3-258-98 International Financial Management

Contact Information

Professor:	Simon van Norden
Office:	4.228
E-mail:	simon.van-norden@hec.ca
Office hours:	Just drop by or make appointment
WWW:	www.hec.ca/pages/simon.van-norden

Required Readings

Eiteman, Stonehill and Moffett, *Multinational Business*, 9th ed. (new!)

The Media: You should read the international financial press at least weekly.

Examples:
- The Economist
- The Wall Street Journal
- The Financial Times
- Reuters
- Bloomberg
- Euromoney

See course outline for web sites.

Course Web Site: *http://www.hec.ca/sites/cours/3-258*

Various useful resources, but only *News* is required reading.

Suggested Resources

Course Web Site

For schedule, overheads, errata, links.

La Salle des marchés: *http://www.hec.ca/salledesmarches*

Good for news, data, technical analysis, seeing how it all fits together.

Publisher's Site: *http://www.awl.com/eiteman*

Organized by Chapter.

Solutions to selected problems, all the (updated) links to resources mentioned in the text.

Schedule

Week	Dates	Chapters	Theme
1	5 Sept.	1	Intro. & Multinational Firms
2	12 Sept.	2	The International Monetary Environment
3	19 Sept.	3	Foreign Exchange Rate Determination
4	26 Sept.	4	The Foreign Exchange Market
5	3 Oct.	5	Foreign Currency Options
6	10 Oct.	6	Transaction Exposure
7	17 Oct.	7	Operating Exposure
	24 Oct.	1-7	Mid-Term Exam (50%)
8	31 Oct.	8	Accounting Exposure
9	7 Nov.	9	Interest Rate Exposure and Swaps
10	14 Nov.	10	Global Cost of Capital and Financial Structure
11	21 Nov.	11	Sourcing Equity Globally
12	28 Nov.	12	Sourcing Debt Globally
13	4 Dec.	22	International Portfolio Theory and the MNE
	???	8-12, 22	Final Exam (50%)

Trends in Globalisation

News Flash: Globalisation Increasing (Film at 11)!

What do we mean by globalisation?

- Trade flows are more important < = > Economies are more open.
- Financial flows are more important < = > Financial markets are more open.
- The world is becoming more interdependent
  (and more multipolar according to Paul Kennedy.)

Globalisation has been rising in the Post WWII period.

This is very much the result of a few men and conferences around 1944

- Yalta, Bretton Woods, Churchill, Roosevelt & Stalin.
- The GATT, IMF, World Bank, IFC, WTO, AMI, EU, APEC, NAFTA, etc.

Actually, some economic historians argue that globalisation was higher in the latter part of the 1800s under Queen Victoria.

- trade flows, financial flows, speed of light communications, migration.

What Makes International Finance Different?

Exchange Rate Risk

Country (Political) Risk

Expanded Opportunities

- Diversification.
- Different institutions, resources
- Comparitive advantage

Market Imperfections

- Regulatory barriers are everywhere.
- Limited tax harmonization.
- Information travels slowly (even with the Internet.)

Risks Unique to International Finance

Foreign Exchange Risk

The variability of exchange rates introduces uncertainty into the value of assets held abroad.

- Accounting and valuation more complex
- FX risk premium may mean higher discount rates, higher cost of capital

Political Risk

Foreign investors are disenfranchised.

See Exhibit 1.1 & 1.2

The most important political risks are firm-specific (micro risk), and affect operations, not ownership.

- contrast with expropriation (e.g. Zimbabwe - but not foreign farms)

Country-specific (macro) risk leads one to invest across many countries.

What Makes International Finance The Same?

Much of International Finance consists of the same financial and economic principles applied in different or more complex (international) settings.

Principles

1. Arbitrage and Efficient Markets
2. Risk Management and Benefits of diversification
3. Comparative advantage
4. Goals of the financial manager/firm

The Multinational Corporation

Definition: A Multinational Enterprise (MNE) is a corporation that has *operations* in many countries.

Definition: A Transnational Enterprise is a corporation whose *ownership* is spread across many countries.

However, even domestic firms can face the risks in Exhibit 1.1

Common Steps in Overseas Expansion: Exporting, Licencing, Production, Design, Ownership/Management

Motives for Going Multinational

- Raw Materials (e.g. HBC & BHP in Canada)
- Costs (e.g. Volkswagen in Mexico, aluminum in Québec)
- Markets (e.g. Coke in China, Russia)
- Knowledge Seekers (e.g. foreign engineering and software firms in U.S.)
- Political Safety (e.g. Hong Kong firms pre-1999.)

The Multinational Corporation (cont.)

Multinational Firms tend to thrive when

1. economies of scale matter (in production, marketing, design, sales, financing, information etc.)
2. markets are highly imperfect
   - e.g. log exports forbidden
   - e.g. hub-and-spoke trading systems in FTAs
3. protected by governments encouraging “development” (esp. colonial govts.)
4. Products follow a life-cycle
   - go abroad as products age & competition increases
5. Customers are abroad (e.g. Boeing thought Seattle was too far away!)

Critiques of Multinationals: They are not acting in the national interest.

- but who believes that domestic corporations do?

What is the Goal of a MNE?

"One must realize that the so-called universal truths taught in basic finance courses are actually culturally determined norms." [Eiteman et al, p. 7]

Shareholder Wealth Maximization: This is what you saw in 2-200/2-208, and the dominant goal in the English-speaking world.

With the assumption of efficient markets, this means maximizing firm's market value. Agency problems, corporate takeovers also play important roles.

Corporate Wealth Maximization: This is the dominant goal most everywhere else. Also called Stakeholder Capitalism.

Market value is only one part of firm's "Wealth", which also includes technical, market and human resources. Long-term performance + stakeholders important.

Contrasts: Concept of risk, hostile takeovers [Exhibit 1.3], cronyism.

Trend: SWM is spreading, in part due to financial market globalization. (See Veba AG on p. 11)

What is the Goal of a MNE? (cont.)

Universal Truths vs. Cultural Norms

1. Interests of stakeholders always differ; which group dominates varies.
2. Firms always try to maximize value; how to measure it varies.
3. Firms are always risk averse; how to measure it varies.

Ultimate Goals of an MNE may vary.

Operational Goals

The primary operational goal of the MNE is to maximize consolidated profits, after-tax.

- Consolidated means across all units of the firm and expressed in a common currency,

Where Do We Go From Here?

Four weeks on Markets for Foreign Exchange

History, Theories, Market Structure.

Four weeks on Risk

Taxonomy, where found, how to manage.

Four weeks on Global Markets for Long-Term Capital

Capital structure, market structure, portfolio investment.

Homework for Week 1

Problems

- Try all, but esp. 2 and W1

Readings

- Read the media.

For next class

- read Ch. 1&2
- What’s been happening in Argentina?