QUESTION – 61

An Indian Exporter is to receive € 200000 after 1 month. The customer is requesting a total period of 3 months. The Indian exporter is planning to allow additional 2 months to the foreign party at an interest of 6% p.a.

H.W

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1 month FR € 1 = ₹ 56.70 – 57.20

3 month FR € 1 = ₹ 57.80 – 58.45

The rate of interest is Indian deposit rate is 14% p.a. for ₹ deposit made for 2 months.

Advise the exporter as to whether he should receive at the end of 1 month or at end of 3 month.

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EXAMPLE – 68

Payable = \$ 3,00,000

Receivable = \$ 2,00,000

Exchange Rate (3 months FR)

₹/\$ = 70.50/71.75

Calculate cash flows at the end of 3rd month

(i) Without Netting.

(ii) With Netting.

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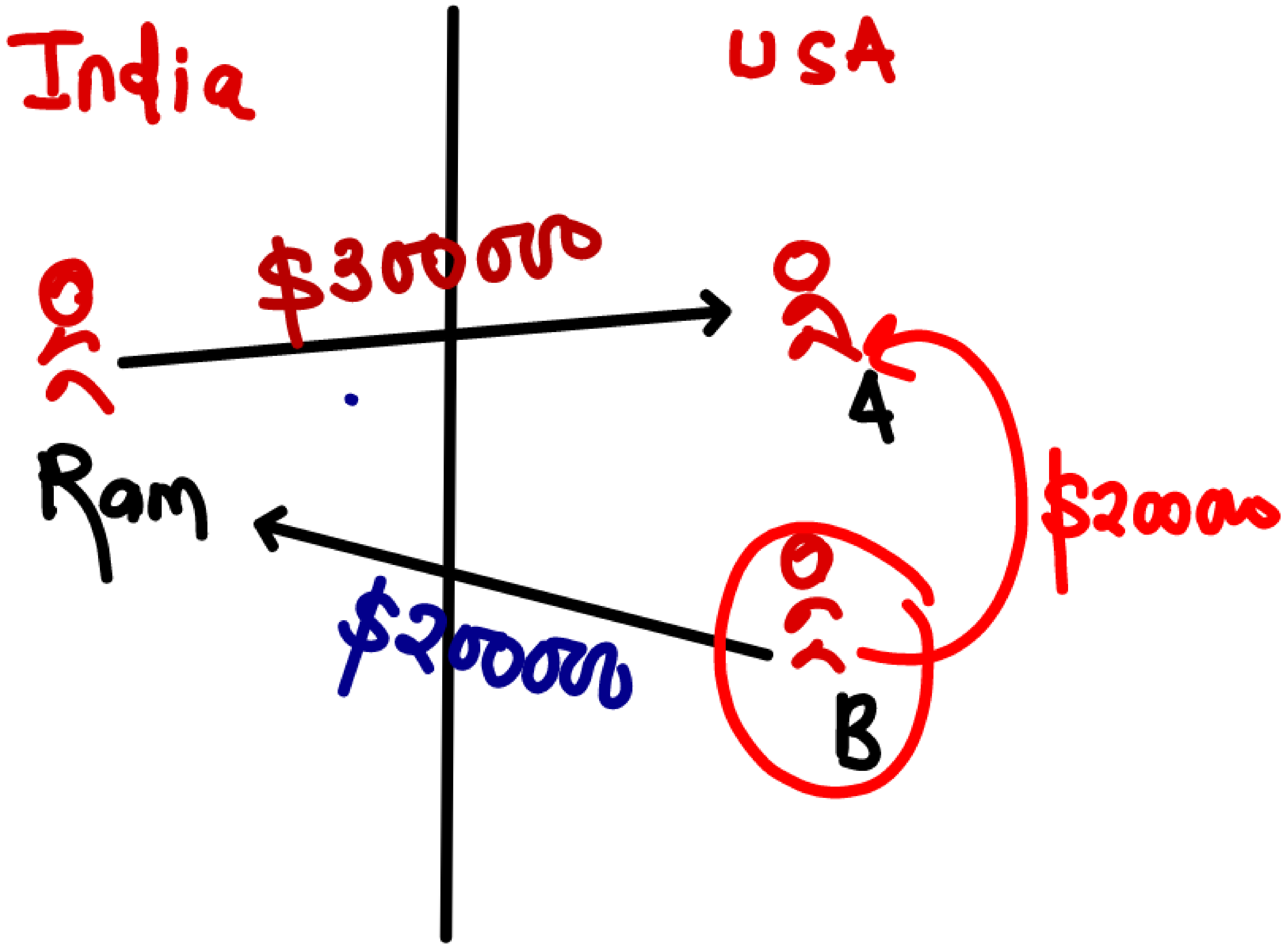

Cash flows

Without Netting

Buy \$ 300000 at ₹ 71.75 = (21525000)

Sell \$ 200000 at ₹ 70.50 = 14100000

Net Cash Outflows = ₹ 7425000

With Netting

Buy Net \$ payable i.e. \$100000 at FR

\$100000 × 71.75 = ₹ 7175000

Netting is better due to lower C.O.

