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A STUDY ON FINANCIAL RISK MANAGEMENT

1.BODDU AJAY KUMAR,2. DR.B.RENUKA

[1]MBA STUDENT SCHOLAR, TKR COLLEGE OF ENGINEERING&TECHNOLOGY, HYDERABAD,TELANGANA,INDIA

[2]ASSISTANT PROFESSOR ,TKR COLLEGE OF ENGINEERING&TECHNOLOGY, HYDERABAD,TELANGANA,INDIA

ABSTRACT: Today's money is not equal to tomorrow's money", this says that the money invested today does not have same value tomorrow, the time value of money affects to a great extent. So, one has to consider time value of money when going for investment especially in securities as equity shares etc. because the price fluctuations are very rapid. Every individual wants to save money and instead of keeping it idle he/she wants to invest it further for its appreciation i.e., for the returns earned from it in the future. There are many number of investment alternatives, it depends on the individual who wants to invest as which alternative he has to choose i.e., it depends on the rate of return or the amount of return and risk that the individual expect from the investment. Some individuals want high returns and ready to take high risk, few don't want to take risk and they will be satisfied with the returns they get from the minimum risk. The individuals or the investors who are willing to take risk will go for equity investment, in which they can earn more returns and the other hand those who don't want to take risk or who wants to minimize the risk will go for bank deposits, investments in mutual funds, debenture bonds, preference shares etc, where they can get a fixed amount who don't take risk or avoid risk are called as risk averters. Thus our study is mainly conducted to find out the risk and return that has been associated with the banking stocks of the BSE Banked and also to know the relationship between Banks return and market returns.To study the foreign exchange risk at AurobindoPharma Ltd.To analyze the revenues of the company when the exchange rates fluctuates.To analyze income statement to find out the revenue when the dollars are converted into INR. To study the methodology of risk management adopted by the company.

KEY WORDS: . RISK RETURN ANALYSIS,CONCEPTUAL FRAME WORK,

I. INTRODUCTION

1.1.The Risk Management to Business Success:

Risk management is an important part of planning for businesses. The process of risk management is designed to reduce or eliminate the risk of certain kinds of events happening or having an impact on the business.

1.2.Definition of Risk Management:

Risk management is a process for identifying, assessing, and prioritizing risks of different kinds. Once the risks are identified, the risk manager will create a plan to minimize or eliminate the impact of negative events. A variety of strategies is available, depending on the type of risk and the t

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1.3 Goals of Risk Management:

The idea behind using risk management practices is to protect businesses from being vulnerable. Many business risk management plans may focus on keeping the company viable and reducing financial risks. However, risk management is also designed to protect the employees, customers, and general public from negative events like fires or acts of terrorism that may affect them.

1.4.Process for Identifying and Managing Risk:

While a variety of different strategies can mitigate or eliminate risk, the process for identifying and managing the risk is fairly standard and consists of five basic steps. First, threats or risks are identified. Second, the vulnerability of key assets like information to the identified threats is assessed. **1.5.Strategies for Managing Risk:**

There are as many different types of strategies for managing risk as there are types of risks. These break down into four main categories. Risk can be managed by accepting the consequences of a risk and budgeting for it. Another strategy is to transfer the risk to another party by insuring against a particular, like fire or a slip-and-fall accident.

1.6 CONCEPTUAL FRAME WORK

a. Risk:

The term risk is widely used in day-to-day business for unknown outcome or the loss out of the business. Everyone understands the meaning of the word risk in laymen terms. There is some degree of risk involved in every sphere of life. We are exposed to either take or avoid various kinds of risks in our daily lives. In a more straight way risk can be used to describe any situation in which there is an uncertainty about outcome and the result may be loss.

b. Risk Management:

Risk management is a process to identify loss exposure faced by an organization and to select the most appropriate technique such exposures.

1.8. RISK RETURN ANALYSIS:

All investment has some risk. Investment in shares of companies has its own ris

II.REVIEW OF LITERATURE

2.1.Risk:

The term risk is widely used in day-to-day business for unknown outcome or the loss out of the business. Everyone understands the meaning of the word risk in laymen terms. There is some degree of risk involved in every sphere of life. We are exposed to either take or avoid various kinds of risks in our daily lives. In a more straight way risk can be used to describe any situation in which there is an uncertainty about outcome and the result may be loss.

2.2.Risk Management:

Risk management is a process to identify loss exposure faced by an organization and to select the most appropriate technique such exposures.

2.3.Principles of risk management:

The International Organization for Standardization (ISO) identifies the following principles of risk management:

Risk management should:

- Create value - resources expended to mitigate risk should generally exceed the consequence of inaction, or (as in value engineering), the gain should exceed the pain
- Be an integral part of organizational processes
- Be part of decision making

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- Explicitly address uncertainty and assumptions
- Be systematic and structured
- Be based on the best available information
- Be tailor able
- Take into account human factors
- Be transparent and inclusive
- Be dynamic, iterative and responsive to change
- Be capable of continual improvement and enhancement
- Be continually or periodically re-assessed

Process:

According to the standard ISO 31000 "Risk management -- Principles and guidelines on implementation," the process of risk management consists of several steps as follows:

III.RESEARCH METHODOLOGY

3.1.Process:

According to the standard ISO 31000 "Risk management -- Principles and guidelines on implementation," the process of risk management consists of several steps as follows:

3.2.Establishing the context:

Establishing the context involves:

1. Identification of risk in a selected domain of interest
2. Planning the remainder of the process.
3. Mapping out the following:
   a. the social scope of risk management
   b. the identity and objectives of stakeholders
   c. the basis upon which risks will be evaluated, constraints.
4. Defining a framework for the activity and an agenda for identification.
5. Developing an analysis of risks involved in the process.
6. Mitigation or Solution of risks using available technological, human and organizational resources.

