



SK


SKEMA BUSINESS SCHOOL

COUNTRY RISK RATING II

Michel-Henry Bouchet

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COUNTRY RISK SPECIFIC INDICES



ICRG
Euromoney
Institutional Investor
OECD
COFACE

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ICRG



- ▶ The *ICRG* model for forecasting financial, economic, and political risk was created in 1980 by the editors of International Reports (weekly newsletter)
- ▶ To meet the needs of clients the editors created a statistical model to calculate risks and backed it up with analyses that explain the numbers and examine what the numbers do not show.
- ▶ the *ICRG* model allows users to make their own risk assessments based on the *ICRG* model or to modify the model to meet their specific requirements.

Source: www.icrg.com

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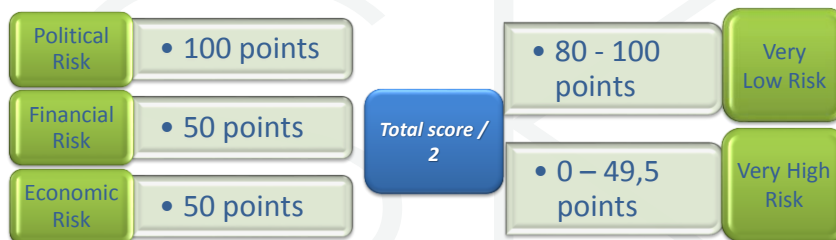
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INTERNATIONAL COUNTRY RISK GUIDE (ICRG)

- ▶ Monitors 140 countries
- ▶ The *International Country Risk Guide (ICRG)* rating comprises 22 variables in three subcategories of risk: political, financial, and economic.



- ▶ Testing has proven *ICRG's* reliability and its uniqueness:
 - Claim to have the longest history of country risk data for analysis
 - Easy to customize and merge with in-house systems
 - Useful for multinational firms, banks, and equity and currency traders

Source: www.icrg.com

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ICRG: POLITICAL RISK COMPONENTS

Weights	ICRG's Political Risk Assessment Criteria
12	Government Stability
12	Socio-Economic conditions
12	Investment Profile
12	Internal Conflict
12	External Conflict
6	Corruption
6	Military in Politics
6	Religious Tensions
6	Law and Order
6	Ethnic Tensions
6	Democratic Accountability
4	Bureaucratic Quality
100	Total number of points for weighted influence

Source: www.icrg.com

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ICRG: ECONOMIC RISK COMPONENTS

(50 MAX)

GDP Per capita	10 points
Real GDP Growth	10 points
Annual inflation rate	10 points
Budget Balance	10 points
Current account/GDP	10 points

Source: www.icrg.com

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ICRG: FINANCIAL RISK COMPONENTS (50 MAX)

Foreign debt	10 points
Debt service/XGS	10 points
Current account	15 points
Net liquidity	5 points
Exchange rate stability	10 points

Source: www.icrg.com

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EUROMONEY

EUROMONEY : RATING METHODOLOGY

- ▶ 186 countries
- ▶ 15 criteria
- ▶ Delphi Technique: Panel of 250 leading economists in international financial institutions evaluating performance in the financial markets (market access, bond issue, spreads, selldown, terms and maturity...)
- ▶ Scoring between **100** (excellent) and **0** (high risk)
- ▶ Panel of political analysts to measure short-term risk of destabilization