Money Market Cover

1. Money Market Hedge for Importer
2. Money Market Hedge for Exporter

EXAMPLE – 69

Import from USA & $ 1,03,000 payable after 3 months.

Interest Rate

India	= 15%/16%
USA	= 12%/13%
SR ₹/$	= 70/71
3 months FR ₹/$	= 72/73

Which option is better

(i) Money market cover.

(ii) Forward cover

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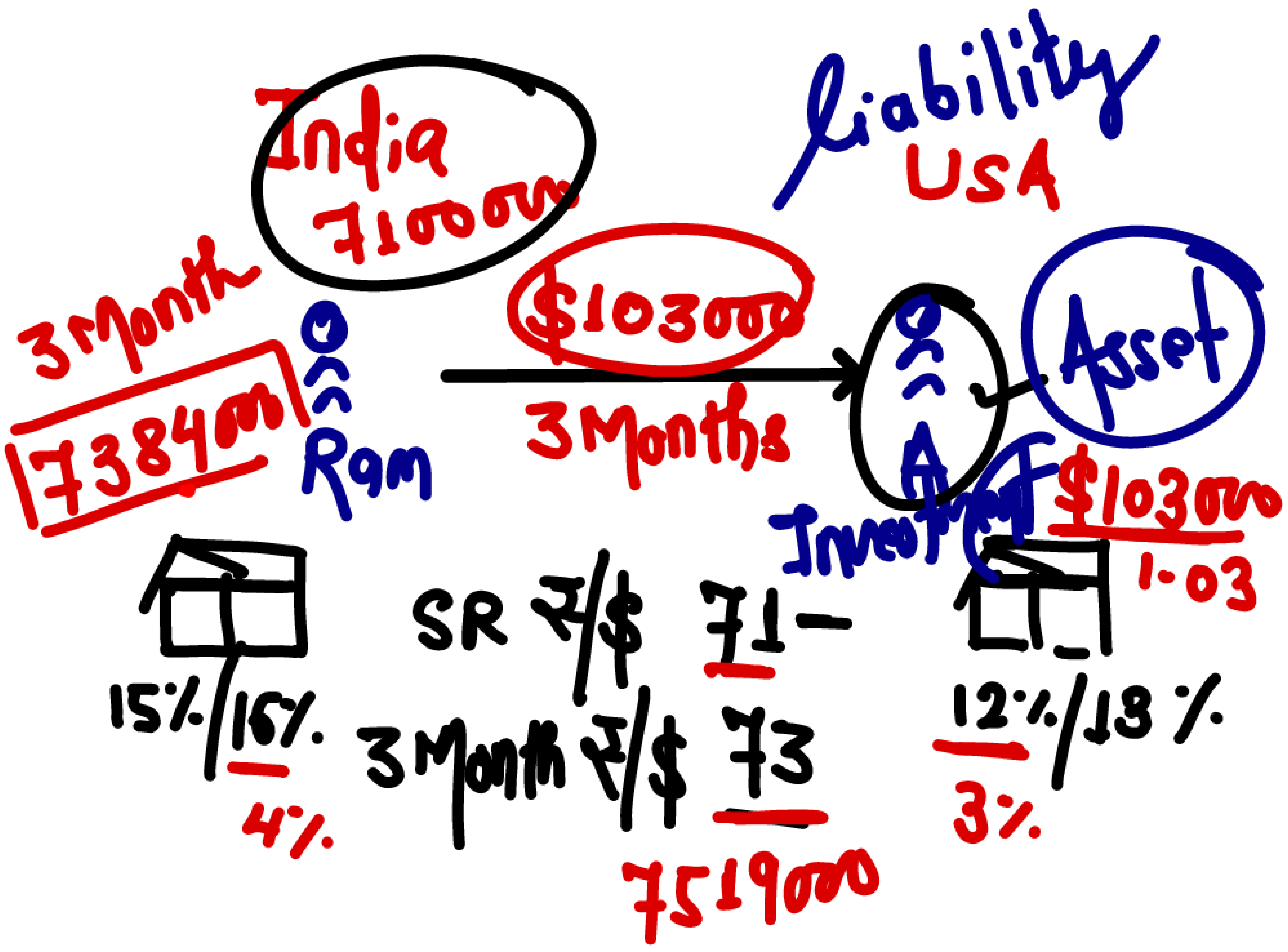

Option 1 Money Market Cover

Step 1 Calculation of Amount to be invested in US money market @ 12% p.a. for 3 months

$$Amt = \frac{\$103000}{1.03} = \$100000$$

Step 2 Rupees required to buy \$100000 at SR

$$\$100000 \times 71 = ₹7100000$$

Step 3 Borrow ₹7100000 from Indian money market @ 16% p.a. for 3 months

$$\text{Cash outflows} = 7100000(1.04) = ₹7384000$$

option 2 forward Cover

Cash outflows: $\$103000 \times 73$

$= ₹75{,}19000$

Money Market is better due to Lower Cash outflows

EXAMPLE – 70

Export to USA & $ 1,06,000 receivable after 6 months

Interest Rate

India	= 8%/10%
USA	= 10%/12%
SR ₹/$	= 70/71

6 months FR ₹/$ = 68/69

Which option is better

(i) Money market cover.

