

# 金融专业英语证书考试指南

贺瑛 潘飞 邹平 编著

JINRONGZHUANYE YINGYU ZHENGSHU KAOSHIZHINAN

## 总论

上海财经大学出版社

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上海财经大学出版社出版

(上海市中山北一路 369 号 邮编 200083)

新华书店上海发行所发行 上海市印七厂一分厂印刷

开本 787×1092 1/16 印张 11.625 字数 307000

1996 年 12 月第 1 版 1996 年 12 月第 1 次印刷

印数 1—6000

ISBN 7-81049-062-1/G·10

定价:40.00 元

(全书共三册,《总论》内附《试题库软盘》一张)

# 前 言

金融专业英语证书考试是我国第一个国家级的行业性英语证书考试制度。为配合读者提高专业英语水平,我们邀请了曾在金融机构供职,现又从事高校科研、教学工作的教授、学者编写了这套考试指南。本书是其中之一。

《金融专业英语证书考试指南——总论》一书共分外汇、信贷、会计三大类,由课文、生词词组、课文练习、课文全文翻译、综合练习及习题答案六部分组成。对于准备应考的读者来说,本书有实用价值。对于一般读者来说,它有助于巩固已有的基础知识。

本书外汇、信贷部分的生词词组、课文翻译,由邹平负责编写;会计部分的课文翻译及总练习中会计部分的习题,由潘飞、许康玮等负责编写;会计部分的生词词组、课文练习及总练习中外汇、信贷部分的习题,由贺瑛编写。本书最后由贺瑛总纂并定稿。

由于编者水平有限,再加之时间匆促,错误、疏漏在所难免,恳请广大读者批评指正。

编者

1996年3月

## Contents

### Foreign Exchange Business

Unit 1. Foreign Exchange — Some Definitions .....	( 2 )
Unit 2. Banks and Foreign Exchange Market .....	( 3 )
Unit 3. Foreign Exchange Quotations .....	( 5 )
Unit 4. Financial Instruments .....	( 9 )
Unit 5. Risks in Foreign Exchange .....	(16)

### Credit Loans

Unit 1. Credit Loans — Categories .....	(27)
Unit 2. Credit Risk Analysis .....	(29)
Unit 3. The Five P's of Credit Analysis .....	(31)
Unit 4. Cash Flow Analysis .....	(33)
Unit 5. Credit Risk Management .....	(36)
Unit 6. Loan Agreement .....	(37)
Unit 7. Guarantee .....	(40)

### Accounting

Unit 1. Definition.....	(48)
Unit 2. Users of Accounting Information .....	(50)
Unit 3. Specialized Accounting Services .....	(52)
Unit 4. Accounting Concept and Principles .....	(54)
Unit 5. Accounting Equation .....	(57)
Unit 6. Financial Statements .....	(58)
Unit 7. Classification of Assets and Liabilities .....	(61)
Unit 8. The Double-Entry Bookkeeping Systems .....	(63)
Unit 9. Profit and Loss Statement and Balance Sheet .....	(65)
Unit 10. Verification of Statements of Account .....	(67)

### The Chinese Versions of Texts & Key to Exercises

#### Foreign Exchange Business

Unit 1 ( 72 )      Unit 2 ( 73 )      Unit 3 ( 73 )      Unit 4 ( 76 )      Unit 5 ( 80 )

#### Credit Loans

Unit 1 ( 87 )      Unit 2 ( 88 )      Unit 3 ( 90 )      Unit 4 ( 91 )      Unit 5 ( 93 )  
Unit 6 ( 93 )      Unit 7 ( 96 )

#### Accounting

Unit 1 ( 98 )      Unit 2 ( 99 )      Unit 3 ( 100 )      Unit 4 ( 100 )      Unit 5 ( 102 )  
Unit 6 ( 103 )      Unit 7 ( 105 )      Unit 8 ( 106 )      Unit 9 ( 107 )      Unit 10 ( 107 )

Sample Test ( 110 )

