

An Integrated Approach to Risk as a Determinant of Foreign Direct Investment:

ii. An empirical study

Background

One of the authors has conducted a survey of the attitude to risk and the risk control behaviour of large Australian companies as it relates in particular to decisions on direct foreign investment. The survey was directed mainly at the attitude to country risk but there were two open-ended questions which gave the respondents an opportunity to identify all elements of risk which were significant for the enterprise. On the basis of the survey it is possible to check the categories identified in the first part of this paper for their relevance to such companies.

There were 61 respondents in the survey, 13 in the primary sector, mainly miners and energy producers, 20 in the secondary sector, manufacturers of various kinds, and 28 in the tertiary sector, service providers.

The survey of Australian enterprises engaged in foreign direct investment included two questions of particular relevance to this paper - what specific features of the industry in which you operate create the most risk? and - what element of your industry has been identified as carrying the greatest level of risk?. These questions are open-ended and the entries by the respondents did not correspond exactly with the terminology used in the first half of this paper. The responses are referred to and made consistent with the terminology developed earlier in order to denote the different types and components of risk regarded as important by the respondents. The entries were interpreted so that they fall within particular component or sub-component groups.

Statistical tests were then conducted to see whether there were significant differences between the different groups of respondents, distinguished by sector, size and by investment orientation.

Because the questions in the survey invited the taking of an initiative by the respondent in making responses and identifying relevant elements any results in this area are likely to be strong. Later in the survey questions were asked using the specific terminology developed in part 1 of this paper; the relevant responses are the topic of a separate paper.

The Australian survey results

The following table summarises the responses to the first question.

Table 1: Types of Risk by Responding Firms

		Total N of Risk Categorized at Country, Industry and Enterprise Level N=178	Country Industry Enterprise Risks N=178	Risk Subcomp onents N=178	Identified Risks N=178	%
Political Risks:	Political instability risk			4	4	6.60%
	Government policy risk: Tax structures				6	9.80%
	Government policy risk: Nationalism				3	4.90%
	Government policy risk: Government regulation				9	14.80%
	Government policy risk: Host government interference (expropriation, confiscation)				8	13.10%
	Government policy risk: Ineffective legal system				6	9.80%
	Government policy risk: Regulatory risk: Industry standard			43	11	18%
	Social instability risk: Civil unrest undermines infrastructure				2	3.30%
	Social instability risk: Demonstrations				1	1.60%
	Social instability risk: Low-level terrorism		52	5	2	3.30%
Economic Risks:	Performance risk: Economic slowdown			5	5	8.20%
	Market context risk: Commodity price risk				12	19.70%
	Market context risk: Transfer risks: Foreign exchange risks/movements			28	16	26.20%
	Infrastructure risk: Lack of sufficient infrastructure support		39	6	6	9.80%
Financial Risks	Financial risks: Creditworthiness risk, sovereign risk		7	7	7	11.50%
Cultural Risks	Cultural risk: Transaction cost risks: government corruption, nepotism	99	1	1	1	1.60%
Product Nature Risks:	Product nature risk: Product liability risk: e.g. producing a highly flammable product				7	11.50%
	Product nature risk: Production process liability risks: Emission of pollutants		14	14	7	11.50%
Input Market Risks:	Input market risks: Quality product supply		13	13	13	21.30%
Product Market Risks:	Product market risk: Changes in consumer tastes/trends/demand				11	18%
	Product market risk: Availability of substitute goods		16	16	5	8.20%
Competitive Risks:	Competitive risks: Rivalry among existing competitors				4	6.60%
	Competitive risks: New entrants		9	9	5	8.20%
Technological Risks:	Technological risk: Product/process innovation, technology advancement	54	2	2	2	3.30%
Operating Risks:	Operating Risks - Labour risk: Labour unrest, union militancy				1	1.60%
	Operating Risks - Input supply risks: Raw material shortage				8	13.10%
	Operating risks - production risks: Machine failure		14	14	5	8.20%
Finance Risks:	Finance risks - Liquidity / maturity risk: Problem with collectibles		4	4	4	6.60%
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaving unethically				2	3.30%
	Behaviour risks: Deficiencies of skills and experience: Management/execution risks	25	7	7	5	8.20%
	Total	178	178	178		

The number of separate elements included in the respondent answers ranged from 1 to 16. There were a total of 178 separate elements, which is an average of almost three per respondent.

