Quiz For Lecture # 13

Hedge a Swiss watches transaction

Use the following information below to answer questions a through g: [1]

An American importer places an order with a Swiss watch manufacturer. The order, to be delivered in August, is value at 2`000`000 Swiss Francs. The cash price for the franc is $ .5975 and September futures are trading at $ .5715.

(<u>Reminder</u>: Showing the *essential* steps along the way will enhance your chances of partial credit in case you make an error.)

1a. (3 pts) The total value of the order on the day it is pace is:

a $ 2`000`000
b $ 1`195`000
c $ 1`143`000
d non of the above

1b. (3 pts) The most effective hedge for the importer would be:

a Buy Swiss francs in the cash market and sell Swiss franc futures.
b Sell Swiss francs in the cash market and buy Swiss franc futures.
c Buy Swiss franc futures.
d Sell Swiss franc futures.

1c. (3 pts) If the importer were to take a position in the futures market, and the Swiss franc contract size is 125`000, he would take a position of

a 4 contracts
b 6 contracts
c 8 contracts
d 16 contracts

1d. (3 pts) On the day the watches are delivered, the cash market price of the Swiss franc is $ .6135 and September futures are $ .5855. If the importer did not take any action in the futures market when he place the order, it would now cost him:

a $ 2`000`000
b $ 1`227`000
c $ 1`195`000
d $ 1`169`000

[1] This question is taken from a former final exam. It was worth 25% of the entire final exam.

1e. (3 pts) If the importer did not take any action in the cash or futures market on the day he placed the order, his cost would be:

a the same
b increased by $ 32`000
c decreased by $ 32`000
d non of the above

1f. (3 pts) If the importer hedged his position, his net result on the hedge would be:

a a profit of .016
b a loss of .016
c a profit of .002
d a loss of .002

1g. (3 pts) If the importer had hedged when he placed the order, his net cost would have:

a increased by $ 9`000
b decreased by $ 17`000
c increased by $ 4`000
d decreased by $ 4`000

1h. (4 pts) As a result of the change in the cash and futures prices, how was the importer's hedge affected?

a. a favorable change from 0.026 under to 0.028 under
b. a favorable change from 0.026 over to 0.028 over
c. an adverse change from 0.026 under to 0.028 under
d. an adverse change from 0.026 over to 0.028 over