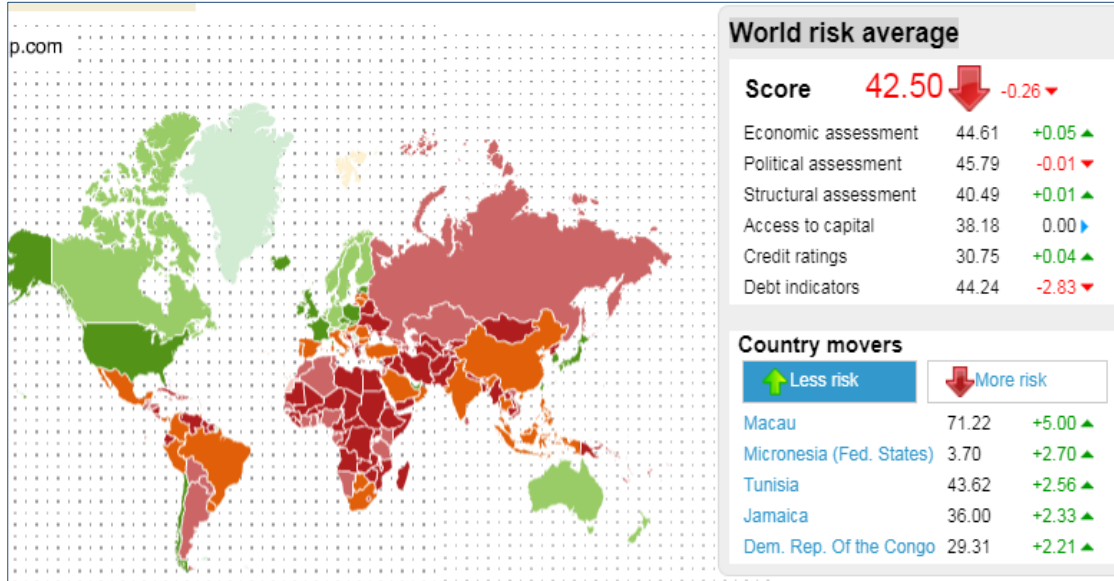
EUROMONEY: RATING WEIGHTS

1. Growth performance: 25% (GDP projection)
2. Political risk: 25%
3. External debt indicators: 10% (debt/GDP and debt/X)
4. External payment default and rescheduling: 10%
5. Credit rating Moody's or S&P: 10%
6. Short-term credit market access: 5%
7. Commercial bank MT credit: 5%
8. Capital markets access: 5%
9. Spread over US Treasury bills: 5%

EUROMONEY COUNTRY RISK RATINGS 2001-2016

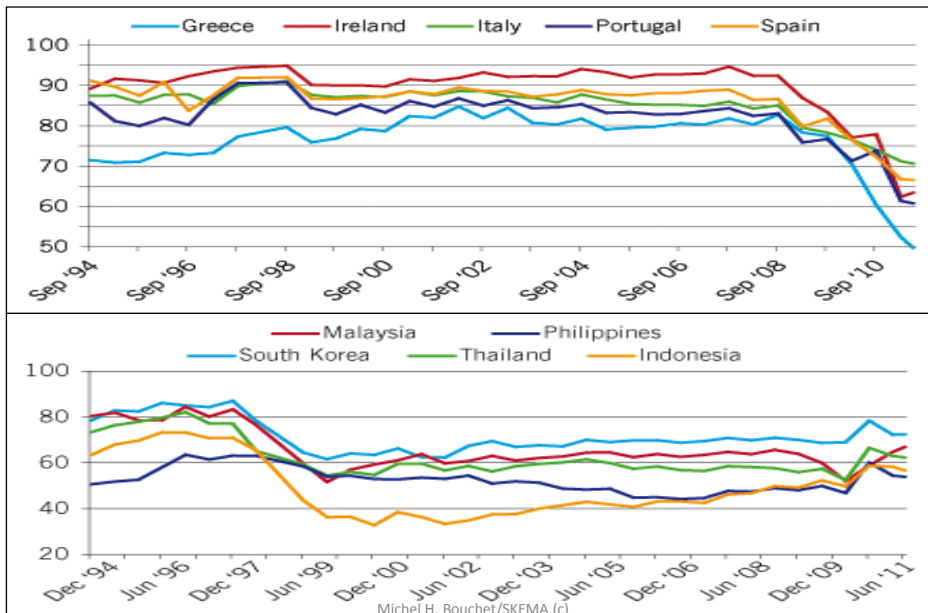
End-2001	End-2005	End-2006	End-2012	End-2016
14= Singapore	9= Ireland	20=Singapore	11=Singapore	1= Singapore
28= Taiwan	19= Singapore	41=Hungary	15= USA	
30= HongKong	22= New Zealand	44= Poland	19= Chile	
40= Chile	24= Taiwan	52= China	41=Hungary	
39= Hungary	35= Hungary	62= Russia	44= Poland	
40= Brunei	58= China	77= Algeria	46= China	
41. Greece	73= Iran	79= Iran	49= Russia	18= Taiwan
42= Poland	74= Vietnam	82= Vietnam	76= Indonesia	
45= China	77= Russia	85= Indonesia	79= Vietnam	
56= Malaysia	85= Algeria	167= Ivory Coast	100= Greece	
89= Romania	96= Indonesia	178= Congo	127= Algeria	
93= Bulgaria	127= Ivory Coast	182= Cuba	141= Ivory Coast	
163= Congo	182= Cuba	185= North Korea	178= Congo	

