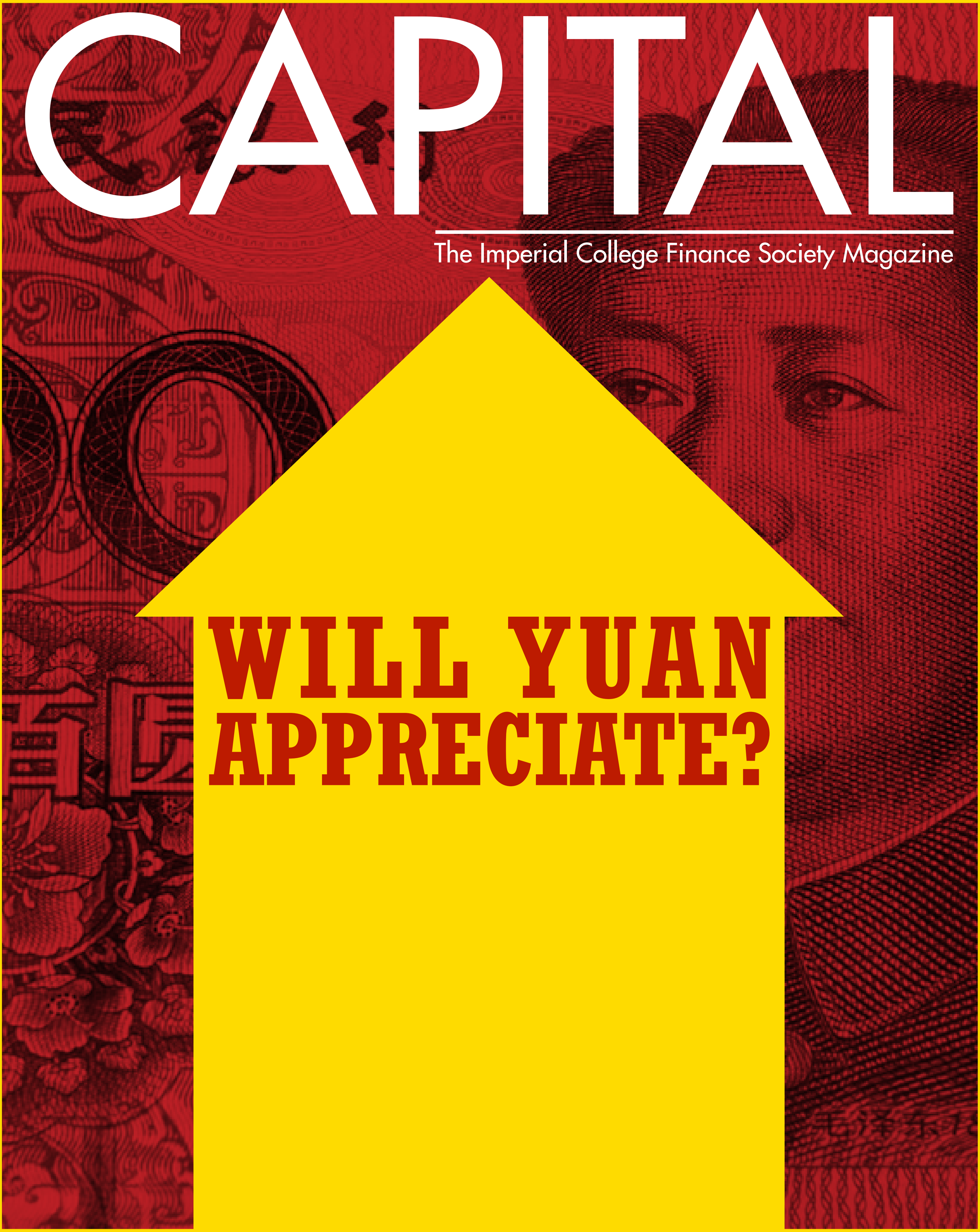
Spring Issue - Insights 2013

CAPITAL

The Imperial College Finance Society Magazine



WILL YUAN APPRECIATE?

The uniqueness of the Japanese Yen

Opportunities and Challenges for RMB Internationalization

INSIDE BUZZ - Interview questions you should be prepared for

This issue

4

6

10

14

16

19

Chief editor
Mario Hayashi

Editors
Giri Kesavan
Deepka Rana

Contributors
Dat Cheam
Tao Ding
Shiyang Zhang

Cover designer
Lazar Vukadin

Stock photos
123rf

Print production
Mixam Print

Contact
Capital Magazine is a publication of the Imperial College Finance Society. If you have any questions about our publications, please e-mail us at **giridhar.kesavan10@imperial.ac.uk or deepka.rana10@imperial.ac.uk**

Visit our website
www.financesociety.co.uk

Thank you for reading this magazine.

President's welcome

Dear Members,

A warm welcome to our Spring issue of Capital Magazine – a new Asia-themed publication which also contains our year in review for 2012-2013 ! Along with the support of our sponsors, Imperial College Union, Imperial College Business School and of course our 3000+ members, the ICFS has had an incredible year and we are thrilled with the great feedback we've had from across the industry on a national and international scale.

When we were planning our activities for the year we knew that above all, we truly wanted to create a more informal, relaxed and fun society and it was great to see that our members identified perfectly with this new society ethos. Indeed, it's made my role far more interesting (and challenging) that I could ever have expected! I've truly enjoyed the creative freedom with Facebook banners and YouTube videos – and thanks to everyone for the positive feedback on all these new marketing initiatives.

At the time of writing, we've run around 50 events and 2 conferences, a mini finance course and we're of course looking forward to our 2 international trips – Hong Kong and Kenya ! This has been coupled by a huge surge in membership and thriving social media accounts. A personal thanks to all of our members who have supported the society by attending our events and taking advantage of the opportunities!

Of course, a critical factor in our success has been my spectacular committee – who have performed far above and beyond all expectations – it's really been the dream team for me this year.

Thomas, thank you for transforming the way we look at analytics and for building a truly next generation sign-up platform for the society. It's been a critical part in streamlining our mailing list operation and it's provided the next committee with a solid platform upon which to build on.

Tia, thank you for handling all ICFS transactions swiftly and efficiently. We've had almost 200 transactions this year and thanks for keeping on top of everything – and making sure we are compliant with VAT rules in the process! Strict financial control has been a major strength this year and you've set the benchmark for how to handle the record budget of the society this year whilst keeping the union closely informed.

Avtar, you did it ! Thanks for all the logistical planning and organisation of all the events on and off campus throughout the year. It's hardly been straightforward with the introduction of specific, tailored events per sponsor – but all events have been met with exceptional feedback. Thank you for leading a highly pro-active and determined event officers team who have truly redefined the way an event is run.

Mario, Capital Magazine in the Autumn was a tremendous success and thanks for your hard work over the summer in putting it together. Despite numerous deadlines and a high workload – I'm delighted that we've managed to do two issues of our flagship publication this year so thank you for truly taking CapMag to a new level.

Tracy and Christine, thank you both for always being ready to lend a helping hand towards the society and of course for the quick and efficient organisation of the Annual Dinner for this year. Thanks for helping out in our Market Insights videos and for handling member requests and queries swiftly.

