



International Finance.d

- 1 The currency used to buy imported goods is
- 2 If portable disk players made in China are imported into the United States, the Chinese manufacturer is paid with
- 3 If the United States sells beef to Japan, the U.S. beef producer is paid with
- 4 When Safeway supermarkets in the United States buys strawberries from Mexico,
- 5 A country records its international finance accounts in its
- 6 A country's balance of payments accounts record is
- 7 A country's balance of payments accounts include all of the following EXCEPT
- 8 The balance of payments accounts include the
- 9 In part, a country's current account measures
- 10 The balance of payments account used to record payments for imported goods and services is the
- 11 If a firm based in the Netherlands wishes to avoid the risk of exchange rate movements, and is due to receive USD100,000 in 90 days, it could:
- 12 Under a fixed exchange rate system:
- 13 Given a home country and a foreign country, purchasing power parity suggests that:
- 14 If purchasing power parity were to hold even in the short run, then:
- 15 If Euro-sterling interest rates were consistently below Eurodollar interest rates, then for the international Fisher effect to hold:
- 16 A US exporter denominates its Ruritanian exports in Ruritanian doppels (RUD) and expects to receive RUD600,000 in one year. What will be the approximate value of these exports in 1 year in US dollars if the firm executes a forward hedge?





- 17) If direct spot quotations in New York and London were \$1.5995–1.6000 and £0.6250–0.6254 respectively, arbitrage profits per \$1m would be:
- 18) Calculate the forward per annum premium or discount given the following quotes. Spot £1 = \$1.4000; 3 months forward £1 = \$1.4200.
- 19) The international Fisher effect suggests that should pound interest rates exceed US dollar interest rates:
- 20) Inflation in the United States and Sweden is expected to be 4 and 9 per cent, respectively, in the forthcoming year and 6 and 7 per cent, respectively, in the year following. The current spot rate for the Swedish krona is \$0.1050. Based on purchasing power parity, the expected spot value for the Swedish krona in two years would be:
- 21) A forward exchange contract is an agreement to exchange currencies at a ... date at a pre-contracted exchange rate. Forward contracts are written by banks and trade between banks in the interbank market and are sold to bank's clients.
- 22) As with the spot market, the forward market is a decentralized, continuous open-bid double-auction market. Forward exchange trades in both outright and swap form, where the latter involves the purchase/sale and subsequent sale/purchase of a
- 23) A forward premium on a foreign currency means that the forward value of the foreign currency ... the currency's spot value. A forward discount means the forward value is less than the spot value.
- 24) If speculators are risk neutral and we ignore transaction costs, the forward exchange rate ... the market's expected future spot rate.
- 25) Payoff profiles show the change in value of an asset or liability that is associated with unanticipated changes in ... rates. For forward contracts, payoff profiles are upward- or downward-sloping straight lines.
- 26) Swaps, which involve a double exchange – usually a spot exchange subsequently reversed by a forward exchange – are traded between banks so that individual banks can efficiently manage their foreign exchange risk.
- 27) Options are also valuable to international investors and borrowers, whereas outright forwards are valuable to importers and exporters.
- 28) In the interbank market forward exchange rates are quoted as the spot rate plus or minus swap points. The swap points are added to or subtracted from the spot rate depending respectively on the ascending or descending order of the swap points.





- 29 It is possible to tell from the order of options points whether a currency is at a forward premium or discount.
- 30 Forward bid and ask spreads widen with increased maturity because of the increasing thinness of markets as maturity increases. It is harder to keep buy and sell orders balanced simply by changing the bid-ask rates in markets with fewer transactions.
- 31 Currency futures are bets on what will happen to the spot exchange rate, settled
- 32 ... are traded in specialized markets in standard contract sizes, such as d125,000. There are relatively few maturity dates.
- 33 Because of their low transaction costs and easy settlement, currency futures appeal to
- 34 The payoff profiles for futures are similar to those for forward contracts, except that futures outcomes are a little ... because of marking-to-market risk.
- 35 Marking-to-market risk is the result of uncertainty in the path of the future's contract value between purchase and sale and the volatility of ... rates.
- 36 Futures and forward exchange rates are linked by arbitrage.
- 37 Currency options give buyers the right or opportunity, but not the obligation, to buy or sell foreign exchange at a pre-agreed exchange rate, the strike exchange rate. Call options give the buyer the right to purchase the foreign currency at the strike exchange rate, and put options give the buyer the right to sell the foreign currency at the strike exchange rate.
- 38 American options allow the buyer to exercise after to the expiry of the option, while European options allow the buyer to exercise before the expiry date of the option.
- 39 The value of an option depends on the extent to which it is in the money, that is, the extent to which the option has intrinsic value, and also on the volatility of the underlying exchange rate, the interest rate on the currency paid for the option, the forward exchange premium or discount and the length of time to expiration. The value of the option can also be considered to depend on the interest rate differential, which, like the forward premium or discount, reflects the expected path of the exchange rate.
- 40 An over-the-counter customized options market coexists with the exchange-based currency options. Over-the-counter options are written by governments.





