

FUNDAMENTALS OF
MULTINATIONAL FINANCE

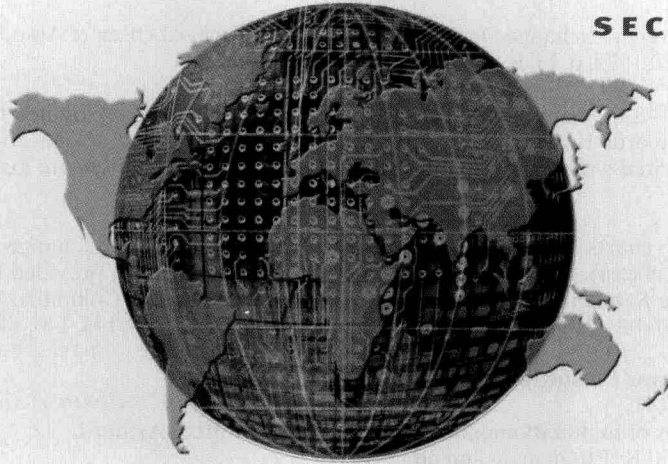
SECOND EDITION



Michael Moffett ✨ **Arthur Stonehill** ✨ **David Eiteman**

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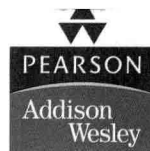
SECOND EDITION



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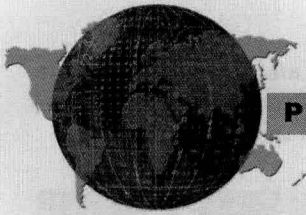
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PREFACE

Fundamentals of Multinational Finance, Second Edition, views the multinational enterprise (MNE) as an organization that poses unique demands on the *business leaders* of tomorrow. Those leaders — possibly some of the readers of this text — will be confronted with a multitude of challenges that will test their ability not only to *comprehend* global markets, but more importantly, to *lead* their organizations through the constantly shifting currents and tides of global change. Competent leadership may indeed be the scarcest global commodity.

This book is about multinational management, and more specifically, the financial management dimensions of leading a multinational enterprise. The MNE itself acts as a *catalyst* and a *facilitator* of international trade, and as an important producer and distributor in the host countries where it operates. The MNE's potential success, however, rests in the hands of the truly competent *global leader*. The success of any MNE is dependent on its leadership's ability to lead and manage the global organization.

Our vision in writing this book is to aid in the development of tomorrow's MNE leaders. It is their ability to recognize and benefit from business opportunities such as imperfections in national markets, unequal costs, and efficiencies of the factors of production, to tap the well-springs of intellectual property, and to access sources of global funding to facilitate growth, that will add value.

The financial managers of MNEs face numerous foreign exchange and political risks. These risks can be daunting, but they also present opportunities for creating value if properly understood. These opportunities and risks are most effectively understood in the context of the global business itself, and the ability of management to integrate the strategic and financial challenges that business faces.

Audience

Fundamentals of Multinational Finance, Second Edition, is aimed at university-level courses in international financial management, international business finance, international finance, and similar titles. It can be used at either the undergraduate or the graduate level, as well as in executive education courses.

A prerequisite course or experience in corporate finance or financial management would be ideal. However, we review the basic finance concepts before we extend them to the multinational case. We also review the basic concepts of international economics and international business.

We recognize that a significant portion of our audience lives outside of the United States and Canada. Therefore, we have included a significant number of non-U.S. examples, mini-cases, and *Real World Examples* (anecdotes and illustrations).

Organization

Fundamentals of Multinational Finance, Second Edition, is organized into six parts. The six parts are unified by the common thread of the globalization process by which a firm moves from a domestic to a multinational business orientation. Part 1 introduces the global financial environment. Part 2 explains foreign exchange theory and markets.

Part 3 analyzes foreign exchange exposure, both measurement and management. Part 4 covers the financing of the global firm. Part 5 analyzes international investment decisions. Part 6 examines the management of multinational operations.

What Is New in the Second Edition?

