

- \_\_\_\_1. Interbank interest rates in various cities around the world are often the basis for interest rates in contractual loan agreements. What is the most important of these rates?
- London Interbank Offer Rate (LIBOR)**
  - Frankfurt Interbank Offer Rate (FIBOR)
  - Hong Kong Interbank Offer Rate (HIBOR)
  - Euro Interbank Offer Rate (EURIBOR)
- \_\_\_\_2. If  $F_t$  is the forward exchange rate (forward price of foreign currency),  $S_t$  is the spot exchange rate,  $i_t$  is the domestic interest rate, and  $i_t^*$  is the foreign interest rate, what do we call the relationship expressed as  $F_t = S_t \frac{1+i_t}{1+i_t^*}$  ?
- Purchasing power parity
  - Covered interest rate parity**
  - Domestic and foreign interest rates
  - Spot and forward exchange rates
- \_\_\_\_3. Which one of the following would be the most logical reason to use a synthetic forward contract to hedge?
- forward contracts are not available in the currency of choice**
  - when time horizons are short, forward contracts can be expensive
  - forward contracts are too risky
  - the underlying transaction gives you an asset
- \_\_\_\_4. The spot rate on the euro is \$1.39 and the 180-day forward rate is \$1.40. The difference between the spot and forward rates means that \_\_\_\_\_.
- interest rates are higher in the U.S. than in the Europe.**
  - the euro has risen in relation to the dollar.
  - the inflation rate in the Europe is rising.
  - the euro is expected to fall in value relative to the dollar.
- \_\_\_\_5. If annualized interest rates in the U.S. and Switzerland are 10% and 4%, respectively, and the 360-day forward rate for the Swiss franc is \$.3864, at what current spot rate will interest rate parity hold?
- \$.3902
  - \$.4087
  - \$.4188
  - \$.3653**

- \_\_\_6. Suppose uncovered interest parity and covered interest parity both hold. Which of these statements is true? (Assume the exchange rate,  $S_t$ , and the forward rate,  $F_t$  are expressed as dollars per euro (that is,  $\$/\text{€}$ .)
- $E_t(S_{t+1}) = F_t$
  - $E_t(S_{t+1})(1 + i_t(\text{€})) = F_t(1 + i_t(\$))$
  - $E_t(S_{t+1})(1 + i_t(\$)) = F_t(1 + i_t(\text{€}))$
  - $E_t(S_{t+1}) = 0$
- \_\_\_7. The risk that is associated with an asset's return arising from the covariance of the return with the return on a large, well-diversified portfolio is known as \_\_\_\_\_ risk.
- business
  - exchange rate
  - market
  - systematic***
- \_\_\_8. If the expected  $\$/\text{€}$  exchange rate one year from today is \$1.40, and the 360-day forward rate is \$1.35, an investor expects to make a profit by
- contracting to buy euros on the forward market and planning to sell dollars on the spot market in one year.***
  - contracting to sell euros on the forward market and planning to buy dollars on the spot market in one year.
  - buying euros on the spot market and using them to purchase a Ferrari
  - none of the above.
- \_\_\_9. Suppose uncovered interest parity holds. If the U.S. dollar interest rate exceeds British pound interest rate, the market expects
- the dollar will depreciate against the pound.***
  - the dollar will appreciate against the pound.
  - there are expected dollar profits from foreign exchange speculation.
  - the exchange rate will not change.