

Lecture28

Operating Exposure Management: At Strategic Level

Short Questions:

1. What roles re-invoicing centers play in management of operating exposure?
2. What are Yankee Bonds?
3. Why foreign currency derivative contracts are of less use to manage operating risk?
4. Auto Spare parts Ltd. of India exports AC units to be fitted in cars manufactured in USA. The current FX rate is INR 46.40/\$. Auto Spare parts Ltd. of India exports 3000 units a year at price of \$ 650 each. Auto Spare parts Ltd. economist submitted a report to the CEO expressing that spot INR is going to appreciate by 10 % by the next year and would remain unchanged for coming 3 years. Its per annum fixed cost is INR 19mn and incurred in INR terms. Auto Spare parts Ltd. does not generate sales from any other source. Accepting this forecast as given, Auto Spare parts Ltd. faces a pricing decision to be made for the coming year: It may either (1) maintain the same USD price and in effect sell for fewer INR, without changing the volume sales. or (2) Increase the USD price so that its INR receipt remain unchanged as of current level and experience 15% drop in volume.
 - (a) What would be the short-run (one-year) implication of pricing strategy (1)?
 - (b) What would be the short-run (one-year) implication of pricing strategy (2)?
 - (c) Which strategy do you recommend?