# FOREIGN EXCHANGE BUSINESS

World trade and the cross-border money and capital movements resulting from financial transactions are the basis of foreign exchange dealings. Take a simple example: if a Swiss exporter sells a machine to a Japanese buyer, to conclude the transaction the Yen which the Japanese business man has available will have to be changed into Swiss francs, the currency sought by the supplier of the machine. Or, if Continental banks want to place excess funds in the Eurodollar market rather than in their own domestic markets, they have to buy dollars against local currency. The observation of the French economist Gaétan Pirou that foreign exchange deals spring from "the coexistence between the internationalism of trade and nationalism of currencies", thus aptly describes at least the original motive of this "métier". Clearly, the day that sees the arrival of a single world currency will also witness the disappearance of foreign exchange business.

# **Unit One   Foreign Exchange**

## **— Some Definitions**

All claims to foreign currency payable abroad, whether consisting of funds held (in foreign currency) with banks abroad, or bills or cheques, again in foreign currency and payable abroad, are termed foreign exchange. All these claims play a part in the relations between a bank and its customers. In the trading of foreign exchange between banks, which is the job of the foreign exchange dealer, only foreign currency held with banks abroad is concerned. For the purposes of this book, the term "foreign exchange" applies only to bank balances denominated in foreign currency.

Foreign bank notes are not foreign exchange in the narrower sense. They can be converted into foreign exchange, however, provided they can be placed without restriction to the credit of an ordinary commercial account abroad. The exchange regulations of some countries do not allow this conversion of bank notes into foreign exchange, although the operation in reverse is nearly always permitted.

A currency, whether in foreign exchange or bank notes, is usually called convertible if the person holding it can convert it, in other words change it, freely into another currency. A distinction needs to be made, however, between unrestricted convertibility and the various forms of partial convertibility. The Swiss franc, for example, is fully convertible whether the holder is resident in Switzerland or abroad, and regardless of whether current payments or financial transactions are concerned.

Many countries, on the other hand, recognize only external or non-resident, convertibility. Until October 1979, for instance, this was still the case with the United Kingdom: if a German exporter, say, had sterling funds in a British bank, he could (and can) simply instruct the bank to convert his pounds into any other currency and remit the proceeds abroad; but a person domiciled in Britain could not, as a general rule export capital except with the consent of the Bank of England.

Exchange regulations may also draw a distinction, as far as convertibility is concerned, between funds arising from current transactions (goods and services) and those coming from purely financial operations, only the latter being subject in some degree to a restriction on convertibility. In a few countries, this distinction between commercial and financial transactions has culminated in the establishment of two-tier markets. This is the case in South Africa, and has applied temporarily, for instance, to France, Italy and Belgium in recent years.

## **Unit Two Banks and the Foreign Exchange Market**

The banks are the natural intermediary between foreign supply and demand. The main task of a bank's foreign exchange department is to enable its commercial or financial customers to convert assets held in one currency into funds of another currency. This conversion can take the form of a "spot" transaction or a "forward" operation. Banking activities in the foreign exchange field tend inevitably to establish a uniform price range for a particular currency throughout the financial centres of the world. If at a given moment the market rate in one centre deviates too far from the average, a balance will soon be restored by arbitrage, which is the process of taking advantage of price differences in different places. It can be seen that the foreign exchange market acts as a very important regulator in a free monetary system.

Only the big banks and a number of local banks specializing in this kind of business have a foreign exchange department with qualified dealers. Banks which merely carry out their customers' instructions and do no business on their own account do not really require the services of a foreign exchange expert. For these it will be sufficient to have someone with a general knowledge of the subject because his role in practice will be that of an intermediary between the customer and a bank professionally in the market.

A foreign exchange dealer acquires his professional skill largely through experience. Here we should point out how important close cooperation is among a team of dealers. The group can work together smoothly only if each member is able to shed his individuality. We must not forget that, almost incessantly, all the dealers are doing business simultaneously on different telephones, and when large transactions are completed the rates may change, whereupon the other dealers must be brought up to date immediately. It is essential for a dealer to have the knack of doing two things at once so that he can do business on the telephone and at the same time take note of the new prices announced by his colleagues.

