



1. Read the paragraphs of the following news and answer questions:

「Taipei, Taiwan, R.O.C. March 5, 2008 - Chunghwa Telecom Co., Ltd. ("CHT" or the "Company", TAIEX: 2412, NYSE: CHT) today reported its unaudited ROC GAAP February 2008 financial summary.

For the month of February 2008, total revenue increased by 3.6% year-over-year to NT16.0 billion while net income decreased by 47.4% year-over-year to NT1.9 billion. As a result, earnings per share for the month of February 2008 decreased by 44.5% to NT\$0.21, or NT\$2.11 per ADS.

This decrease in net income was primarily due to a NT\$3.0 billion charge for an unrealized valuation loss related to a 10-year foreign currency derivatives contract entered into between the Company and an international investment bank in September 2007. The purpose of the contract is to hedge against capital expenditure payments and international call settlement fees denominated in US dollars. As at February 29, 2008, the Company's accumulated mark-to-market ("MTM") unrealized valuation loss relating to the contract was NT\$4.0 billion, as compared to NT\$0.5 billion as at December 31, 2007 and NT\$1.0 billion as at January 31, 2008.

Excluding the NT\$3.0 billion charge, for the month of February 2008, adjusted net income was NT\$4.16 billion and adjusted earnings per share was NT\$4.45 per ADS.

...
Dr. Joseph Shieh, Chief Financial Officer of Chunghwa Telecom, stated, "The contract was classified as a derivative financial instrument for trading purposes, so any changes to the valuation of the contract is calculated as of each reporting period and shown as either a gain or loss on the income statement....."

- (1) Please explain the meaning of derivative financial instrument? (5%)
- (2) List some examples of derivative financial instrument? (5%)
- (3) What is the purpose for Chunghwa Telecom Co., Ltd to use the derivative contract mentioned in this news? (5%)
- (4) What is the effect on income of using derivative contract by Chunghwa Telecom Co., Ltd's? Why? (5%)



2. The Sarbanes-Oxley Act of 2002 has caused worldwide attention and led to various amendments to the stock exchanges' regulations. Please answer the following questions:

- (1) What is the major content of Sarbanes-Oxley Act of 2002? (10%)
- (2) What is the purpose of this act? (5%)

3. Multiple choice (15%)

(1) Over the past 75 years, we have observed that investments with higher average annual returns also tend to have the highest standard deviations in their annual returns. This observation supports the notion that there is a positive correlation between risk and return. Which of the following lists correctly ranks investments from having the highest returns and risk to those with the lowest returns and risk?

- a. Large-company stocks, small-company stocks, long-term corporate bonds, long-term government bonds, U.S. Treasury bills.
- b. Small-company stocks, long-term corporate bonds, large-company stocks, long-term government bonds, U.S. Treasury bills.
- c. Large-company stocks, small-company stocks, long-term corporate bonds, U.S. Treasury bills, long-term government bonds.
- d. U.S. Treasury bills, long-term government bonds, long-term corporate bonds, small-company stocks, large-company stocks.
- e. Small-company stocks, large-company stocks, long-term corporate bonds, long-term government bonds, U.S. Treasury bills.

(2) An analyst has estimated how a particular stock's return will vary depending on what will happen to the economy:

<u>State of the Economy</u>	<u>Probability of State Occurring</u>	<u>Stock's Expected Return if this State Occurs</u>
Recession	0.10	-60%
Below Average	0.20	-10
Average	0.40	15
Above Average	0.20	40
Boom	0.10	90



- What is the coefficient of variation on the company's stock?
- 2.121
 - 2.201
 - 2.472
 - 3.334
 - 3.727
- (3). The Altman Company has a debt ratio of 33.33 percent, and it needs to raise \$100,000 to expand. Management feels that an optimal debt ratio would be 16.67 percent. Sales are currently \$750,000, and the total assets turnover is 7.5. How should the expansion be financed so as to produce the desired debt ratio?
- 100% equity
 - 100% debt
 - 20 percent debt, 80 percent equity
 - 40 percent debt, 60 percent equity
 - 50 percent debt, 50 percent equity
4. As you know the central bank in Taiwan controls two key rates to (dis)/stimulate the overall economy, what are the two key rates? (10 pts)
Can you describe the status of the two rates in the past decade? (5 pts)
and why? (5 pts)
Last year people began to talk about the fear of stagflation, what is it? (5 pts)
Starting from this year the central bank has faced a dilemma in terms of the two rates, please describe it? (10 pts)
Financial innovations are two-edged swords. For instance, a wide-spread use of structured notes causes the subprime credit crisis.
Can you give some examples of structured notes? (5 pts)
What is the subprime credit crisis? (10 pts)