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International financial management: 35 years later—what has changed?

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Abstract

International financial management, essentially an extension of corporate finance to a global context has undergone an extraordinary metamorphosis since the mid-1960's. From a relatively stable and predictable economic environment at that time, the forces of inflation, technological innovation, and deregulation led to new and volatile markets and a plethora of financial instruments. Many of these developments would not have been possible without the academic research in this subject which went from mainly descriptive and anecdotal to analytical. Arguably the most important theoretical developments in finance took place since then: the capital asset pricing model [CAPM], option pricing models, and the recognition of agency costs as a potential conflict of interest between management and shareholders of a firm. These are still areas of disagreement: the cost of capital for a company with global markets and investors needs more study; managing currency, interest rate, and other risks in a complex international organization is still a work in progress. On balance, the case can be made that the changes seen over more than three decades have been positive.

Keywords: Financial environment; International financial management; Capital investment; Cost of capital; Foreign cash flows; Risk management; Currency forecasting

1. Background

It was more than 35 years ago that Michael Brooke and I began to look at some of the issues raised by the rapid expansion of multinational business. We had embarked on a Ph.D. program of studies at the University of Manchester under the supervision of Peter Smith of that institution. Michael's focus was on how multinational companies (MNCs) were organized and how the various parts of the

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group and the management in different countries related to each other; mine was mainly how they managed their finances and controlled their operations. Although a number of other studies were getting underway at that time, with a particularly large and well-funded effort started at Harvard, I think it is fair to say that we were among the pioneers. Up to that time, relatively little academic attention had been given to addressing this subject which was beginning to concern, even to preoccupy, policy makers in Europe, North America, and elsewhere. This began to create a demand to understand better the impact MNCs would have on the economies, institutional and social structures of the various countries where investment took place. This quickly stimulated the offering of courses to study this phenomenon at universities and in business school programs. Not much was available to serve as teaching material for these courses. I think the fact that we sold between 10,000 and 20,000 copies of *The Strategy of Multinational Enterprise* (Brooke & Remmers, 1970),[1] the book that grew out of our research, attests to this demand and relative lack of anything solid at that time on which to base a serious course of study.

2. Research methodology in the 1960s

Part of our research was based on a large number of interviews of company managers in Europe, both at corporate headquarters and at the level of the subsidiaries, government officials, and of professionals mainly in the accounting and tax advisory services. This gave us a valuable insight into management practice at the time. The travel that this required was done on more or less a shoestring budget—a grant of £ 1,000 (worth maybe £ 6,000 or £ 7,000 in today's money) from the OECD plus a modest salary from our respective institutions. A serious problem that we encountered was the lack of financial or accounting data available on individual affiliates or subsidiaries of MNCs from which cross-sectional or longitudinal analysis could be done. Therefore, an important part of the study concerning financial practices was building a database. This was laboriously constructed from an analysis of the annual accounts filed by over 100 British-based subsidiaries of foreign companies covering the 9 year period, 1959–1967. Comparable data from other host countries were not accessible. Aggregate data describing financial practices of MNCs were also obtained from official sources as well as from various other studies. We did not have access to computers to help process and analyze data, classify information, or even to put together and edit our study. Cut and paste was literally what we did. In fact, electronic calculators were not even available at that time. Data tabulation was done on a hand-cranked calculating machine; multiplication and division using a slide rule. Of course, in the 1960s, no Internet existed to mine for information or data, or to help check sources. No convenient data bases providing easy access to historic exchange rates, interest rates,

[1] Translations were published in French by éditions Sirey, 1973, and in Japanese by Sangyo Nohritsu Tanki Daigaku, 1975. A second edition was published in 1978 by Pitman, London with a Spanish translation by ediciones Aguilar, Madrid 1981.