The first four components referred to relate to what we have called country risk, the next five to industry risk and the final three to enterprise risk. The absence of anything which could be described as global risk is striking. Although there is much talk about risk factors which reflect global risk this does not have an obvious impact on decision makers in Australian enterprises. The relative importance of the different elements is shown by the number of entries – country risk 99, industry risk 54 and enterprise risk 25. In the perception of the respondent managers country risk is the most important risk type. However industry risk is not insignificant.

Within country risk the political risk (52 entries) and economic risk components (39 entries) are far more important than financial (7 entries) or cultural risk components (just one entry) – political risk being significantly more important than economic risk. Within political risk by far the most important component is government policy uncertainty (43 entries). Within economic risk market context uncertainty is the main sub-component (28 entries), largely accounted for by foreign exchange rate uncertainty, what is often called transfer risk (16), and price uncertainty in general.

For industry risk the share of specific components was much more even – product market uncertainty (16), product nature uncertainty (14), input market uncertainty (13), and competitive uncertainty (9) accounting for most entries. Technological and regulatory uncertainties were not important at the industry level.

Clearly some items are regarded as more important than others. More than one in four of the respondents considered the transfer risk sub-component of market context risk (country risk) as important, more than one in five referred to the problem of quality of inputs (industry risk). Grouped together the single most striking component is government policy uncertainty with a total of 43 entries, in crude terms 70% of the respondents referred to it.

The following table summarises the responses to the next question asked for the identification of the single most important element. This reflected the funnel approach in which the analysis moves from the more general to the more specific. Respondents are invited to narrow their focus to the single most important risk factor.

Table 2: Types of Risks at Enterprise Level by Responding Firms

		Total N of Risk Categorized at Country Industry and Enterprise Level N=178	Country Industry Enterprise Risks N=178	Risk Subcomponents N=178	Identified Risks N=178	%
Political Risks:	Political risk: Government policy risk: Changes of Government regulation at the industry level				9	14.80%
	Political risk: Government policy risk: Host government interference				5	8.20%
	Political risk: Government policy risk: ineffective legal systems			17	3	4.90%
	Political risk: Social instability risk: Demonstration				2	3.30%
	Political risk: Social instability risk: low level terrorism		21	4	2	3.30%
Economic Risks:	Economic risk: Performance risk: Economic condition			4	4	6.60%
	Economic risk: Market context risk:				8	13.10%

	Foreign exchange risks, Currency stability					
	Economic risk: Market context risk: Commodity price risks: Financial instruments			18	10	16.40%
	Economic risk: Infrastructural risk		26	4	4	6.60%
Financial Risks:	Financial risk: Credit risk	50	3	3	3	4.90%
Product Nature Risks:	Product nature risks: Product liability risks - Product liability		4	4	4	6.60%
Input Market Risks:	Input market risks: Quality of product supply, ability to guarantee supply to customers			7	7	11.50%
	Input market risks: Shift in market supply		9	2	2	3.30%
Product Market Risks:	Product market risks: Changes in consumer tastes			8	8	13.10%
	Product market risks: Availability of substitute goods		12	4	4	6.60%
Competitive Risks:	Competitive risks: Rivalry among existing competitors			5	5	8.20%
	Competitive risks: New entry, barriers to entry, brand integrity		12	7	7	11.50%
Technological Risks:	Technological risk	38	1	1	1	1.60%
Operating Risks:	Operating risks - Input supply risks: Raw material shortage			11	11	18%
	Operating risks - Input supply risks: quality changes in input			2	2	3.30%
	Operating risks - Production risks: Machine failure			1	1	1.60%
	Operating risks - Production risks: Other random production factors		21	7	7	11.50%
Finance Risks:	Finance risk - Credit risk/exposure: Liquidity problem		4	4	4	6.60%
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaviour unethically			1	1	1.6
	Behaviour risk: Deficiency of skill or experience: capital cost overruns	29	4	3	3	4.90%
	Total	117	117	117		

There were less entries, 117 as against 178, an average of two per respondent which reflects in itself the inability of respondents to pick out one element as the most important. A response of this kind is an assertion of the importance of more than one factor since the question specifically asked for one element. The relative picture changes, but not dramatically – country risk (50), industry risk (38), and enterprise risk (29). Enterprise risk surprisingly rises in importance, if only by a small amount, whereas the other two fall. The funnel effect seems to be reflected in an increased focus on the enterprise and risk factors specific to the enterprise. The rise in the importance of enterprise risk reflects in particular the rising importance of operational uncertainty which rises to a level comparable with the political component of country risk (at 21 entries).

