[This question paper contains 2 printed pages.]

Sr. No. of Question Paper : 2557 **Roll No............**

Unique Paper Code : 101504

Name of the Course : BFIA 2013

Name of the Paper : International Finance

Semester : V

Duration : 3 Hours

Maximum Marks : 75

Instructions for Candidates

1. Write your Roll No. on the top immediately on receipt of this question paper.
2. Answer **all** questions.
3. Marks are indicated against the question.

1. Explain in brief (any **six**) :

   (a) Capital account
   (b) Monetary Movement
   (c) Basis risk
   (d) TT buying rate
   (e) CTA
   (f) GDR
   (g) Transaction exposure
   (h) Temporal Method

   (6×2.5=15)

2. (a) The following quotations are available in a market :

   USD/INR = 61.2250/60

   GBP/USD = 1.1590/96

   EUR/USD = 1.3120/26

   EUR/INR = 80.4550/60

   Calculate all possible arbitrage opportunities. Also write a short note on synthetic rate. (8+2=10)

P.T.O.

(b) "Forward rate is an unbiased predictor of future spot rate." Do you agree with the statement ? Justify. (5)

3. Critically evaluate different methods of exchange rate forecasting. (15)

4. What do you mean by multilateral netting ? Show the possible netting in the following case :

Country I to Country B: \$250m; Country I to Country C: \$50m

Country I to Country D: \$250m; Country B to Country I: \$300m

Country B to Country C: \$150m; Country B to Country D: \$300m

Country C to Country I: \$270m; Country C to Country B: \$230m

Country C to Country D: \$400m; Country D to Country I: \$600m

Country D to Country B: \$500m; Country D to Country C: \$300m

(3+12=15)

5. (a) FDI is more preferred mode of investment by any country. Why ? (7)

(b) What do you mean by political risk ? Explain different methods used by MNCs to manage political risk. (8)

Paper No. 504 2012

[This question paper contains 4 printed pages.]

Sr. No. of Question Paper : 1229 **Roll No............**

Unique Paper Code	: 101504
Name of the Paper	: International Finance
Name of the Course	: BFIA
Semester	: V
Duration	: 3 Hours
Maximum Marks	: 75

Instructions for Candidates

1. Write your Roll No. on the top immediately on receipt of this question paper.
2. Attempt **All** questions.

1. The principle task of a Central Bank is to keep inflation under check. Should it also adjust interest rates in response to excessive movements in assets prices ?

Foreign exchange intervention is unlikely to work unless it is allowed to feed into interest rates. Many Central Bankers in the past did not favor raising of interest rates to prick a stock market bubble. They argued that monetary policy should focus solely on inflation.

In a recent meeting of Central Bankers, it was concluded that Central Bankers should indeed change interest rates in direct response to movements in equity prices or exchange rates. By doing so, it observed they would reduce the variability of both inflation and output over time. The analysis of the meet also has the virtue of encompassing exchange rate misalignments and equity bubbles within the same framework. Markets in both shares and currencies tend to overshoot at times, leading to the formation of bubble that can have similar consequences such as misallocation of resources.

Most Central Banks already take some account of assets prices in making inflation forecasts. Thus they will raise interest rates if the "wealth effect" caused by higher equity prices threatens to increase consumer spending and hence future inflation. Similarly, they may raise rates if a weak exchange rate threatens to push up import price. However, the Committee report argues that Central Bankers should respond to asset price movements for other reasons than merely their direct impact on inflation.

For instance, a stock market bubble typically encourages a buildup of debt. When share prices collapse, the financial system and economy as a whole is at risk. Likewise, large exchange rate misalignments rarely correct themselves without some pain.

By paying more attention to asset prices, Central Bankers can actually improve their long-term inflation record. Consider a share price bubble: raising interest rates may initially put inflation below target. But by letting some air out the bubble sooner, the impact on inflation and output, when it bursts is more modest. By undershooting inflation a little now, it reduces the risk of undershooting to a great extent at some time in future.

Similarly, if a currency seems significantly undervalued, a Central Bank should raise interest rates by more than necessary to keep a lid on future inflation. If a currency seems ludicrously overvalued, interest rates should be cut even if that means inflation moves slightly above target in the short term. However, share price bubbles or exchange-rate misalignments are difficult to identify. Monetary policy is always dealing uncertainty, this is no reason to ignore asset price. On the basis of the report, interest rates would probably need to be a bit higher than at present in the Euro area.

Central Banks would have to explain carefully why they are temporarily missing their inflation targets. There is a risk that this could damage a Central Bank's credibility. For instance, if a Central Bank allowed inflation to overshoot its target in order to push down its currency, markets might conclude that it had gone soft on inflation. Likewise using interest rates to resist surging equity prices would be hard to sell to the public. The truth is that single minded inflation target may be flawed.

Answer the following questions : (8×2=16)

(a) In the long run what should be the policy objectives of a Central Bank ? Justify.

(b) Explain how can misalignments in exchange rate lead to misallocation of resources ?

2. You work as an assistant manager in the treasury department. This morning, the managing director informs you that the company has CHF 10,000,000 available for short term investments. He also noted that the following exchange rates are currently available :

Mizuho quote	:	JPY 125.84/USD
Credit Suisse quote	:	CHF1.5365/USD
UBS quote	:	JPY 82/CHF

Required :

The managing director would like to know whether the company could make a profit via triangular arbitrage. Write a report to Managing Director, state your workings with reasons and calculate the amount of profit in Swiss Francs. (7)

3. What is the expected change in the exchange rate that satisfies the uncovered interest rate parity ? Explain with the help of an illustration. (7)

4. JP Infra, an Indian construction firm is bidding on a project in Canada. Briefly explain all the possible exposures and their respective hedging strategies. (7)

5. Explain the ADR and its procedure of issuance in detail. (7)

6. What are the different issues in multilateral netting ? Show the possible netting among the following countries case : (7)

India to Belgium: INR200m; India to China: INR 100m

India to Denmark: INR 250m; Belgium to India: INR 300m

Belgium to China: INR 150m; Belgium to Denmark: INR 400m

China to India: INR 270m; China to Belgium: INR 230m

China to Denmark: INR 600m; Denmark to India: INR 400m

Denmark to Belgium: INR 200m; Denmark to China: INR 500m

7. Alpha Lab has its wholly owned subsidiary operating in London where it maintains its account in GBP. At the end of the financial year 2011-12 the balance sheet and income statement presented in USD are as follows. Translate the balance sheet and Income statements in Indian Rupee using Temporal and Current Rate methods. (12)

Balance Sheet (GBP million)

Cash	200
Inventory	220
Net Fixed Assets	2180
Total Assets	**2600**
Current liabilities	200
Long-term liabilities	910
Common Stock	1000
Retained Earnings	490
Total Liabilities & Equities	**2600**

Income Statement (USD million) G. B. P

Sales	4000
COGS	2900
Depreciation	400
Net Operating Income	700
Income Tax (30%)	210
PAT	490
Foreign Exchange gain & losses	
Net income	490
Dividend	0
Addition to Retained Earnings	490

The Exchange rate of GBP/INR was 84.50 in the beginning of year which changed to 86.20 by the end of the year. The realization value of inventory was expected to be GBP 270.

8. Write short notes on any **four** of the following : (3×4=12)

(a) Political risk

(b) Basis risk

(c) Tick size

(d) Cross rate

(e) Forward premium