

Chapter 10

Multinational Treasury Management

- 10.1 Determining the Firm's Financial Goals and Strategies
- 10.2 Managing the Corporation's International Trade
- 10.3 Financing the Corporation's International Trade
- 10.4 Managing the Multinational Corporation's Cash Flows
- 10.5 Risk Management in the Multinational Corporation
- 10.6 Summary

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Functions of the modern treasury

- Determine the firm's **overall financial goals**
- **Manage the risks** of domestic and international transactions
- **Arrange financing** for domestic and int'l trade
- Consolidate and **manage financial flows**
- Identify, measure, and **manage risk exposures**

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Setting financial goals & strategies

- Identify the firm's **core competencies** and potential **growth opportunities**
- Evaluate the **business environment** within which the firm operates
- Formulate a **strategic plan** for achieving sustainable competitive advantages
- **Develop processes** for implementing the strategic business plan

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The problems of international trade

- Exporters must assure timely payment
- Importers must assure timely delivery of quality goods
- Geographic and cultural distances are greater than in domestic trade
- Trade disputes span several legal jurisdictions

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The Murphy's Law of international business

If something can go wrong, it will.

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Managing the risks of int'l shipments

- **Trade documentation** reduces risk exposures
 - Commercial invoice
 - Certificate of origin
 - Export license
 - Dock receipt
 - Insurance certificate
 - Packing list
 - Export declaration
 - Bill of lading
 - Warehouse receipt
 - Inspection certificate
- **Freight forwarders (shippers)** can coordinate the logistics of trade

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International payment methods

- > **Cash in advance**
 - Buyer pays for goods prior to shipment
 - Buyer provides the financing
- > **Open account**
 - Seller delivers goods and bills buyer under agreed-upon payment terms
 - Receivables can be **discounted** or **factored** (sold); long-term receivables can be sold to a **forfeiter**

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International payment methods

- > **Documentary credits**
 - A **letter of credit (L/C)** issued by the buyer's bank guarantees payment upon receipt of trade documents
 - In some countries, **letters of credit** can be **discounted** or used as **collateral** for new borrowings
 - Other countries do not follow this practice

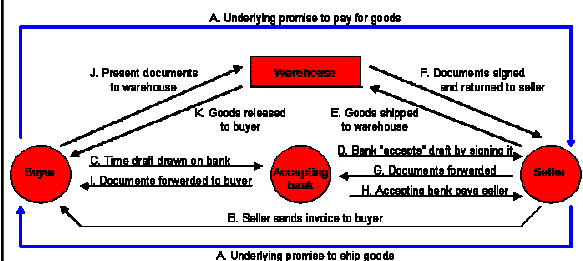
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International payment methods

- > **Documentary collection**
 - **Sight drafts** payable on demand
 - **Time drafts** payable at specified date
 - **Trade acceptances** are drawn on and accepted by the buyer
 - **Banker's acceptances** accepted by a commercial bank
 - Trade acceptances and banker's acceptances can be **discounted**

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Payment with a banker's acceptance



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International payment methods

- > **Countertrade** - exchange of goods or services not involving cash
 - Counterpurchase
 - Offset

Delivery and payment depends on the terms of trade

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Managing multinational cash flows

- > **Cash management**
 - Multinational netting
 - Forecasting funds needs
- > **Relationship management** - between operating divisions and external partners
 - Credit management
 - Transfer pricing
 - Determination of hurdle rates

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A five-step currency risk management program

- **Anticipating and responding to changes in foreign exchange rates**
 - identify the **distribution** of future exchange rates
 - estimate the **sensitivity** of revenues and expenses
 - determine the **desirability of hedging**
 - evaluate **hedging alternatives**
 - **monitor** the position and reevaluate

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Exchange rate forecasting

➤ Market-based forecasts

- Forward parity

$$E[S_t^{d/f}] = F_t^{d/f}$$

- Relative purchasing power parity

$$E[S_t^{d/f}] = S_0^{d/f} [(1+i^d)/(1+i^f)]^t$$

- with equal real interest rates

$$E[S_t^{d/f}] = S_0^{d/f} [(1+p^d)/(1+p^f)]^t$$

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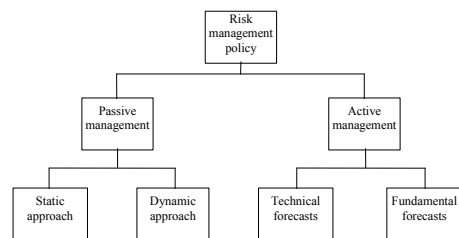
Exchange rate forecasting

➤ Model-based forecasts

- **Technical analysis** - uses the recent history of exchange rates to predict exchange rates
- **Fundamental analysis** - uses macroeconomic data to predict exchange rates

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Risk management should complement the overall business plan



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G30 Global Derivatives Study Group

- **Determine at the highest level of policy** and decision making the scope of involvement in derivatives activities
- **Value derivatives at market**, at least for risk management purposes
- **Quantify market risk** under adverse market conditions, perform stress simulations, and forecast cash investing and funding needs
- **Assess credit risk** arising from derivatives activities based on measures of current and potential exposure against credit limits

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G30 Global Derivatives Study Group

- **Establish** market and credit risk management functions with **clear authority**, independent of the dealing function
- **Authorize only professionals** to transact and manage the risks, as well as to process, report, control, and audit derivatives activities
- **Establish management information systems** to measure, manage, and report the risks of derivatives activities
- **Voluntarily adopt accounting and disclosure practices** for international harmonization and greater transparency

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