NATIONAL UNIVERSITY OF SCIENCE AND TECHNOLOGY
FACULTY OF COMMERCE
DEPARTMENT OF BANKING

BANKING AND FOREIGN EXCHANGE
CBA 2202

SUPPLEMENTARY EXAMINATION **AUGUST 2008**

TIME: 3 HOURS

INSTRUCTIONS TO CANDIDATES

Answer any FOUR (4) questions.

Indicate on your answer booklet whether you are in the conventional or parallel programme.

INFORMATION FOR CANDIDATES

The number of marks is given in brackets [ ] at the end of each question or part question.

Questions may be written in any order, but must be legibly numbered.

The businesses in this question paper are intended to be fictitious.

This paper consists of 4 printed pages

[Turn over]

QUESTION 1

1. (a) Explain what is meant by the terms foreign exchange translation exposure, and economic exposure. **[15 Marks]**

   (b) What is the significance of these different types of exposure to the financial Manager? **[10 Marks]**

TOTAL [25 MARKS]

2 Explain clearly with the aid of diagrams if necessary the following terms.

(i) Marginal Price System and the Dutch Auction System in the forex market. **[6 Marks]**
(ii) A call option is deep in the money **[5 Marks]**
(iii) A covered call option **[5 Marks]**
(iv) A bottom straddle **[5 Marks]**
(v) Letter of credit **[4 Marks]**

TOTAL [25 MARKS]

QUESTION 3

(a) What is the difference between foreign exchange translation exposure and Transactions exposure? **[8 Marks]**

(b) The British Pound Sterling/Zimbabwean dollar spot exchange rate is GBP1/Z$13.5. It is expected that the British Pound will appreciate by 20% Against the Zimbabwean dollar by end of 90 days.

Your company has got a GBP 45 000, 90 days export credit that has been used to
Import commercial vehicle spares. The amount of money has to be paid back by the end of 90 days from today.

(i) How much would your company pay if it were to settle its export credit today? **[7 Marks]**

(ii) How much would your company pay if it were to wait until the end of the 90 days assuming the company could not find any cover? **[10 Marks]**

TOTAL [25 MARKS]

QUESTION 4

(a) What is the importance of the Balance of Payments position to a country? **[5 Marks]**

(b) Define the following terms or concepts clearly showing the difference between them:

(i) Terms of trade.
(ii) Balance of visible trade **[5 Marks]**

(c) State and briefly explain FOUR ways through which a country can protect its home industries against imports. **[4 Marks]**

(d) Give ONE reason why it may not be possible for a country to continue having a Balance of Payments surplus. **[2 Marks]**

(e) State and explain any THREE ways through which governments or monetary Authorities can intervene in the foreign exchange market in order to maintain an exchange rate within given limits. **[3 Marks]**

(f) Write brief notes on any FOUR of the major determinants of foreign exchange rates in a freely floating exchange rate regime. **[3 Marks]**

(g) What do you suggest should be done to eradicate the foreign exchange parallel Market in Zimbabwe? **[3 Marks]**

TOTAL [25 MARKS]

QUESTION 5

.(a) Distinguish between an American and an European put option. Under what circumstances can a trader want to exercise his option early? **[6 Marks]**

(b) Why is it unnecessary for investors to write put options on foreign currencies? **[3 Marks]**

(c) Draw separate and clearly labeled diagrams for each of the following option strategies.

(i) Purchase a put, $5 premium with a strike price of 700ZW$/US$. **[3 Marks]**

(ii) Buy a call with a strike price of 500ZW$/US$ at a cost of $3. **[3 Marks]**

(a) Write short notes on the following.

(i) Confirmed letter of credit. **[2 Marks]**
(ii) Draft **[2 Marks]**
(iii) Bill of lading **[2 Marks]**
(iv) Certificate of origin **[2 Marks]**
(v) Banker's acceptance **[2 Marks]**

TOTAL [25 MARKS]

QUESTION 6

The deposit rates in Zimbabwe and South Africa for comparable investments are 3% p.a and 4% p.a respectively. The spot exchange rate is $750/Rand.

(a) Is covered interest arbitrage possible here? Demonstrate using your own figures
How one can make riskless profits from this opportunity. **[8 Marks]**

(b) What are the effects of arbitrage transactions in any market? **[7 Marks]**

(c) The exchange rate between the Zimbabwean dollar and the South African Rand is ZW$1=0,1255 and that between the Namibian dollar (N$) and Zimbabwean dollar is N$1=ZW$9,554.

(i) The NZ$/ZAR exchange rate. **[7 Marks]**
(ii) What is a cross exchange rate and when is it normally used? **[3 Marks]**

TOTAL [25 MARKS]