



University of Sri Jayewardenepura
Faculty of Humanities and Social Sciences

Bachelor of Arts Third Year Second Semester Examination – January/March, 2019

Economics

ECON 3230.03 – International Finance

Time: Three (03) hours

Answer **Five (05)** questions only.

Legible handwriting is expected.

1. a) Explain the new structure of Balance of Payments. (10 marks)

- b) “The Balance of Payment represents the strength of domestic economy of a country”
Explain. (10 marks)

2. a) How do you identify the functions of a foreign exchange market? Explain. (07 marks)

- b) Using diagrams, explain how foreign exchange rate is determined. (08 marks)

- c) Examine the necessity of a foreign exchange rate. (05 marks)

3. a) Describe how the differences of Fixed and Flexible exchange rates policies are identified?. (12 marks)

- b) Briefly explain Forward Prime and Forward Discount? Which one is the most important one to a speculator? Explain. (08 marks)

4. a) What are the strategies used to minimize the foreign exchange risk? Briefly explain.

(06 marks)

b) A 100 USA dollar worth goods are imported by a Sri Lankan importer under a 03 month forward agreement (suppose forward rate is 1:110). If spot rate is 1:100 in the maturity of the agreement;

i). Explain the nature of the foreign exchange risk. (03 marks)

ii). Explain the primary strategy the importer can take to minimize the foreign exchange risk.

(05 marks)

iii). Can the importer use "Hedging" to minimize exchange risk? Explain.

(06 marks)

5. a) "The theory of Purchasing Power Parity presents a practical idea regarding the exchange rate determination" Do you agree? Give reasons.

(06 marks)

b) What is meant by exchange rate overshooting? Explain using diagrams.

(07 marks)

c) Prove that exchange rate highly depreciates, if the elasticity of exchange market is relatively low under a flexible exchange rate policy.

(07 marks)

6. a) Introduce the balance of payment curve, and explain the determinants of its slope.

(10 marks)

b) "When external capital inflows are not perfectly sensitive to the interest, expansionary monetary policy becomes more efficient" Examine this statement using diagrams.

(10 marks)