Professional foreign exchange dealing requires advanced technical equipment. Business is done by telephone (with many direct lines to important names) and teleprinter, depending on distance and convenience. At many modern banks, the foreign exchange department uses the Reuters dealing system, which combines the functions of a teleprinter with those of a television screen. Spot and forward rates of the most important currencies and money market rates are displayed on a number of rate boards, remote-controlled by the chief dealers. Current quotations can then not only be used by the bank's own dealers but also transmitted electronically to other banks. Electronic data-processing equipment is employed to keep track instantly of the exchange positions, and for the administrative



handling of the business done. Cross rates are worked out with the help of electronic desk-top calculators.

In line with the growth of international trade and the liberalization of capital movements, the volume of foreign exchange business grew tremendously in the course of the Sixties and the early Seventies. Under floating, with its sharp rate fluctuations, the volume grew further but excessive speculation also entered the market, and resulted in some spectacular bank failures in 1974. Despite restrictions imposed by monetary authorities in a number of countries and tightened regulations within the banks themselves, international foreign exchange activities have continued to multiply since these measures were introduced.

## Unit Three Foreign Exchange Quotations

How are foreign exchange rates quoted? Most countries use direct quotation. This means that the exchange rates give the equivalent of a certain quantity of the foreign currency quoted (normally one hundred units, but only one unit in the case of the dollar and the sterling). Thus, foreign currencies are expressed in Swiss francs in Switzerland, in Deutschmarks in Germany, etc. There are, however, exceptions to the rule. Great Britain in earlier times did not have the decimal system, and it was therefore easier to quote the value of one pound sterling in terms of the foreign currency: this method of direct quotation is still used now even though in 1971 Great Britain also switched to the decimal system. In the United States, at least for domestic purposes, the direct quotation is used, which means that the prices for foreign currencies are expressed in dollars; in their international foreign exchange activities, the American banks however adhere to the "European terms", which for them is indirect quotation.

Contrary to what we have just said, when it comes to professional foreign exchange dealing among banks, dealers normally quote dollar rates. In other words, the values of the various local currencies are expressed by indicating the price of one US dollar in local currency. Thus, if we enquire from Zurich with a German bank about their rates, the German dealers will not quote the Swiss franc against the D-Mark but the dollar against the D-Mark.

Due to this habit of quoting dollar rates — which developed in the fifties — the meaning of the word "arbitrage" is no longer the same as in earlier times. Between the two World Wars, foreign currencies were quoted against one's own currency. At the time, if we had called a bank in Stockholm to enquire how it was dealing in the German mark, we would have received a quotation in terms of Swedish kronor. Supposing that we had bought German marks against Swedish kronor, we would then have tried to sell the marks in another country and rebuy the kronor somewhere else, which would have led to a whole series of true arbitrage operations.

"Arbitrage" in the original sense thus meant taking quick advantage of price differences prevailing in different markets, a process which of course tended to make such differences disappear. Nowadays, European currencies are however quoted against the dollar. Since moreover \$ / DM rates are not only quoted in Germany, \$ / Sfr. rates not only in Switzerland, etc., but also in all other major financial centres, rates for a specific currency tend to be the same everywhere. Arbitrage in the old sense is thus hardly possible anymore. Arbitrage nowadays simply means professional business as against customer-related business.

The electronic rate board in the foreign exchange department of a large Swiss bank will thus display the rates for the dollar against the other major currencies rather than rates for foreign currencies expressed in Swiss francs. The same is true in an analogous way for banks in other financial centres.

**Example 1:** On November 8, 1990 (the date is arbitrarily chosen), closing rates were as per the following table (we shall use these rates in the practical examples):

	Buying rate (bid)	Selling rate (offered)
\$ / Sfr.	1.2565	1.2575
\$ / DM	1.4960	1.4960
\$ / Dfl.	1.6860	1.6860
\$ / FFr.	5.0120	5.0170
\$ / Lit.	1123.00	1124.00
\$ / Dkr.	5.7130	5.7180
\$ / Skr.	5.5790	5.5840
\$ / Nkr.	5.8285	5.8335
\$ / Yen	129.90	130.00
\$ / Can. \$	1.1665	1.1676
£ / \$	1.9596	1.9605

The above buying and selling rates are applied to dealings between banks. Slightly wider margins may be applied in transactions with clients.

