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Exposure to FX Rate Risk

A Qualitative Analysis of German Fair Trade Importers

Master Thesis

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Abstract

The aim of this paper is to investigate the exposure of Fair Trade (FT) importers in Germany, operating based on the principles of the World Fair Trade Organization (WFTO), to foreign exchange (FX) rate risk in the light of the current depreciation of the Euro. The ongoing high volatility of the Euro exchange rate strongly affects Fair Trade companies that import products mostly from developing countries and sell them in the European market.

Previous research about hedging foreign exchange risk exposure focused either on large international corporations or on small and medium sized enterprises (SMEs) in terms of their derivative use. However, these studies insufficiently discuss the exposure of micro and small Fair Trade businesses. Their distinctive feature is rooted in the Fair Trade principles such as non-interest bearing pre-financing, lack of pass-through possibilities and Minimum Price.

Using a four-stage qualitative research approach, we gained a unique data set conducting semi-structured interviews with CEOs of Fair Trade companies and financial institutions. Thereby, we can make statements about how micro, small and medium sized Fair Trade importers perceive and manage their FX exposure. Furthermore, we investigated how the demand arising from this exposure can be hedged using derivates.

Our results suggest that vast majority of Fair Trade importers perceive FX volatility to have a strong impact on their businesses. Moreover, most Fair Trade importers do not know how to deal with currency volatility. We find indication that Fair Trade Importers cannot draw on financial instruments provided by banks since their specific derivative demand is mostly below the invisible line of €50,000. This situation is condensed in the FX exposure framework. Our findings indicate that a possible solution can be achieved by pooling a number of smaller hedging demands into larger tradable batches.

Key words: Fair Trade, FX Exposure, Hedging, SMEs, Sustainable Finance

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Abbreviations

CEO	Chief Executive Officer
CNY	Chinese Yuan Renminbi
EFTA	European Fair Trade Association
eG	Eingetragene Genossenschaft (German for ‘Registered Cooperative’)
FLO	Fairtrade Labelling Organisation
FT	Fair Trade
FX	Foreign Exchange
GmbH	Gesellschaft mit beschränkter Haftung (German for ‘Limited Liability Company’)
IFP	International Fisher Parity
LLC	Limited Liability Company
Mn	Million
NAFTA	North American Free Trade Agreement
NEWS!	Network of European Worldshops
OTC	Over the Counter
SME	Small and Medium Sized Enterprises
TCA	Thematic Content Analysis
USD	United States Dollar
WFTO	World Fair Trade Organisation
WLDV	Weltladen-Dachverband (German for ‘Umbrella Organization of Worldshops’)

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1 Introduction

> *"If the exchange rate stays at this level or the depreciation even continues, we will be out of business in half a year maximum." (General Manager of a company that works with 120 different supplier families)*

From close to $1.40 for €1 in May 2014, the exchange rate dropped to $/€ 1.25 until January 2015, and continued to drop to a 12 year-low of $/€ 1.05 in mid-March 2015 (Bloomberg Business, 2015) – a depreciation of more than 20 percent. Undoubtedly, the recovering US economy, as a result of the Federal Reserve's loose monetary policies and the ongoing economic uncertainty in Europe, have led to this development (Sjolin, 2015). Additionally, in order to fight deflation, the European Central Bank presented an aggressive easing program in January 2015 announcing to buy €60 billion in government bonds on a monthly basis starting in March 2015 and ending in September 2016 (ARD-aktuell, 2015).

On February 26, 2015, the 'Jährliche Lieferantenkonferenz der Weltläden', an annual conference of registered suppliers of the Worldshops in Germany took place. Those micro, small and medium sized businesses supply more than 470 Worldshops in Germany with Fair Traded products from around the globe (Weltladen-Dachverband, 2015). The depreciation of the Euro was a major topic among the suppliers and they were desperate for solutions. Many companies reported that they face serious impacts from the depreciation, as their purchasing power in their purchase markets has decreased significantly and their domestic margins are increasingly shrinking. Of course, the depreciation not only hits companies operating in the Fair Trade sector, but eventually affects companies of all sizes. However, there are several factors that distinguish Fair Trade businesses from other companies and make their exposure to foreign exchange risk unique.

> *"The current currency depreciation is unique in 40 years of Fair Trade business and hits us [the Fair Trade Importers] tremendously. Especially, as most of us pre-finance up to 100 percent of our supplier's production months before delivery, the situation is more than serious. We have established a partnership of trust with our producers and contrary to traditional commerce, we are price takers. They [the producers] tell us how much money they need to cover their costs, we evaluate their offers and agree if we consider them to be reasonable." (General Manager of an established Fair Trade player)*

Fair Trade businesses operate alongside special business principles with the goal to drive sustainable partnerships with suppliers. Most of the products are bought in developing and emerging countries in Africa, Latin America and South-East Asia. As part of the business model, purchases are pre-financed and sometimes other interest-free credits are provided. In addition, another central point in the Fair Trade business model is fair pricing. Producers are paid a Minimum Price which is designed to cover all costs of sustainable production regardless of whether the world's market prices have decreased or not. When market prices lie above the Fairtrade Minimum Price, producers should receive the current market price or the price negotiated at closing (Altman, 2010; Dragusanu, Giovannucci and Nunn, 2014; FLO, 2015; Sukhamay, 2013). This means that price fluctuations are not be passed through to Fair Trade producers. Traditional wholesale, on the contrary, is usually looking for the lowest purchasing price possible. The purchase habits are not the only factors distinguishing Fair Trade businesses from other businesses. Being rather small and often having an unfavourable legal form, credits in the home market are expensive and hard to obtain. Additionally, Fair Trade companies mainly purchase in foreign currency, yet generate their income almost exclusively in domestic currency.

> *"As we operate under the legal form of an incorporated association, we are not allowed to build up capital. All profits have to reflow directly into our charitable activities. Until today, we have been able to absorb losses with the little cash that we were holding. But those reserves were used up very fast." (General Manager of an established Fair Trade player)*

All the aforementioned reasons highlight the uniqueness of the Fair Trade importer's situation which led us to postulate that FX volatility hits Fair Trade importers differently than traditional companies and therefore calls for examination. As basis for our study we started to analyse the Fair Trade market consisting of Fair Trade principles and the business models of Fair Trade importers. Moreover, our research is related to several studies by Smith and Stulz (1985), Hagelin and Pramborg (2004), Afza and Alam (2011), Peterson and Schweser (1980) as well as Copeland and Joshi (1996) among others who focus on hedging as a general risk management tool. Those papers analyse the mechanics as well as the pros and cons of hedging FX rate risk exposure using derivatives. In addition, the studies discuss how companies manage their FX exposure and whether hedging creates or destroys company value. The majority of academic papers discussing the topics mentioned above concentrates on large international corporations. However, as our target group ranges among micro, small and medium sized companies, the literature review is expanded to scrutinising the special characteristics of SMEs towards managing FX exposure. In doing so, we looked at studies by Pennings and Garcia (2004), Smith and Stulz (1985) and Ehrlich, Woodward and Tiong (2012) who put a special focus on the different type of risk exposure and the difference in organizational structure.

To our knowledge, no research to date recognizes the special needs of micro, small and medium sized Fair Trade organisations and discusses their FX exposure. Our study will contribute to existing literature by shedding light on the unique needs of Fair Trade businesses towards managing FX rate risk exposure and aims to close the gap in literature identified above. Examining the FX exposure of Fair Trade businesses will become more and more important as there is a strong trend towards sustainable business models (KPMG International, 2013) on the one hand and sustainable investment opportunities (Deutsche Bank Group, 2012; McKinsey&Company, 2011) on the other hand. As sustainable commerce is one of the current and future trends, micro, small and medium sized companies will need adequate financial products and other strategies to cope with the FX rate risk.

The objective of this thesis is to investigate the current exposure of Fair Trade importers to FX rate risk in the light of the depreciation of the Euro. The complexity of the topic discussed in this thesis calls for a systematic structure. Therefore, the following three research questions will aid in developing an understanding of the unique situation of these companies.

- How do micro, small and medium sized Fair Trade importers perceive FX exposure?
- How do they manage this exposure?
- How can the demand arising from this exposure be hedged using derivates?

In order to answer the research questions stated above, a combination of secondary as well as qualitative primary research was used. The reason behind conducting a qualitative study is explained by the nature of the research topic, which demands in-depth knowledge of a relatively unexplored topic. In doing so, we divided our research into four stages, conducting three sets of semi-structured interviews as well as one online survey. As quantitative studies aim to test facts and generalise problems instead of exploring phenomena in-depth, the qualitative approach suits our research purpose best.

The key finding of our research is that the vast majority of Fair Trade importers perceive FX rate risk as having a strong impact on their businesses. Moreover, most Fair Trade importers do not know how to deal with currency volatility. We find indication that they cannot rely on help from banks to hedge against foreign exchange risk, since their specific derivative demand does not match the supply provided by the financial market. However, our results indicate that, in order to arrive at a viable solution to this shortage, all segments of the Fair Trade FX framework need to be taken into account. Our conclusion indicates that a possible solution can be attained by pooling a number of smaller hedging demands into larger tradable batches.

The structure of the thesis is as follows: **Chapter 2** contains the literature review and covers key articles on the characteristics of the Fair Trade niche market, the basic idea behind hedging foreign exchange risk as well as the exposure of SMEs. Subsequently, **chapter 3** discusses the research strategy and method as well as techniques used for executing research concepts, data collection and analysis. This is followed by the analysis and discussion of the findings of the study which are reported in **chapter 4**. Finally, **chapter 5** presents the conclusion and covers limitations of this study as well as recommendations for future research.

2 Literature Review

The literature review is conducted with the objective to obtain deeper insights into knowledge of the research field, thereby sharpening the research focus of this thesis (Collis and Hussey, 2003). We start by analysing the unique exposure of the Fair Trade as a niche market. Then, the feasibility of currency hedging as a risk management tool is examined. Following this, we investigate how SMEs manage their exposure to foreign exchange risk. This chapter will serve as basis for the data collection and subsequent analysis outlined in chapters 3 and 4 respectively.

2.1 Fair Trade as a Niche Market

As the estimated sales volume of Fairtrade International products worldwide surged from €830 mn in 2003 to up to €5.5 billion in 2013 (Statista, 2015), it becomes apparent that the research topic has become increasingly interesting for academics (Bezencon & Blili, 2009). What started off as a social movement of a few activists based on an ideology of encouraging community development in the global South, in order to allow for a more equal distribution between developed and undeveloped countries, grew into a well organised multi-billion dollar business (Doherty, Davies & Tranchell, 2013; Raynolds, Murray & Wilkinson, 2007; Wielechowski & Roman, 2012). Today, Fair Trade complements conventional 'free trade' by offering an alternative approach to manage trade by connecting producers, traders and consumers more directly (Fridell, 2007; Murray et al. 2003).

> *"Fair Trade is a trading partnership, based on dialogue, transparency and respect, that seeks greater equity in international trade. It contributes to sustainable development by offering better trading conditions to, and securing the rights of, disadvantaged producers and workers – especially in the South. Fair Trade organisations, back by consumers, are engaged actively in supporting producers, awareness raising and in campaigning for changes in the rules and practice of conventional international trade" (EFTA 2001; FLO 2015;NEWS!, 2001; WFTO, 2013).*

This definition of Fair Trade was commonly agreed upon by FINE, a conglomerate of the four main Fair Trade networks: the Fair Trade Labelling Organisation International (FLO), the World Fair Trade Organisation (WFTO), the Network of European Worldshops (NEWS!) and the European Fair Trade Association (EFTA). This network is a voluntary partnership among producers, seller and buyers rather than a legal agreement among countries such as the North American Free Trade Agreement (NAFTA) (Stenzel, 2012). The quotation above is the most frequently cited definition of Fair Trade in literature (Bezencon & Blili, 2009; Bowen, 2001; Fisher & Corbalán, 2015; Low & Davenport, 2005; Moore, 2004; Stenn, 2014) and emphasises three actors in the Fair Trade business: **producers** mostly small and located in the South, i.e. Africa, South-America or Asia (Boonman, Huisman, Sarrucco-Fedorovtsjev & Sarrucco, 2010), **organisations and institutions** that coordinate and promote Fair Trade and **consumers** who regulate the quantity sold by their willingness to purchase Fair Trade products (Altmann, 2010; Bezencon & Blili, 2009). Stenn (2014) argues that Fair Trade consists of a four-pillar structure and hence adds **government and policy** as another player to the game.

When looking at Fair Trade literature, it becomes apparent that the aforementioned definition of Fair Trade is widely accepted by scholars. Hence, extensive research has been conducted around the four actors identified above. To make studies more tangible and comprehensive, Fair Trade bananas and coffee – the most consumed and hence most important Fair Trade products in Europe and America – are often used as a point of departure for many studies and discussions around the aforementioned players (Hudson & Hudson, 2003; Raynolds, 2002; Renard, 2003; Tallontire, 2002). There has been ample attention in literature given to the reaction of **consumers** to Fair Trade motivated price increases, their perception towards price fairness and their loyalty (Arnot, Boxall & Cash, 2006; Campbell, Heinrich & Schoenmüller, 2015; Hainmueller, Hiscox & Sequeira, 2011; Hertel, Scruggs & Heidkamp, 2009). The experiment in Campbell et al.'s (2015) study, for instance, reveals that consumer's actual buying behaviour is in line with their stated intentions to purchase Fair Trade coffee. Additionally, the results of the research demonstrate that consumers are willing to pay up to 40cents more for a Fair Trade coffee compared to a conventional coffee. This outcome finds support from previous studies by Arnot et al. (2006), Hainmueller et al. (2011) and Hertel et al. (2009) who conclude that Fair Trade coffee is insensitive to price increases even if the price is raised by 50 cents or more. This price inelasticity for Fair Trade coffee is an interesting finding that we will come back to in our analysis and discussion.

Moreover, numerous scholars such as Dragusanu et al. (2014), Stenzel (2012) and Strong (1997) investigate the Fair Trade concept in relation to **policies and governmental** support and the development on the future of trading in general. In doing so most researchers see close links between Fair Trade and sustainability and hence argue for the vital role Fair Trade plays in addressing the challenge of achieving sustainable development (Le Velly, 2012; McMurty et al., 2012; Morgan & Moreley, 2006; Stenzel, 2012; Strong, 1997; Walker & Brammer, 2009). Opposing views are being uttered, mostly by economists, raising the question of whether Fair Trade is a truly fair and ethical concept transferable to all trade or whether it rather stands in the way of free trade, the predominant model of our hemisphere (Dragusanu, et al., 2014; Stenzel, 2012). While there is still a lot of contention around this issue, the majority of Fair Trade activists advocate harmonization of Fair Trade practices and principles with those of conventional trade (Stenzel, 2012). Nowadays, Fair Trade products are not only distributed via Worldshops whose employees are mainly retired people, housewives or volunteers who work for free but also via other retail channels such as supermarkets and other conventional stores, e.g. boutiques (Bezencon & Blili, 2009).

In line with these discussions, a range of research papers examine the role **institutions and organisations** play in the future of Fair Trade (Doherty et al., 2013; Corner & Ho, 2008; Low & Davenport, 2005, 2006; Murray & Raynolds, 2000; Raynolds et al., 2007). Identity crises arising from growing into a multi-billion-dollar business and the issue of mainstreaming Fair Trade by distributing Fair Trade products via supermarket chains are highly debated topics (Bezencon & Blili, 2009; Doherty et al., 2013; Low & Davenport, 2005, 2006; Moore, 2004; Raynolds et al., 2007). Besides the benefit of increased awareness of Fair Trade, many scholars such as Doherty et al. (2013) raise awareness to negative aspects such as dilution, reputational risks as well as cannibalisation by supermarket own label Fair Trade products. In relation to the discussion surrounding mainstreaming Fair Trade, buzzwords such as 'fairwashing' and 'green- or clean-washing' frequently emerge in writings (Corner & Ho, 2008; Low & Davenport, 2005, 2006). All refer to the practice of Fair Trade labelling by international brands such as Nestlé, Starbucks or McDonalds that only implement Fair Trade in a very limited way: Generally only five percent of the coffee they sell was sourced using Fair Trade practices (Bezencon & Blili, 2009; Corner & Ho, 2008). Due to their negotiation power, those market-driven mainstream buyers often only fulfil the minimum criteria and thereby hurt the underlying goals of the Fair Trade movement (Dragusanu et al., 2014). Hence, Fair Trade institutions such as the FLO[1] and the WFTO argue for a uniform certification process for Fair Trade products. The first Fair Trade certification system was launched in the Netherlands in 1988 by the Max Havelaar Foundation[2]. The idea behind the system served and continues to serve two main purposes. Firstly, it should aid consumers in identifying and distinguishing Fair Trade products. Secondly, it should provide a systematic approach to compliance with Fair Trade standards along the supply chain and measure oversight (Stenzel, 2012). As a result, consumers trust in the Fair Trade certification as it conveys credible information about the production process, the material used as well as the working conditions (Boonman et al., 2010; Campbell et al., 2015). Yet, besides meeting the standards required to become certified producers and farmers, the certification costs pose an entry barrier to many producers and farmers as fees are high and need to be renewed on a yearly basis (Vieira & Maia, 2009).

Various case studies such as Becchetti, Conzo and Gianfreda (2011), Lyon (2007), Stenn (2014) as well as Vakilia and Nygren (2010) explore and discuss the impact Fair Trade has on the lives of local **producers** and farmers in the South. For instance, Stenn (2014) analyses the effects of Fair Trade on the freedom of Bolivia's Indigenous Women. Overall the studies show that Fair Trade is perceived to have a positive impact on the producers' and farmers' lives by empowering people, developing skills and raising income levels. However, there is still room for improvement, e.g. in terms of allowing for more transparency, reciprocity, and public reasoning (Becchetti et al., 2011; Lyon, 2007; Stenn, 2014; Valkila & Nygren, 2010). Moreover, the question of whether Fair Trade producers and farmers are truly being empowered is widely discussed in literature (Lyon, 2007; Valkila, Haaparanta & Niemi, 2010). Although Fair Trade guarantees Minimum Prices and Price Premiums, a study by

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[1] The FLO owns the right to the Fairtrade Certification Mark which verifies that the organisation's standards have been met (FLO, 2012). To avoid confusing and to be in line with current literature, the notation Fair Trade is used to refer to general discussion about the topic. Fairtrade only refers to the Trademark certified by the FLO.