- We have added 12 new mini-cases and retained 10 of the most popular ones in response to user feedback.
- We have expanded the number of *Real World Examples* (formerly titled *Global Finance Perspectives*), spread throughout the text, to 37.
- We have updated and expanded the number and use of Internet exercises, end-of-chapter questions, and end-of-chapter problems. There are now at least 10 quantitative problems in each chapter — more than 210 problems throughout the text.
- Chapter 1, Financial Goals and Corporate Governance, includes an expanded treatment of corporate governance, including failures, reform, family ownership, ethics, and a comparison with a number of countries.
- Chapter 2, The International Monetary System, now covers eurocurrencies, LIBOR, and the expansion of the euro zone by 10 new countries.
- Chapter 3, The Balance of Payments, features expanded coverage on the interaction of balance of payments with other macroeconomic variables, including GDP, exchange rates, interest rates, and inflation.
- Chapter 5, Foreign Exchange Rate Determination, replaces the Brazilian crisis with the Argentine crisis of 2002.
- Chapter 11, *Global Cost and Availability of Capital*, now covers the relationship between corporate governance and the cost of capital. The mini-case for the chapter describes how Nestlé could use the international capital asset pricing model (ICAPM) to calculate its cost of capital.
- Chapter 17, Political Risk Assessment and Management, has been revised to focus only on political risk, with an expanded section on global-specific risks such as terrorism.
- Chapter 21, Repositioning Funds, and Chapter 22, Working Capital Management, from the first edition have been revised and combined to create a new Chapter 21. We have also moved leads and lags and re invoicing centers to Chapter 9, Operating Exposure, and transfer pricing to Chapter 20, Tax Management.
- The second edition has moved the following mini-cases from the text to the book's Web site for selective instructor and student use: Tsar Alexander III's Russian Gold Loan, Russian Purchasing Power and Western Automakers, Ford Range Rover Asia Pacific, Telecom Italia, Romanian Communications and Cyprus Offshore, Private Equity in Latin America (Soto Group), Corporate Governance at Brasil Telecom, Motorola and TelSim of Turkey, and Cemex of Mexico Bids for Semen Gresik of Indonesia.

PEDAGOGICAL TOOLS

In order to make *Fundamentals of Multinational Finance*, Second Edition, as comprehensive as possible we utilize a large number of proven pedagogical tools. Our efforts have been informed by the detailed reviews and suggestions of a panel of professors who have

earned recognition individually for teaching excellence in the field of international finance, particularly at the undergraduate level. Among these pedagogical tools are:

- A student-friendly writing style combined with a tightly structured presentation, beginning with *learning objectives* for each chapter, and ending with a summary of how those learning objectives have been realized.
- A wealth of *illustrations and exhibits* that provide a visual parallel to the concepts and content presented. The entire book utilizes a multicolor presentation, which provides a visual attractiveness that contributes significantly to reader attention and retention.
- A running case on a hypothetical U.S.-based firm, *Trident Corporation*, which provides a cohesive framework for the multifaceted globalization process and is reinforced in several end-of-chapter problems.
- *Spreadsheet analyses*, prepared by our colleague Francis Clauss, that illustrate the quantitative dimensions of the analysis. These spreadsheet analyses provide not only the computational support to improve reader understanding, but also the detailed formulas behind their construction.
- A *mini-case* at the end of each chapter (22 in all) that illustrates the chapter content and extends it to the multinational financial business environment.
- *Real World Examples* in nearly every chapter to illuminate the theory with accounts of actual business practices. These applications extend the concepts without adding to the length of the text itself.
- The power and resources of the *Internet*, which are leveraged throughout the text in a variety of applications. Most chapters have a number of end-of-chapter exercises requiring the use of the Internet, while a variety of Internet references are dispersed throughout the chapters in text and exhibits.
- An increased number of end-of-chapter *Questions and Problems*, which assess the students' understanding of the course material. End-of-chapter problems that use spreadsheets available online at www.aw-bc.com/moffett are flagged with a spreadsheet icon.



A Rich Array of Support Materials

A robust package of materials for students and instructors accompanies the text to facilitate learning and to support teaching and testing.

