

COUNTRY RISK IN FOREIGN DIRECT INVESTMENT: SIMILARITIES AND DIFFERENCES WITH COUNTRY RISK IN EXPORTS

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<http://dx.doi.org/10.5209/NOMA.53538>

Abstract.- Country Risk in exports is derived from the capacity of payment and the losses that insolvency can cause to the creditors. Instead, the country risk in foreign direct investment is related to breach of contract, deprivation of property rights, damage to assets or cessation of activities. The operations of foreign direct investment (FDI) are different in nature to exports. Therefore, regarding country risks some questions arise: is country risk different also?, which are the common risks and which are specific risks to exports and FDI? Both share five types of country risk: the transfer risk, the impossibility of converting currencies, the exchange rate risk, the risk of war or political violence and sovereign risk. The risk of expropriation is specific to foreign direct investment and does not affect trade. This paper makes a comparative analysis of the risks in exports and foreign direct investment. The aim is to find out to what extent they differ. The conclusions are valid for multinational firms and developing countries with a growth strategy based on FDI .

Keywords.- *Foreign direct investment, political risks, export, country risk, multinational*

JEL CODE: F23

1. Introduction

A multinational firm is exposed to two different kind of risks in its foreign direct investment (FDI)ⁱ operations: those risks related to the management of their own business in a different country and those related to the political and macroeconomic environment of the host country. The former are the commercial risks and depend on how efficient the direction and management of the Project are. The latest are part of country risk categories. The economic, political and social contexts can eventually cause losses to foreign investors. Having said that, how can those losses be originated? Which elements can become country risk events? Is country risk similar for exporters and for foreign direct investors?

The goal of this work is to identify the dynamic elements of a country that can generate losses to foreign firms operating inside the borders. We consider the events of risk for exporters as a starting point and make a comparative analysis

based on econometric literature, not based on data. The result is a map of the risk events that can face multinational in front of the risk events that can affect to exporters. The findings are valid for both, multinational and exporter firms, as well as for countries whose development strategy is based on foreign investment.

Country risk assessment in international trade is based on the assessment of payment capacity. Instead, losses in FDI are related to damage on assets, violation of property rights and cessation of activities. Exports and FDI operations are different in nature and so are their potential losses. According to these differences, is country risk similar for both in a single country? To answer this question, the first task is to gain a deep knowledge of the concept and categories of country risk. Furthermore, the events related to every category will be identified. Once the events are defined, it will possible to compare the risk of non payment and the foreign direct investment risks. Finally, we conclude about the differences for both operations in a single country.

2. The concept of country risk

In economics, risks are related to losses and risk assessing is related to loss measuring. In country risk, the elements than can provoke a loss are of three kinds: economic, political and social. Behind the risks, the whole complexity of the social sciences have to be studied. Therefore, country risk is a wide and complex concept. Some good definitions are David James (2004): “Political risks are human, subjective, severe and unpredictable”, and Vilariño (2001): “Country risk is a difficult and slippery concept, that resists to be classified in formal models”. According to Moosa (2002), country risk is “the exposure to an economic loss in transnational operations caused by events in a certain country which are, in a way at least, under the control of the government”.

Such events can have a macroeconomic origin as high inflation, a deterioration in the current account of balance of payments or an increase in external debt. Events can also be political, such as government interference or breach of contracts. But even the economic events are the direct result of policies. Both, political and economic events have their origin in politics, and that is why we use either political risk or country risk to refer to these causes of loss. By politic we mean the persons in charge of the business of the state and also the activity of those who have an influence in public issues through their acts and through their opinions. Therefore, political risk has its origin in government’s decisions which are influenced by the groups who aspire to replace them and by citizens who can alter the activity of both.

3. Country risk in FDI.

In exports country risk increases o diminishes the credit riskⁱⁱ related to the paymen deferment. An exporter, a bondholder or a financing bank are all exposed to credit risk or to non payment risk. Instead, a direct investor can register losses as a consequence of the breach of contract by the local authorities, violation of property rights, damage to assets and cessation of activities. It is not necessary to complete cessation of activities. In some cases,

power cuts, cuts in the supply of local inputs or tariff regulations can provoke a notorious decrease in the local activities of the firm, damaging the profit and loss account. Meldrum (2000) and Herber (2002) consider the decrease of profits among the consequences of country risk whereas Simon (1992) refers exclusively to the impossibility of repatriate funds, dividends or profits. The World Bank, through the Multilateral Investment Guarantee Agency (MIGA) define political risk as “risks associated to government acts that i) reduce the rights of an investor or a proprietor to use or profit from its assets and ii) reduce the value of the firm” (MIGA, 2011).