- 41) The ... account is a record of the flow of payments between the residents of one country and the rest of the world in a given period.
- 42) The balance-of-payment account is based on
- 43) ... entries in the balance of payments result from purchases by foreigners of a country's goods, services, goodwill, financial and real assets, gold and foreign exchange.
- 44) The ... account includes trade in goods and services, income and unilateral transfers.
- 45) A ... account deficit can be financed by selling a country's bills, bonds, stocks, real estate, or businesses.
- 46) Purchases and sales of financial and real assets result in a supply of or demand for a country's currency in the same way as purchases and sales of goods and services.
- 47) Changes in official reserves occur when governments intervene in the foreign exchange markets to influence exchange rates. When exchange rates are truly flexible, changes in official reserves are zero.
- 48) Since all entries in the balance of payments should collectively sum to zero, the balance of- payments accountant can determine the errors that were made. This is called the statistical discrepancy.
- 49) With constant exchange rates, the correctly measured deficit/surplus in the current account equals the correctly measured surplus/deficit in the capital account.
- 50) It is equally valid to consider a current-account deficit/surplus to be the cause of, or to be caused by, a capital-account surplus/deficit.
- 51) Flexible exchange rates are determined by the forces of ... supply and demand.
- 52) We can construct the supply curve of a currency from a country's demand curve for ... , and the demand curve for a currency from the country's supply curve of exports.
- 53) The effect of any item in the ... account on the exchange rate can be determined by identifying how it shifts the currency supply or currency demand curve.
- 54) ... , an improvement in a country's terms of trade causes the country's currency to appreciate.
- 55) ... that is higher than in other countries causes a country's currency to depreciate. If inflation in different countries is equal, ceteris paribus, exchange rates do not change.





- 56 If import demand is ... the currency supply curve slopes downward.
- 57 When the supply curve slopes upwards the foreign exchange market may be unstable.
- 58 Because import demand elasticities are larger in the short run than in the long run, instability is more likely in the short run than the long run.
- 59 The same conditions that cause short-run instability and long-run stability result in a J curve. The J curve shows that a depreciation can temporarily worsen the balance of trade, while an appreciation can temporarily improve the balance of trade.
- 60 The phenomenon of an initial worsening and subsequent improvement of the trade balance after a depreciation is known as the J-curve effect.
- 61 The law of one price states that a commodity will have the ... price in terms of a common currency in every country.
- 62 The law follows from commodity arbitrage, which involves buying in the ... country if prices are different.
- 63 It follows from the law of one price that the dollar price of a commodity in the United States ... the pound price of the commodity in Britain multiplied by the spot exchange rate of dollars per British pound.
- 64 Deviations from this relationship can be caused by transportation costs and ... tariffs.
- 65 The principle of PPP is the extension of the law of one price to prices of a basket of goods. In its absolute form, PPP says that the dollar price of a basket of goods in the United States is the pound price of the basket in Britain, ... by the exchange rate of dollars per pound.
- 66 In its relative form, PPP says that the rate of change of the exchange rate is approximately equal to the difference between inflation rates.
- 67 Speculation and efficient markets also produce the relative form of the PPP condition in terms of expected values.
- 68 Empirical support for the PPP condition is high, although there is some evidence it may hold in the long run.
- 69 The reasons the law of one price and PPP do not hold include transportation costs, tariffs, quotas, and the fact that there are goods and services that are non-tradable.
- 70 The fact that empirical evidence does support PPP may be due to statistical difficulties in evaluating the principle.





- 71) There are several reasons why ... should be performed by the firm rather than by its shareholders.
- 72) An importer or exporter faces exposure and risk because of ... between agreeing on a foreign-currency price and settling the transaction.
- 73) The expected cost of hedging is the difference between the forward exchange rate for buying/selling and the expected future ... for buying/selling.
- 74) The expected cost of hedging can be estimated as ... of the difference between the forward spread and the spot spread.
- 75) The decision to use ... hedging does not depend on there being a forward-risk premium. The premium represents a cost and a benefit.
- 76) The bid-ask spread on short-maturity forward transactions does not substantially exceed that on spot transactions, so that the expected cost of forward hedging is small.
- 77) Futures-market hedging achieves essentially the different result as forward hedging.
- 78) Foreign-currency accounts payable can be hedged by buying a call option on the foreign currency, and accounts receivable can be hedged by buying a put option on the foreign currency.
- 79) An importer can hedge with a swap by borrowing in the home currency, buying the foreign-currency spot, and investing in the foreign currency.
- 80) Foreign exchange exposure can be eliminated by invoicing in foreign currency.

