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**Research Paper**

**A PROJECT REPORT ON EXPLORING CURRENCY DERIVATIVES:  
TYPES, APPLICATIONS, AND THEIR ROLE IN GLOBAL FINANCIAL  
MARKETS WITH REFERENCE TO HDFC**

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**ABSTRACT**

Now a day's all the technological changes are being made in the competitive environment. In all fields computerization as taken place. In case of stock exchange also they go for on line trading. So the investors have to be aware of online trading procedure, in order to know the minute-to-minute changes in trading in stoic exchanges.

The main aim of this study to make the investor aware of the online trading procedures, and the disadvantages from it. When the investor come to know the changes in the trading in stock exchanges, then only he can sell or buy the securities which give high return and in order to minimize the risk. The online trading system displays the overall changes in the world of trading per second. So the knowledge of online trading is must for every investor.

The online system displays the graphs of senses, Nifty, and the risk and return of a security which the investor need to invest and displays the profile of the company, dividend declare by that company. The main advantage to the investor is that he can buy and sells shares by sitting at home instead of calling the broker and ordering him to buy or sell.

Futures or future contracts are transferable specific delivery forward contracts. They are agreements between two counter parties that fix the terms of an exchange, or that lock in the price today of an exchange, which will take place between them at some fixed future dates.

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**I. INTRODUCTION**

Each country has its own currency through which both national and international transactions are performed. All the international business transactions involve an exchange of one currency for another.

The foreign exchange markets of a country provide the mechanism of exchanging different currencies with one and another, and thus, facilitating transfer of purchasing power from one country to another.

With the multiple growths of international trade and finance all over the world, trading in foreign currencies has grown tremendously over the past several decades. Since the exchange rates are continuously changing, so the firms are exposed to the risk of exchange rate movements. As a result the assets or liability or cash flows of a firm which are denominated in foreign currencies undergo a change in value over a period of time due to variation in exchange rates.

This variability in value of assets or liabilities or cash flows is referred to exchange rate risk. Since the fixed exchange rate system has been fallen in the early 1970s, specifically in developed countries, the currency risk has become substantial for many business firms that was the reason behind development of currency derivatives.

The financial environment today has more risks than earlier. Successful business firms are those that are able to manage these risks effectively. Due to changes in the macroeconomic structures and increasing internationalization of businesses, there has been a dramatic increase in the volatility of economic variables such as interest rates, exchange rates, commodity prices etc. Firms that monitor their risks carefully and manage their risks with judicious policies enjoy a more stable business than those who are unable to identify and manage their risks. There are many risks which are influenced by factors external to the business and therefore suitable mechanisms to manage and reduce such risks need to be adopted. One of the modern day solutions to manage financial risks is 'hedging'.

The project is all about what are the hedging instruments (Currency Derivatives) available in India and how the business corporations are using currency derivatives as a risk management tool.

## II. SCOPE OF THE STUDY:-

- To know what is foreign exchange and what are the various foreign exchange services.
- To know how the transactions related to foreign exchange volatility carried out.
- To have a brief knowledge about various foreign currencies and their exchange rates compare to other nations currencies.

## III. NEED AND IMPORTANCE OF THE STUDY

The world nations are increasingly becoming more interrelated global trade, and global investment. These international result in

cross country flow of world nations. Countries hold currencies of other countries and that a market, dealing of foreign exchange results.

Foreign exchange means reserves of foreign currencies. More aptly, foreign exchange refers to claim to foreign money balances. Foreign exchange gives resident of one country a financial claim on other country or countries. All deposits, credits and balances payable in foreign currency and any drafts, travelers' cheques, letters of credit and bills of exchange payable in foreign currency constitute foreign exchange. Foreign exchange market is the market where money denominated in one currency is bought and sold with money denominated in another currency. Transactions in currencies of countries, parties to these transactions, rates at which one currency is exchanged for other or others, ramificataion in these rates, derivatives to the currencies and dealing in them and related aspects constitute the foreign exchange (in short, forex) market.

Foreign exchange transactions take place whenever a country imports goods and services, people of a country undertake visits to other counties, citizens of a country remit money abroad for whatever purpose, business units set up foreign subsidiaries and so on. In all these cases the nation concerned buys relevant and required foreign exchange, in exchange of its currency, or draws from foreign exchange reserves built. On the other hand, when a country exports goods and services to another country, when people of other countries visit the country, when citizens of the country settled abroad remit money homewards, when foreign citizens, firms and institutions invest in the country and when the country or its business community raises funds from abroad, the country's currency is bought by others, giving foreign exchange, in exchange. Multinational firms operate in more than one country and their operations involve multiple foreign currencies. Their operations are influenced by politics and

the laws of the countries where they operate. Thus, they face higher degree of risk as compared to domestic firms. A matter of great concern for the international firms is to analyze the implications of the changes in interest rates, inflation rates and exchange rates on their decisions and minimize the foreign exchange risk. The importance of the study is to know the features of foreign exchange and the factors creating risk in foreign exchange transactions and the techniques used for managing that risk.

