NATIONAL UNIVERSITY OF SCIENCE AND TECHNOLOGY
FACULTY OF COMMERCE
DEPARTMENT OF BANKING
BACHELOR OF COMMERCE HONOURS DEGREE IN BANKING

INTERNATIONAL BANKING - CBA 4105

FINAL EXAMINATION   **APRIL 2009**

TIME: 3 HOURS

INSTRUCTIONS TO CANDIDATES

- The paper contains **SIX (6)** questions.

- Answer questions one (1) and three (3) other questions from section B .

- All questions carry equal marks **[25 marks].**

- Start the answer to each question on a fresh page of the answer sheet.

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

INFORMATION FOR CANDIDATES

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

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

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[Turn over]

SECTION A

QUESTION 1 COMPULSORY

(a) Explain briefly the following foreign exchange exposure risks

    (i) Accounting exposure

    (ii) Operation exposure

    (iii)Transaction exposure   [8 marks]

(b) The following is the balance sheet for the Global limited Zimbabwe. It is a subsidiary to Global World with its headquarters in the United Kingdom

Balance sheet for Global World Limited

	Z$(000)(Local currency)
Assets	
Current assets	
Cash, marketable securities and receivables	2 600
Inventory (at market)	3 600
Prepaid expenses	200
Total current assets	6 400
Fixed assets less accumulated depreciation	3 600
Goodwill	1 000
Total assets	**11 000**
Liabilities	
Current liabilities	3 400
Long term debt	3 000
Deferred income taxes	500
Total liabilities	6 900
Capital stock	1 500
Retained earnings	2 600
Total equity	4 600
Total liability plus equity	**11 000**

Given that the current exchange rate at the time of translation was Z$5/£ and the historical exchange rate is Z$4/£, calculate the translation gains / losses on the adjusted Global World balance sheet of its subsidiary using:

(a) Monetary / non Monetary method   [6 Marks]

(b) Temporal method   [3 Marks]

(c) Current / Non current method   [8Marks]

TOTAL   **[25 MARKS]**

SECTION B

Answer any **three** questions from this section

QUESTION 2

(a) What are the basic reasons for the existence of the Eurocurrency and Eurobond markets? What factors have accounted for the growth of such markets over time?
[10 Marks]

(b) State 5 activities that can be undertaken or carried out by international banks

[5Marks]

(c) The interest rate parity theory ensures that any interest rate differentials between markets or countries are eliminated. Given this background , that interest rates must not vary among different markets , give a detailed account explaining reasons for the presence of the interest rate differentials between the Eurocurrency markets and the domestic market , in particular as regards to both deposit and lending interest rates
[10 Marks]

TOTAL   **[25 MARKS]**

QUESTION 3

a) Microsoft needs to raise $1billion and is trying to decide between a domestic dollar bond issue and a Eurobond issue. The US bond can be issued at a coupon of 6,75% paid semiannually with underwriting and other expenses totaling 0.95% of the

issue size. The Eurobond would cost only 0.55% to issue but would bear an annual coupon of 6.88%. Both issues would mature in 10 years.

b)

    (i) Assuming all else is equal which is the least expensive issue for Microsoft? [13Marks]

    (ii) What factors should Microsoft consider before deciding Which bond to issue ? [2 Marks]

c) Commerzbank is seeking to invest $100million short term. It has the choice between buying Euro Commercial Paper (Euro CP) yielding 6.34% annually and a US bank deposit yielding 6.36% annually, both maturing in 150 days. The Euro CP yield is calculated on a 360 day year, whereas the US bank deposit yield is calculated on a 365 day year.

    (i)   How much Euro CP in terms of face value can Commerzbank's $100million buy [3 Marks]

    (ii)   Assuming that all else is equal, what will be Commerzbank preferred investment and explain why. [2 Marks]

    (iii)   What would the annual yield on the U S bank deposit be if it is quoted on a 360 day year ? [21/2Marks]

    (iv)   What would the annual Euro commercial Paper yield if it was quoted on a 365 year? [2 1/2Marks]

        TOTAL   **[25 MARKS]**

QUESTION 4

(a) State and briefly explain three instruments that can be used to hedge financial institutions against risk. [6 Marks]

(b) What are the main problems that are associated with hedging? [2 Marks]

(c) Compare and contrast forward and futures contracts. In your comparison bring out the advantages and disadvantages of each instrument. [10 Marks]

(d) What are the advantages and disadvantages of an interest rate swap? [7 Marks]

        TOTAL   **[25 MARKS]**

QUESTION 5

(a) What is Gap analysis   [2 Marks]

(b) State and explain two Gap management strategies, clearly highlighting problems that can be encountered in gap analysis management.   [7Marks]

(c) Consider a bank with a summary of its balance sheet in market value terms as follows:

Maturity	Assets	Liabilities & assets	Duration
90 days	100	300	0.2
180 days	200	300	0.5
1 year	400	100	1
2 years	200	100	2
3 years	100	100	2.5
		equity	
		100	

(i)   Calculate the duration Gap of the bank   [7 Marks]
(ii) Given the duration gap calculated above, what are the implications to the bank of an interest rate increase on the value of the banks equity?

                                                                                          [3 Marks]

(iii) If three month Treasury bill futures contracts are sold at a price of $94 for delivery in three months. What is the number of contracts needed to completely hedge the balance sheet of the bank for the next three months? Comment on your answer   [6 marks]

                         TOTAL   **[25 MARKS]**

QUESTION 6

(a) Giving examples where possible, discuss two methods that can be used to measure a banks liquidity position. In your discussion clearly highlight the strengths weaknesses of each method. From the banks point of view.   [15Marks]

(b) In your opinion what could be the main causes of cash flow problems in financial institutions.   [10 Marks]

                         TOTAL   **[25 MARKS]**