Regulation of foreign exchange operations of commercial banks in financing construction projects

Aynura Kanybekovna Askarova1, Elvira Sheishembekovna Satylganova2, Asel Kubatbekovna Samaibekova3, Umut Maratovna Omurzakova3, Elnura Idirisbekovna Murzalieva3

1Jalal-Abad State University named after B.Osmonova, Jalal-Abad city, Kyrgyz Republic
2Kyrgyz National University named after Zh. Balasagyn, Bishkek, Kyrgyz Republic
3Kyrgyz State Technical University n.a.I.Razzakov, Bishkek, Kyrgyz Republic

Abstract: This article is devoted regulation of foreign exchange operations of commercial banks in financing construction projects. The expansion of international relations and internationalization of economic life, especially in view of the foreign economic activities of enterprises, make it necessary to study currency operations in special currency markets. In this context, commercial banks play an important role in reducing financial risks, especially currency risks in financing construction projects. Over the years of existence of the currency market in Kyrgyzstan, the experience of currency operations, currency trading and currency services for corporations and individuals has been accumulated, which proves the efficiency and profitability of such operations. In addition to receiving commissions, commercial banks also play a role in the financial stabilization of national monetary systems and international payment and settlement systems. In the context of inter-bank competition, the range of services offered to satisfy the foreign exchange needs of market participants is steadily growing, thanks to the development of international trade integration and considerable simplification of monetary circulation in the currency operations of banks around the world. The purpose of this study is to reveal the need for regulation of currency transactions in financing construction projects and in the financial-credit system and the digitalization of these processes.

Keywords: financial-credit system, currency, regulation, commercial banks, digitalization, foreign exchange transactions, currency risks, construction, projects

1. Introduction

The bank's foreign exchange operations include the purchase and sale of foreign currency, currency conversion, processing of foreign currency loans and deposits, international payments and money transfers, and foreign exchange risk management. Currency transactions would not be possible without currency exchange and quotes. The quotation of a currency is the determination of the exchange rate of that currency. In the interbank foreign exchange market,
exchange rates are quoted mainly against the dollar, which is generally recognized as an international settlement and reserve asset.

The bank carries out foreign exchange transactions, including the purchase and sale of foreign currency, conversion, issuance of loans and deposits, international payments and risk management. For effective risk management and optimization of profitability the Bank uses methods of analysis of volumes and structure of operations, profitability and efficiency of resource utilization, as well as risks and their management. The difference between seller's and buyer's rates serves to cover the bank's expenses and to insure the currency risk. Banks are interested in attraction of clients for currency operations and have to possess enough own funds for quoting rates for transactions of certain volume. Competition forces banks to cut their margins.

A foreign exchange transaction in financing construction projects is a mutual obligation of the parties to exchange currencies at a certain rate on a predetermined date. Cash currency transactions can take the form of cash transactions or foreign exchange forward contracts. Cash transactions are carried out on a spot basis and are mostly used to obtain foreign currency immediately in order to avoid possible exchange losses due to fluctuations in exchange rates, as well as to move capital quickly. The currency is delivered to the buyer immediately upon conclusion of the transaction or at the latest within two business days. This type of transaction is the most mobile element of currency position and is connected with a certain risk degree. Therefore, for insurance purposes, banks conclude forward transactions for a period not exceeding six months. The parties agree on provision of a fixed amount at a fixed rate by a fixed date. The bank undertakes to record the KGS equivalent of the currency purchased or sold at the agreed exchange rate on the date of receipt of foreign exchange proceeds, regardless of changes in the KGS exchange rate against the currency in the period between the receipt of payment in foreign currency and the conclusion of the guarantee transaction. However, this type of transaction, like futures, swaps and options, is very rarely used by commercial banks. This is due to the fact that the country is just at the beginning of the transition period preceding the development of market relations and the creation of a strong economy, and therefore a strong national currency.

2 Materials and Methods

This article is based on methods of analysis containing analysis of scientific and practical publications in the field of scientific problems, as well as economic and statistical methods involved in the analysis of the subject area.

