

# Financial Markets

## Chapter Three

Cihan University – Business Administration Department

3<sup>rd</sup> Stage

2023-2024

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# Introduction to Foreign Exchange Markets

**Foreign exchange markets (Forex)** are global decentralized markets where participants trade currencies. These markets are crucial for international trade and investment.

- **Key Participants:**

- **Banks:** Major players in currency trading, facilitating client transactions and engaging in proprietary trading.
- **Corporations:** Use Forex to manage currency risk in international operations.
- **Investors:** Individuals and institutions engage in speculative trading.
- **Governments:** Central banks influence exchange rates and manage currency reserves.

# Exchange rates

An exchange rate is the price at which one currency can be exchanged for another. They are essential for international trade, investment, and financial markets.

- **Exchange Rate:** The price of one currency in terms of another. (e.g., 1 USD = 0.85 EUR)
- **Currency Pairs:** Exchange rates are quoted in pairs (e.g., EUR/USD, USD/JPY).

# Factors Influencing Exchange Rates

- 1. Interest Rates:** Higher interest rates in a country may attract foreign capital, increasing demand for its currency.
- 2. Inflation:** Low inflation rates tend to increase a currency's value.
- 3. Economic Indicators:** Strong economic performance often strengthens a country's currency.
- 4. Political Stability:** Stable governments and policies can attract investment, supporting currency value.
- 5. Market Sentiment:** Investor perceptions and sentiment can drive short-term exchange rate movements.

# How Exchange Rates Affect Global Business Strategies

Exchange rates play a pivotal role in shaping the strategies of businesses operating globally.

## **Exchange Rate Fluctuations:**

Exchange rates constantly fluctuate, impacting international businesses' costs and revenues.

Instability in exchange rates can lead to unpredictability in financial results.

## **Exporting Strategies:**

A strong domestic currency can make exports more expensive for foreign buyers, potentially reducing competitiveness.

A weaker domestic currency can enhance export opportunities by making products more affordable abroad.

# How Exchange Rates Affect Global Business Strategies

## **Importing Strategies:**

A strong domestic currency can lower the cost of imported materials and goods, benefiting businesses reliant on imports.

Currency appreciation can improve the affordability of imports, potentially benefiting cost-sensitive industries.

## **International Expansion:**

Market selection may be influenced by the stability and strength of a local currency.

Businesses must employ exchange rate risk management strategies to protect investments and profitability.

# How Exchange Rates Affect Global Business Strategies

## Currency Risk Management:

Hedging (protecting) techniques, such as forward contracts and options, help mitigate (lessen) the impact of adverse (negative) exchange rate movements.

Budgeting and financial planning with currency risk contingencies are essential for effective management.

## Financial Planning:

Cash flow projections should incorporate exchange rate scenarios to anticipate potential financial impacts.

Consideration of profit margins is critical, as exchange rate changes can significantly affect profitability in different markets.

# Block chain

Blockchain is a distributed ledger technology that underlies cryptocurrencies like Bitcoin and has a wide range of applications beyond digital currencies. It is essentially a decentralized and secure digital ledger used to record transactions across many computers or nodes in a network.

**1. Decentralization:** No central authority, maintained by a network of participants.

**2. Immutable Records:** Data once added is extremely difficult to alter or delete.

**3. Transparency:** Transactions are visible to all network participants.

**4. Security:** Cryptography ensures data integrity and makes it resistant to tampering.

**5. Consensus Mechanisms:** Used to validate and agree on the state of the ledger.

**6. Smart Contracts:** Self-executing contracts automate predefined conditions.

**7. Use Cases:** Applicable in various industries beyond cryptocurrencies.

**8. Efficiency:** Streamlines processes by removing intermediaries.

**9. Trust:** Provides a high level of trust and accountability in transactions.

**Innovation:** A transformative technology with wide-ranging potential.

# Cryptocurrency

Cryptocurrency is a digital or virtual currency that uses cryptography for security. Unlike traditional physical currencies like coins or paper money, cryptocurrencies exist only in digital form. They are decentralized, meaning any central authority, such as a government or central bank does not control them.

## Popular Cryptocurrencies

- **Bitcoin (BTC):** The original and most well-known cryptocurrency.
- **Ethereum (ETH):** Known for its smart contract capabilities.

# Characteristics of Cryptocurrency

- 1. Digital Nature:** Cryptocurrencies exist in digital form and have no physical representation.
- 2. Decentralization:** They are not controlled by any central authority, relying on a distributed network of computers.
- 3. Cryptographic Security:** Cryptocurrencies use cryptography to secure transactions and control the creation of new units.
- 4. Digital Wallets:** Ownership and management of cryptocurrencies are done through digital wallets.
- 5. Public Ledger:** Transactions are recorded on a public ledger called the blockchain, providing transparency.
- 6. Limited Supply:** Many cryptocurrencies have a capped supply, setting a maximum number of coins.

# Characteristics of Cryptocurrency

- 7. Global Use:** Cryptocurrencies can be used and transferred globally, making cross-border transactions more efficient.
  - 8. Resistance to Fraud:** Cryptography and decentralization make cryptocurrencies resistant to fraud and tampering.
  - 9. Volatility:** Cryptocurrency prices can be highly volatile, leading to significant price fluctuations.
  - 10. Diverse Types:** There are thousands of different cryptocurrencies, each with unique features and purposes.
  - 11. Use Cases:** Cryptocurrencies serve various purposes, including digital payments, investments, and value transfer.
  - 12. Regulatory Environment:** They are subject to varying degrees of regulation in different countries.
- Innovation:** Cryptocurrencies are at the forefront of financial and technological innovation.



***Watch a video!***

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Thank you!

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