

# Exam 2 Cheat Sheet

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Brooks Walsh

- 1) Futures: Standardized // on-exchange // marked-to-market // initial performance required  
Forwards: Customized // Over-the-counter // maturity @ Forward rate // Bank relationship required
  - 2) Selling/Buying Futures:  $(\text{change in Price}) \times (\text{contract value}) = \text{change to performance bond}$
  - 3) Call Option: right to buy at strike price // if:  $\text{Strike} < \text{Spot} \Rightarrow \text{In-the-money}$  (spot = real)  
Put Option: right to sell at strike price // if:  $\text{Strike} > \text{Spot} \Rightarrow \text{In-the-money}$
  - 4) Exposures: Transaction: contractual cash flows // Operating: Firm Value // Translation: Financial statements (Accounting)
  - 5) Hedge Transaction: Forward Hedge // Money-Market Hedge // Options market hedge  
 Forward: sell Foreign Curr. forward // MM: Borrow Foreign curr. // Puts: buy For. Options  

  - 6) Operating Exposure: Operating CFs affected // changes in competitive positions (unmeasurable)  
Effects: Competitive: CFs affected by comp. position // Conversion: given CF in For. Cur. converted to less \$
  - 7) Translation Exposure: Fin. statements of Foreign subsidiaries must be restated in dom. curr. for consolidation
  - 8) Current Rate: AL use current E // IS (Ret E) use Avg E // Dividends use pay-date E // common stock uses Historic E
  - 9) Temporal Method: Monetary Assets use current E // Nonmonetary assets use E @ value statement // rest same as CR vs. TM: Curr. Rate gains/losses reported separate (on BS) // Temporal method gains/losses  $\rightarrow$  consolidated income  
Balance Sheet Hedge: keep equal exposed Assets=Liabilities // Monetary Balance w/ temporal method // complete balance is impossible w/ curr. rate
  - 9) Market liquidity: Firm can issue new security without depressing existing price (decreases WACC)  
Market segmentation: If required return on securities differs from comparables (increases WACC)
  - 10) Appropriate to use WACC as disc. rate on projects when risk of project is same as overall firm
  - 11) Euroequity is the initial sale of shares in two or more markets and countries simultaneously
  - 12) Cross-Listing: Pros: Improve Liquidity // increase P by overcoming mispricing // increase visibility // position for M+A  
Cons: disclosure/listing requirements // validity spillovers from overseas // potential of foreign take-over
  - 13) Domestic Beta:  $B = (\text{Corr}_{\text{Firm} \times \text{Dom}} \times \text{SD}\%_{\text{Firm}}) / \text{SD}\%_{\text{Dom}}$  // World Beta:  $B = (\text{Corr}_{\text{Firm} \times \text{World}} \times \text{SD}\%_{\text{Firm}}) / \text{SD}\%_{\text{World}}$
  - 14) ADR: Calc Price per share in dom curr. then multiply by shares per ADR
  - 15) ADR: shares held by For. Bank  $\Leftrightarrow$  ADR in dom. bank // represent and act like typical shares
  - 16) Eurobond: International bond issued in non-native currency (GER bond of USD in UK) // Foreign Bond: issued in native-currency  
Eurobond Advantages: Less regulation interference // less disclosure requirements // Favorable tax status
  - 17) Coupon on Floating-Rate Notes:  $C_p = \text{FaceVal} \times (\text{Libor}_{n\text{-term}} + \text{addition}) // (n\text{-term per year})$