[2] In 1988, the Max Havelaar Foundation joined forces with other organisations to form a certification umbrella mandated to apply and monitor Fair Trade standards worldwide, today known as FLO (Stenzel, 2012).

Valkila et al. (2010) found that a large share of the retail prices remained with the consuming countries, i.e. the North.

The previous paragraphs give an overview of already existing literature on those four key players within Fair Trade but at the same time draw attention to aspects that have not yet been investigated. As pointed out, even though literature on Fair Trade is prolific, discussing a plethora of questions associated with Fair Trade especially on the producer and consumer side, to our best understanding the unique financial position and exposure to foreign exchange rate risk of **importers** have not yet been investigated. In order to determine why the situation of micro, small and medium sized Fair Trade buyers is different from other importing SMEs, it is necessary to understand their business model. The Fair Trade principles seek to empower consumers in developed countries to contribute to the fight against poverty in developing countries by purchasing Fair Trade products. In order for Fair Trade to work, all actors along the supply chain need to comply and engage with the Fair Trade principles, that are not defined as a law but are rather a set of rules and standards predetermined by the Fairtrade Labelling Organisation. The organisation sets, reviews and updates its standards on a regular basis and discloses them on their webpage. Setting new standards is a complex process in accordance with the 'ISEAL Code of Good Practice on Standard Setting' as it involves the consultation of a wide range of stakeholders (FLO, 2015). According to the FLO (2015) the main principles in order to achieve the objectives defined by the Fair Trade movement are the following:

- It must be ensured that producers receive prices that cover their average costs of sustainable production.
- An additional Fairtrade Premium needs to be provided to ensure investment in projects that enhance social, economic and environmental development.
- Producers in need of pre-financing should receive adequate possibilities.
- Long-term trading partnerships are favoured and enable greater producer control over the trading process.
- Clear core and development criteria need to be set to ensure that the conditions of production and trade of all Fair Trade certified products are socially, economically fair and environmentally responsible.

These principles are requirements that are unique to Fair Trade, such as mandatory social organisation, the Fair Trade Minimum Price and Premium as well as pre-financing. They are designed to improve the situation of farmers and producers in the South and apply to both producers and traders (Altman, 2010; FLO, 2012; 2015). The standards set by the FLO give a full list for all certified products on Minimum Price and Premium. For many producers and farmers the most important and fundamental standard of all is the Fair Trade Minimum Price (Dragusanu et al., 2014; Sukhamay, 2013), since it is designed to cover the cost of sustainable production regardless of whether the world's market prices have decreased or not. When market prices lie above the Fairtrade Minimum Price, producers should receive the current market price or the price negotiated at closing (FLO, 2015; Sukhamay, 2013). As demonstrated, an array of research has been conducted to testify the effects of these principles on the producers and consumers, however, the implications on micro, small and medium sized Fair Trade importers have not been assessed. And yet it is exactly the Fair Trade principles and requirements that make the business model of importers that make their exposure so unique. Paying a Minimum Price, a Price Premium, as well as pre-financing up to 100 percent of the production months before delivery puts micro and small importers in a very difficult position especially in volatile markets. Fair Trade importers must pay the agreed prices no matter whether the market fluctuations are favourable or unfavourable. Since unfavourable market fluctuations are not passed through the supply chain, Fair Trade importers are committed to foreign exchange rate fluctuations.

2.2 Currency Hedging as a Risk Management Tool

2.2.1 Reasons for Hedging

In the following section, the current research on managing exposure to foreign exchange rate is investigated. We will examine what is meant by hedging and which different hedging instruments exist, as well as at the existing discussion about whether hedging is value creating or not and which strategies managers can choose.

Over the last decades, many organisations spread their businesses beyond geographical boundaries, increasing their purchase markets and sales markets and thereby benefiting from competitive advantage and economies of scale (Afza & Alam, 2011). This cross-border activity leads to a high exposure to contracts and deals in foreign currencies. As stated in the introduction, foreign exchange rates are very unpredictable, so the depreciation of currency often appears out of nowhere, and hits companies unprepared (Rossi, 2013). Due to the strong exposure to foreign currencies and the unpredictability, the need for managing foreign exchange risk to reduce variability in cash flows from foreign operations gains importance (Afza & Alam, 2011; Peterson & Schweser, 1980).

By implementing hedging strategies, companies can insure themselves against the downside potential of a change in the exchange rate. This can be achieved using different financial hedging instruments such as forward contracts, futures contracts, options, swaps or caps (Investopedia, 2015). In addition, a wide range of non-financial hedging instruments exist. A company may implement natural hedges through an alignment of cost and revenue currency, a relocation of headquarters, an expansion of the portfolio, or borrowing in the foreign currency, amongst many others (Copeland & Joshi, 1996). Those financial and non-financial instruments, with their pros and cons, are not discussed in detail as this will go beyond the scope of this research.

In order to understand the basic mechanics of a financial hedge, a transaction using a future contract is explained. The view of an importing company paying in foreign currency is taken as the companies of interest in this study are micro, small and medium sized importers. If an importing company seeks to reduce its exposure to foreign exchange risk, it can take a long position in a currency future contract. This means, the company buys a currency future contract. The company may do so, when it anticipates a need of foreign currency due to its purchase activities in foreign currency and expects an increase in price of that currency or simply seeks a fixed rate for planning purposes. This can be illustrated using an example from

Copeland and Joshi's (1996) study. A Japanese firm buys its goods in the United States in USD and sells them in Japan for Yen. In the case of a weakening yen, the company needs to pay the same amount of USD for its products but will need more yen to buy the necessary amount of USD. Unless sales prices are raised, the firm still receives the same amount of yen for its product in the domestic market; hence the profits of the firm are reduced. The Japanese firm could hedge to protect itself against this exposure.

2.2.2 Advocates and Opponents of Hedging FX Exposure

As the previous example demonstrates, the primary purpose of hedging FX exposure is to reduce cash flow volatility caused by FX movements leading to smoothed earnings (Copeland & Joshi, 1996). Academics discuss controversially, whether hedging as a risk management tool to reduce variability in cash flow actually creates value for a company, as by smoothing earnings, one not only takes away the operational losses caused by FX movements, but also the potential gains (Copeland & Joshi, 1996).

A number of researchers such as Allayannis and Weston (2001), Froot, Scharfstein and Stein (1993), Stulz (1996) as well as Pérez-González and Yun (2013) emphasize the advantages of hedging transaction exposure such as less volatile earnings and reduced information asymmetry, hence increased debt potential. Froot et al. (1993) state that derivatives may be beneficial "when the external financing cost exceeds the opportunity cost of internal financing and [...] when the correlation between investment expenditures and a firm's cash flows is negative" (Afza & Alam, 2011, p.411).

Contrasting this viewpoint, Modigliani and Miller argued back in 1958, that using derivatives to reduce risk is useless for corporations under perfect capital market conditions. Copeland and Joshi (1996, p.66) agree, claiming that "many hedging programs destroy value instead of protecting it" because they assume a static world where only FX rates change. However, this does not hold up in real life as many other variables such as the supply of raw materials, demand for products, cost and productivity of labour and capital change at the same time. Finally, Copeland and Joshi (1996) conclude that derivatives are not necessarily the right answer to FX exposure. This is supported by Hagelin and Pramborg (2004) who also claim that when exchange rate changes, many other factors change simultaneously and therefore hedging activities will destroy rather than create value for shareholders. This is in line with Coppé, Graham and Koller's (1996) perspective who argue that derivatives alone do not reduce the foreign exchange risk of large multinational corporations. The idea behind their argument is the claim that CFOs – no matter how talented – are unable to comprehend or identify all their business risks, let alone the relationship between those risks. Therefore, Coppé et al. (1996) suggest approaching the issue at hand by breaking down risk into three categories: structural risk, transactional risk and portfolio risk; a strategy that is believed to be superior to traditional derivative focused approaches. Structural risk is understood as a mismatch between cash inflows and outflows. If severely out of balance, such a mismatch can cause financial distress. The use of derivatives is ineffective because the market for long-term derivatives is very illiquid and therefore expensive. Possible solutions could be to borrow in the currency in which company is long or to shift production facilities. Transaction risk is believed to be generally rather small and can be mitigated using derivatives to hedge transactions or net position, however this is costly. Portfolio risk can be reduced by borrowing in the currency of foreign operations to reduce cash flow volatility. Each risk category has to be assessed, which helps to understand the firm´s risks and “suggest actions to reduce or moderate them” (Coppé et al., 1996, p.89).

2.2.3 Dealing with FX Rate Risk Exposure

According to Pennings and Garcia (2004), the way a company handles its foreign exchange exposure is determined by various factors such as risk attitude, risk perception, risk exposure, educational level of manager, and company size among others.

Firstly, the risk attitude of a manager is crucial to the choice of the hedging strategy of a company. The more risk averse a manager or a firm, the more likely they are to hedge (Pennings & Garcia, 2004). If and how a company will hedge its exchange rate exposure is usually a top management decision and depends on the manager’s view of the market as well as their risk attitude (Oxelheim & Wihlborg, 2008). Oxelheim and Wihlborg (2008) define four possible strategies taking into account if the manger is risk-neutral or risk-averse, and if the manager believes that profits can be made in the international financial currency market, or if he/she believes in the theory of international fisher parity. If the manager is risk-neutral, he/she chooses the laissez-faire approach when he/she believes that no profit can be made in the financial markets (IFP) and the aggressive strategy when it is believed that profits can be made. The risk-averse manager under IFP will be willing to incur a cost to minimize its exchange rate exposure, whereas he/she will be selectively hedge and trade off risk versus return when he/she believes that profits can be made (Oxelheim & Wihlborg, 2008).

Secondly, the risk perception or awareness of the manager or a firm is an important variable. Only when managers are aware that there is a risk or feel that the situation or uncertainty could be risky, they might willingly engage or willingly not engage in the use of derivatives or other hedging strategies.

As a third factor, the company´s risk exposure has to be taken into account. According to Hagelin and Pramborg (2004) the firm’s foreign exchange exposure is measured as the difference between revenues and foreign currency costs. The more a firm is exposed to risk, the more likely it is to use derivatives. Scholars distinguish between economic exposure and translation exposure. Shapiro (1994) separates economic exposure into two types: 1) Short to medium-term transaction exposure occurs if the company has already entered into a financial obligation and the future cash out- or inflow potentially changes in value due to expected or unexpected changes in exchange rates (Hagelin & Pramborg, 2004). A hedge for transaction exposure can eliminate this cash flow volatility. 2) Operational exposure on the other hand is non-contractual future cash flows, much less plannable and can also occur even if the company is not directly engaged in international contracts. A more medium to long-term translation exposure is rather an accounting concern, e.g. occurring when foreign subsidies statements are translated into the home currency (Hagelin & Pramborg, 2004). Some scholars recommend not to hedge translation exposure since gains or losses have no or little impact on firm value (Butler, 1999 cited in Hagelin & Pramborg, 2004). Due to the nature of the business model, Fair Trade businesses are mostly facing transaction exposure.

Finally, Pennings and Garcia (2004) also stress the importance of the level of education of the managers: the higher the educational background, the more likely it is that the manager uses derivatives since instruments are complex, and there are high costs involved in gathering information and using them efficiently. Moreover, size is also positively correlated to the usage of derivatives (Pennings & Garcia, 2004). Small firms often rely on the opinion of experts like consultants or banks when taking their decisions regarding the usage of financial instruments (Pennings & Garcia, 2004).

2.3 FX Risk Exposure and Risk Management of SMEs

In the last section, we looked at hedging in general, advantages and disadvantages and the factors influencing whether or not hedging is applied. In this section, a focus will be put on the distinguishing characteristics of SMEs, which influence the current risk management strategies regarding foreign exchange exposure. Table 1 illustrates the SME´s classification by the European commission.

Table 1 EU Size Categories of SMEs

Company category	**Employees and**	**Turnover or**	**Balance sheet total**
Medium-sized	< 250	≤ € 250 mn	≤ € 43 mn
Small	< 50	≤ € 50 mn	≤ € 10 mn
Micro	< 10	≤ € 10 mn	≤ € 2 mn

Source: European Commission (2014)

According to Pennings and Garcia (2004), a vast amount of research about the main drivers and motivation for the use of derivatives within large and publicly traded companies has been conducted by “Froot, Scharfstein and Stein (1993), Nance, Smith and Smithson (1993), Mian (1996), Tufano (1996), Geczy, Minton and Schrand (1997), Lee and Hoyt (1997), Koski and Pontiff (1999)” (p.952) and many others. Pennings and Garcia (2004) extended the research to small and medium sized enterprises, focusing on the special characteristics of those firms and their managers, as those are different to the needs of large companies. The different characteristics of companies and managers lead to a differing usage behaviour of derivatives. Based on these findings, the financial sector needs to focus on the different characteristics and motivations of SMEs and by that will be able to develop more customized financial products (Pennings & Garcia, 2004). As the financial sector becomes more and more competitive, this becomes increasingly important (Pennings & Garcia, 2004).

One important characteristic of a company is its organizational structure. A significant amount of companies does not have separate departments (Pennings & Garcia, 2008). One single manager is often responsible for various areas such as R&D, sales and accounting. Additionally, ownership in such companies is often concentrated, meaning that managers and owners are the same person (Pennings & Garcia, 2008). According to Smith and Stulz (1985), managers who own a significant part of the firm are more likely to be risk averse. They want to reduce risk for two reasons: Firstly, because they do not hold a diversified portfolio which would allow them to mitigate the risk and secondly, because their personal wealth is closely linked to the return of the firm (Smith & Stulz, 1985). Connecting this to the study by Oxelheim and Wihlborg (2008) outlined in the previous section, it can be expected that SMEs will tend to take on a minimizing exposure strategy, or a selective hedging strategy, depending on their manager´s view of the market. According to McCharty (1999), more than 50 percent of Australian SMEs believe FX exposure management to be important or very important to their performance.

Most SMEs know about financial instruments such as forwards and swaps, yet about 40 percent do not know about options, futures and others (Ehrlich, Woodward & Tiong 2012). According to the same study, forward contracts are the most commonly used hedging instrument for SMEs. A major characteristic of a forward contract is that it is traded privately over the counter (OTC), thereby being a direct agreement between the buyer and the seller. SWAPS is the second most used hedging instrument by SMEs. These findings are supported by McCharty´s (1999) research, which states that forwards and foreign currency accounts are well understood, whereas there is only little to no understanding of future, options and other financial instruments. SMEs are more likely to hedge their expense exposure, than hedge their revenue exposure (Ehrlich, Woodward & Tiong, 2012). McCharthy (1999) found that importers are more likely to hedge than exporters.

Due to their size and cross-border activities, larger firms have more operational hedges in place (Hagelin & Pramborg, 2004). This further decreases their inherent exposure, defined as the difference between revenues and costs denominated in foreign currency. A survey conducted by Ehrlich et al. (2012) finds that about 36 percent of the small companies hedge their foreign exchange rate exposure. This is supported by Berkman et al. (1997, cited in Ehrlich, Woodward & Tiong, 2012) which also found that 36 percent of the small companies hedge their exposure compared to 54 percent of the large companies. The study by McCarthy (1999) finds similar numbers, stating that about 39 percent of Australian SMEs have hedged before. The 39 percent that already have had experience hedging, the majority only hedges sometimes, whereas 29 percent hedge most of the time and only 9 percent hedge every single exposure.

According to the study by Ehrlich et al. (2012), the main reason for not engaging in hedging activities is that the companies consider their amounts of FX exposure as too small and they believe that no suitable financial instruments exist. There are future contracts with a lower threshold of €12,500 and €62,500, called e-micro and e-mini respectively (CME Group, 2015a; 2015b). Those futures are Euro-Dollar futures and have a maintenance costs of $315 and $1,555 respectively (CME Group, 2015a; 2015b). In the analysis in chapter four it will be necessary to analyse if those products would be suitable to Fair Trade importers and if order volumes exceed the mini future contract of €12,500. The reasons for Australian SMEs not to hedge are that they do not believe to gain any value or they do not want to gamble on the FX market (McCarthy, 1999). This means that hedging often is misinterpreted as a speculative instrument instead of as a conservative risk management tool. This finding complements the results of the research done by Ehrlich et al. (2012), which state that another important reason for not engaging in hedging is that the necessary knowledge about financial instruments is not available. They further argue that more than half of the SMEs are depended or strongly depended on bank advice, when it comes to financial decision making.

The Chinese subsidiary of Alibaba, Shenzhen OneTouch Enterprise Services Co. Ltd. (referred to as OneTouch from here onwards) has reacted to the increasing need for small companies to hedge against foreign exchange exposure (Song, 2013). Since traditional forward contracts usually have a threshold of $1 million, the foreign exchange service was not accessible for smaller companies in the Chinese market. According to OneTouch, each trade order for an average Chinese SME is around $30,000 (Song, 2013). The appreciation of the Chinese Yuan (CNY) had a large negative impact on the trading company's profits, discouraged the companies from taking long-term orders or prevented them from doing cross currency business at all (Song, 2013). The inability to hedge against foreign exchange risk was defined as the main determinant for this situation. OneTouch started to offer a pool in which smaller companies could invest and accumulated these hedging needs to make it more interesting to banks. Yet, the administration and paperwork posed a high barrier for SMEs resulting in only little participation. Learning from this, OneTouch now offers a platform where companies can engage directly and without bureaucracy into a hedging contract. OneTouch then engages in forward contracts with the banks, a service offered free of charge. The relatively small FX contracts are bundled together before placing the bulk with the bank, however, the SMEs can still get the contract duration they want ranging from one to 12 months (Ng, 2013).

