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NINTH EDITION

MULTINATIONAL BUSINESS FINANCE



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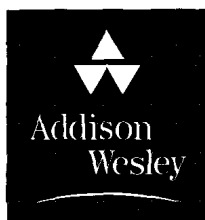
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Library of Congress Cataloging-In-Publication Data

Eiteman, David K.

Multinational business finance / David K. Eiteman, Arthur

I. Stonehill, Michael H. Moffett; with a contribution by Chuck Kwok.—9th ed.

p. cm.

Includes bibliographical references and index.

ISBN 0-201-63538-0

1. International business enterprises--Finance. I. Stonehill,

Arthur I. II. Moffett, Michael H. III. Kwok, Chuck. IV. Title.

HG4027.5. E36 2001

658.15' 99--dc21

00-040586

CIP

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1 2 3 4 5 6 7 8 9 10-CRW-0403020100

PREFACE

As the field of international finance has evolved, so has the content of *Multinational Business Finance*. As in previous editions, we perceive the multinational enterprise to be a unique institution that acts as a catalyst and a facilitator of international trade and as an important producer and distributor in host countries where its affiliates are located. The success of a multinational enterprise continues to be dependent on its ability to recognize and benefit from imperfections in national markets for products, factors of production, and financial assets.

Also carried over from the earlier editions is the theme that volatile exchange rates may increase risk, but they also create opportunities for both investors and firms to profit, given a proper understanding of exchange risk management.

The ninth edition continues to recognize the increasing importance of global integration of money and capital markets, a trend that is creating expanded opportunities for both investors and organizations that need to raise capital. Although global integration of financial markets removes some market imperfections that impede the flow of capital internationally, excellent opportunities continue to exist for investors to increase their returns while lowering their risk through international portfolio diversification and for firms to lower their cost of capital by sourcing it internationally.

WHAT IS NEW IN THE NINTH EDITION?

In preparing this ninth edition of *Multinational Business Finance* a major effort was made to shorten the book and to increase the coverage of emerging market issues.

1. Although the book's length has been reduced from 854 pages to under 700 pages, four new decision cases and numerous new illustrative cases have been added.
2. The new decision cases are a reflection of the need to increase emerging market coverage.
 - The *P.T. Semen Gresik* case illustrates the valuation issues faced by a Mexican multinational (Cemex) that is considering acquiring an Indonesian cement manufacturing company in 1998.
 - The *Northwestern Paper Company* case involves a transfer pricing dispute between two foreign subsidiaries (South Korea and Indonesia) bidding on the same sale of paper to an Australian company in the mid-1990s.
 - The *Far East Trading Company* case describes the problems facing a Swedish multinational firm that has its key markets in Asia adversely affected by the emerging markets crisis in 1997.

- *Tektronix (C)* describes the case of a U.S. multinational firm that is divesting half the company in 1999. This divestment will cause problems for the foreign exchange risk-management strategies of the surviving company. Operating exposure management is particularly difficult since most of Tektronix' products are manufactured in the United States, but half of sales are exported and invoiced in local currencies.
- 3. Three decision cases were retained from the prior edition: *Lufthansa*, *ZAPA Chemical*, and *British Columbia Hydro*.
- 4. Eight decision cases from the prior edition have been transferred to a new casebook, *Cases in International Finance*, authored by Michael Moffett and published by Addison Wesley Longman. This new casebook includes a number of other decision cases. It will be sold separately from *Multinational Business Finance*, but its cases will be keyed to this text's contents. The new case book is being published simultaneously with this text.
- 5. Emerging markets are emphasized throughout the book. Extensive coverage is given to the emerging market crises of 1997–1999. The perspective of multinational firms resident in emerging markets is emphasized in the chapters on cost and availability of capital, sourcing equity globally, capital budgeting, international acquisitions, adjusting for risk in foreign investments, evaluation of performance, international portfolio investment, and working capital management. Political risk is treated throughout the book rather than in a separate chapter.

