Mid-Term Exam Fall 2004 Answer Key FINC 4521

1. The Shareholder Wealth Maximization Model
   a. combines the interests and inputs of shareholders, creditors, management, employees, and society.
   b. is being usurped by the Corporate Wealth Maximization Model as those types of MNEs dominate their global
      industry segments.
   c. clearly places shareholders as the primary stakeholder.
   d. is the dominant form of corporate management in the European-Japanese governance system.

2. The authors describe the multinational phase of globalization for a firm as one characterized by the
   a. ownership of assets and enterprises in foreign countries.
   b. potential for international competitors or suppliers even though all accounts are with domestic firms and are
      denominated in dollars.
   c. imports from foreign suppliers and exports to foreign buyers.
   d. requirement that all employees be multilingual.
   e. All of the above.

3. Systematic risk can be defined as
   a. the total risk to the firm.
   b. the risk of the individual security.
   c. the added risk that a firm’s shares bring to a diversified portfolio.
   d. the risk that can be systematically diversified away.

4. Which of the following correctly identifies exchange rate regimes from less fixed to more fixed?
   a. Independent floating, currency board arrangement, crawling pegs.
   b. Independent floating, currency board arrangement, managed float.
   c. Independent floating, crawling pegs, exchange arrangements with no separate legal tender.
   d. exchange arrangements with no separate legal tender, currency board arrangement, crawling pegs.

5. Countries with a __________ exchange rate regime allow market conditions to determine day-to-day foreign
   exchange rates, but will intervene to maintain their desired exchange rates.
   a. fixed
   b. variable
   c. managed float
   d. none of the above

6. In January 2002, the Argentine Peso changed in value from Peso1.00/$ to Peso1.40/$, thus, the Argentine Peso
   __________ against the U. S. dollar.
   a. strengthened
   b. weakened
   c. remained neutral
   d. all of the above

7. The United States currently uses a __________ exchange rate regime.
   a. crawling peg
   b. pegged
   c. floating
   d. fixed

8. List the three attributes of the “ideal” currency.
   Monetary independence, full financial integration, exchange rate stability.

9. The accounting statement that summarizes all the economic transactions between residents of the home country and
   residents of all other countries is called the
   a. balance of trade
   b. current account balance
   c. balance of payments
   d. capital account balance
   e. none of the above

10. A country experiencing a serious BOP __________ is more likely to __________ imports than otherwise.
    e. surplus; contract
    f. deficit; contract
    g. deficit; expand
    h. None of the above.

11. Which of the following is NOT part of the balance of payments account?
    a. The current account.
    b. The financial/capital account.
    c. The official reserves account.
    d. All of the above are BOP accounts.
12. In 1999 the United States posted a current account deficit of -$331 billion. The bulk of the negative value came from
   a. a net transfer deficit.
   b. an income balance deficit.
   c. a goods trade deficit.
   a. an income trade deficit

13. Significant amounts of United States Treasury issues are purchased by foreign investors, therefore the U.S. must earn
foreign currency to repay this debt.
   a. True
   b. False

14. In its approximate form the Fisher effect may be written as ____________. Where: \( i = \) the nominal rate of interest,
\( r = \) the real rate of return and \( \pi = \) the expected rate of inflation.
   a. \( i = (r)(\pi) \)
   b. \( i = r + \pi + (r)(\pi) \)
   c. \( i = r + \pi \)
   d. \( i = r + 2 \pi \)

15. (4 points) Using the Currency Trading Table, assuming parity holds, list all countries where the inflation rates are
higher than in the United States?
Table specific

16. (2 points each) Using the Currency Trading Table, answer the following.
a. How many Thai Baht can you buy for one dollar?
   Table specific
b. How many Dollars can you buy for one Thai Baht?
   Table specific

17. (2 points each) How would the following transactions affect (increase, decrease, no effect) the following U.S. Balance
of Payment accounts?
a. Publix imports wine from Australia.
   Current Account __decrease____ or Capital Account __________ or Reserve Account __________

b. An American buys a 10,000 Euro bond issued by the Italian Government.
   Current Account __________ or Capital Account __________ or Reserve Account __________

  c. Chinese parents pay for their son to study at the University of West Georgia.
   Current Account __________ or Capital Account __________ or Reserve Account __________

