MACHAKOS UNIVERSITY

University Examinations for 2020/2021 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BUSINESS ADMINISTRATION

SECOND YEAR FIRST SEMESTER EXAMINATION FOR

MASTER OF BUSINESS ADMINISTRATION

BAC 820: INTERNATIONAL FINANCE

DATE: 4/3/2021 **TIME: 9.00-12.00 PM**

INSTRUCTIONS:

1. Answer QUESTION ONE and any other THREE questions
2. All workings where necessary must be shown
3. Be clear, neat and orderly in your presentation

QUESTION ONE (25 MARKS)

a) Discuss a free floating exchange rate system, may be good for developing countries (5 marks)

b) Compare and contrast a futures contract and a forward rate contract (9 marks)

c) Discuss the basic translation hedging strategy that a firm may put in place to hedge against translation exposure (6 marks)

d) During the past two decades there has been more internalization of capital Markets around the world. Discuss the factors that have led to this phenomena (5 marks)

QUESTION TWO (15 MARKS)

a) X Ltd. an exporting firm expects to receive substantial payments in sterling pounds and US dollars, Based on 2 days' spot rates the KSh. Value of funds to be received is estimated at Ksh. 600,000 for sterling and Ksh. 400,000 for USD. Based on the data for the last 20 months it is estimated that the standard deviation of monthly percentage changes is 7% for sterling pound and 8% for USD and correlation coefficient of 0.5 between sterling pound and USD. What is the standard deviation of portfolio?

(7 marks)

b) What is the price of a European call option on the USD with an exercise price of Sh.60 and has a life of 6 months to maturity if the treasury bill rate is 5% and d on the USD exchange rate in the last 6 months is10%? The spot e exchange rate is USD = KSh.65. (8 marks)

QUESTION THREE (15 MARKS)

a) Consider a Danish based company that exports consumer goods to several countries. The company has contracted to supply 10 million USD worth of goods to the US and expect to receive payment in three months' time in US dollars. The global Financial risk manager working in this company believes that the dollar will appreciate against the Danish Krona over this three-month period. The company considers three alternative strategies; leave the future cash flow unhedged, enter into a forward contract or an option contract. Contrast these three possibilities and possible results. (7 marks)

b) Tom Wanyonyi is the financial analyst for Spec Inc., which is a Canadian subsidiary based in the Philippines. The company has a number of subsidiaries spread across South East Asia. Discuss the inputs that Tom requires for a successful capital budgeting for the multinational company that he works for. (8 marks)

QUESTION FOUR (15 MARKS)

a) Explain corporate motives for forecasting exchange rates. (3 marks)

b) Explain the fundamental technique for forecasting exchange rates and the limitations of using a fundamental technique to forecast exchange rates? (5 marks)

c) Explain the market-based technique for forecasting exchange rates. What is the rationale for using market-based forecasts? If the euro appreciates substantially against the dollar during a specific period, would market-based forecasts have overestimated or underestimated the realized values over this period? Explain. (7 marks)

QUESTION FIVE (15 MARKS)

a) Briefly explain any five problems faced by international financial managers of contemporary multi-national corporations in the global world (8 marks)

b) With the aid of examples, explain the following theories of international business

i. The theory of comparative advantage (3 marks)

ii. The Imperfects markets theory (2 marks)

iii. The Product life cycle theory (2 marks)