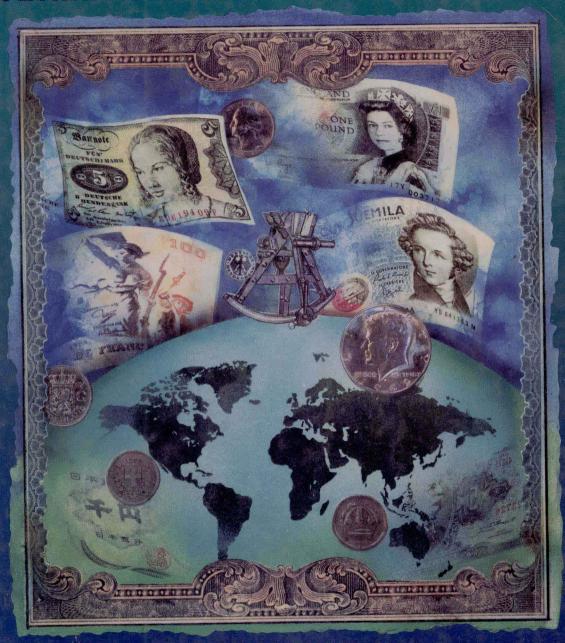
FIFTH EDITION

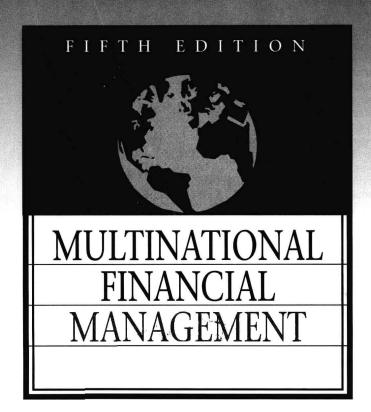
MULTINATIONAL FINANCIAL MANAGEMENT



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APPROACH

The basic thrust of this fifth edition of *Multinational Financial Management* is to provide a conceptual framework with which the key financial decisions of the multinational firm can be analyzed. The approach is to treat international financial management as a natural and logical extension of the principles learned in the foundations course in financial management. Thus, it builds on and extends the valuation framework provided by domestic corporate finance to account for dimensions unique to international finance.

Multinational Financial Management focuses on decision making in an international context. Analytical techniques help translate the often vague rules of thumb used by international financial executives into specific decision criteria. The book offers a variety of real-life examples, both numerical and institutional, that demonstrate the use of financial analysis and reasoning in solving international financial problems. These examples have been culled from the thousands of illustrations of corporate practice that I have collected over the years from business periodicals and my consulting practice. The examples scattered throughout the text show students the value of examining decision problems with the aid of a solid theoretical foundation. Seemingly disparate facts and events can then be interpreted as specific manifestations of more-general financial principles.

All the traditional areas of corporate finance are explored, including working capital management, capital budgeting, cost of capital, and financial structure. However, these areas are explored from the perspective of a multinational corporation, concentrating on those decision elements that are rarely, if ever, encountered by purely domestic firms. These elements include multiple currencies with frequent exchange rate changes and varying rates of inflation, differing tax systems, multiple money markets, exchange controls, segmented capital markets, and political risks such as nationalization or expropriation. Throughout the book, I try to demystify and simplify multinational financial management by showing that its basic principles rest on the same foundation as the principles of corporate finance.

The emphasis throughout this book is on taking advantage of being multinational. Too often, companies focus on the threats and risks inherent in venturing abroad rather than on the opportunities that are available to multinational firms. These opportunities include the ability to obtain a greater degree of international diversification than security purchases alone can provide as well as the ability to arbitrage between imperfect capital markets, thereby obtaining funds at a lower cost than could a purely domestic firm.

AUDIENCE

Multinational Financial Management is designed for use in master's-level courses. It is also suitable for use in bank management and other executive development programs.

FEATURES

Multinational Financial Management presumes a knowledge of basic corporate finance, economics, and algebra. However, it assumes no prior knowledge of international economics or international finance and is, therefore, self-contained in that respect. For those who are not familiar with Multinational Financial Management, here are some of the distinctive features that have led to its widespread adoption.

Distinctive topic coverage includes the following:

- Role of expectations in determining exchange rates (Chapter 2)
- Discussion of the equilibrium approach to exchange rate determination (Chapter 2)
- Analysis of the Mexican currency crisis (Chapter 2)
- Discussion of currency boards and the role of central bank credibility in the context of the dramatic changes made recently in Argentina and New Zealand (Chapter 2)
- Analysis of the September 1992 and August 1993 European currency crises (Chapter 3)
- Discussion of monetary union and optimum currency areas (Chapter 3)
- Use of the balance-of-payments framework to assess the economic links among nations (Chapter 4)
- Comprehensive discussion of the foreign exchange market and its institutions and mechanisms, including electronic trading (Chapter 5)
- Understanding of currency futures and options contracts (Chapter 6) and their use in exchange risk management (Chapter 9)
- Discussion of the key parity conditions in international finance, including putcall option parity with numerous real-world applications (Chapter 7)
- Use of currency risk sharing in international contracts (Chapter 9)
- Identification of the economic, as opposed to accounting, aspects of foreign exchange risk (Chapter 10)
- Development of marketing and production strategies to cope with exchange risk (Chapter 11)
- Evaluation of foreign currency-denominated debt (Chapter 12)
- Role of countertrade in financing international trade (Chapter 13)
- Costs and benefits of managing interaffiliate fund flows on a global basis (Chapter 15)
- Integration of tax management with financial management based on the Tax Reform Act of 1986 and the 1993 Tax Act (Chapters 15, 21, and 23)

