AFM/SFM Test-1

Mission 80+ in AFM/SFM for Nov/Dec 2024 attempt

Time Allowed – 60 Min

Maximum Marks - 30

All Questions are Compulsory.

Working Notes should form part of the respective answer.

PART I – Case Scenario based MCQs (9 Marks)

In our CA Final AFM paper / CMA Final SFM Paper conducted by Institute, it is not required to show the working for MCQs. However, for our test series, we highly recommend that students provide detailed workings. This allows us to better evaluate your preparation and understanding of the concepts.

Case Scenario I:

An exporter is a UK based company. Invoice amount is $2,50,000. Credit period is three months. Exchange rates in London are:

Spot Rate ($/£) 1.5865 – 1.5905

3-month Forward Rate ($/£) 1.6050 – 1.6102

Rates of interest in Money Market:

	Deposit	Loan
$	7%	9%
£	5%	8%

(i) Whether a money market hedge is possible? **1 Mark**

(a) No

(b) Yes, by borrowing Invoice amount in US Money Market

(c) Yes, by depositing PV of invoice amount in US Money Market

(d) Yes, by borrowing PV of Invoice amount in US Money Market

(ii) Inflow under Money Market Hedge (MMH) will be **2 Marks**

(a) £ 1,53,724 (b) £ 2,44,499

(c) £ 1,55,646 (d) £ 1,51,415

(iii) What should be the depositing rate prevailing in UK market, so that Inflow from MMH will be equal to Inflow under Forward contract? **2 Marks**

(a) 4.5% (b) 5.5%

(c) 4% (d) None

Case Scenario: II

The following 2-way quotes appear in the foreign exchange market:

Spot Rate: ₹/US $ ₹83.25/₹83.75

6m Swap point: **75/50**

(i) How many Rupees is the firm required to pay to obtain US $ 2,00,000 after 6 months? **2 Marks**

(a) ₹1,68,50,000 (b) ₹1,67,50,000
(c) ₹1,66,50,000 (d) ₹1,65,00,000

(ii) Assume the firm has US $ 69,000 invested in US Market. ROI on US $ investment is 2%.
Firm can either encash the US$ now or 6 months later.
Assuming that after encashing $ into Rupee, Rupee will remain idle in current account earning no interest. **2 Marks**

(a) Encash US $ into Rupee now.
(b) Encash US $ into Rupee after 6 months.
(c) both (a) and (b) will be at indifference
(d) None

PART II – Descriptive Questions (21 Marks)

1. (i) The rate of inflation in India is 8% per annum and in the U.S.A., it is 4%. The current spot rate for USD in India (₹/US $) is 83.50. What will be the expected rate after 3 years applying the Purchasing Power Parity Theory. **6**

(ii) On April 1, 3 months interest rate in the UK £ and US $ are 3.5% and 7.5% per annum respectively. The UK £/US $ spot rate is 0.7570. What would be the forward rate for US $ for delivery on 30th June?

2. A company is considering hedging its foreign exchange risk. It has made a purchase on 1st July 2024 for which it has to make a payment of US$ 80,000 on December 31, 2024. The present exchange rate is 1 US $ = ₹75. It can purchase forward 1 $ at ₹74. The company will have to make an upfront premium @ 2% of the forward amount purchased. The cost of funds to the company is 12% per annum. **8**

In the following situations, compute the profit/loss the company will make if it hedges its foreign exchange risk with the exchange rate on 31st December 2024 as:

(i) ₹78 per US $.

(ii) ₹72 per US $.

3. Pioneer Limited has imported 15000 bottles of shampoo at landed cost in Mumbai, of US $ 25 each. The company has the choice for paying for the goods immediately or in 3 months' time. It has a clean overdraft limited where 15% p.a. rate of interest is charged. **7**

Calculate which of the following method would be cheaper to Pioneer Limited.

(i) Pay in 3 months' time with interest @ 12% p.a. and cover risk forward for 3 months.

(ii) Settle now at a current spot rate and pay interest of the overdraft for 3 months.

The rates are as follows:

Mumbai ₹ /$ spot : 60.25-60.55

3 months swap points : 35/55