futures contract represents an agreement to buy or to sell, a certain foreign currency amount, at a fixed price at the moment of signing the contract, but the transactions being carried out at a date to come. This type of contract is different from the forward contract by the fact that it is sold on the stock market and not negotiated by the parties. The futures contracts may be bought and sold in
any moment, but if a contract has an exchange rate that leads to a progressive loss, then, the contract owner may have to make an additional collateral, as a guarantee for the delivery of funds at tenor.

- The Currency Option represents an agreement by which the seller (the option issuer) grants the buyer (the option owner) the right, but not also the obligation, to perform a certain foreign currency transaction in certain conditions (validity term, price). In present, the foreign currency options are available in almost all currencies in all countries where there exists a liquid foreign currency forward market, that is not restricted by the foreign currency regulations. There exist two basic Options types: CALL (for buying) and PUT (for selling). The CALL option gives the owner the right, but not the obligation, to buy a foreign currency against another one, at a certain date and for a certain price, while the PUT option gives the owner the right not but the obligation, to sell a certain foreign currency against another, in the same mentioned conditions. Both for the buying options and for the selling options, there exist two distinct positions: as a buyer (long) and as a seller (short), the buyer being the one that buys the additional right from the seller, by paying a premium (bonus).

4. Starting from the importers’ example, that have to stand the effects of the foreign exchange rate risk in their turn if the currency of the contract is increasing during the period of time between the contract signing moment and its expiration date, we consider that, also the individuals will also have to be more determined when negotiating with the banks for, at least, partially counteracting the unwanted effects of the foreign exchange rate risk. These potential losses may be counteracted or, at least, diminished, by applying some contractual measures such as choosing the foreign currency of the contract and also by mentioning a certain stipulation about the foreign currency or about the price reviewing, within the contract. Up to the present moment, the credit contract was imposed to the clients by the banks as a standard contract of adhesion, by following the „take it or leave it” principle. In our opinion, it is high time for the clients to impose their own protection measures for themselves within the contracts they sign, as the banking market became favourable to the clients, not to the banks.

6. Introducing or, as the case may be, enlarging the study base of economic sciences, of general management, of risk management, entrepreneurship, finance, accounting, etc, in the Romanian education institutions with technical and economical profile, both for pre-university and university courses. These disciplines fully proved their necessity to be studied, only if we judge through the negative effects we analyzed in this paper. The above mentioned disciplines and not only them, must be taught by professors with an excellent experience, both didactical and practical. In this work, no matter whether we described the doctrines transmitted to us by the father of accounting, Luca Pacioli more than 500 years before, use the scientific arguments the Romanian Civil Code from 150 years before, or we place ourselves towards the European actuality of the latest years, months and even days, we inevitably reach to the same conclusion.

This is what this paper aims to make, to action as a guide that to lead its readers to achieving their target: eliminating the gap between theory and practice, namely the people, the ordinary families to get to know the economic phenomena and the risks described by the specialists in the books but, most importantly, to apply them in their every day lives, for thus not to repeat the errors they make over and over again. Ignoring the laws (be they nature’s, juridical or economic) does not spare any of us of responsibility. And, from this very reason, we elaborated this paper. To know, not to mistake...

Bibliography
Correlating the Foreign Exchange Rate Risk With the Interest Rate Risk

The foreign exchange rate risk can be perceived when losses are registered due to the evolution of the price of one foreign currency in relation with another.

The exchange rate is tightly connected with the interest rate risk. Establishing the exchange rate is based on the theory of purchase power parity, according to which, an identical good, produced no matter where, has the same price. There results that, any modification of the internal prices determines a modification of the foreign exchange rate.

The exchange rate level, in this context, may or not be influenced by the modification of the interest rates in the two countries, as determined by the capitals mobility. The law of the interest rates parity or Fisher’s law becomes, in these circumstances, important.

\[
\text{Interest} = \text{IRD} \cdot \frac{\text{SR} + \text{FR}}{\text{SR}}
\]

According to the theory of the interest rate parity:

\[
d\left(\frac{\text{FR} - \text{SR}}{\text{SR}}\right) = \frac{1 + I_i}{1 + E_i}
\]

Where:
- SR = Spot Rate
- FR = Forward Rate (Usually, over three months)
- I_i = internal interest
- E_i = external interest
- IRD = interest rate differential between Romania and the Euro zone
- a = conversion factor, for reaching to E_i annual model

The Fisher effect confirms the theory of the money neutrality against time, according to which, on a long term, the modifications of the amounts of money will produce effects just upon the nominal variables, and not upon the real ones. In this case, if the inflation rate increases with 2%, the nominal rates will also increase with 2%, fact that means that the real rates remain constant.

Figure 1. The Fischer Effect– The Influence of the Expected Inflation Modification against the Interest Rates


The Fischer Effect explains the impact of the long term interest rates upon the foreign exchange rate. According to Bojesteanu (2010), the long term equilibrium involved by the monetary model, an increase of the interest rate differential between Romania and the Euro zone (IRD) cannot happen else but in price increasing conditions, and thus of the inflation’s, in Romania, (the variables within the Euro zone are considered as exogenous), aspect that justifies a depreciation of the national currency. On a long term, when the total monetary amount increases, we cannot speak anymore about a decrease of the interest rates as, when the prices are perfectly flexible, their level increases, fact that also leads to the increase of the nominal interest rates.