A chapter-by-chapter summary of changes follows:

PART 1. THE INTERNATIONAL FINANCIAL ENVIRONMENT

Chapter 1, International Financial Management and the Multinational Firm now includes a section on motives for foreign direct investment (FDI) that had previously appeared in our chapter on foreign investment decisions. It also has a more detailed explanation of the risks faced by multinational enterprises (MNEs). Conceptual material on political risk is treated here, while additional material on political risk has been disseminated throughout this ninth edition.

Chapter 2, The International Monetary Environment, features three illustrative cases, on Thailand, Russia, and Brazil, that highlight the emerging market crises of 1997–1999. The birth of the euro is described in detail.

Chapter 3, Foreign Exchange Rate Determination, is a revision and expansion of our old chapter on international parity conditions and balance of payments. New foreign exchange rate determinants that came to light because of the emerging market crises have been added to the traditional balance-of-payments and parity-conditions determinants of foreign exchange rates.

Chapter 4, The Foreign Exchange Market, has been revised to reflect the introduction of the euro. A revised section on foreign currency futures has been placed within the chapter rather than in an appendix, and the use of futures is compared with forward contracts.

Chapter 5, Foreign Currency Options, includes new material on the euro but is otherwise mostly unchanged.

PART 2. MEASURING AND MANAGING FOREIGN EXCHANGE EXPOSURE

Chapter 6, Transaction Exposure, now reflects the advent of the euro in all examples and end-of-chapter problems.

Chapter 7, Operating Exposure, has been revised to reflect the euro but is otherwise the same.

Chapter 8, Accounting Exposure, has been revised to reflect the euro, but is otherwise the same.

Chapter 9, Interest Rate Exposure and Swaps, has been completely rewritten. It now features a student-friendly explanation of the various types of interest rate and currency swaps.

PART 3. FINANCING THE GLOBAL FIRM

Chapter 10, Global Cost of Capital and Financial Structure, has been completely rewritten. It now features an expanded calculation of the cost of capital for Nestlé compared to a hypothetical domestic Swiss company. The former chapter on financial structure has been integrated into this chapter.

Chapter 11, Sourcing Equity Globally, has been heavily revised. It now has a greater managerial focus featuring alternative paths for a firm to follow to achieve improved global cost and availability of capital. Equity market descriptions have been updated.

Chapter 12, Sourcing Debt Globally, has been given more of a managerial focus, and the descriptive tables have been updated.

PART 4. FOREIGN INVESTMENT DECISIONS

Chapter 13, Corporate Strategy: Foreign Direct Investment and Political Risk, has been revised to include part of the former political risk chapter.

Chapter 14, Multinational Capital Budgeting, has been completely rewritten with a new greenfield investment case that is then also used in the next two chapters. The greenfield investment decision case, P.T. Semen Gresik, is about a Mexican cement producer, Cemex, considering an investment in Indonesia.

Chapter 15, International Acquisitions and Valuation, is a brand new chapter. It continues the P.T. Semen Gresik case from Chapter 14 with the Mexican producer (Cemex) now considering acquisition of an existing Indonesian cement producer (P.T. Semen Gresik). Various valuations techniques are explored.

Chapter 16, Adjusting for Risk in Foreign Investments, is another new chapter. Again utilizing the P.T. Semen Gresik case, it features the various new techniques that have been proposed to adjust the discount rate for foreign direct investments.

PART 5. MANAGING MULTINATIONAL OPERATIONS

Chapter 17, Multinational Taxation, is a very streamlined and tightened version of the eighth edition's chapter on taxation. Some of the detailed description of the U.S. taxation of foreign source income has been dropped in favor of a more generic treatment of the subject.

Chapter 18, Repositioning Funds, has been lightly revised to reflect the euro, but otherwise is the same as it was in the prior edition of this book.

Chapter 19, Working Capital Management, now includes financing working capital in addition to the management of current assets. The interface with various types of banking facilities has been moved here from its position in the import and export financing chapter in the eighth edition.