Since we are considering different forms of losses and different elements than can produce them (economics, political and social), then we can presume that the events can be diverse also. Even though the concept of country risk generates a huge debate, its events generate quite a wide consensus. A comparative analysis has been done among seven sources. One is the Berne Union, the associations of sixteen insurer companies that manage the export credit with official support for their respective countries (Export Credit Agencies). The second source is MIGA (MIGA 2011). The third is Iranzo (2008) published by Banco de España, the Central Bank of Spain, and the rest are academics and multinational executive authors: Simon (1992), Meldrum (2000) and Herber (2002). All the sources in the table agree about the origins of risks:

- Transfer restrictions
- Currency convertibility restrictions
- Confiscation, expropriation and nationalisation of foreign assets
- War or political violence
- Sovereign decisions

The last event in the previous list, named as sovereign risk by Meldrum (2000), include several circumstances that, in our opinion, deserve a different analysis. On one hand, there are the legislative changes that a government can create as part of their economic, industrial or development policies. That would be the case of a change in the price of public services, which would affect national as well as foreign supply companies. On the other hand, there is the breach of contract signed with the foreign investors. Restriction of access to local inputs, cuts in the supply of power or water or the breach of previously signed licenses for natural resources extraction are some examples of events of this kind. Furthermore, in these kind of events it can be registered as a generalised breach of commitments in a whole productive sector or a specific breach of contract that affects one only operation. Finally, Heber (1992) posits the willingness to pay as an event that can affect the foreign direct investors and Meldrum (2000) relates it to sovereign risk. This isn't very accurate for in FDI operations, the host state is not in a debtor position with the foreign firm. Therefore, in this study the sovereign risk understood as non payment by the state is not considered as an event of risk.

The only source that considers the exchange risk is Meldrum (2000). Broad and unexpected variations in exchange rates can provoke huge losses. A recent example is the devaluation by 46% in Bolivia ordered by the government of former President Hugo Chávez in Venezuela in 2013 and the losses caused to commercial firms operating in the country, like the Spanish Inditex. For this reason, exchange rate is included among the categories of country risk.

As a result, there are six categories of country risk in FDI compared to those in foreign trade (table 1).

Table 1: Categories of country risk in FDI

Categories of country risk in FDI	¿Does affect also to exports?
Transfer Risk	Yes
Convertibility Risk	Yes
Exchange Rate Risk	Yes, in foreign exchange
Confiscation, Expropriation and Nationalization Risk	No
War or political violence	Yes
Breach of contract and regulation risk	Payment commitments

An analysis of the elements involved in every kind of risk is to follow.

3.1. Transfer and convertibility risks

Convertibility is the exchange of local currency to an accepted foreign currency inside the country with the aim to transfer it overseas. Transfer is the possibility to transfer the currency overseas. The foreign firm can be interested in transferring currency, normally repatriate, disinvested funds, dividends or payments for loans to foreign banks. Risks derive from the lack of foreign exchange availability in the local banking system or from a prohibition to transfer foreign exchange, once it has been obtained inside the country. The origin of these risks is generally economic and basically balance of payments. The current account deficit is often registered together with a high indebtedness in foreign currency and that combination produces an increase in these two forms of risk. Such a circumstance is out of the control of the private sector and involves the whole country beyond the nature or the interests of economic agents operating in the country. This is the reason why convertibility and transfer risks are categories of country risk. The restrictions to convertibility is the result of a lack of foreign currency in the country, that means an inability *de facto*. It is an economic risk related to balance of payment and debt dynamics, considering that economic risk are political risk in last resortⁱⁱⁱ. Transfer risk is, instead, the direct result of a political decision, a prohibition. Furthermore, the ultimate cause for that prohibition could have nothing to do with economic reasons. Transfer risk is a *pure* political risk.