The fall in the number of entries for country risk (99 to 50) is greater than for industry risk (54 to 38). Within country risk economic uncertainty (26) rises above political uncertainty (21) in number of entries. Government policy uncertainty falls from 43 entries to 17. Clearly government policy uncertainty, while still significant, appears to be a general background risk underpinning other types of risk.

The overall picture present is one in which the main focus is on country risk but complemented by significant sensitivity to risk factors at both industry and enterprise

levels. Moreover economic risk is regarded as at the same level of importance of political risk but the latter provides an underpinning of risk which shapes the whole risk environment.

Patterns in the responses

The data was tested for any consistent patterns of difference between three types of group. The groups were distinguished by sector, size and investment orientation. The first defined the sector of the respondent enterprise as to whether it is primary - mainly mining and energy, secondary – manufacturing, and tertiary - services. The second relates to the size of commitment as represented by the level of gross revenue raised abroad. Again a division was made into three groups – large, intermediate and small. The third relates to country orientation. All investment host countries were divided into developed and developing and number of target investment destinations in the two groups counted for each enterprise.

The tests were carried out for the first question.

Table 3: Types of Industry Risks by Responding Firms Comparison by Sectors

		Primary N=13		Secondary N=20		Tertiary N=28		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political instability risk	2	15.4	1	4.3	1	4.0	0.424b
	Government policy risk: Tax structures	3	23.1	2	8.7	1	4.0	0.162b
	Government policy risk: Nationalism	2	15.4	1	4.3	0	0.0	0.107b
	Government policy risk: Government regulation	2	15.4	4	17.4	3	12.0	0.899b
	Government policy risk: Host government interference (expropriation, confiscation)	3	23.1	5	21.7	0	0.0	0.025b*
	Government policy risk: Ineffective legal system	2	15.4	2	8.7	2	8.0	0.739b
	Government policy risk: Regulatory risk: Industry standard	3	23.1	6	26.1	2	8.0	0.217b
	Social instability risk: Civil unrest undermines infrastructure	2	15.4	0	0.0	0	0.0	0.043b*
	Social instability risk: Demonstrations	1	7.7	0	0.0	0	0.0	0.213b
	Social instability risk: Low-level terrorism	2	15.4	0	0.0	0	0.0	0.043b*
Economic Risks:	Performance risk: Economic slowdown	0	0.0	2	8.7	3	12.0	0.719b
	Market context risk: Commodity price risk	4	30.8	3	13.0	5	20.0	0.463b
	Market context risk: Transfer risks: Foreign exchange risks/movements	2	15.4	7	30.4	7	28.0	0.594a
	Infrastructure risk: Lack of sufficient infrastructure support	1	7.7	4	17.4	1	4.0	0.297b
Financial Risks	Financial risks: Creditworthiness risk, sovereign risk	1	7.7	1	4.3	5	20.0	0.266b
Cultural Risks	Cultural risk: Transaction cost risks: government corruption, nepotism	1	7.7	0	0.0	0	0.0	0.213b
Product Nature Risks:	Product nature risk: Product liability risk: e.g. producing a highly flammable product	2	15.4	5	21.7	0	0.0	0.038b*
	Product nature risk: Production process liability risks: Emission of pollutants	2	15.4	5	21.7	0	0.0	0.038b*
Input Market Risks:	Input market risks: Quality product supply	1	7.7	6	26.1	6	24.0	0.442b
Product Market Risks:	Product market risk: Changes in consumer tastes/trends/demand	0	0.0	5	21.7	6	24.0	0.162b