Chapter 20, Export and Import Financing, is shorter, but the topics are the same as in the prior edition. The eighth edition's section on forfaiting has been moved to the web page for this book.

Chapter 21, Evaluation of Performance, is a new chapter but is really just a shift of material from the chapter on current industry practices in the prior edition.

PART 6. ADVANCED TOPICS IN MULTINATIONAL FINANCE

Chapter 22, International Portfolio Theory and the MNE, is a new chapter that combines material from our eighth edition's chapters on the global cost of capital and the technical appendix to that chapter.

Chapter 23, Advanced Topics in Currency Risk Management, is based on a portion of the prior edition's chapter on advanced topics in multinational finance.

Chapter 24, Advanced Topics in Interest Rate Risk Management, contains the remaining portions of our eighth edition's chapter on advanced topics in multinational finance.

PEDAGOGICAL FEATURES

Multinational Business Finance, ninth edition, continues to provide an instructor-friendly package of supplements. An instructor's manual and power point slides will be provided to teachers who adopt the book for classroom use. The manual includes a disk that contains a variety of spreadsheet solutions to problems and case material, a multiple-choice test bank, and short-essay test bank.

Thanks to improved technology, we are greatly expanding our usage of Addison Wesley Longman's web page support for the text at <http://www.awl.com>. A number of "remedial" topics that were in the eighth edition have been moved to this web site. The web page will be continually updated with new illustrative cases and other relevant material as they arise.

Some chapters have in addition to new and expanded end-of-chapter questions, a separate set of Internet exercises in which students are directed to specific sources of information on the World Wide Web about current company, market, and business events. Many of these exercises have been designed to require the student to use real-time resources in the preparation of executive briefings and decision-based support.

AUDIENCE

The ninth edition of *Multinational Business Finance* is appropriate for the same audiences as the previous editions. Earlier editions have been widely used in international financial management courses in university degree programs, university-run executive education programs, and company management development programs.

Readers will find *Multinational Business Finance* most meaningful if they have the background knowledge or experience equivalent to a basic finance course. A previous course in international economics is desirable, but the text and web-site supplements are designed to cover sufficient economic material so that a separate background is not essential.

ACKNOWLEDGMENTS

The authors are very grateful to the numerous person who have provided critical comments and suggestions to improve both the current and earlier editions of this book. The ninth edition has benefitted immensely from comments we received on the previous edition, both from formal reviews and from colleagues' replies to our surveys.

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Special thanks to those who provided detailed input into the construction of the ninth edition through detailed book evaluations.

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Inevitably woven into the fabric of this book are ideas received from faculty and students at institutions all over the world where we have taught. These include our home universities of University of California, Los Angeles; Oregon State University; University of Hawaii; and Thunderbird. Our visiting stints have been at the Hong Kong University of Science and Technology; University of California, Berkeley; University of Michigan, Ann Arbor; Cranfield School of Management, United Kingdom; University of Hawaii at Manoa; Northern European Management Institute, Norway; Copenhagen Business School, Denmark; Aarhus School of Business, Denmark; Helsinki School of Economics and Business Administration, Finland; Institute for the Development of Executives, Argentina; National University of Singapore; International Centre for Public Enterprises, Yugoslavia; Beijing Institute of Chemical Engineering and Management; and Dalian University of Science & Technology, China. Further ideas came from consulting assignments in Argentina, Belgium, Canada, Denmark, Finland, Guatemala, Hong Kong, Indonesia, Japan, Malaysia, Mexico, the Netherlands, Norway, People's Republic of China, Peru, Sweden, Taiwan, the United Kingdom, and Venezuela.

We would also like to thank all those with Addison Wesley Longman who have worked so diligently on this ninth edition; Denise Clinton, Andrea Botticelli, and Patty Mahtani.

Finally, we would like to rededicate this book to our parents, the late Wilford and Sylvia Eiteman, the late Harold and Norma Stonehill, and Bennie Ruth and Hoy Moffett, who gave us the motivation to become academicians and authors. We thank our wives, Keng-Fong, Kari, and Megan, for their patience through the years spent preparing this edition.

