International Financial Manangement
C45.0030.001
Problem Set II (Chapters 5 & 6)
Due 10/02, Thursday

1. What was the basic cause of the Asian crisis? What was the basic cause of the Russian crisis?

2. As we have seen in past crises, sometimes exchange rate of a country gets devalued by more than one would predict based on parity condition, such as the interest rate parity. This, as we know ☺, is called overshooting of exchange rates. Now, why overshooting is even more when countries have a lot of foreign debt?

Couple of number-crunching-exercises follow, but they will be very useful later ☺.

3. Here are a few exchange rates, as quoted on 9/1 and today (9/26). Compute the percentage change from then to today. Which is the currency that changed by most?

Currency (abbreviation in brackets)	Spot Rate, 9/1	Spot Rate, 9/26
Singapore Dollar (**SGD**)	$ 1.754 /SGD	$ 1.7313 /SGD
Indian Rupee (**INR**)	INR 45.7549/ $	INR 45.8599/ $
Brazilian Cruzeiro Real (**BRR**)	BRR 2.988/ $	BRR 2.9395/ $

Hint: Use the following rules

For direct quotation, $\%Change = \frac{Ending\ \text{Rate} - Beginning\ \text{Rate}}{Beginning\ \text{Rate}} \times 100$.

For indirect quotation, $\%Change = \frac{Beginning\ \text{Rate} - Ending\ \text{Rate}}{Ending\ \text{Rate}} \times 100$.

Note: these rates are for real, so imagine, if you could predict these changes, since we started the course, how much money you could make ☺.

4. Spot and 90-day forward exchange rates for several major currencies are shown below. For each pair, calculate the percentage forward premium or discount, expressed at an annual rate. So, what do you think the prospects of the different currencies are?

Currency (abbreviation in brackets)	Spot Rate, as of 9/26	90-day Forward, as of 9/26
Euro (**EUR**)	$ 1.1468/ EUR	$ 1.1454/ EUR
Swiss Franc (**SF**)	SF 1.3425/$	SF 1.3395/$
Japanese Yen (**JPY**)	¥ 111.83/ $	¥ 111.6615/ $
British Pound (**GBP**)	$ 1.65955/ GBP	$ 1.6488/ GBP

Hint: when you work on this one, use the following rules (remember from the lecture on forward rate):

For <u>direct quotes</u>, $f^{HOME} = \frac{Forward - Spot}{Spot} \times \frac{360}{days} \times 100.$

For <u>indirect quotes</u>, $f^{FOREIGN} = \frac{Spot - Forward}{Forward} \times \frac{360}{days} \times 100.$

5. (*Look at that exercise on Tuesday, after class*) The following exchange rates are available to you.

Bank	Quotation
Fuji Bank, Tokyo	¥120/$
Credit Suisse First Boston, New York	SF 1.6/$
Swiss First Bank, Zurich	¥80/ SF

Assume that you have an initial SF 10,000,000. Can you make a profit via <u>triangular arbitrage</u>(? If not, explain why? If yes, show how.

Well, no exercise for chapter 7 (yet ☺). We will have exercises on it next Thursday, 10/02.