

# INTERNATIONAL FINANCE – PROF. MURILLO CAMPELLO

## Final Project Details: Milestones & Objectives (and Tips for Success)

### 0. Intro

The goal of the final project is that you use the main elements of our International Finance lectures in an applied problem. For this to work, you have to make the problem as realistic as possible. This project will account for 30% of your grade in the course and only one grade will be assigned equally to all members of a group. The only exception to the same-grade rule applies to cases where a group member is referred to me by all other group members as unwilling to work and uncooperative. That student will get a lower grade. All students in a group must be officially enrolled in the same section of the course (no cross-section enrollments). Both a memorandum and a formal presentation are needed for this assignment. Plan for no more than 25-page long memo (plus tables, graphs, etc.) and for a (approximately) 20- or 25-minute presentation (depending on class size). As a ‘general guideline’ to the grading procedure on this, I assign 2/3 of the points to the written memo and 1/3 to the presentation, but in reality I look at the whole project as a package. Notice that since you are in charge of creating a problem and solving it, there will be little to say as to whether the analysis is absolutely “right” or “wrong.” As is the case in real business life, there will be poorly- versus well-conducted discussions of a business argument; consequently, some of the grading will be based on comparisons of arguments across different groups (i.e., you will be judged both on an absolute as well as on a comparative basis). The memo and the presentation must be professionally executed.

### 1. Relevant dates

Fourth/Fifth Week of Classes (or as announced) – Provide via e-mail the list of people in the group (min. of 2 and max. of 4 people, depending on the class size), the foreign country(ies) and the industry to be studied. Individual projects are not allowed. Please, select one contact person in the group and have that person (only) send that e-mail to me. The contact person is in charge of communicating to me changes in the list of group members and any other material news regarding the project (including, members dropping the class, change of country/industry of interest, etc.)

Note: When sending the project e-mail, the group’s contact person should “cc” the e-mail to all members and write the following in the e-mail’s subject line:

“International Finance, Final Project Group, Class Time Section ???”

Tenth Week of Classes (typically right after Spring Break) – **[OPTIONAL]** Submit a hard copy of the initial parts of the memo. This should contain some details the company and its proposed investment (of course, not yet the full financial analysis of the particular project), and full complete analysis of issues covered in the course up to that point: analysis of country-level economic, financial, legal, etc. environments. I'll return this memo to you in a few days with either of 3 following remarks:

- *Very Satisfactory*: which means that you can use the current country-analysis in your final memo.
- *Marginal*: which means that the analysis is “acceptable,” but should be generally improved.
- *Unsatisfactory*: which means that the analysis is generally poor and requires major overhaul.

Note: Don't turn in “half-baked” 1-2 page memos at this stage. I can always talk to you about the progress of your group, but I can't seriously grade a 1-2 page note with just a general plan/idea in it. To help you with in writing the initial memo, I provide a list of issues that I expect to have covered up to Lecture Note #4—and thus should be included in your initial memo—in Part 5 of these notes (see below). Again, do not send me a rudimentary report that you know will not meet the minimum standards for this task (e.g., if all you have is very basic country facts, it does not meet the criteria of this report).

Third/Second to Last Week of Classes – Submit both a hard copy and an electronic version (in a properly (detailed) labeled floppy disk, CD, or flash drive) of the final memo no later than Friday (**April 18, 2008**) 5:00 pm in my mailbox at 340 Wohlers Hall. Do not submit your project via e-mail (these will be disregarded). Make copies for you since I'll keep in archive all the materials that you submit. Note that I will check your project against projects submitted by other groups in this year as well as against projects submitted in previous years to my class. As is standard at the University of Illinois, any signs of plagiarism will be dealt with to the fullest consequences of the rules of the University. These are very harsh and my include expulsion from the University.

Last Week of Classes – Group presentations. Group dates will be randomly assigned and class attendance is absolutely required for all presentation dates.

**Note:** Missing any of these deadlines will imply point losses in your final project's grade. In particular, missing the last deadline will imply a 50% automatic loss of the project's total points (30% of your final grade)! There will be no time to make-up/compensate for this large loss with other course activities.

## **2. Short Description**

The description of the project is broad on purpose; your own inputs are the main ingredients of the project. Construct a scenario about an existent or fictitious company trying to invest in a foreign country. Be specific as to what kind of service/product the company sells right now and what are the plans to take it

internationally. Perhaps your company makes toys, and is currently planning to open in China a plant twice as large of that you currently have in the U.S. You are part of the finance department in the company and the CFO asks you to prepare a memo containing the most important issues to be considered when investing in that country from a (mostly) financial perspective, but also concerning strategic issues (e.g., demand for product and industry competitors). A solid project will contain: 1) country- level analysis, 2) industry- level analysis, and 3) firm-level analysis.

### **3. Execution**

It is part of the assignment to identify the most relevant issues pertaining to the country you chose. The relevant issues will, of course, also depend on your company's line of business, on the mode of entry, etc.