EUROMONEY COUNTRY RISK MAP



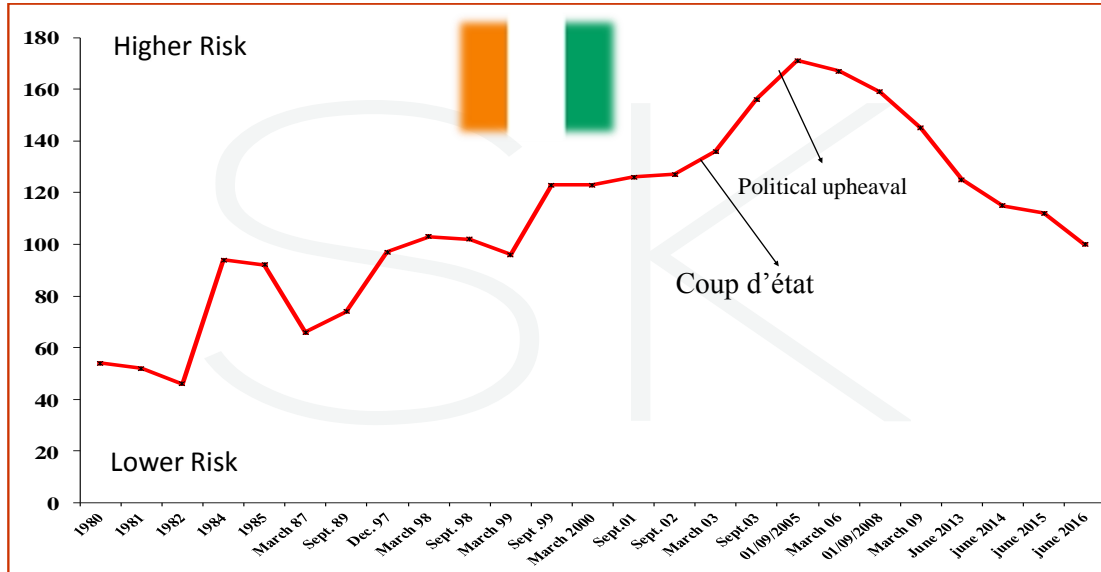
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EUROMONEY COUNTRY RISK SCORE 1994-2011



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EUROMONEY RISK RATING: IVORY COAST 1980-2016



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SCORING/RATING OF COUNTRY RISK

- ▶ 0-100 semi-annual Rating of 179 countries' creditworthiness based on survey of 100 leading **international bankers**
- ▶ **Best** : Switzerland, Finland, Norway, Germany, Netherlands, France, US, UK, Luxembourg... Singapore, Australia, Taiwan, Chile
- ▶ **Worst**: Cuba, Myanmar, Cambodia, Nicaragua, Rwanda, Sudan, Iraq, Congo, Sierra Leone, North Korea, Liberia

Global average risk rating as of 03/2000 = 41

Global average risk rating 03/2015 = 45

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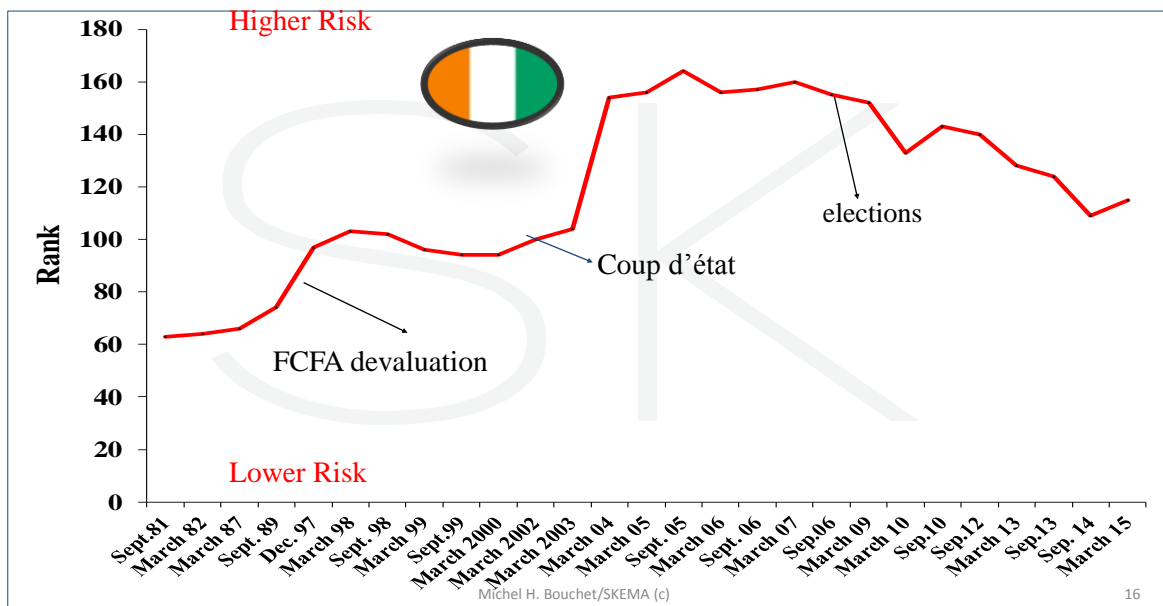
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INSTITUTIONAL INVESTOR RISK RATING

- Information provided by leading international banks.
- Bankers are asked to grade each of the countries on a scale from 0 to 100 (100 = best creditworthiness)
- Sample updated every six months, ranges from 75 to 100 banks, each of which provides its own ratings. The names of all participants in the survey are kept strictly confidential. Banks are not permitted to rate their home country.
- Individual responses are weighted using an *Institutional Investor* formula that gives more importance to responses from banks with greater worldwide exposure and more sophisticated country analysis systems.

