5. (a) Derive International Fisher Effect by combining Purchasing Power Parity and Interest Rate Parity.

(b) The analysis of demand and supply curve of a currency shows that the foreign exchange markets can become unstable. Critically examine the above statement.

(c) Write a short note on Currency Swaps.

6. (a) Assuming zero transaction costs complete the following table with all spot prices are given in dollar terms:-

		Currency			
Currency	$	£	₹	€	¥
One $	1	0.76	92.73	0.86	159
£		1			
₹			1		
€				1	
¥					1

(b) Develop a Payoff profile for currency futures

(c) How does inflation in home country and foreign country affect the exchange rate. 8,5,5

7. Write short notes on any **three** of the following:

(i) J-curve

(ii) Role of exchange brokers in Forex markets

(iii) Currency Market Spread

(iv) Bill of Lading

(v) Hybrid System of exchange rates

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[This question paper contains 4 printed pages]

Your Roll No. : .....

Sl. No. of Q. Paper : **1197 I**

Unique Paper Code : 2923102005

Name of the Paper : International Financial Management

Name of the Course : **B.A. (H) Business Economics**

Semester : IV/VI/VIII

Time : 3 Hours ***Maximum Marks : 90***

Instructions for Candidates :

(a) Attempt any **five** questions, all questions carries equal marks.

(b) Use of simple calculator is allowed.

(c) If any assumption is made while solving a problem, the same must be stated clearly.

1. A US Semi-conductor company agrees to sell its product to a UK based firm for 10,00,000 £. with an agreement that the payment for the same would be made in 90 days. At the time of deal, forward and spot rates between dollar and pound were: S($/£): 1.3490 and F($/£): 1.3321. The interest rates prevailing in two countries were as under :

Interest Rates (%)	UK (p.a.)	US (p.a)
Deposit	7	4
Borrowing	9	6
Working Capital (in money market)	12	-

Further, in currency options market, a call option is available with a strike rate of 1.341$/£with a premium as 0.921 $. The dollar-pound market three month forecast of spot rates are 1.3301 $/£ and 1.3311 $/£ with probabilities 0.7 and 0.3 respectively.

Determine the payoffs for the UK based importer if the finance manager is considering the following plans :

1. Company decides to hedge its position in the forward market
2. Company decides to hedge by borrowing funds from US and creating a UK deposit
3. Company decides to hedge by borrowing funds from US and lending in U.K money market
4. Company decides to hedge in currency options market
5. Company does not go for any kind of hedging
6. Prepare a results table with three columns, first is the Hedging Strategy, Second is the Outgo from the strategy and third rank given by you (best (1) to worst (5)) (3×6=18)

2. (a) An Indian importer has to pay 1 million $ to pay for imports in 6 months. It enters a 6 month call option contract at ₹ 92.40/$ with a premium of 5%. Determine the final amount to be paid the Company if on the expiry of option, the spot price behavior is expected to be (i) Discount of 1.92% on Rupee (ii) Premium of 2.96% on Rupee. Under which of the two conditions mentioned above the call option becomes meaningless, clearly present with a comparative table.

(b) If inflation in India is 7.25% while it is 4.25% in US. With the aim to restore the PPP, determine whether rupee shall appreciate or depreciate and by how much.

(c) US interest rate is 4.25%, and India interest rate is 7.25%, exchange rate between these two currencies at 92.11 INR/$ Spot and 93.11 INR/S Forward.

Mr X sees an arbitrage opportunity in above set of figures, do you agree with Mr X, if yes then try to derive an arbitrage opportunity with an amount 1000 $ (using borrowing, lending, spot and forward rates). Compute actual arbitrage gain on 1000 $. (Transaction costs may be taken as zero) 7,4,7

3. (a) Giving your own hypothetical example show how possibility of arbitrage created under the Gold Standard and Gold Exchange System of payments gets wiped out.

(b) You are given spot rates as S($/£): 1.235/245 and S(INR/S): 91.221/277, compute cross rate between S(INR/£), your answer should be upto three decimals.

(c) Using all the three quotes, the two given and one computed, apply triangular/three point arbitrage to determine if arbitrage exists. 6,6,6

4. (a) What are the two important considerations to compute forward rate from spot rates when swap points are given. Applying the same, calculate the forward rates from the following quotes S(INR/$): 91.221/277 1-month swap rates 12/18, 2 month swap-4/2

(b) The one year interest in Country '1' is 2% and the same in Country '2' is 4%. If the spot rate of Country 1's currency per unit of country 2's currency is 0.67, calculate the forward rate between the two currencies using Interest rate parity theorem.

(c) Do you think the statistical concept of correlation and standard deviation are helpful to a Finance Manager when he is managing the foreign exchange exposure of the Company's currency. Discuss. 6,6,6