The movement of capital from one country to another, monetary settlements for goods and services, as well as credit and settlements related to non-commodity transactions are important in foreign economic relations. With the abolition of the currency monopoly, commercial banks were allowed to engage in foreign exchange transactions in financing construction projects. However, not all commercial banks may engage in foreign exchange transactions, but only those banks that have obtained a license from the NBKR to conduct foreign exchange transactions. This license allows banks to engage in the following types of foreign exchange activities [1]

- opening and keeping settlement currency accounts for their clients
- making international payments for import, export, and non-commodity transactions through correspondent accounts at authorized banks; and
- establishment of correspondent relations with authorized banks and foreign banks on the territory of the CIS countries.
- Provision of credit services for raising and placing foreign currency in the country.
- Both residents and non-residents open currency accounts with authorized banks to make foreign economic payments. To open a foreign currency account, the client-legal entity has to provide to the commercial bank the following documents:
  - Application form for account opening
  - Certificate of registration of the legal entity at the national statistical office
  - A copy of the Articles of Association, a copy of the Memorandum of Association authenticated in accordance with the established procedure;
  - Two cards with specimen signatures and seal impressions;
  - A certificate of registration with the tax authorities.
- Individuals willing to open a foreign currency account shall submit the following:
  - Application form for account opening.
  - Identity card of the client.

The departments of currency operations in the financial and credit system institutions in their work will be guided by the NBKR and other legislative acts of the Kyrgyz Republic and perform:
- Duties and functions of the Currency Operations Department
- customer service
- Qualitative customer service
- Carrying out primary accounting;
- Improvement and implementation of new methods of international settlements.

Functions of the Currency Operations Department
- Developing and adopting departmental procedures;
- Providing recommendations to improve accounting, reporting and interbank operations related to foreign exchange transactions;
- Advising clients engaged in foreign economic activities on import and export transactions.
- Developing and amending the document flow of the Currency Operations Department as necessary;
- Participate in solving issues and proposals related to automation of banking operations within the competence of the Department and the department.
- Banks Monitor correspondent account balances in the head office on a daily basis.
- Analyze and forecast the activities of the bank subdivisions.

When opening a current account in a foreign currency, employees of the back office explain the procedure for opening an account, the terms of opening and servicing the account, as well as the regulations on working with clients of the back office. All documents submitted for current account opening are checked for validity and compliance.

Upon submission of the documents, the back office employee opens the current currency account and enters the following data into the program "Transaction Date" and the currency accounts register: balance account, personal account, name of the account owner, date of opening the current account. Prepares two copies of the Agreement on effecting cash settlements in foreign currency, signed and certified. It is also signed jointly by the Director of the Bank and the client and certified by the seals of the parties to the agreement. A password is established with the client, which allows the client to obtain the necessary information about the movement of funds on the client's current account by means of telephone contact. However, under no circumstances can the client be informed by telephone about the amount of receipts and the balance of the current account. Collect all submitted documents and keep them in a separate file/folder for each account opened (corporate folder for legal entities, general folder for individuals). The folder with the client's documents is kept in a safe. The first copy of the card with the specimen signature and seal shall be kept in the file cabinet. The second copy of
the card with the specimen signature and seal shall be handed over to the employee of the cash management department who keeps the second copy of the client card.

That is, the account shall be debited when purchasing currency and credited when selling it.

Banks may charge a fee for maintaining foreign currency accounts. Commissions are set by commercial banks independently. Banks may charge interest for keeping foreign currency in an account. Foreign currency accounts are used to record export earnings transferred from abroad for the provision of goods, works and services, foreign currency purchased on the domestic market, dividends, income in foreign currency, and contributions in foreign currency to the charter capital of joint ventures.

Currency regulation in financing construction projects is the activity of the state aimed at regulating the settlement and procedures for transactions with monetary value. By means of currency regulation, the state puts currency operations, lending and borrowing to foreign legal entities and individuals, import, export and movement of foreign currency abroad under state control in order to maintain the balance of payments and currency stability.

The main areas of foreign exchange regulation include exchange rate management, capital controls, and financial sector monitoring.[2]

The purpose of foreign exchange regulation is to ensure a stable economic situation in the country, protect its currency and financial system, reduce the risks of financial crises, ensure the competitiveness of the economy and support international trade.

The principles of foreign exchange regulation include financial stability, transparency and predictability, balance and flexibility, risk control and cooperation with international partners.

