Research on the Exchange Losses of Multinational Corporations

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Abstract. In the wave of global trade and investment, foreign currency transactions are increasingly frequent, and the risk of currency mismatch is prominent. Academia and industry are deeply studying its impact on the accounting conservatism of enterprises, and seeking to effectively manage this risk through financial derivatives and other means. This paper proposes a solution to introduce a third-party financial platform as an intermediary bridge on the basis of cross-currency interest rate swaps. The proposed model aims to significantly broaden the scope of CCIRS applications, making it easy for more multinational companies to use this financial tool to manage their exposure to exchange rate and interest rate risks. Looking ahead, with the deepening of global economic integration, the exchange rate and interest rate risks faced by multinational enterprises will become increasingly complex and volatile. The cross-currency interest rate swap model based on third-party financial platforms proposed in this paper is expected to provide a practical and efficient risk management tool for many multinational enterprises, help them move forward steadily in the global market, and contribute to the in-depth development of economic globalization.

1 Introduction

Since 2020, profound changes in the global landscape have been intertwined with the ongoing impact of the COVID-19, shaping a more complex and volatile external environment. In this context, the volatility of the exchange rate market has increased significantly, posing a serious challenge to the global fund management and operation of multinational companies. The frequent fluctuation of foreign exchange rates is not only directly related to the financial status of enterprises, but also has become a key factor that cannot be ignored by multinational companies in their global operations. Moreover, according to the forecasts of several international economic institutions, global trade is expected to achieve significant growth in 2024, so corporations need to pay great attention to foreign exchange losses.

In the face of this challenge, how to effectively manage and deal with foreign exchange gains and losses has become an important issue to be solved urgently in the field of financial management of multinational companies.

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There have been previous studies on the exchange gains and losses of TNCs. According to Song and Li, exchange rate fluctuations are influenced by a variety of factors, including economic data, political events, trade relations, and the level of interest rates [1]. According to Zhang, the uncertain impact of exchange rate fluctuations on enterprise value, mainly including transaction risk, economic risk and translation risk, is one of the important goals of enterprise risk management [2]. For a more specific classification of foreign exchange gains and losses, Zou believes that there are three categories: foreign exchange gains and losses on transactions, foreign exchange gains and losses, and adjusted foreign exchange gains and losses [2]. Some of the studies have a positive attitude towards the study of the foreign exchange market, with Song and Li arguing that the foreign exchange market is traded 24 hours a day, divided into three main time zones: Asia, Europe and the Americas. As a result, the foreign exchange market has a large trading volume, providing a wide range of trading opportunities for all types of investors [3]. Zou agrees that companies have recognized the importance of foreign exchange risk management, actively used a variety of risk hedging tools, and are becoming more sensitive to exchange rate fluctuations [4]. Li and Zhang believe that China's guidance on foreign currency translation and its exchange gains and losses was relatively late and relatively simple, while the existing literature has little research on such issues and has a very limited guiding role [5].

In order to better deal with the risks brought by foreign exchange gains and losses, He, Wang and Liu believe that both financial hedging and operational hedging can improve the value of enterprises and reduce their exposure to exchange rate risks, and there is a certain complementary relationship between the two, and high-quality internal control can play a good complementary role in traditional financial hedging and operational hedging [6]. Zou shows that many international investors believe that their exposure to exchange rate risk should also be compensated accordingly [4]. Bai and Wang believe that the government also needs to make efforts on this issue, strengthen the development of foreign exchange market policies, and provide more consulting and information services to enterprises while managing their own foreign exchange risks, and launch foreign exchange hedging products to meet market demand, so as to broaden the hedging channels of enterprises [7].

Although there are many ways to deal with the exchange losses of multinational corporations, these methods have their limitations, so it still need to explore and study new ways for multinational corporations to deal with foreign exchange losses. This article will use the case of Tokyo Disneyland to analyze the limitations of some existing methods (Options and futures, and swap bonds in different currencies）. Tokyo Disney was chosen as an example, because Disney is a multinational company with huge cash flow, and the exchange profits and losses greatly affect Disney's profits. Therefore, Disney has rich experience in processing the exchange gains and losses, which can provide diverse reference value for other multinational companies. The purpose of this paper is to discuss the exchange rate risks faced by multinational companies in the current environment, and to propose innovative and effective management and response strategies to provide strong support for the financial stability and sustainable development of enterprises.