(ii) Forward cover.

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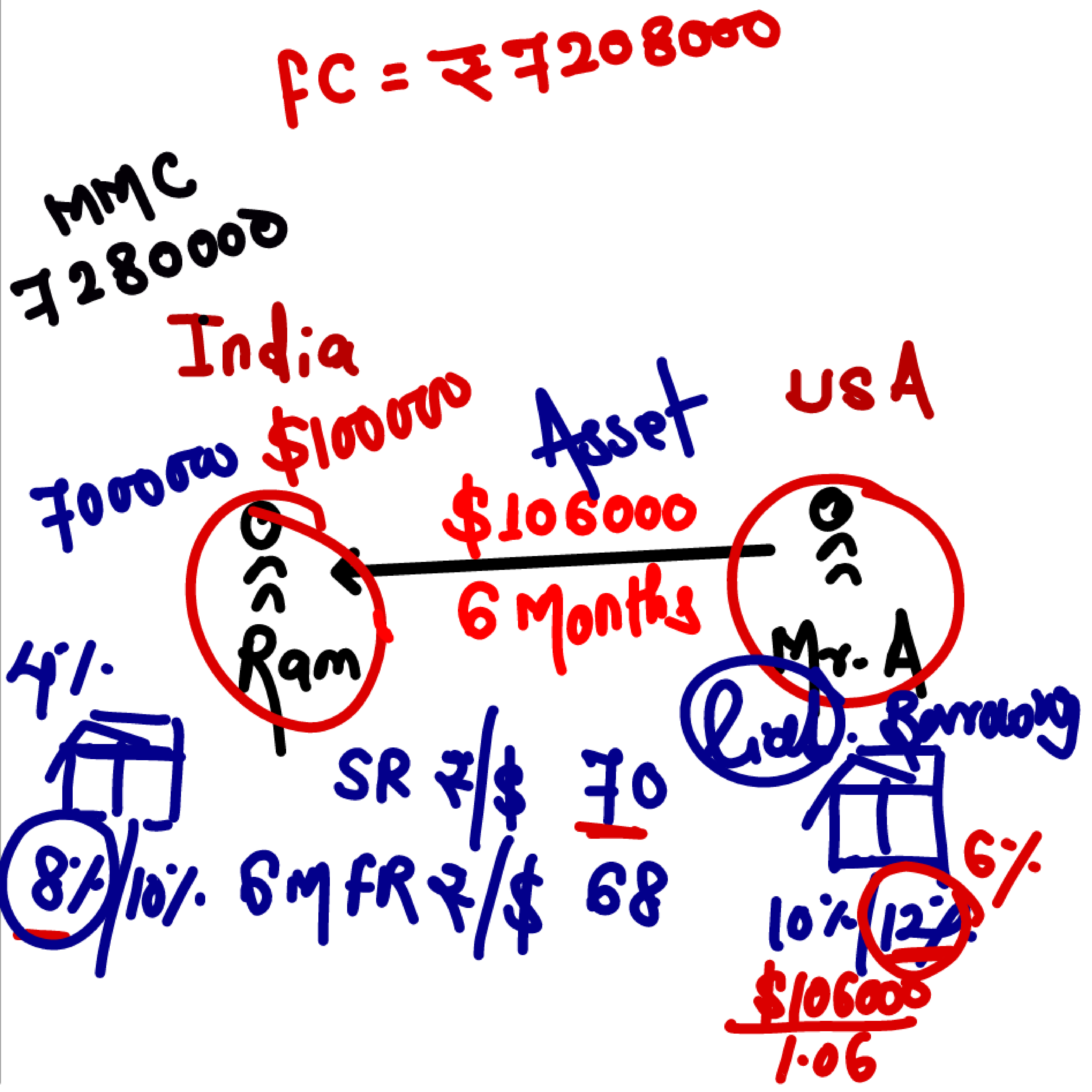

Option 1 Money Market Cover

Step 1 Borrowing Amount from US money market
@ 12% p.a. for 6 Months

$$\frac{\$106000}{1.06} = \$100000$$

Step 2 Sell \$100000 at SR

$$\$100000 \times 70 = ₹7000000$$

Step 3 Invest ₹7000000 in Indian money market
@ 8% p.a. for 6 Months

Cash Inflows = 7000000 × 1.04 = ₹7280000

Option 2 Forward Cover

Cash Inflows = $106000 × 68 = ₹7208000

MMC is better due to Higher Cash Inflows.

- If payable है means liability है तो Asset creat करना होगा means Investment.
- If Receivables है means Asset है तो liab. creat करना होगा means Borrowing.