3.2. Exchange rate risk.

Large fluctuations in exchange rates can be the cause of huge losses or profits for foreign investors. Exchange rate risk in the short term can be easily covered using the mechanisms available in the financial system. Nevertheless, in the long term, exchange rate insurance is not efficient. Therefore, exchange rate risk is another category of country risk since it can reduce the value of profits, dividends or repatriated funds. Fluctuations can be originated by political decisions to modify the exchange system, replacing a parity with a crawling peg system, for example. They can also be originated by the dynamics of the forex market. In the former case, the political character of the risk is of no doubt whereas in the latest case, the risk could be the result of speculative attacks against the local currency. Be that as it may, there are mechanisms available to local authorities to manage those attacks and counteract their effects. Therefore, whatever the origin, the exchange risk has to be considered as a country risk.

3.3. Confiscation, expropriation and nationalisation risk (CEN risk)

The Spanish Constitution recognises the private property right and sets down that "nobody can be deprived of his own goods and rights but for a justifiable reason of public utility or social interest, according to the law and with due compensation. The Spanish Language Royal Academy's dictionary (RAE, 2001) defines to expropriate as "to deprive the administration to an individual the property or a good or of a right, in exchange of a compensation and due to public and social interest that are provided by law. Colex (2006) posits that expropriation is "a private property or right deprivation method used imperatively by the government due to public utility or social interest and in exchange for a compensation". In the jurisprudence of the Supreme Court and the Constitutional Court "the right of property is configured as a statutory right modifiable by law", emphasising the possibility of transferring private property to the State in the circumstances described above. However, the law provides for the possibility of transferring the property to the State but also stipulates the procedure: Act of December 16, 1954^{IV} establishes that "to proceed with the expropriation, previous declaration of public utility or social interest is needed" (Article 9). Article 10 of the same Act relates the goods with public utility is implicitly understood and Articles 11 and 12 determine the requirement that, for all other goods not included in that list, the public utility has to be declared expressly and uniquely a priori by Law. Chapters III and IV, respectively, stipulate the need to "determine the fair price" and the requirement to perform the "payment and swearing."

The confiscation and nationalisation also constitute acts of transfer of ownership to the State. While expropriation is justified by the common interest, confiscation is defined in RAE (2001) as "penalty with deprivation of property" and therefore has connotations of punishment imposed by the State either by the Treasury, in the case that the owner has debts to public finances, or because of unlawful possession, in the case of drugs or seizures, for example. Confiscation of property to a foreign investor could answer these two circumstances, but for the purpose of country risk we consider the non-punitive aspect. Thus, we consider

any confiscation expropriation acts which are not justified by the public interest or accompanied by financial compensation.

The definition of nationalisation in Colex (2006) resembles that of expropriation while the public interest or the common interest of the object is not justified: "Legal legislative expropriation of property ownership, rights or undertakings belonging to individuals or companies, transferring the property to the State". The concept of nationalisation is well understood if explained as the inverse process of privatisation. It is the transfer of domestic or foreign private property to the state, whatever the reasons for such decision. Again, nationalisation of a foreign company by sovereign decision can be done without any compensation or with a less than fair compensation. In these cases we should consider it as a confiscatory action, not expropriation as Colex (2006) notes. However, this definition, although incomplete, is useful for the purpose of country risk to describe the differences between nationalisation, confiscation and expropriation.