To fulfill these goals and principles, the central bank and other regulatory bodies may use such measures as changing the level of interest rates, introducing exchange rate restrictions and capital controls and monitoring capital flows and the financial market. Regulating the foreign exchange operations of commercial banks is necessary for the following purposes:

- Protecting the national currency. The regulation of foreign exchange operations allows the government to control the exchange rate and prevent it from changing sharply, which helps protect the national currency from sharp losses in value.
- Risk Reduction. Foreign exchange regulation helps reduce the operational risks of commercial banks and increases the reliability of the foreign exchange system as a whole.
- Capital controls. Currency regulations give the government the ability to control capital flows, which helps prevent unwanted capital flight abroad.
- Countering financial crime. Foreign exchange regulations help combat financial crimes, including money laundering, terrorist financing, and other forms of fraud.
- Improving economic stability. Currency regulations can also be used to encourage exports and limit imports, which helps improve a country's economic stability.

3. Results

Overall, effective currency regulation in financing construction projects is necessary to maintain a healthy global economy that benefits all people. Using these methods, governments can help ensure stable prices, sustainable growth, and financial security for all.

Methods of currency regulation are important to keep prices stable, economies growing sustainably, and people feeling financially secure.

There are several basic methods that countries use to regulate their currency and maintain economic stability. The first is currency regulation, which involves controlling the value of a country's currency in relation to other currencies on the world market.[3] Another method is capital controls, which limit the amount of money brought into a country.
In general, these methods help to ensure price stability, sustainable economic growth, and the financial security of the people. It is important for governments to carefully consider and implement these measures to promote sustainable growth and prosperity.

Banks will also be required to implement sound risk management practices to identify potential vulnerabilities in their currency operations.

With this growth, however, comes the need for increased regulation to ensure that these transactions are conducted safely and responsibly.

To meet this challenge, regulators are taking action by imposing stricter compliance requirements on banks engaged in foreign exchange transactions. This includes raising reporting standards, mandating the use of secure electronic platforms, and strengthening government oversight.

Banks themselves will also be responsible for implementing sound risk management practices to identify potential vulnerabilities in their currency transactions. In doing so, they will help minimize the risk of financial harm to both themselves and their customers.

4. Discussion

Banks are exposed to foreign exchange risk because of their international activities. Therefore, it is important for them to have a well-defined risk management strategy. This strategy should include both quantitative and qualitative methods to help the bank identify, measure and manage its foreign exchange risk. By understanding the risks associated with currency movements, banks can make informed decisions about how best to protect their profits and minimize losses due to changes in market conditions.

Banks face a growing need to manage foreign exchange risk to ensure safe and responsible foreign exchange transactions. As the industry evolves, regulators are becoming more stringent.

Banks are facing an increasing challenge to manage the risks associated with foreign exchange in financing construction projects. Because the industry is evolving at such a rapid pace, there is no room for error or complacency. We must be vigilant and responsible in our transactions, taking all necessary precautions to ensure that we navigate the ever-changing landscape of exchange rates.

Banks must understand how exchange rates affect their business and take steps to mitigate the risks associated with them. This includes hedging strategies, diversifying portfolios, and being aware of any potential changes in exchange rates. By managing these risks, banks can ensure that they remain profitable even in volatile markets.

Simply put, foreign exchange risk management is crucial for banks because it helps us protect ourselves from losses caused by fluctuations in exchange rates. By closely monitoring these changes and adjusting our strategies accordingly, we can minimize the impact of any unexpected changes and protect our financial interests.

Moreover, as regulators become increasingly strict about compliance, it is more important than ever for banks to prioritize their foreign exchange risk management practices. Banks cannot afford to take shortcuts or cut corners when it comes to protecting our clients' investments and ensuring the stability of the banking system.

Effective foreign exchange risk management is essential for banks operating in today's complex financial environment. Banks face a complex financial world in which currency risks can make or break their success. To stay on top, it is critical to manage these risks effectively. Banks have an obligation to ensure the safety and security of their customers' assets.

