trade. But there are a number of ways companies can reduce some of the risks inherent to international trade. By reducing risk (or hedging) and maintaining the same return, the net return on trading internationally rises. As international trade has grown, so has the availability of services and products to manage the associated risks.

Given that exchange rate volatility is one of the main risks associated with international trade, several risk management techniques exist so as to reduce, or at least spread, that risk.

In 1972, currency futures were first introduced. The holder of a currency future agrees to either purchase or sell a fixed amount of foreign currency on a future date at a fixed exchange rate.[38] Options contracts are similar to futures, except the holder has the right, but not the obligation, to purchase or sell foreign currency by a future date at an agreed exchange rate.

By the early 1980s, another instrument was developed to manage currency risk. A currency swap is an exchange of liabilities in two different currencies.[39] If a French firm wants to raise U.S. dollars and an American firm requires French francs, each can borrow domestically where it is likely to receive more favourable loan terms and agree to a swap. Both companies benefit by obtaining funds more cheaply than if they had directly accessed their desired currency market. The French company pays, in dollars, the U.S. company's debt and the U.S. company pays, in francs, the French company's debt, presumably out of the proceeds of export sales into each other's market.

Swaps are also used to reduce the cost of borrowing. If interest rates are lower in a foreign market or a company or government has already borrowed heavily in domestic markets, a swap can be arranged to take advantage of lower borrowing costs abroad. The borrower acquires funds in the foreign market and swaps back to the domestic currency.

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[38] The forward market in foreign exchange is an informal network of banks and brokers set up to trade contracts similar to futures except they are not standardized.

[39] The explanation of currency swaps and their use is drawn from B. Solnik, *International Investments*. Second Edition, New York: Addison-Wesley Publishing, 1991, pp. 176-7. The term "swap" generally refers to interest rate swaps, where the payment terms of two liabilities are exchanged. Typically, a swap involves the exchange of fixed-rate and flexible-rate debt instruments.