

Economic exposure to exchange rate risk and financial hedging: Influence of ownership as a governance mechanism 🛒

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Purpose

The purpose of this paper is to examine the potential non-linear relationship between family ownership as a governance mechanism and exchange rate exposure of firms that use financial hedging.

Design/methodology/approach

The exchange rate exposure is estimated using two-factor Jorion (1990) model for a sample of 312 Indian firms over the period from 2001 to 2016. The cross-sectional regression model is used at the second stage to investigate the effects of family ownership on exposure for the firms that use currency derivatives.

Findings

The results suggest a significant non-linear cubic relationship between family ownership and exchange rate exposure. Exchange rate exposure increases with family ownership at low and high levels (as a result of improper hedging) and decreases with family ownership at intermediate levels (as a consequence of value-enhancing hedging).

Practical implications

The study has practical significance for firms to understand the circumstances in which currency derivatives usage is ineffective in alleviating exposure. Firms that have high or low family ownership should integrate operational hedges with financial hedges and should incorporate other firm-level governance mechanisms to avoid the misuse of derivatives.

Originality/value

This study provides new evidence that the relationship between family ownership and exchange rate exposure is non-linear for firms that use financial hedging which has not been investigated before in the prior literature.

Keywords: [India](#), [Family ownership](#), [Exchange rate exposure](#), [Financial hedging](#)

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