INSTITUTIONAL INVESTOR RISK RANKING 1981-2015

IVORY COAST



INSTITUTIONAL INVESTOR RISK RATING OF ASIA

➤ **Switzerland = 1**

➤ **Norway = 2**

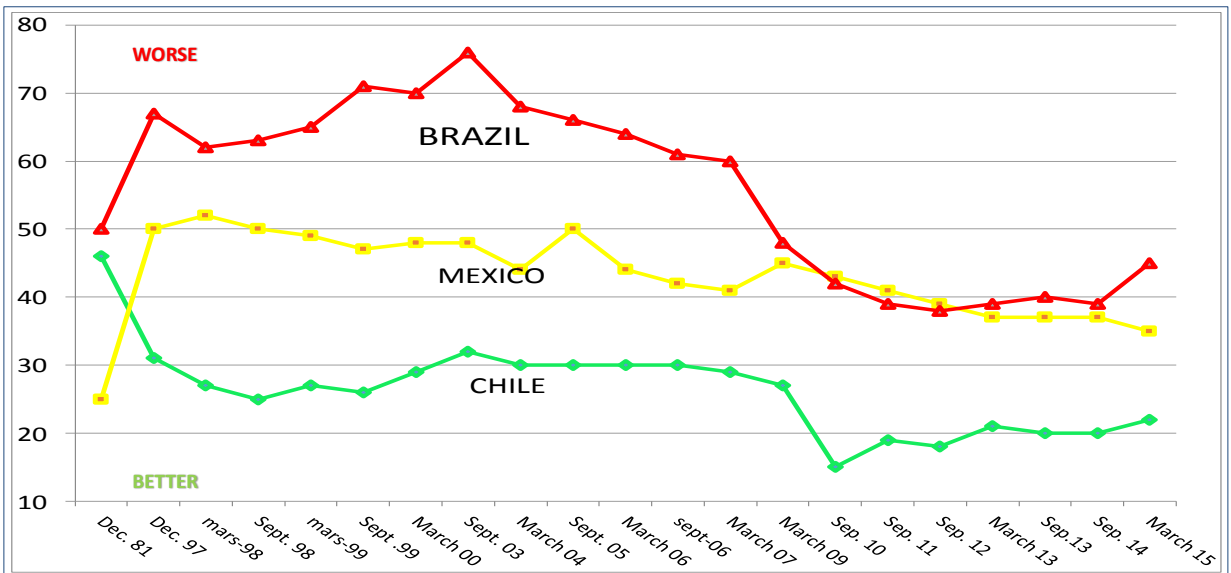
- Singapore = 6
- Australia = 11
- HK= 17
- Japan = 19
- South Korea = 20
- Taiwan = 21
- **China = 26**
- Malaysia= 37
- Thailand= 47
- India= 48

- Philippines=49
- Indonesia= 57
- Vietnam= 73
- Sri Lanka= 103
- Bangladesh= 111
- Cambodia= 119
- Pakistan= 128
- Laos= 136
- Myanmar= 150
- East Timor= 153
- North Korea= 173

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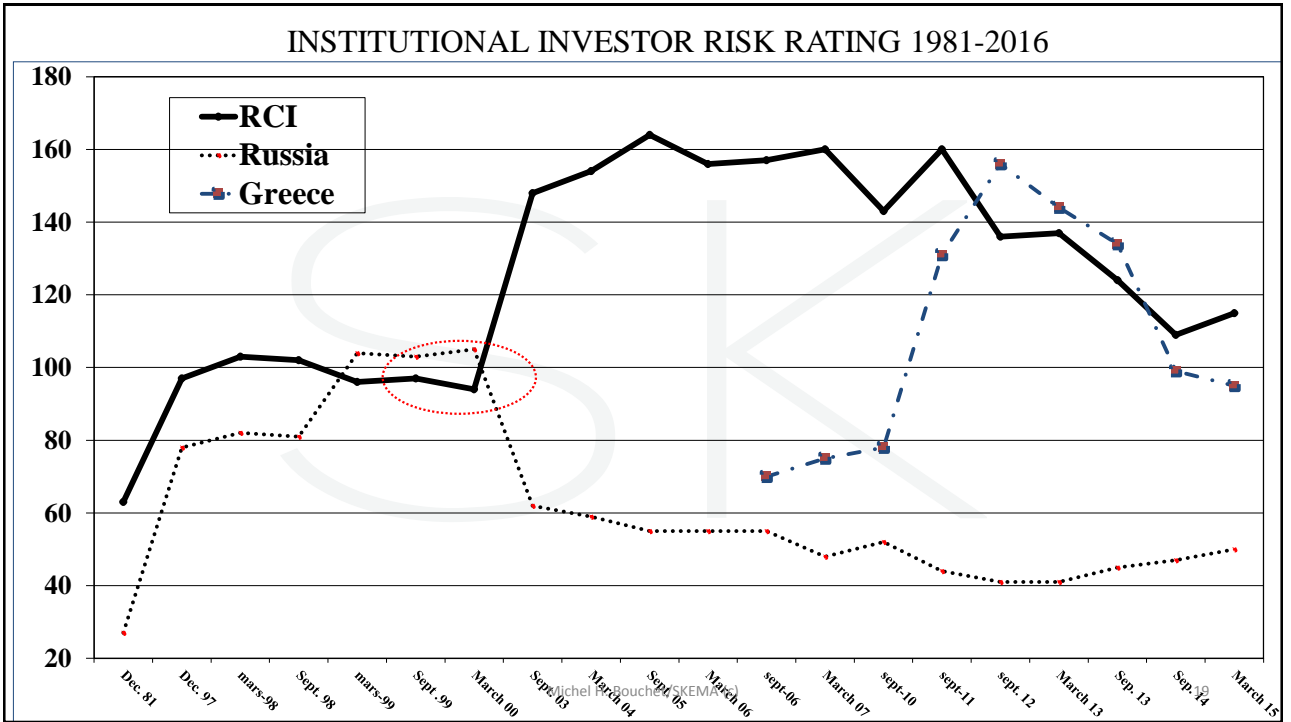
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INSTITUTIONAL INVESTOR RISK RATING 1981-2017



