The Co-operative University of Kenya

END OF SEMESTER EXAMINATION – DECEMBER 2016

EXAMINATION FOR THE BACHELOR OF CO-OPERATIVE BUSINESS / BACHELOR OF COMMERCE
(BCOB YR III SEM I /BCOB YR IV SEM I / BCOM YR IV SEM I)

UNIT CODE: HCOB 2437/ HBF 2401

UNIT TITLE: INTERNATIONAL FINANCE

DATE: 8TH DECEMBER, 2016 **TIME: 2:00 PM – 4:00 PM**

INSTRUCTIONS:

- Answer question **ONE (compulsory)** and any other **TWO** questions

QUESTION ONE

(a) Discuss the criteria considered by MNCs in making international financing decisions (6 Marks)

(b) Briefly explain the key motivation behind governments encouraging MNCs to invest in their countries (4 Marks)

(c) Briefly explain how various economic factors can affect the equilibrium exchange rate of the Kenya Shilling value with respect to that of the US dollar (10 Marks)

(d) Assume that Annex Ltd, a US firm expects to receive 1 million Euros in one year. The existing spot rate of the euro is $1.20. The one year forward rate of the euro is $1.21. Annex Ltd expects the spot rate of the euro to be $1.22 in one year. Assume that one year put options on Euros are available with an exercise price of $1.23 and a premium of $0.40 per unit. Assume the following money market rates;
Required:
   i. Determine the dollar cash flows to be received if Annex uses a money market hedge (Assume Annex Ltd does not have any cash on hand) (5 Marks)
   ii. Why would Annex Ltd enter into a money market hedge? (5 Marks)

QUESTION TWO

(a) In the past the spot exchange rate of the euro was $1.20 at the time, Talent Ltd a US firm invested $4 million to establish a project in the Netherlands. It's expected that this project would generate cash flows of 3 million euros at the end of the first and second years. Talent Ltd always uses the spot rate as its forecast of future exchange rates. It uses a required rate of return of 20% on international projects
The conditions in the Netherlands were weaker than expected hence the cash flows in the first year of the project were 2 million euros. Talent Ltd now believes that the expected cash flows for the next year will be 1 million euros. A company offers to buy the project from talent Ltd today for $1.25 million. Assure no tax effects and that the spot rate of the euro is now $1.30. Should Talent Ltd accept the offer? Show your workings. (10 Marks)

(b) The management of working capital is usually complex for MNCs that have foreign subsidiaries because each subsidiary must have adequate working capital to support its operations.
   i. Briefly explain the techniques MNCs can use to optimize cash flows (4 Marks)
   ii. Briefly explain THREE (3) general complications in optimizing cash flows (6 Marks)

QUESTION THREE

(a) Managers of MNCs International portfolio investors, importers and exporters and government officials must deal with determination of exchange rates almost daily discuss the determination of exchange rates as explained by parity conditions (10 Marks)

(b) Clearly explain how each of the following may influence country risks
   i. Government involvement in business
   ii. Political and social tension in a country
   iii. Wasteful government expenditure on non-productive prestigious projects

(10 Marks)

QUESTION FOUR

(a) When a government runs short of foreign exchange and cannot obtain additional funds. It usually limits transfer of foreign exchange out of the country. Briefly explain how MNCs can transfer funds of countries having exchange or remittance restrictions. (12 Marks)

(b) Briefly explain the objectives of the government policy on taxation of foreign source income in the manufacturing and industrial sector (8 Marks)