

Mock Examination Paper June Term 2023

Programme: BA Business Management

Module: International Financial Management

Module code: LCBB 6002

Contribution to Overall Module Assessment (%): 0%

Module Leader: Dr. Taye Timothy Osadiya

Internal Verifier:

Mock Examination Duration: 3 Hours

Mock Examination Date & Time: To be announced by the London Assessment Team.

***You must attempt all sections A, B & C questions.**

Section A

1. **Which of the following is a legitimate reason for international investment?**
 - (a) Dividends from a foreign subsidiary are tax exempt in the United States.
 - (b) Most governments do not tax foreign corporations.
 - (c) There are possible benefits from international diversification.
 - (d) International investments have less political risk than domestic investments.

2. **By definition, currency appreciation occurs when:**
 - (a) The value of all currencies fall relative to gold.
 - (b) The value of all currencies rise relative to gold.
 - (c) The value of one currency rises relative to another currency.
 - (d) The value of one currency falls relative to another currency.

3. **Theory which considers change in exchange rate with fluctuations in inflation rates is classified as:**
 - (a) Liquidated power parity
 - (b) Purchasing power parity
 - (c) Selling power parity
 - (d) Volatile power parity

4. **If purchasing power parity were to hold even in the short run, then:**
 - (a) Real exchange rates should tend to decrease over time.
 - (b) Quoted nominal exchange rates should be stable over time.
 - (c) Real exchange rates should tend to increase over time.
 - (d) Real exchange rates should be stable over time.

5. **Given a home country and a foreign country, purchasing power parity suggests that:**
 - (a) The home currency will appreciate if the current home inflation rate exceeds the current foreign inflation rate
 - (b) The home currency will depreciate if the current home interest rate exceeds the current foreign interest rate
 - (c) The home currency will depreciate if the current home inflation rate exceeds the current foreign inflation rate

- (d) The home currency will depreciate if the current home inflation rate exceeds the current foreign interest rate

6. Interest Rate Parity (IRP) implies that:

- (a) Interest rates should change by an equal amount but in the opposite direction to the difference in inflation rates between two countries
- (b) The difference in interest rates in different currencies for securities of similar risk and maturity should be consistent with the forward rate discount or premium for the foreign currency
- (c) The interest rates between two countries start in equilibrium, any change in the differential rate of inflation between the two countries tends to be offset over the long-term by an equal but opposite change in the spot exchange rate
- (d) In the long run real interest rate between two countries will be equal
- (e) Nominal interest rates in each country are equal to the required real rate plus compensation for expected inflation

7. In equilibrium position, spread between foreign and domestic rate of interest must be equal to spread of:

- (a) Domestic rates
- (b) Forward and spot exchange rates
- (c) Forward rate
- (d) Spot rates

8. Rule which states that similar set of goods and services produced in various countries should have equal price is classified as:

- (a) Law of similar mortgage rate
- (b) Law of one type manufacturing
- (c) Law of similar labour rules
- (d) Law of one price

9. Example of derivative securities includes:

- (a) Swap contract

- (b) Option contract
- (c) Futures contract
- (d) All of above

10. Authority which intervenes directly or indirectly in foreign exchange markets by altering interest rates is considered as:

- (a) Central government
- (b) Centralised stocks
- (c) Central corporations
- (d) Centralised instruments

11. The forward market is especially well-suited to offer hedging protection against:

- (a) Translation risk exposure.
- (b) Transactions risk exposure.
- (c) Political risk exposure.
- (d) Taxation.

12. Suppose that the Japanese yen is selling at a forward discount in the forward-exchange market. This implies that most likely:

- (a) This currency has low exchange-rate risk.
- (b) This currency is gaining strength in relation to the dollar.
- (c) Interest rates are higher in Japan than in the United States.
- (d) Interest rates are declining in Japan.

13. Hedging is used by companies to:

- (a) Decrease the variability of tax paid
- (b) Decrease the spread between spot and forward market quotes
- (c) Increase the variability of expected cash flows
- (d) Decrease the variability of expected cash flows
- (e) Increase the variability of tax paid

14. Which of the following is true of foreign exchange markets?

- (a) The futures market is mainly used by hedgers while the forward market is mainly used for speculating.
- (b) The futures market and the forward market are mainly used for hedging.
- (c) The futures market is mainly used by speculators while the forward market is mainly used for hedging.
- (d) The futures market and the forward market are mainly used for speculating.