	Product market risk: Availability of substitute goods	0	0.0	2	8.7	3	12.0	0.719b
Competitive Risks:	Competitive risks: Rivalry among existing competitors	0	0.0	2	8.7	2	8.0	0.671b
	Competitive risks: New entrants	0	0.0	3	13.0	2	8.0	0.434b
Technological Risks:	Technological risk: Product/process innovation, technology advancement	0	0.0	0	0.0	2	8.0	0.508b
Operating Risks:	Operating Risks - Labour risk: Labour unrest, union militancy	0	0.0	1	4.3	0	0.0	0.590b
	Operating Risks - Input supply risks: Raw material shortage	3	23.1	1	4.3	4	16.0	0.234b
	Operating risks - production risks: Machine failure	2	15.4	1	4.3	2	8.0	0.524b
Finance Risks:	Finance risks - Liquidity / maturity risk: Problem with collectibles	0	0.0	2	8.7	2	8.0	0.671b
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaving unethically	0	0.0	1	4.3	1	4.0	1.000b
	Behaviour risks: Deficiencies of skills and experience: Management/execution risks	1	7.7	2	8.7	2	8.0	1.000b

- a. Chi-square test is performed
a. Fisher's exact probability test is performed
† P<.10; *: p<.05; **: p<.01; ***: p<.001

There were some differences which were significant statistically. Enterprises in the primary sector were sensitive to the possibility of host government interference, of civil unrest, of low-level terrorism, and to some degree to product nature uncertainty. Those in the secondary sector were sensitive to the possibility of host government interference but even more than primary sector enterprises to product nature uncertainty. In all these areas service providers have no worries. For other components and sub-components there were no significant differences.

The same exercise was carried out for the responses to the second question.

Table 4: Types of Risks at Enterprise Level by Responding Firms: Comparison by Sectors

		Primary N=13		Secondary N=20		Tertiary N=28		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political risk: Government policy risk: Changes of Government regulation at the industry level	3	23.1	2	8.7	4	16.0	0.467b
	Political risk: Government policy risk: Host government interference	2	15.4	3	13.0	0	0.0	0.090b†
	Political risk: Government policy risk: ineffective legal systems	1	7.7	2	8.7	0	0.0	0.316b
	Political risk: Social instability risk: Demonstration	1	7.7	1	4.3	0	0.0	0.344b
	Political risk: Social instability risk: low level terrorism	1	7.7	1	4.3	0	0.0	0.344b
Economic Risks:	Economic risk: Performance risk: Economic condition	0	0.0	2	8.7	2	8.0	0.671b
	Economic risk: Market context risk: Foreign exchange risks, Currency stability	1	7.7	4	17.4	3	12.0	0.793b
	Economic risk: Market context risk: Commodity price risks: Financial instruments	5	38.5	2	8.7	3	12.0	0.072b†
	Economic risk: Infrastructural risk	0	0.0	2	8.7	2	8.0	0.671b

Financial Risks:	Financial risk: Credit risk	0	0.0	0	0.0	3	12.0	0.225b
Product Nature Risks:	Product nature risks: Product liability risks - Product liability	0	0.0	4	17.4	0	0.0	0.045b*
Input Market Risks:	Input market risks: Quality of product supply, ability to guarantee supply to customers	1	7.7	4	17.4	2	8.0	0.584b
	Input market risks: Shift in market supply	0	0.0	2	8.7	0	0.0	0.181b
Product Market Risks:	Product market risks: Changes in consumer tastes	0	0.0	4	17.4	4	16.0	0.336b
	Product market risks: Availability of substitute goods	0	0.0	3	13.0	1	4.0	0.338b
Competitive Risks:	Competitive risks: Rivalry among existing competitors	0	0.0	2	8.7	3	12.0	0.719b
	Competitive risks: New entry, barriers to entry, brand integrity	0	0.0	3	13.0	4	16.0	0.453b
Technological Risks:	Technological risk	0	0.0	0	0.0	1	4.0	1.000b
Operating Risks:	Operating risks - Input supply risks: Raw material shortage	5	38.5	3	13.0	3	12.0	0.121b
	Operating risks - Input supply risks: quality changes in input	1	7.7	0	0.0	1	4.0	0.686b
	Operating risks - Production risks: Machine failure	1	7.7	0	0.0	0	0.0	0.213b
	Operating risks - Production risks: Other random production factors	3	23.1	1	4.3	3	12.0	0.229b
Finance Risks:	Finance risk - Credit risk/exposure: Liquidity problem	0	0.0	0	0.0	4	16.0	0.069b†
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaviour unethically	0	0.0	1	4.3	0	0.0	0.590b
	Behaviour risk: Deficiency of skill or experience: capital cost overruns	1	7.7	1	4.3	1	4.0	1.000b

- a. Chi-square test is performed
b. Fisher's exact probability test is performed
† P<.10; *: p<.05; **: p<.01; ***: p<.001

There is some overlap with the results for the first question, which clearly reinforces those results. The possibility of government interference is still significant for enterprises in both the primary and secondary sectors. Product liability is still important for some secondary enterprises. The new features are the emergence of market context risk, or commodity price fluctuations as important for the primary sector, and of liquidity problems as important for service enterprises.

