

d. Which currency is expected to appreciate in value?

The Canadian dollar.

e. Which country do you think has higher interest rates—the United States or Canada?

Explain.

I would have to say that both US and Canada have the same interest rates. I say this because of the International Fisher Effect which is a theory that real interest rates are equal across countries.

7). Interest Rates and Arbitrage [LO2] The treasurer of a major U.S. firm has \$50 million to invest for three months. The interest rate in the United States is .31 percent per month. The interest rate in Great Britain is .34 percent per month. The spot exchange rate is £.573, and the three-month forward rate is £.575. Ignoring transaction costs, in which country would the treasurer want to invest the company's funds? Why?

Value of US\$ in US after 3 months

$$\begin{aligned}
 &= I(1+r)^I \\
 &= 30,000,000(1+.0031)^3 \\
 &= \$30,000,000(1.00933) \\
 &= \$30,279,900
 \end{aligned}$$

Value of US\$ in GB after 3 months

$$\begin{aligned}
 &= \frac{(I)(S)(1+r)^I}{F} \\
 &= \frac{(\$30,000,000)(£0.573)(1+.0034)^3}{£0.575} \\
 &= \frac{(\$30,000,000)(£0.573)(1.01023)}{£0.575}
 \end{aligned}$$