

# Contents

Preface 9

Chapter 1

Macroeconomic Uncertainty in a Corporate Perspective

- 1.1 Introduction 11
- 1.2 The macroeconomic environment of the firm 15
- 1.3 What level of concern? 22
- 1.4 Macroeconomic Uncertainty Strategy (MUST) 24
- 1.5 The contents of this book 25

Chapter 2

Concepts of Macroeconomic Risk and Exposure

- 2.1 Introduction 28
- 2.2 Corporate risk – a brief review of the concept 29
- 2.3 Corporate risk: who cares? 33
- 2.4 Macroeconomic risk 39
- 2.5 What could be gained from a risk management programme? 43
- 2.6 Risk management and the creation of options 45
- 2.7 Concluding remarks on the conceptual issue of risk and exposure 49

Chapter 3

Traditional Approaches to Measuring Macroeconomic Exposure

- 3.1 Introduction 51
- 3.2 From transaction exposure to economic exposure 52
- 3.3 Translation exposure 62
- 3.4 From translation exposure to economic exposure 65
- 3.5 Does the translation method matter? 66
- 3.6 A comparison of exchange rate exposure measures 67

3.7	Interest rate exposure measures	72
3.8	Concluding remarks on traditional exposure measures	80
Appendix 3.1:	Measuring translation exposure under the monetary/non-monetary and the all-current methods	81
Appendix 3.2:	Purchasing Power Parity and real exchange rates	86
Appendix 3.3:	International Fisher Parity	94

#### Chapter 4

##### Measuring Macroeconomic Impact on the Firm

###### – a Comprehensive Approach

4.1	Introduction	99
4.2	Determinants of cash flow exposure	101
4.3	Estimating cash flow exposure	108
4.4	Decomposing cash flow exposure	118
4.5	Exposure coefficients and sizes of shocks	119
4.6	The share price and macroeconomic fluctuations	120
4.7	Concluding remarks on the comprehensive approach	121

#### Chapter 5

##### Measuring Macroeconomic Exposure

###### – The Case of Volvo Cars

5.1	Introduction	124
5.2	Exposure coefficients	125
5.3	The choice dependent variable	127
5.4	The choice of independent variables and time horizon	131
5.5	Volvo Cars	133
5.6	Results, interpretations, and the use of coefficients	140
5.7	Using the exposure coefficients for future periods	149
5.8	Concluding remarks on the case of Volvo Cars	152

#### Chapter 6

##### Hedging Macroeconomic Exposure

6.1	Introduction	156
6.2	Derivative contracts and transaction exposure – an overview	157

- 6.3 Practices in managing translation exposure 164
- 6.4 Hedging interest rate and inflation risks 170
- 6.5 Hedging macroeconomic exposure to market price variables 175
- 6.6 Hedging with uncertain exposure using derivatives 184
- 6.7 Taxes and hedge contracts 189
- 6.8 Concluding remarks on approaches to hedge macroeconomic uncertainty 191

## Chapter 7

### Strategies for Exposure Management

- 7.1 Introduction 194
- 7.2 Choice of target variable and time horizon 196
- 7.3 The firm's and management's risk attitude 199
- 7.4 Price adjustment in goods and financial markets 200
- 7.5 Choice of exposure management strategies 202
- 7.6 Information requirements 206
- 7.7 Adjustability of commercial operations – real options 209
- 7.8 Concluding remarks on the choice of strategy 211

## Chapter 8

### Recognizing Macroeconomic

### Fluctuations in Value-Based Management

- 8.1 Introduction 214
- 8.2 VBM and macro fluctuations 216
- 8.3 Cash flow decomposition and valuation: the case of Electrolux 218
- 8.4 Decomposition in performance assessment 222
- 8.5 Taking flexibility into account 224
- 8.6 Concluding remarks about MUST analysis in performance assessment 227

## Chapter 9

### What Shareholders Ought to Know

- 9.1 Introduction 231
- 9.2 Efforts to create standards 234

- 9.3 A comprehensive approach to assessing the impact of macroeconomic fluctuations on the firm 240
- 9.4 Current practice relative to IAS 1 (rev. 1997) on reporting of macroeconomic influences 242
- 9.5 Illustration of an information release that satisfies the demands of the outside shareholder 250
- 9.6 Concluding remarks on the reporting of the impact of macroeconomic fluctuations on corporate performance 253

#### Chapter 10

##### Macroeconomic Uncertainty Strategy (MUST) Analysis

– a Summary 257

10.1 Introduction 257

10.2 Shortcomings of traditional methods 259

10.3 Measures of corporate performance and exposure assessment 260

10.4 Elements of MUST analysis 262

References 269

Index 281