You've certainly eased my own workload – many thanks !

Thanks to our committee and our dedicated members, we've been able to truly transform the ICFS this year – leading to ESSA Accreditation as an enterprising society. We've also been thrilled with being named as one of the top 3 student societies in the whole of the UK by Rate My Placement (by the time you read this, we'll know the final result!).

None of the above could have been achieved without the unwavering dedication, commitment and effort shown by Deepka over the last year. From our marathon meetings over the summer, over 6000 emails/texts and endless discussions and organisation, you've truly defined the society over the past year. Hard to believe that 12 months ago I barely knew you! I could not have asked for a more calm, hard--working, kind, loyal, efficient and trustworthy friend to help me achieve my vision this year. You've been a dream Vice President and I'll always be eternally grateful for your help in making this an unforgettable year in ICFS !

So I guess this is it ! I hope all our members and committee enjoy reading this new Spring Issue of Capital Magazine and enjoy looking back on an action packed year. This year will truly define my time at Imperial and I'm incredibly lucky to have shared it with a fantastic member base and what has been the most amazing team of friends I've ever worked with. Thank you to you all and I wish you well for your remaining time at Imperial and your future careers.

Giri Kesavan
President
Imperial College Finance Society 2012-13
giridhar.kesavan10@imperial.ac.uk
www.financesociety.co.uk

President of Imperial College Finance Society 2012-2013

Hong Kong skyline & urban skyscrapers at night. ICFS HK trip is the next big thing.

Manifesto review

With a record number of events and activities this year, the ICFS has truly cemented its place as not only the leading careers related society at Imperial – but on a national scale. I promised a lot in my election manifesto last March and it certainly was a significant challenge to top the great platform set by the previous committee. However, thanks to our great team, we truly believe we have exceeded all expectations and have set the foundations for a fantastic 2013-14. I've just listed here some of our key achievements this year – it's beyond the scope of the review to list every tailored event – but I've included the main ones ! I'd of course value your own thoughts on how you feel we've done – please feel free to just send me an email with your feedback and comments.

This review doesn't include the New Financial Worlds Conference or the Imperial College Investment Club – both of which ran as total subsidiaries under ICFS and as such, have had their own committees this year.

Finance Industrial Placements in the Department of Electrical Engineering
The EEE department introduced a six-month industrial placement scheme that enabled students to gain a longer term of work experience as part of their degree. We realised that in order for students to have diverse opportunities, it would be fantastic if students could undertake these industrial placements at investment banks. Over the summer, we drafted a 20-page proposal document to the EEE department, outlining the transferable skills that engineers would gain by working at investment banks and how these could be applicable to an EEE degree. The department accepted our proposal and the role profiles and as a result, EEE students are now able to do a range of placements in Investment Banks (naturally mostly in Technology although non-technical roles are allowed) across the city – directly creating and giving students opportunities at no cost.

Record number of sponsors and level of sponsorship
With a targeted approach to sponsorship over the summer and a clear strategy for each firm, we were able to generate record levels of sponsorship for the ICFS. This was due to a change in tactic – we went out to sponsors directly and pitched rather than relying on outline proposals (which we also wrote). This led to the generation of personal links with our sponsor firms – so much so that we're now literally friends with all of our investment bank contacts! We wanted to main this close link with our firms throughout the year hence the reduced importance placed on the CLO sub-committee this year. We found that with just two people handling all company contacts – the link between ICFS and the firm was significantly stronger (although it did increase our workload) and this has been the key reason why we've been successful in sponsorship this year.

Multiple editions of Capital Magazine
The publication you're currently reading didn't exist last year ! I felt that we should really emphasise Capital Magazine this year as it gives a chance for students to put across their own viewpoint on financial issues as well as being informative for all members. The Autumn issue proved to be a startling success with so much demand that we ran out of magazines at Freshers Fair on Day 1. As such, following this great success we decided to publish a second issue in the Spring – with a theme of Asia to relate to our Hong Kong trip. We believe our totally in-house produced Capital Magazine really highlights the creative aspect of the society and we are proud of its elevated position within ICFS this year.

ICFS Hong Kong International Trip
Having helped organised the New York trip last year, I had a good idea of the strengths and weaknesses of prior international trips and we used this to our advantage. Put simply, the trip to Hong Kong is the most ambitious yet and required precision planning. We collaborated with our sponsors last September and all company visits were booked in October – with flights booked by November. This long term planning has helped us create what will be an unforgettable trip towards the end of March. As with Capital Magazine, we really wanted to put the focus on the trip and turn it into our flagship event of the year – sponsors correspondingly agreed and championed the trip, with Asia Pacific recruitment events, profiles on a new dedicated Asia webpage and of course, hosting our members for company visits in Hong Kong. ICFS HK is turning out to be an amazing, unforgettable and genuinely useful experience for our members!

New role of Senior Vice President
This was unexpected and purely happened by circumstance. Over the summer, I realised that sponsors really liked dealing with just two people for all communication – and as Deepka & I were both in London to do sponsorship this happened automatically. Following the start of the academic year, it became evident that the role of VP Partnerships was rapidly increasing in importance and considering the effort and commitment put in by Deepka – I felt that the role should

Imperial College London
BUSINESS SCHOOL

"The array of financial institutions who visit the Business School throughout the year has provided me with an opportunity to interact with industry professionals and develop an understanding of both current market conditions and future career opportunities."

David Doherty
MSc Finance 2012

MSc FINANCE
MSc RISK MANAGEMENT & FINANCIAL ENGINEERING

To learn more, visit:
imperial.ac.uk/business-school/future-career-opportunities

change to reflect the level of work. As such, we changed our constitution to remove the roles of VP Partnerships and VP Corporate Relations – consolidating them into one role: Senior Vice President – which made Deepka second in command of the whole society. I feel that this is more reflective of the workload and also more importantly, it gives a team dynamic to ICFS leadership.

Corporate Citizenship Conference
Being a keen volunteer and having been involved in volunteering internationally – I really wanted to highlight the Corporate & Social Responsibility side of investment banks through a dedicated conference. We successfully collaborated with the Student Led Projects Symposium (SPS) and Imperial Hub for this fantastic pilot event which was a stunning success and a great collaborative effort. ICFS secured the speakers, Mithila Patkunan from the SPS secured interested student projects and marketed the event, while Imperial Hub showcased their own activities and how students could get involved. It was a very wide reaching event – students had a chance not only to learn about CSR projects from guest speakers but also had a chance to pitch their own CSR projects for £750 worth of sponsorship funded by the ICFS. Furthermore, this was a national conference and we had delegates from several other universities attending. As a pilot event, it was essential that it went well and thankfully the conference proved to be a success.

