



## ASSIGNMENT MEMORANDUM

**SUBJECT : FINANCE AND PAYMENTS II (FP2)**

**ASSIGNMENT : 1<sup>st</sup> SEMESTER 2010**

### QUESTION 1 [40]

**STUDY UNITS 2 & 3, pp. 23-63**

#### 1.1 Foreign exchange contracts

	<b>FEC 04</b>		<b>FEC 05</b>
Spot rate 31/5	7,2205	Spot rate 31/5	7,2205
3 mths fwd pts	+ 835	4 mths fwd pts	+ 1095
Forward rate (2)	7,3040	Forward rate (2)	7,3300

FEC No.	USD amount	Value date	Forward rate	ZAR amount
01	35,000	June 30	7,3590	257,565 (1)
02	48,000	July 31	7,4450	357,360 (1)
03	67,000	August 31	7,3830	494,661 (1)
04	28,000	August 31	7,3040	204,512 (1)
05	19,000	September 30	7,3300	139,270 (1)

#### 1.2 Extension

Description	Value date	Debit	Credit
Bank takes delivery of USD 35,000 under FEC 01 at 7,3590	30 June		257,565 (3)
Bank sells USD 35,000 at spot mid-rate 7,1503	30 June	250,261	(3)
Bank buys USD 35,000 forward for one month			
Spot mid-rate 30/6		7,1503	
1 mth fwd pts		+ 280	
Fwd rate	31 July	7,1783	
		251,241 (5)	
		250,261	508,806
			250,261
Net credit			258,545 (2)

**Comments (2)**

30 June: The company experiences a positive cash flow of ZAR 7,304 (ZAR 257,565 – ZAR 250,261).

31 July: The net result of this extension to the contract realises a net credit of ZAR 258,545 instead of ZAR 257,565 under the original contract, that is, a gain of ZAR 980.

**1.3 Early delivery**

Description	Value date	Debit	Credit
Bank buys USD 67,000 at spot mid-rate 7,2790	31 July		487,693 (3)
Bank sells USD 67,000 1 month forward			
Spot mid-rate 31/7		7,2790	
1 mth fwd pts		+ 335	
Fwd rate	31 August	7,3125	489,938 (5)
Bank takes delivery of USD 67,000 under FEC 03 at 7,3830	31 August		494,661 (3)
		489,938	982,354
			489,938
Net credit			492,416 (2)

**Comments (3)**

31 August: The positive cash flow is ZAR 4,723, being the difference between the original contract and the neutralising swap contract (ZAR 494,661 – ZAR 489,938).

31 August:

Overall, the company experiences positive cash flow but receives less money. In terms of the original contract, they expected to receive ZAR 494,661 but realised a net credit of ZAR 492,416 or ZAR 2,245 less.

**QUESTION 2****[20]****STUDY UNITS 2 & 3, pp. 23-63**

2.1

EUR/ZAR	$\frac{7,1757 - 7,3517}{7,1757}$	x	$\frac{365}{90}$	x	100	=	<b>9,95% p.a.</b>
	$\frac{7,4990 - 7,6860}{7,4990}$	x	$\frac{365}{90}$	x	100	=	<b>10,11% p.a.</b>
ZAR/AUD	$\frac{0,1658 - 0,1613}{0,1658}$	x	$\frac{365}{90}$	x	100	=	<b>11,01% p.a.</b>
	$\frac{0,1662 - 0,1618}{0,1662}$	x	$\frac{365}{90}$	x	100	=	<b>10,74% p.a.</b>

$$\begin{array}{l}
 \text{ZAR/CHF} \quad \frac{0,1748 - 0,1694}{0,1748} \times \frac{360}{90} \times 100 = \mathbf{12,36\% \text{ p.a.}} \\
 \\
 \frac{0,1826 - 0,1772}{0,1826} \times \frac{360}{90} \times 100 = \mathbf{11,83\% \text{ p.a.}} \\
 \\
 \text{ZAR/JPY} \quad \frac{16,2380 - 15,6698}{16,2380} \times \frac{360}{90} \times 100 = \mathbf{14,00\% \text{ p.a.}} \\
 \\
 \frac{16,9227 - 16,4585}{16,9227} \times \frac{360}{90} \times 100 = \mathbf{10,97\% \text{ p.a.}} \\
 \\
 \text{GBP/ZAR} \quad \frac{14,2977 - 14,6944}{14,2977} \times \frac{365}{90} \times 100 = \mathbf{11,25\% \text{ p.a.}} \\
 \\
 \frac{14,7759 - 15,2034}{14,7759} \times \frac{365}{90} \times 100 = \mathbf{11,73\% \text{ p.a.}}
 \end{array}$$

