Managing Your Own Multinational Corporation (MNC)

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Sample paper: MNC Project

Your team-project paper should be a minimum of 18 pages in length and not exceed 20 pages (inclusive of cover page, table of contents, charts, tables, bibliography, etc.) Typing should be double-spaced using a font size of 12. For information on Datateam and other library resources for this project please contact Mr. Joel Thornton (joelthor@library.tamu.edu; 862-8933), Assistant Professor, West Campus Library.

In this project (running your own MNC), you will have the opportunity to apply key concepts learnt in the course. Many MNCs started as small firms that focused initially on exporting a single product or service to another country. The exported product or service were sold initially through a single distributor based in a foreign country or may have been sold through the mail based on mail-order ads. As for your project, you may choose your MNC’s home base to be the United States or another country. You should focus your effort on conducting business with a target country (and deal with that target country’s local currency). Many issues addressed in this project will allow you to learn a lot about conducting international business between two countries and their currencies.

1. Stage I: Develop Your Idea for Exporting (Chapters 1 & 2)

Develop a strategy and make a convincing case why your MNC would like to produce a particular product or service and initially export it to the target country. It is extremely important that you clearly (and in detail) identify the comparative advantage of sourcing the product/service at your home country and initially export it to the target foreign country. Hence, you should look into the supply side as well as the demand side for your product/service. Your idea should be practical to the degree that you could possibly implement this project yourself someday. However, your idea should also be sufficiently creative to be successful if done properly. You should focus sales to one target country and its currency since many MNCs started operations in this manner. To appreciate issues related to foreign exchange rate risk that are discussed in this course, you should assume that you will receive foreign currency (other than the home currency) when selling your product abroad. The following questions will help you define your MNC objectives:

1. What product/service do you plan to produce at home (rationale? competitive advantage?) and sell abroad?
2. What foreign country (and why) do you plan to target? What is their demand for your product/service?
3. How will you market the product in the target country? (i.e., through a distributor? retailer? franchise? By mail? etc.)
4. What is your evidence (or rationale) that consumers in the target country would buy your type of product/service?
5. Will you need to purchase foreign inputs or hire foreign labor to sell overseas?
6. Will any expense that you incur related to production and marketing the product/service be in the target country's currency?
7. Identify factors such as tariffs/quotas that can affect trade in goods/services between your home country and the target country of business. Explain how each of these factors may affect the demand for your product.

8. Which of the above factors, if any, is likely to be most important in affecting the demand for your product?

**Accessing Trade Data:** Determine whether the product/service that you plan to sell is already one of the main exports to the target country. (Sources: Economist Intelligence Unit (EIU) West Campus Library; www.state.gov/r/pa/elia/bgn/; and www.cia.gov/library/publications/the-world-factbook/docs/profileguide.html (CIA - The World Factbook, Guide to Country Profiles); www.stat-usa.gov/tradtest.nsf; globaleedge.msu.edu/resourceDesk/).

**Accessing Import Controls:** Review the import controls set by that country's government. Determine whether your business would be affected by trade regulations.

2. **Using the Foreign Exchange Market to Ensure Payment for Exports (Chapter 3, 5, 11, and 19)**

1. Explain how you will ensure payments for your exports.
2. What bank do you plan to use to exchange the foreign currency received for exports? What is the bid/ask spread (in percentage) in the spot market for the foreign currency on a recent quotation by that bank? (Call the bank to obtain quotations or check a financial newspaper or DataStream. Determine the prevailing bid and ask exchange rates for the foreign currency that you will use for your business transactions.) What is your interpretation of the spread’s magnitude?
3. Explain what types of forward contracts are available for hedging.
5. Are currency options available to hedge the exchange rate risk of your company?
6. Will the importer of the product/service be willing to pay you with the home currency? Why could this be a problem for the importer?

3. **Forecasting Foreign Currency Movements (Chapters 4 & 6)**

1. Go to http://www.oanda.com Click on FXTrends. Explain how the target foreign currency for your business has moved over (a) the last month, (b) the last three months, (c) the last year, and (d) past five years. Is there a trend over the last year? Last five years? What is the mean percentage change in each of the above four periods.
2. Is it likely that the target foreign currency will follow the past one-year trend? If you believed that the currency's value would continue following the recent trend, would it appreciate, depreciate, or remain about the same in the near future? What key factors likely affect the value of the foreign currency of concern over time? Does the foreign central bank intervene to support/weaken their currency? How will you determine this? (Accessing Central Bank Information: Go to http://research.stlouisfed.org/fred2/categories/32145. Go to the Web site link for the central bank in your target country. Determine whether this central bank...
intervenes to control its currency in the foreign exchange market. Also, by looking at that country’s balance of payments statistics (level of international reserves and exchange rate movements over the same time period) determine if foreign central bank intervenes in the foreign exchange market? How will that affect your business?

3. What key factors (using regression analysis - using monthly or quarterly historical data) likely affect the value of the foreign currency of concern over time? Based on this information forecast (next five years) the exchange rate of the target foreign currency. Will the foreign currency (a) continue to strengthen, (b) continue to weaken, or (c) remain stable at current rates over the next five years. You will use this forecast in your cash flow analysis in State II of your project.

4. Stage II: Establishing a Subsidiary in Foreign Country (Chapter 13)

1. Assuming that your international business strategy is successful, identify how you would go about establishing a subsidiary in the foreign country rather than continue exporting. Develop a cash flow statement for a five-year (investment year + four years of operation) project. Utilize the foreign exchange forecast (Item #3) that you developed earlier to adjust your five-year cash flows.

2. Given the nature (economic and geopolitical environment) of your foreign target country, identify your exit strategy associated with your MNC subsidiary.

5. Recognizing Exposure to Exchange Rate Risk (Chapter 10)

When you created your business strategy, it was assumed that your receivables would be denominated in the foreign currency in Stage I. In Stage II, operations are somewhat different.

1. Describe and quantify your exposure to foreign exchange rate risk in Stage II. Describe the exchange rate conditions (stable, appreciating, depreciating, fixed, etc.) affecting the performance of your business.

2. Is your business subject to transaction exposure? economic exposure? translation exposure? Explain why your business is or is not subject to each of these types of exposure.

6. Deriving a Required Rate of Return for an International Project and Assessing Exposure to Country Risk (Chapter 14, 16, and 17)

1. Explain the capital structure that you would use to run your foreign subsidiary.

2. Describe the economic factors that expose your subsidiary to country risk.

3. Describe the geopolitical factors that expose your subsidiary to country risk.

Having decided to establish a subsidiary overseas as indicated above, determine how you would derive a required rate of return (using WACC and country risk premium: http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/ctryprem.html) for this project.
7. Conclusion

Based on the subsidiary's cash flows in foreign currency, exchange rate forecast, your required rate of return, and capital structure, determine your project's net present value and determine if your project will be viable.