The next statistical test was for size, again carried out for the two questions in turn.

Table 5: Types of Risks at Industry Level by Responding Firms: Comparison by Size of Overseas Investment

Types of Industry Risks by Responding Firms		1-100 million N=17		100 million - 1 billion N=27		1 - 50 billion or more N=16		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political instability risk	1	5.9	1	3.7	2	12.5	0.684
	Government policy risk: Tax structures	0	0.0	2	7.4	4	25.0	0.046*
	Government policy risk: Nationalism	0	0.0	2	7.4	1	6.3	0.611
	Government policy risk: Government regulation	3	17.6	1	3.7	5	31.3	0.037*
	Government policy risk: Host government interference (expropriation, confiscation)	1	5.9	4	14.8	3	18.8	0.564
	Government policy risk: Ineffective legal system	0	0.0	2	7.4	4	25.0	0.046*

	Government policy risk: Regulatory risk: Industry standard	2	11.8	4	14.8	4	25.0	0.612
	Social instability risk: Civil unrest undermines infrastructure	0	0.0	1	3.7	1	6.3	0.741
	Social instability risk: Demonstrations	0	0.0	0	0.0	0	0.0	
	Social instability risk: Low-level terrorism	0	0.0	2	7.4	0	0.0	0.497
Economic Risks:	Performance risk: Economic slowdown	2	11.8	2	7.4	1	6.3	0.854
	Market context risk: Commodity price risk	4	23.5	3	11.1	5	31.3	0.273
	Market context risk: Transfer risks: Foreign exchange risks/movements	4	23.5	6	22.2	6	37.5	0.492
	Infrastructure risk: Lack of sufficient infrastructure support	2	11.8	4	14.8	0	0.0	0.401
Financial Risks	Financial risks: Creditworthiness risk, sovereign risk	2	11.8	1	3.7	4	25.0	0.093†
Cultural Risks	Cultural risk: Transaction cost risks: government corruption, nepotism	0	0.0	1	3.7	0	0.0	1.000
Product Nature Risks:	Product nature risk: Product liability risk: e.g. producing a highly flammable product	2	11.8	4	14.8	1	6.3	0.876
	Product nature risk: Production process liability risks: Emission of pollutants	1	5.9	4	14.8	2	12.5	0.778
Input Market Risks:	Input market risks: Quality product supply	3	17.6	4	14.8	6	37.5	0.263
Product Market Risks:	Product market risk: Changes in consumer tastes/trends/demand	3	17.6	6	22.2	2	12.5	0.910
	Product market risk: Availability of substitute goods	0	0.0	3	11.1	2	12.5	0.430
Competitive Risks:	Competitive risks: Rivalry among existing competitors	1	5.9	2	7.4	1	6.3	1.000
	Competitive risks: New entrants	2	11.8	2	7.4	1	6.3	0.854
Technological Risks:	Technological risk: Product/process innovation, technology advancement	2	11.8	0	0.0	0	0.0	0.145
Operating Risks:	Operating Risks - Labour risk: Labour unrest, union militancy	0	0.0	1	3.7	0	0.0	1.000
	Operating Risks - Input supply risks: Raw material shortage	1	5.9	2	7.4	5	31.3	0.061†
	Operating risks - production risks: Machine failure	0	0.0	3	11.1	2	12.5	0.430
Finance Risks:	Finance risks - Liquidity / maturity risk: Problem with collectibles	1	5.9	1	3.7	2	12.5	0.684
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaving unethically	1	5.9	1	3.7	0	0.0	1.000
	Behaviour risks: Deficiencies of skills and experience: Management/execution risks	2	11.8	2	7.4	1	6.3	0.854

There are some significant differences between the enterprises categorized by size. These are very much as might be expected. The bigger the enterprise the more likely it is to be concerned about a range of government policies, including tax changes and new regulations. It is also likely that such larger companies are concerned with ineffective legal systems and with the level of sovereign risk. Such concerns are not surprising, given the visibility of such companies.