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COUNTRY RISK: GOVERNANCE MATTERS!

- ▶ Corruption
- ▶ Regulatory framework
- ▶ Business conditions
- ▶ Transparency
- ▶ Corporate and sovereign governance

WORLD BANK: « DOING BUSINESS » 2017 RANKING	
Singapore	1
New Zealand	2
Denmark	3
Korea, Rep.	4
Hong Kong SAR,	5
United Kingdom	6
United States	7
Sweden	8
Norway	9
Finland	10
Taiwan, China	11
Macedonia, FYR	12
Australia	13
Canada	14
Germany	15
Estonia	16
Ireland	17
Malaysia	18
Iceland	19
Lithuania	20

*189 Countries
10 Parameters*

Russia=	51
South Af=	73
China=	84
Brazil=	116
India=	130

Nigeria	169
Yemen, Rep.	170
Djibouti	171
Cameroon	172
Timor-Leste	173
Bangladesh	174
Syria	175
Congo, Rep.	176
Afghanistan	177
Guinea-Bissau	178
Liberia	179
Equatorial Guinea	180
Angola	181
Haiti	182
Chad	183
Congo, Dem. Rep.	184
Central Af Rep	185
Venezuela	186
South Sudan	187
Libya	188
Eritrea	189

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DOING BUSINESS IN CHINA?

TOPICS	DB 2015-Rank
Starting a Business ✓	128
Dealing with Construction Permits	179
Getting Electricity	124
Registering Property	37
Getting Credit	71
Protecting Minority Investors	132
Paying Taxes ✓	120
Trading Across Borders	98
Enforcing Contracts	35
Resolving Insolvency	53

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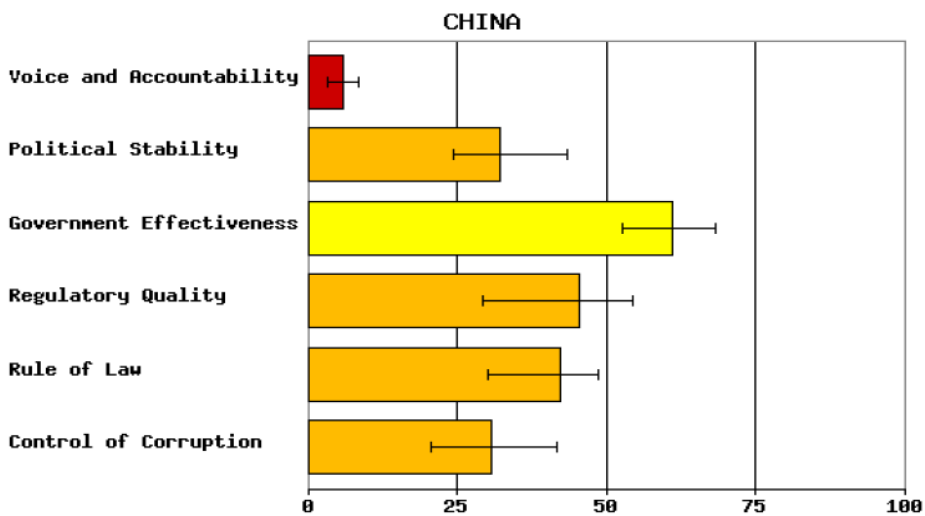
BLOOMBERG DOING BUSINESS RANKING

2014 Rank	Country	Less-tangible costs score	Readiness of local consumer base score
1	Hong Kong	88.8	75.2
2	Canada	91.5	76.2
3	United States	79.7	71.1
4	Singapore	89.5	71.9
5	Australia	83.3	71.6
5	Germany	86.2	74.7
7	United Kingdom	85.2	71.1
8	Netherlands	88.8	70.7
9	Spain	76.0	68.5
10	Sweden	87.1	72.9

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GOVERNANCE =
TRADITIONS AND INSTITUTIONS BY WHICH AUTHORITY IS EXERCISED
= OVERALL QUALITY OF PUBLIC AND PRIVATE MANAGEMENT PROCESS



Source: World Bank

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HOW ASSESSING CORRUPTION?