(10)

## 2.2

## 1. Calculation of forward rate as follows:

Spot rate USD/CHF	1,2184	1,2194	
3-month forward points (discount)	+ 14	+ 16	(3)
Forward rate	1,2198	1,2210	
Spot rate USD/ZAR	7,2850	7,3265	
3-month forward points (discount)	+ 845	+ 915	(3)
Forward rate	7,3695	7,4180	

## 2. Calculation of forward cross rates as follows:

The USD signs are on the same side	1,2198	1,2210	
of the slash: cross division	7,4180	7,3695	(4)
<b>3-month forward ZAR/CHF</b>	<b>0,1644</b>	<b>0,1657</b>	

**QUESTION 3 [15]****STUDY UNIT 4, pp. 75-76****Rand value**

- 30% of EUR 15,000 = EUR 4,500
- EUR/ZAR exchange rate on 6 August: 1,3147 x 7,3865 = 9,7110
- Rand value: EUR 4,500 x 9,7110 = ZAR 43,699,50 (3)

**Balance left in the Euro-CFC account**

<u>Receivables:</u>	12 October	70 x EUR 235	EUR	16,450
	9 November		EUR	8,759
		<u>Total received:</u>	EUR	25,209
<u>Payables:</u>	28 December		EUR	4,628
	2 <sup>nd</sup> half of January '10		EUR	10,500
		Balance left:	EUR	10,081
				(6)

**Situation on 9 April 2010**

- The total payables amount to EUR 15,128 (EUR 4,628 + EUR 10,500).
- This total of EUR 15,128 is offset against the first receivable of EUR 16,450 with a balance of EUR 1,322 left.
- On 9 April 2010, the EUR/ZAR exchange rate is  $1,1892 \times 7,5375 = 8,9636$ .
- On 9 April 2010, the bank will convert the balance of the first receivable at spot, that is,  $EUR\ 1332 \times 8,9636 = ZAR\ 11,939,52$  and credit the company's rand bank account with this amount.
- 180 days from date of receipt of the second receivable EUR 8,759 is 7 May 2010.
- If there are no payables between 9 April 2010 and 7 May 2010, the bank will convert this amount to rands at the buying spot rate applicable on 7 May. (6)

**QUESTION 4****[25]****STUDY UNIT 2, pp. 23-29, 31-35; STUDY UNIT 4, pp. 71-73**

- In terms of South Africa's current exchange control regulations, a company may take steps to cover its foreign exchange risk only when the commitment in respect of a sales contract or a purchase contract is firm and ascertainable.
- No clear definition of 'firm and ascertainable' exists but it is generally accepted that once the South African company and the foreign company have agreed on a transaction value in foreign currency, and have confirmed this agreement in writing, the commitment is 'firm and ascertainable'.
- In its simplest form, the written agreement could be a fax or email to the other, confirming the currency, amount, value date and, of course, a description of the assets involved in the transaction. (3)

**Sources of exposure**

- Money payable to foreigners for imports
- Money owed by foreigners for exports
- Offshore trade finance, whereby foreign bank credit is used to extend payable or receivable periods
- Offshore loans used for working capital purposes
- Other foreign currency commitments such as royalties, technical fees, travel costs, and so forth. (5)

**Creation of exposures**

- The exposure can be created by any number of departments within a company – most notably the sales, purchasing and finance departments.
- In order to effectively quantify the exposure, the company needs to set up a formalised reporting system.
- Under such a system, all departments and personnel, with the capability and authority to commit the company to a foreign exchange risk, must immediately report any such commitment to the person responsible for managing the exchange risk portfolio.
- The type of information that the foreign exchange manager would need in respect of each foreign exchange transaction includes:
  - The currency and amount
  - The beneficiary
  - Details of the liability, for example, the goods involved
  - The shipment or completion date
  - The value date
  - Money transfer details.

**(10)****Consolidating exposures**

- In order to effectively manage foreign exchange risk, the aggregate of exposures in various currencies needs to be consolidated into a report by due date or due period.
- This consolidated report would, in effect, take the form of a cash flow forecast for each currency.
- Each report would reflect opening balances by source of exposure, for example, payables to suppliers, or receivables from customers, trade credits, and so forth.
- To these opening balances would be added any new or expected commitments, while actual payments or expected payments would be deducted.
- The resulting closing balance would be the gross foreign exchange exposure of the company.
- From this information, the person, manager or department dealing with the company's foreign exchange exposure would be able to record and build up a complete picture of the company's exposures over a period of time.
- Such a system can also be used to reflect the effects of forward exchange contracts (which the company has concluded with the bank) on the exposure position.

**(7)**