

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE IN BACHELOR OF COMMERCE

BCOM 434: INTERNATIONAL FINANCE

STREAMS:

TIME: 2 HOURS

DAY/DATE: THURSDAY 13/04/2023

2.30 P.M. –4.30 P.M.

INSTRUCTIONS**Attempt Question one and any other two questions****Do not write on this question paper****Question One**

a) Write short notes on the foreign (FX) market. (6 marks)

b) A major dealer of frontier forex market provides the following quotes:

Kenya shilling/Birr 1014.00-1015.00

ZAR/Kenya shilling 1.5200-1.6250

Required:

The ZAR/Birr bid ask cross exchange rate. (6 marks)

c) Explain any four common forms of potential risk encountered in international business environment. (6 marks)

d) RQ Ltd expects to pay £750, 000 to a supplier in the European Union in six months 'time.

The spot exchange rate is £2.349 per Kes 1 and the six months forward rate is £2.412 per

Kes.1. The following commercial interest rates (per annum) are available to the firm:

Euros 4.0% -8.0%

Kenya Shillings 2.0%-3.5 %

Required:

Advise the management of the firm on which hedging strategy to consider. (6 marks)

e) consider the following market rates:

USD/GBP 1.7019-1.7036

USD/EUR 0.9850-0.9867

EUR/GBP 1.7200-1.7300

Required:

Arbitrage profit, if any, assuming you have \$1, 000. (6 marks)

Question Two

a) Dawn Ltd, a Kenyan firm, is considering undertaking a new project in Egypt. This will require initial capital expenditure of 1, 750, 000 Egyptian Pound (EGP) with no scrap value envisaged at the end of the five-year lifespan of the project. A cash inflow before depreciation and tax of 800, 000 Egyptian Pound is expected to be generated each from the project.

The company tax will be charged in Egypt at a rate of 30%, with depreciation on a straight-line basis being an allowable deduction for tax purposes.

There is a double taxation agreement between Kenya and Egypt, which means that no tax will be payable on the project profits in Kenya.

The current EGP/0.625. Inflation rates are 3% in the Kenya and 4.5% in Egypt. A project of similar risk recently undertaken by firm in the US had a required post-tax rate of return of 10%.

Required

Advised whether the project should be implemented. (14 marks)

b) Explain any four the benefits that would accrue to an investor investing in the international equity markets (6 marks)

Question Three

a) Bidii Lt is a large company based in the Kenya that trades mainly within the country and with republic of South Africa. It has a significant amount of borrowing in Rands. Debt interest of ZAR 530, 000 is due on 31 December. The company is to hedge the risks involved in all foreign currency transactions. The current spot is KES 1.5584- 1.5590.

Prices for a KES/ZAR option on a KES securities exchange (cents per ZAR, payable on purchase of the option, contract size ZAR 31, 250) are:

Strike price (KES/ZAR)	Calls	Puts
1.56	3.00	2.16
1.57	1.32	2.85
1.58	2.12	3.14

Required: Option hedge outcome.

b) Explain what is a transaction exposure/risk and describe how it arises in a business. (6 marks)

Question Four

a) Tower Ltd, a company based in the Kenya, imports and exports to the US. On 1 March it signed two agreements, all of which are to be settled on 30 September.

- i. A sale to a US customer for KES 550, 000
- ii. A Purchase from a US supplier for \$1.5500-1.5520. The shilling futures contracts trades at \$1.4970 in March and \$1.5667 in September. The shilling futures contracts size KES 62, 500.

Required:

Demonstrate how a futures hedge could be set up and calculate the result of the futures hedges if, by 31 October, the spot market price for dollars has moved to \$1.5800-1.5820. (12 marks)

b) In any international trade transaction, credit is provided by either the supplier (exporter), the buyer (importer), one or more financial institutions, or any combination of these. Explain any four the basic methods of payment that can used to settle international transactions adopted by exporter and importer (8 marks)