Change in ethos & marketing
This is really what I'm most proud of this year. I've always felt that ICFS takes itself too seriously and should simply just relax a bit ! None of us are bankers – we are all students ! As such, I wanted the committee to lead by example and be pretty informal in our outlook. This has driven a sense of community, approachability and has ensured members are not intimidated by the society. As such, we totally transformed marketing – and it helped that I'm interested in digital graphics and film ! With initiatives such as Market Insights (our own news show), professional quality trailers for events and pretty much a fun new Facebook cover photo every day – it's really kept members interested and has kept the society fresh. ICFS no longer has a professional outlook however it delivers professional opportunities and maintains professional relationships. The fact that we've been able to do this throughout the year has transformed the relationship that we have with members. Simply put, people now actually know who the committee are and are interested in the society itself – not only individual events. I'll definitely miss doing all the fun marketing this year! Our sponsors have also loved this – as one firm said: "You're the only society I've seen that comes to a sponsorship pitch and shows us a Facebook group with a picture of Gandalf."

Technology & Social Media
Another key strength of this year has been the strong technology focus. Thomas has done a great job of building and providing the technology platforms that we need to market events and keep members informed. I've had fun maintaining our YouTube channel (which has over 4300 views) and my new found obsession: Twitter. With over 190 followers on Twitter in just a couple of months – delivering 24/7 market news direct to members, it's really been an overhaul. The Facebook group has gone from just containing marketing text to having cool banners, pictures and videos on a daily basis – and the group has almost doubled in number since last October ! It really is one of the most active society Facebook groups at Imperial and we are proud of our social media legacy.

Special Events – DB & BAML
As Deepka & I both have worked at BAML & DB respectively – we gave our "home" firms special events that showcased them to the whole society. Deutsche Bank was our sponsor for the Autumn term first year dinner, a new initiative where we took 25 first year students and 6 DB reps out for dinner in the City for an informal evening dinner. The best event of the year however was undisputedly the BAML Winter Festival. Whoever thought an ICFS event would have a 100kg ice-sculpture, Christmas trees, fake snow and huge cakes ? The Winter Festival showcased Bank of America to over 120 members in the Autumn and was our flagship event of 2012. Again, it proved that our informal approach endeared members to our events – resulting in great turnout.

Tailored Company Events
Usually sponsors request events to be run with societies. That's not quite how it worked in ICFS ! Deepka and I specifically talked through tailored sponsorship proposals and marketing packages for each individual firm, ensuring that we suggested events, not our sponsors. This meant that we were confident about the success of each event – as from personal experience we knew that members would like them ! It meant that pretty much no event was a generic company presentation and so events were far more innovative, useful and targeted. Finally of course, it ensured that despite the large number of sponsors – we were able to successfully differentiate between our sponsor firms, keeping everyone happy!

ICFS Kenya International Trip
As a follow up from the Corporate Citizenship Conference, we decided to run a second international trip on a similar scale to Hong Kong – taking members to Kenya in June to work on microfinance projects and initiatives. Co-ordinated with Enactus (SIFE) Imperial and the MASH Foundation Trust, we are going to Kenya to build upon the work done by SIFE projects and introduce members to this whole new area of finance. A totally pilot initiative, we are keen to see the feedback from the trip in June and I'm sure it will match Hong Kong – ending our year in ICFS in style !

Cross Partnership with Imperial College Business School & Finance Imperial
We've always wanted a closer link with the Business School and we achieved those aims this year with over 700 members from Imperial College Business school attending our events. The Business School became a Platinum sponsor and we now work closely together on cross-marketing events and organising initiatives. One of our key initiatives was to run a mini finance course series to introduce Undergraduate students to the world of academic finance and further MSc study. At the time of writing, this pilot course has been completely organised and is about to start ! It's just another example of a pilot initiative that next year's committee can build upon.

Overall, we feel that we have vastly exceeded the expectations of all our members and our sponsors and this has been met with national recognition, with ESSA Accreditation and Rate My Placements naming us as one of the top three student societies in the whole of the UK. The key this year really has been our relaxed, informal and fun approach, tailored events, innovative marketing and most importantly, a team of close friends united with a common passion for the ICFS and a superb Senior Vice President. As such, we truly feel that this year has been a tremendous achievement at all levels and we have no hesitation in stating that this has been by far the most successful year in ICFS history – and we look forward to the next committee taking the society to even further heights !

Giri Kesavan
President
Imperial College Finance Society
2012-13

momentum

Set opportunity in motion

Careers in Europe, the Middle East & Africa

Face challenges with confidence. Nimbly navigate every obstacle in your path. It's that unique quality that's positioned you where you are today. And it's what we value at Bank of America Merrill Lynch. Join our team, and we'll open your career path and give you new opportunities to take the possible and make it real. We'll solicit your input and provide training, mentorship, and support to boost your aspirations to a global level. And as part of the world's leading financial institution, you can create the kind of opportunity that begets greater opportunity and bigger impact than you ever imagined.

baml.com/campusEMEA

Bank of America Merrill Lynch

The uniqueness of the Japanese Yen

What makes the Yen so special?
An examination of the currency's unique characteristics
By Dat Cheam

There are 178 currencies in the world today but just 7 of them account for 80% of the world's foreign exchange. The Japanese Yen is one of the seven above, which is fitting considering that Japan is home to the world's third largest economy. Nonetheless, the Japanese Yen and the Japanese economy in general have provided the world with several lessons in monetary policy. From the "Lost Decade" to current valuations, the historical conditions that have shaped the anomaly that is the Yen will be presented.

The Bubble of the 80s
Post-war Japan saw incredible growth as Japan shifted its focus from an expansionist military state to an industrialised nation. This was a golden age for Japan, as for three decades it saw its economy grow by leaps and bounds. Average annual growth rates (as measured by GDP) for the 1960s were a staggering 10%, followed by 5% in the 1970s and 4% in the 1980s. Even at 4%, Japanese growth was outpacing its contemporaries in the developed world with the US registering 3% in the same timeframe. However, unbeknownst to policy makers of the time, rising stock and real estate prices were forming a bubble - a bubble that was soon to be popped.

The Lost Decade of the 90s
The overheating Japanese economy was brought to an abrupt standstill at the start of the 1990s. Equity values plunged 60% from late 1989 to August 1992, while land values in 2001 were in some places less than 30% of their peak value. There are several theories behind the severity of the Lost Decade, among which are the central bank's stop-go interventions. The Bank of Japan's (BoJ) initial policy of low interest rates led to the markets being flooded with cheap credit, which in turn led to rapid growth and the beginnings of the bubble. Concerned with rising asset prices and inflation, the BoJ then decided to intervene by restricting the money supply in the late 1980s. Their methods were effective in putting a stop to rising asset prices, but at a terrible consequence: rapid deflation and a liquidity trap. Consumers stopped consuming, having no confidence that they can earn a higher rate of return (as cash would increase in value relative to fixed assets in a deflation), as well as believing that goods and services will simply be cheaper tomorrow.

The BoJ then dramatically reversed course by cutting its interest rates to historical lows in the hopes of kick-starting their economy. It was too late however; the vicious cycle was already in place. It took a decade of several ineffective fiscal policies, but nonetheless in 2001, the BoJ began to re-inflate their economy through its money supply (by debt monetization).

The aftermath from the Lost Decade continues on to this day. Japan has rarely exceeded a 2% annual growth between 2001 and 2011, and the effects of the event on Japanese policy makers have yielded a somewhat politically-influenced BoJ, which in turn directly affects the free-market flows of the Yen.