- Understanding of the nature and consequences of international portfolio investment, including investments in emerging markets (Chapter 16)
- Development of global strategies of multinational corporations (Chapter 17), including joint ventures (Appendix 17A) and the strategy for Europe 1992 (Appendix 17B)
- Analysis of foreign investments, including assessing the true profitability of a foreign operation, calculating adjusted net present values, and factoring in various economic and political risks (Chapter 18)
- Valuation of the growth options often associated with foreign investments (Chapter 18)
- Assessment of the cost of capital for foreign investments, with an added discussion on the claimed differences between the cost of capital for U.S. and Japanese multinationals (Chapter 19)
- Understanding of political risk measurement and management, with a discussion of the dramatic changes taking place throughout Latin America, Eastern Europe, and China (Chapter 20)
- Use of interest rate and currency swaps and less-developed country debt-equity swaps (Chapter 22)
- Design of a global financing strategy (Chapter 23)
- Discussion of new perspectives on the international debt crisis and country risk analysis (Chapter 26)

CHANGES TO THE FIFTH EDITION

Changes that have been made to the fifth edition include the following:

- Extensive discussion of the August 1993 currency crises in the European Monetary System and currency crisis in Mexico in 1994–1995
- Extensive discussion of the changes taking place in Mexico and Latin America in recent years
- Pricing of currency options contracts using the Garman-Kohlhagen option pricing model, along with a discussion of its shortcomings
- Discussion of the monetary approach to exchange rate determination
- Analysis of how Japanese firms have coped with yen appreciation
- Calculating the cost of acceptance financing and factoring
- Discussion of new transfer pricing issues and "earnings-stripping" charges involving foreign company operations in the United States
- Analysis of exchange risk associated with foreign portfolio investments
- Extended discussion on alternative approaches to estimating the cost of capital for foreign operations
- Addition of several cases, including a comprehensive case on the financing and cash flow analysis of Euro Disneyland and another on risk management (Link Technologies)
- Update on Japanese banking and international risk-based capital standards
- Additional discussion of currency swaps
- Update of Chapter 21 on international tax planning to reflect tax law changes along with a discussion of value-added taxes

- Comparison of the cost of capital in Japan and the United States
- Discussion of how the Japanese financial system helps reduce the cost of financial distress
- Discussion of Euro-medium term notes

The book also contains many new charts and illustrations of corporate practice that are designed to highlight specific techniques or teaching points. Again, the emphasis is on reinforcing and making more relevant the concepts developed in the body of each chapter. To make the text more suitable as a teaching vehicle, I have added at the ends of the chapters numerous questions and problems, most of which are based on up-to-date information and real-life situations.

PEDAGOGY

The pedagogical thrust of the book is greatly enhanced by the following learning and teaching aids:

- **1.** Focus on corporate practice: Throughout the text, there are numerous real-world examples and vignettes that provide actual applications of financial concepts and theories. They show students that the issues, tools, and techniques discussed in the book are being applied to day-to-day financial decision making.
- **2.** Extensive use of examples and illustrations: Numerous short illustrations and examples of specific concepts and techniques are scattered throughout the body of most chapters.
- **3.** Lengthier illustrations of corporate practice: There are nine longer illustrations of actual company practices, at the end of key chapters, that are designed to demonstrate different aspects of international financial management.
- **4.** Problems and discussion questions: Hundreds of realistic end-of-chapter questions and problems offer practice in applying the concepts and theories being taught. Many of these questions and problems are related to actual situations and companies.
- **5.** Learning objectives: Each chapter opens with a statement of its action-oriented learning objectives. This statement enhances learning by previewing and guiding the reader's understanding of the materials that will be encountered in the chapter.
- **6.** Glossary: A glossary at the back of the book defines key terms in the text.
- **7.** Supplements: A complete set of ancillary materials is available for adopters of Multinational Financial Management to supplement the text. These include:

- An Instructor's Manual containing detailed solutions to the end-of-chapter questions and problems and tips for teaching each chapter.
- A Testbank containing over 160 additional questions and problems suitable for use in multiple-choice exams.
- Lotus 1-2-3 templates designed to solve a wide variety of international financial management problems. Problems in the text that can be solved using these templates are noted in the Instructor's Manual.
- A *Study Guide* written by Professor Anderea L. DeMaskey, University of Nevada, Reno, is available. The *Study Guide* contains detailed chapter outlines and solved questions and problems.

THANKS

I have been greatly aided in developing *Multinational Financial Management* by the helpful suggestions of the following reviewers: Robert Aubey, University of Wisconsin; James Baker, Kent State University; Donald T. Buck, Southern Connecticut State University; C. Edward Chang, Southwest Missouri State University; Jay Choi, Temple University; Robert C. Duvic, University of Texas, Austin; Janice Wickstead Jadlow, Oklahoma State University; Steve Johnson, University of Texas at El Paso; Boyden C. Lee, New Mexico State University; Marc Lars Lipson, Boston University; Dileep Mehta, Georgia State University; Margaret Moore, Franklin University; William Pugh, Auburn University; Bruce Seifert, Old Dominion University; Jay Sultan, Bentley College; Paul J. Swanson, Jr., University of Cincinnati; and Steve Wyatt, University of Cincinnati.

My family, especially my wife, Diane, as well as my mother and three brothers, have provided me (once again) with continual support and encouragement during the writing of this book. I appreciate the (usual) cheerfulness with which Diane and my children, Thomas and Kathryn, endured the many hours I spent writing the fifth edition of this text.

A.C.S. Pacific Palisades

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