Similar solutions can be observed in the micro finance sector. There are numerous public and financial institutions which offer credits to the exporters in developing and emerging countries. Derivatives solutions exist for other businesses in a similar sector. 'MFX Solutions LLC' for instance, offers derivatives to entrepreneurs in developing countries (Heath, 2014). The company's target group are so-called micro-entrepreneurs operating very small businesses. These entrepreneurs struggle because they receive micro development loans in USD, buy materials needed for production in their local currency and then need to pay back the loan in USD. This currency mismatch leads to an elevated foreign exchange rate risk when the local currency depreciates. MFX Solutions LLC intermediates between borrower and lender and redistributes the currency risk. This way the borrower can repay the loan in local currency and the lender receives down payments in USD. MFX Solutions deals with the risks by investing the money in large pools of international risk capital (Heath, 2014).

3 Methodology

In the previous chapter, existing literature on the unique exposure of Fair Trade importers, hedging as way of managing risk as well as the exposure to foreign exchange rate risk faced by SMEs was reviewed. In this chapter the research method and design for collecting and analysing the data will be outlined.

3.1 Research Strategy and Method

In aiming to explore the phenomenon discussed in this thesis in depth, a combination of secondary as well as qualitative primary research has been chosen to answer the research questions. Ghauri and Grønhaug (2005) reason that for exploratory research "qualitative methods are most useful, as they are used when the research problem focuses on uncovering a person's experience or behaviour, or where we want to uncover and understand a phenomenon about which little is known" (Marschan-Piekkari & Welch, 2004 in Ghauri & Grønhaug, 2005, p.111) which is the case in this thesis. The lack of research about the exposure of Fair Trade buyers to foreign exchange rate risk gives this research an exploratory orientation, demanding the collection of qualitative data. Qualitative methods are characterized by "their ability (…) to understand people's meaning" (Easterby-Smith, Thorpe & Jackson, 2012, pp.27). Bryman & Bell (2007) argue that this method offers the advantage to "see through the eyes of the people being studied" (p.416) which allowed us to gain in-depth knowledge of the research field and facilitated the understanding of the exposure Fair Trade importers are faced which was essential for this study. Hence, due to the topic's actuality and the lack of research the "exploratory and flexible" (Ghauri & Grønhaug, 2005, p.202) characteristics of qualitative methods suited the research purpose best. Since the aim of this thesis is not to generalise but to explore the phenomenon stated above and since quantitative research mostly aims at generalizing certain problems or testing facts, this research method has been ruled out.

3.2 Data Collection

Following the previous arguments, we decided to apply a qualitative research design which consists of four stages and two different data collection methods. On the one hand, semi-structured interviews with Fair Trade Importers (derivative demand perspective) as well as experts from both banks and financial institutions (derivative supply perspective) were constructed. On the other hand an online survey was sent out to all 66 members of the Weltladen-Dachverband (WLDV).

The semi-structured interviews as an instrument of qualitative data gathering allow us to identify "what is happening, to seek new insights, to ask questions and to assess phenomena in a new light" (Robson, 2002, p.59). Two decisive factors can be highlighted which led to the selection of the semi-structured interview approach as our primary data collection tool. Firstly, this interview type is especially applicable and beneficial in our situation since an overall theoretical understanding of the research question has already been obtained via extensive use of secondary data: journals, articles and papers (see chapter 2) and hence we as researcher are "beginning the investigation with a fairly clear focus" (Bryman & Bell, 2007, p.479). Secondly, semi-structured interviews follow a list of questions that we want to cover that is flexible in "the order of the questions depending on the flow of the conversation" (Saunders et al., 2009, p.320) and open to additional questions that may arise during the conversation. As a consequence, better comparisons between the different statements of the interviewees are facilitated as the same topics are addressed, although in a different order. Denzin (1989) argues that validity and reliability are not depending on the repeated use of the exact same wording but on conveying equivalence of meaning. In addition, semi-structured interviews offer the possibility that new aspects and topics, which the researcher did not have in mind, arise naturally during the interview (Bryman & Bell, 2007). The nature of semi-structured interviews allows the collection of both structured information and information about the interviewee's attitudes, beliefs and opinions towards the research topic e.g. how Fair Trade importers perceive the impact FX rate risk has on their businesses (King, 2004; Saunders et al., 2009). Hence, conducting semi-structured interviews provided us with "specific information which can be compared and contrasted with information gained" (Dawson, 2002, p. 29) and offered the desired rich understanding concerning the situation of Fair Trade importers relevant for the research topic of this thesis (Marschan-Piekkari & Welch, 2004; Morris & Wood, 1991).

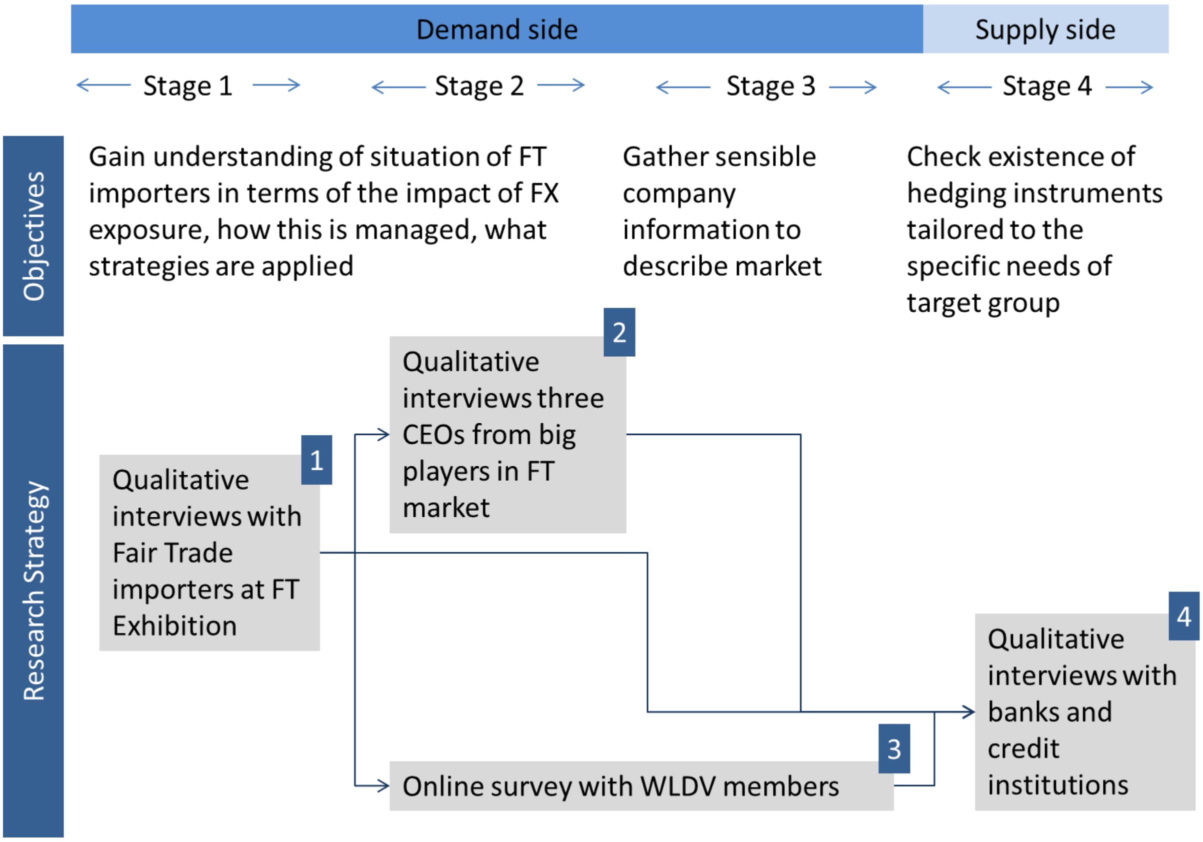
All interviewees were selected according to purposive sampling which implies a strategic selection based on the participant's ability to contribute to the understanding of the research question due to their special knowledge in their respective field (Bryman & Bell, 2007). It has been considered critical that the questions asked during the interview were easily comprehensible for the participants. Therefore the interview guide was tested in advance of conducting the interviews (Ghauri & Grønhaug, 2005; King, 2004) at the exhibition and via telephone with two Fair Trade companies which are not part of the samples. The interview guideline was sent to the respondents before conducting the interview in stage 2 is attached in Appendix 1. These questions only represent a guideline for the interviews as follow-up, probing and specifying questions were asked during the interviews to ensure that the information was understood correctly.

To gather sensitive company information such as purchase volumes and cost structure to describe the Fair Trade importer market an online survey (see Appendix 6) was chosen. Due to the sensitivity of the information a method allowing for anonymous data collection was necessary. In addition, in order to describe the market a large amount of data to ensure significance was needed. In the following passage, an overview of the participants and the consecutive stages involved in answering the research questions is displayed.

3.3 Research Stages

In the following, the research design is illustrated (see figure 1). Then each stage is discussed and outlined in detail. The section concludes with a summary of the four stages and their main purposes (see table 2).

Figure 1 Illustration of Research Design



Source: Own representation

Target Group

The target group analysed in this study are companies selling products that fulfil the conventions by the German World Shops ('Konvention der Weltläden') and the conventions by the Federal Association of Fair Import and Sale ('Bundesverband für fairen Import und Verkauf'), which are based on the principles of the WFTO. Additionally, companies which import products with the official Fairtrade seal have been taken into account. The observed population purchases its products in a market that uses a different currency than the Euro and mainly sells in Euro. In addition, the companies should have their office registered in Germany.

Participants

- Stage 1: Fair Trade importers at the 'Fair Handeln' Exhibition in Stuttgart, Germany
- Stage 2: CEOs of three medium sized Fair Trade firms: dwp, Contigo and El Puente
- Stage 3: Members of the WLDV, the German Network of Worldshops
- Stage 4: Banks and credit organisations

3.3.1 Stage 1

In order to examine whether Fair Trade buyers generally perceive the depreciation of the Euro as having a significant impact on their businesses and thereby express a need for some kind of solution to deal with this exposure we conducted 19 **semi-structured interviews** with Fair Trade importers during two consecutive days at the 'Fair Handeln' exhibition in Stuttgart, Germany in the beginning of April 2015. The aim of the interview execution was to investigate a number of assumptions in order to get in-depth information about the current situation of Fair Trade importers in the light of the Euro depreciation:

1. Fair Trade importers experience financial difficulties that originate from their unique exposure to foreign exchange risk.
2. Resulting from this exposure, there is a need in the market to manage foreign exchange risk.
3. Fair Trade importers do not know about hedging or other risk management strategies.

Since we wanted to interview as many firms as possible to get an even better understanding of the exposure they face, the Fair Trade Exhibition proved to be an excellent event for gathering a large amount of qualitative data from a wide variety of Fair Trade importers. Typically interviews lasted between 25-45 minutes. Interviewees were selected at random. The interviews were conducted in person and on a one-on-one basis. At the beginning of each interview the researchers presented themselves and asked for the position of the interview partner. We considered this as an important step since our target interview partner was the decision maker and/or managing director of each company as they are concerned with hedging decisions according to Oxelheim and Wihlborg (2008). After presenting ourselves we explained the purpose of the interviews in the overall setting (see Appendix 1). By that, we wanted to make sure not to bias the interview partner with any judgemental comments. This neutral perspective was held up throughout the whole conversation. The interviewees also received a clear instruction in terms of the estimated length of the interview. Due to the sound level at the exhibition, the interviews could not be recorded. Therefore, the researchers prepared to allow enough space to take notes during the interview and also to make additional comments on questions and topics that arose during the interviews. At the end of the day, we transferred our notes into a predefined Excel spreadsheet (see Appendix 2).

3.3.2 Stage 2

After analysing the data collected in step one, we realised that due to the nature of the exhibition we mainly talked to micro and small Fair Trade importers. To make sure that the larger sized Fair Trade importers were not left out and to seize the opportunity of gaining more information in the process, another set of semi-structured interviews was conducted. Hence, the second step consisted of **semi-structured interviews** with managing directors from three big players among the SME Fair Trade importers, namely Contigo Fairtrade GmbH, dwp eG and el Puente GmbH. We also contacted the CEOs of Gepa The Fair Trade Company mbH and Globo Fair Trade Partner GmbH and asked for interviews but eventually were unable to conduct interviews as appointments got delayed and eventually got pushed beyond our internally set deadline. The interviews were conducted via skype or telephone. The aim of the second interview set was to investigate the same assumptions outlined in stage one. Thereby, the information gained during these conversations completed the first stage our data collection resulting in a good understanding of micro and small but also medium sized Fair Trade importers. In addition, benefiting from the CEOs' rich experience and expertise in the Fair Trade industry, further topics such as past and current strategies as well as possible designs for hedging instruments and the question of who would need to offer these approaches to solution were discussed in-dept. Prior to conducting the interviews we sent an interview guideline to all three participants (see Appendix 1). However, these questions merely served as a guide for the interviews as follow-up, probing and specifying questions were asked during the interviews to make sure that the interviewees' statements were understood correctly. Besides recording the interviews, we were taking notes during the interview. This approach facilitated the preparation of a summary of the key statements of each interviewee rewritten in a structured manner directly after the interview (see Appendix 5). We send these summaries to each participant in order to grant our interviewees the possibility to verify or modify the interview transcript before giving their final approval.

3.3.3 Stage 3

Subsequent to the previous two stages, an **online survey** using the free online survey tool 'Survio' was sent out to all 66 members of the WLDV. The purpose of the survey was to gather data about, for instance, the companies' revenues and yearly import volumes per country in order to describe the target market closer (see Appendix 6). The survey was designed using a free online tool allowing for anonymous completion by the respondents. We believe that securing anonymity was a critical feature, as many interviewees at the exhibition expressed concerns about revealing sensitive data to 'more or less complete strangers'. We therefore hoped that by securing anonymity, participants would feel more comfortable about sharing this private information. Moreover, we decided to ask the German Fair Trade association (WLDV) for help. Sending the link to the online survey via their mailing list not only backed the importance of our survey but also increased its credibility. Applying descriptive statistical measurements such as testing proportions as well as calculating medians and averages allowed us to describe the Fair Trade market.

3.3.4 Stage 4

After having confirmed that demand exists in stages one and two and specifying this demand further in the consecutive third stage, an investigation into the financial market as a possible supplier of approaches to solving this problem was conducted. Therefore, in the final stage several **semi-structured interviews** with regional German banks, investment and online banks as well as an internationally operating micro-financing organisation were conducted (see Appendix 8). The objective of this last step was to learn whether financial hedging instrument tailored to the specific needs for micro as well as small and medium sized Fair Trade importers are provided in the market. Our point of departure was talking to regional banks since we discovered during the first two stages that the majority of the interviewees had bank accounts with regional banks. Hence it seemed reasonable to start there. In addition, we spoke to investment and online banks as they are known to provide a wider range of products and are the banking partners of the larger Fair Trade importers. Since both attempts concluded that at that point in time, no financial hedging instrument accustomed to the particular needs of Fair Trade SMEs was supplied by the traditional financial market we decided to approach a micro-finance institution.

Table 2 Overview Research Steps

Stages	Participants	Tool	Respondents	Purpose
Stage 1	Micro and small Fair Trade importers at the Fair Trade Exhibition in Stuttgart, Germany	Semi-structured interview	19 participants	Gain understanding of the severity of FX exposure; Identify whether there is a need to manage that exposure; Learn about past and current strategies applied by these firms
Stage 2	Managing directors of medium sized Fair Trade importing firms	Semi-structured interview	3 participants	Complement stage one with CEO interviews of medium sized firms
Stage 3	Members of the WLDV	Online survey	13 out of 66	Gather sensible company information about e.g. yearly import volumes to describe the market size we are looking at in this study
Stage 4	Regional and international banks, microcredit organisation	Semi-structured interview	5 participants	Identify existence of hedging instruments tailored to the specific needs of micro, mall and medium sized FT importers

Source: Own representation

The main focus of these cooperative societies is to offer loans or investment capital to small and medium-sized enterprises in developing countries. Hence, an interview with a member of the executive team of Oikocredit[3], one of the world's largest private financiers in the microfinance sector was conducted.

3.4 Data Analysis

The analysis of the three interview stages follows the thematic content analysis approach (TCA). Therefore, interviews were transcribed whenever possible and permitted and in the case where recording was not possible (Stage 1 and parts of stage 4), the written notes, which were made during the interview, were rewritten in a structured manner directly after the interview. These summaries were then sent to the respondents in order to grant them the possibility to modify their interview transcript (see Appendix 5). The analysis of the interviews follows an approach outlined by Meuser and Nagel (1991) where a thematic arrangement of the data is followed by a thematic comparison.

The first step of the TCA requires establishing categories that are applied to the data. Argumentative-connected sentences were defined as the unit of analyses. A two-step approach was used to identify the categories. First, a priori themes which are based on the "investigator's prior theoretical understanding of the phenomenon under study" (Ryan & Bernard, 2003, p.88) were established. Consequently, the thematic belonging of a passage to a question and the corresponding argumentation was required for each analysed data extract. In our coding example illustrated below, the perception of FX impact and the corresponding arguments represent the level-one categories and level-two categories, respectively. Second, the theme identification technique of similarities and differences (Ryan & Bernard, 2003) was applied. This implied that we "begin with a line-by-line analysis, asking, what is this sentence about? And how is it similar to or different from the preceding or following statements?" (Ryan & Bernard, 2003, p.91). Afterwards, we compared the different kinds of statements. At the same time, we paid attention to the "degree of strength in themes" (Ryan & Bernard, 2003, p.91) in order to identify subthemes. Furthermore, linguistic connectors indicating causal relations were carefully considered (Rossi, Freeman & Lipsey, 2004).

