1. The theory that suggests specialization by country can increase worldwide production is
   a. the theory of comparative advantage
   b. the theory of foreign direct investment
   c. the international Fisher effect
   d. the theory of working capital management

2. ______________ risk is measured with beta.
   a. Systematic
   b. Unsystematic
   c. International
   d. Domestic

3. If Interest rate parity holds, this ensures that the return on a hedged foreign investment will just equal the
domestic interest rate on investments of identical risk.
   a. True
   b. False

4. Portfolio diversification can eliminate 100% of risk.
   a. True
   b. False

5. From class discussions, why does the U.S. stock market have the highest return of any stock market in the
last century?
   a. The U.S. economy has experienced faster growth than other countries.
   b. The United States is riskier than other countries and therefore has higher required returns.
   c. The United States stock markets have avoided gambler’s ruin.
   d. The United States has a low correlation with other markets, producing a low beta, and therefore a
   high expected return.
   e. The above statement is false; many countries have experienced higher total stock returns in the
   past century.

6. Unsystematic risk is
   a. the remaining risk in a well-diversified portfolio.
   b. measured with beta.
   c. can be diversified away.
   d. all of the above.

7. Who is more likely to gain from investing in another country, a resident of the United States or a resident
of Algeria? Briefly explain your answer.

8. Capital markets around the world are on average less integrated today than they were 20 years ago.
   a. True
   b. False

9. __________ are certificates of ownership by a U.S. bank as a convenience to investors in lieu of the
underlying shares it holds in custody.
   a. Emerging market indexes
   b. Regional funds
   c. American depository receipts
   d. American derivative claims
10. In determining why a firm becomes multinational there are many reasons. One reason is that the firm is a market seeker. Which of the following is NOT a reason shy market seeking firms produce in foreign countries?
   a. Satisfaction of local demand in the foreign country.
   b. Satisfaction of local demand in the domestic markets.
   c. Political safety and small likelihood of government expropriation of assets.
   d. All of the above are market-seeking activities.

11. Which of the following is NOT considered to be a type of competitive advantage that may be enjoyed by an MNE?
   a. competitiveness in their home markets
   b. foreign exchange risks
   c. economies of scale
   d. economies of scope

12. Which of the following is the motivation for making foreign direct investment?
   a. knowledge seeking
   b. market seeking
   c. raw material seeking
   d. all of the above

13. The traditional financial analysis applied to projects, foreign or domestic, to determine the project’s value to the firm is called ________________.
    a. cost of capital analysis
    b. capital budgeting
    c. capital structure analysis
    d. agency theory

15. The _______ is defined as the present value of future cash flows discounted at the project’s cost of capital minus the initial net cash outlay for the project.
    a. net present value    b. equity-adjusted present value
    c. cost of capital    d. value additivity principle

16. When evaluating capital budgeting projects, which of the following would NOT necessarily be an indicator of an acceptable project?
    a. an NPV > $0
    b. an IRR > the project’s required rate of return
    c. an IRR > $0
    d. all of the above are correct indicators

17. Generally speaking, a firm wants to receive cash flows from a currency that is ___________ relative to their own, and pay out in currencies that are ___________ relative to their home currency.
    a. appreciating; depreciating
    b. depreciating; depreciating
    c. appreciating; appreciating
    d. depreciating; appreciating
Use the following information to answer questions 1 – 4.
In September 2002 a U.S. investor chooses to invest $500,000 in German equity securities at a then current spot rate of $0.95/€. At the end of one year the spot rate is $1.00/€.

1. (4 points) How many euros will the U.S. investor acquire with his initial $500,000 investment?

2. (4 points) At an average price of €60/share, how many shares of stock will the investor be able to purchase?
   a. 8750 shares  
   b. 8772 shares  
   c. 7917 shares  
   d. 7956 shares

3. (4 points) At the end of the year the investor sells his stock that now has an average price per share of €57. What is the investor's average rate of return before converting the stock back into dollars?

4. (4 points) At the end of the year the investor sells his stock that now has an average price per share of €57. What is the investor's average rate of return after converting the stock back into dollars?
   a. 0.0%  
   b. 5.0%  
   c. –5.0%  
   d. –2.0%

5. (4 points each) two countries, the United States and Italy, produce only one good, widgets. Suppose the price of widgets in the U.S is $15.40 and the price of widgets in Italy is 132,000 lira.
   a. According to the law of one price, what should the $: Lira exchange rate be?

   b. Suppose the price of widgets is expected to fall in the U.S. to $15.50 and increase to 193,000 Lira over the next year. What should the one year $: Lira forward rate be?

   c. Based on the difference between the spot and forward rates, who has the higher inflation rate? What is the differential in inflation between the Italy and the U.S.?

5. (5 points) Suppose the initial price of a French bond is FF 850, the coupon income is FF 70, the end of period bond price is FF 1,000, and the franc devalues by 6% against the dollar during the period. What was the bond’s total dollar return during the period?
6. (5 points) A Mexican buys a bond denominated in U.S. $. During the year the bond goes from $1,017 to $981. In addition the bond paid a coupon of $50. At the same time the exchange rate went from $1:9.4 pesos to $1:9.8 pesos. What was your total peso return in Percent during the year?

7. (10 points) Suppose an investor buys a share of Sony at a price of ¥38,720 at the start of the year. During the year, the investor receives a dividend of ¥500. At the end of the year, the price of Sony is ¥49,560. During the year, the exchange rate goes from ¥150 = $1 to ¥175 = $1.

a. What was the percent return in $ for an American investor?

b. What was the percent return in yen for a Japanese investor?

Homework: 5% of course grade, Turn in any 6 Questions and Problems,