

MAASAI MARA UNIVERSITY

**REGULAR UNIVERSITY EXAMINATIONS**

**2015/2016 ACADEMIC YEAR**

**FOURTH YEAR SECOND SEMESTER**

**SCHOOL OF BUSINESS AND ECONOMICS**

**BACHELOR OF BUSINESS MANAGEMENT**

**COURSE CODE: BBM 415**

**COURSE TITLE: INTERNATIONAL FINANCE**

**DATE:9TH MAY 2016 TIME: 8.30AM – 10.30AM**

**INSTRUCTIONS TO CANDIDATES**

* ***Answer question ONE (compulsory) and any other THREE questions.***
* ***Question one carries 25 marks***
* ***All other questions carry 15 marks***

*This paper consists of 3 printed pages. Please turn over.*

**QUESTION ONE**  
(a) “Weak home currency is not a perfect solution to correcting a balance of trade deficit”. Discus this statement in light of international finance, paying special attention to the Kenya’s balance of payment **(8 Marks)**   
(b) XYZ Co a firm in Kenya would like to cover itself against a likely depreciation of pound sterling. The following data is given:  
Receivables of XYZ Co and Bros: £1,200,000  
Spot rate: Kshs.122/£  
Payment date: 3 months   
3 months interest rate: Kenya: 18 per cent  
UK: 5 percent  
What should the exporter do? Justify. **(7 Marks)**

(c) Define the term ‘Foreign Direct Investment’ as used in International Finance.

**(2 Marks)**  
(d) There are arguments for and against the alternative exchange rate regimes.  
 (i) Discuss two arguments for the flexible exchange rate regimes. **(4 Marks)**  
 (ii) State and briefly explain the differences between transaction and translation exposure. **(4 Marks)**

**QUESTION TWO**

(a)Given that shareholders can diversify away an individual firm’s exchange rate by investing in a variety of firms, why are firms concerned about exchange rate risk?

**(5 Marks)**

(b) Recently, Kenya Airways declared a loss of Ksh 25 billion. The media reported that part of the loss was attributed to the fact that the company transacts internationally through foreign currency. Show how this could have led to the said loss. Using illustrations, suggest the possible solutions. **(10 Marks)**

**QUESTION THREE**   
(a) A call option on US dollars with a strike price of £0.60 is purchased by a speculator for a premium of £0.06 per unit. Assume there are 50,000 units of this option contract. If the US dollar’s spot rate is £0.605 at the time the option is exercised;  
i) What is the net profit or loss per unit to the speculator if the option were to be exercised now?  **(2 Marks)**   
ii) What is the net profit or loss for one contract?  **(2 Marks)**

iii) What would the spot rate need to be at the time the option if exercised now

**(4 Marks)**

iv) What is the net profit per unit to the seller of this option if exercised now?

**(4Marks)**

b) Briefly discuss the factors that affect currency put option premiums. Illustrate.

**(3 Marks)**

**QUESTION FOUR**   
(a) Discuss any three important functions of foreign exchange markets.

**(3 Marks)**

(b) Explain the following two types of markets at work in the global economic systems;

1. Factor market **(3 Marks)**
2. Product market **(3 Marks)**

(c) Describe the role of international monetary fund in international trade and financial transactions **(6 Marks)**

**QUESTION FIVE**

(a) A French tourist arrived in Kenya with Euros 45000 in travelers cheques. He changed his traveler’s cheques into Kshs. At the spot rate of 78.140/1 Euro. The bank charged him 1%. He spent Ksh.300, 000 and left for France. He converted the outstanding amount into Euros at the sport rate of Ksh.80/1 Euro. How much money did he take home? **(5 Marks)**

(b) Explain the following types of foreign currency risk exposure:

(i) Transaction exposure **(2 Marks)**   
(ii) Translation exposure **(2 Marks)**

(c) Explain the two broad ways in which a firm can hedge against a currency transaction exposure. **(6 Marks)**