The Yen Carry Trade
Due to the incredibly low interest rates as an aftermath of the Lost Decade, the Yen of the 2000s became synonymous with the carry trade. Generally speaking, the term "carry trade" implies borrowing at a low interest rate and investing in an asset that provides a higher rate of return, thus allowing the investor to leverage and pocket the difference. The Yen, with real interest rates close to 0%, is thus uniquely suited for this trade. By early 2007, it was estimated that about US $1 trillion had been invested in the Yen carry trade, making the Yen one of the most borrowed currencies in the world.

However, there is a caveat in that the Yen carry trade only works when there are higher yielding (and thus usually riskier) assets available to the investor. This unravelled in late 2007 when the global credit crunch forced scarce returns on practically every risky asset class, prompting investors to liquidate their portfolios in favour of safe-havens such as bonds. Speculators unwinding their Yen carry trade to repay their Yen-denominated loans and further repatriation of the Yen drove the Japanese currency to surge against its rivals. In 2008, the Yen had gained a staggering 29% against the Euro.

The Currency Wars
As a result of the unprecedented global economic meltdown of 2008, central banks around the world attempted to stimulate their economies by inducing liquidity. Interest rates were cut to encourage borrowing and spending, while bonds buybacks were issued to essentially place liquid cash directly in the hands of investors. Wall Street called it "quantitative easing". It was in truth, nothing short of printing money.

With an increased money supply, currencies that had undergone quantitative easing were soon being devalued by virtue of supply and demand. The Yen, which was already at such low interest rates, began appreciating relative to currencies such as the Dollar and Euro. This hurt the export-driven Japanese economy severely as it relied on a weak Yen to make its exports more competitive.

How can I go further, faster?

If you've got the drive and ambition to ask, then come and talk to us. Our clients across the world demand people with exceptional skills and knowledge to help them make vital business decisions every day. That's why we provide world-class mentoring, training and professional qualifications to take you from strength to strength.

Start a career that goes further, faster:
ey.com/uk/careers

ERNST & YOUNG
Quality In Everything We Do

The Bubble in the 80s, low interest rates and the Yen carry trade are few of the many properties of the Yen that make the currency so unique

In response to the currency wars and its middling growth, the Japanese government soon joined in, demanding a 2% inflation target from the BoJ. This target was astonishingly high, considering that inflation had barely topped 1% in its past years, and thus was an indirect license for the BoJ to pursue aggressive easing. Markets responded immediately with the Nikkei posting fresh highs and the Yen devaluing from ¥76 to ¥90 per USD. Nonetheless, as the past 20 years has shown, whether further calls for liquidity will spur growth remains to be seen.

The Japanese Debt
The direct consequence of its abnormally loose monetary policy can be seen in the Japanese national budget. The continuous spending has led to a current debt load of a massive 230% of its annual GDP. By contrast, Greece, the most indebted of the crisis EU nations, had a debt load of 165% in its worst times. Such profligate spending would have, in most countries, alerted the world to a ticking time bomb.

Japan once again proves an anomaly. Unlike most countries, most of its debt is held domestically, i.e.: it borrows money from its own people. What's more, the Japanese are apparently so convinced that their government would be able to pay off its debts that they are continuing to lend money. Japanese borrowing rates are at a mere 0.75%, even less so than Germany, the euro-zone's healthiest economy.

The Yen Today
The Yen today remains an oddity with its own set of governing economic theories. It retains its safe-haven appeal despite its massive national debt, so much so that several Asian countries retain the Yen as a secondary currency in their central banks. Its export driven economy relies on the promotion of a weak currency, as opposed to the common notion of "strong is good" held by a consumer-centric country such as ours. Furthermore, severe disasters that cripple its economy such as a tsunami hardly weaken the Yen; instead, repatriation flows to repair the damaged infrastructure actually strengthened the Japanese currency.

" Carry trades still remain a major funding source and help lend to the safe-haven appeal of the currency. "

The BoJ is also continuing on its path of low interest rates and bond buying despite its past ineffectiveness and obvious risk to its expanding budget. Despite the low rates however, the Yen carry trade is now less attractive since central banks have largely cut their interest rates as well. Nonetheless, carry trades still remain a major funding source and help lend to the safe-haven appeal of the currency.

The Yen today also remains a traditional market determinant of risk. Currently, the Japanese currency is often traded in tandem with risk-sensitive currencies such as that of the Australian Dollar in carry trades. The USD/JPY pair is also known to have a close correlation with US treasuries and thus appeal to risk plays by speculators.

Lastly, recent currency flows have brought a field day for the Yen bears. The fall of the Japanese currency on the 2% inflation target set by Prime Minister Shinzo Abe has led to what is known as "Abe-conomics". Whether Abeconomics will be different from its predecessors remains to be seen, but in the short-term at least it seems to have finally placed Japan in a favourable position.

Deutsche Bank
db.com/careers

Do you have to be a banker to work in investment banking?

Agile minds value ideas as well as experience

Graduate Outreach for Women (GROW)

In a highly competitive job market, there has never been a broader range of opportunities available to graduates. But how to make the most of them? And what skills will you need to succeed in a highly competitive world? GROW is designed to help you. If you are a female student in your first year of study and unsure about your career path, think of this as a chance to discover your motivation and potential through access to valuable skills and development training, whilst gaining a privileged insight into the range of opportunities available in an investment bank – opportunities that go beyond just being a banker.

GROW runs throughout your studies, and comprises a tailored series of workshops and events. Together these will provide you with valuable skills training, industry exposure, development and networking opportunities. At the end, if you want to learn more about our industry, you'll be in an excellent position to make a successful application to our Global Analyst Internship Program.

For further information and how to register, discover something different at db.com/careers/GROW

Passion to Perform

Opportunities and challenges for RMB internationalization

What lies ahead for the Ren Min Bi (RMB)

By Tao Ding

With more and more Chinese studying, travelling or doing business abroad, the Chinese currency, Renminbi (RMB), has become more and more influential. In the next decade, the internationalization of RMB may become one of the most important financial developments in the world. In the course of last decade, things such as the continual growth of the Chinese economy and subprime mortgage crisis (that led to the financial crisis in 2008) make people contemplate the probability that the USD may lose its status as the world's reserve currency.

The Chinese government has the incentive to promote the RMB as a world currency. China has been recording consistent trade surpluses since 1995 but China's trade surplus may, in the future, turn to a trade deficit because of an increase in imports resulting from a large population base and lack of natural resources. However, China can seize the initiative if it can purchases the resources it requires in domestic currency. Furthermore, if trade between China and other countries can be settled in domestic currency, China can, to a great extent, avoid monitoring by the United States. There would, therefore, be more flexibility to export goods and import the required natural resources.

