## The Political Risk Cont.

### Typical Political Risks
- Expropriation and confiscation
- Nationalization → sell to nationals
- Terrorism - severe random political risk
  kidnapping of CEOs in Mexico
- Macro-political risk event - affects all companies in a given country
- Micro-political risk event - affects a particular industry or business
- Discriminatory treatment
- Barriers to repatriation of funds
- Interference in managerial decision making
- Dishonesty by government officials

### Political Risk Assessment
- Helps companies manage exposure to risk and minimize financial loss
- **Two forms:**
  - Consultation with experts
  - Development of internal staff and in-house capabilities
Managing Political Risk

**Avoidance and Adaptation**
- Equity sharing - initiating a joint venture with nationals
- Participating management - hiring nationals and actively involving them in management
- Localization of the operation - modify the company name, the management style to suit local tasks
- Development assistance - actively participate financially in infrastructure development

**Dependency and Hedging**
- Input control - parent co. keeps control over means of production: raw materials, technology
- Market control - parent co. keeps control over means of distribution
- Position control - parent co. keep control over key management positions
- Staged contribution
- Political risk insurance (OPIC and FCIA)
- Local debt financing

*Keep the host government dependent on parent corporation - mitigating risk.
Managing Terrorism Risk

ex. kidnappings, hijackings, blackmail

1. Develop a charitable image
2. Maintain a low profile, minimize publicity
3. Use teams familiar to monitor terrorism
4. High counterterrorism specialists
   train employees
Economic Risk

- level of development (economic) $\rightarrow$ level of economic stability $\rightarrow$ level of economic risk

- connection exists between economic risk and political risk

- determined by a country's ability and intent to honor their financial obligations
Categories of Economic Risk

1. Loss of profitability due to abrupt changes in monetary and fiscal policy
2. Loss of profitability due to changes in foreign investment policies
3. Risk of exchange rate volatility
   - Ex. 1990 devaluation of peso
   - Extent of damage depends on balance sheet
Managing the Economic Risk

Ability & Intent to Repay or honor financial obligations

Credit

1. Quantitative Approach ⇒ statistically measures a country's ability to honor debt repayment
   assigning weights to different variables & creates index

2. Qualitative approach ⇒ assess competence & other characteristics of leaders & essentially make predictions about their future economic policies

3. Checklist Approach ⇒ uses predetermined, easily measurable criteria that reflects a country's credit
   ex. Vulnerability indication
The Legal Environment

1. local laws that govern the country in which the company operates
2. International law - governs relationship between countries
The Legal Environment

Types of Legal Systems

- **Common law**: U.S. and 26 other countries. Past court decisions act as a precedent to current interpretation of law.
- **Civil law**: Series of codes. Interpretation based on references to codes in Japan, Europe.
- **Islamic law**: Law based on religious beliefs. 27 countries.

Approaches to Contract Law

- **Common law**: Details must be written in the contract explicitly to be enforced.
- **Civil law**: Assumes promises will be enforced without explicit details.
- **In Asia**: Muslims in the relationship.
- **Islamic law**: Allah.
Other Regulatory Issues

1. Protectionist Policies → trade restrictions that favor national companies, products, etc.
   - tariffs
   - quotas

2. Local tax system → affect profitability
   - depreciation allowances
   - foreign tax credits

3. Level of government involvement in regulatory environment
   Quebec →
The Technological Environment

- Internet (e-commerce)
- Property rights (intellectual)
- Appropriability of technology
- Paris Union - International Convention for the Protection of Industrial (Intellectual) Property - Oversees protection of patents
- Foreign governments prefer labor-intensive processes, capital-intensive processes (only modern technology)
- Cultural obstacles to use of technology - ex: financial technology, research and development methods, marketing
Global E-Business

E-business: the integration of systems, processes, organization's, value chains and entire market using Internet technologies.

E-commerce - refers to the marketing and sales process via the Internet.

* B2B - business to business

* Supply chain distribution

* B2C - business to customer