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#### **V. OBJECTIVES OF THE PROJECT**

The basic idea behind undertaking Currency Derivatives project is to gain knowledge about currency market.

Primary objectives:

- To study the basic concept of currency future.

- To study exchange traded currency future.
- To analyze different currency derivatives products.

Secondary objective:

- To know how the currency futures are used as risk management tool.
- To analyze income statement and find out the revenues when the dollars are converted into Indian rupees.
- To study the different types of foreign exchange exposure including risk and risk management techniques which the company is used to minimize the risk.
- To present the findings and conclusions of the company in respect of foreign exchange risk management

**VI. METHODOLOGY**

All the data and information is collected by me from different sources for the preparation of this report. To prepare this report, I have adopted following methodology.

**Primary data:**

- The primary data has been collected from experts, officials and employees working in HDFC LTD.

**Secondary data:**

- For secondary data, I have use internet. Links are given for the same.

**LIMITATIONS**

- The study is confined just to the foreign exchange risk but not the total risk.
- The analysis of this study is mainly done on the income statements.
- This study is limited for the year 2021-2024.
- It does not take into consideration all Indian companies foreign exchange risk.
- The hedging techniques are studied only which the company adopted to minimize foreign exchange risk.

**DERVATIVES**

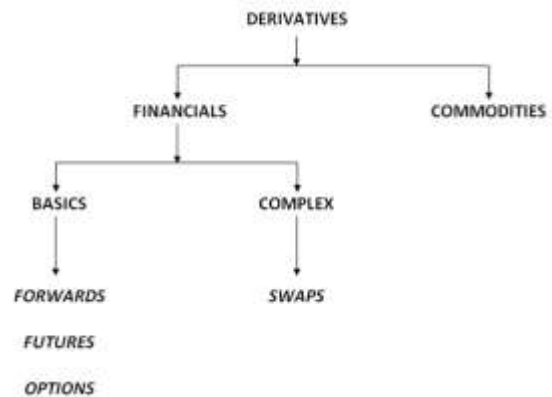
In the Indian context the Securities Contracts (Regulation) Act, 1956 [SC(R)A] defines "Derivative" to include-

1. A security derived from a debt instrument, share, loan whether secured or unsecured, risk instrument or contract for differences or any other form of security.
2. A contract which derives its value from the prices, or index of prices, of underlying securities.

➤ The Underlying Securities for Derivatives are :

1. Commodities: Castor seed, Grain, Pepper, Potatoes, etc.
2. Precious Metal: Gold, Silver
3. Short Term Debt Securities: Treasury Bills
4. Interest Rates
5. Common shares/stock
6. Currency derivatives

**V. TYPES OF FINANCIAL DERIVATIVES**



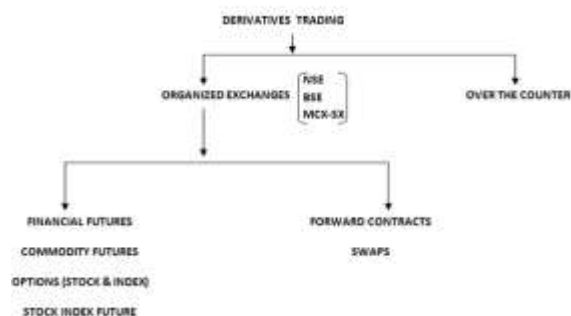
One form of classification of derivative instruments is between commodity derivatives and financial derivatives. The basic difference between these is the nature of the underlying instrument assets.

In commodity derivatives the underlying instrument is commodity which may be wheat,

cotton, pepper, sugar, jute, turmeric, corn, crude oil natural gas, gold, silver, zinc and so on.

In financial derivatives the underlying instrument may be treasury bills, stocks, bonds, foreign exchange, stock index etc. it is to be noted that financial derivative is fairly standard and there are no quality issues whereas in commodity derivative, the quality may be the underlying matters.

## TRADING OF FINANCIAL DERIVATIVES



Derivatives traded at exchanges are standardized contracts having standard delivery dates and trading units.

OTC derivatives are customized contracts that enable the parties to select the trading units and delivery dates to suit their requirements.

A major difference between the two is that of counterparty risk – the risk of default by either party. With the exchange traded derivatives, the risk is controlled by exchanges through clearing house which act as a contractual intermediary and impose margin requirement. In contrast, OTC derivatives signify greater liability.



## CURRENCY FORWARDS MARKETS

Forward contracts are agreements to exchange currencies at an agreed rate on a specified future date. The actual settlement date is more than two working days after the deal date. The agreed rate is called forward rate and the difference between the spot rate and the forward rate is called as forward margin. Forward contracts are bilateral contracts (privately negotiated), traded outside a regulated stock exchange and suffer from counter-party risks and liquidity risks. Counter Party risk means that one party in the contract may default on fulfilling its obligations thereby causing loss to the other party.