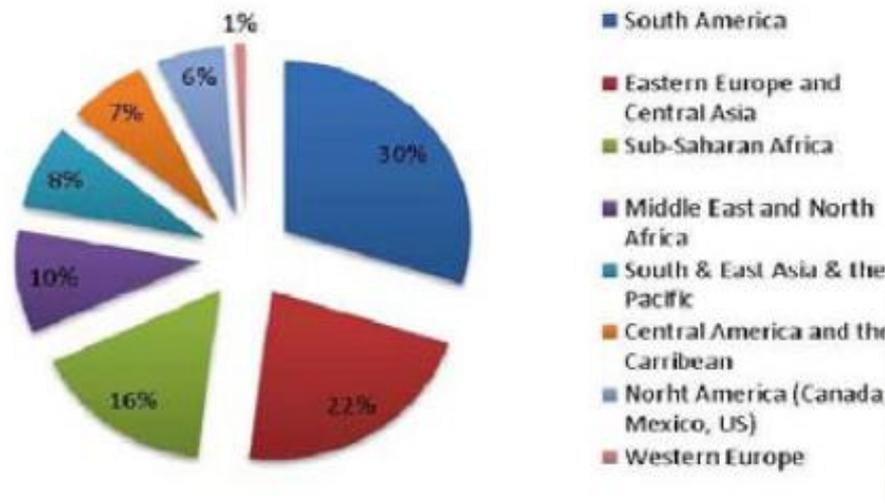
All of the above refers to the Spanish legislation. Each country has its own legal framework with regard to these issues, and there is no supranational legislation that conditions in any way the scope of each sovereign regarding these kind of decisions. Notwithstanding the legislative specifications of each particular country or differences arising out of them between the states, with regard to foreign direct investment we can generalise as noted below. Nationalisation means the transfer of ownership of the shares of the firm, local or foreign, to the State. For an action to be considered an expropriation it must be done with legal basis, with payment of fair price and according the public utility or social interest of the expropriated object. If legal basis and just compensation are lacking, the action will be confiscatory.

Although different, the three events have enough in common to be grouped into a single category of country risk for FDI. Therefore, they can be analysed together. All three causes a reduction in property rights to the owner of the goods. The three are associated to an economic loss which will be higher or lower depending on the value of compensation. All three are government decisions, regardless of their proximity or distance to what the law states, and, as such, they constitute a sovereign risk against which no appeal is possible. All three, when performed on foreign companies, are aimed to comply with national interests and with aspects of political expediency, not only social, that can be placed above law. Furthermore, the government that has the ability to undertake an action of this type has also the ability to change the law to suit their interests. The result will be similar in terms of control of the company, while in terms of profitability depends on the value of the payment, as we have said. It is in the perception of a lower than fair compensation where the risk is. Consequently, we will discuss the three actions within the same category of risk, the risk of confiscation, expropriation or nationalisation or risk CEN. The CEN risk does not affect trade, it is specific to direct investments.

The International Centre for Settlement of Investment Disputes^V (ICSID) records disputes between foreign investors and host states for reasons of CEN events. According to UNCTAD (2011), in late 2010 the number of registered ICSID countries was 83 of which 51 were developing countries and 15 transition

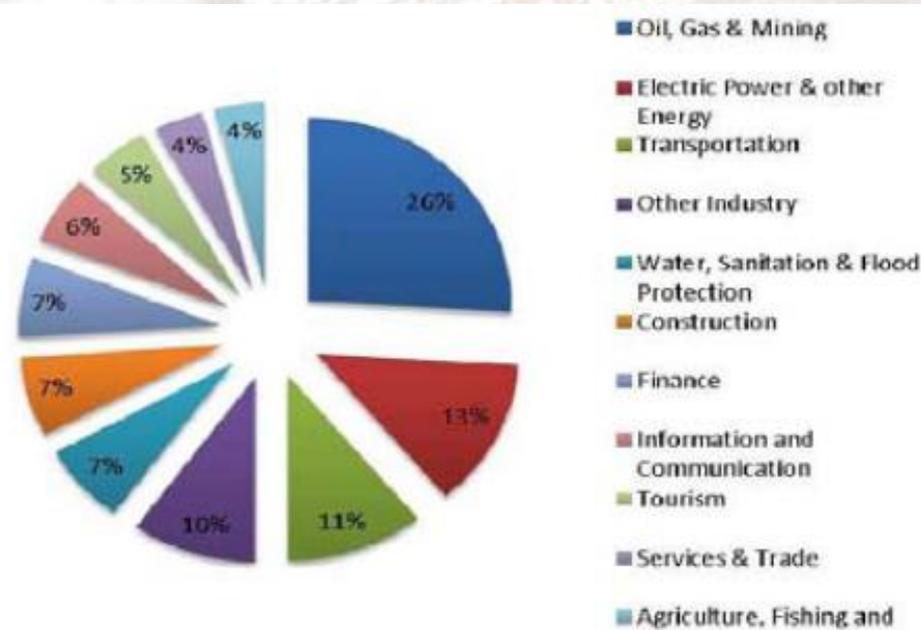
economies. Figures 1 and 2 show that these disputes cover a wide range of business sectors and all geographical areas of the world, respectively.