2 Deal with the problem of exchange losses

2.1 Start from internal

Enterprises should build a comprehensive exchange rate risk management system, first of all, establish an exchange rate risk management system, clarify management objectives, principles, processes and responsibilities, and cover risk identification, assessment, monitoring and reporting; Then, on the basis of the system, a special exchange rate

management department can be set up to gather professional forces to quickly respond to and control exchange rate risks, and ensure the standardization and institutionalization of exchange rate risk management. At the same time, a regular risk assessment mechanism is implemented to provide in-depth analysis of market, policy and exchange rate trends, so as to provide strong support for decision-making. Finally, it is necessary to establish a risk reporting mechanism to regularly inform the senior management of the risk status and management effectiveness, so as to achieve comprehensive, timely and efficient management of exchange rate risks [4].

2.2 Start from external

This article will take a closer look at the case of Tokyo Disneyland to illustrate the limitations of multinational corporations in resolving exchange losses by means that are not in-house.

2.2.1 Tokyo Disney

Since the opening of Tokyo Disneyland in 1983, Franchise fees has continued to grow. Disney's management is concerned about the risks that may arise from fluctuations in the yen's exchange rate against the US dollar, especially in the current situation of the yen's depreciation. In 1984, royalty revenues exceeded 8 billion yen, and revenues are expected to grow at a rate of 10 to 30 percent in the coming years as the park attracts more domestic and foreign visitors. To address exchange rate risk, Disney needed to find and implement more effective risk management strategies [8].

2.2.2 Limitations

Option 1: Options and Futures. Futures, options and bank FX forwards generally have a shorter expiration date, typically less than two years, which limits their use in long-term exchange rate risk management. For companies, despite having access to long-term foreign exchange forward contract quotations from banks, banks often view the provision of such services as a financing consideration, which may tie up the company's credit resources. When a company needs to seek additional financing or loans for other projects or operational activities, it may face the dilemma of insufficient credit lines. Not only can this increase the cost of financing, but it can also affect the company's liquidity and overall financial flexibility.

Option 2: Convert US dollar debt into Japanese yen debt. Indeed, long-term reliance on single-currency bond issuance may not only weaken shareholder confidence for companies with high debt ratios, but also gradually push up their financing costs, forming a vicious circle. In addition, financial regulations vary from country to country, as exemplified by the strict restrictions imposed by the Ministry of Finance of Japan on the issuance of Euroyen bonds, which require companies to have a high degree of regulatory awareness and strategic flexibility when raising funds internationally.

3 Solution

3.1 Comprehensive approach

In order to effectively manage the risk of exchange rate fluctuations, a variety of methods have been developed. First, by choosing multiple suppliers and partners to build a flexible

supply chain can reduce the dependence on a single currency or region, thereby mitigating the potential risks caused by specific currency fluctuations [9]. Second, a flexible exchange rate adjustment mechanism can be incorporated into the contract design to ensure that the interests of the enterprise can be protected in the event of adverse changes in the exchange rate. In addition, the active use of the financial derivatives market, such as the purchase of foreign exchange options, futures or forward contracts, can also have positive effects. Finally, through careful planning of cash flow management, enterprises are given the ability to flexibly respond to exchange rate fluctuations to ensure financial stability, so as to comprehensively reduce the impact of exchange rate risks on corporate operations.

3.2 Upgrade the cross-currency interest rate swap method

In the traditional way of using cross-currency interest rate swaps, an authoritative third party (like financial institution) can be introduced.

First of all, a third-party organization can play a role in risk management. Especially in cross-border transactions or situations involving unfamiliar counterparties, third-party institutions play a crucial role in risk management. The third-party institution can conduct a comprehensive and objective assessment of the credit status of both parties to the transaction, including financial stability, historical performance records, market reputation, etc. To a large extent, it helps both parties to the transaction to understand the actual situation of the other party more accurately, so as to achieve risk reduction.

Secondly, in the process of cross-currency swap transactions, a large amount of capital flow and settlement work is involved. As the custodian or clearing party of funds, an authoritative third-party institution can also ensure the safe, timely and accurate flow of transaction funds, and there will be no malicious withholding of funds, which also enhances the trust between the two parties to each other to a certain extent. The introduction of a third party also has the effect of facilitating the smooth progress of the transaction, and in the course of the transaction, if a dispute or controversy arises, the third-party institution can provide neutral and professional dispute resolution and arbitration services to facilitate the continuous progress of the transaction.