The second step in the TCA comprises the actual coding process. Thereby, we manually applied a cutting and sorting process since according to Ryan and Bernard (2003) this is a suitable technique for the analysis of textual, verbatim, and rich narrative data. After having highlighted important text passages in the summary transcripts to identify "quotes or expressions that seem somehow important" (Ryan & Bernard, 2003, p.94), we cut and sorted

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[3] Oikocredit is a worldwide cooperative and social investor, providing funding to the microfinance sector, Fair Trade organizations, cooperatives and small to medium enterprises. The organisation is guided by the principle of empowering people and creating a just society in which resources are shared sustainably (Oikocredit International, 2015).

these passages into relevant "piles of things that go together" (Ryan & Bernard, 2003, p.94). In doing so, we individually "went through the transcripts and cut all the quotes that pertained to each of the major themes" (Ryan & Bernard, 2003, p.95). Whenever we disagreed, the categorization was discussed until consensus was reached which required a constant re-reading of the summary notes. This separate coding proved time consuming but we considered it to be important in the content analysis because it increases objectivity. In order to facilitate understanding of the coding process the following example from the second stage illustrates how we applied the cutting and sorting technique for interviews at all stages.

Coding Example

Example 1: Ralph Wüstefeld, Contigo

Exchange rate risk has a huge influence on our company. Most of the invoices are paid in local currency or USD and prices are fixed (49 companies). Only five are being paid in Euro which has an impact on the producers and famers as they receive up to 30 percent less money due to the depreciation of the Euro. Usually a minimum of 50 percent is pre-financed when the order is place, sometimes even up to 100 percent. In general, there is a time span of six to eight months between placing an order and receiving the delivery, sometimes additional delay for transportation issues.

Example 2: Martin Moritz, El Puente

Generally, Mr. Moritz attests that the current depreciation has had a very large impact on his business. He makes clear, that all businesses basically face the same problem, regardless of whether Fair Trade or not. He points out, that the impact strongly depends on the type of product imported. There usually are higher margins on non-food [...] Price Premium and rather accept price increases. However, there will be a limit of what they will accept. Therefore, Mr. Moritz expects that price sensitivity of the consumers is more important than the prices set by the competitors.

Example 3: Thomas Hoyer, dwp eG

Mr. Hoyer is of the opinion that the currency volatility has an impact on the business [...] and has a different view on that, as products often are order long before they are delivered and hence sold, there is a need for some kind of insurance. Another reason is given by the Fair Trade principles which according to them, at least 50 percent of the products should be pre-financed. Especially when it comes to the import of commodities such as coffee and sugar, the need for insurance becomes more obvious. The competition in the market is much higher, as those products often are delivered to other manufactures which process the Fair Trade commodities in their production.

Coding categorisation

Level 1: Perception of FX impact

- Perception 1: Huge influence

- Perception 2: Very large impact
- Perception 3: Impact

Level 2: Argumentation

- Argument 1: Pre-financing 50 percent of production or more
- Argument 2: Time span between placing and receiving the orders
- Argument 3: Type of product importer, food vs. non-food
- Argument 4: Price sensitivity
- Argument 5: Prices are fixed

Analysis

All three experts experience that the FX rate risk has a (large) impact on their business. The extent of this influence however differs among the respondents. Nevertheless, all three sources mention different reasons to explain this impact. While the second and third interviewees differentiate between food and non-food products in terms of FX impact, the first interviewee does not pick up on this difference. The issue of the time lag between placing an order and receiving the order as well as the problem of pre-financing is discussed by the first and third interviewee, but not by the second. Price sensitivity and fixed prices are mentioned by the second and first interviewee respectively.

3.5 Research Limitations

The selected research method has some limitations. According to Saunders et al. (2009) it is difficult to replicate qualitative research since the specific context and time determines the research's findings. This is exactly the case in our study since the topicality resulting in the strong exposure is only temporary. As a result, answers are likely to differ once the Euro regains strength. Consequently, researchers conducting similar studies at different times and contextual settings might find other results. Therefore, the process of interpreting data is critical in qualitative research (Easterby-Smith et al., 2012). However, by clearly stating the research strategy, its underlying assumptions and the analysis of data (see Section 3.4) our approach is open to scrutiny for other researchers (Saunders et al., 2009).

The purposive sampling which has been applied in stage four includes some bias because the participants were not selected randomly (Bryman & Bell, 2007). However, the purpose of this study requires to interview individuals who understand this particular problem in order to gain meaningful opinions and insights about the issue at hand. The online survey which was sent to all 66 members of the WLDV via the emailing list of the WLDV in the third stage could also include some bias. Being supported by the WLDV might have increased the number of responses since it established trust. However, only 13 out of 66 companies completed the survey. Possible reasons are analysed in section 3.6.2.

3.6 Reliability, Validity and Generalisability

In research, the validity and reliability of the research findings are of immense importance to their credibility. Easterby-Smith et al. (2012) fortify this viewpoint by pointing out that ”one of the key justifications for doing ‘research’ is that it yields results that are more accurate and believable than common everyday observations” (p.70). In particular quantitatively focused researchers often argue that qualitative research and analysis is ’soft’, ’subjective’ or even ’unreliable’ (Lee and Lings, 2008). In their book ‘Research Methods for Business Students’, Saunders et al. (2009) have identified two main issues in qualitative research that require careful attention in order to ”reduce the possibility of getting the answer wrong” (p.156). In the following, both aspects are dealt with in more detail.

3.6.1 Reliability

Reliability is concerned with the extent to which the data collection techniques yield consistent findings (Easterby-Smith et al., 2008). Robson (2002) identifies four threats to reliability, the first threat being *subject or participant error*. It is argued that the time dimension of the interview or survey has an impact on the results received. Employees are said to have a different degree of enthusiasm at different times of the week, i.e. Monday morning or Friday afternoon. As a result, experts advise researchers to “choose a more ‘neutral’ time” (Saunders et al., 2009, p.156). In our case, the interviews were not conducted during normal office hours but during an extraordinary event, the Fair Trade Exhibition. Therefore, some participants focused more on achieving sales and were therefore less interested in talking to us than they might be in a different setting. On the other hand, due to the negative topicality of the depreciation, they might were more interested in talking to us than in times of a strong Euro. For the telephone interviews we had to comply with the busy schedules of our interview companions.

Subject or participant bias is the second threat brought forward by Robson (2002). Here he argues that interviewees may be biased towards saying what they think their bosses would want them to say. This problem has been identified especially in authoritarian management style organisations. However, in our case this bias can be disposed as the interviewees were mainly the owners of the company or at least in managing positions. Additionally, in order to ensure that they felt free to state their opinion and speak freely of their concerns, anonymity when analysing the data was promised.

Third, *observer errors* could have occurred. Since the interviews were conducted by two different people, the potential danger of having two different ways of asking questions receiving answers is a real one. Different comments, tone or non-verbal behaviour could have influenced the responses of the interviewees (Easterby-Smith et al., 2012; Saunders et al., 2009). The same is true for the interpretation of the results (Easterby-Smith et al., 2012). However, since an interview guide that was identical for both interview days was followed by both interviewers, this threat was reduced to an acceptable level. In addition, the preparation and set up for the event was conducted in a joint effort. Nevertheless, we are aware that an interview is always the interaction of two people and that this interaction is different for each pair and hence might unknowingly influence the answers of the interviewee. Furthermore, we surely have experienced some kind of learning curve while conducting the interviews and thereby acquired not only more knowledge about the research topic but also about the way of probing questions following the interview guide. Therefore, a complete elimination of this bias seems to be impossible and the steps taken towards trying to minimise the threat i.e. following an interview guide is a good starting point to reduce any observer errors to a minimum as well as having tested the interview beforehand.

Lastly, there is a risk of *observer bias*. As already stated there are two people working on the analysis of the data and hence there is a chance that there might be two different ways of interpreting the replies (Saunders et al., 2009). However, since the analysis of the results has been done together, this threat can be reduced. Another issue with the analysis of data is that their reliability can be affected by converting the raw data into codes and categories. This is a highly subjective procedure which relies on the subjective judgement of the researcher as to what is considered to be relevant. Therefore, we tried to focus solely on the raw data gathered from the interviews, thereby reducing personal inferences to a minimum in order to ensure reliability.

To summarise, another response to the issue of reliability when it comes to findings derived from using non-standardised research methods such as interviews is that they are not intended to be repeatable but should rather reflect reality at the time when the interviews were conducted. The assumption that underlies this type of research is "that the circumstances to be explored are complex and dynamic" (Saunders et al., 2009, p.328). The reason for choosing this research tool lies in its strength to gain insights from experts in the field that cannot be gained any other way.

3.6.2 Validity

According to Easterby-Smith et al. (2012) and Saunders et al. (2009), semi-structured interviews are regarded as highly valid in terms of data collection because the interviewer can use clarifying questions, probe answers or ask follow up questions to improve and ensure comprehensiveness and sharpen up the interviewee's response. However, some threats to validity remain (Robson, 2002). Firstly, Robson (2002) identifies history as a threat to validity. If the researcher decides to study people's opinion on a certain aspect e.g. a certain organisation or incident and this study is conducted shortly after a major event that has either a positive or a negative influence on that organisation or event then this might result in misleading findings (Saunders et al., 2009). In our thesis, the depreciation of the euro and its negative effect on the importing businesses could be seen as such an incident. However, this specific circumstance was the trigger event in the objective of the research to find out about how importers react to this phenomenon and what they do about it. For this reason this threat is not relevant in our case. Secondly, ambiguity about the causal direction is particularly difficult. In some cases it is hard to properly assess the causal relationship between the findings. Nevertheless, the issue is quite clear in our case. The depreciation of the euro causes perplexity in terms of how to go about the negative effects that hit the importers. Thirdly, a well know issue with qualitative methods is the relevance of the research to the interviewee.

Easterby-Smith et al. (2012) utter concern about the validity of answers given by respondents who do “not see any benefit or value in the study” (p.157). Hence, we decided to follow Easterby-Smith et al.’s (2012) advice and offered the interviewees access to the research findings in exchange for their participation in the study. This deal not only provided an incentive but also established trust.

The survey was sent out by the WLDV just before a weekend followed by a week of holidays. Coming back to work after a long weekend usually means a large amount of workload, which might have impacted the willingness to spend time on the survey. In order to elevate the response rate, the WLDV sent out three reminders with the request to participate in the survey. The first reminder led to an almost immediate response of three new participants, whereas no effects of the reminders two and three could be registered. The WLDV was conducting an own survey at the same time. We assumed that this might improve the response rate since companies had two reasons to gather financial data. Yet, it is also possible that companies only spent time on completing one survey and answering two surveys was simply too much of a time effort. This assumption is in line with the reasons mentioned by the companies that it is very time consuming to gather operational data. As many of the firms do not have a finance department, this data has to be generated. Most of the companies taking part in the online survey spent between 10 and 30 minutes on completing the survey.

The main reason for the low participation rate is believed to be that companies are not willing to share sensitive information about their operations with strangers. This issue was already brought up at the Exhibition and again in the following up communication after the exhibition. Furthermore, many of the companies in stage one answered that they believe that they are too small for using derivatives. As in the survey instructions the aim of our survey “providing possible solutions for Fair Trade importers” is mentioned, we believe that many companies thought that our research would not concern their specific needs. Additionally, as the Euro rate started to recover in the time of the survey conduction, the companies might not feel the need for a solution anymore. Finally, the low participation rate could also mean that there is no interest in this topic. However, reflecting upon our impression and answers at the exhibition, the vast majority of companies we approached felt interested and affected by this topic. In addition to the above mentioned, the catastrophic earthquake in Nepal on April 25, 2015 is believed to negatively impact the response rate since ten of the 66 surveyed companies are collaborating with producers in that country. We believe that these companies were very busy dealing with the effects on their producers and the situation in Nepal therefore we did not expect responses from those companies.

3.6.3 Generalisability

Generalisability is concerned with designing research in a way so that it can be generalised across other settings, organisations or the like. Saunders et al. (2009) argue that this can be difficult in a number of cases: If the study focuses on one organisation, a small number of organisations or organisations that are noticeably different in some way. Should this be the case, the research would not be very generalizable since the generalisability is defined as the extent to which the findings of a research study are applicable to other settings (Saunders et al., 2009). In our case, the studied sample could be seen as organisations that are noticeably different in terms of their mind-set and the overall industry values and conventions as outlined in the introduction, so generalisability would not be given. However, the research was first and foremost conducted in order to study this phenomenon in this specific research field, so generalisability was not a top priority. Nevertheless this does not mean that the research findings will only be valid or useful for this very industry and situation.

4 Analysis and Discussion

4.1 Analysis of Stage 1: Exhibition Interviews

The semi-structured interviews can be divided into three main areas of interest:

- Description of sample with general information about the company and operational data
- Perception and business effects of Euro depreciation
- Knowledge, decision making process and actions towards dealing with currency volatility.

The data collected was transcoded whenever possible in order to retrieve statistical measures such as average and median. Qualitative answers were grouped whenever possible, which allowed a statistical evaluation.

4.1.1 Description of Sample

Size

In the first part the companies were classified in four size categories. As it was not possible to gather reliable data about yearly revenues, we considered headcount as a good approximation.

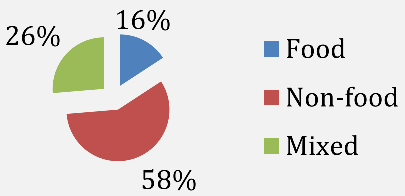
The first group is one-man enterprises making up 37 percent, the second group is two to three man enterprises with 26 percent, 10 to 19 person enterprises is the third group with 21 percent, and above (three companies with 25, 50 and 120 employees respectively) is the group of large enterprises representing 16 percent of our sample (see table 3).

Sample at the Glance

Size and Management

- Headcount (median): 2
- Two thirds operate with 3 persons or less
- 80% owner-managed

Sectors



Associations and banks:

- Main banking partners: Sparkassen & Volksbanken
- 95% member of at least one trade association

Main sales channels

- Exhibitions and markets
- Worldshops

Purchase Characteristics

- Implied yearly order volume of sample: €4.2 mn
- Median of implied yearly import volume: €50,000.00
- 50% of a single company´s order does not exceed €10,000
- 75% of a single company´s order does not exceed €20,000
- 17 out of 19 companies pay in USD and/or local currency
- 11 out of 19 pre-finance in average 50% of the order (non-interest bearing).

Table 3 Size Groups of Companies in Sample

Size group	Headcount	Amount in Sample (in %)
1	1	7 (37%)
2	2-3	5 (26%)
3	10-19	4 (21%)
4	25, 50 and 120	3 (16%)

Source: Own representation

A general observation is that most companies, about two-thirds of the sample, consist of less than three people. The median amount of people is two. The average headcount of 14.6 persons is misleading, as it takes one large company with 122 employees and two also rather larger companies with 25 and 50 employees respectively into account. At this point we need to mention that it was not possible to interview larger companies at the exhibition (Stage 1), since they were usually represented by sales staff only. As previously mentioned, these did not serve as a suitable interview candidates since managing risks falls within the area of responsibility of the decision maker (Oxelheim & Wihlborg, 2008).

Management

About 80 percent of the companies interviewed at the Fair Trade exhibition were owner-managed. The four companies that were not owner-managed are found to be equally distributed in our two largest size groups that were set up in the previous section. In five companies managers did not work full-time. Those companies are among the two smaller size groups. About 50 percent of the companies interviewed had more than one manager. Hence, Fair Trade businesses cannot be referred to as only one-man businesses and half of the companies not only depend on the human capital of a single person. Due to the fact that smaller companies are overrepresented in the sample, our findings are may not be representative of the actual situation in the market.

Product Categories

Furthermore, the companies can be classified into two product groups namely food and beverage (F) and non-food. Three companies are only importing food products, whereas eleven companies solely focus on non-food products. Five companies import both food and non-food products. The non-food category can be further separated into three main subgroups: craft jewellery (J), craft living (L), crafts wearing (W). Following this categorisation the companies are operating in four sectors F, J, L, W (see Appendix 2). Size groups one and two tend to focus mainly on the non-food sector. Only one company within these two groups also imports food products. One company in size group three as well as one company in size group four solely import food products, whereas the others are mostly mixed range importers.

Associations and Banks

95 percent of the companies belong to at least one Fair Trade association. 47 percent are part of two or more associations. It can therefore be argued, that associations play a significant role and are an important partner for Fair Trade businesses. The majority of companies seem to choose local banks such as Sparkasse or Volksbanken and Raiffeisenbanken as the main banking partner. In addition, some companies work with investment banks such as Deutsche Bank or ethical banks such as GLS. Some companies even work with both investment as well as ethical banks. There is no identifiable link between size and choice of financial partner.

Sales Channels

Although the main focus of this thesis lies on the importing side of the company, the revenue side was also taken into account. The idea behind this is to investigate in which currencies the companies sell and to find out if there exists a special dependency on a specific distribution channel. Self-explaining, all companies interviewed during the exhibition offer their products on exhibitions but also on other occasions such as Christmas markets. The respondents mention that this distribution channel was very important and also effective in order to make the company known among interested clientele. However, the participation is considered to be expensive due to staff expenses and registration fees. At this point it is also important to mention that we were not in contact with Fair Trade businesses that could not attend the exhibition. The second most frequently mentioned distribution channel is the Worldshop, which 90 percent of the companies use. Some companies also use additional third party online and offline retailers. More than half of the companies also operate their own online shop. Other distribution channels mentioned are direct sales, own stores and wholesalers.