Table 1 Weaknesses and Strengths of Foreign Exchange Risk Management at Commercial
Banks | Weaknesses | Strengths
--- | --- | ---
Necessity of constant monitoring and analysis of exchange rates market | Ability to protect the bank from potential losses related to changes in exchange rates |
Need to constantly update and improve the tools and methods used | Ability to offer customers flexible and efficient tools for currency risk management |
Risks of imperfection of methods used for currency risk assessment | Possibility to save costs and increase bank profitability thanks to efficient exchange rate risk management |
Potential for errors in calculations and decision making in currency risk management | Enhance the bank's reputation through effective foreign exchange risk management |
Need for well-prepared and trained specialists to manage the currency risk | The ability to diversify the investment portfolio and increase its stability due to proper currency risk management |

Currency risk management in financing construction projects is becoming increasingly digital. This means using technology to help companies keep track of changes in currency values and avoid losses. This is an exciting time for companies looking to manage their risk more effectively. With digital tools, they can track currency rates in real time and make informed decisions about buying or selling currencies. The benefits are obvious: less uncertainty, higher efficiency, and ultimately higher profits. [4]

Innovative tools now use advanced algorithms to analyze market trends and predict potential risks. They provide real-time updates and alerts so you can make informed decisions quickly and confidently.

Gone are the days of manually tracking currency rates and worrying about unexpected losses. Key areas of digital currency risk management at commercial banks:[5]
- Using digital tools to automate currency risk management processes, such as forecasting, analysis and risk monitoring systems.
- Development and implementation of specialized software products that will enable foreign exchange risk managers to better understand, monitor and manage their risks.
- Training bank employees to manage currency risk through digital tools and technologies, such as e-courses and simulators.
- Using analytical tools and machine learning to identify and analyze risks and decide on strategies to manage those risks.
- Developing risk management systems that allow banks to manage currency risks in real time using data collected from various sources.[6]
- Using blockchain technology to improve the authentication and security of currency risk management processes.

As banks become increasingly reliant on technology and digital services, risk management strategies are needed to ensure the security of customer data and financial transactions. Risk management strategies should include a thorough assessment of potential risks such as cyberattacks, fraud and compliance issues. Banks must also consider the impact of new technologies, such as artificial intelligence (AI) and blockchain, on their risk management strategy. In addition, banks must develop a comprehensive plan to respond to any potential risks.
By taking these factors into account when developing a risk management strategy for banks, they can protect their customers' data and financial assets by taking advantage of new technologies.[7]

**Conclusion**

One of the economic measures taken by the government to improve the financial system of Kyrgyzstan was the liberalization of the monetary system, which allowed the main financial institutions - banks - to engage in foreign exchange transactions. The main objective of commercial banks is to extract maximum profit. There are various ways by which banks can make a profit. These are expanding the range of services offered by the bank, increasing the prices of the services offered, and reducing the costs of banking activities. [8] Among the many factors that determine the level of prices for banking services, the main ones are creating a competitive market environment, expanding the supply of banking services and the regulatory role of the state, mainly through the setting of discount rates by national banks.[9]

Banking activities are characterized by the fact that the partnership between banks and their customers is based on mutual benefit, that is, the interests of both parties are most effectively combined to generate profits. At the same time it should be remembered that banks can achieve their goals only by satisfying the needs of their customers. Therefore, it is extremely important for banks to optimally structure these interests and their activities in terms of time and service delivery in both active and passive areas of business.

If a few years ago commercial banks were only exchanging currency in financing construction projects, conducting payment card operations, arranging encashment and issuing guarantee certificates. New banking technologies require a high level of specialists. Thus, competitive banks consider not only the quantitative and qualitative indicators of their activity, but also the qualitative side of bank work. [10]

The following suggestions should be made.

Secondly, the bank should pay special attention to innovative operations in the field of currency operations.

Firstly, the bank should develop its strategy to improve the quality of currency operations management.

The banking sector is one of the most important sectors of any country's economy. It is also one of the most vulnerable sectors to currency risk because of its global nature. For banks to effectively manage their currency risk, they need to adopt advanced technologies such as artificial intelligence (AI) and machine learning (ML). These technologies can help banks identify and predict potential currency risks, allowing them to take proactive steps to mitigate them.

Using them, banks can better understand their currency risks and understand how different currencies might move in the future. This allows them to develop more effective strategies to manage currency risk and reduce losses due to exchange rate fluctuations. In addition, AI-powered tools can help banks automate routine tasks such as data collection and analysis, allowing them to focus on more strategic risk management tasks.

**References**
