K. J. SOMAIYA INSTITUTE OF MANAGEMENT STUDIES & RESEARCH
VIDYA NAGAR, VIDYA VIHAR (E), MUMBAI- 400 077

PGDM/MMS- V; Trim 2017-19

International Finance

(End- Trimester Examination)

Max marks 50 | Duration: 3 Hrs | Date : 19/01/2019

Note: Restrict each of your answers to around 40 lines.

1. Answer **any four** questions from Section A (4*10)
2. Both case studies in Section B are **compulsory (2*5)**

Section A

1. Explain the concept of translation exposure, various methods of translation of an MNC with suitable examples.

2. What factors determine hedging strategies of a MNC? Discuss four internal hedging strategies with suitable examples.

3. Discuss 2010-13 Eurozone crisis in detail and proposed options

4. Why Indian economy survived during the Asian Currency Crisis of 1997?

5. Explain the concept in practice "Swiss Franc Pegging – free float to Intervention".

6. Explain the measures to quantify political risk faced by an MNC. What are various economic and financial risks that are taken into account while assessing country risk rating models?

7. a) Calculate the cross currency rates based on the following quotations.
   The exchange rates for Mexican Peso and Indian Rupee with respect to USD are:

Rupee/USD	65.00	65.50
Mex Peso/USD	19.00	19.25

   Find out at what rate would the bank buy Mexican Peso and sell Mexican Peso? What is

the exchange rate of rupee per Peso?

b) Using PPP and below mentioned information, calculate real depreciation of rupee.

Exchange rate of pound in India in

1990	45.00
2005	65.00

Inflation increased by 75% and 50% in this 15 year period. Assume 1990 as the base year.

8. What impact would the following events have on India's balance of payments? Your response should include effect in terms of positive/negative/no impact and also which account (current/capital/reserves) will this get reflected as debit/credit/inflow/outflow.
   a) India increases limits by 5 bln USD on capital inflows of investments in government securities and portfolio investments
   b) China devalues its currency that resulted in 5 bln decrease in Indian Exports
   c) USA imposes a tariff amounting to value 5 mln rupees on exports of 1 bln garments from India
   d) Thai Baht appreciates with respect to all major currencies
   e) Euro appreciates with respect to Indian rupee, exports decreased by 10 bln USD
   f) American investor sold ADRs worth 2000 USD
   g) Indian MNC bought European technology firm for 2 bln Euros
   h) An Indian parent remits USD 20,000 towards payment of tuition fee for his daughter.
   i) Swiss based subsidiary repatriates profits to the tune of 500 mln USD to Indian Parent Company
   j) India exports onions worth 500 USD to Bangladesh.

Section B (5*2 = 10 marks)

a) Caterpillar in a world of fluctuating currencies

Caterpillar, operates in 200 countries exporting construction equipment, mining equipment and engines for a long time. Japanese firm Komatsu was its major competitor. From 1980s on wards, the dollar yen exchange rate changes had impacted adversely on the profitability and competitiveness of Caterpillar due to strong dollar and labor union problems for restructuring its business. However, by 2000, The Company was able to reduce costs, increase productivity and turned into profitable. Dollar was weak during

mid-2000 and worldwide boom helped to increase exports. In the year 2008, dollar started strengthening due to increased dollar demand post global financial crisis. Due to diversification and expansion of production to other countries, strong dollar did not affect its profitability as the costs have reduced in other locations. 102 out of 237 locations were outside US and revenues generated by these when translated with strong USD declined, but the costs of production was also on declining trend hence it profit margins did not fall compared to the earlier strategy of almost 50% producing in US. This strategy of spreading production locations helped the Company to manage its transaction exposure.

Case Discussion Questions

1. In the 1980s a stronger dollar hurt Caterpillar's competitive position, but in 2008 a stronger dollar did not seem to have the same effect. What had changed?
2. How did Caterpillar use strategy as a "real hedge" to reduce its exposure to foreign exchange risk? What is the downside of its approach?
3. Explain the difference between transaction and translation exposure using material in the Caterpillar case to illustrate your answer.

b) Quantitative Easing, Inflation, and the value of US Dollar

In the year 2010, the US Federal reserve decided to expand the US money supply by entering the open market and purchasing $600 billion in US government bonds from bond holders, a technique known Quantitative easing. Where did the $600 billion come from? The Fed simply created new bank reserves and used this cash to pay for the bonds. In effect it had printed the money. This action was aimed to stimulate the US economy after the financial crisis of 2008-09. It also reduced short-term interest rates to near zero. It further infused two rounds of QE in 2011 and 2012 and announced that it will continue until the unemployment rate fell below 6.5 %.

Critics were quick to attack the Fed's moves. Many claimed that expanded money supply would fuel inflation and lead to decline in value of dollar on foreign exchange market.

However, these charges may be unfounded for two reasons. First, at the time, the core US inflation rate was the lowest in 50 years. In fact, fear of deflation is a dangerous as it results in collapse of aggregate demand and lead to high unemployment. Secondly, US was facing weak economic growth, high unemployment and excess capacity. Consequently, if the injection of money supply did stimulate and not translated into inflation due to business started expanding the capacity. As for the currency market, its reaction was muted and traders did not seem to be selling off the dollar or reflecting worries of high inflation rate.

Case Discussion questions

1. How quantitative easing helps to recover economy from recession?

2. Why it did not impact US inflation?
3. What is the relationship between unemployment and inflation?
4. How money supply expansion is stimulates the demand and recovery in the economy?

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