Possible scenarios/discussions could be as follows. Maybe corporate taxes are so high that investing in apparel manufacturing in India is a bad idea, as Pakistan has the same potential but lower taxes. Maybe political/economic instability is so high in Argentina that opening a new plant there should be disregarded for the next two years. Investing in Germany could be a good idea for your firm, but note that falling interest rates in that country means that the dollar will rise in the future and thus receipts from Germany needed to be heavily discounted or we might spend a lot of money hedging against those undervalued cash flows. Perhaps opening a car manufacture in Mexico looks attractive, but the tendency of the local government to fix the Peso/\$ FX at artificially high real rates for long periods poses a problem in terms of global competitiveness. Maybe investing in Japan is good, but you have to be aware of problems that foreign firms have faced before in dealing with Japanese suppliers and thus you might want to keep your French suppliers, but then you are exposed to even greater exchange rate risks (both A/Ps and A/Rs denominated in foreign currencies). Maybe your MNC wants to sell (desinvest) our gold mines in Angola if a certain left-wing party wins the presidential elections (expropriation risk). Maybe you want to invest in an oil-dependent industry only after a meeting of the OPEC countries, as they will decide on their oil exploration policies for the coming years. Maybe your MNC wants to go to Peru via FDI, say invest in telecommunications infrastructure, if it can secure a monopoly from the government for the next 15 years.

Of course, you want to analyze the industry conditions in the country you are studying. You have to ask questions such as: Are there significant growth trends (in demand) for products? Are the local competitors protected by the local government (local legal monopolies or trade tariffs/quotas)? Are there many foreign firms willing to enter (assuming they are not there yet)? Are there many large competitors able to put up a fight should you enter? Or are rivals mainly small firms? Any particular environmental or labor laws

affecting business in this industry? Is the local government inviting foreigners to invest in this sector (tax breaks, free land, tax-free fund repatriation, etc.)?

Finally, you must also present actual company-level financial statements (i.e., NPV-type calculations). The best guidance for international capital budgeting (mainly cash flow estimations and currency conversion) will be the “Wendy’s in Neverland” case discussed in Lecture Note #3. Another good reference is the discussion of the Olin Corporation case (discussed later in the course). Make sure that you construct your case (i.e., make investment recommendations) after contemplating a number of different scenarios for the proposed project. Sensitivity analysis is a must here!

The memo you prepare must have arguments such as (but not necessarily exactly like) those just suggested above. The arguments must be clearly and concisely constructed, and must be accompanied by supporting (real data) financial analysis. Only include information that is relevant for decision-making. (Irrelevant text will hurt your case.) At the end of the memo you must clearly indicate whether or not the firm should pursue the proposed project. Usually in this case, there’s no right and wrong, just well- and poorly-constructed supporting arguments/recommendations.

#### **4. Tips for project memo and presentation**

Start the paper and the presentation giving the background of the problem: who is your company (country of location, size, and current lines of business), which industry your company is interested in investing abroad, which foreign country is your company considering, why does that particular country would look attractive in the first place (consider mostly broad, non-financial reasons here: local demand, good geographical location (easy to export from there), well-trained workers, cheap labor, good/enforced law system, etc.). Then tell us (i.e., me and the other students in the classroom) about the purpose of you report. For example, maybe you were asked by the CFO to present a summary of your research on a proposed investment in Germany to the board of directors of your company, or maybe to a group of equity investors, or even regulators. Your task is to characterize this situation before start talking about the details of your memo. (It is often useful to say up front how much money we are suppose to invest, so we have a sense for the “size/importance” of the project very up front.) Then after presenting what is the problem before the company (e.g., whether to invest in joint-venture in China or in S. Korea), give a well thought out recommendation. Note: In the final presentation phase all students vote on the other students’ projects. Over the years, this has shown incredible value added to the experience. Bad presentations will be disliked by you and your classmates, while great ones will be lauded as such. It is quite amazing how close the

students' votes capture the quality of the projects, even when the audience hasn't really read the written memo.

When presenting facts about a country and an industry remember a few important things. First, provide insights about them. For example, the current exchange rate figure only matters if you can make sense of it in a context, otherwise is just a meaningless number. (Remember, this is not a history lesson about a country nor about statistical figures one can get on the internet. Any high school student can collect these simple things.) Second, make sure you know (cite) the sources of your "facts" (e.g., provide all web addresses and article cites used). Past/current facts are useful, but make sure you emphasize future prospects (look at forecasts made by analysts in the private sector and/or by government agencies).

In writing the memo, do not use small font size (min. 11pt) and avoid single-space page format. Also, the final project must be put together in a professional form (e.g., use a neat binder). Colorful covers, tables, etc. are usually a plus. Do it "fancy." It is only a few bucks more, and you split the cost with multiple group members. In the end, competition with other groups matter (just as in real life). Expect your group rivals to give their best in their memos too!

When choosing a country and industry, make sure you make selections for which you can find a lot of data on. I.e., don't choose to describe the idea of investing in the apparel industry in Cambodia if you find that there is little data on both the apparel industry as well as on Cambodia. Once and a while one could make "educated guesses" when data is not available, but if nearly no data are available chances are that you will make a series of potentially large miscalculations.