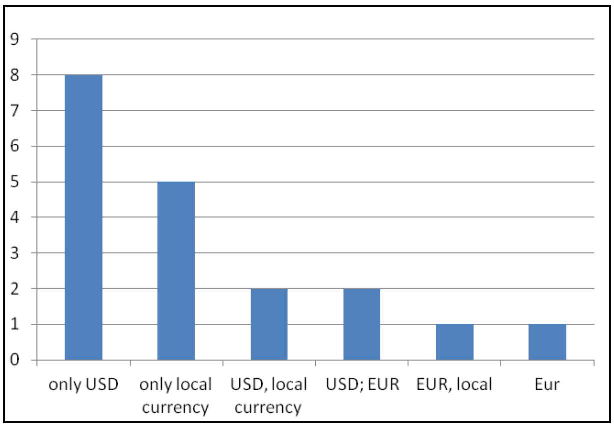
Since the Worldshops play an important role in the distribution of products, this relationship was investigated in more detail. Eight out of 17 companies generate more than one third of their revenues through them. About a quarter of the companies, that uses the Worldshop as their distribution channel generates more than two thirds of their revenue through this channel. Considering the importance of Worldshops in the distribution of Fair Trade importers, it is worth mentioning that Worldshops purchase their merchandise at half of the recommended retail price. Hence, Fair Trade importers have lower margins on products sold via Worldshops compared to sales generated by products sold through their own online shops. Following this reasoning, importers try to sell fewer products via the Worldshops and more products through alternative distribution channels, as this generates higher margins. Therefore, Worldshops could play a critical role in dealing with currency volatility. A more flexible purchasing policy which consists of accepting lower margins in times of depreciation and higher margins in times of appreciation is worth looking at.

Currency usage

More than 50 percent of the interviewed companies sell exclusively in Euros. The other half exports products to Switzerland denominated in Swiss Franc. However, all exporting companies state that the exporting volumes are very small, ranging from less than 10 percent to less than one percent in most cases. Reasons mentioned for the low export activities are the high export costs due to customs as well as setup cost related to distribution.

On the importing side, 78 percent of the companies pay their suppliers in USD, in local currency or in a mixture of local currency and USD (see graph 1). This finding underlines the large exposure to foreign currency risk. Additionally, there are also companies that pay in a mixture of USD and Euros or Euros and local currency which are less exposed to the foreign exchange volatility. The companies in the sample source their products mainly from countries in Central and South America, Africa and Asia. By investigating this aspect further, one might be able to determine country clusters. On this basis, local and regional financial institutions could be defined and contacted for discussion about foreign exchange volatility.

Graph 1 Currency of Payments to Producers



Source: Own representation

Purchase Patterns

Furthermore, ordering patterns of the interviewed companies were investigated. Since there are some companies ordering weekly, the average of 12.4 orders per year is misleading. A better measure is the median of 4.8 orders per year. The median indicates a foreign exchange exposure of roughly every ten to eleven weeks, i.e. whenever an order is placed. Again, it has to be mentioned that this number might change when taking larger players in the market into consideration. In the interviews, only 11 out of 19 companies mentioned making down payments on the day of placing the order. This finding contradicts the Fair Trade principles outlined in section 2.1. According to these principles, all Fair Trade importers are expected to pre-finance their suppliers. Thereby, they also create exposure to foreign currency exchange rate risk, yet on an irregular basis. Other companies which do not pre-finance are mostly found in size group one and stated that they would start offering pre-financing as soon as order volumes increased. The companies which pre-finance their suppliers make their down payments between 12 to 13 weeks before delivery. Usually this down payment is 50 percent of the order volume, in some cases even up to 100 percent. As a result of the pre-financing, Fair Trade importers face multiple exposures to FX rate risk with one order because the total amount of the order is spread across several payments.

Therefore, the difference in order frequency of companies with pre-financing and without pre-financing was investigated. Companies that do not make down payments to their suppliers, have a yearly amount of orders of 9.7 on average with a median of 3.8. Companies pre-financing their suppliers order on average 14.3 times with a median of 7.4. As the number of observations is too small to prove a statistical relation, it is not possible to generalize. Yet, within the sample of the interview participants, we discovered that companies which engage in pre-financing also tend to order more often. This means that their exposure frequency to foreign currency exchange rate risk is higher due to a higher amount of orders and also higher as each order comprises at least two transactions. Some of the companies which do not make down payments allow other types of credits, such as financing of machinery and packaging to their suppliers.

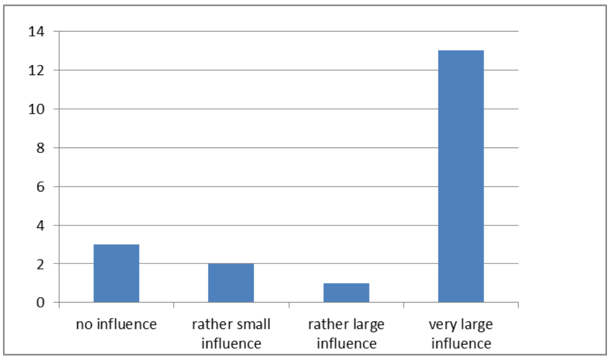
Order Size

The implied yearly order volume of the 19 companies interviewed is almost €5 million. However, one of the larger players alone stands for €3.15 million. The median of implied yearly order volume is €50,000. The average order size of the companies interviewed is about €21,000. Again the median of €7,500 is the better statistical measure. About half of the companies order for less than €10,000 in an average order, a quarter of the companies orders between €10,000 and €20,000, and the two larger companies have an average order of €60,000 and €150,000 respectively. Many companies talked about seasonal ordering, where the largest order for the Christmas business is in late summer or early autumn. Some suppliers order only once a year. Seasonal and one-time orders are maximum exposure orders, averaging in €42,200 with a median of €23,250. Comparing these numbers with the investigation about future contracts in the literature review (see chapter 2). This becomes apparent, when taking into account the payment agreements between Fair Trade importers and suppliers, which cuts each hedging size by 50 percent on average as explained above.

4.1.2 Perception of FX Rate Risk

A significant amount of companies feel that the depreciation of the Euro has a very large influence on their business (see graph 2), even stating that it could drive them to bankruptcy.

Graph 2 Influence of FX Volatility on Business

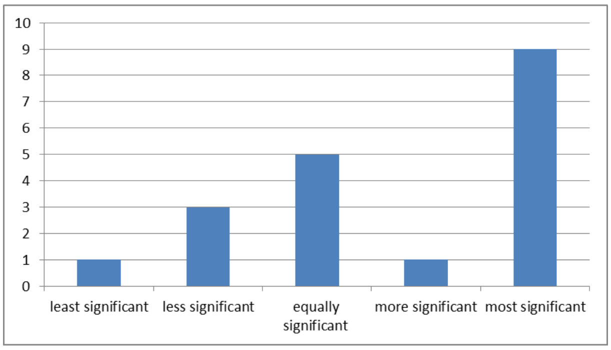


Source: Own representation

Some companies mentioned that the influence is so large, that they do not know how long they will be able to keep operating because their margins are diminishing or turning negative. Several companies stated that they order upon an advance order from their customers, meaning that they are bound to the prices fixed in the contract and are not able to adapt prices according to currency price volatility. On a transcoded scale from 0 meaning ‘no influence’ to 3 meaning ‘very large influence’, the respondents perceive the influence of the current Euro depreciation on their business to be between ‘rather large influence’ and ‘very large influence', on average at 2.3. Due to the size of the sample this average is only partly informative, yet reveals a trend regarding the managers' opinions. Furthermore, we found that with increasing company size the respondents find an increasing influence of the depreciation on their businesses.

When asked to cite other operational risks, purchase risks related to quality and punctuality as well as the merchandising risks were mentioned most frequently by managers. Other risks mentioned are liquidity and financial distress, competition and the political situation in purchase markets. Compared to those others risks, currency volatility risk was found to be equally important in five cases and most significant in nine cases. On a transcoded scale from 1 to 5, one meaning 'least significant' and five meaning 'most significant', the average risk is found to be 3.7 meaning that the FX risk is perceived between equally significant and more significant compared to other risks (see graph 3). Within our sample we observe that larger companies tend to view currency volatility as more significant in relation to other business risks compared to smaller companies.

Graph 3 Significance of FX Risk Compared to Other Business Risks



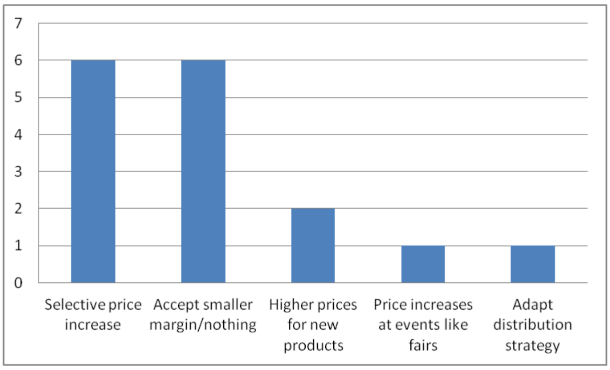
Source: Own representation

It is important to mention that the responses to both questions are most probably influenced by the negative topicality of the topic. Therefore, the same questions should be asked in times of a very stable Euro-dollar exchange rate as well as in times of an appreciating Euro. Furthermore, due to the size of the sample, the averages are only partly explanatory, yet reveal a general trend regarding the managers' opinions. Hence, both findings are important in answering our research question of whether a demand for hedging exists.

4.1.3 Knowledge, Decision-Making Process and FX Strategies

In the previous sections it was stated that the managers feel the exchange rate has a rather strong influence on their businesses and that, compared to other operational risks, the foreign exchange volatility is at least equally significant as other business risks, or even the most significant one. Therefore, we continue to analyse how companies cope with this risk. The most frequent reaction is to selectively increase prices for some products (see graph 4). Other strategies are to increase prices for new products or before events like fairs and markets. Six companies stated to simply accept the fact of having to pay more Euros for their products, and to not react at all to the depreciation. Asking why they have not done anything, the main answer was that there is nothing out there, since their volumes were too small and the banks did not offer adequate products. In no single case, a company directly addresses the volatility of the foreign currency, e.g. through financial products.

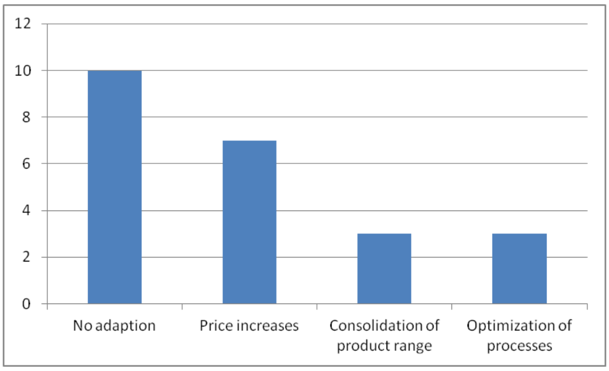
Graph 4 Usual Reaction to Depreciation



Source: Own representation

Moreover, when asked about their strategies and possible adaptions in the light of the Euro depreciation since starting in January 2015, the majority of companies stated that they had not made any changes (see graph 5). Another large part of the companies increased the prices in March, whereas a smaller amount of companies reacted by consolidating their product range. They claimed to buy fewer low-margin products and to buy fewer products from countries where the general business risk is higher. On the one hand, consolidating the product ranges can be positive in terms of becoming more profitable. On the other hand, it also means that the depreciation indirectly translates into less or no orders from several suppliers. Hence, the last and weakest link in the chain carries the main burden, which goes against the principles of Fair Trade discussed in the literature review. Other companies adapted their processes, such as ordering less frequently or lowering their average inventory on hand.

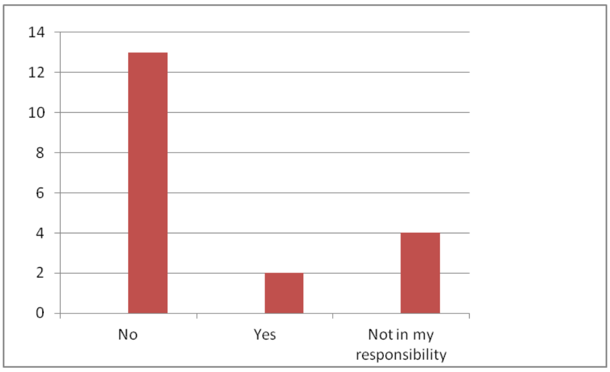
Graph 6 Adaption of Strategy Since January 2015



Source: Own representation

As financial instruments such as forwards, foreign currency accounts or others have not been mentioned as a risk management strategy, companies were then asked if they have informed themselves about any possible external solutions (see graph 6). The majority of companies answered with ‘no’, stating that they were too small which is way banks would not be interested in them, a reason also mentioned by Ehrlich et al. (2012). Asking if they would know any financial instruments, half of the companies answered with no, and the other half answered with yes listing forward contracts, SWAP, future contracts and currency accounts. There were only two companies which have experiences with financial instruments. One company used forward contracts for two years, yet complained about the inflexibility, less liquidity due to tied-up capital, unfavourable exchange rates, and the amount of time invested. Another company used a currency account for about two months, yet soon experienced liquidity problems as the foreign currency money was tied up and they were not able to finance part of the amount with credit.

Graph 5 Gathered Information About How to Manage FX Exposure

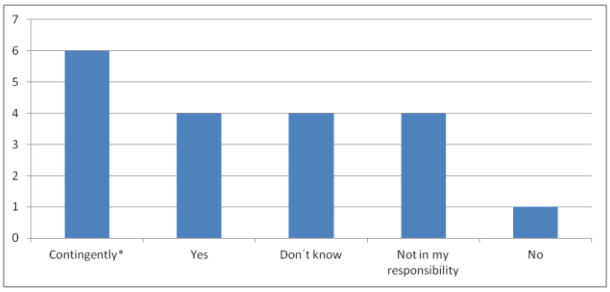


Source: Own representation

Next, the companies were asked about currency rate insurance, whether they would be interested and if so, how much they would be willing to pay for it (see graph 7). Most of the companies answered that their interest would depend on an internal cost-benefit evaluation. Four companies answered that they are definitely interested and immediately looking for a solution. These two groups make up more than half of the companies interviewed. When asked what they were willing to pay for such an insurance, seven companies could not make a statement as they would have to analyse their past losses attributed to foreign exchange volatility first. Three companies are willing to pay up to 5 percent of their purchase volume.

Only one company answered that it is not interested, as it just started to operate and feels that it is not yet affected by the exchange rate risk. Four interviewees could not make a statement, as currency volatility is not in their area of responsibility. This is an important finding for answering the research question since the majority of the companies stated that they at least contingently interested. This finding is in line with study results from Smith and Stulz (1985) who argue that when managers are owners they tend to be more risk averse hence are more likely to demand insurance. Speaking to more companies and decision makers would be necessary to confirm this assumption.

Graph 7 Interest in an FX Volatility Insurance



*contingently: if cost/benefit analysis is positive

Source: Own representation

Finally, we can confirm that decisions regarding strategy and foreign exchange risk are made at the management level (see Oxelheim & Wihlborg, 2008). Only the three largest companies mentioned that decisions are made in a team including executives from purchase, financial and sales departments. About half of the companies sometimes uses external assistance. Consultancy firms were not mentioned, since advice is rather obtained from managers of other businesses, trade organizations, friends or banks. However, Pennings and Garcia (2004) suggest that especially small and medium sized enterprises depend on external advice of consultants or bankers regarding the usage of derivatives.

4.1.4 Summary of Findings

Our findings show that foreign currency exposure is very high as 78 percent of the companies interviewed pay their suppliers in USD, local currency or in a mixture of USD and local currency. A significant number of the companies interviewed feel that the depreciation of the Euro has a very large influence on their business. Similar findings were attained in McCharty´s (1999) study of Australian SMEs. Thus, managers are aware of the risk which is a fundamental condition for engaging in hedging, as explained by Pennings and Garcia (2004). The main strategy in dealing with currency volatility is to adapt prices. The lack of knowledge about financial products is in line with research about SMEs discussed chapter two. The companies are interested in a solution to their FX exposure and are willing to pay for an insurance instrument depending on the cost-benefit. This finding is in line with Pennings and Garcia's (2004) research which suggests that in case of concentrated ownership, which is the case in our sample, a company´s management is more risk averse, and hence has a greater readiness to engage in hedging. This higher likelihood of engaging in hedging is also given as the inherent exposure, being the difference between revenues and costs denominated in foreign currency, is very large as there are hardly any foreign currency revenues. Furthermore, it was found that companies which pre-finance their suppliers with non-interest bearing down payments tend to order more frequently than companies which do not. This means that for each order there are at least foreign currency transactions. Several companies have also started to rationalize their product range and decrease order volumes. This may have some positive effects in terms of less tied up capital, but it might also lead to underinvestment or a slowdown in expansion. This is in line with Culp's theory (2002), which states that hedging can create value by decreasing the underinvestment problem as a result of the cash flow volatility. The analysis of this stage brings us closer to describing the current exposure of Fair Trade importers to FX rate risk in the light of the Euro depreciation, by answering the first two research questions. Thereby, the third research question asking how their demand for currency volatility insurance can be hedged using derivatives is derived.

4.2 Analysis of Stage 2: CEO Interviews

4.2.1 CEOs of Contigo GmbH, El Puente GmbH and dwp eG

The second set of interviews was conducted in order to gain insights into hedging activities of medium sized businesses, accounting for the underrepresentation of larger sized companies interviewed at the exhibition. Therefore, in May 2015, we conducted interviews with the managing directors of El Puente GmbH, Contigo GmbH and dwp eG (referred to as El Puente, Contigo and dwp respectively from here onwards), three of the big players in the German Fair Trade import market. The CEO of Banafair was already interviewed at the fair and his opinions were already included in section 4.1. A summary of the key findings of the interviews is presented in the following paragraphs.

- For more than 25 years **Martin Moritz, CEO of *EL PUENTE GmbH*** has been working in the Fair Trade industry, being exposed to many ups and downs. During an email conversation we discovered that Mr. Moritz has gathered experience using financial instruments and drives research on how the financial industry could complement the Fair Trade movement. His thoughts about the situation in the markets are therefore considered to be very valuable.

- For over six years, **Ralph Wüstefeld has held the position of CEO of *CONTIGO GmbH***, one of the large players in the Fair Trade industry that not only sells their products to retailers, but operates its own retail chain. Mr. Wüstefeld was not present at the fair but his sales personnel offered to contact him on our behalf. With his diverse experience in traditional retail (REWE Group, full-range trader) as well as passion for the Fair Trade industry, his knowledge about the current situation allowed us vital insights into our research topic.

