



Name :

Roll No. :

Invigilator's Signature :

CS/MBA/SEM-4 (FT) & 6 (PT) /FM-405/2012

2012

INTERNATIONAL FINANCE

Time Allotted : 3 Hours

Full Marks : 70

The figures in the margin indicate full marks.

Candidates are required to give their answers in their own words as far as practicable.

GROUP – A

(Multiple Choice Type Questions)

1. Choose the correct alternatives for any *ten* of the following :

10 × 1 = 10

- i) If forward rate > spot rate, then
 - a) it is quoted at premium
 - b) it is quoted at discount
 - c) cannot be said, further information required.
- ii) The price of a currency option is also called the option
 - a) discount
 - b) premium
 - c) return
 - d) face value.



- iii) Suppose the current spot rate for the Euro is \$ 0.7427. A call option with an exercise price of \$ 0.7550 is said to be
- a) in the money
 - b) out of the money
 - c) at the money
 - d) none of these.
- iv) An option which gives the buyer a right to buy foreign currency is a
- a) call option
 - b) put option
 - c) none of these
- v) The forward market is especially well suited to offer hedging protection against
- a) translation risk exposure
 - b) transaction risk exposure
 - c) political risk exposure
 - d) taxation.
- vi) Fundamental disequilibrium in the Bretton-Woods system means
- a) consistent balance of payments deficit
 - b) consistent devaluation
 - c) rising inflation rate in the country
 - d) none of these.
- vii) International trade is based on the principle of
- a) law of diminishing return
 - b) law of comparative costs
 - c) PPP theory
 - d) none of these.



- viii) Floating rate is determined by
- a) the government of the country
 - b) on the basis of value of some other currency
 - c) by the interaction of demand and supply of the currency
 - d) none of these.
- ix) Which of the following is not an example of internal hedging ?
- a) Lead
 - b) Lag
 - c) Money market
 - d) Re invoicing centre.
- x) The Bretton-Woods System fell apart because
- a) of the oil crisis
 - b) USA had a large deficit
 - c) monetary policy of USA
 - d) none of these.
- xi) Real operating exposure takes into account
- a) only changes in cash flow
 - b) changes in price level
 - c) changes in prices & exchange rate
 - d) none of these.
- xii) You purchased a one month forward dollar from a bank in New York on April 09 (Friday) of a year. The one month forward settlement date on that same year is
- a) May, 10
 - b) May, 11
 - c) May, 12
 - d) May, 13.



GROUP – B

(Short Answer Type Questions)

Answer any *three* of the following. $3 \times 5 = 15$

2. What do you mean by Cross-Rate ? Explain it with examples.
3. What do you mean by Inter-Bank Rate and Merchant Rate ?
4. For US \$ in the inter-bank market, the bid rate is Rs. 45.4550 and an exchange margin of 0.125%. Find out TT buying rate. For US \$ in the inter-bank market, the ask rate is Rs. 45.4650 and an exchange margin of 0.125%. Find out TT selling rate.
5. Differentiate between Call Option and Put Option and Forward and Future market in the context of International Finance.
6. Companies like Good Credit & Poor Credit have been offered the following rates per annum on a \$ 10 million five year loan :

<i>Cost of Funds</i>	<i>Fixed Rate</i>	<i>Floating Rate</i>
Good Credit	6%	Libor
Poor Credit	10%	Libor + 1%

Good Credit Company requires a floating rate loan whereas Poor Credit Company requires a fixed rate loan. How can the two companies enter into a coupon swap arrangement in which each benefits equally ?



7. The following are the quotes available at the market :

Spot \$/€	0.8775/0.8777
3 months forward	0.8760/0.8767
3 months interest rates are :	\$ 2.25/2.5%p.a.
3 months interest rates are :	€ 3.50/3.75% p.a.

Verify whether there is any scope for covered interest arbitrage. Estimate the amount of arbitrage profit say for borrowing \$ 100.

GROUP – C

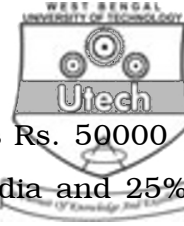
(Long Answer Type Questions)

Answer any *three* of the following. $3 \times 15 = 45$

8. An Indian company is appraising a project to be set up by its subsidiary in the USA. The initial project cost is US \$ 125000 which will add Rs. 30 lakhs to the Indian company's borrowing capacity over 3 years. A sum of Rs. 40 lakhs of the initial investment is met by the Indian parent and the remaining US \$ 25000 is borrowed at 10% in the USA. The project has a life of 3 years.

The net operating cash flow is \$50000, \$60000 and \$72000 in the 1st, 2nd and 3rd years respectively. The salvage value is expected to be \$10000.

The spot exchange rate is Rs. 50/\$. Anticipated annual rates of inflation are 8% in rupees and 5% in dollars. Depreciation allowance is Rs. 15 lakhs per year for three years. Expected



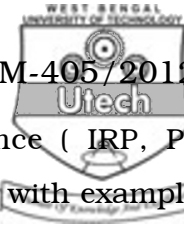
tax saving from intra-firm transfer pricing is Rs. 50000 per year in all the years. Tax rate is 30% in India and 25% in USA. Cost of equity is 20%. Discount rate for depreciation/tax saving on interest deduction is 12%. Discount rate relating to loan repayment is 20% and on tax saving due to transfer pricing is 25%. Should the project be accepted ? Use the Adjusted Present Value (APV) method for your evaluation.

9. a) An Indian exporter has an ongoing order from USA for 2000 pieces per month @ \$100. To execute the order, the exporter has to import ¥ 6000 worth of material per piece. Labour costs are Rs. 350/- per piece while the other variable overhead adds up to Rs. 700/piece. The exchange rates are currently Rs. 35/\$ & ¥120/\$. Assuming the order will be executed after 3 months and payment is obtained immediately on shipment of goods, calculate the loss/gain due to this transaction if the exchange rates change to Rs. 36/\$ & ¥110/\$.
- b) Cropdex is an Indian firm exporting handicrafts to America. It is considering the use of money market or forward market to cover a receivable of \$50,000, expected to be realized 3 months hence. Cropdex has the following information :

Rs/\$	Exchange Rate	Interest Rate
Spot	43.65/44.0	3-m Rs. : 9%p.a.
3-m forward	43.95/44.4	3-m \$: 6%p.a.

Which option is better ?

$$2 \times 7 \frac{1}{2} = 15$$



10. Describe in detail the Four-way Equivalence (IRP, PPP, Fisher Effect and Expectation Theory) Model with examples.
11. Explain with example how a company can use the various external hedging strategies, *i.e.* money market hedge, option market hedge & future market hedge to manage translation exposure.
12. Write short notes on any *three* of the following :
 - a) BOP
 - b) IMF
 - c) EMU
 - d) EURO
 - e) MNC
 - f) BOT.