Figure 1. Geographical distribution of records involved in ICSID by country (2010)



Source: UNCTAD (2011)

Figure 2. Sectoral distribution of recorded disputes in ICSID (2010)



Source: UNCTAD (2011)

There is not a database registering expropriation laws or events CEN^{vi} but this does not prevent us from knowing about several cases that have been recorded

in CIADI or published by the media. In 2004, Namibia started a land reform expropriating the properties of 18 white race farmers (France Press cited in Li 2009). In April 2006, the former venezuelan President Hugo Chávez expropriated two oilfields from the french Total and the italian ENI due to the inability to close a deal for PDVSA to obtain the majority of shares (Economist Intelligence Unit, 2006, cited in Li 2009). In April 2012, argentinian President Cristina Fernández presented a bill for the expropriation of 51% of Yacimientos Petrolíferos Fiscales from the spanish oil company Repsol. The reason alleged were lack of investments, versus the favourable opinion expressed by the government in the previous months about the management of business by Repsol in Argentina. In February 2013, former President Chávez ordered the temporal closing of shops owned by the spanish Inditex as the response to the increase in prices that the firm had applied to counteract the devaluation by 46% of the Bolivia. This official decision did not threaten property rights but it did provoke losses due to the temporal cessation of activities.

3.4. War and political violence risk

Even though we all have in mind what a war is, when considering war as a cause of loss an accurate definition is needed. A practical way of obtaining it is to start from a wide concept of situations similar to war, including all possible circumstances of violence, and to define afterwards which of them should be considered as events of country risk for FDI. The aim is to analyse the scope and the motivations for violence. Depending on the percentage of population involved and on the kinds of motivations, different forms of violence will arise.

War is an armed conflict between two or more nations or between sides of one nation that use violence to gain the right to rule, to become a state or to own other's land. Nowadays war is not explicitly declared and peace relationships can, surprisingly, coexist with violent acts between two confronted countries. India and Pakistán, Iraq and Iran or Israel and Gaza are some examples. In these cases, embassies are open but hostilities are serious enough to consider them into this category of risk.

An insurrection is an uprising against the state that refers to an individual attitude that has legal consequences according to the law. It is important to take into account that an insurrection is an individual act, involving one or few persons. Insurrection is an incipient rebellion^{vii}. It becomes a rebellion when it is an open resistance to the authority or an organised armed conflict against the government. In the cases where that political aim is reached, and the government is replaced, then the movement is called revolution. The differences among these three concepts are based on the scope of the population involved and on the kind of goals that are pursued. When a high percentage of populations are pursuing political aims, then the movements is an event of country risk. The personal protest of a young tunisian in December 2010 due to the economic difficulties became a revolution, with President Ben Alí escaping out of the country. One year after, President Marzouky was elected in democratic polls.

This latest example is related to other forms of social destabilisation, those led by students, workers or trade unions. These grievances are not strictly political,

so they cannot be strictly considered as country risk events. Having said that, in some cases popular grievances have changed the political program or even have overthrown the governments, like in Argentina in several occasions or in Tunisia and Egypt, more recently. It is difficult to establish a frontier between public demonstrations of repudiation of government policies and mass movements with a potential to destabilise the political context and, there, with a potential to losses for FDI. It is in this frontier where country risk arises. In exports, risk is related with insolvency. In FDI operations risk is, instead, related with social movements against foreign interests, fed by nationalist feelings and by a conflict of interests.

Regarding terrorism, the combination of the criminal and the political component has to be considered. Terrorist activity is a criminal act punished by law in almost every country. Motivations are often religious, ideological or nationalist. In the last resort, they become political due to the obligation of the ruling politicians to manage the issues that raise terrorism acts^{viii}. Terrorism can cause losses to foreign investors and, therefore, is an event of country risk. Some multinational firms have been obliged to manage terrorism, like FENOSA in Colombia. Be that as it may, it is important to specify that the terrorism as a country risk event is not necessary related to the scope of the act or the dimension of damages. Furthermore, the political component of terrorism must not make us forget about the criminal component, which is also inherent.

The most frequent form of political violence in the last decades has been civil war. One of the most complete investigations about the origins of civil war is Collier Hoeffler (2002, 2004), which has become a reference in the analysis of armed conflicts. These authors consider the definition of civil war developed in *Correlates of War*, a database of events understood as armed conflicts between the army and one or more group of insurgents which cause 1000 or more deaths, at least 5% in each contender.