The new global economic structure also has a positive impact on accelerating the pace of the internationalization of the RMB. During the financial crisis, USD liquidity dried up and in order to preserve USD reserves, neighbouring countries and trading partners of China agreed to the cross-border RMB trade settlement program offered by China's central bank, the People's Bank of China. Under the agreement, foreign firms are able to borrow RMB funds for trade settlement from local banks. In other words, foreign firms can import goods from China by paying in RMB instead of USD. Although it has been almost 5 years since the advent of the financial crisis, both foreign countries and Chinese government are interested in extending the time horizon of the program.

The internationalization of the RMB has been a popular topic among international banks from the start, because it means a new opportunity for them. The development speed of international banks such as HSBC and Standard Chartered, in Mainland China, has been constrained. But, every transaction, or deal, involving the RMB, is totally new to them. With the largest networks in developing countries, those banks are able to benefit from international trading with China. In fact, some banks have taken action. On April 18, 2012, HSBC launched London's first offshore Yuan bond, also known as "dim sum" bond. It's also a signal that London may become a centre for offshore Yuan trading alongside Hong Kong. On Nov 14, 2012, Standard Chartered launched the Renminbi Globalization Index (RGI), which is the first benchmark of its kind to properly and effectively monitor Renminbi-based business activity around the globe.

Challenges usually come with opportunities. With the progress of the internationalization of the RMB, it might weaken the control of government over capital flows and ability to set interest rates and so forth. For instance, the initiation of the internationalization of the RMB coincided with the period that China was experiencing an overheated economy. The inflow of RMB increased the pressure on excess domestic capital. Money will always flow to the most profitable area. When the Chinese government reduces the constraint on the convertibility of the capital account, capital can inflow and outflow more freely. As a result, the regulatory authority will have to confront the new challenges.

In contrast to the foreign-owned banks, stated-owned banks in China have little incentive, or interest, to push the internationalization of the RMB. There are a couple of reasons to explain their behaviour. First of all, stated-owned banks have relatively small global networks. Most of them only cover the Chinese market. They don't have any advantages when competing with others in foreign or third market. Second, stated-owned banks don't have enough incentive to expand their global network. In Mainland China, stated-owned banks have absolute advantages and are protected by the government-mandated spread between the deposit rate and the lending rate. With the pressure of meeting capital adequacy ratio, Stated-owned banks want to spend the capital on the most profitable and stable businesses. In other words, they are reluctant to be involved in any risky businesses even though businesses may bring profits. Without the full support from stated-owned banks, the RMB may walk advance at a much slower pace on its way to internationalization.

With the expectation of the appreciation of the RMB, it has become quite popular among investors. However, apart from the lure of appreciation, RMB assets have limited attraction for investors. In the event that the exchange rate of the RMB remains basically in the equilibrium, bi-directional volatility may be reinforced. This phenomenon may be beneficial to the development of derivatives, but, as an asset, the RMB's attraction to investors is reduced. Additionally, the internationalization of the RMB depends on the continuing performance of Chinese economy and the degree of reform and opening-up policy, which are quite uncertain.

Although people seem to have reached the consensus that the internationalization of the RMB is an inevitable trend, there are lots of debates about the process such as, the risks involved, how big the risk is and how fast the pace should be. If the RMB could be converted freely in the future, government's control over capital inflows and outflow will be definitely weakened. I believe, however, that the benefits will outweigh the cost.

Will the Yuan appreciate?

A look into the dynamics of the Ren Min Bi (RMB)

By Shiyang Zhang

Graph 1: Imports from China by the USA is much greater than the exports to China during the past two years (this is similar for the rest of the world), resulting in a continuous trade surplus for China

Graph 2: USD/CNY over the past year

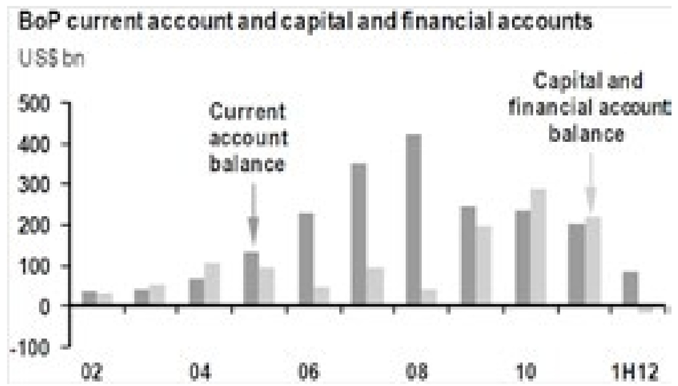
The term "Yuan" is used in the sense to represent the modern Chinese currency — Ren Min Bi (RMB), and it is the base unit of Chinese currency. Therefore when talking about the appreciation and depreciation of Yuan, we mean RMB. Therefore we ask, what could be the reasons for the RMB to appreciate? Why hasn't the RMB appreciated much even under the pressure of USA? And what are the advantages and disadvantages if the RMB appreciates? Also, what is the Chinese government is aiming at? This article will illustrate those points, and hopefully by the end you will have a basic understanding of RMB.

So, what does appreciation mean? In reality, the appreciation of RMB will only reflect on the international market. For example, on 14th Jan, RMB hit a new high against US dollar at 6.2696:1, however, on 21st Jul 2005, the ratio was 8.11 Yuan per US Dollar - indicating a 29% increase of RMB's appreciation against the Dollar. That simply means the purchasing power of RMB increased, in another term, one Yuan can buy more units of goods than before on international market. Therefore, what makes RMB appreciate? And where does the pressure come from? The biggest pressure comes from the USA as the USA is the biggest importer of Chinese goods. The USA claims that the cheap price of Chinese goods results in mass unemployment of US industries and they want the RMB to appreciate in order to drive the price for producing goods to the same starting point as the Chinese manufacturers. However, this argument could be of limited usefulness because when RMB appreciates (Jul 2012-Nov2012), the imports from China do not decrease but increase by roughly 33%. The reason is that goods being exported from China are mainly labour intensive goods, which the USA does not produce much of. Furthermore, it has a relatively inelastic price elasticity of demand, therefore as RMB appreciates, exports from China does not decrease.

As can be seen on Graph 1, the imports from China by the USA is much greater than the exports to China during the past two years (this is similar for the rest of the world), resulting in a continuous trade surplus for China – meaning that the demand for RMB will be much higher than the supply of RMB, which has a tendency to drive the price of RMB higher in free market trade. What the Chinese government do, in simple terms, is to "make" the supply of RMB higher by buying the Dollars to drive the demand and supply for RMB in equilibrium - this is criticised by the USA as currency manipulation, implying that China has rigged the trade market in its favour.

Graph 3 shows that both current account surplus and capital

Graph 3: Current account surplus and capital account surplus have been falling. Notable: capital account deficit for the second quarter of 2012



account surplus have been falling, even a capital account deficit for the second quarter of 2012. A downward trend has been marked, if China's trade surplus keeps shrinking, following the weak demand in European countries suffering from recession. The net balance might possibly become negative. Then either the Chinese government will use its massive amount of foreign exchange reserve to keep RMB up, or let the market force to push the currency down. However, following a 7.8% increase in GDP for China last year (the first time below 8% for the last 13 years), the imports of China is likely to decrease and trade surplus might grow again.