TRANSPARENCY INTERNATIONAL'S CPI

- ▶ Germany-based NGO, founded in 1993
- ▶ Global network with national chapters in >70 countries
- ▶ Annual **Corruption perception index** ranking 180 countries
- ▶ Annual Bribe index

CPI is a composite index: poll of polls conducted over a 3-year period, drawing on 13 surveys from 8 independent organizations

MEASURING CORRUPTION?

1	New Zealand
2	Denmark
3	Singapore
3	Sweden
5	Switzerland
6	Finland
6	Netherlands
8	Australia
8	Canada
8	Iceland
11	Norway
12	Hong Kong
12	Luxembourg
14	Germany
14	Ireland
16	Austria



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162	Guinea-Bissau
162	Kyrgyzstan
162	Venezuela
168	Burundi
168	Equatorial Guinea
168	Guinea
168	Haiti
168	Iran
168	Turkmenistan
174	Uzbekistan
175	Chad
176	Iraq
176	Sudan
178	Myanmar
179	Afghanistan
180	Somalia

EMCS & SHADOW ECONOMY

Country↓	% GNP Informal Economy
Georgia	67.3
Bolivia	67.1
Panama	64.1
Azerbaijan	60.6
Peru	59.9
Zimbabwe	59.4
Tanzania	58.3
Nigeria	57.9
Thailand	52.6
Ukraine	52.2
Guatemala	51.5
Uruguay	51.1
Honduras	49.6
Zambia	48.9
Belarus	48.1
Armenia	46.3
Russia	46.1
Benin	45.2
Nicaragua	45.2
Moldova	45

Sources: World Bank
Hernando de Soto

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UNDP HUMAN DEVELOPMENT INDEX

- ▶ What is development?
- ▶ **Economic growth** + those conditions that make growth **sustainable** over the long-term
- =
- ▶ Σ life expectancy, education, health, infrastructure, institutions, governance...

HUMAN DEVELOPMENT INDEX

- ▶ HDI developed by UNDP
- ▶ A composite index measuring average achievement in three basic dimensions of human development—a long and healthy life, knowledge and a decent standard of living, as measured by real GDP per capita on a purchasing power parity basis.

1. Norway		170	Malawi	
2. Australia		171	Sudan	
3. United States		172	Zimbabwe	
4. Netherlands		173	Ethiopia	
5. Germany		174	Liberia	
6. New Zealand		175	Afghanistan	
7. Ireland		176	Guinea-Bissau	
8. Sweden		177	Sierra Leone	
9. Switzerland		178	Guinea	
10. Japan		178	Burundi	
11. Canada		180	Central African	
12. Korea		181	Eritrea	
13. Hong Kong		182	Mali	
14. Iceland		183	Burkina Faso	
15. Denmark		184	Chad	
16. Israel		185	Mozambique	
17. Belgium		186	Niger	
18. Austria		186	Congo (DR)	
19. Singapore				
20. France				

CONCLUSION

ASSESSING COUNTRY RISK?

1. Market consensus: rating agencies
2. Macroeconomic analysis
3. Balance of payments analysis: liquidity & solvency
4. Socio-political analysis
5. Business environment: corruption, bureaucracy, institutions, transparency
6. Economic Intelligence!

HERITAGE FOUNDATION: INDEX OF ECONOMIC FREEDOM

- ▶ **Economic freedom** = *absence of government coercion or constraint on the production, distribution, or consumption of goods and services beyond the extent necessary for citizens to protect and maintain liberty itself.*
- ▶ The Index includes a broad array of institutional factors determining economic freedom: corruption, non-tariff barriers to trade, the fiscal burden of government, the rule of law, regulatory burdens, restrictions on banks, labor market regulations, black market activities...

CRITERIA OF ECONOMIC FREEDOM

- ▶ To measure economic freedom and rate each country, the *Index* is based on 50 independent economic variables within 10 broad categories of economic freedom:
 1. Trade policy,
 2. Fiscal burden of government,
 3. Government intervention in the economy,
 4. Monetary policy,
 5. Capital flows and foreign investment,
 6. Banking and finance,
 7. Wages and prices,
 8. Property rights,
 9. Regulation, and
 10. Black market activity

HERITAGE FOUNDATION'S INDEX OF ECONOMIC FREEDOM

- ▶ 1. HongKong
- ▶ 2. Singapore
- ▶ 3. Luxemburg, New Zealand
- ▶ 5. Ireland
- ▶ 6. Denmark, Estonia, USA
- ▶ 9. Australia, UK
- ▶ 11. Finland, Iceland, Netherlands, Sweden
- ▶ 15. Switzerland
- ▶ 16. Chile
- ▶ 18. Canada
- ▶ 19. Austria, Belgium, Germany
- ▶ 40. France

- ▶ Trade + Fiscal Burden, + Government Intervention, + Monetary Policy, + FDI + Inflation + External Competitiveness + Banking sector

WORST:
Argentina, Colombia, Venezuela, China, Russia, Vietnam, Romania, Ukraine, Nigeria, Iran, Syria, Cuba...

