

PREFACE

When we were graduate students, we chose to study international finance because we wanted to understand issues such as how exchange rates are determined and how people manage the risks that fluctuations in exchange rates create. We also recognized that the economic forces that people now call *globalization* were trends that would only increase in importance over time. We like to think that we made a good call on our careers because, without a doubt, globalization of business is now a fact. Our goal with this book is to equip future global business leaders with the tools they need to understand the issues, to make sound international financial decisions, and to manage the myriad risks that their businesses face in a competitive global environment.

Over the years, the markets for goods and services as well as capital and labor have become increasingly open to the forces of international competition. All business schools have consequently “internationalized” their curriculums. Nevertheless, our combined 54 years of teaching experience indicates that most students will not be ready for the real world, with its global complications, unless they know the material in this book. They will not really understand how fluctuations in exchange rates create risks and rewards for multinational corporations and investment banks, and they will not understand how those risks can be managed. They will not really understand how to determine the value of an overseas project or the nature of country risk. The purpose of this book is to prepare students to deal with these and other real-world issues.

THIS BOOK’S APPROACH: MAKING BETTER DECISIONS BY BLENDING THEORY AND PRACTICE WITH REAL-WORLD DATA ANALYSIS

International Financial Management, 2nd Edition, continues to blend theory, the analysis of data, examples, and practical case situations to allow students to truly understand not only what to do when confronted with an international financial decision but why that decision is the correct one. When we explore international financial markets, we do so with an eye on risk management. We thereby incorporate practical considerations into what other textbooks take as background theory or institutional detail.

Multinational companies face a daunting array of risks, but they also have a wide variety of financial instruments available to manage them. In this book, we detail the sources of risks that arise in international financial markets and how these risks can be managed. For example, a basic risk of international trade involves the fact that goods are being shipped out of the country. How does an exporter make sure that he is paid? We do not stop at identifying the risks and showing how to manage them; we also reflect on why a firm should manage them and how that management affects the firm’s value. We do this by developing the valuation methodologies needed to determine the value of any foreign project—from the establishment of a foreign subsidiary to the takeover of a foreign company. Because we have a well-defined valuation methodology, we present international financial management using

a modern, theoretically correct approach, building on the newest insights from international corporate finance. How international risk management affects the value of a firm falls out naturally from our framework. We also provide considerable detail about the institutional aspects of international financial markets for debt and equity. For example, we show how firms can obtain international equity financing, but we also discuss theories and empirical work on the costs and benefits of these decisions.

WHAT'S NEW IN THE SECOND EDITION

In the new edition, all data have been updated to reflect the most recent information. The newest research ideas in international finance are reflected in the text. Some examples include an in-depth discussion of novel research on why the carry trade makes money and the risks involved in Chapter 7; a discussion of new research on exchange rate determination that explains why exchange rates are so hard to predict in Chapter 10; and new terminal value calculations in Chapter 16.

Between the writing of the first edition and this one, a global financial crisis has roiled markets and economies, and its ramifications are explored in many different chapters. Chapter 1 contains a general discussion of the crisis, and Chapter 2 explores the effects of the crisis on transactions costs in the foreign exchange market. Chapter 6 covers the breakdown of covered interest rate parity during the crisis, and Chapter 18 examines its effects on trade finance. Chapter 20 reflects on how emerging-market companies dabbling in exotic options got burned when the dollar became a safe haven during the crisis. Lessons from the crisis are drawn throughout the book. Chapter 20 now also includes an appendix that discusses the valuation of foreign currency options, and a spreadsheet is available to do the calculations.

While the first edition explored the developments leading up to monetary union in Europe, we now put this material to good use to more fully understand the recent European sovereign debt crisis in Chapter 5. Our swaps chapter (Chapter 21) now also includes a section on credit default swaps, which are important in understanding global sovereign debt markets and also played a role in the 2007 to 2010 global financial crisis.