18. When the Russian Ruble reached the limits of the bands about its managed float targets (Ru5.70/\$ to Ru6.35/\$) in
1997, the Russian government would intervene in the markets to stabilize the Ruble. If the exchange rate approached
Ru5.70/\$ the government would _________ Rubles using foreign exchange and gold, or if the exchange rate approached
Ru6.35/\$ they would _________ Rubles.
   a. buy; sell
   b. sell; buy
   c. buy; buy
   d. sell; sell

19. Currency trading lacks profitability for large commercial and investment banks but is maintained as a service for
corporate and institutional customers.
   a. True
   b. False

20. In the foreign exchange market, ____________ seek all of their profit from exchange rate changes while
    ____________ seek to profit from simultaneous exchange rate differences in different markets.
   a. wholesalers; retailers
   b. central banks; treasuries
   c. speculators; arbitrages
   d. dealers; brokers
1. (3 points) The U.S. dollar suddenly changes in value against the euro moving from an exchange rate of $.8909/€ to $.08709/€. Thus, the dollar has ____________ by _______.
   a. appreciated; 2.30%
   b. depreciated; 2.30%
   c. appreciated; 2.24%
   d. depreciated; 2.24%

2. (3 points) A major U.S. multinational firm has forecast the Euro/dollar rate to be 1.10/$ one year hence, and an exchange rate of $1.40 for the British pound (£) in the same time period. What does this imply the companies expected rate for the Euro per pound to be in one year?
   a. 1.40Euro/£
   b. 1.40£/Euro
   c. 1.54£/Euro
   d. 1.54Euro/£

3. (3 points) If the current exchange rate is 134 Japanese yen per U.S. dollar, the price of a Big Mac hamburger in the United States is $2.99, and the price of a Big Mac hamburger in Japan is 294 yen, then other things equal, the Big Mac hamburger in Japan is ________.
   a. correctly priced
   b. under priced
   c. over priced
   d. not enough information to determine if the price is appropriate or not.

4. (6 points) Assuming no transaction costs, suppose 1 Canadian Dollar = .91 U.S. Dollars in Toronto, 1 U.S. Dollar =1.28 Euros in New York, and 1 Canadian Dollar = .77 Euros in Paris. Explain in detail how you take profitable advantage of these rates. If you started with $100,000 in U.S. Currency, how much money could you have after one round trip through the currencies?
   Convert $ to E in New York, Fly to Paris, convert E to CD, fly to Toronto, convert CD to $, fly to New York. End with $151272.73.

5. Using the Currency Trading Table, answer the following (2 points each).
   a. (2 points) How many British Pounds would be needed to buy $137,000 U.S. Dollars in 6 months?
   Table Specific
   b. (3 points )What is the cross rate between Argentinean Peso and South Korean Won?
   Table Specific
   c. (3 points) How many Argentina Peso could you buy with 2,000,000 South Korean Won?
   Table Specific
   d. (3 points) Using the Currency Trading Table, list all currencies which have inflation rates lower than the United States?
   Table Specific
   e. (3 points) Other things equal, and assuming efficient markets, if a Honda Accord costs $22,351 in the U.S. then at current exchange rates, then the Honda Accord should cost ________ in Great Britain.
   Table Specific

6. Using the Currency Trading Table, Suppose that since the table was printed that Japan and the United States have had a major disagreement on trade policy. Both countries intervened in Currency Markets and the result is that the new Yen: Dollar exchange rate to 118 Yen = $1. (3 points each).
   a. If the U.S. sold $5,000 dollars to buy yen, at the currency table spot exchange rate, how much did the intervention cost, or profit the United States?
   Table Specific
   b. If Japan sold 7,000 yen to buy dollars, at the currency table spot exchange rate, how much did the intervention cost, or profit, the Japanese government?
   Table Specific
   c. If you had correctly forecast the above result, it is possible for you to make a profit from the above information.
   Table Specific

Homework: 5% of course grade. Turn in solutions to any 10 questions and problems from Chapters 1-6.