Another upward pressure for RMB is the hot money flow; hot money literally means "quick in, quick out." It could be a huge amount of money, which pushes the demand for RMB, driving the appreciation. Indeed, it is very hard to calculate the amount of hot money, but the trend could be possibly predicted, following the rising period of China's macro-economy in the forth quarter last year. International hot money might target China due to the economic growth rate and the return on investment. With the upward trend for the appreciation of RMB, hot money is likely to flow into China's financial assets.

What else could put an upward pressure for RMB? As the USA is China's biggest exporter and 25% of China's GDP comes from exports; the RMB is pegged to the US Dollar by the Chinese government as over the past years, China has accumulated a massive amount of US government debt. If RMB appreciates, which means the Dollar depreciates, the scale of the debt would therefore be smaller than before, and the depreciation of the Dollar would result in a stimulation of the USA's export industries. China has an average growth rate of 8.5% over the last few years; therefore RMB is regarded as a life-saving straw by the world economy. Pressure came from everywhere in the world: Asian countries like Japan are trying to secure their own position by putting upward pressure on RMB.

> " There are already some facts in favour of RMB: China has grown to be the second largest economy in the world, the biggest exporter and the second biggest importer, holding the largest amount of foreign reserve currency. "

Therefore, what is going to happen if RMB appreciates? Will the Chinese government allow RMB to appreciate? Firstly, just like a coin has two sides, the appreciation of RMB has both advantages and disadvantages. China's export industries are the first to be affected; appreciation of RMB will drive the price high therefore decreasing demand. Countries like China, which heavily depends on exports, could not afford the loss in its export revenue - this would result in companies closing down and unemployment rates increasing. However, the appreciation might stimulate the reforms of exporting firms, to improve the technology thus the production efficiency. A good example is Japan: during 1949-1971, the exchange rate was fixed at 1 Dollar to 360 Japanese Yen, after 1971, the fixed rate regime collapsed and Yen started to appreciate, the loss in the international competitiveness stimulated Japanese firms to innovate and reform their structure - the production efficiency offsetting the loss in competitiveness. Therefore in the long term, appreciation of Yuan might improve the exports.

Secondly, the appreciation of RMB influences the foreign direct investment (FDI) – the buying in of capital from another country. The appreciation of RMB might decrease the amount of FDI as the cost of employing labour and buying machines will go up. The possible slowing down of FDI might result in growing unemployment of labour, increasing the social instability. Furthermore, as mentioned above, the hot money flow caused by the appreciation of RMB will increase – and based on the fact that the financial regulation system of China has lots of defects, it is likely that the hot money would create more "bubbles." Furthermore, the expectation that RMB is going to rise further could possibly attract more hot money creating false prosperity. Finally it might lead to financial crisis. Therefore, the Chinese government will pay very careful attention to the exchange rate.

Thirdly, the appreciation of RMB will make imports less expensive and therefore the standard of living could improve as imports become cheaper. The appreciation also supports the foreign direct investment by Chinese enterprises, simply because it is cheaper. However, when import prices become cheaper, the Chinese agriculture sector becomes less competitive and this would result in Chinese farmers (the largest group of people by sector in the country) losing their welfare and means of sustainable living.

Finally, what is facing RMB in the future? What the Chinese has done in order to make RMB as a world reserve currency? There are already some facts in favour of RMB: China has grown to be the second largest economy in the world, the biggest exporter and the second biggest importer, holding the largest amount of foreign reserve currency. However, there is still a long way for RMB to go to become the world reserve currency: The completely convertibility of RMB is essential and the capital account liberalisation is also a critical precondition. RMB has to conquer speculative investment, the reform of capital markets, interest rates and exchange rates. Therefore, in the long term, to become the world reserve currency, RMB has to be the charge unit, medium of exchange and measure of value. The appreciation of RMB is unpredictable, based on the fact that so many factors are influencing it. However, it is widely believed that RMB will become a more stable currency and gradually replace US dollars.

Tricky Interview Questions

By Inside Buzz

CORPORATE FINANCE / CORPORATE VALUATION

How do you value a company?
This is quite a broad question, so start with the methods you would use and go through them one at a time. It will also impress if you discuss the pros and cons of each method. The main ways to value a company are: precedent transactions analysis, comparable company analysis and discounted cash flow analysis.

1

Precedent Transactions Analysis
This is when you look at how much others have paid for similar companies to the one you are valuing to determine how much the company is worth. To use this method effectively you need to be extremely familiar with the industry of the company you are valuing as well as the normal premiums paid for such a company. This can be a relatively easy method to use since all the information is public and thus easy to obtain and also since the past transactions actually happened, you can be confident that analysis based on this is extremely plausible. But on the other hand, what if the market during the past transactions was extremely different from present market conditions? Can you really base the value of one company on the value of another that is not exactly the same? These are some issues you should think about before your interview so you can discuss them at length with your interviewer.

2

Comparable Company Analysis
This is similar to Precedent Transactions Analysis except you are using the whole company as a comparison unit, not the purchase of a company. So to use this method you would also seek out similar companies to the one you are valuing and look at their price vs. earnings, EBITDA, stock price and any other variables you think would be an indicator of the health of a company.

3

Discounted Cash Flow Analysis
This is when you use future cash flow, or what the company will make in the future, to determine what the company is worth now. To calculate DCF you need to work out what the projected or future cash flow is for a company for the next 10 years. Then work out how much that would be in today's terms by "discounting" it at the rate that would give a return on investment. Then you add in the terminal value of the company and that will tell you how much the company is worth. Though this is the preferred method to value a company, it still has its flaws because the projected earning and discounted rate are figures that you set using your best guess, there's no concrete maths equation to work it out so DCF does have a certain amount of subjectivity to it.

What's a leveraged buyout?
A leveraged buyout (LBO) is when a company or investor buys another company using mostly borrowed money, loans or even bonds to be able to make the purchase. The assets of the company being acquired are usually used a collateral for those loans. Sometimes the ratio of debt to equity in an LBO can be 90-10. Any debt percentage higher than that can lead to bankruptcy.

EQUITIES

What is a P/E ratio?
This stands for price to earnings and simply is the price of the share divided by the earnings per share (EPS). This will tell you the price of the stock related to the earnings of the company. So if a stock has a high P/E ratio that means it's expensive as you are paying more for those earnings per share. If two companies have the same EPS but one has a higher P/E ratio, that one is a more expensive of the two and means you are paying more for the same EPS. Often the P/E ratio as expressed by saying that a company is trading at 20 times its earnings if it has a P/E ratio of 20.

What is a PEG ratio?
This stands for Price/earnings to growth ratio and takes the P/E ratio and then accounts for how fast the EPS for the company will grow. A stock that is growing rapidly will have a higher PEG ratio. A stock that is well priced will have the same P/E ratio and PEG ratio. So if a company's P/E ratio is 20 and its PEG ratio is also 20 some might argue that the stock is too expensive if another company with the same EPS has a lower P/E ratio, but that also means that it's growing faster because the PEG rate is 20.