3.5. Breach of contract risk or sovereign risk in FDI

The breach of contracts by the government is a sovereign decision. Sovereignty is the quality of sovereign by which it exercises the supreme authority in political power. There is not a higher authority than a sovereign. When talking about risk, this aspect is important for one of the consequences is that there is not any legal action against sovereign decisions. As a result, regarding the definition and the assessment of sovereign risk, the political regime and the holder of sovereignty is crucial. Sovereign exercise develops in very different manner depending on whether sovereign is an absolute monarch or sovereignty is held by the people and is transferred to an elected government, like in democracies. The sovereign instrument is the law, and law ruling can have considerable economic consequences for a country and for firms operating in it. It is a country risk event of unpredictable effects that have to be managed by exporters and by direct investors but, how are both exposed?

As we have mentioned, by sovereign risk Moosa (2002) and Simon (1992) understand the non payment of debts by the state due to insolvency or to unwillingness to pay. However, from the investor's point of view, the breach of contracts by the state and the regulatory changes entails the sovereign capacity

to decide in one way or another. Therefore, in a comparative analysis, breach of contracts and regulatory changes will be contrasted with the unwillingness to pay by the government.

Therefore, to establish the similarities and the differences between the country risk in exports and in foreign direct investments and to assess in what degree the analysis of the former is valid for the later the following risk assessments are needed: transfer risk, convertibility risk, exchange rate risk, war and political violence risk and sovereign risk. For these common risks it will be necessary to find out whether a different assessment is resulting from a different prism and from operations of a different nature. If so, then the differences will have to be identified. We have to find out how a transfer restriction affects payment for imports and to repatriation of funds. We also have to find out whether the lack of dollars affects in a similar way to importers than to investors and whether a specific social or political destabilisation can cause losses to both.

Instead, the CEN risk does not exist in trade and must not be included in a comparative analysis. The non payment capacity must not be included also, since it is a risk in trade but it does not exist in direct investment. That is the reason why it is not listed above. We do consider indeed the sovereign risk in FDI operations related with breach of contracts and regulatory changes. Sovereign risk has to be analysed in comparative terms taking into account these qualifications.

4. Is country risk identical or different in FDI and foreign trade operations?

Once the risk categories in FDI and in exports have been identified, the similarities and the differences in the assessment from both perspectives are to be explained.

4.1. Transfer risk

Transfer risk in payment for imports is different than transfer risk in repatriation due to several reasons. Firstly, in commercial operations the impossibility of transferring the payment of a debt is related to a situation of insolvency or liquidity of the state. Secondly, imports can increase the external debt, feeding the problem of insolvency. Dividend or disinvested funds repatriation have nothing to do with debt. Furthermore, foreign direct investment does not increase the level of external debt. We are considering the same action, transfer of funds, but the state can have several reasons to forbid transfers only for foreign investors or, conversely, to declare a moratorium of payments without harming repatriation funds, either decision depending on economic policy. The development strategy and subsequent motivations for favouring or reducing FDI are also determinants of the differences between the risk assessment in both cases for it determines the attitude of the authorities with foreign firms. The official attitude with multinationals depends on the country of origin, on the location in the host country and on the sector of operation. To the extent that the sector is relevant for the domestic economy and to the extent that bilateral relationships are strained, the risk assessment will change among investors in the same country. Third, the fact that official bilateral debt can be rescheduled

in Paris Club is an added argument for a government to grant a different treatment to debt payment and to repatriation of dividends. Lastly, in countries with an administrative structure with autonomous local governments, these kind of decisions have an inherent sub-sovereign. The assessment of sub-sovereign in contrast with sovereign risk will depend partly on whether the political sign of both governments are the same or the contrary, for obvious reasons. Sub-sovereign risk in Argentina or in Brazil is as relevant as the sovereign risk, both in trade and direct investments.

4.2. Convertibility and exchange rate risks

Convertibility risk assessment is related with the availability of foreign exchange in the country's financial system. The higher the availability, the lower the convertibility risk. The lack of foreign exchange in a system have identical effects for creditors than for foreign investors. Risk assessment is identical from both perspectives. Regarding the exchange rate risk, it occurs exactly the same. Exchange rate fluctuations have identical impact from every economic agent operating in the country. It is necessarily so except in dual exchange rate systems, which have different rates depending on the operation, but these cases are very rare nowadays and would be an exception.