Use proper sequence of ideas. There's no "unique" formula for that, but make sure that your report/presentation has a natural flow of ideas. Example: I know this fact and that other fact, therefore I conclude you should follow such and such course of action.

Be focused on what really matters! Give us some broad idea of what's going on in the country of your choice, but make sure you emphasize the issues that affect your industry/firm.

Dress well and be (and look) confident and assertive. Be nice and considerate in handling questions from the audience – they will come inevitably as I'll potentially give extra points for members of the audience who ask questions. Look at your audience all the time (not at the computer or blackboard). And try to smile, look comfortable.

At either the beginning or the end summarize your recommendations. A short list of pros and cons will help.

**Practice your presentation prior to coming to class!** It won't do any good for the group if during

the presentation it feels like one (or more) of the presenters has not prepared the talk in advance, and doesn't really know what's going on. You have to look integrated as a group and individually deeply knowledgeable about the project (country, industry, and firm). Reading facts off of some piece of paper counts little towards a convincing talk (in fact, it hurts more than it helps). If time gets tight towards the end (it always do) be prepared to skip some of your slides in a nice smooth way, simply highlighting the main points. When time is short, don't insist in reading through all your transparencies just because you wrote them, nor speak faster. Save time and grace, going overtime will be penalized (just like in the real-world). The overall good flow/smoothness of the presentation is **key**.

Over all, it the group's responsibility to ensure the project (both paper and presentation) has a meaning, and thus it is worthwhile for me to read the memo and for the other students in the class to assist the presentation. If the presentation/memo comes across weak and pointless to everybody in the class, you should expect a low grade on the final project.

I expect that most presentations will be conducted in Power Point. I think this is the ideal means of delivering the project. However, let me remind you that glitches occur sometimes (e.g., files are corrupt or not uploaded correctly). Because of this, I urge you to have other means of delivering your project in the class when you are called. Having trouble loading your electronic file is not an excuse for not presenting the project when requested. I'd suggest that you have multiple ways to retrieve your file (e.g., on the web, on a USB key, and on a CD) and also have traditional transparency slides handy should all else fail. Unless there is a power outage or if the class computer is otherwise completely inoperable, the group is responsible for not preparing a plan to present under less than ideal circumstances.

*Excess hurts:* Grossly exceeding the stipulated parameters for memo length and presentation duration will hurt your grade in the final project.

Note: Every group member should be assigned a part of the presentation. Part of the grading of the presentation will be driven by the individual performances. As such, one bad performance will have some impact on the overall group grade.

Final note on the presentation participants (**important**): If one of the group members is not able to make it to class on the day of the presentation this will not excuse the rest of the group to go ahead and present all of the project. It is expected that all of the members know the contents of the entire analysis. Again, this is a group effort! If the group won't present, this will lead to an irrevocable massive loss of points in the final grade. This will make me very sad, but there is nothing I can do about this.

Note for the other class participants (non-presenters): Each presentation is a "board meeting." I'll distribute a "ballot" so that you vote on the presenters' recommendation. This will help me assess the

quality of the presentation as well as in informing me of who came to class and who didn't. Also, I'll bring the class roster with me and will be making side marks on the people asking (relevant) questions. Those people will **potentially** (no promises) have 1 or 2 extra points added to their final grade (which goes from 0 to 100, so this can be very important in the end).

### 5. List of topics discussed in class (initial memo)

As a suggestion for the project's initial memo content, let me list here some of the particular points pertaining to each of the chapters of our textbook which you should consider, as these are discussed in class. I believe that a good memo should contain, among various other things, most of the following points:

- Chapters 2-5: Brief analysis of the balance of country's payments (e.g., current account, capital account, and financial account). Find your country's exchange arrangements in the textbook (of course, it may have changed recently). Describe the currency of your country (e.g., historical nominal and real FX value vis-à-vis US\$). Inflationary trends, surplus/deficit national budgets, international reserves, FX volatility. (Recall the Merrill Lynch analysis shown in class.) Will economic and monetary projected trends hurt or help entry in your country of choice in the next few years? The IMF's and the World Bank's webpages are a good source of information for some of the items here (see also YahooFinance). The Economist's (Intelligence Unit) also has interesting data as well as forecasts. Analysis of how receptive a country is to foreign investments (laws, taxes, etc.) is found in the US State and US Commerce departments.
- Chapter 17: Description of the country's tax system (perhaps also the neighboring country's tax system; big issue in Europe). Look at table in textbook as a starting point. How does it affect to the proposal of the investment?
- Chapters 14 and 19: Descriptive analysis of the components of your country's main sources of risk; is it political or financial? How does the country rank its risk "indices" as provided in the financial press (see also book). What can (or should) we try to negotiate with the host country's Government. How is the legal environment of the country? Are laws friendly to business (particularly foreign firms) and do they seem to be enforced? Is corruption a potential problem? How does corporate governance work there? Does that country have an active market for corporate control? Does it help or hurt your entry plans?
- Chapters 6, 7, and 8: Description of the most likely hedging instruments to be used. For example, if dealing with China, then absence of the Chinese currency in organized markets will make using futures contracts infeasible. Options markets are perhaps promising (even though expensive) when dealing with European countries.