  - 18) Political risk Mitigation: Stakeholder Engagement // Dom. Partners // Inv. Agreements // Gradual investing // Blocked Funds // Dispute Resolution
  - 19) Foreign Project: Tracked in Parent company terms // Only invest if:  $\text{Project}_{\text{Foreign}} - \text{Risk} > \text{Project}_{\text{comparables}}$  // Political risk insurance
  - 20) Cross-Border M+A vs. Greenfield: M+A tend to be: Faster, large opportunity // easy to pay too much, culture-diff, Political risk
- | Hedging Strat | Action-Inflow (receivables)  | Action-Outflow (payables)  | Proceeds  |
|---------------|--|--|---|
| 1) Forwards   | Sell For. Cur. Forward @ $F_t$ rate                                | Buy For. Cur. Forward @ $F_t$ rate                                     | Init. amount @ $F_t$ rate   |
| Money-Market  | Borrow For. Cur.; convert (PV) $\rightarrow$ invest $\text{dom}^*$ | Borrow Dom. Cur.; convert (PV) $\rightarrow$ invest $\text{Foreign}^*$ | Invested amount $\times (1 + i_{\text{loc}})$                         |
| Options       | Put option for transaction amount                                  | Call option for transaction amount                                     | Premium: Trans. Amount $\times \text{SPOT}_0 \times \text{Premium}\%$ |
- Inflow Break-Even:  $(\text{Trans.} \times S_t) - (\text{Prem} \times (1+i)) = \text{Proceeds from comparison (Find } S_t)$   
 Outflow Break-Even:  $(\text{Trans.} \times S_t) + (\text{Prem} \times (1+i)) = \text{Proceeds from comparison (Find } S_t)$   
 In:  $\text{Trans.} \times \text{Max}(\text{SPOT}_t, \text{Strike}) - \text{Prem} \times (1+i_{\text{dom}})$   
 Out:  $\text{Trans.} \times \text{Min}(\text{SPOT}_t, \text{Strike}) - \text{Prem} \times (1+i_{\text{dom}})$
- 2) CTA account Balance:  $\Sigma (\text{differences between method rate and actual Spot rate})$  (see 8 above for current rate method)  
For temporal method: (Cash, A/R, etc...) uses current E // (FA, Inv, etc...) uses rate @ valuation // I/S uses Avg E (dep use Hist.)  
 $\rightarrow$  Dividends use date-of-payment E // Equity uses Historical E // No CTA == more NOI volatility
  - 3) PPP:  $F_n = S_0 \frac{(1+i_f)^n}{(1+i_d)^n}$  //  $S = \frac{P_t}{P_t^*}$   $P = \frac{\text{Price of goods basket}}{\text{Price of goods basket}}$  // IRP:  $F_n = S_0 \frac{(1+i_f)^n}{(1+i_d)^n}$   $\leftarrow$  i.e. of  $n^{\text{th}}$ -year bond  
 Conversions:  $CF_0 = CF_0^* \times S_0$  //  $CF_1 = CF_1^* \times F_1$  //  $CF_2 = CF_2^* \times F_2$  //  $CF_n = CF_n^* \times S_0 \frac{(1+i_f)^n}{(1+i_d)^n}$   $\rightarrow$  use FinCalc for NPV
  - 4) writer  
 BE = Strike - Premium // Intrinsic = Strike -  $S_0$ , 0  
 Max Profit = Premium // Max Loss =  $(\text{Strike} - \text{Prem}) \times \text{Op. Val.}$   
 Holder  
 BE = Strike - Premium // Intrinsic = Strike -  $S_0$ , 0  
 Max Profit =  $(\text{Strike} - \text{Prem}) \times \text{Op. Val.}$  // Max Loss: Premium  
 Time Value of Put: Premium - Intrinsic  
 Call  
 BE = Strike + Premium // Intrinsic =  $S_0 - \text{Strike}$ , 0  
 Max Profit = Premium // Max Loss =  $((S_0 - \text{Strike}) - \text{Premium}) \times \text{Op. Val.}$   
 BE = Strike + Premium // Intrinsic =  $S_0 - \text{Strike}$ , 0  
 Max Profit =  $((S_0 - \text{Strike}) - \text{Premium}) \times \text{Op. Val.}$  // Max Loss = Premium  
 Time Value of Call: Premium - Intrinsic