NATIONAL UNIVERSITY OF SCIENCE AND TECHNOLOGY
FACULTY OF COMMERCE
GRADUATE SCHOOL OF BUSINESS
EXECUTIVE MASTER OF BUSINESS ADMINISTRATION

INTERNATIONAL TRADE AND FINANCE – EMB 507
SUPPLEMENTARY EXAMINATION

DATE: **17 JUNE 2004**

TIME ALLOWED: 3 HOURS + 30 MINUTES

Reading time is 30 minutes. Candidates are permitted to make notes on the question paper but not to write in the answer book during this period.

INSTRUCTIONS

1) Answer any four (4) questions.
2) All questions carry **equal** marks.
3) Show all **workings, notes** where necessary.

Question 1.

(a.) Describe constraints that interfere with the MNCs' finance managers' objective of attempting to maximize shareholders' value.
(6 Marks)

(b.) It is always suggested that floating exchange will adjust to reduce or eliminate any current account deficit. Explain why this adjustment would occur. **(6 Marks)**

(c.) What restrictions would prevent the exchange rate not always to adjust to accommodate current account deficit?
(4 Marks)

(d.) What are some of the major objectives of the IMF?
(9 Marks)

Question 2.

(a) Why should capital budgeting for subsidiary projects be assessed from the parent's perspective?
(4 Marks)

(b) The Belgian owner of a Brussels Billiard ball-manufacturing firm wants to manufacture in the United States to supply the American Market. The investment will amount to BF. 20 million ($400,000 @ BF 50/$), all in fixed assets, which may be depreciated over five years by the straight-line method with no scrap value expected. An additional BF. 5 million ($100,000) will be needed for Working Capital.

The Belgian entrepreneur expects to sell the U.S. subsidiary as a going concern at the end of three years for $40,000 (after all income taxes), at which time she will purchase a country villa in Ardennes Mountains in Belgium.

In evaluating the venture, the following forecasts were used:

End of Year	Unit Demand in U.S. '000	Unit Sale Price ($)	Exchange Rate BF 50/ 1$	Fixed Costs $ '000	Depreciation $ '000
0	-	-	-	-	-
1	700	1.00	50	100	80
2	900	1.03	48	103	80
3	1000	1.06	47	106	80

Variable manufacturing costs are expected to be 50 percent of sales.
The United States imposes no restrictions on repatriation of any funds, including liquidating dividends. No new funds are to be invested in the United States for at least the first three years.
The US. Corporate tax rate is 40 per cent, and the Belgian rate is 50 per cent levied on earnings remitted to Belgium.

The Belgian entrepreneur's weighted-average cost of capital is 18 percent per annum, and her objective is to maximize her present wealth.

Is the investment strategy attractive?

(21 Marks)

Question 3.

(a.) What are the advantages and disadvantages to a corporation that uses currency options rather than forward contracts to hedge against exchange rate fluctuations?

(10 Marks)

(b.) Explain the concept of covered interest arbitrage, and when does it become feasible between any two currencies.

(5 Marks)

(c.) Assume the following information:

	Quoted Price
Spot rate of Canadian dollar	$ .80
90-day forward rate of Canadian dollar	$ .79
90-day Canadian interest rate	5 %
90-day U.S interest rate	3 %

Given the above information;

(i.) What would be the yield to a U.S investor who used covered interest arbitrage? **(7 Marks)**

(ii.) Would you say there is interest rate parity between the U.S and Canada? **(3 Marks)**

Question 4.

(a.) How can a firm hedge long-term currency exposures? Explain each method. **(15 Marks)**

(b.) How can leading and lagging be used by an MNC in intra-group financing? **(5 Marks)**

(c.) What is "netting" and how can it improve an MNCs' performance?

(5 Marks)

Question 5.

Assume that a US based MNC needs $ 3 million for a one-year period. Within one year, it will generate enough US dollars to pay off the loan. It is considering three options:

1.) Borrow US dollars at an interest rate of 6 %;

2.) Borrow Swiss francs at an interest rate of 3 %; or

3.) Borrow German marks at an interest rate of 4 %

The MNC has forecasted that the Swiss franc will appreciate by 1 % over the next year, and that the German mark will appreciate by 3 %.

(a) What is the expected "effective" financing rate for each of the three options? **(12 Marks)**

(b) Which of the above options appear to be feasible? **(3 Marks)**

(c) Why might the MNC not necessarily choose the option reflecting the lowest effective financing rate? **(5 Marks)**

(d) Why would a U.S firm consider issuing bonds denominated in multiple currencies for financing? **(5 Marks)**

Question 6.

a) What is the role of a factor within international trade transactions and how can a factor be useful to an exporter? **(6 Marks)**

b) Explain how the development of foreign trade would be affected if banks did not provide trade-related services. **(6 Marks)**

c) What is counter trade? Illustrate your answer. **(6 Marks)**

d) Describe the possible errors involved in assessing country risk. **(6 Marks)**

END OF EXAMINATION PAPER!!!!