Tell me about specific stocks you like
The interviewer may ask you about individual stocks or companies and what you think of them. They may also ask you to "pitch a stock", which means you'll have to pick a company you know of and make a strong argument as to why investing in them is a good idea. It goes without saying: if you are not up on the latest stock news, financial trends, and general business current events, you shouldn't be in the interview in the first place. Before your interview make sure to take a close look at a few companies and their stocks, pick two or three that you would buy. Write down brief bullet points as to why you would buy them (Are you impressed with their management? Have they successfully negotiated a tricky situation? Do their financials look particularly healthy to you? Do their institutional investors give you confidence?), a bit about the company and also list some similar companies that have done well so you can use them as favourable comparisons. Basically, you need to know everything about these companies from why they've been in the news lately to which market factors could affect them. Even go into detail about their cash flow statements so you know the company inside and out. Most importantly, make sure you can argue your point well and think about how to defend yourself if your interviewer plays "devil's advocate" to try to rattle you. Also do this same exercise for a few companies you would short. You can never prepare enough of this specific kind of information in preparation for an investment management interview.

Let's discuss a company that you think is undervalued. Why is it undervalued? Give me an example of a company you think is overvalued and why.
It goes without saying: if you don't read up on the financial aspects of multinational companies, the latest industry news or study any trends, then you will not have a successful interview. Look into some companies and their stocks and then decide whether you think they are overvalued or undervalued. Write down why you think that along with facts to bolster your argument. Try to memorise your points but it wouldn't hurt to have them with you so you can quickly refer to them (avoid blatantly reading off the page). If you can pick out a company whose stock has gone down based on some bad press, but you're not convinced that the bad press is really going to affect the bottom line - that would be an example of a company that you think is undervalued. Obviously, go into as much detail as possible. Any knowledge of the industry, history of specific companies and any other knowledge you can display in your interview, the better.

FIXED INCOME

What is duration/Macaulay duration/ Modified duration?
Duration is a measure in years that not only measure how the bond will react to changing interest rates, but also how long it will take for the fixed income payments to be made Macaulay's Duration is a formula widely used to calculate duration and is named after the man who came up with the formula, Frederick Macaulay. This weighted formula has been around since 1938 (if you are technically-minded and it is appropriate to the position you are interviewing for, you may go into detail about the actual formula). Modified duration only deals with the question of price relative to fluctuating interest rates and does not go into the weighted average of time until repayment.

What is convexity?
This is a more accurate measure of the relationship between yield and price changes in bonds in relation to the change in interest rates. Duration calculates this as a straight line, when in actuality it is a convex curve, hence the name. This is used as a risk calculation because it can tell how a bond yield will respond to interest rate changes.

Tell me about the different kinds of bonds.
Here are a few different bonds you should know about:

1. **Plain Vanilla**
The most simple kind of bond where everything is spelled out at the start – a fixed maturity/ expiry date, when the principal is due and how much and how often the interest is paid.

2. Convertible
This can be converted into the issuing company's stock at a fixed price. Good for the buyer as it is a bond with an option to buy stock if they decide they want to invest that way. Good for the issuing company as it offsets the potentially negative reason they might issue stock in the first place.

3. **Callable**
Sometimes also called a redeemable bond, this is when the bond has a call date, or dates, when the issuer has the right, not the obligation to buy back the bond at a pre-determined price. To compensate for the possibility of redeeming the bond before the maturity date, these bonds have higher coupons (amount of interest paid to the investor).

FX

Define risk adjusted rate of returns?
When looking at an investment you cannot simply look at the return that is projected. If the profit from investment A is greater than the profit from investment B you may immediately want to go with investment A. But investment A might have a greater chance of a total loss than investment B so even though the profit may be larger, it is a lot riskier and therefore not necessarily a better investment. Adjusted rate of return is when you not only look at the return that an investment may give you, but you also measure the risk of that investment. The adjusted rate of return is usually denoted as a number or rating. If you are technically minded you may also want to mention the ways that risk is measured: beta, alpha, the Sharpe ratio, r-squared and standard deviation.

Would a price of a call option go up or down when the maturity of the option is longer?
In an option, the price is pre-determined when the contract is written up. That is why an option is so attractive to both sides – the price is locked in so that if the price of the instrument in question goes down, the seller is protected and if it goes up, the buyer will get a good deal. So the actual price of the option doesn't change. Whether the market rate for the particular instrument goes up or down depends on the market and can go either way no matter how long the contract is for. Since a call option is to buy a futures contract (a put option is to sell one) you would have to be confident that the price would rise during the length of the contract to make the option profitable for you.

What is the Euro/Pound exchange rate today? Where do you think it will be in one year and why?
Obviously you need to keep up on the currency market at all times as it can change in a matter of minutes. Right before your interview check the prices of the major currencies (GBP, EUR, USD, JPY, CHF), the ones that interest you the most and of course, if the bank or firm tends to focus on one market or area, make sure you know what those currencies are doing. The part of the question that deals with what you think about that exchange rate in the future has to come from your views on the market. Be prepared to give your opinion and then be able to back it up with facts, historical evidence and corollary evidence. This is your opinion so really there is no wrong answer, but if you are unable to intelligently articulate why you hold the views that you do, you will not have a successful interview.

If the Yuan (CNY)/USD exchange rate is 100 CNY/1 USD today and the one year forward rate is 105 CNY/1 USD, what does this imply?
Since in a year it will take more yuan to equal one dollar that implies that the yuan is weaker than the dollar. The dollar is stronger because it can buy more yuan in a year from now than today.

COMMODITIES

What has fuelled the commodities boom of recent years and why? What are its implications for the asset management industry?
If you have had any work experience in commodities, be sure to relate your work to why you think there has been resurgence in commodities after a brief dip due to the credit crisis. You don't have to go into minute detail, but any real world experience you can point to will be a plus. Be sure to discuss the rise in emerging market populations and why this has had such a strong impact on the demand of food commodities. Discuss all of the electronics that everyone has today (iPads, iPods, mobile phones) and how that has impacted the prices for metals used to make those gadgets (mention specifically palladium, cadmium, nickel and platinum). Also read up on what oil is doing before your interview as this is sure to crop up in your discussion. Think about the impact that an increased number of people trading have and how as it's easier for individuals and novices to trade, how has this affected the commodities market. As for the asset management portion of the question, simply think about how you would advise a client about investing in commodities and what issues that client would face in doing so. Try to tie in specific commodities such as gold.

What is the current price of gold, corn, wheat, etc?
Right before your interview check Reuters, Bloomberg or another website or newspaper and jot down the price of major commodities from precious metals, other metals, food, energy and oil/fuel. Obviously if you know the role will focus on one of these categories, focus your research there.

Have you ever advised your client to invest in a commodity market and the client has faced losses after taking your suggestion? In such situation how would you try to cover up the losses of the client?
This will be a hard question to tackle if you have not had any previous experience in the industry. If you have had work experience, definitely mention that, even if you did not directly advise a client. If you have, be honest about the situation and what the result was. If you have never advised a client, say so, but then add that if you had advised a client, or if in the future you are advising a client and that client suffered a loss you would do x. Don't say that client losses haven't happened/ won't happen to you because you are that good! Everyone experiences losses at some point in their financial career. What the interviewer is looking for is how you deal with those difficult times. Of course clients will not be happy with a loss but how will you make it up to them? What new, creative investment have you been working on that will make them back their money plus more? Make sure you highlight how you have/would turn a negative situation into a positive one (and make sure you highlight your soft skills and your ease at dealing with clients too).

