

Hong Kong University of Science and Technology

FINA 342 International Finance  
Casey Lim, PhD, CFA  
Adjunct Associate Professor  
Department Finance  
Tel: 2358 8498  
Email: [caseylim@ust.hk](mailto:caseylim@ust.hk)  
Room Number: 2429

Lectures: Mon, Wed: 2 – 3:20 pm.  
Office Hours: Mon, Wed, Fri: 10: 15 – 11: 30 am.

### ***I. Course Objectives and Overview***

In this course we will examine the institutional features of international financial markets, and address certain issues in international corporate finance and international investments.

We will be looking at the various issues in international finance from the perspectives of the various participants in the international markets. While foreign markets in the USA and Europe are very important, we will put more emphasis on the PRC, Hong Kong and our neighbouring Asian markets. Most of you will be working in these markets or with firms dealing in these markets when you graduate and a strong familiarity in these markets would give you a very good head start and advantage.

I will relate the topics in this course with the various positions or roles that business/finance graduates would be involved in after graduation. For e.g., an investment banker in Hong Kong needs to know how a Mainland company can structure its businesses for listing in Hong Kong or Singapore.

A portfolio manager needs to know the various financial instruments and the international financial markets to make informed decisions. Bond portfolio managers needs to know how to analyse balance of payments of various countries, interest rates movements in other countries, certain macroeconomic policies, etc.

An analyst doing research on stocks and debt securities needs to know what is happening in foreign markets so as to provide more well-rounded analyses on the valuation of a firm. A corporate Treasurer of a Hong Kong or multinational company definitely needs to know the international financial markets to know where else to raise funds, etc. He/she needs to know how to hedge interest rate and currency risk.

A regulator needs to have an understanding of both foreign and domestic markets so that he/she could make policies that bring about smooth functioning of financial markets. A commercial banker needs to know about LIBOR, Eurodollar rates, foreign interest rates, analyse political risk, etc., so as to price syndicated loans and project financing deals.

Several issues we will cover are given as follows. From the point of view of a multinational corporation, what are the benefits from investing overseas? What should the multinational

corporation take into consideration when planning to invest overseas? What cost of capital should it use when evaluating project overseas? Are there sources of capital elsewhere in other countries that costs less than what the corporation can get locally? What are the various mechanisms that a multinational can undertake to hedge exchange rate risk?

From the perspective of an investor, are there gains from diversifying overseas? What are the sources for such gains? What are the barriers to international investments?

From the perspective of governments and policy makers in various countries, what are the advantages and disadvantages of foreign investments in their countries? Is intervention in the foreign exchange markets feasible?

## ***II. Class philosophy:***

The student should always free to discuss, give comments and raise questions in class. My method is to encourage you to analyse and discuss the various issues in class. I will ask questions frequently so as to make sure you understand what I say. When you go up the corporate ladder in the years to come, it is certain that you will have to speak up quite a lot in meetings, etc. Getting students to provide comments and their views *will* make the class experience more enjoyable and productive. To encourage more class discussion, there will be bonus points for students doing that.

## ***III. Recommended textbooks:***

Main Textbook:

1. Multinational business finance by Eiteman, Stonehill, and Moffett (ESM), 10th ed., Pearson Addison Wesley, 2004.

Other Reference Books:

2. International investments by Bruno Solnik and Dennis McLeavey, 5<sup>th</sup> ed., 2003.
3. Multinational Financial Management by Shapiro, Alan, 7<sup>th</sup> ed., 2003.

It is advisable that students also read the South China Morning Post, Wall Street Journal, Asian Wall Street Journal, Euromoney, and other publications which are of interest to them so as to stay abreast of the latest developments in the international financial markets.

## ***IV. Course Outline***

Part I: Financing a PRC firm

1. Foreign investments in China. Learning from success stories. Venture capital financing. Structuring a PRC firm for listing as H-share or red-chip. What are possible investment opportunities in China in the near future? How could a foreign enterprise evaluate a project for investment in the PRC?

Lecturer's Notes

Part II: The International Financial Environment.

2. Brief discussion on the roles of International Trade

The theory of absolute advantage. The theory of comparative Advantage. Protectionism. Problems of trade and tariff.

Lecturer's Notes

3. The International Monetary System

ESM: Ch. 2

4. Balance of payments

Current account. Capital account. Changes in reserves. The meaning of a deficit or surplus.

ESM: Ch. 3

5. Spot and Forward Markets

Functions of the foreign exchange market. Market participants. Foreign exchange market quotations. Premium and discounts on forward quotations. Arbitrage.

ESM: Ch. 4

6. International Parity Relations

Theory of Purchasing Power Parity. Fisher Effect. International Fisher effect. Interest Rate Parity.

ESM: Ch. 6

7. Futures and Option Markets

Foreign currency futures. Forward contracts. Foreign currency options. Options on futures contracts.

ESM: Ch. 5

Part III: The Foreign Exchange Risk Management.

8. Forecasting Foreign Exchange Rates

Do exchange rates follow a random Walk? Efficiency of the foreign exchange market. Economic indicators.

ESM: Ch. 7

9. Transaction Exposure.

Causes of transaction exposure. Managing transaction exposure; forward exchange market hedge, money market hedge, option market hedge, leads and lags, re-invoicing centers, swap agreements.

ESM: Ch. 8

#### 10. Operating Exposure

Examples of Operating Exposure. Managing operating exposure; diversifying operations, diversifying financing.

ESM: Ch. 9

#### 11. Translation Exposure

Is it worthwhile to hedge translation exposure?

ESM: Ch. 10

### Part IV: Capital Markets and Financing Instruments

#### 12. Eurocurrency Markets

Eurodollars and other Eurocurrencies. Asian Currency Market. Eurodollar Bank Loans.

ESM: Ch. 13

#### 13. International Bond Markets

Eurobonds. Foreign Bonds; Yankee bonds, Samurai bonds, Bulldogs. Floating Rate Notes. Euro-commercial paper.

ESM: Ch. 13

#### 14. International Market for Equities

Problems in investing overseas. Financial analysis and valuation. International vs. domestic influence on Stock Returns.

ESM: Ch. 12

#### 15. International Portfolio Diversification

Correlations of world stock markets. Gains from international portfolio diversification. Effects of fluctuating exchange rates. Performance of international mutual funds.

ESM: Ch. 20

## 16. Cost of Capital and Capital Structure

Market imperfections and the cost of capital. Foreign sources of capital. Listings on foreign stock exchanges. Market segmentation. Exchange rate risk and the cost of debt. Theory of optimal capital structure.

ESM: Ch. 11

## Part V: International Banking

### 17. International Trade Finance

ESM: Ch. 23

### 18. Syndicated Loans, Project Financing, Political Risk Management.

Pricing syndicated loans, assess project financing deals, analyse political risk.

Lecturer's Notes.

## ***V. Grading***

One Project: 15%

Analysis of two Mini Cases: 10% per case, altogether 20%.

Mid-Term Examination: 20%

Final Examination: 45%

Bonus Points for Class Participation: 5%

Students may form groups of not fewer than 2 and not more than four to work on both the mini-cases and project. More details on the project and mini-cases will be given in class.