

2014

M B A

4th Semester Examination

Subject : INTERNATIONAL FINANCIAL MANAGEMENT

(Specialization : Financial Management)

PAPER—F-402

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 questions : 4×5

- (a) What are the different types of foreign exchange market? Who are the common participants in those markets?

(Turn Over)

- (b) Distinguish between Portfolio Investment and Foreign Direct Investment. Which type of investment a Multi-national Corporation may be interested in ?
- (c) What is Cross exchange rate ? How can you determine cross exchange rate in spot market and in forward market. Give example.
- (d) From the following data find out the possibilities of arbitrage gain, if any :
- Spot Exchange Rate : US\$ 1.5178/£
- 6-months Forward Exchange Rate : US\$ 1.5175/£
- Annualised interest rates (6 month) : US\$: 3.5%,
British £ : 7%.
- (e) Make distinctions among arbitrage, hedging, and speculation.
- (f) Distinguish between the main features of a forward exchange contract and a futures exchange contract.

2. Answer any *two* questions :

2×10

- (a) (i) Mr. Joyram buys a French franc put option (contract size is FF 2,50,000) at a premium of \$0.01 per franc. If the exercise price is \$0.21, compute Joyram's profit or loss on the put option when the spot price of franc at the date of expiration is :

(x) \$0.215, (y) \$0.208.

- (ii) Distinguish between the terms open interest and trading volume in relation to Options contract. Explain how margins protect investors against the possibility of default.
- (b) (i) Why are margins maintained with respect to a currency futures contract but not with currency forward contracts?
- (ii) With the help of an example draw the Payoff Profile for the Writer of a Put Option. 5+5
- (c) (i) A trader buys a Swiss franc futures contract (contract size is SFr 1,25,000) at a price of \$0.83. If the spot rate for the Swiss franc at the date of settlement is SFr 1 = \$ 0.8250, what is the trader's gain or loss on this contract?
- (ii) Give a brief overview of the structure of a spot foreign exchange market. 5+5

[Internal Assessment : 10 Marks]

(Second Half)**(Marks : 50)**

3. Answer any *four* questions : 4×5
- (a) What kind of risk is borne by a swap dealer?
 - (b) Explain in brief, different forms of transfer of funds of multinational enterprise.
 - (c) Describe the concept of leads and lags.
 - (d) Distinguish between 'Payback Period', and 'Internal Rate of Return'.
 - (e) Describe the factors leading to the growth of international banking.
 - (f) From the following facts, determine the effective cost of debt to the US parent MNC :
 - (i) Principal amount of debt Rs. 1 billion.
 - (ii) Rate of interest 16%
 - (iii) Floatation cost of debt Rs. 60 million.
 - (iv) Principal sum borrowed is to be repaid in lump sum at the end of the 5th year and Interest is to be paid at the end of each year.
 - (v) The rupee is expected to depreciate in relation to the US dollar at the rate of 3% each year for 5 years.
 - (vi) Subsidiary is subject to no taxes in India.
- Assume the current exchange rate of US \$ to Indian rupee to be 56.

4. Answer any *two* questions :

2×10

(a) (i) A has floating rate funds on which it is paying LIBOR 0.3 percent. But it could borrow fixed rate debt at 10.50 percent to be computed half-yearly. B has fixed rate debt on which it is paying 9.50 percent. But it could borrow floating-rate funds at 6 months LIBOR flat. Can the two counter parties go for interest-rate swap? If so, indicate the gains accruing to them including swap dealer.

(ii) Total demand for raw materials is 100 tonnes during time T. The carrying cost is \$ 10 per tonne of stock during time T and the order cost is \$ 1 per order. Will you call it stockpiling if the firm makes an order for 6 tonnes of raw material?

6+4

(b) As US multinational is faced with a problem to choose between the following two options :

(i) continue to export every year 20,000 units of a product of a unit price of US \$ 80; its variable cost per unit is \$ 45.

(ii) installation of a manufacturing unit to produce 5,00,000 units in the 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 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 subjected to 40 per cent tax rate and its cost of capital is 15 percent.

Assuming that the MNC has a restriction of non-remission of funds till the termination of project. Further, assume that the intermediate CFAT can be invested locally at 10% compound interest. Advise the MNC regarding financial viability of the proposal in the scenario of restrictions on fund remission.

- (c) (i) Why does an international firm hold cash ?
(ii) Describe the different ways of internationalisation of banks.

[Internal Assessment : 10 Marks]
