BIMTECH
BIRLA INSTITUTE OF MANAGEMENT TECHNOLOGY
Excellence with Values

Programme: PGDM (International Business)

Batch: 2015-17

Trimester: 4th

PGDM (IB), 2015-17

International Financial Management

IB-401

Trimester – IV, End-Term Examination: September 2016

Time allowed: 2 hrs 30 min | Max Marks: 50

Roll No: ____________

Instruction: Students are required to write Roll No on every page of the question paper, writing anything except the Roll No will be treated as **Unfair Means.** In case of rough work please use answer sheet.

Sections	No of Questions	Marks	Marks
A	3 out of 5 (Short Questions)	5 marks each	3*5=15
B	2 out of 3 (Long Questions)	10 marks each	10*2=20
C	Compulsory Case	15 marks	15 marks
		Total	50 marks

Section A 15 Marks

There are five questions in this section. Attempt any three questions. Each question carries five marks

A1)What do you understand by foreign exchange transaction?

A2)What is the real cost of hedging payables?

A3)How would you differentiate between operating cash flows and financing cash flows?

A4)How is FASB 52 superior over FASB 8?

A5) Who are the principal users of the forward market? What are their motives?

Section B 20 Marks

There are three questions in this section. Attempt any two questions. Each question carries ten marks

B1 The following transactions (expressed in U.S. $ billions) take place during a year. Calculate the U.S. merchandise-trade, current-account, capital-account, and financial-account balances.

a. The United States exports $300 of goods and receives payment in the form of foreign demand deposits abroad.
b. The United States imports $225 of goods and pays for them by drawing down its foreign demand deposits.
c. The United States pays $15 to foreigners in dividends drawn on U.S. demand deposits here.
d. American tourists spend $30 overseas using traveler's checks drawn on U.S. banks here.
e. Americans buy foreign stocks with $60, using foreign demand deposits held abroad.
f. The U.S. government sells $45 in gold for foreign demand deposits abroad.
g. In a currency support operation, the U.S. government uses its foreign demand deposits to purchase $8 from private foreigners in the United States.

B2)The movement towards fuller convertibility of rupee will necessarily have to be gradual, sequenced and calibrated to the overall macro economic situation and emerging needs of the economy" Comment

B3)Chemex, a U.S. maker of specialty chemicals, exports 40 percent of its $600 million in annual sales: 5 percent goes to Canada and 7 percent each to Japan, Britain, Germany, France, and Italy. It incurs all its costs in U.S. dollars, while most of its export sales are priced in the local currency.

a. How is Chemex affected by exchange rate changes?
b. Distinguish between Chemex's transaction exposure and its operating exposure.
c. How can Chemex protect itself against transaction exposure?
d. What financial, marketing, and production techniques can Chemex use to protect itself against operating exposure?
e. Can Chemex eliminate its operating exposure by hedging its position every time it makes a foreign sale or by pricing all foreign sales in dollars? Why or why not?

Section C 15 marks (Compulsory)

Merck Inc. is a pharmaceutical company. It is not currently exporting its products to India. However, it is proposing to establish manufacturing facility in India in the near future.

The Company to be set up in India is to be a wholly owned affiliate of Merck Inc. which will provide all funds needed to build the manufacturing facility. Total initial investment is estimated at Rs.50, 000,000. Working capital requirement, estimated at Rs. 5,000,000, would be provided by a local financial institution at 8 per cent per annum, repayable in five equal instalments beginning on December 31 of the first year of operation. It the absence of this concessional facility, Merck would have financed these requirements by a loan from its bankers in the United States at 15 per cent per annum.

The cost of the entire manufacturing facility is to be depreciated over five years on a straight-line basis. At the end of the fifth year of operation, all remaining assets would be taken over by a public corporation to be designated by the Government of India with no compensation.

Sales, Prices and Exchange Rate Data

Sales, price and exchange rate projections are presented in Table below:

- Variable costs are Rs. 600 per unit in year 1 and are expected to rise by 15 per cent each year.
- Fixed costs (other than depreciation) are Rs. 20 million in year 1 and are expected to rise by 10 per cent per year.

Year	Sales in Units	Unit Price	Exchange Rate
1	2,00,000	Rs. 1,000	Spot rate Rs. 42.20/$

2	2,25,000	Rs. 1,500	42.50/$
3	2,50,000	Rs. 1,800	42.60/$
4	2,75,000	Rs. 2,000	42.80/$
5	3,00,000	Rs. 2,200	43.50/$

Other Information

- All profits after tax realized by the affiliate are transferable to the parent at the end of each year. Depreciation funds are to be blocked until the end of year 5. These funds may be invested in local money market instruments, yielding to a tax-free 15 per cent per annum. When the operating assents are turned over a local corporation, the balance of these funds including interest, may be repatriated.

- The income tax rate in India is 48% but there are no withholding taxes on transfer of dividends. Dividends received by Merck Inc. in the United States would be subject to a 50% per cent tax with credit allowed for taxes paid on affiliate" income abroad.

- Merck Inc. used a 14 per cent weighted average cost of capital for evaluating domestic projects similar to the ones planned in India. For foreign projects in developing countries a 6 per cent political risk premium is added.

Based on the above information, what is your advice to Merck Inc?