3.3. Identification:

After establishing the context, the next step in the process of managing risk is to identify potential risks. Risks are about events that, when triggered, cause problems. Hence, risk identification can start with the source of problems, or with the problem itself.

- Taxonomy-based risk identification The taxonomy in taxonomy-based risk identification is a breakdown of possible risk sources. Based on the taxonomy and knowledge of best practices, a questionnaire is compiled. The answers to the questions reveal risks.
- Common-risk checking In several industries, lists with known risks are available. Each risk in the list can be checked for application to a particular situation.
- Risk charting This method combines the above approaches by listing resources at risk, threats to those resources, modifying factors which may increase or decrease the risk and consequences it is wished to avoid. Creating a matrix under these headings enables a variety of approaches. One can begin with resources and consider the threats they are exposed to and the consequences of each. Alternatively one can start with the threats and examine which resources they would affect, or one can begin with the consequences and determine which combination of threats and resources would be involved to bring them about.

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3.4.Assessment:

Once risks have been identified, they must then be assessed as to their potential severity of impact (generally a negative impact, such as damage or loss) and to the probability of occurrence. These quantities can be either simple to measure, in the case of the value of a lost building, or impossible to know for sure in the case of the probability of an unlikely event occurring.

Even a short-term positive improvement can have long-term negative impacts. Take the "turnpike" example. A highway is widened to allow more traffic. More traffic capacity leads to greater development in the areas surrounding the improved traffic capacity. Over time, traffic thereby increases to fill available capacity. Turnpikes thereby need to be expanded in a seemingly endless cycles. There are many other engineering examples where expanded capacity (to do any function) is soon filled by increased demand. Since expansion comes at a cost, the resulting growth could become unsustainable without forecasting and management.

The fundamental difficulty in risk assessment is determining the rate of occurrence since statistical information is not available on all kinds of past incidents. Furthermore, evaluating the severity of the consequences (impact) is often quite difficult for intangible assets. Asset valuation is another question that needs to be addressed. Thus, best educated opinions and available statistics are the primary sources of information. Nevertheless, risk assessment should produce such information for the management of the organization that the primary risks are easy to understand and that the risk management decisions may be prioritized. Thus, there have been several theories and attempts to quantify risks.

Numerous different risk formulae exist, but perhaps the most widely accepted formula for risk quantification is: Rate (or probability) of occurrence multiplied by the impact of the event equals risk magnitude

3.5.Composite Risk Index:

The above formula can also be re-written in terms of a Composite Risk Index, as follows:

Composite Risk Index = Impact of Risk event x Probability of Occurrence

The probability of occurrence is likewise commonly assessed on a scale from 1 to 5, where 1 represents a very low probability of the risk event actually occurring while 5 represents a very high probability of occurrence. This axis may be expressed in either mathematical terms (event occurs once a year, once in ten years, once in 100 years etc.) or may be expressed in "plain english" - event has occurred here very often; event has been known to occur here; event has been known to occur in the industry etc.). Again, the 1 to 5 scale can be arbitrary or non-linear depending on decisions by subject-matter experts.

3.6.Identification of risk:

In order to understand the risk in the better manner, it is very important to explore the various types of risk faced by the organization. Risk can be classified according to their origin. The organization mainly adopt strategies to avoid, transfer or mange the various types of risk.

3.7.TYPES OF RISK:

aInterest rate risk
b.Market risk
c.Credit risk
d.Foreign exchange risk
e.Sovereign risk
f.Liquidity risk

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g.Insolvency risk

h.Operational risk

i.Technology risk

j.Off -balance sheet risk

3.8.Foreign exchange risk

Foreign exchange is the mechanism by which the currency of one country gets converted into the currency of another country. The conversion is done by banks who deal in foreign exchange. These banks maintain stocks of foreign currencies in the form of balances with banks abroad. For instance, Indian Bank may maintain an account with Bank of America, new York, in which dollar are held.

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IV.INDUSTRY PROFILE& COMPANY PROFILE

The first Indian pharmaceutical company, Bengal Chemicals and Pharmaceutical Works, which still exists today as one of 5 government-owned drug manufacturers, appeared in Calcutta in 1930. These five public sector drug-manufacturing units under the Ministry of Chemicals and Fertilizers are: Indian Drugs and Pharmaceutical Limited (IDPL), Hindustan Antibiotics Limited (HAL), Bengal Immunity Limited (BIL), Bengal Chemicals and Pharmaceutical Limited (BCPL) and Smith Stanistreet Pharmaceutical Limited (SSPL). In addition, there are a number of pharmaceutical manufacturing units under the control of state governments such as Goa Antibiotics Ltd and Karnataka Antibiotics Ltd. For the next 60 years, most of the drugs in India were imported by multinationals either in fully-formulated or bulk form. There are 24,000 licensed pharmaceutical companies. Of the 465 bulk drugs used in India, approximately 425 are manufactured here. India has more drug manufacturing facilities that have been approved by the U.S. Food and Drug Administration than any country other than the US.