4.3. War and political violence risk.

Regarding the war and political violence risk, taking into account that direct investment entails a physical presence and a production activity, risk assessment can be different from the investor point of view. A correct assessment requires to consider the location into the country and the sector of activity. None of these elements are involved in capacity of payment. In fact, uprising risk in a specific area is higher in some countries, like in Mexico (Chiapas), the Russian Federation (Chechenia) or India (Cachemire). Regarding the sector of activity, it can be more or less sensitive for the government, to the extent that it contributes to GDP, to foreign exchange reserves or to public income. The sector of activity can be also sensitive for the population if it is perceived as a public service or as a public resource. Both, location and sector of activity can alter risk assessment in FDI and exports, and even among FDI operations.

Besides, as posit by Simon (1992), in risk assessment it is important to take into account the *visibility* factor. External trade is less visible than foreign direct investment activities in a specific country. Physical presence in natural resources extraction or production and distribution of goods and services makes these activities more visible to citizens and, therefore, more vulnerable to political violence.

4.4. CEN and sovereign risks

CEN risk is not susceptible to a comparative analysis since it is inherent only to FDI operations. As stated before, sovereign risk in investments, that means breach of contracts and regulatory changes, are to be contrasted with

unwillingness to pay in the side of trade. Nevertheless, they are both very different due to the nature of operations. Furthermore, sovereign risk is a wider concept than breach of contract and regulatory changes. It has a dynamic component that arises in what is called *inconsistency risk*. Let's see an example: in the last decades of XX century large privatization processes have been registered in many emerging countries providing opportunities to foreign investors. When time has elapsed, governments can have incentives to reverse or revoke that process. In countries like Czech Republic and Ukraine privatization process were not transparent and in circumstances that could motivate a change in the process causing losses to investors. In Zimbabwe, the authorities developed a generalised expropriation and redistribution process involving farms and land properties that had been private owned by nationals and foreigners for decades. A reverse in the attitude of the government regarding foreign investments can be motivated by the need of building a complex engineering project and hires a foreign specialised company to do so. Initially, the government commits itself to favour the project with special tariffs, tax exemption, etc. Once the most specialised part of the project is finished, if the running of the plant does not require a specific qualification and can be developed by locals then the government can have an incentive to breach contracts or even expropriate. The recent case of expropriation of YPF to the Spanish Repsol in Argentina is an example of time inconsistency, since the authors were in favor of selling the company at the time. Inconsistency risk is associated to CEN risk and to sovereign risk. However, it is unquestionable the negative effect that an inconsistent government has in the investment climate and in the development strategy of its country. Therefore, there is a counterpart to inconsistency risk that is related to the *reputation* of countries, making a government to desist of hostile attitudes.

Table 2 shows the elements that cause a different or similar perception of risks. The last column indicates whether the risk is different or not. CEN risk is not listed for being exclusive of FDI. Among the common risks, the only risks that affect similarly to exporters and investors are convertibility and exchange rate. The payment capacity of the state is not listed since it does not exist in FDI. The rest of risks are different depending on the operation.

Table 2: Comparative analysis of country risk in exports and FDI

Risk	Exports	FDI	Different?
Transfer	Prohibition that depends on the external debt position	Prohibition that does not depend on the external debt position	Yes
	Insolvency or illiquidity situations		
	Susceptible to rescheduling in Paris Club	Investment climate and development strategy damage	
Convertibility	Lack of foreign exchange due	Lack of foreign	

	to balance of payment and debt crisis	exchange due to balance of payment and debt crisis	No
Exchange Rate	Large fluctuations in the exchange rate	Large fluctuations in the exchange rate	No
CEN	Not applicable	Applicable	Not applicable
War and political violence	Uprisings with political aims that provoke insolvency situations	Uprisings against foreign interests	
	Inefficient management of natural resources by the state. Corruption	FDI operates in a sensitive sector or in natural resources extraction.	Yes
	Unmet social needs. Failed states	FDI interests are counter to domestic interests	
	Invisible operations	Physical presence, visibility	
Sovereign	Willingness to pay	Breach of contract and regulatory changes	
	Reschedulings in Paris Club	Official attitude with FDI: case by case	
	Bilateral relationship	Bilateral relationship	Yes
		Inconsistency vs reputation	