If we have a quote of 1.4950/ 1.4960 for \$ / DM, the first rate is the buying rate for the dollar or the selling rate for the D-Mark, while the second is the selling rate for the dollar or the buying rate for the D-Mark.

Over the past few years, trading in "Cross Currencies" has increased considerably and naturally, clients and smaller banks may often wish to do business with us against currencies other than the dollar, for instance DM against Sfr., or £ against FFr. In such cases we have to work out the so-called "Cross Rates". At this stage we will just briefly explain how we arrive at the formula for calculating "Cross Rates".

What is the middle rate for D-Mark / Swiss franc, based on the middle rates for dollar / D-Mark and for dollar / Swiss franc?

The result is obtained by establishing a so-called chain equation.

$$\begin{aligned}
 &X \text{ Sfr.} = \text{DM } 100, \text{ if} \\
 &\text{DM } 1.4955 = \$ 1, \text{ if } \$ 1 = \text{Sfr. } 1.2570 \\
 &\$ 1 = \text{Sfr. } 1.2570 \quad \text{Thus: DM } 1.4955 = \text{Sfr. } 1.2570
 \end{aligned}$$

Thus: the product of the right-hand side of the equation divided by the product of the left-hand side.

$$\text{DM } 100 = \frac{100 \times 1 \times 1.2570}{1.4955 \times 1} = \text{Sfr. } 84.05$$

What is the middle rate for £ / Sfr., based on the middle rates for £ / \$ and \$ / Sfr.?

$$\begin{aligned} \times \text{Sfr} &= \text{£ } 1, \text{ if} \\ \text{£ } 1 &= \$ 1.9600, \text{ if} \\ \$ 1 &= \text{Sfr. } 1.2570 \end{aligned}$$

Thus:

$$\text{£ } 1 = \frac{1 \times 1.9600 \times 1.2570}{1 \times 1} = \text{Sfr. } 2.4637$$

You will have noted the influence the indirect quotation for has on the formula!

What are "long" and "short" positions, and how do they arise?

A bank active in international business has to maintain sufficient working balances in all major currencies for the conduct of international payments.

As a rule, current or checking accounts maintained with foreign correspondents must not be overdrawn, but in any case, if a debit balance develops, briefly and by chance, we would have to pay appropriate debit interest. Such working (credit) balances are foreign currency assets and thus "long" positions. Since these foreign currencies had to be bought with another currency — let's assume with our domestic currencies — we are automatically "short" with the respective amounts in our domestic currency, i.e. we have corresponding liabilities in Swiss francs.

Our foreign exchange position is, however, in most cases by no means identical with the working balances maintained, for a number of reasons. First, Swiss banks will often not be enthusiastic about maintaining large working balances in all major trading currencies because of the inherent exchange risk, and will therefore seek to eliminate this risk. For this purpose, instead of buying the required foreign currencies on a spot basis, we create them by means of a swap transaction, i.e. we buy them spot but simultaneously sell them forward.

**Example 2:** We need working balances in lira but do not want to run the exchange risk. Thus, instead of simply buying say Lit. 100 mill. against Swiss francs, we simultaneously sell the lire forward; our so-called nostro account with the Italian correspondent will thus show a credit balance of Lit. 100 mill. as a result of the spot purchase, but our exchange position in lire will be zero because we have sold forward the same amount.

Money market operations can also result in "short" and "long" positions different from our working balances. Let us assume the nostro account with our Paris correspondent is long with FFr. 1,000,000. We now receive a FFr. 10,000,000 3-month deposit from a customer; we decide (for various reasons) to convert this sum into dollars and place a corresponding 3-month dollar deposit. Our exchange position in French francs would thus be "short" to the tune of FFr. 9,000,000 (assets of FFr. 1,000,000 minus liabilities of FFr. 10,000,000), although our working balance is still FFr. 1,000,000.

