BINDURA UNIVERSITY OF SCIENCE EDUCATION

FACULTY OF COMMERCE

DEPARTMENT OF ECONOMICS

MASTER OF SCIENCE DEGREE IN ECONOMICS

SPECIALISING IN FINANCIAL ECONOMICS

INTERNATIONAL FINANCE: MEC 526(1)

DURATION: 3 HOURS

INSTRUCTIONS TO CANDIDATES

1. **Answer four (4) questions**
2. **The paper carries six questions**
3. **All questions carry equal marks of 25 each**
4. **No cell-phones allowed in the examination room**
5. **Names mentioned in this paper are fictitious**

QUESTION 1

a) Despite the agenda to globalise trade activities, give strong arguments against this view. (10 marks)

b) Explain how Zimbabwe can gain from trade using the concept of Comparative Advantage as propounded by Ricardo and the Hecksher-Ohlin model. (15 marks)

[Total 25 marks]

QUESTION 2

Illustrate using COMESA and SADC trading blocs to discuss how country risk exposure has hindered success in regional trade integration in Sub Saharan Africa. (25 marks)

[Total 25 marks]

QUESTION 3

a) Explain the importance of recourse in international trade and finance. (5 marks)

b) Describe the flow of documents and flow of payments between the parties involved in a documentary collections method of international trade payments. (20 marks)

[Total 25 marks]

QUESTION 4

a) Consider the following illustrative exchange rates.

	U.S. Dollars Required to Buy One Unit of Foreign Currency
Japanese yen	0.009
Australian dollar	0.650

i. Calculate the indirect quotation for the Japanese yen and the Australian dollar. (2 marks)

ii. Calculate the two cross rates between the Japanese yen and Australian dollars. (6 marks)

iii. Assume Citrus Products can produce a litre of orange juice and ship it to Japan for \$1.75. If the firm wants a 50% mark-up on the product, what should the orange juice sell for in Japan? (3 marks)

iv. Now assume Citrus Products begins producing the same liter of orange juice in Japan. The product costs 250 yen to produce and ship to Australia, where it can be sold for 6 Australian dollars. Compute the dollar profit on the sale? (5 marks)

b) Explain the basic differences between the operation of a currency's forward market and a futures market. (6 marks)

c) Distinguish spot rates from forward rates. (3 marks)

[Total 25 marks]

QUESTION 5

a) Cray Research sold a super computer to the Max Planck Institute in Germany on credit and invoiced DM 10 million payable in six months. Currently, the six-month forward exchange rate is \$1.50/DM and the foreign exchange advisor for Cray Research predicts that the spot rate is likely to be \$1.43 in six months.

(i) What is the expected gain/loss from the forward hedging? (5 marks)

(ii) If you were the financial manager of Cray Research, would you recommend hedging this DM receivable? Justify. (5 marks)

(iii) Suppose the foreign exchange advisor predicts that the future spot rate will be the same as the forward exchange rate quoted today. Would you recommend hedging in this case? Justify.
(5 marks)

b) Explain Special Drawing Rights (SDRs). (5 marks)

c) Examine how political risk can be incorporated into the capital budgeting process of foreign investment project. (5 marks)

[Total 25 marks]

QUESTION 6

a) Explain the merits and demerits of currency convertibility to a developing country.
(10 marks)

b) Discuss causes to the international bank crisis that affected less developed countries.
(10 marks)

c) Compare and contrast transaction exposure and economic exposure. (5 marks)

[Total 25 marks]

END OF PAPER