15. Exchange rates:

- (a) Are always fixed
- (b) Fluctuate to equate the quantity of foreign exchange demanded with the quantity supplied
- (c) Fluctuate to equate imports and exports
- (d) Fluctuate to equate rates of interest in various countries

Total Mark for Section A (15)

...and they are

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3. What are the difference between economic exposure and transaction exposure? (5 marks)

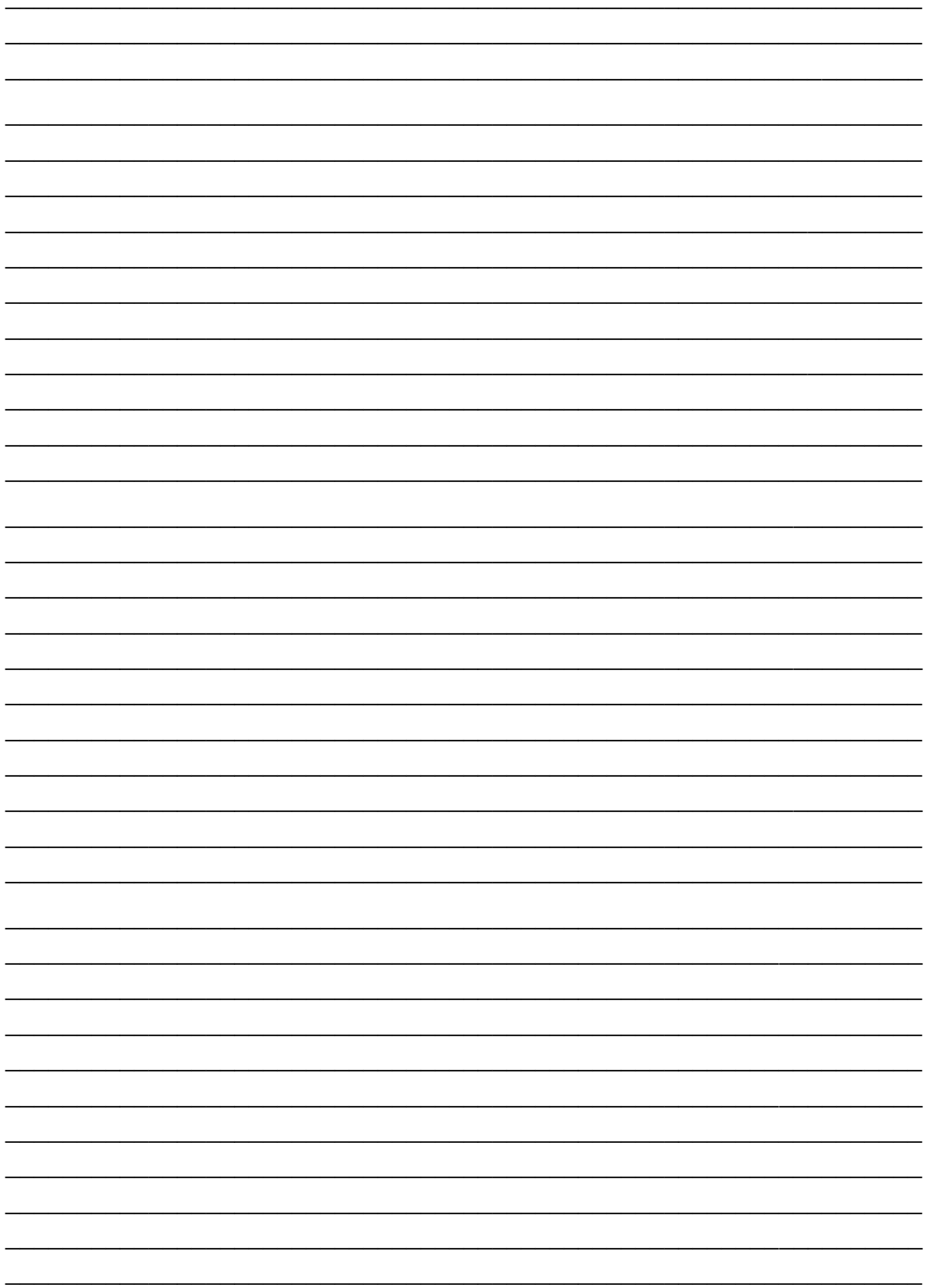
[illegible]

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4. Discuss the factors that cause the demand and supply curves to shift, consequently leading to changes in exchange rates. (5 marks)

5. Exchange rates cannot be predicted because they are determined by news. Explain. (5 marks)

[illegible]

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- 10.** Under what conditions are foreign-currency-denominated bonds preferred even if they offer a lower rate of return (in foreign currency terms) than domestic bonds? (5 marks)

- 11.** What is the efficient frontier? What does international diversification do to the efficient frontier? (5 marks)