5. Conclusion

Country risk assessment in exports is a good starting point for country risk assessment in FDI but it is not enough for two reasons. Firstly there are categories of risks which are specific of FDI and do not affect to exports. This is the case of CEN risk. Secondly, the risks that are common to both operations can affect in a different way and in different degree to one and another. War or political violence is considered as a category of country risk in export if they have political aims and if they involve a high percentage of the population so they have a potential to cause a deterioration in the economic fundamentals and insolvency. Such result would not necessarily affect to foreign investors

operating in the country. FDI can instead suffer losses due to uprisings motivated by a conflict of interests with foreign firms. The exposure and the perception of this risk are unequal and, furthermore, they are different even among direct investors operating in different sectors or territories into the country.

Transfer risk is also unequal. Capital transfer limitations are related to the debt position in the case of trade operations. In the case of FDI, external transfer prohibitions are only motivated by a sovereign decision. Both are completely independent so they can be decided separately.

Regarding the sovereign risk, on one side we are referring to voluntary unpayments, not insolvency, which is the sovereign decision affecting exporters. On the other side, we are referring to breach of contracts and to regulatory changes, which are the sovereign decisions that can cause losses to FDI operating in the country. There are three elements that make this risk unequal: i) the development strategy and the subsequent interest in maintaining a good investment climate, ii) the debt rescheduling in Paris Club as a last resort, which can be an incentive to unmeet payment commitments and iii) the need of gaining and maintaining a reputation in international context.

The only categories of country risk that are equal for exporters and foreign direct investors are convertibility risk and exchange rate risk. There aren't any reasons to consider that lack of foreign exchange or large fluctuations on exchange rate would affect unevenly to both operations. Lastly, focusing only in FDI, there can be discrepancies in risk assessment among several operations due to the location and the sector of activity. Therefore, risk assessment in FDI operations requires a case by case basis.

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ⁱ The definition of Mossa (2002) of foreign direct investment is the process by which residents of a country acquire ownership of some assets in another country in order to control the production and / or distribution and other activities conducted by them. The IMF, in its Balance of Payments Manual defines FDI as "an investment made in order to acquire a lasting interest in a firm operating in another country, being the interest of the investor to have a voice in the firm's management". In UNCTAD's World Investment Report, FDI is defined as an investment involving a long-term relationship and represents a lasting interest in a firm established in an economy other than that of the investor. In this paper, we will consider the process of creation or acquisition of assets, excluding portfolio investment, in order to develop a long-term management control of the activity.

ⁱⁱ Vilariño (2001) defines credit risk as the possibility of suffering a loss caused by the breach of contractual payment obligations. Causes are specified as: decline in the creditworthiness of borrowers related to liquidity problems, continuing losses and even bankruptcy for companies, or declining revenues in families, but can also be caused by lack of willingness to pay.

ⁱⁱⁱ In the public sector imports health of public finances is another crucial indicator.

^{iv} Published in BOE. 351 of December 17, 1954

^v ICSID is the principal institution for the settlement of investment disputes. It was established under the Convention on the Settlement of Investment Disputes between States and Nationals

of Other States (the ICSID Convention), which is an international multilateral treaty Differences. The ICSID Convention entered into force on October 14, 1966. A January 20, 2013, ICSID had 158 States had signed the Convention and 147 Contracting States that had ratified it. The primary purpose of ICSID is to provide facilities for conciliation and arbitration which might be submitted to the international investment disputes. Arbitration and conciliation under the Convention are entirely voluntary and for their use of the investor and the consent of the State concerned are required. Once given, such consent can not be withdrawn unilaterally and becomes a binding commitment.

^{vi} ICSID is a record of disputes between investors and host countries, not CEN events themselves. Registered in ICSID disputes may lead or not to CEN events and on the other hand, not all events are recorded in the ICSID.

^{vii} In english, the meaning of insurrection and rebellion are the contrary to the meaning of insurrection and rebellion in spanish. In spanish, rebelión is an incipient insurrección.

^{viii} Note that we refer to political terrorism, not terrorists acts of common violence.