FREEDOM HOUSE:

POLITICAL FREEDOM IN THE WORLD ANNUAL REPORT (1972-2011)

- ▶ Since 1972, Freedom House has published an annual assessment of the state of freedom in all countries in the world, based on a checklist of questions on political rights and civil liberties that are derived from the Universal Declaration of Human Rights. Each country is assigned a rating for PR and a rating for CL based on a scale of 1 (best) to 7 (worst).
- ▶ <http://www.freedomhouse.org/ratings/index.htm>

FREEDOM HOUSE:

FREEDOM IN THE WORLD ANNUAL REPORT

Free countries (89)

- ▶ Australia
- ▶ Finland
- ▶ Malta
- ▶ Slovenia
- ▶ Uruguay
- ▶ Bulgaria
- ▶ Chile
- ▶ Costa Rica
- ▶ Mauritius
- ▶ Poland

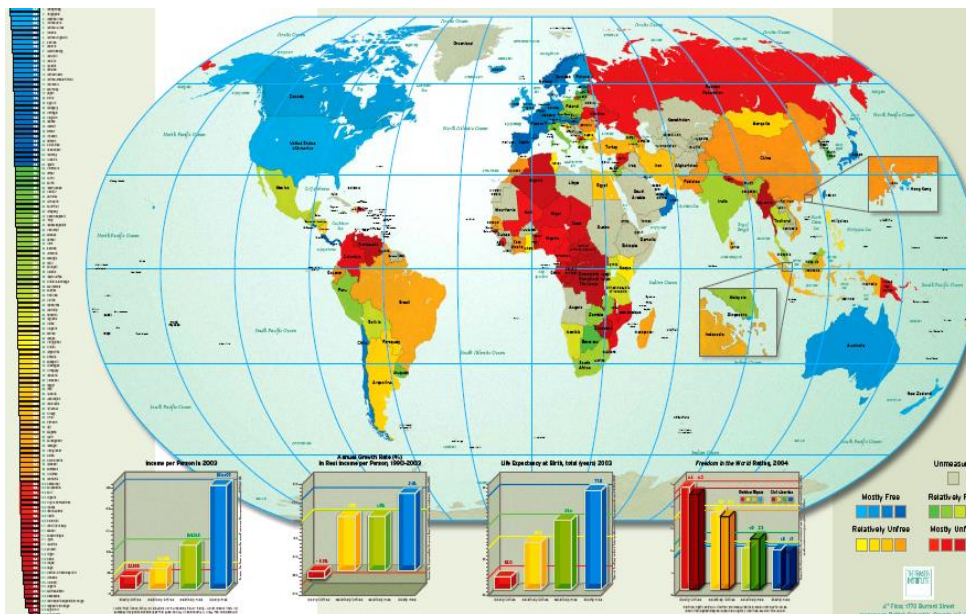
Not Free countries (47)

- ▶ Cameroon
- ▶ Congo
- ▶ Haiti
- ▶ Iran
- ▶ China
- ▶ Vietnam
- ▶ Burma
- ▶ Cuba
- ▶ Saudi Arabia
- ▶ Syria
- ▶ Turkménistan

