

# Managing Operational Risk in Foreign Exchange Activities

An intensive two-day course detailing how FX trading processes work, what the risks are and how these can be managed and mitigated

## Why you should attend

### Who Should Attend

The course has been specifically designed for operations and business staff at all levels involved in any aspect of foreign exchange.

This include staff from

- commercial banks
- investment banks
- foreign exchange dealers and brokerage companies
- multinational corporations
- money managers
- commodity trading advisors
- insurance companies
- Governments
- central banks
- pension
- hedge funds
- investment companies
- brokers/dealers
- participants in the interdealer market.

The foreign exchange market is the largest and most liquid sector of the global economy. According to the 2004 Triennial Survey conducted by the Bank for International Settlements, foreign exchange turnover averages \$1.9 trillion per day in the cash exchange market and an additional \$1.2 trillion per day in the over-the-counter (OTC) foreign exchange and interest rate derivatives market.

The foreign exchange market serves as a primary mechanism for making payments across borders, transferring funds, and determining exchange rates between different national currencies.



The last decade has seen the diversification and massive expansion of the foreign exchange market. While in the past, commercial banks dominated the market, participants today also include commercial as well as investment banks, foreign exchange dealers and brokerage companies, multinational corporations, money managers, commodity trading advisors, insurance companies, governments, central banks, pension and hedge

funds, investment companies, brokers/dealers, and other participants in the interdealer market.

The increased complexity of the market plus the higher trade volumes have necessitated constant changes in trading procedures, trade capture systems, operational procedures, and risk management tools.

This course provides a solid foundation to all parties involved in foreign exchange activities whether at executive, marketing, audit or operational levels into how the actual trading processes work, what the risks are and how these can be mitigated by using clearly defined Standards of Best

# What is the curriculum focus?

## What the course covers

### The Foreign Exchange Marketplace

We begin this course by setting the scene and examining nature and extent of the foreign exchange market.

- The size of the market
- Who the participants are (both key players and occasional users).
- How the market is developing and its past growth.

### Basic Foreign Exchange Principles



- How foreign exchange operates.
- We provide a range of examples that clearly illustrate the operation of foreign exchange markets in terms of the transactions, how they are processed and how they are settled.
- What does the jargon mean – we explore foreign exchange definitions.
- Foreign exchange settlements – Correspondent banking and Continuous Linked Settlement (CLS).



### Operational Risk

In this session we explore the world of risk.

- What is risk?
- What are the different types of risks that effect foreign exchange operations?
- Why operational risk is 'special'
- How these risks effect the bank

### The Theory of Managing Risk

We explain the basic Operational Risk Model in action, dealing with all the relevant components as they interact with one another

- The Model
- Managing operational risk
- Risk analysis
- Risk impact/frequency

**Case Study.** “A bank, a foreign exchange trading system and operational risk”. This case study illustrates all the aspects of operational risk and is drawn from recent events in a major bank’s trading division.

**For further details please contact**

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# What is the curriculum focus?

## Foreign Exchange Best Practice

- What are best practices?
- We explore how using these practices may also help to reduce the level of risk in the foreign exchange market more generally. How can these practices help reduce operational costs?

## Future Trends in Foreign Exchange

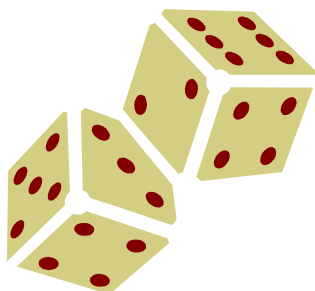
- What are the major trends in the foreign exchange market today and how will they foreign exchange operational risk
- Management's role in effective risk mitigation.
- Why operational risk is 'special'.

## The Foreign Exchange Process Flow



- In this session we the generic view of the foreign exchange process flow, from pre-trade preparation, trade capture, confirmation, netting, settlement, nostro reconciliation, and the accounting & financial control processes. This lays the foundation for a detailed examination of each of these processes, the activities that they entail and the risks and their mitigation.

- Examples are given for each of the processes involved to give the delegate a clear understanding of the key operating and risk issues involved.



## Using Foreign Exchange Best Practice to Manage Risk

The course details a range of practices that will assist in mitigating some of the operational risks that are specific to the foreign exchange industry

We examine each of the seven processes on the following basis;

- The individual process, what it is meant to achieve and how it operates (we cover in turn pre-trade preparation, trade capture, confirmation, netting, settlement, nostro reconciliation, and the accounting & financial control processes).
- What are the risks?
- The best practices used to mitigate these risks.

For each process we show below some of the mitigation factors that will be covered in detail.

## How participants will benefit

By the end of the training, participants will:

- Clearly understand each of the seven stages of foreign exchange trade and settlement, and fully comprehend how each phase is related to the larger process flow.
- Gain knowledge of the varied processes involved in each of the seven stages.
- Have a clear understanding of operational risk in the context of foreign exchange operations and how to use this knowledge to manage their own foreign exchange activities more effectively.
- Obtain a clear insight into practices that may mitigate some of the operational risks that are specific to the foreign exchange industry.
- Understand how acceptance and use of these practices may help reduce operational costs.
- Understand the key best practices that are used in the foreign exchange industry.
- Understand current developments in foreign exchange activities and practices and obtain a clear insight into future trends and directions.

# What is the curriculum focus?

## Pre-trade preparation

- Know your customer
- Documentation requirements
- Master netting agreements
- Agreement on trading and operational practices.

## Trade capture

- Entering trades
- Using Straight-Through-Processing
- Use of real-time credit monitoring
- Standing settlement instructions.

## Confirmation

- Special requirements for confirming by non-secure means (structured or non-standard trades confirming by telephone)
- Controls electronic trading platforms



- Verify expected settlement instructions
- Netted transactions
- Internal transactions - Block trades and split allocations
- Third-party advices
- Confirmation matching process
- Exception processing and escalation procedures.

## Netting

- Online settlement netting systems
- Bilateral net amounts
- Cut-offs for netting
- Consistent operational practices and documentation.

## Settlement

- Real-time nostro balance projections
- Electronic messages for expected receipts
- Cancellation and amendment facilities
- Payment failures
- The settlement process and settlement exposure
- Crisis situations outside your organization.

## Nostro reconciliation

- Nostro account reconciliation
- Identifying non-receipt of payments
- Operational standards for nostro account users.



## Accounting & financial control processes

- General Ledger reconciliation
- Daily position and Profit & Loss reconciliation
- Daily position valuation
- Trade prices for Off-Market Rates.

## General Best Practices for Managing Foreign Exchange Operations Risk

- Segregation of duties
- Business and operational roles
- Understand operational risks
- Procedures for introducing new products
- new customer types, or new trading strategies
- Control system access
- Audit/risk control groups
- Operational performance measures
- Outsourcing & industry standards and best practices
- Record keeping
- Contingency plans.