- **Thomas Hoyer is the chairman of the cooperative *dwp eG*,** one of the best known Fair Trade importers. Dwp was founded from several Worldshops, we therefore consider Mr. Hoyer to understand not only the importing and wholesaling side, but also the main retail channel of Fair Trade importers. As dwp imports commodities, we expect Hoyer to add have highly interesting value.

The findings from the interviews are structured as follows. Firstly, the impact of the exchange rate volatility on Fair Trade businesses; secondly, the experience with and strategies resulting from managing FX exposure; and finally where they see the responsibility of setting up suitable solutions. In the following section, the most relevant and interesting points regarding our research questions are presented and analysed. At the end, a summary stating the main findings and key implications is provided.

4.2.2 Impact on Business

All interviewees agree that the currency volatility and the resulting FX exposure has a very large impact on their respective companies. Moritz (interview, May 12, 2015) stressed that this is not only an issue for Fair Trade companies but for all importers no matter how small or large. Moritz (interview, May 12, 2015) points out that the impact strongly depends on the **type of product imported**. This is because there are usually higher margins on non-food articles. Companies with a high share of non-food products in their product range are able to absorb the currency depreciation better than companies importing mostly food products, Moritz (interview, May 12, 2015) knows. In the food business, especially the coffee business, conventional retailers possess high bargaining power thereby exercise pressure on retail prices by putting down margins. As a result, the influence of currency volatility for food products is higher than for non-food products. Hoyer (interview, May 15, 2015) also highlights this issue arguing that, especially when it comes to the import of commodities such as coffee and sugar, the need for dealing with FX exposure becomes more obvious, since the competition in the market is much higher.

Another reason for the high exposure can be found in the **principles underlying Fair Trade** which we discussed in section 2.1 in the literature review. Wüstefeld (interview, May 12, 2015) and Hoyer (interview, May 15, 2015) stress that usually a minimum of 50 percent of the goods is pre-financed when the order is placed, sometimes even up to 100 percent. In general, there is a time span of six to eight months between placing an order and receiving the delivery and sometimes additional delay for transportation issues increases the waiting time. The resulting uncertainty towards market fluctuations demands some kind of insurance to guarantee planning reliability, according to Hoyer (interview, May 15, 2015). Moritz (interview, May 12, 2015), however, argues that fixing an exchange rate would lead to significant disadvantages compared to competitors, in the case of appreciating currency. This dilemma is closely linked to the controversy discussed in the literature review (see section 2.2.2); whether or not hedging adds value to a company as it not only limits the downside but also the upside potential. In Moritz's (interview, May 12, 2015) opinion particularly the non-food articles, which are sold and priced through catalogues, should be hedged using financial instruments, since prices are predetermined at the beginning of each year and cannot be adapted. Hoyer (interview, May 15, 2015), however, reinforces that all products sold via catalogues or fixed long-term agreements should be hedged since prices cannot be adjusted flexibly. Wüstefeld (interview, May 12, 2015) sees the Price Premium as an additional critical factor for the exposure Fair Trade importers face, besides, pre-financing and the long time span between placing an order and receiving the products. The Price Premium Fair Trade importers pay ranges between 30-100 percent and depends on the absolute price of the product. Products with a higher value such as ceramic artwork have a smaller Price Premium than lower value products such as candles and the like, according to Wüstefeld (interview, May 12, 2015).

Another issue related to FX exposure is the **price elasticity** of Fair Trade products. Moritz (interview, May 12, 2015) experienced that consumers of Fair Trade products are generally inelastic to price changes. He argues that those consumers are not only willing to accept the Price Premium but also price increases related to macroeconomic factors. However, there will be a limit to what consumers accept, Moritz (interview, May 12, 2015) warns. Therefore, Moritz (interview, May 12, 2015) highlights the important link between, for example, Fair Trade coffee prices and conventional coffee prices (see section 2.1).

4.2.3 FX Rate Risk Strategies and Experiences

Moritz (interview, May 12, 2015) explained that his company has used various hedging instruments such as foreign currency accounts, forward contracts, options, and other personalized derivatives provided by Commerzbank. In his opinion, engaging in hedging in any form is speculative and a necessary evil. Generally the trading volume ranged from €50,000 to €100,000. Smaller volumes were not enough to start working with banks. El Puente´s strategic mix to deal with its foreign exchange exposure consists of hedging one third of the exposure with options, one third with forward contracts and buying the last third on the spot market. While options are most expensive they offer the advantage of being able to decide whether to execute or not. Moritz (interview, May 12, 2015) argues that compared to forward contracts, options are too expensive since the upside potential usually does not justify the cost premium. If an option is suitable to the needs of the company, the price is about eight to nine percent of the contract volume. An option with a reasonable cost of about two or three percent, does not fulfil the needs. Some of the financial instruments El Puente used were contracts valid for one or two years, he argues. For this time certain exchange rates are fixed, hence those agreements are fairly inflexible. Due to the lack of flexibility, hedging with long-term engagement creates an even higher risk. Evaluating the effectiveness, Mr. Moritz (interview, May 12, 2015) says that they have compared the results of their hedging strategy over the past four years with the results they would have had only buying at the spot market. The difference, he states, was not very large. Yet, in the years of an appreciating Euro, they realized yearly profits attributed to the currency of about 1.5 to 2.5 percent of their import volume. This was achieved with a mix of hedging and buying on the spot market. With the current depreciation, they face currency related losses of about 10 percent of the import volume.

Dwp uses forward contracts to secure their larger orders. Their main banking partner is Sparkasse and contracts are available from €50.000 onwards. According to Mr. Hoyer, this hedging instrument is quite suitable for dwp due to its low costs. However, smaller orders starting between $5.000 and $30.000 cannot be covered with forward contracts. Dwp investigated if options would also be a possible instrument for them, yet, due to their evaluation and values, they believe that options are much more speculative and do not meet with their requirements. A recurring strategy for dwp was to increase prices when the Euro depreciated below a certain mark.

According to Wüstefeld (interview, May 12, 2015), an importer's strategy for managing FX rate risk is three fold. The first option is to negotiate with the producer and pay them less respective to the market fluctuations, the second possibility is to reduce its own margins and thereby swallow the bitter pill themselves, and the third opportunity is to pass the exposure on to the end consumer by raising prices. Yet, for Contigo, as Fair Trade importer, the first option is not viable since it would contradict the Fair Trade principles such as the Minimum Price and Price Premium. However, this is only a temporary solution. Therefore, the third option is likely to become reality soon but depends on how the retailing industry in general reacts to the market fluctuations. Since, as stated in the beginning, this issue does not only affect Fair Trade importers but all kinds of importers, e.g. companies importing products from low-wage countries in the same regions, the only difference in terms of dealing with the exposure is the possibility of passing fluctuations on to the producers and farmers for conventional traders. Ten years ago, Contigo opened up a foreign currency account in indischer Rupie at Commerzbank (since their largest supplier is located in India) in order to circumvent high transaction fees resulting from the money conversion and the international money transfer. Transaction costs without a foreign currency account were three times as expensive compared to transaction costs resulting from the foreign currency account as this fee could be reduced to one percent of the transaction volume. The money paid in to the foreign currency account allowed a cushion for six months but was used up in the beginning of the year. The main issue with this strategy is that it is highly speculative and therefore is no alternative to hedging itself.

Summing up, we can observe that the companies have different approaches: from the least speculative instrument which is the currency account, through to forward contracts to options. All companies state that engaging in any kind of foreign currency hedging is speculative and they depend on bank advice. Additionally, FX exposure can only be hedged if the amounts are large enough. Another problem mentioned is the inflexibility which is often created through hedging, as it binds up capital. This argument was also mentioned in the interviews at the exhibition.

4.2.4 Institutions Responsible for Setting up a Solution

Wüstefeld (interview, May 12, 2015) states that, for now, Contigo is out of the woods, since he believes that the Euro will not depreciate any further. Nevertheless, until there is a monetary union between the Euro and the Dollar, the FX exchange rate will always be up for speculation and this speculation will rest in the hands of either the CEO or the financial department. Since all Fair Trade importers are profit-oriented businesses, they work exactly like conventional SMEs, hence there is no charity. Therefore, in his opinion, Fair Trade importers cannot hope for special treatment from the financial market.

The three interview candidates mention a variety of different responsible institutions. All of them mention Fair Trade organizations such as the **WFTO** and the **WLDV,** but also ethical banks. Moritz (interview, May 12, 2015) considers WFTO to carry responsibility when it comes to driving some kind of currency volatility solution, as this institution has a lot of credibility among the market participants, which is important since Fair Trade importers are suspicious towards traditional financial institutions. He wishes to have some informative guidance by the WFTO, e.g. in terms of recommending to Fair Trade players how to cope with the currency volatility and when to engage in insurances. By that, he believes, the currency speculation gains or losses could be disregarded within the industry because the whole market would react in a similar way. Hence, companies could focus on the core of their businesses. Mr. Moritz (interview, May 12, 2015) knows, that this is a very noble wish and quite hard to achieve.

Hoyer (interview, May 15, 2015) and Moritz (interview, May 12, 2015) mentioned ‘Shared Interest Society Limited’ which already works as a clearing company for transactions between importers and producers. Shared Interest focuses its work on Fair Trade companies which are members of the WFTO. Concerning corporate and currency financing, Contigo is in contact with ‘Procredit Bank AG’, yet this bank does not provide derivatives or any kind of FX hedging to manage the exposure. In order to engage in either one of those possibilities, liquidity reserves are needed which, in the case of Contigo, were not high enough. Hoyer (interview, May 15, 2015) and Wüstefeld (interview, May 12, 2015) see possible solutions within financial institutions such as ‘Oikocredit’ or ‘GLS’, however derivatives do not belong to the banks´ expertise at the moment. From Sparkasse and Commerzbank, banks that the three companies work closely together on general matters, Moritz (interview, May 12, 2015) and Wüstefeld (interview, May 12, 2015) do not see any major possibility that they would offer more small scale solutions in the future. Hoyer (interview, May 15, 2015) on the other hand thinks that Sparkasse could also engage in smaller scale solutions, as they have a regional focus and seek close customer relationships.

On the other hand, there is the WLDV which carries responsibilities. According to Wüstefeld (interview, May 12, 2015), the Worldshops have significant margins which they use to finance their own charity projects. Worldshops see Fair Trade importers as their suppliers and do not think all the way until the end of the supply chain. Therefore, the WLDV will most likely not intervene on behalf of the importers when those face shrinking margins due to depreciating currency. Importers are already in contact with WLDV to work on this issue, especially to foster communication to raise awareness among Worldshop owners. All importers pay two percent of their revenue as a fee to the network in order to become and stay a certified supplier. Hoyer (interview, May 15, 2015) does not see a responsibility and potential within the Worldshops, as in his opinion Worldshop margins are actually too low in many cases. Worldshops would need to raise fixed costs for location and employees and become more profitable. This is the only way to grow and expand sustainably. His opinion might be biased, as dwp originated from several Worldshops and operates its own stores today.

4.2.5 Summary of Findings

The larger companies in the Fair Trade industry engage in some kind of currency volatility insurance. Insurance is especially important when it comes to commodity purchases such as coffee and sugar as the competition on the retail side is much higher and hence margins are rather low. Smaller orders of non-food products are often completely unhedged since those orders are less foreseeable, irregular and have small contract sizes. Banks provide no solutions since their smallest hedging solutions such as forward contracts and options have contract size minimums starting at €50,000. Since hedging instruments usually tie up large amounts of capital and since Fair Trade companies experience a general lack of liquidity, which has been discussed in stage one, companies feel a need for short term solutions that provide more flexibility and bind less resources. A currency volatility solution may be triggered and supervised by an organization such as the WFTO, also driving the lobby work within the financial sector and promoting solutions among Fair Trade companies. The CEOs find that a financial institution already engaging in social activities should take on the lead as those are more creditable for Fair Trade companies. Options are seen as less suitable as they often appear to be too speculative, complicated and inflexible for the nature of the businesses. Furthermore, we can confirm the Fair Trade principles, as purchase prices are not renegotiated. Buying in Euros, the suppliers are allowed to increase the prices or charge the income difference in local currency.

4.3 Analysis of Stage 3: Online Survey

4.3.1 Online Survey

> **Survey Sample at Glance**
>
> - Combined yearly order volume of sample: €15,4mn
> - Median of yearly import volume: €300.000
> - Average of yearly import volume: €1,200.000
> - Amount of orders (median): 12
> - Import value/revenue: 50-51% (non-interest bearing).

The online survey was conducted to support the findings of the previous two stages. The survey is used as a descriptive tool, enabling us to further describe the specific insurance demand of Fair Trade importers. the exhibition. Since we decided to conduct the survey anonymously by sending out an online link it is important to mention, that for this reason, it is impossible to distinguish whether the companies who participated in this survey have already been interviewed before stage one or two. Intentionally, it was not asked if companies participated in the interviews at the exhibition since our priority was to avoid suspicion and ensure anonymity. The response rate of 19.7 percent is low, even though the survey was conducted anonymously and channelled through the WLDV, a credible institution. 62 out of 66 companies opened the link to the survey but did not start or complete it. The reasons for the low response rate have been explicitly analysed in section 3.6.2.

The findings of this stage can be seen as a complementary part, supporting the findings of stages one and two. It will not be possible to describe the market quantitatively, i.e. in terms of categorizing the market in exact foreign currency exposure groups. Notwithstanding the above, we believe that the combined 76 members of Association of Worldshops and Fairband represent most of the companies operating in the market since all of them fulfil the requirements of Fair Trade principles. Hence, the total population examined in this research paper is 76. With our survey sample of 13 we are able to observe 17.1 percent of the total population. For this reason, by combining and comparing these observations with the data collection from stage one and two, it will still be possible to make some qualitative statements about trends among the target group. To develop suitable financial products, a categorization and in-depth analysis of companies' financial data will be necessary.

4.3.2 Findings of Online Survey

In order to describe the FX exposure, size, frequency and purchasing patterns were analysed. In the survey we found different numbers when it comes to order size. The median of a average order is €19,690 compared to €7,500 in the interview sample. The maximum exposure order has a median of €30,630 compared to €23,250. Contrasting these numbers to the findings from the interviews at the exhibition interviews (see section 4.1) the companies in the survey ordered more frequently, with a median of 12 times a year. The time between first payment and delivery is 12 weeks on average and has a median of 13 weeks. For those reasons, we can infer that the companies which answered the survey are larger than the companies interviewed at the exhibition. It is not possible to combine both data sets as it is impossible to make a well-grounded distinction regarding whether a company has participated in both, survey and interview.

The average import over revenue ratio as well as the median is 51 percent. Hence, import values represent a large share in gross margin. The average earning before tax over revenue ratio is 3.3 and has a median of 1.9. Three of the companies have stated to have no or negative profits. Four of the remaining nine companies have earnings before tax ratio between 5.9 and 7.2 percent. This data is not informative due to the small sample size and large variation in answers. Yet we can observe that the values of imports make up a large share in the cost structure. Furthermore, we can assume that profit margins are rather low. Combining those two observations, a price increase of imports due to Euro depreciation will directly and strongly affect the profits.

We further investigated how much the companies rely on credits and we found that about two thirds use debt to finance their orders. We also tried to find out the leverage of financing, yet as the sample size is too small, the results are not informative. Having to pay principles and interest on credits, lower cash flow volatility is preferable in order to lower financial distress costs and increase the debt potential (see for example Froot et al., 1993 in section 2.2).

Evaluating the natural hedge potential, the companies participating in the survey have vanishingly low shares of revenues in currencies other than the Euro. This finding is in line with our findings in the interviews conducted at the exhibition. Only one company realises around 10 percent of its revenues in Switzerland. A similar picture to that seen in the exhibition interviews is also seen within the interest for exchange rate insurance. While more than half of the companies are interested, another quarter is unsure.

Summing up, it can be established that Fair Trade companies are in a special situations when it comes to FX exposure. Their order behaviour with pre-financing, price-taker attitude as well as their import heavy cost structure and lack of natural hedge possibilities make them strongly dependent on a stable currency which is in line with findings from the first two stages. It can also be confirmed that the companies are strongly interested in some kind of currency volatility insurance.

4.4 Analysis of Stage 4: Financial institutions

The previous stages demonstrate that Fair Trade companies believe that they are too small for a hedging solution offered by banks. In this section, we investigate whether financial institutions offer hedging instruments which take into account the special characteristics of small and medium Fair Trade enterprises. In doing so, we put ourselves in the shoes of Fair Trade importers, approaching financial institutions with the specific characteristics of a regular small scale Fair Trade order pattern based on the results of section 4.1: €7,500 every 11 weeks. Our research in the previous sections reveals that Fair Trade importers mainly collaborate with the traditional regional banks therefore those institutions were approached first.

