2008

M B A

4th Semester Examination

INTERNATIONAL FINANCIAL MANAGEMENT

PAPER—F402 & M406

Full Marks : 100

Time : 3 Hours

The figures in the right-hand margin indicate full marks.

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

Illustrate the answers wherever necessary.

Write the answers to Questions of each Half in separate books.

First Half

(Marks : 50)

1. Answer any *four* of the following questions : 5×4

(a) What is a Multinational Corporation ? How does it differ from Foreign Direct Investment ? What benefits are derived by an MNC through its operations as such ?

(b) What do you mean by an 'Open-bid, Double-auction market' ? Also explain the terms 'limit order' and 'inside spread' as these are used in Foreign Exchange Markets.

(c) From the following exchange rates as quoted by Bank you have to compute the direct quote for Pound (Sterling) in India :

Sterling : US $ 2.0000 — 97
Rupee : US $ 0.0213 — 56

(d) Given the following :

Exchange rates : Can $ 0.665/DM (Spot)
Can $ 0.0670/DM (3 months forward)

Interest rates (3 months duration) : DM 7% p.a.
Can $ 9% p.a.

Calculate the possible arbitrage gain percentage. Clearly indicate the steps.

(e) What do you mean by Swaps ? What are the different types of Swaps ? Who can use Swap ?

(f) What is a currency futures ? What are its features ?

(g) Explain quotation conventions applicable for currency options.

2. Answer any *two* of the following : 10×2

(a) (i) What do you mean by Effective Exchange Rate ?

(ii) Show that in the absence of transaction cost Direct exchange rate must be equal to implicit Indirect exchange rate.

(b) Graphically represent the Pay off Profiles on Currency Futures. Use imaginary figures to demonstrate it.

(c) Explain the relationships between Strike Price and Spot Exchange rate in currency options.

[*Internal Assessment : 10 marks*]

Second Half

(Marks : 50)

3. Answer any *four* questions : 5×4

(a) Describe in brief the purposes of lending by international banks.

(b) The following information is furnished by a US parent MNC :

Principal amount of debt –	Rs. 1 billion
Rate of interest –	16% per annum
Flotation cost of debt –	Rs. 60 million

Interest is to be paid at the end of each year and the principal sum borrowed is to be repaid in a lumpsum at the end of the 5th year. Subsidiary is subject to no taxes in India.

The rupee is expected to depreciate in relation to the US dollar at the rate of 3% each year for 5 years. Determine the effective cost of debt to the US parent MNC. Assume the current exchange rate of US $ to Indian rupee to be 36.

(c) State the peculiarities in the management of working capital in an international firm.

(d) What additional factors deserve consideration in multinational capital budgeting that are not normally relevant for a purely domestic project ?

(e) Describe in brief the steps involved in cash management of multinational firm.

(f) Write a note on Financial Swap.

4. Answer any *two* questions : 10×2

(a) 'Fast growth of international trade and investment has motivated banks to operate abroad'. Elucidate the statement in the context of functions of international banks.

(b) A hypothetical MNC has to choose between the following two options :

(i) Continue to export 2,00,000 units of a product annually at a unit price of US $ 80; its variable cost per unit is $ 45.

(ii) Install a manufacturing unit to produce 5,00,000 units in country X — the destination for exports.

Setting up of the manufacturing plant will involve an investment outlay of $ 50 million. The plant is expected to have a useful life of 5 years with $ 10 million salvage value. The MNC follows the straight line method of depreciation. To support additional level of activity, investment will require additional working capital of $ 5 million.

Since the costs of production are lower in the country X, the variable cost of production and sales would be lower, i.e., $ 20 per unit. Additional fixed costs per annum are estimated at $ 2 million. Further, the forecasted selling price is lower, i.e. $ 70 per unit to sell 5,00,000 units. The MNC is subjected to 40 per cent tax rate and its cost of capital is 15 per cent.

Assuming that there will be no variation in the exchange rate between the two countries and all profit can be repatriated, advice the MNC regarding financial viability of the proposal.

(c) Describe the methods for transferring cash from one unit to another in the case of multinational enterprise.

[*Internal Assessment : 10 marks*]
