

CHUKA



UNIVERSITY

## UNIVERSITY EXAMINATIONS

### FOURTH YEAR EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE

**BCOM 434: INTERNATIONAL FINANCE**

**STREAMS:**

**TIME: 2 HOURS**

**DAY/DATE : WEDNESDAY 22 /09/ 2021**

**8.30 AM – 10.30 AM**

**INSTRUCTIONS TO CANDIDATES:**

- Answer Question One and any other Two Questions.
- DO NOT WRITE ANYTHING on the question paper.

**QUESTION ONE**

- (a) Examine four strategies that a multinational corporation could use to hedge its economic exposure. [6 Marks]
- (b) Tabitha Wanjiku specializes in forex trading. She is considering the following quote from two different banks located in different locations:

Currency Quotes	Real Bank		Safe Bank	
	Bid	Ask	Bid	Ask
Naira /KES	0.8226	0.8293	0.8361	0.8395

**Required:**

Arbitrage profit, if any, assuming Tabitha has Naira 20,000 to invest. [6 Marks]

- (c) ABC Ltd is a Kenyan based import-export company. It has an invoice, which it is due to pay on 30 June, 2021 in respect of \$350,000. The company wishes to hedge its exposure to risk using traded options and has obtained the following information from the financial

market. The current \$/KES spot rate is 1.5190 -1.5230. The contract size of KES25,000 is available.

Exercise Price (\$/KES)	June contracts	
	Calls	Put
1.45	8.95	10.20
1.50	6.80	12.40

Option quotes are given in cents per shilling (KES).

Assume that it is now the 31 March 2021 and the expected (\$/KES) spot rate on 30<sup>th</sup> June 2021 is 1.4810 – 1.4850.

**Required:**

Calculate the cash flows in respect to the payment. [6 Marks]

d. Explain three main types of foreign exchange risk exposure that are likely to affect the organization and advise the company on policies it could consider to reduce exposure to these risks. [6 Marks]

e. Generations ltd is expected to receive \$400,000 in next 3 months from a customer in the United States. The company has obtained the following information from the financial market.

	\$/KES
The current spot rate	1.8250-1.8361
Forward rates	1.8338 – 1.8452
Deposit rates (p.a) Kenya 4.5% and US 4.2%	
Borrowing rates(p.a) Kenya 5.75% and US 5.1%	

Required: Advice management on hedging strategy to adopt [6 Marks]

**QUESTION TWO:**

a. Mark limited is a Kenyan based multinational company that has affiliates in Ethiopia, Rwanda and Tanzania. The following payment matrix relates to the inter-affiliates cash flows for the month of March 2020.

	Kenya	Ethiopia	Rwanda	Tanzania
	Receipts			
Affiliate	Sh “000”	Sh “000”	Sh “000”	Sh “000”
Kenya	-	40,000	75,000	55,000
Ethiopia	8,000	-	-	22,000
Rwanda	15,000	-	-	17,000
Tanzania	11,000	25,000	9,000	-

disbursements

**Required:**

Illustrate the effect of multilateral netting on inter-group receipts and payments and determining the savings from the multilateral netting assuming that the foreign exchange cost of transferring funds is one percent of the transactions value. [14 Marks]

b. Describe the international equity markets. [6 Marks]

**QUESTION THREE:**

a. Distinguish between foreign bonds and Eurobonds. [4 Marks]

b. Heko Ltd constructed a manufacturing plant in Ghana. The construction cost 9 billion Ghanaian cedi. The Company intends to leave the plant open for three years. During the three years of operation, cedi cash flows are expected to be 3 billion cedi, 3 billion cedi, and 2 billion cedi respectively. At the end of the third year, the co. expects to sell the plant for 5 billion cedi. The company has a required rate of return of 17 percent. The current spot rate is cedi 8,700 /KES 1. It currently takes to buy one U.S dollar and the cedi is expected to depreciate by 5 percent per year.

**Required:** Advice the management [12 Marks]

**QUESTION FOUR**

a. Most developed financial markets are considered to be integrated. However, it is sometimes claimed that international financial markets are not integrated because of

various impediments to capital mobility. Briefly, explain any four impediments to capital mobility in international financial markets. [8 Marks]

- b. Baraka Ltd is a Kenya Company supplying agricultural products to Switzerland. It is 1<sup>st</sup> January 2021. The company's treasury department is currently dealing with a sale to a Swiss customer of CHF12.3 million which has been agreed with the customer to pay for the products on 30 June 2021. The treasury department intends to hedge the foreign exchange risk on this transaction and has obtained the following information from the financial market.

Exchange rates (quoted as KES/CHF)

Spot	1.0292 – 1.0309
Six months forward	1.0358 – 1.0380
Expected spot rate on 30 <sup>th</sup> June	1.0361 – 1.0381

The currency futures details are as follows:

(Contract size CHF 125,000, futures price quoted as KES Per CHF 1)

January	1.0318
March	1.0345
June	1.0369

**Required:**

Advise the firm's management

[12 Marks]

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