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08MBAFM426/IB466/BF476

Fourth Semester MBA Degree Examination, December 2010
International Financial Management

Time: 3 hrs. Max. Marks:100

Note: 1. *Answer any FOUR full questions, from Q1 to 7.*
2. *Q.No. 8 is compulsory.*

Important Note : 1. On completing your answers, compulsorily draw diagonal cross lines on the remaining blank pages.
2. Any revealing of identification, appeal to evaluator and /or equations written eg, 42+8 = 50, will be treated as malpractice.

1 a. What is BOP? (03 Marks)
b. Why does disequilibrium in BOP exists? What is J curve effect? (07 Marks)
c. Given the following data , Show how arbitrage possibility exists for 1000 units of currency.
Spot rate F.Fr 6.00 = $ 1.6
6 month forward rate F Fr 6.002 = $ 1
Interest rate F Fr = 8% p.a US $ = 5 %. (10 Marks)

2 a. How is international financial management different from domestic financial management? (03 Marks)
b. If the direct quote for dollar is Rs 35 in Delhi and transaction costs are 0.5%, what are the minimum and maximum possible direct quotes for the rupee in New York? (07 Marks)
c. Explain role of IBRD. (10 Marks)

3 a. What is SWIFT mechanism? (03 Marks)
b. What are the factors affecting for exchange rate? (07 Marks)
c. Two companies have following borrowing rate applicable to them.

Company	Fixed market	Floating market
X	T	LIBOR + 0.2
Y	T + 1.5	LIBOR + 0.75

Company X plans to borrow floating rate and Y at fixed rate. Bank acts as intermediatory, and two companies sign a contract. X will pay to bank LIBOR + 0.25 and Y will pay to it T + 0.70. Bank has 0.30% profit. Design swap and show. (10 Marks)

4 a. What is difference between risk and exposure with respect to foreign exchange management? (03 Marks)
b. What is translation exposure? Explain the translation methods. (07 Marks)
c. How do you measure currency exposure? Find the currency exposure coefficient βeta for the following data :

State	Probability	Q'	S	Q
1	⅓	£ 980	$ 1.4	$ 1372
2	⅓	£ 1000	$ 1.5	$ 1500
3	⅓	£ 1070	$ 1.6	$ 1712

Where Q' = pound price of asset ; S = exchange rate in dollar ; Q = P'.s (10 Marks)

5 a. What is the difference between FDI and F I I? (03 Marks)
b. What are the strategies a company can use to manage its operating exposure? (07 Marks)

c. From the following, show how opportunity of triangular arbitrage exists, if you have $ 10,000. [MYR = Ringit of Mynmar] **(10 Marks)**

Quote	Bid rate	Ask rate
Value of £ in USD	$ 1.600	$ 1.610
Value of MYR in USD	$ 0.200	$ 0.201
Value of £ in MYR	MYR 8.10	MYR 8.20

6 a. What is forward rate agreement? **(03 Marks)**

b. What is political risk? How MNCs hedge political risk? Explain. **(07 Marks)**

c. An Indian importer has to pay £ 2 million to an U.K firm in 4 months time. To guard against possible rise of pound, he buys an option by paying 2% premium on current price. Spot rate is Rs 77.50 per pound. Strike price is Rs 78.20/pound. What will be his action if the pound rises to Rs 80 and if it falls to Rs 76? **(10 Marks)**

7 a. What is multilateral netting? **(04 Marks)**

b. Explain i) ECB ii) ADR iii) GDR. **(06 Marks)**

c. An Indian importer imports goods worth $ 1000 from USA and has to make the payment after 90 days. Spot exchange rate is Rs 40 / $ and 90 day forward rate is Rs 39.50 / $. Interest rate on borrowing in India and US is 6% p.a, and on the deposit the rate is 5% p.a. Spot rate on 90th day is Rs 39.80 / $. Evaluate following alternatives i) No hedge ii) Hedge using forward market iii) Hedge in money market iv) 90 day call option with strike price of Rs 39.60 and premium of Rs 0.05 per dollar. **(10 Marks)**

8 **CASE STUDY** :

A US MNC is planning to set up a subsidiary in India (where hitherto it was exporting) in view of the rising demand for its products and competition from others. The initial cost of the project is estimated to be $ 400 million. Working capital requirement is estimated to be $ 50 million. If follows straight line method depreciation.

At present it is exporting 2 million units every year at a unit price of $ 80. Variable cost per unit is $ 40. The finance manager of the firm has following estimates for the project:

i) Variable cost of production → $ 20 per unit.
ii) Additional fixed cost per annum → $ 30 million.
iii) Capacity of plant in India to produce and sell → 4 million units.
iv) Life of the plant with no salvage value → 5 years.
v) Firm's existing working capital investment in the production and sale of 2 million units → $ 10 million

The manager mentions that the exports will fall to 1.5 million units, in case the firm does not setup subsidiary in India. Tax rate is 35%, Required rate of return is 12%. Assume no change in exchange rate and no with holding tax. Advise the MNC. **(20 Marks)**

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