Table 6: Types of Risks at Enterprise Level by Responding Firms: Comparison by Size of Overseas Investment

Types of Risks at Enterprise Level by Responding Firms		1-100 million N=17		100 million - 1 billion N=27		1 - 50 billion or more N=16		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political risk: Government policy risk: Changes of Government regulation at the industry level	3	17.6	2	7.4	3	18.8	0.435
	Political risk: Government policy risk: Host government interference	1	5.9	3	11.1	1	6.3	1.000
	Political risk: Government policy risk: ineffective legal systems	0	0.0	2	7.4	1	6.3	0.611

	Political risk: Social instability risk: Demonstration	0	0.0	1	3.7	0	0.0	1.000
	Political risk: Social instability risk: low level terrorism	1	5.9	1	3.7	0	0.0	1.000
Economic Risks:	Economic risk: Performance risk: Economic condition	1	5.9	2	7.4	1	6.3	1.000
	Economic risk: Market context risk: Foreign exchange risks, Currency stability	2	11.8	3	11.1	3	18.8	0.795
	Economic risk: Market context risk: Commodity price risks: Financial instruments	4	23.5	3	11.1	3	18.8	0.554
	Economic risk: Infrastructural risk	2	11.8	2	7.4	0	0.0	0.469
Financial Risks:	Financial risk: Credit risk	1	5.9	0	0.0	2	12.5	0.096†
Product Nature Risks:	Product nature risks: Product liability risks - Product liability	1	5.9	2	7.4	1	6.3	1.000
Input Market Risks:	Input market risks: Quality of product supply, ability to guarantee supply to customers	2	11.8	4	14.8	1	6.3	0.876
	Input market risks: Shift in market supply	0	0.0	2	7.4	0	0.0	0.497
Product Market Risks:	Product market risks: Changes in consumer tastes	4	23.5	3	11.1	1	6.3	0.383
	Product market risks: Availability of substitute goods	2	11.8	2	7.4	0	0.0	0.469
Competitive Risks:	Competitive risks: Rivalry among existing competitors	1	5.9	3	11.1	1	6.3	1.000
	Competitive risks: New entry, barriers to entry, brand integrity	2	11.8	4	14.8	1	6.3	0.876
Technological Risks:	Technological risk	1	5.9	0	0.0	0	0.0	0.550
Operating Risks:	Operating risks - Input supply risks: Raw material shortage	3	17.6	6	22.2	2	12.5	0.910
	Operating risks - Input supply risks: quality changes in input	0	0.0	2	7.4	0	0.0	0.497
	Operating risks - Production risks: Machine failure	0	0.0	1	3.7	0	0.0	1.000
	Operating risks - Production risks: Other random production factors	2	11.8	3	11.1	2	12.5	1.000
Finance Risks:	Finance risk - Credit risk/exposure: Liquidity problem	1	5.9	0	0.0	3	18.8	0.028*
Behavioural Risks:	Behaviour risks: Business ethics, Loss of reputation by behaviour unethically	0	0.0	1	3.7	0	0.0	1.000
	Behaviour risk: Deficiency of skill or experience: capital cost overruns	0	0.0	2	7.4	1	6.3	0.611

There are only two statistically significant differences, both relating to credit risk and credit exposure for the largest of enterprises.

The tests were then conducted for three groups distinguished by investment orientation.

Table 7: Types of Risks at Industry Level by Responding Firms: Comparison by FDI Investment Orientations

Types of Industry Risks by Responding Firms		Developed economy orientation N=34		Equal economic investment orientation N=9		Developing economy orientation N=18		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political instability risk	2	5.9	1	11.1	1	5.6	0.794
	Government policy risk: Tax structures	2	5.9	1	11.1	3	16.7	0.410
	Government policy risk: Nationalism	1	2.9	0	0.0	2	11.1	0.400
	Government policy risk: Government regulation	4	11.8	1	11.1	4	22.2	0.608
	Government policy risk: Host government interference (expropriation, confiscation)	3	8.8	1	11.1	4	22.2	0.326