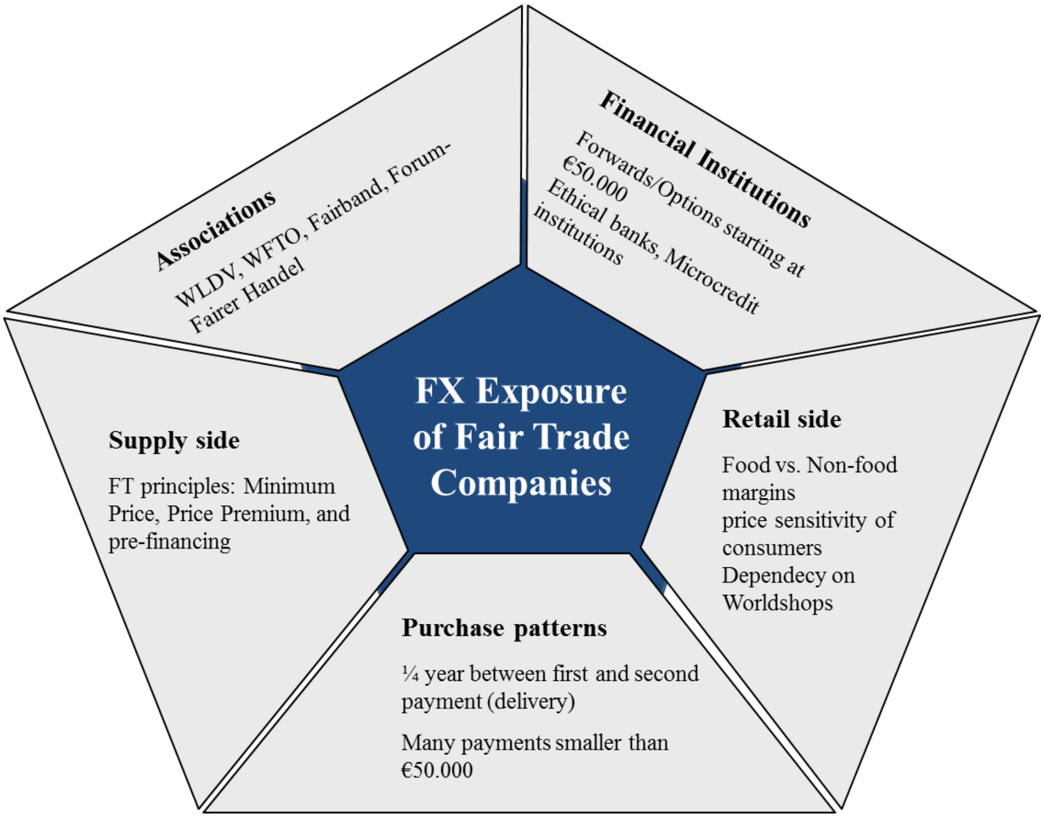
Sparkasse was present at the exhibition and was approached at its exhibition stand as well as at a regional office in Esslingen. According to their sales representatives, no special hedging instruments are offered to Fair Trade companies and no instruments for such small foreign currency exposures exist. GLS representatives interviewed at the Fair Trade exhibition stated that they would not engage in any currency related instruments except ordinary money transfer. As some Fair Trade companies also work with investment banks such as Deutsche Bank and Commerzbank, the Deutsche Bank was selected and contacted via telephone. It was stated that there are no small hedging instruments below €100,000. Additionally to a possible offline solution, Katonx Limited was contacted as an online financial service company, entirely specializing on foreign exchange solutions. For Kantox, the minimum contract size for hedging deals is also €100,000.

As conventional banks did not provide us with any suitable solutions, we decided to contact the cooperative Oikocredit. Since 2012, Dr. Florian Grohs has been Credit Director of Oikocredit International, with extensive professional experience in the financial sector working for DZ Bank and the Worldbank before joining Oikocredit in 2002. During his time at Oikocredit he held management positions such as Regional Director for Central and Eastern Europe, and Director of Oikocredit Germany. In addition, Dr. Grohs is vice chairman of Transfair e.V., an association labelling Fair Traded products. His experience in and knowledge of the market were conceived as very valuable, therefore a semi-structured telephone interview was conducted. To the knowledge of Mr. Grohs, there are no financial institutions or products in the market that focus on the special needs of Fair Trade importers. In his opinion, the main reasons are the small monetary importing volumes of those companies. He compares hedging instruments with credits arguing that the setup costs of the financial products are almost the same no matter how large or small the contract size is. Hence, it might not be interesting for financial institutions to enter into this niche business. Being asked what he thinks about the idea of pooling many small hedges into one large hedging contract (see section 2.3), Dr. Grohs argues that this could be an interesting approach to solve the dilemma. However, in his opinion such a solution should not only be aimed at Fair Trade importers, but also be accessible for other small importers with similar needs. By that, Grohs believes, the critical factors such as total volume might be able to be solved and the instrument could be a success.

4.5 Discussion of Key Findings

Combining the findings of all four stages, we can clearly observe that the hedging situation is influenced by various different factors, leading to a unique FX exposure situation. Not only the order patterns influence the exposure, but also the type of product imported, the price sensitivity of consumers and the Worldshop dependency on the retail side. On the supply side the largest influence can be attributed to the Fair Trade principles. Associations such as the WLDV play a major role when it comes to managing expectations in terms of support, whereas financial institutions only offer insufficiently suitable products. Thus, we developed the FX Exposure Framework for Fair Trade Importers displaying this situation (see figure 2).

Figure 2 FX Exposure Framework for Fair Trade Companies

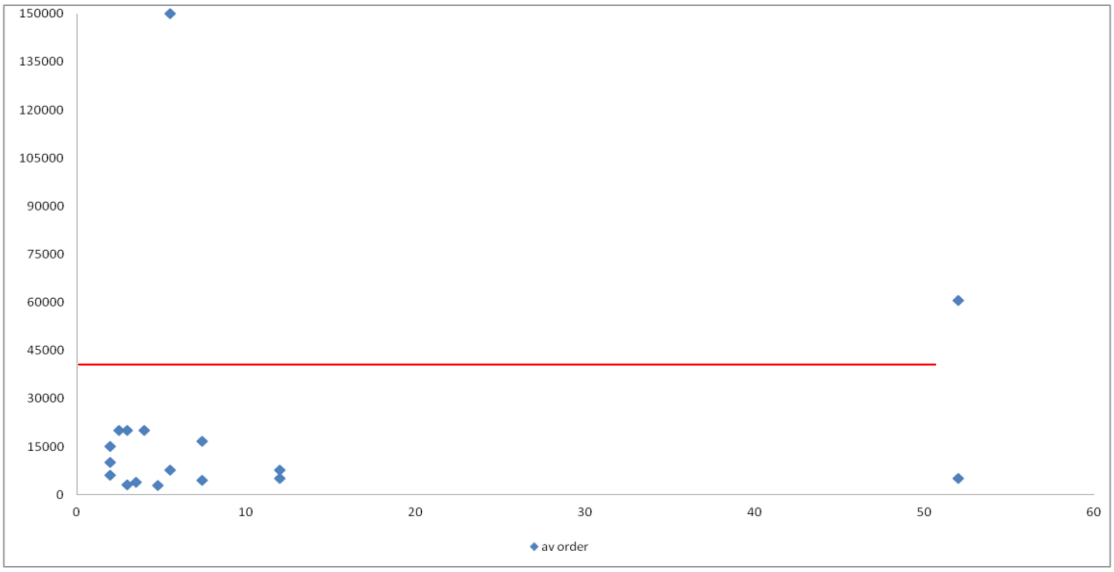


Source: Own representation

In the following paragraph, the key findings of our analysis regarding the segments of the framework are presented, thereby answering our research questions. On the supply side of the companies, import expenses represent a large share in gross margin as the import over revenue ratio is around 50 percent (stage 3). A deprecating Euro therefore strongly affects the EBIT margin since most of the companies pay their suppliers either in Dollar or in domestic currency (stage 1, 2 and 3). As a response to the Euro depreciation the companies allow their suppliers to increase the purchase prices or charge the income difference in local currency (stage 2). Many companies already have low margins therefore shrinking margins are especially harmful, as on the retail side within the framework they distribute a high share of their products through Worldshops (stage 1, 2 and 3). The majority of companies feels a need for currency volatility insurance and is willing to pay up to 5 percent of its purchase volume (stage 1, 2 and 3). The company's main reaction to the depreciation is to increase retail prices, yet companies state that there is a limit due to the already elevated prices compared to traditional trade and the price sensitivity of consumers (stage 1 and 2). Few companies use hedging instruments such as foreign currency accounts, forward contracts or options (stage 1 and 2). A foreign currency account can be seen as a first step, followed by forward contracts (stage 1 and 2). Options are believed to be least effective, due to the complexity, their speculative nature and the higher costs (stage 2). As stated above, forward contracts and options can be used with a foreign currency demand of €50,000 or more (stage 2 and 4). Many companies have lower order volumes especially those that import non-food products. However, when importing food products the need for hedging increases due to lower margins (stage 2). Within the sample, we found that companies which pre-finance also tend to order more often thus are exposed to more foreign exchange transactions (stage 1). Three months is the usual time between the first and second payment and about two thirds of the companies finance their orders with credits (stage 1, 2 and 3).

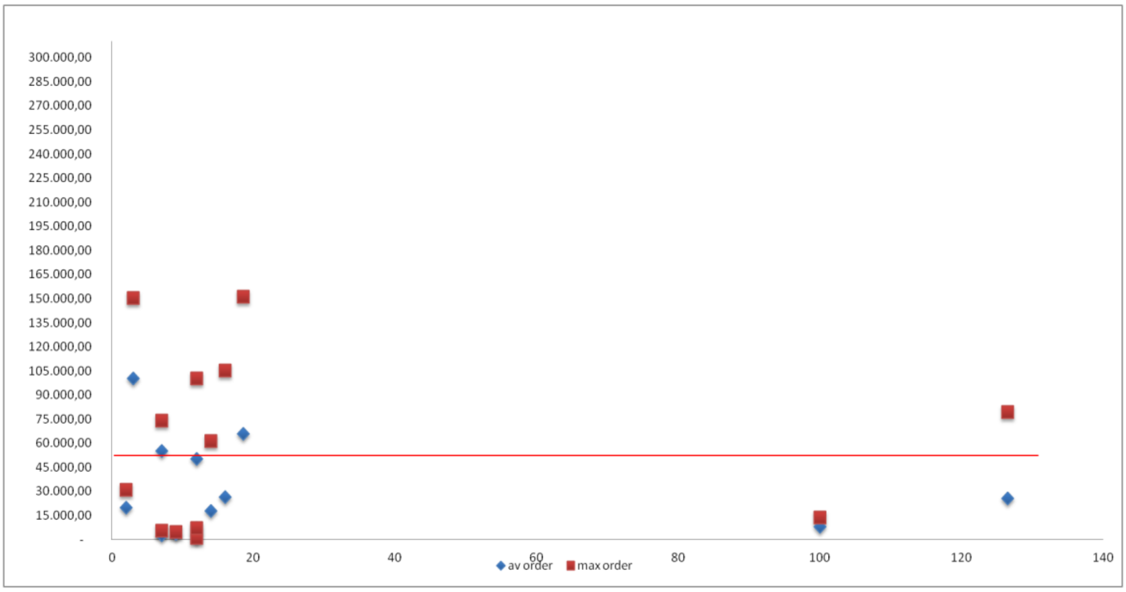
Concluding, we can clearly state that Fair Trade companies perceive a strong impact from foreign exchange rate exposure. Companies are hit especially hard, as Fair Trade principles allow no passing through. Companies use very little hedging instruments, which can be mainly attributed to the lack of suitable financial products which we found by extending our research to the supply side. Until today, the main answer to the depreciation has been increasing retail prices.

Graph 8 Order Frequency and Size for Companies at the Exhibition



Source: Own representation

Graph 9 Order Frequency and Size for Companies Answering the Online Survey

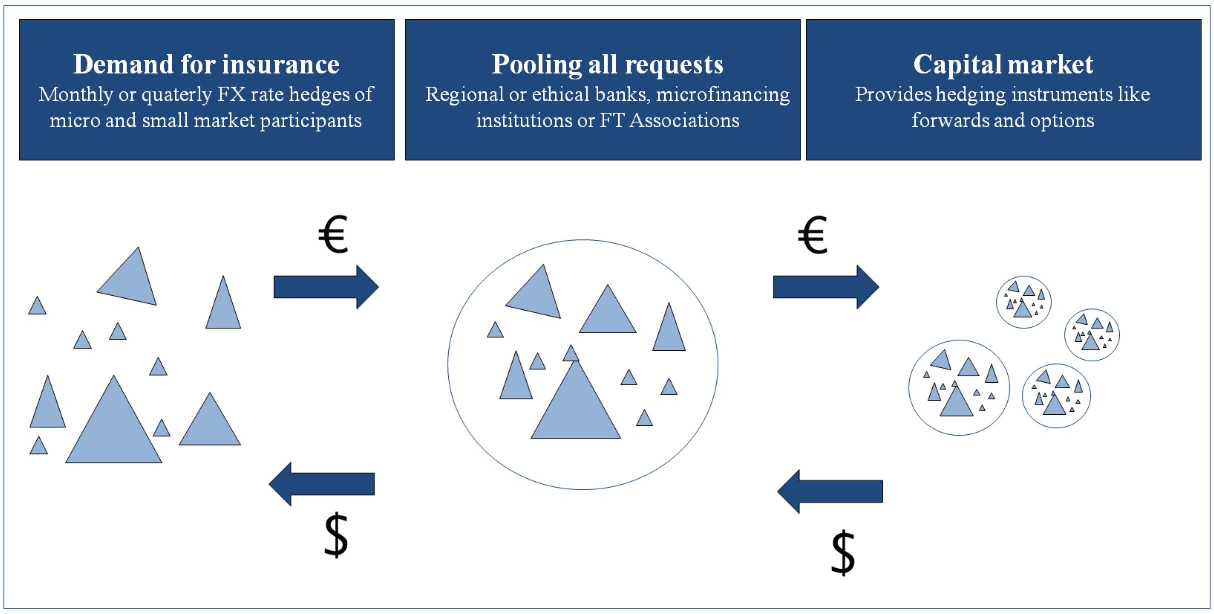


Source: Own representation

Larger Fair Trade companies are able to cover part of their foreign exchange exposure with hedging instruments such as foreign currency accounts, forward contracts or options (stage 2). Those products are not exclusively created for them but are just ordinary financial instruments accessible to all types of companies. An ordinary Fair Trade importer, with a yearly purchase volume of €50,000 to €300,000 and much smaller individual orders will hardly find any currency hedging solution, besides a foreign currency account (all stages) since the FX exposure is below the invisible line of €50,000 (see graphs 9 and 10). A solution may be triggered by combined efforts of Fair Trade associations and the financial sector with social or traditional financial institutions.

In our opinion the Fair Trade companies, represented by their associations WFTO, WLDV and Fairband need to stand up for themselves and work together regarding a solution for their FX needs. In doing so, institutions such as Shared Interest, Oikocredit or Sparkasse will understand that there is a high demand for forward contracts with sizes smaller than €50,000.
By establishing a pooling institution a number of smaller FX demands of Fair Trade companies could be pooled together thereby exceeding the critical size for ordinary hedging products (see figure 3). Since the total market of FX needs might still be rather small for financial institution to get active, the pooling system could be extended to a wider range of companies with the same issues.

Figure 3 Examplary Solution Approach



Source: Own representation

5 Conclusion

Our research extends previous research on SME foreign currency exposure by Ehrlich et al. (2012), Pennings and Garcia (2004) as well as Smith and Stulz (1985) who suggests that SMEs tend to use less derivatives due to their specific characteristics. Our study contributes to existing literature by examining derivative use of micro, small and medium sized Fair Trade importers in Germany. We investigate how micro, small and medium sized Fair Trade importers perceive and manage FX exposure. We find that, mainly due to the Fair Trade principles (Altman, 2010; Dragusanu et al., 2014, LFO, 2015; Sukhamay, 2013) our target group experiences a strong impact by FX exposure but hardly uses hedging instruments to manage this exposure. The results suggest that micro, small and medium sized Fair Trade enterprises experience a need for currency volatility insurance. Hence, we extended our research to discover whether financial institutions offer hedging instruments which take the special characteristics of micro, small and medium Fair Trade enterprises into account. We conclude that the supply is insufficient. Many companies are excluded due to the fact that, in most cases, their exposure lies below the invisible line of €50 000. Based on these results, we were able to develop a framework describing the parties involved in determining the FX exposure of Fair Trade businesses.

The fact that the study was conducted during a time of a historically weak Euro might have biased our results towards participants feeling a stronger need for managing FX volatility compared to times of a stronger Euro. Hence, we suggest analysing the Fair Trade market in a different time window to ensure that the perceived need for hedging instruments is subsistent. Should results prove to be subsistent, we further recommend analysing the exact derivative volumes of the companies. Due to a rather low response rate and high variations in our survey, we were unable to make sufficient statements concerning precise figures. In addition, our research can be transferred to studying hedging needs of all micro and small companies, no matter whether Fair Trade or not. Should they also experience a need for hedging micro volumes the demand might become more attractive for financial institutions. In order to gain a more holistic view of the Fair Trade framework we propose to conduct further qualitative studies among Fair Trade associations as well as financial institutions; two important segments in our framework.

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Appendix 1 – Stage 1 Semi-Structured Interview Guide

The interview guide was translated. The original document had enough space for taking notes. The interview did usually not follow the exact order stated below, yet changed dynamically from respondent to respondent.