This new edition also more prominently recognizes the increased importance of emerging markets. The so-called BRICs (Brazil, Russia, India, and China) account for an increasingly larger portion of the global economy, global trade, and global financial markets, with China dominating many debates about international business. Several of our new illustration boxes and examples provide insights about the Chinese economy and its place in global business. Chapter 1 discusses the attempted takeover of a U.S. oil company by a Chinese company; the *Point-Counterpoint* in Chapter 4 discusses the balance of payments imbalances between the United States and China and their consequences; Chapter 5 discusses China's capital controls; Chapter 12 its equity markets; and so on. We also analyze how Brazil's capital controls affect covered interest rate parity in Chapter 6.

PEDAGOGY FOR STUDENTS

This book necessarily combines theory and business practice. We provide plenty of real-world examples and case studies, and at the same time, we stress fundamental concepts, principles, and analytical theories that are bound to be more resilient to the constantly changing challenges of operating in a competitive global marketplace.

To help students develop an in-depth and enduring knowledge of international financial management, *International Financial Management*, 2nd Edition, incorporates the following features:

- **Real data analysis:** We incorporate the analysis of data in each relevant chapter to allow students to learn how well or poorly the current theories are supported by the data. All Exhibits in the 2nd Edition use the most recent data possible.
- **Extended cases:** Where relevant, we introduce and solve intricate cases that illustrate the application of theory. These case solutions can serve as templates for future analyses.
- **Point–Counterpoint features:** We reinforce the subtleties of many international financial management issues by presenting a *Point–Counterpoint* feature for each chapter. Many textbooks provide short, easy answers to difficult questions. That approach is fine when there is general agreement about an issue, but many situations are more subtle and intricate than standard books may lead the reader to believe. The *Point–Counterpoint* features are designed to raise issues that are contentious and that are often not fully resolved or well understood by the academic and practitioner communities. Each *Point–Counterpoint* feature ends by summarizing the state-of-the-art thinking on the issue.
- **Boxes:** We provide boxes to serve two purposes. First, they may contain concrete historical or current illustrations of important concepts introduced during the chapter. Second, they explore and illustrate basic finance concepts that are used in the chapter.
- **Appendixes:** We have included some mathematical and statistical material in appendixes to various chapters in an effort to make the book self-contained. We intend the book to be accessible to students with limited financial backgrounds.
- **End-of-chapter questions and problems:** At the end of each chapter, we have provided a set of interesting questions and problems that are designed to help students ensure that they have mastered the chapter material.
- **Bibliographies:** Each chapter contains a bibliography of further reading that contains not only citations to the books and articles mentioned in the text but also some additional readings that interested students can explore.

MATERIALS FOR INSTRUCTORS

At the Instructor Resource Center, located at www.pearsonhighered.com/irc, instructors can download a variety of print, digital, and presentation resources available for this textbook, including the following:

- Solutions Manual
- Test Item File
- TestGen EQ
- PowerPoint slides

Solutions Manual—Prepared by the authors, Geert Bekaert and Robert Hodrick. The Solutions Manual contains fully worked out solutions for all the end-of-chapter questions and problems.

Test Item File—Prepared by Dr. April Knill. The Test Item File for each chapter will contain approximately 25 multiple choice questions with fully worked out solutions, 5 short answer questions with answers, and 2 essays with answers. The question difficulty levels of each chapter will be approximately 60% easy, 30% moderate, and 10% difficult.

TestGen—The computerized TestGen package allows instructors to customize, save, and generate classroom tests. The test program permits instructors to edit, add, or delete

questions from the test banks; edit existing graphics and create new graphics; analyze test results; and organize a database of test and student results. This software allows for extensive flexibility and ease of use. It provides many options for organizing and displaying tests, along with search and sort features. The software and the test banks can be downloaded from the Instructor's Resource Center (www.pearsonhighered.com/irc).

PowerPoint slides—Prepared by Dr. April Knill. These entirely new PowerPoint slides provide the instructor with individual lecture outlines to accompany the text. The slides include many of the figures and tables from the text. These lecture notes can be used as is, or professors can easily modify them to reflect specific presentation needs.

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YOUR FEEDBACK

We would appreciate hearing from you! Let us know what you think about this textbook by writing to <http://247pearsoned.custhelp.com/app/ask/>. Please include “Feedback about Bekaert and Hodrick” in the subject line.

If you have questions related to this product, please contact our customer service department online, at <http://247pearsoned.custhelp.com>.

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