

HOW FLUCTUATING CURRENCY RATES AFFECT TRAVEL INDUSTRY

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Introduction. For most major economies, the floating exchange rate system is the norm, meaning the currency's value is allowed to fluctuate in accordance with the foreign-exchange market. Currency rates are influenced by numerous fundamental and technical factors that are usually in a state of perpetual flux. These include interest rate differentials, economic performance, supply and demand of the two currencies, and inflation. If you run a travel business, you'll directly be impacted by fluctuating currency rates. The relative strength, or lack thereof, of the dollar against other major currencies will dictate your business traffic.

Foreign exchange earnings from tourism are the receipts of non-domestic currency earned by selling goods and services to foreign tourists. It is useful to classify earnings into hard, i.e. convertible currencies and soft, nonconvertible currencies. Hard currencies such as the US dollar, the deutschmark, the yen and the Swiss franc are freely convertible, internationally acceptable and can be exchanged without restriction. As these currencies are issued by the most economically advanced countries they are most used in international trade. On the other hand, soft currencies are those which are not freely convertible, and have severe limitations imposed on exchange outside their country of issue, such as the Indian rupee or the Thai baht. However, there is a discernible trend for more countries to make their currencies freely convertible. Although this trend will make more currencies available for trading, it does not mean that traders will want to use or hold these currencies. The more unstable the economic situation in a country, the greater the prospect of currency fluctuation and therefore losses on currency holdings or on trading contracts. The determination of nominal and real exchange rates is a complex subject. A nominal exchange rate is that which is quoted for one particular currency against another at a particular date. This is the rate which a tourist receives when buying and exchanging foreign currency. A real exchange rate is the currency dealers' view of the 'true' value of any currency, i.e. what its 'true' or 'real' purchasing power is in the international market relative to other major trading currencies. The real exchange rate is important for future transactions, with many forward contracts having different rates quoted for buying specified currencies one, two and three months ahead of delivery. For tour operators who have to pay future accounts in foreign currencies, the forward exchange market is important as a means of hedging against major currency fluctuations and limiting potential losses through currency depreciation. Most governments in developing countries encourage international tourism because such tourists usually travel from hard currency countries.

Conclusion. The travel and tourism sector is, by nature, an international business. Although your company will conduct transactions using the dollar, payments from overseas will involve foreign currencies, the values of which can fluctuate sharply or unexpectedly through the currency futures markets, exposing your business to economic uncertainties and making it difficult to protect your projected profit margins. Furthermore, vacation time for most people tends to be seasonal, taken in conjunction with school closings and holidays. Unfavorable exchange rates covering these months can lead to changes in travel patterns and vacation scheduling, leading to unpredictable travel seasons for your company.

References:

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