	Government policy risk: Ineffective legal system	2	5.9	0	0.0	4	22.2	0.166
	Government policy risk: Regulatory risk: Industry standard	6	17.6	0	0.0	5	27.8	0.214
	Social instability risk: Civil unrest undermines infrastructure	2	5.9	0	0.0	0	0.0	0.666
	Social instability risk: Demonstrations	0	0.0	0	0.0	1	5.6	0.443
	Social instability risk: Low-level terrorism	1	2.9	1	11.1	0	0.0	0.359
Economic Risks:	Performance risk: Economic slowdown	5	14.7	0	0.0	0	0.0	0.205
	Market context risk: Commodity price risk	8	23.5	3	33.3	1	5.6	0.139
	Market context risk: Transfer risks: Foreign exchange risks/movements	11	32.4	2	22.2	3	16.7	0.521
	Infrastructure risk: Lack of sufficient infrastructure support	2	5.9	1	11.1	3	16.7	0.410
Financial Risks	Financial risks: Creditworthiness risk, sovereign risk	5	14.7	1	11.1	1	5.6	0.854
Cultural Risks	Cultural risk: Transaction cost risks: government corruption, nepotism	1	2.9	0	0.0	0	0.0	1.000
Product Nature Risks:	Product nature risk: Product liability risk: e.g. producing a highly flammable product	4	11.8	0	0.0	3	16.7	0.552
	Product nature risk: Production process liability risks: Emission of pollutants	4	11.8	0	0.0	3	16.7	0.552
Input Market Risks:	Input market risks: Quality product supply	9	26.5	0	0.0	4	22.2	0.258
Product Market Risks:	Product market risk: Changes in consumer tastes/trends/demand	7	20.6	1	11.1	3	16.7	1.000
	Product market risk: Availability of substitute goods	4	11.8	0	0.0	1	5.6	0.683
Competitive Risks:	Competitive risks: Rivalry among existing competitors	3	8.8	0	0.0	1	5.6	1.000
	Competitive risks: New entrants	5	14.7	0	0.0	0	0.0	0.205
Technological Risks:	Technological risk: Product/process innovation, technology advancement	1	2.9	1	11.1	0	0.0	0.359
Operating Risks:	Operating Risks - Labor risk: Labor unrest, union militancy	0	0.0	0	0.0	1	5.6	0.443
	Operating Risks - Input supply risks: Raw material shortage	5	14.7	0	0.0	3	16.7	0.667
	Operating risks - production risks: Machine failure	3	8.8	0	0.0	2	11.1	0.837
Finance Risks:	Finance risks - Liquidity / maturity risk: Problem with collectibles	3	8.8	0	0.0	1	5.6	1.000
Behavioral Risks:	Behavior risks: Business ethics, Loss of reputation by behaving unethically	0	0.0	1	11.1	1	5.6	0.192
	Behavior risks: Deficiencies of skills and experience: Management/execution risks	3	8.8	2	22.2	0	0.0	0.116

There are no statistically significant differences between the relevant groups.

Table 8: Types of Risks at Enterprise Level by Responding Firms: Comparison by FDI Investment Orientations

Types of Risks at Enterprise Level by Responding Firms		Developed economy orientation N=34		Equal economic investment orientation N=9		Developing economy orientation N=18		Exact Sig. (2-sided)
		N	%	N	%	N	%	
Political Risks:	Political risk: Government policy risk: Changes of Government regulation at the industry level	4	11.8	1	11.1	4	22.2	0.608
	Political risk: Government policy risk: Host government interference	0	0.0	2	22.2	3	16.7	0.014*
	Political risk: Government policy risk: ineffective legal systems	0	0.0	1	11.1	2	11.1	0.115
	Political risk: Social instability risk: Demonstration	0	0.0	1	11.1	1	5.6	0.192
	Political risk: Social instability risk: low level terrorism	0	0.0	1	11.1	1	5.6	0.192
Economic Risks:	Economic risk: Performance risk: Economic condition	4	11.8	0	0.0	0	0.0	0.262