Changes in our foreign exchange positions are of course arising continuously from our dealing activities. If we start the day with a "long" position in dollars of \$ 10,000,000 and later sell \$ 2,000,000 spot to a customer and \$ 3,000,000 3 months forward to a bank, our "long" position is reduced to \$ 5,000,000.

The bank's foreign exchange department has to keep constant track of the positions in the various currencies, which in modern trading rooms is done by computers. This so-called "dealer position" has to reflect our exposure in the various currencies regardless of maturities; it has to record not only spot but also forward transactions and currency exposures resulting from money market operations (the term "risk position" is frequently used to make clear that one refers to the total position, i.e. the one including forward positions, and not just to the spot positions). On the other hand, the currency exposures are measured on a net basis. If we receive a DM 10,000,000 3-month deposit and place again a DM 10,000,000 deposit, in the balance sheet both the foreign currency liabilities and assets would increase but the dealer position would not change because our net exposure in D-Marks remains the same.

# Unit Four Financial Instruments

## Spot Transaction

Spot transaction means the actual and variable amount of the currency of one country which at any given time, can be bought for a fixed sum in the currency of another country. It is a term meaning that these transactions are settled the second working day from the date of the deal.

**Example 3:** On Oct. 10th I buy sell value Oct. 12th.

The "value date" given to a transaction is the date on which the moneies must be paid to the parties involved. For all spot, or current, exchange operations the value date is set as the second working day after the date on which the transaction is concluded (to allow for the administrative handling of the deals). Since banks are closed in the western world on Saturdays and Sundays, spot deals made on Thursday will show Monday as value or settlement date.

It is possible, though exceptional, to conclude foreign exchange transactions for delivery one business day after conclusion of the deal (or sometimes even value same day). Such deals will however not be made at the quoted spot rates but a slightly different rates, depending on the interest rates for the currencies concerned.

## Forward Operations

Foreign exchange can be bought and sold not only on a spot or cash basis, but also on a forward basis (for delivery on a stipulated future date). Theoretically, the forward price for a currency can be identical with the spot price. Almost always, however, the forward price in practice is either higher (premium) or lower (discount) than the spot price.

Forward transactions can serve a number of different purposes. First of all, by doing forward transactions one can cover, or hedge an otherwise existing exchange risk, be it of a commercial (trade) or financial nature. In connection with money market (deposit) transactions, we encounter the swap operation, which is the combination of a spot purchase with a simultaneous forward sale (or vice versa). To avoid confusion when talking about forward business, dealers use the term "outright" operation when it is a single forward transaction, as against a forward transaction forming part of a swap operation. Outright deals can, as just seen, be a hedge; however, they are speculative transactions if they lack a commercial or financial background.

International trade always creates the need for forward operations, if the exchange risk is to be hedged. Let us consider the case of a Swiss importer who has bought goods in Germany, invoiced in

D-Marks, payable in 90 days. To eliminate the risk of a significant rise of the D-Mark in the meantime — and also to have the basis for an exact price calculation — he buys the D-Marks 90 days forward (outright). In the converse case a Swiss exporter knows that in three months he will receive French francs in payment for his exports. Here again, in order to eliminate the exchange risk, he hedges by selling the French francs three months forward (outright). Not to do these forward transactions would be equivalent to speculating, on a fall of the D-Mark in the first case, or a rise of the French franc in the second case.

Currency exposures, and thus the need to hedge them, can also arise from a variety of non-trade operations:

— Securities investments, money market deposits, loans extended to subsidiaries abroad, direct investments, etc., if done in foreign currencies all represent foreign currency assets; the currency risk can be covered by selling the respective currencies forward.

— Borrowings in capital markets abroad, for instance, if done in foreign currencies, represent foreign currency liabilities; the inherent exchange risk can be hedged by forward purchases of the respective currency.

In this connection, it should be noted that hedging by means of forward operations is possible even if the underlying transaction is of a medium — or long-term nature. For many currencies, forward deals of more than twelve months are difficult to arrange, but by regularly renewing, say, a twelve-month forward contract at maturity, we can match the hedge with the tenor of the underlying longer-term transaction. True, in such a case one only knows the cost of the hedging for the first period while the costs for the ensuing periods are not known in advance; this, however, need not be a reason for not hedging.