- **Instructor's Manual.** The Instructor's Manual, prepared by the authors, contains complete answers to all end-of-chapter questions, problems, and chapter mini-cases. All quantitative end-of-chapter problems are solved using spreadsheets, which are accessible from the online catalog page for this textbook (found at www.aw-bc.com/finance) and the Instructor's Resource Disk.
- **Test Bank.** The Test Bank, prepared by Curtis J. Bacon of Southern Oregon University, contains over 1,200 multiple-choice and short-essay questions. The multiple-choice questions are labeled by topic and by category — recognition, conceptual, and analytical types.
- **Computerized Test Bank.** The Test Bank is also available in Pearson Education's TestGen Software. Fully networkable, it is available for Windows and Macintosh.

TestGen's graphical interface enables instructors to view, edit, and add questions; transfer questions to tests; and print different forms of tests. Search-and-sort features enable the instructor to locate questions quickly and arrange them in a preferred order. The TestGen plug-in allows the instructor to administer TestGen tests in CourseCompass. QuizMaster, working with TestGen and the school's computer network, automatically grades exams, stores the results on a disk, and allows the instructor to view and print a variety of reports. More information on TestGen software is available at www.aw-bc.com/testgen.

- **PowerPoint Presentation Slides.** Prepared by Shafiq Jadallah and Mark J. Bradt, the extensive set of PowerPoint slides available on the Instructor's Resource Disk and on the online catalog page for this textbook provides lecture outlines and selected graphics from the text for each chapter.
- **Study Guide.** Written by Timo Korkeamaki of Gonzaga University, the Study Guide enhances students' understanding and retention of concepts by providing detailed study outlines and helps students prepare for tests through a series of self-test questions, including true/false, multiple-choice, and short essay. The answers to the self-test questions also appear in the Study Guide.
- **Instructor's Resource Disk.** This CD-ROM contains the Computerized Test Bank files (TestGen), the Instructor's Manual files (PDFs), Test Bank files (Word), spreadsheet solutions (Excel), and PowerPoint files.
- **Web Site.** A companion Web site at www.aw-bc.com/moffett contains the Internet exercises from the book with wired links, electronic flash cards of glossary terms, self-assessment quizzes, a Web chapter, and selected solutions and spreadsheets for end-of-chapter problems.
- **Web Chapter: Cross-Border Mergers & Acquisitions.** Available as a PDF on the Companion Web site (www.aw-bc.com/moffett), the *Cross-Border Mergers & Acquisitions* chapter has been updated for the second edition and includes a mini-case and expanded questions and problems sections. This Web chapter introduces students to the increasingly important field of cross-border mergers and acquisitions, a viable alternative to a greenfield foreign direct investment.

INTERNATIONAL EDITIONS

Fundamentals of Multinational Finance and *Multinational Business Finance* have been used throughout the world to teach students of international finance. Our books are published in several foreign languages, including Chinese, French, Indonesian, Portuguese, Spanish, and Ukrainian.

Acknowledgments

The authors are very thankful for the many detailed reviews and suggestions from a number of colleagues. These reviews included 15 detailed chapter-by-chapter reviews, and answers to a comprehensive questionnaire by 104 adopters and nonadopters. The final version of this second edition reflects most of the suggestions provided by these

reviewers. The survey reviewers were anonymous, but the 15 reviewers who submitted detailed comments are as follows:

Morten Balling	W. Brian Barrett
Aarhus School of Business (Denmark)	University of Miami
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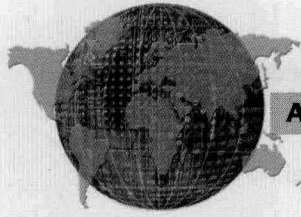
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University of Wisconsin, Madison	University of Cincinnati
Benjamin Uzoaru	
Southeast Missouri State University	

We would also like to thank the staff at Addison-Wesley who have worked so diligently on this edition, notably Donna Battista, Acquisitions Editor for Finance, and Amy Fleischer, Assistant Development Editor.

Finally, we would like to dedicate this book to our parents, Bennie Ruth and Hoy Moffett, the late Harold and Norma Stonehill, and the late Wilford and Sylvia Eiteman, who gave us the motivation to become academicians and authors. We thank our wives, Megan, Kari, and Keng-Fong, for their patience while we were preparing *Fundamentals of Multinational Finance*, Second Edition.

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