	Economic risk: Market context risk: Foreign exchange risks, Currency stability	4	11.8	1	11.1	3	16.7	0.870
	Economic risk: Market context risk: Commodity price risks: Financial instruments	5	14.7	3	33.3	2	11.1	0.400
	Economic risk: Infrastructural risk	2	5.9	1	11.1	1	5.6	0.794
Financial Risks:	Financial risk: Credit risk	2	5.9	1	11.1	0	0.0	0.256
Product Nature Risks:	Product nature risks: Product liability risks - Product liability	3	8.8	0	0.0	1	5.6	1.000
Input Market Risks:	Input market risks: Quality of product supply, ability to guarantee supply to customers	6	17.6	0	0.0	1	5.6	0.321
	Input market risks: Shift in market supply	0	0.0	0	0.0	2	11.1	0.103
Product Market Risks:	Product market risks: Changes in consumer tastes	5	14.7	1	11.1	2	11.1	1.000
	Product market risks: Availability of substitute goods	3	8.8	0	0.0	1	5.6	1.000
Competitive Risks:	Competitive risks: Rivalry among existing competitors	4	11.8	0	0.0	1	5.6	0.683
	Competitive risks: New entry, barriers to entry, brand integrity	6	17.6	0	0.0	1	5.6	0.321
Technological Risks:	Technological risk	0	0.0	1	11.1	0	0.0	0.148
Operating Risks:	Operating risks - Input supply risks: Raw material shortage	6	17.6	1	11.1	4	22.2	0.811
	Operating risks - Input supply risks: quality changes in input	2	5.9	0	0.0	0	0.0	0.666
	Operating risks - Production risks: Machine failure	0	0.0	0	0.0	1	5.6	0.443
	Operating risks - Production risks: Other random production factors	3	8.8	1	11.1	3	16.7	0.750
Finance Risks:	Finance risk - Credit risk/exposure: Liquidity problem	3	8.8	1	11.1	0	0.0	0.455
Behavioral Risks:	Behavior risks: Business ethics, Loss of reputation by behavior unethically	0	0.0	0	0.0	1	5.6	0.443
	Behavior risk: Deficiency of skill or experience: capital cost overruns	1	2.9	1	11.1	1	5.6	0.553

The only significant difference relates to the danger of government interference for enterprises. Those with a developing country orientation are more likely to be sensitive to this risk component.

Conclusions

The survey results complete the triangular sources of information on risk. It is now clear what Australian managers, as well as theorists and rating agencies, think about risk. The results tend to confirm the role of country risk in the general structure of risk as set out in the first half of the paper.

The responses to the relevant questions revealed the general view of the relative importance of different types of risk. Clearly country risk is considered more important than industry risk but the latter is sufficiently important to confirm that enterprises are faced with risk specific to particular industries. The responses confirmed the importance of country risk as against industry or enterprise risk, but showed that the picture was a complex one of interacting risk factors, in which country risk is omnipresent even where other types of risk predominate.

For the most part the survey confirmed the usefulness of the terminology developed for the different types of risk and the significance of the filtering of both country and industry risk down to the enterprise level. The responses revealed a subtle understanding by respondent managers of this interactive process and placed both

country and industry risk in a broad context of all types of risk. Respondents selected more components and sub-components than would be the case in a simple world of uni-dimensional risk, on average almost three per respondent for the first question and almost two for the second question, despite the question expressly inviting a response indicating an element in the singular.

However the responses show that the traditional picture of a combination of government policy uncertainty and transfer uncertainty as characterising country risk is shared by the respondent managers. Government policy uncertainty does stand out as the most important single sub-component of risk in responses to the first question. It is clearly a sub-component which is part of the general mind-set of most respondents.

Differences between the groupings based on sector, size and investment orientation were not generally significant nor surprising where they existed. Larger enterprises, those which are obviously more prominent, have a greater concern about various elements of political risk. There were few differences in the sensitivity to different components of risk on the part of enterprises with a differing investment orientation. The only difference was for the danger of host country intervention, referred to in entries to the second question. There was a clear difference of sensitivity, greater for those with a developing country orientation. Such differences clearly reflect differences in the nature of the assets which are relevant to the sector and exposed to risk.

It is probably true that a focus on country and industry risk considered in the context of enterprise risk is a reasonable approach. The importance of global risk is exaggerated. Within country risk it is also acceptable to ignore cultural risk and to fuse economic and financial risk into one, with the latter as a sub-component of the former. The investment risk matrix is therefore for country risk a reasonable description of the situation facing decision makers, implying a roughly equal importance of political and economic risk.

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