



## THE ROLE OF STRUCTURING DERIVATIVE TRANSACTIONS OF COMMERCIAL BANKS BASED ON ISDA (INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION) STANDARDS IN MANAGING CURRENCY RISKS

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**Abstract:** This article analyzes the importance of structuring foreign exchange derivative transactions in commercial banks based on the standard documentation of ISDA. The study examines the advantages of ISDA-based agreements. The findings show that netting and collateral mechanisms applied under ISDA reduce counterparty risk and enhance hedging effectiveness. In the context of Uzbekistan, the opportunities for developing derivative operations are assessed, and the necessity of implementing ISDA standards is substantiated.

**Keywords:** exchange rate risk, derivative transactions, ISDA standards, hedging, netting, collateral, counterparty risk

### Introduction:

The volatility of exchange rates is making the management of currency risks an increasingly important task for commercial banks. The growth of open currency positions can negatively affect the financial stability of banks. Under such conditions, the use of derivative instruments serves as a modern and effective tool for risk mitigation. However, the effectiveness of derivative transactions also depends on their legal framework.

In international practice, derivative transactions are structured based on ISDA (International Swaps and Derivatives Association) standard documentation. These standards reduce counterparty risk through netting (the mutual offsetting of multiple financial obligations between two parties) and collateral mechanisms (assets or



funds pledged by parties to reduce counterparty risk in derivative transactions), while also enhancing the effectiveness of hedging strategies.

In the context of Uzbekistan, there is a growing need to develop derivative operations. Therefore, the purpose of this article is to analyze the importance of transactions structured under ISDA standards and to justify the necessity of their implementation in practice.

### **Literature Review:**

Issues related to the management of currency risks have been extensively studied by both foreign and domestic scholars. At the international level, studies and standards developed by the Bank for International Settlements (BIS), International Monetary Fund (IMF), and the Basel Committee on Banking Supervision outline the institutional foundations of bank risk management. Within the frameworks of Basel II and Basel III, currency risks are considered as a component of market risks, and mechanisms for covering them through capital requirements are established.

In addition, the scientific literature provides extensive coverage of the nature of currency risks, their impact on banking activities, and various management mechanisms. In particular, the works of Frederic S. Mishkin, John C. Hull, V.A. Kazakov, and S. Walters elaborate on the theoretical foundations of currency risks. At the same time, local scholars such as T.I. Bobakulov, U.A. Abdullayev, and J.X. Ataniyazov analyze currency risks and international financial relations from the perspective of the banking system.

Although these scientific sources cover the theoretical aspects of currency risks and approaches to the use of derivative instruments, the issue of systematizing them in the context of organizing derivative transactions in commercial banks based on ISDA standard documentation—adapted to the conditions of Uzbekistan’s banking system and developing practical mechanisms has not been sufficiently studied. Therefore, research aimed at enhancing the effectiveness of currency risk management through the organization of derivative operations based on ISDA standards remains highly relevant. At the same time, the adaptation of international experience to the national banking system and the formation of a unified legal and



institutional framework for derivative transactions have not yet been adequately substantiated from a scientific perspective.

### **Research Methodology:**

This study employed systematic and logical analysis, comparative analysis, and the generalization of statistical data. The experience of structuring derivative transactions based on ISDA (International Swaps and Derivatives Association) standard documentation in both foreign and domestic banking practices was examined. During the research process, the effectiveness of derivative transactions structured with and without ISDA standards was compared, and the impact of netting and collateral mechanisms on counterparty risk was analyzed. In addition, the impact of derivative operations on bank balance sheets under conditions of exchange rate fluctuations was modeled, and the feasibility of implementing ISDA standards in the context of Uzbekistan's banking system was assessed.

### **Analysis and Results:**

The findings of the study indicate that the level of organizing derivative operations in commercial banks based on ISDA (International Swaps and Derivatives Association) standards varies significantly across countries, and this directly affects the effectiveness of currency risk management. In developed financial markets, the majority of derivative transactions are structured under the International Swaps and Derivatives Association Master Agreement, which ensures the full functioning of netting and collateral mechanisms. As a result, counterparty risk is minimized, and the effectiveness of hedging operations is significantly enhanced.

In practice, ISDA is primarily applied in transactions involving international counterparties. The main reasons for this include:

- the need for a unified legal framework;
- foreign banks' unwillingness to enter into transactions without ISDA documentation;



- the international recognition of netting and collateral mechanisms.

In contrast, in the banking system of Uzbekistan, derivative operations are still at a developmental stage, and the application of ISDA standards is not yet widespread. Banks are mostly limited to simple foreign exchange transactions, and in many cases, simplified local contracts are used. This creates constraints in effective risk management.

The analysis also shows that ISDA standards are predominantly used in transactions with international counterparties due to the need for a unified legal platform across different jurisdictions. However, the insufficient implementation of these standards in the domestic market leads to a persistently high level of counterparty risk and limits the full effectiveness of hedging mechanisms. Therefore, it is necessary to expand the application of ISDA standards not only in international operations but also within the national financial market.

Overall, the research results demonstrate that the effectiveness of derivative operations depends more on their legal and institutional frameworks than on the execution mechanisms themselves. The implementation of ISDA standards can enhance the currency risk management systems of commercial banks, strengthen financial stability, and deepen integration into international financial markets.

### **Conclusion and Recommendations:**

The findings of the study demonstrate that structuring currency derivative transactions in commercial banks based on ISDA (International Swaps and Derivatives Association) standards enhances the effectiveness of currency risk management. In current practice, the matching policy alone is insufficient, highlighting the need to further develop derivative and legal mechanisms. Therefore, it is advisable to gradually implement ISDA standards, legally strengthen netting and collateral mechanisms in derivative transactions, improve the qualifications of bank personnel, and establish a unified legal framework for derivative operations. These measures will contribute to strengthening the stability of commercial banks and enhancing their integration into international financial markets.



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