An important segment of the Forex derivatives market in India is the Rupee forward contracts market. This has been growing rapidly with increasing participation from corporates, exporters, importers, banks and FIIs. Till February 1992, forward contracts were permitted only against trade related exposures and these contracts could not be cancelled except where the underlying transactions failed to materialize. In March 1992, in order to provide operational freedom to corporate entities, unrestricted booking and cancellation of forward contracts for all genuine exposures, whether trade related or not, were permitted. Although due to the Asian crisis, freedom to re-book cancelled contracts was suspended, which has been since relaxed for the exporters but the restriction still remains for the importers.

## THE FUTURE MARKET

Futures is a standardized forward contract to buy (long) or sell (short) the underlying asset at a specified price at a specified future date through a specified exchange. Futures contracts are traded on exchanges that work as a buyer or seller for the counterparty. Exchange sets the standardized terms in term of quality, quantity, price quotation, date and delivery place (in case of commodity).

### Features:

The features of a futures contract may be specified as follows:

- ✚ These are traded on an organized exchange like NSE, BSE, MCX etc.
- ✚ These involve standardized contract terms viz. the underlying asset, the time of maturity and the manner of maturity etc.
- ✚ These are associated with a clearing house to ensure smooth functioning of the market.
- ✚ There are margin requirements and daily settlement to act as further safeguard.
- ✚ These provide for supervision and monitoring of contract by a regulatory authority.
- ✚ Almost ninety percent future contracts are settled via cash settlement instead of actual delivery of underlying asset.

Futures contracts being traded on organized exchanges impart liquidity to the transaction. The clearinghouse, being the counter party to both sides of a transaction, provides a mechanism that guarantees the honoring of the contract and ensuring very low level of default.

### Types:

Following are the important types of financial futures contract:

- ✚ Stock Future or equity futures,
- ✚ Stock Index futures,
- ✚ Currency futures, and
- ✚ Interest Rate bearing securities like Bonds, T- Bill Futures.

## VI. FINDINGS

1. There is not much change in percentage of operating profit.
2. As currency of other country is increased or decreased there exists volatility in net operating income.
3. As foreign exchange rate is sensitive phenomena that affect the profitability of the company, the company should make study of the impact of exchange rate volatility on its profitability in different foreign markets.
4. To have expanded knowledge on impact on company's profitability when foreign exchange rates changes, various statements like cash flow, funds flow, etc need to be checked.

Total revenues are assumed as 80% domestic and 20% foreign and total expenses are assumed as 80% foreign and 20% domestic, thus this factor affects both incomes and expenses when exchange rate is increased or decreased.

## SUGGESTIONS

Often, foreign ships travel through India and dock their vessels at various ports / harbors in the country. One of the major requirements during such temporary stays, is that of FCY Cash that has to be made available to the Captain of the Ship for covering Crew wages or for other expenses on board the ship.

These requirements are usually met through a facility called "Cash to Master". To collect this cash, the master of the ship has to approach the branch with his passport and a duly filled up application form. This product is available only in United States Dollars, Pounds Sterling and Euro Currencies.

Foreign exchange facilities can be availed by customers at any of our branches transacting in Foreign Exchange. You can buy FCY Cash, TC's and FCY DD's from any our branch and also encash your TC's and Cash at our branches.

Foreign Exchange can be availed against payments by Cash, Cheque or Pay Order/ Demand Draft. A maximum of Rs. 49,999/- (as per Indian Tax Laws) will be accepted in cash and any amount above Rs. 49,999/-, against a Pay Order or Cheque after clearance of the same. You need to carry the required Documentary Proof for issuance of Foreign Exchange.

## VII. CONCLUSION

By far the most significant event in the finance during the past decade has been the extraordinary development and expansion of financial derivatives. These instruments enhance the ability to differentiate risk and allocate it to those investors most able and willing to take it a process that has undoubtedly improved national productivity growth and standards of livings.

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

Initially only NSE had the permission but now BSE & MCX-SX has also started currency future contracts. It shows that how currency future covers ground in the compare of the other available derivative instruments. Last month MCX-SX ranked top amongst all three with more than 50% trades of currency futures contracts in India in sense of volumes and number of contracts also.

Not only big business houses, exporters and importers use this but individuals who are interested and having knowledge about forex market they can also invest in currency future. At Marwadi Shares also many individual investors are investing in currency futures.

Exchange between USD-INR markets in India is very big and along with it other currency contracts of Euro, Pound and Japanese Yen are in the market and attracting the investors which is the reason behind higher growth rate of currency futures in India.

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- ✚ [www.economywatch.com](http://www.economywatch.com)
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- ✚ [www.moneycontrol.com](http://www.moneycontrol.com)
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### Books

- ✚ NCFM: Currency Future Module
- ✚ CDBM Workbook
- ✚ Recent Development in International Currency Market