It should be pointed out here that, contrary to widespread belief, hedging does not necessarily involve costs. One normally hedges “weak” currencies against “stronger” ones, by selling the former forward, and to many people “weak” currencies are those with a discount; in such cases hedging involves costs. Yet, it has happened many times that the supposedly “weak” currency strengthened, while the supposedly “strong” one (with a premium) declined. Examples: From February to October 1992, sterling weakened from \$ 1.82 to \$ 1.61, although the pound was always at a premium. From the end of 1982 to the beginning of 1985, the dollar strengthened against most other hard currencies despite the fact that it was constantly at a discount. In these special instances, it would have been advisable to hedge sterling and German marks against dollars (i.e., buy forward dollars). This would not only have prevented an exchange loss but even yielded a hedging “profit”!

## Swaps

It contains two simultaneous inseparable contract-deals, the first for spot delivery, and the second (the contrary of spot) for future delivery (in this case your position is squared).

Or, in other words: the simultaneous purchase and sale of identical amounts of a currency for different value dates.

Swaps can be done for fixed periods:

- "overnight swap"
- "tomorrow / next swap"
- "spot / next swap"
- "week / end swap"
- "1, 2, 3, etc. months swap"

or for broken periods: 45, 65, 95 days.

**Example 4:**

Date of deal: 5 / 6 (5th June) spot value: 7 / 6.

We are in Italy and we buy \$ against Lit at the shorter value date and sell \$ against Lit at the longer value date, through a swap deal.

we should have:

Kind of Swap	Settlement Dates	
= overnight	5 / 6	+\$ - Lit
	6 / 6	-\$ + Lit
= tomorrow / next (tom/next)	6 / 6	+\$ - Lit
	7 / 6	-\$ + Lit
= spot / next	7 / 6	+\$ - Lit
	8 / 6	-\$ + Lit
= spot / week	7 / 6	+\$ - Lit
	14 / 6	-\$ + Lit
= 1 month etc.	7 / 6	+\$ - Lit
	7 / 7	-\$ + Lit

**Example 5:**

Given a spot position — 100 mio \$



Date: 6 / 6      value: 8 / 6

To have the roll-over of this position we might:

(1) On 7th June make a tom / next

I buy \$ value 8 / 6

to match the position

and sell \$ value 9th June

(2) On 8th June, make an Overnight

I buy \$ value 8 / 6

and sell \$ value 9 / 6

NB : Among other techniques SWAPs consent to roll-over mismatched position.

## Currency and Interest Rate Options

With the transition to floating exchange rates, central banks were no longer obliged to maintain exchange rates within narrow limits as defined in the Bretton Woods Agreement. Continuing disequilibria in international balances of payments led to increasing fluctuations in exchange rates especially after the liberalization of cross-border capital movements. The need to eliminate currency risks therefore became extremely urgent. The market for foreign exchange options, set up in the early 1980's, was a decisive step in minimizing exchange rate risks and creating greater flexibility than had previously been possible with existing instruments.

Whereas a forward transaction provides the possibility of setting an exchange rate for a future foreign exchange transaction, the buyer of the option acquires the right, but not the obligation, to go ahead with the contract, i. e. to take up the option or to allow it to expire. It is therefore possible to hedge against a currency loss as well as to benefit from any profit on a foreign exchange transaction.

The following are types of (European) option contracts:

### 1. Call option

The right to buy a certain amount of a currency at a fixed rate (strike price) at a pre-arranged expiry date.

### 2. Put option

The right to sell a certain amount of a currency at a fixed rate (strike price) at a pre-arranged expiry date.

It should be noted that the right does not imply the obligation to exercise an option.

The buyer of an option decides whether or not he will take up (call) or supply (put) the amount of a currency stipulated in the contract and pays a premium for this right. The seller (option writer) has no choice in either case and for this he receives the premium from the buyer which has to be paid to close the contract.

The increased volatility on international financial markets has changed the operating environment for companies, institutional investors and financial institutions and has led to a new level of risk aware-