4.1. India:

As regards the pharmaceutical marketing in the world, India is becoming one of the front runner destinations because of its second largest population in the world, the pace of development of its economy, adoption of technological advancements, economical medical treatment cost and also availability of world renowned

4.2. Booming Sales:

India is gaining importance as a manufacturer of pharmaceutical. Between 1996 and 2006, sales of pharmaceutical were up by 9% per annum and thus expanded much faster than the global pharmaceutical market as a whole.

4.3. Medical Tourism:

The concept of medical tourism is an age old concept. In this digital era, half a million people travel across the globe for health purposes. People from developed and affluent countries are moving out of their own countries to other destinations, seeking solitude, natural and holistic remedies and eco friendly experiences. Medical Tourism is one such new area that is ripe with potential.

4.4. Penetration in the world market exports:

The Domestic pharmaceutical sector has been expanding and has is estimated at US$ 11.72 billion (` 55454 crore) from US$ 6.88 billion (` 32575 crore) in last one year. Indian exports are destined to various countries around the globe including highly regulated markets of USA, Europe, Japan and Australia.

4.5. Growing exports:

Exports have been the major growth enabler of the Indian pharmaceutical industry in recent years. India exports

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pharmaceutical products, APIs and intermediates to more than 200 countries across the world. **4.6.Development of India's pharmaceutical industry:**

Up until the 1970s, India's pharmaceutical market was mainly supplied by large international corporations. Only economical bulk drugs were produced domestically by state-owned companies founded in the 1950s and 60s with the help of the World Health Organization (WHO). These state-run firms provided the foundation for the sector's growth since the 1970s. Back then, Indian government aimed to reduce the country's strong dependence on pharmaceutical imports by flexible patent legislation and to create a self-reliant sector.

4.7. COMMITTEES OF THE BOARD:

Committees appointed by the Board focus on specific areas and take informed decisions within the framework of delegated authority, and make specific recommendations to the board on matters in their areas or purview. All decisions and recommendations of the committees are placed before the Board for information or for approval.

4.8. AUROBINDOHAS SEVEN BOARD-LEVEL COMMITTEES, NAMELY:

- The Audit Committee
- The Compensation Committee
- The Governance Committee
- The Shareholders' Grievance Committee
- The Investment Committee
- The Management Committee

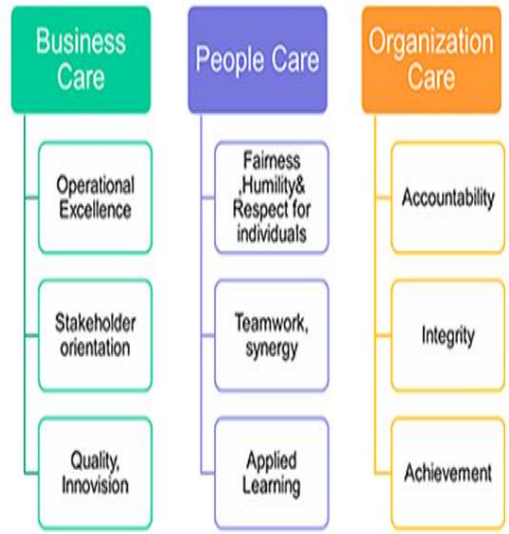

Fig.4.1. AUROBINDOHAS SEVEN BOARD-LEVEL COMMITTEES, NAMELY

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SCOPE OF THE STUDY

- It helps to understand the Profit & loss account of the company and currency
- This study helps to understand the Risk involved in international market.

Exchange rates paradigm in detail

Three years of data helps us to forecast future shifts in exchange rates and hence the scope is extended to analyse the financial strengths of the company.

CONCLUSION

After the detailed study on foreign exchange risk management of AurobindoPharma Ltd it is concluded that the company is using VaR AND Hedging techniques for minimizing foreign exchange risk. To improve rupee viability and preserve profits, exporters need to be efficient and productive and bring down aggregate rupee cost.

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By far the most significant event in finance during the past decade has been the extraordinary use of foreign exchange risk management methods.

The currency futures give the safe and standardized contract to its investors and individuals who are aware about forex market or predict the movement of exchange rate so they will get the right platform for the trading in currency futures. Because of exchange traded future contract and its standardized nature gives counter party risk minimized.

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STUDENT PROFILE

BODDU AJAY KUMAR

He is completed his degree from sreevignan degree college and now pursuing MBA in TKR college of engineering & technology,Hyderabad,Telangana, India.

GUIDE PROFILE

DR.B.RENUKA

Working as Assistant professor in TKR college of engineering & technology, Hyderabad,Telangana,India.