Introduction

- Presentation, Purpose to contribute to sustainable finance and help Fair Trade importers
- Ask for role of interview partner to see if he/she is decision maker

Topics covered

- **General data**
    - Products
    - Amount of executives and employees; management-owned
    - Membership in Associations and house bank
- **Operational data**
    - Revenues in Worldshops
    - Other retail channels and retail markets
    - Import countries and currencies
    - Order frequency and average/maximum amount
    - Pre-finance
- **Perception of FX exposure**
    - Influence of depreciation on business (include Likert scale: no influence, rather small influence, rather large influence, very large influence)
    - Other risks besides FX volatility
    - Importance of FX risk compared to other risks (include Likert scale: least significant, less significant, equally significant, most significant)
- **Decision making process and external advice**
- **FX volatility strategies**
    - In the past
    - Adaption within last month
    - Knowledge about products
    - Experiences if applicable
    - Interest in FX rate insurance
- **Personal background and follow up contact possibility**

Appendix 2 – Stage 1 Overview Sample

Sample size #19

Company code	CEO(s)	Owner-managed	Manager full-time	Amount Employee	Total Headcount	% - groups	Sector (F = Food, J = Jewelery, W = Art Wearing, L = Art Living)
1	1	yes	yes	0	1		J
2	1	yes	yes	0	1		JLW
3	1	yes	yes	0	1		F
4	1	yes	yes	0	1	36,8%	JLF
5	1	yes	no	0	1		w
6	1	yes	no	0	1		j
7	1	yes	yes	0	1		L
8	2	yes	no	0	2		JLW
9	1	yes	yes	2	3		JLW
10	2	yes	no	0	2	26,3%	L
11	2	yes	yes	0	2		J
12	2	yes	no	0	2		W
13	4	yes	yes	7	11		F
14	2	no	yes	16	18	21,1%	JLWF
15	3	no	yes	10	13		JLWF
16	2	yes	yes	15	17		L
17	1	no	yes	25	26		F
18	2	no	yes	50	52	15,8%	JLWF
19	2	yes	yes	120	122		JWF
Median					2		
Average					15		
Other results		yes = 15, no = 4	yes = 14, no = 5				

Appendix 3 – Stage 1 Purchase Patterns

Sample size #19

	Retail through	in %	# of yearly orders	Payment currency	Average order size (Euro)	Maximum order size (Euro)	Implied yearly order volume	Pre-finance	Pre-finance (% of order)	Time to delivery after first payment
	yes	5%	4	Euro	20.000,00	20.000,00		no	n.a.	n.a.
	yes	10%	3	USD	3.000,00	26.500,00		no	n.a.	n.a.
	no	10%	3	USD	n.a.	n.a.		other	n.a.	n.a.
	yes	20%	52	USD	48.125,00	48.125,00		other	n.a.	n.a.
	yes	30%	2	USD, LC	6.000,00	n.a.		no	n.a.	n.a.
	no	30%	12	USD, LC	5.000,00	n.a.		yes	100%	13
	yes	40%	3	LC	20.000,00	n.a.		yes	50%	10,83
	yes	45%	5,5	Euro, USD	150.000,00	200.000,00		no	n.a.	n.a.
	yes	60%	4,8	LC	2.750,00	n.a.		no	n.a.	n.a.
	yes	60%	2,5	USD	20.000,00	20.000,00		yes	50%	14
	yes	70%	52	USD	n.a.	n.a.		yes	50%	26
	yes	80%	5,5	LC, Euro	7.500,00	15.000,00		yes	75%	4
	yes	80%	2	Euro, USD	15.000,00	50.000,00		yes	50%	n.a.
	yes	90%	12	LC	7.500,00	n.a.		yes	n.a.	n.a.
	yes	n.a.	2	LC	10.000,00	10.000,00		yes	50%	15,16
	yes	n.a.	3,5	USD	3.750,00	5.000,00		no	n.a.	n.a.
	yes	n.a.	7,4	LC	4.500,00	4.500,00		yes	50%	3
	yes	n.a.	52	USD, LC	5.000,00	30.000,00		yes	50%	14
	yes	n.a.	7,4	USD, LC	13.125,00	52.500,00		yes	30%	13
Sum							4.196.500,00			
Median		42,5%	4,8						0,5	13,0
Average		45,0%	12,4						0,6	12,6
Other results	yes = 89,5%			only USD = 8; LC = 5, USD, Eur = 3, USD, LC = 3, Eur, LC = 1, Eur = 1				yes = 11, no = 6, other = 2		

*For reasons of confidentiality, company code is not shown and companies are in the order of increasing share of Worldshop retail in percentage (second column).

Appendix 4 –Stage 1 FX Perception, Management & Hedging Knowledge

Sample size #19

Company code	**Q1:** Impact on business	**Q2:** How important compared to other risks
	FX Risk Perception	**messured on Likert-Scala**
1	3	5
2	3	5
3	0	2
4	3	4
5	3	5
6	0	1
7	3	3
8	3	3
9	3	5
10	3	5
11	1	2
12	0	2
13	3	3
14	3	5
15	1	3
16	3	5
17	3	5
18	2	3
19	3	5
Scale	0 to 3	1 to 5
Median	3,0	4,0
Average	2,3	3,7

Other risks mentioned	**Count**
Order (quality, punctuality, guarantees)	6
Commodity prices	2
Sales	5
Credit/liquidity	2
Political	3
Competition	2
Self-motivation	1

Management of FX risk	
Selective price increase	6
Higher prices for new products	2
Price increase at events	1
Accept smaller margin/nothing	6
Adapt retail strategy	1

Change in FX management strategy	
No change	10
Prices up	7
Consolidation of product range	3
Optimization of processes	3

Informed about external solutions	**Count**
n.a.	4
No	13
Yes	2

Knowledge of financial instruments	
n.a.	4
No, but too small	3
No	2
Yes, but too small	1
Yes	2

Instruments mentioned	
Futures	1
Forwards	2
SWAP	2
Currency account	1

Interested in insurance instrument	
Possibly/Depends	6
Yes	4
No	1
No opinion/not thought about	4
n.a.	4

Appendix 5 –Stage 2 Interview Summaries

The interviews used a similar guide than in stage one. It was put more emphasis on the hedging experience and possible solutions to the problem.

Interview #1: Ralph Wüstefeld, Contigo GmbH (May 12, 2015)

Exchange rate risk has a huge influence on the company. Most of the invoices are paid in local currency or USD (48 - 49). Only 5-6 are being paid in Euro which has an impact on the producers and famers as they receive up to 30% less money due to the depreciation of the Euro. Usually a minimum of 50% is pre-financed when the order is place, sometimes even up to 100%. In general, there is a time span of 6-8 months between placing an order and receiving the delivery, sometimes additional delay for transportation issues. Difference to conventional SME importers where there is a 500% trade level from the price the producer or farmer demands to what the end consumer actually pays. On the contrary, in Fair Trade the trade level is at 100% plus value-added tax. This can be explained when looking at the supply chain. In conventional trade, there is generally a lot more intermediaries involved in bringing the product from the producer to the end consumer. In Fair Trade on the other hand, there is usually not more than one intermediary involved. The product is imported from the Fair Trade importer and distributed either directly via own shops, online shops or the World shops.

Current strategy when it comes to dealing with FX rate risk: Mr. Wüstefeld sees three options. The first is to negotiate with the producer and pay them less respective to the market fluctuations, the second is to reduce its own margins and thereby swallow the bitter pill themselves, and the third is to pass the exposure on to the end consumer by raising prices. Yet, for Contigo as Fair Trade importer, the first option is not viable as it would contradict the Fair Trade principles (Price Premium and Minimum Price etc.). Hence, for now Contigo swallows the bitter pill. However, the third option is likely to become real soon but depends on how the retailing industry in general reacts e.g. if prices for coffee and the like increase overall. Since like stated in the beginning, this issue does not only affect Fair Trade importers but all kinds of importers, e.g. companies importing products from low-wage countries in the same regions, the only difference is that conventional traders can easily pass market fluctuations on to their producers which is no option for Fair Trade importers. The Price Premium Fair Trade importers pay ranges between 30-100 percent and depends on the absolute price of the product. Products with a higher value such as ceramic artwork have a smaller Price Premium than lower value products such as candles and the like.

According to Mr. Wüstefeld, the currently experienced exposure to FX rate risk is unique in 40 years of Fair Trade. Ten years ago, Contigo opened up a foreign currency account in South African Rupie in order to circumvent high transaction fees resulting from converting Euros into Rupie and making an international money transfer to their main supplier in Africa (Commerzbank / Sparkasse). Transaction costs without a foreign currency account are up to 3% of the transaction volume. With a foreign currency account this fee can be reduced to 1% of the transaction volume. The money paid in to the foreign currency account allowed a cushion for six months but was used up in the beginning of the year. Concerning corporate and currency financing contigo is in contact with two more banks: shared interest (playing with the name) in the UK and pro credit in Frankfurt, Germany. However, derivatives do not belong to the banks expertise.

Derivatives or some kind of FX hedging to manage the exposure was not possible in the case of Contigo. In order to engage in either one of those possibilities, liquidity reserves are needed. In Contigos case, they were not high enough. The company did not receive any support or advice from either Commerzbank or Sparkasse, the banks they work closely together in general terms.

For now, Mr. Wüstefeld believes that they are out of the woods. They do not assume the Euro to depreciate again and are hopeful that the depreciation does not continue. Nevertheless, until there is a monetary union between the Euro and the Dollar, the FX exchange rate will always be up for speculation and this speculation will rest in the hands of and be subject to the experience of either the CEO or the financial department.

All Fair Trade importers are profit oriented businesses and therefore work exactly like conventional SMEs. There is no charity. Therefore the network of world shops will most likely not intervene on behalf of the importers and lend a helping hand. The world shops have large margins which they use to finance their own care projects. They see the Fair Trade importers as their suppliers and do not think all the way until the end of the supply chain. Communication should foster this kind of thinking, the importers are in contact with the network to work on this issue. All importers pay 2% of their revenue as a fee to the network in order to become and stay a certified supplier. Contigo uses their surplus to grow so that they can expand their network of producers and farmers and thereby improve more people’s lives. The relationship to the other big players in the industry is rather based on partnership than on competition. Besides distributing products via world shops, Contigo has their own stores. 85% of their products are craft works and only 15% are food. The other big players have a larger percentage of food products hence there is a bigger competition among Gepa and El puente as they offer similar products.

Interview #2: Martin Moritz, El Puente GmbH (May 12, 2015)

Generally, Mr. Moritz attests that the current depreciation has had a very large impact on his business. He makes clear, that all businesses basically face the same problem, regardless of whether Fair Trade or not. He points out, that the impact strongly depends on the type of product imported. There usually are higher margins on non-food articles. Companies having a high share of non-food products in their product range, are able to absorb the currency depreciation better than when importing food products, he believes. As in the food business, especially the coffee business, traditional retailers put pressure on the retail price, margins are quite low. Hence, the influence of currency volatility is higher. It is important to state, that the price elasticity of buyers of Fair Trade products can be expected to be lower than of other customers. They already are willing to accept a Price Premium and rather accept price increases. However, there will be a limit of what they will accept. Therefore, Mr. Moritz expects that price sensitivity of the consumers is more important than the prices set by the competitors.

Based on the position stated above, one could expect that there is more hedging within companies that import a higher share of food products. In Mr. Moritz´s opinion, this is not the case, as orders for food product often are made six or more month in advance. Fixing an exchange rate would then might lead to significant disadvantages compared to competitors, in case that the currency appreciates. This dilemma is very much linked to the controversy discussed in the literature review, whether or not hedging adds value to a company as it eliminates the benefits from the upside development of the underlying. In his opinion, especially the non-food articles which are sold and priced through a seasonal catalogue are applicable for financial instruments.

Mr. Moritz states that any kind of currency insurance measurement is speculative, even an intentional laissez-fair approach. He explains that his company has used various different hedging instruments such as foreign currency accounts, forward contracts, options, and other personalized derivatives from Commerzbank. Generally the volume they trade is between €50.000 and €100.000, sizes needed for the bank to start working.

Usually, there strategic mix to deal with their foreign exchange exposure is by hedging one third of the exposure with options, one third with forward contracts and buy the last third on the spot market. Option solutions are the most expensive once, yet give them the advantage to optionally decide whether to execute or not. Compared to forward contracts, options are usually too expensive regarding the upside advantages which do not justify the cost premium. Some of the financial instruments they used, contracts were signed agreements valid for one or two years. For this time certain exchange rates are fixed, hence those agreements are fairly inflexible. Due to this lack of flexibility, the long-term engagement in hedging creates an even higher risk.

Evaluating on the effectiveness, Mr. Moritz says that they have compared the results of their hedging strategy over the past four years with the results they would have had only buying at the spot market. The difference, he states, was not very large. Yet in the years of an appreciating Euro, on average they realized yearly profits attributed to the currency of about 1,5% - 2,5% of the import volume. This was achieved with a mix of hedging and buying at the spot market. With the current depreciation they face currency related loss of about 10% of the import volume.

Mr. Moritz considers the World Fair Trade Organization (WFTO) to carry responsibility when it comes to driving some kind of currency volatility solution. This institution has a lot of credibility among the market participants, which is important as there always is a little suspicion towards traditional financial institutions. Mr. Moritz wishes to have some kind of guidance by the WFTO, as they should recommend Fair Trade players how to cope with the currency volatility and when to engage in insurances. By that, he believes, the currency speculation gains or losses could be disregarded within the industry, as the whole market would react in a similar way. Hence, companies could focus on the core of their businesses. Mr. Moritz knows, that this is a very noble wish and quite hard to achieve. Nevertheless, he does see a responsibility within this organization. There is also a link to topics like loan default security and equity investments, which in the opinion of Mr. Moritz should also be taken into account by the WFTO and financial institutions. Banks should focus on these fields, while working together with an organization such as WFTO. There are banks such as Etica and Shared Interest which could be the financial partners.

Interview #3: Thomas Hoyer, dwp eG (May 15, 2015)

Mr. Hoyer is of the opinion that the currency volatility has an impact on the business. Mr. Hoyer has a different view on that, as products often are order long before they are delivered and hence sold, there is a need for some kind of insurance. On the other hand Mr. Hoyer has the same opinion when it comes to products sold via catalogues and fixed long term agreements, as those prices need to be reliable as they can only be adapted twice a year.

Especially when it comes to the import of commodities such as coffee and sugar, the need becomes more obvious. The competition in the market is much higher, as those products often are delivered to other manufactures which process the Fair Trade commodities in their production. In those cases, the company name and value does not matter and no Price Premium in the domestic market can be achieved. Another reason is given by the Fair Trade principles which according to them, at least 50% of the products should be pre-financed.

Dwp uses forward contracts do secure their larger orders. Their banking partner is Sparkasse and contracts are available from €50.000 onwards. According to Mr. Hoyer, those instruments are quite suitable, as the costs are quite low. However, smaller order starting at USD5.000 to USD30.000 cannot be backed with forward contracts. They investigated if options would also be a possible instrument for them, yet, due to their evaluation and values, they believe that options are much more speculative and do not meet with their requirements.

Mr. Hoyer could see possible solutions within financial institutions such as Oikocredit or GLS, yet doubt that they have the expertise at the moment. He also mentioned Shared Interest, that already work as a clearing company for the transactions with suppliers. The thoroughly focus on Fair Trade partners, as they require membership in the WFTO, which was also mentioned by Mr. Moritz. Within the Worldshops he does not see any potential, as in his opinion Worldshop margins actually are too low in many cases. Worldshops would need to raise fix costs for location and employees and get more profitable. This is the only way that the market further expands sustainably. This opinion might be biased, as dwp actually was founded by several Worldshops and today operates its own stores.

Appendix 6 – Stage 3 Survey Questions

In the following the questions of the online survey are translated into a condensed version.

Q1: Employee count

Q2: Revenues (net) 2014

Q3: Earnings before taxes 2014

Q4: Revenues not in € (2014)

Q5: Revenues through Worldshops

Q6: Import value and expenses paid in each foreign currency and in Euro

Q7: Amount of orders per year and per currency

Q8: Average order size per currency

Q9: Maximum order size per currency

Q10: Average down payment in percentage (if applicable)

Q11: Time between first down payment and last payment

Q12: Do you usually use credits to finance your orders?
Scale:
- No
- Yes, usually order usually financed from 1 to 24 percent with credit
- Yes, usually order usually financed from 25 to 49 percent with credit
- Yes, usually order usually financed from 50 to 74 percent with credit
- Yes, usually order usually financed from 75 to 100 percent with credit

Q13: Interested in currency volatility insurance – if yes, how much of order volume could it cost?

Q14: Additional information, comments, wishes, et cetera

Appendix 7 – Stage 3 Survey Results

Sample size is #13

Answer to	Q2	Q4	Q5	Q6	Q7
	Revenues 2014	Revenue denominated not in €	Revenue through Worldshops	Total Import (€)	Amount of orders
Sum	29.581.316,00			15.422.545,80	
Median	2.275.485,85	2%	54%	1.186.349,68	26,1
Average	700.000,00	1%	60%	300.000,00	12,0

Answer to	Q8	Q9	Q10	Q11	Q12	Q13
	Order size average	Order size maximum	Pre-finance	Weeks between first and final payment	Credit financing	Insurance
Sum						
Median	29.290,15	60.169,59	55%	12,98		
Average	19.689,75	61.257,00	50%	13,00		
					0% = 5	
					1%-24%= 2	
					25-49% = 2	Yes = 7
					50%-74%=3	Maybe = 3
Frequency					75%-100%=1	No = 3

*due to confidentially, the results are only presented as grouped results

**Q1 - employee count was not always mentioned, therefore results are not valid and not presented

***Q3 - EBT not always mentioned and often states to be zero, which is questionable if this is a accurate response.

Appendix 8 – Stage 4 Interview

The interview guide was translated. The original document had enough space for taking notes. The interview did usually not follow the exact order stated below, yet changed dynamically from respondent to respondent.

Introduction

- Presentation; purpose to contribute to sustainable finance and help Fair Trade importers.

Covered Topics

- **Understanding business model of Oikocredit**
  - Activities of Oikocredit
  - Lending requirements in relation to organic, Fair Trade, sustainability … labels.
  - Customers and investors
- **Knowledge about situation of Fair Trade importers**
  - Characteristics of exposure
  - Confirmation of lack of instruments
- **Solution approach**
  - Ideas of how importers could deal with their exposure
  - Relation between microfinance, Fair Trade and hedging
  - Feasability of Chinese model (OneTouch) → explain how they work

Summary of Main Points

The summary was revised and approved for publication by Mr. Florian Grohs.

To the knowledge of Mr. Grohs, there are no financial institutions or products in the market that focus on the special needs of Fair Trade importers. In his opinion, the main reason for that are the small monetary importing volumes of those companies. He compares hedging instruments with credits, when he says that the setup costs of a financial product is almost the same, not important if the contract size is large or small. Hence, it might not be interesting for financial institutions to enter into this niche business. Being asked what he thinks about the idea of the Chinese company OneTouch (section 2.3), Dr. Grohs states that this could be an interesting approach to solve the dilemma. However, in his opinion such as solution should not only be aimed at Fair Trade importers, but also be accessible for other small importers with similar needs. By that, the critical factors such as total volume might be able to be solved and the instrument could be a success.