

Seminar 10

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International Finance

Problem solving

You were recently hired by the Doolittle Corporation corporate treasury to help oversee its expansion into Europe. Blake Francis, the CFO, wants to hire a foreign exchange forecasting company. Blake has asked you to evaluate three different companies, and he has obtained information on their past performances. Out of a total of 50 forecasts for the \$/€ rate, the companies reported the number of times they correctly forecast appreciations and depreciations:

There are a total of 35 dollar appreciations (down periods) and 15 dollar depreciations (up periods) in the sample. Blake wants to know two things:

- **Can anything be said about the companies' forecasting ability with the available data?**
- **What additional information should Blake try to obtain in order to form a better judgment?**

	Correct Down Forecasts	Correct Up Forecasts
Morrissey Forex Advisors	20	5
Pixie Exchange Land	20	4
FOREX Cures	12	12

Problem solving

Assume a bond with a price equal to \$92 (per \$100 par value).

Assume that the coupon rate is 7%, that the bond has only 2 years to go, and that the one-year and two-year U.S. dollar interest rates are 5%.

- What is the probability of country default (p)?

Problem solving

The following interest rates were available. The latter two rates were offered by Argentine banks.

- What risk does the difference between the 7.10% dollar interest and 3.25% LIBOR reflect?

In February 1994, Argentina's currency board was in place, and 1 peso was exchangeable into 1 dollar.

- What risk does the difference between the rate on 90-day pesos and 90-day dollar deposits by Argentine banks reflect?

U.S. LIBOR 90 days:	3.25%
Peso 90-day deposits:	8.99%
Dollar interest rate in Argentina, 90-day deposits:	7.10%

Country Risk

- GOVIES RISK
 - CDS and Default Probabilities
- Economic Monitor (EM)
 - Find the most important economic events for this week, what is their impact on FX