FRASER INSTITUTE

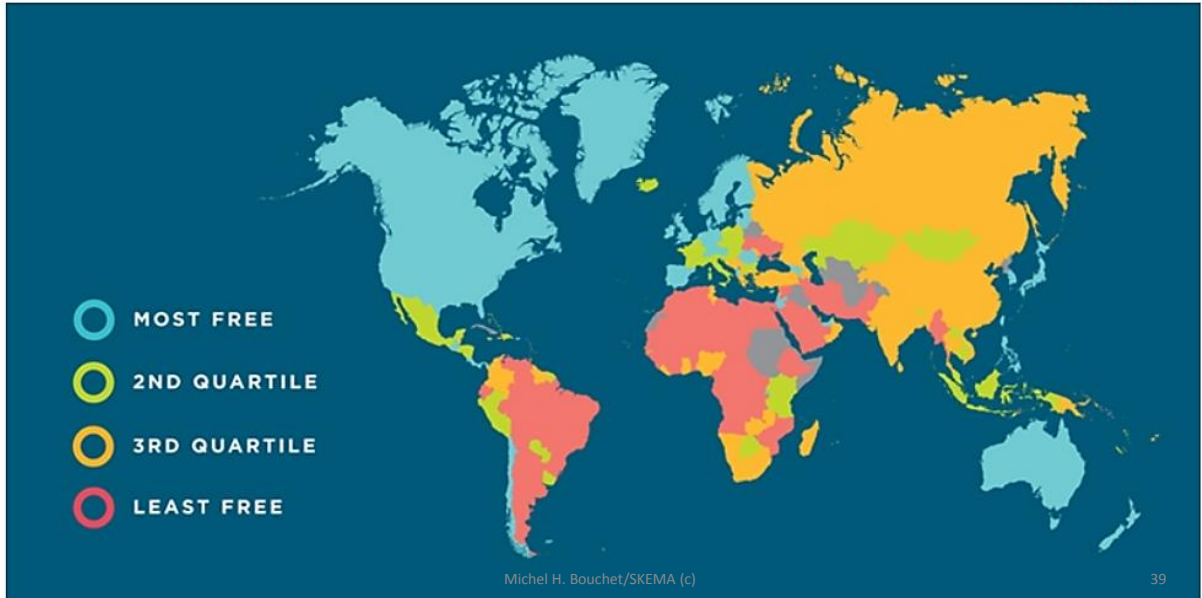
- ▶ Since 1975
- ▶ Annual Indices of Economic & Human Freedom in the world: reliable measure of cross-country differences in economic freedom, using third-party data to help ensure objectivity
- ▶ **Criteria:** government quality, legal structure, security of property rights, access to sound money, personal choice, freedom to exchange with foreigners and to compete in markets, quality of regulations and institutional strength...
- ▶ **The Economic Freedom Annual Report** is the measurement of economic freedom, ranking countries based on five areas: size of government, legal structure and security of property rights, access to sound money, freedom to trade internationally, and regulation of credit, labor and business. The report compares 159 countries and territories

FRASER INSTITUTE'S ECONOMIC FREEDOM WORLD MAP



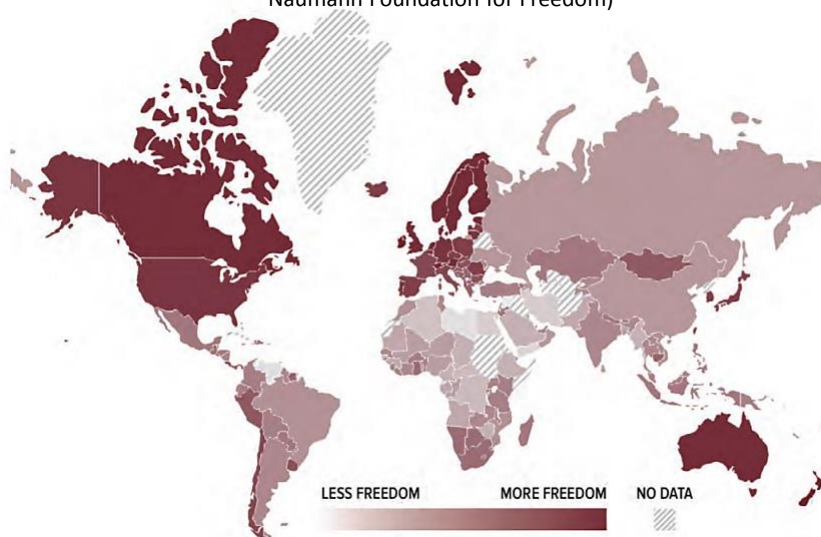
Economic Freedom of the World: 2017 Annual Report

— Sep 28, 2017

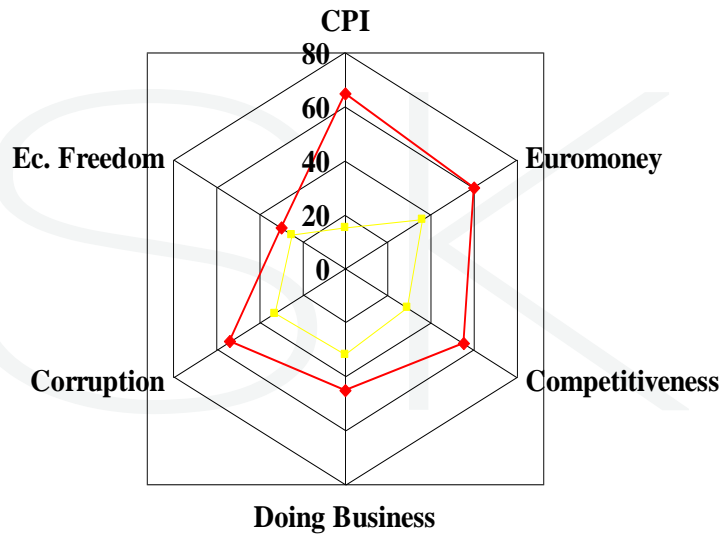


FRASER INSTITUTE: HUMAN FREEDOM INDEX 2018

The index ranks 159 countries and jurisdictions based on 79 indicators of personal, civil and economic freedoms (joint project with the Cato Institute in the U.S. and Germany's Friedrich Naumann Foundation for Freedom)



COUNTRIES X & Y: A MULTI-INDEX COMPOSITE GRAPH



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