

Pionix case solution essay sample



**ASSIGN
BUSTER**

1. Why is Cain concerned by exchange rate fluctuations? Is she long or short? (A sentence or two.) Short in USD—she owes USD in 90 days. 2. Make up a small table showing the total CAD cost at the end of January of the required USD under three scenarios: the optimistic case that the cost per USD is CAD 0.90; the parity case that the cost per USD is CAD 1.00; and the pessimistic case that the cost per USD is CAD 1.10. See attached.

3. What is the total CAD cost at the end of January of the required USD if Pionix hedges forward? (A sentence or two. Show details in an exhibit.) See attached.

4. Show how the total CAD cost at the end of January of hedging with an option varies under the three scenarios. (The total cost includes what you pay for the USD and what you pay for the option. You can combine this with the table in question 2.) Do you use a call or put option? Call option—pay 1.73/100 per unit in the contract (7.5m), in CAD → CAD 129,750. If exercise the call option, pay CAD 7,012,500. Total is CAD 7,142,250. 5. Should Pionix hedge? (A sentence or two.)

Pionix is not, it appears, well placed to bear the FX risk. Risk is pretty big in CAD terms, and Pionix may be small and its shareholders undiversified ... 6. Should Pionix hedge with a forward contract or with an option? (One sentence should do.) Hedge forward.

7. Play the devil's advocate. How would you make the case that paying the premium on an option now to gain the upside potential in the future is not likely to be a wise move for Pionix? What information would the case have to give you to make you think speculating with an option might be a good

idea? Why hedge forward? The option is a guarantee that the most you pay is the forward price. But the option also charges you CAD 129, 750 on the gamble that the CAD price of the USD in three months is less than the strike price. Is there any evidence that Pionix has any information or skill that would make the gamble favorable to it? No. Remember, Pionix has only the information anyone has: Can Pionix use the common information to beat the market?