**Chapter 10 The Foreign Exchange Market**

1) The foreign exchange market converts the currency of one country into that of another country.

2) When Krista traveled from the United States to England, she had to change her money from dollars into pounds. Krista was participating in the currency exchange market.

3) Parla liked to gamble, so she sometimes moved her funds from dollars to euros in the hope that she would make money based on the exchange rates. This demonstrates a carry trade.

4) Currency fluctuations can make seemingly profitable trade and investment deals unprofitable and vice versa.

5) Carry trade is nonspeculative in nature.

6) The value of a currency is determined by the interaction between the demand and supply of that currency relative to the demand and supply of other currencies.

7) If the spot exchange rate is £1 = $1.50 when the market opens, and £1 = $1.48 at the end of the day, the pound has appreciated, and the dollar has depreciated.

8) To minimize the risk of an unanticipated change in exchange rates, a company can protect itself by entering into a forward exchange contract.

9) If $1 bought more yen with a spot exchange than with a 30-day forward exchange, it indicates the dollar is expected to depreciate against the yen in the next 30 days. When this occurs, we say the dollar is selling at a premium on the 30-day forward market.

10) If the spot rate is $1 = 120, and the 30-day forward rate is $1 = ×130, the dollar is selling at a discount in the forward market.

11) A currency swap deal enables companies to insure themselves against foreign exchange risk.

12) The most important trading centers for currencies are Zurich, Frankfurt, Paris, Hong Kong, and Sydney.

13) Arbitrage opportunities in foreign exchange markets tend to be small and disappear quickly.

14) If the law of one price were true for all goods and services, the purchasing power parity (PPP) exchange rate could be found from any individual set of prices.

15) There are many impediments to the free flow of goods and services in an efficient market.

16) The purchasing power parity (PPP) theory is a strong predictor of short-run movements in exchange rates covering time spans of five years or less.

17) The International Fisher Effect states that for any two countries, the spot exchange rate should change in an equal amount but in the opposite direction to the difference in nominal interest rates between the two countries.

18) There is no evidence that psychological factors play an important role in determining the expectations of market traders as to likely future exchange rates.

19) The efficient market school argues that investing in exchange rate forecasting services would be a waste of money.

20) Governments allow convertibility to preserve their foreign exchange reserves.

21) Transaction exposure includes obligations for the purchase or sale of goods and services at previously agreed prices and the borrowing or lending of funds in foreign currencies.

22) The impact of currency exchange rates on the reported financial statements of a company is called economic exposure.