BUY-SIDE / INVESTMENT MANAGEMENT / HEDGE FUND QUESTIONS

Why do you want to work on the buy-side and not the sell-side?

Maybe you were attracted to the buy-side because of the wide range of companies you could work for (such as hedge funds, asset management firms and mutual funds) or the various different securities you could manage? Maybe you liked the structure or culture of most buy-side firms more than the sell-side? They may also ask you why you're not pursuing work in consulting. This is something you'll have to decide for yourself but you must come up with a few points to make sure they know you're not just going to jump ship to an investment bank in a year's time.

If I introduce a risky stock into a portfolio, is that good or bad?
This is not a yes or no answer. One stock does not a portfolio make; the health of a portfolio depends on all of its parts and how they work together, or are correlated. Generally stocks that are negatively correlated make for a less risky portfolio (so a petrol company and an airline would be negatively correlated since when the price of petrol goes up, it's good for the petrol company but bad for the airline as it makes their cost rise). On a related note, to be a good investment manager you'll have to take some risk. If you convey in the interview that you are not comfortable taking any risk and probably would not do so if hired, rather than convince them that you are careful, this will convince them that you won't make any money for the company. The amount of risk you're allowed and encouraged to take varies from place to place, but you may as well get used to the idea now that you're going to have to take some risk to be a successful investment manager.

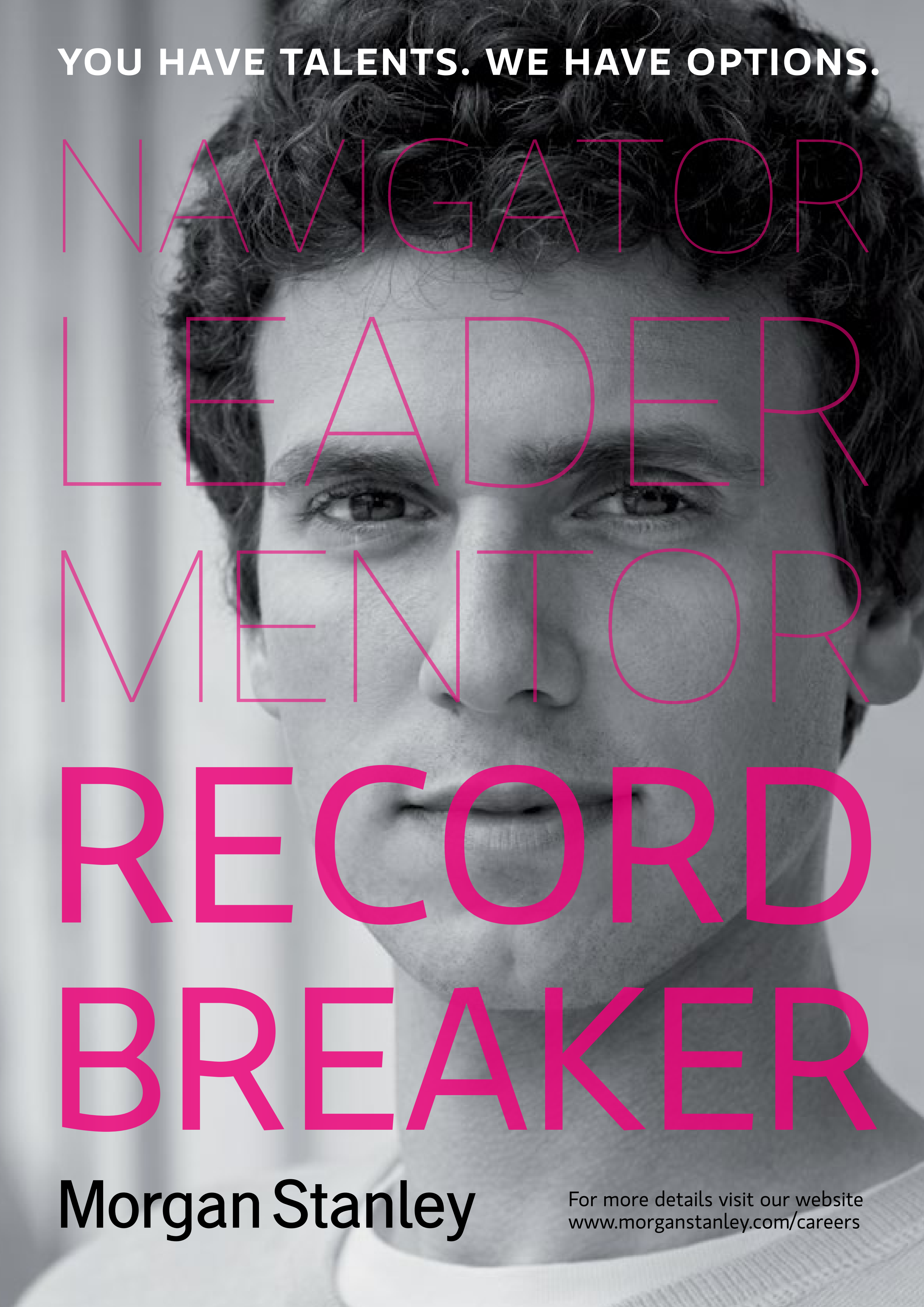
Since you have no previous experience in the markets, tell me why you want to work here and why are you interested in investment management?
This is the most important question for those who have decided on a career change or for those grads who are applying for their first job. They are not going to expect you to be familiar with detailed financial models or know advanced algorithms, but you will have to tell them why you are interested in the markets, describe what about following stocks and companies excites you and highlight which of your qualities makes you best suited to work on the buy-side. People in the industry say that when they first got into the business, their initial interviewers did not expect them to know the technical stuff, they only really looked for people with strong personalities, enthusiasm and drive – don't underestimate the power of those qualities.

MISC / GENERAL

What is an income statement?
This is just a simple record of a company's gains and losses, including expenses. The income sheet represents a specified amount of time and includes everything from the cost of renting the office to the depreciation of assets.

What is a cash flow statement?
A cash flow statement tracks the actual cash that goes in and out of a company. This is important to see how liquid the company is. If it is rich in assets but not necessarily cash, there could be problems.

Explain to me what makes up a cash flow statement
The place to start when looking at a cash flow statement is the beginning cash balance. Then you must look at cash from operations, then the cash made from any investments, then cash from financing. All of that will make up the ending cash.


YOU HAVE TALENTS. WE HAVE OPTIONS.
NAVIGATOR
LEADER
MENTOR
RECORD
BREAKER
Morgan Stanley
For more details visit our website
www.morganstanley.com/careers

FINANCE SOCIETY

IMPERIAL COLLEGE

PRODUCED BY THE IMPERIAL COLLEGE FINANCE SOCIETY

WWW.FINANCESOCIETY.CO.UK