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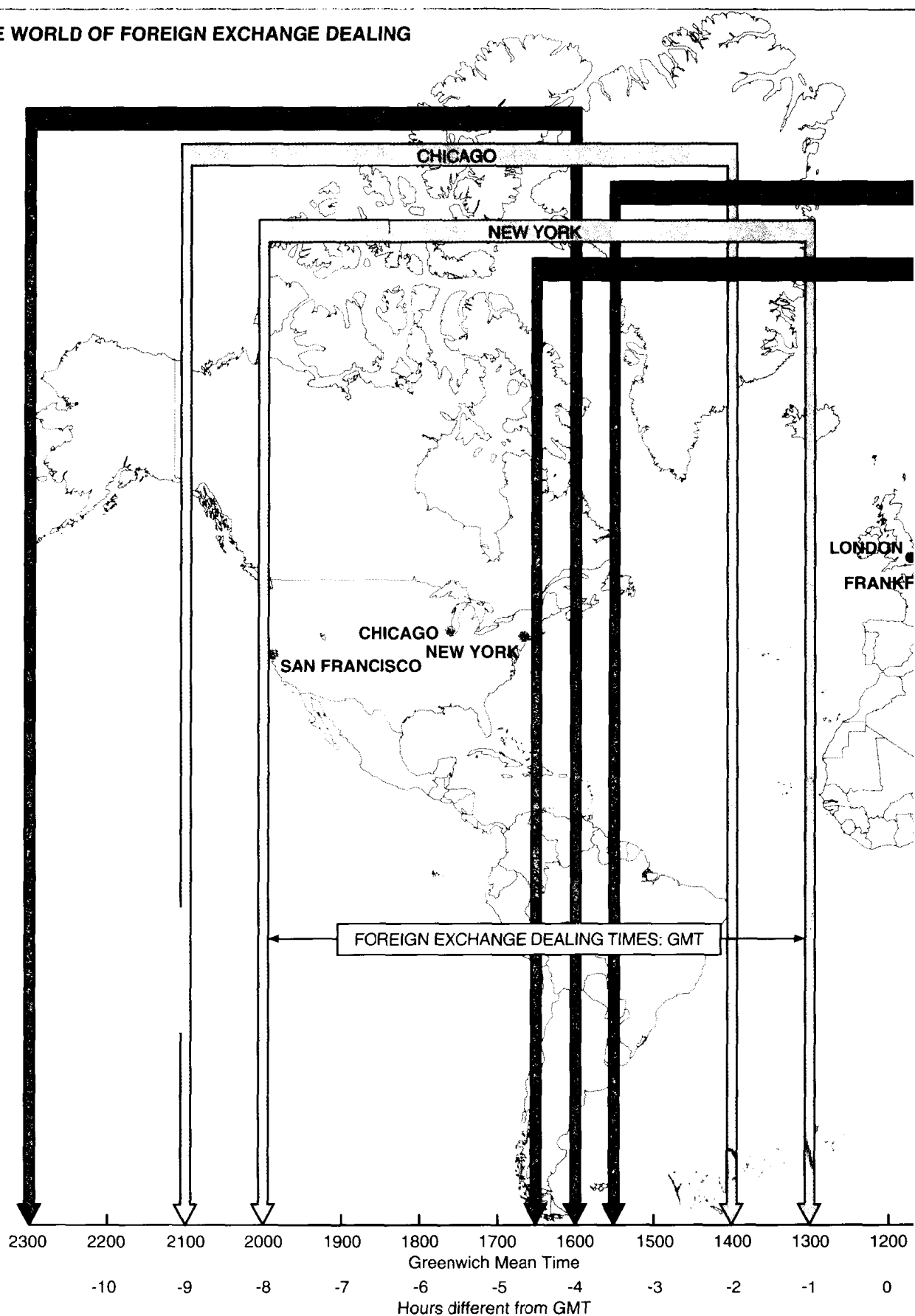
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THE WORLD OF FOREIGN EXCHANGE DEALING



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