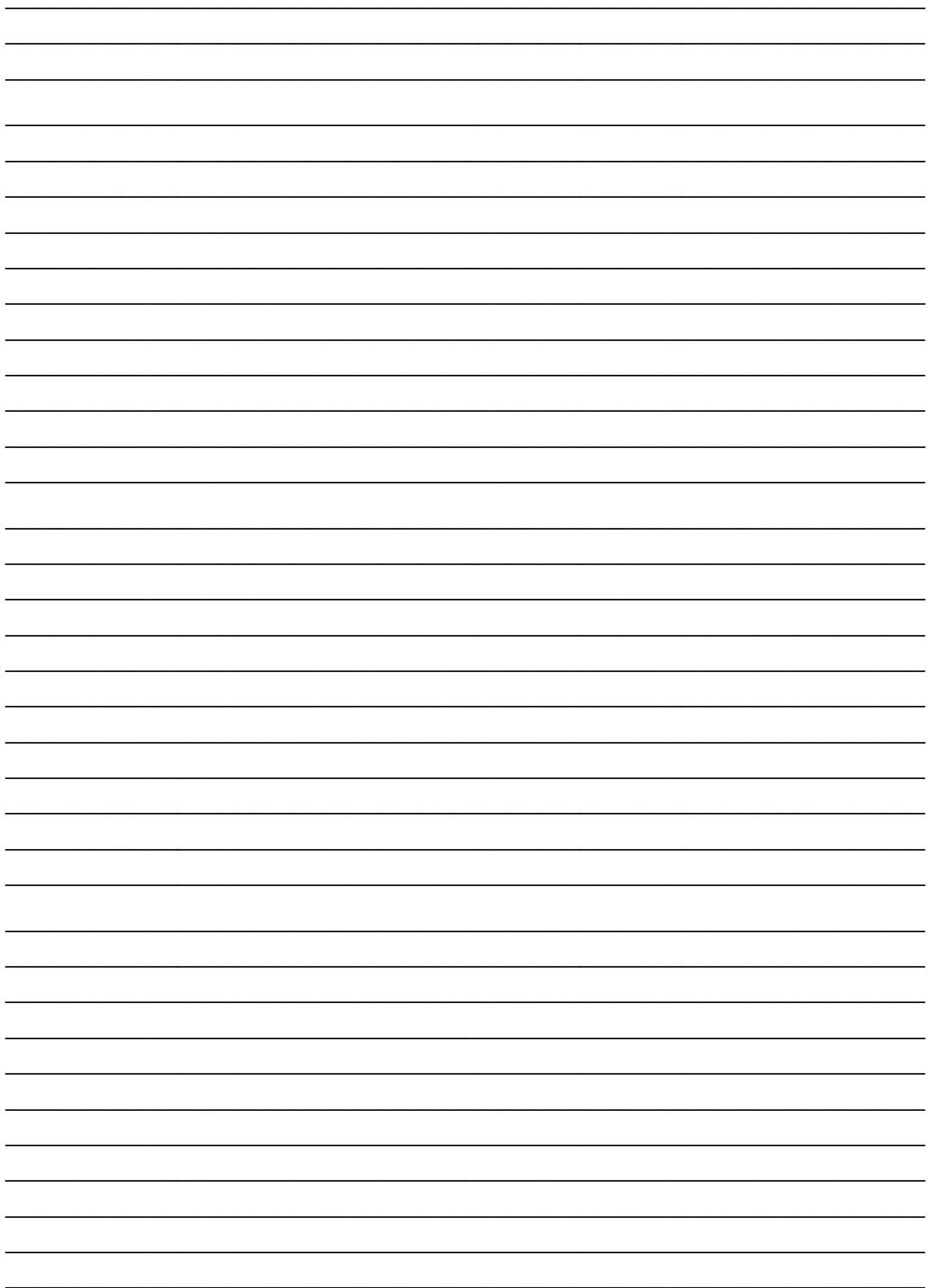
12. International diversification is beneficial only if markets are segmented.

Why, then, do portfolio managers diversify internationally in practice?
(5marks)

[illegible]

13. What are the strategic and long-term factors that determine whether or not to indulge in FDI? (10 marks)

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Total Mark for Section B (75 marks)

Section C

Question 1

Calculate the net present value with a required return of 5% an initial investment of £45,000 and cash flows of £12,000, £20,000, £10,000 and £6,000 for years 1, 2, 3, & 4 respectively.

*Below is the formula for computing the present value factor (PVF).

$$PVF = 1 / (1+i)^n$$

Where,

i = interest rate

n = number of years

**Note that the net present value calculates the difference between the present value of cash inflows and cash outflows. An investment is economically feasible only if it has a net present value that is greater than zero.*

From the above given information, calculate the NPV. (10 marks)

[illegible]