In addition, third-party platforms can also integrate similar or identical transaction needs and facilitate larger transactions or split them into smaller transactions through consolidation. This operation requires the third-party platform to split or consolidate orders based on the original transaction terms (such as interest rates, principal amounts, maturity dates, etc.). For transaction parties with minor differences in demand, they can entrust the third-party platform to negotiate and make partial modifications or differentiated treatment to the original order.

4 Expectation

In fact, the above innovative methods have not been well used at present. This article divides the current low enforceability of this method into three main reasons: low liquidity, high credit risk, and complex operation. Therefore, I think the introduction of a global financial platform (similar to swift, Alipay) can largely solve these three thorny problems.

4.1 Market liquidity

At present, a big obstacle encountered in the operation of this method is that it is difficult to find the right trading partner and obtain the right price in time. Therefore, it is hoped that in the future, more companies will have a deeper understanding of the importance of foreign

exchange gains and losses to the company's finances; At the same time, hope that third-party financial institutions can further expand their service scope and depth, and expand the actual needs and operating conditions of enterprises in different industries and different sizes while becoming more international. By building a more comprehensive and detailed enterprise information database, accurately match the needs of both parties of the transaction or lead multi-party transactions, to provide more rapid and effective financial services.

4.2 Credit risk

Another reason why many companies that know the financial importance of foreign exchange gains and losses do not choose the cross currency rate is the distrust of their counterparties. Although the counterparty is assessed for credit before the transaction, credit risk remains. In the event of financial difficulties or default on the counterparty, investors may not be able to recover their principal and interest on time and suffer losses. Therefore, it is expected that in the future, there will be financial platforms jointly led by major countries, and the governments of major countries will jointly supervise the operation of the platforms to ensure that the information(like the real-time market quotation, counterparty information and historical data information and so on)disclosed is open and fair. At the same time, the platform can cooperate with insurance enterprises of these major countries to develop new insurance products for exchange profit and loss trading or jointly launch customized insurance services to provide additional security for investors [10].

4.3 Complex operation

For inexperienced enterprises, the difficulty of the method is too high and it is prone to problems. Cross-currency swaps involve multiple currencies and complex financial terms, requiring investors to have a certain amount of expertise and experience. At the same time, the legal requirements of different regions need to be taken into account during operation. If the relevant practitioners can actively familiarize themselves with the relevant processes, they can also greatly promote the losses caused by exchange rate changes. Or third-party platforms could actively take on this operation business, and third-party platforms could collaborate with universities to precisely train talent that matches this business to meet the current global demand for individuals with the ability to operate cross-currency interest rate swaps.

From the perspective of corporate internal governance, large-scale enterprises often appear relatively insufficient in flexibility due to their large organizational structure and complex decision-making process. This lack of flexibility is particularly evident when cooporating with other companies whose terms differ slightly from those of the original contract. Such transactions often require multiple levels of approval, from front-line business units to middle management to top decision makers, to ensure transaction compliance and risk control. Long approval processes can delay transaction timing, increase transaction costs, and even lead to the loss of potential partner It is hoped that enterprises can consider ways such as simplifying the approval process and delegating the approval authority to improve the efficiency of the company's operation [11]. At the same time, strengthening internal communication and collaboration to ensure the smooth flow of information between various departments is also the key to improve flexibility.

5 Conclusion

This paper explores a variety of strategies for dealing with foreign exchange gains and losses, not only analyzes the inherent limitations and shortcomings of each strategy, but also proposes an innovative solution: integrating third-party financial platform elements into the traditional cross-interest rate swap mechanism. This innovative model first makes full use of the advantages of the cross-interest rate swap mechanism itself in resisting the risk of exchange rate fluctuations. Then, through the introduction of a third-party platform, the threshold for adopting the strategy was greatly reduced, and at the same time, the risk management efficiency and operational flexibility were also significantly improved.

Looking ahead, if the world's major countries can work together to build this third-party financial platform, its effectiveness and credibility will leap to a new level. Such cooperation will not only provide enterprises with more solid and reliable exchange risk management tools in international economic and trade activities, help enterprises effectively resist exchange losses, but also further promote the prosperity and development of international trade and deepen economic ties and cooperation between countries. On the basis of this platform, new ways to work with government agencies and insurance companies can be further explored to design and launch customized insurance products designed to accurately transfer and effectively manage the potential risks that may be encountered as a result of adopting this innovative model.

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