

HOW TACKLING POLITICAL RISK?

FAILED STATES AND INSTITUTIONAL WEAKNESSES



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1

STATE FAILURE AND POLITICAL RISK ASSESSMENT

- ▶ **Country Risk** is the possibility that a foreign country may be **unable or unwilling** to fulfill its obligations fully and on time, towards a foreign lender and/or investor, or exporter, or domestic residents!

State failure produces **political risk**, hence the unexpected unfavorable consequences of the arbitrary exercise of power by a government and its ramifications

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THE COST OF GLOBAL POLITICAL RISK

The Annual Economic Impact Of Global Violence

Economic impact of violence/conflict to the world economy (in trillion U.S. dollars)



<https://www.statista.com/chart/3948/the-annual-economic-impact-of-global-violence/>

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MIGA: THE KEY CHALLENGE OF POLITICAL RISK

MAJOR CONSTRAINTS ON FOREIGN INVESTMENT IN EMERGING MARKETS

Percent of respondents



In your opinion, which of the following factors will pose the greatest constraint on investments by your company in emerging markets this year and over the next three years?

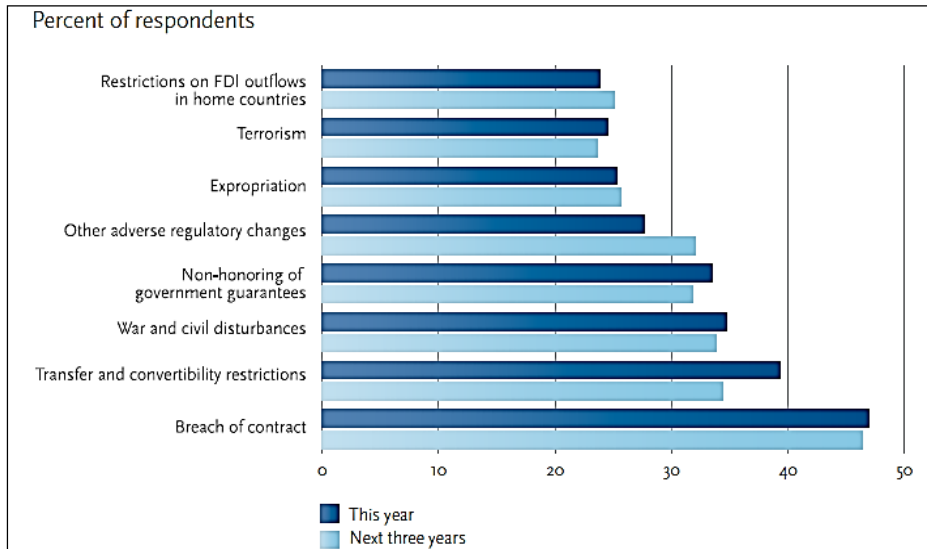
Source: MIGA-EIU Political Risk Survey 2009.

Note: Percentages add up to more than 100 percent due to multiple selections.

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MIGA: TYPES OF POLITICAL RISK OF HIGHER CONCERN TO MNCs IN EMCS



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WHAT IS A FAILED STATE?

WHY DO STATES FAIL?

HOW CAN ONE MEASURE THE RISK AND DEGREE OF STATE FAILURE?

WHICH COUNTRIES MOST EXEMPLIFY THE FEATURES OF INSTITUTIONAL WEAKNESSES?

AND

WHAT ARE THE EARLY WARNING SIGNALS OF STATE FAILURE?

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What is a Failed State?

State fragility and state failure...

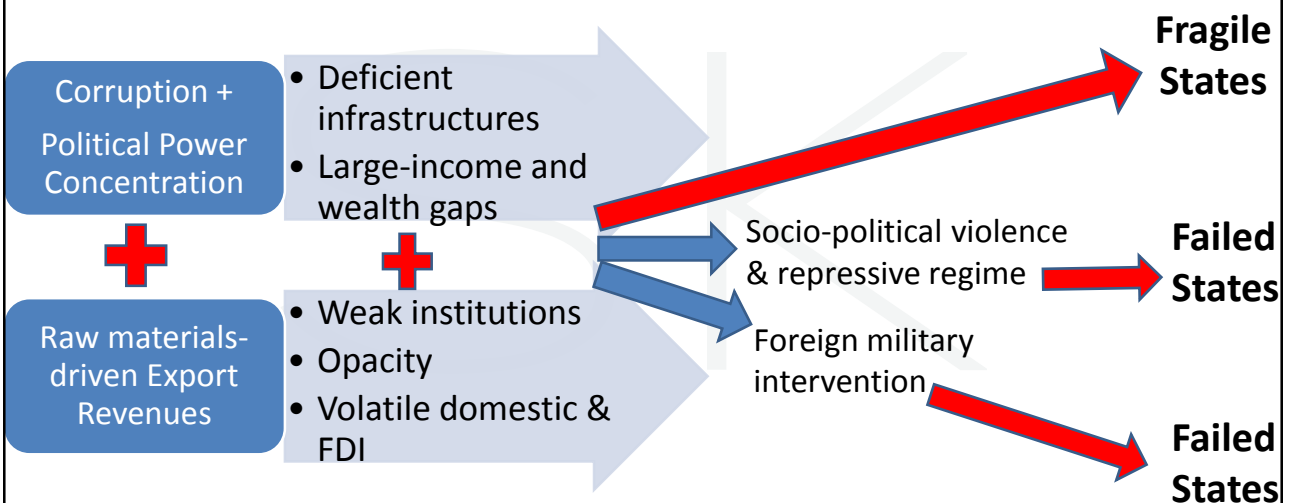
A “FRAGILE AND WEAK STATE » IS A STATE WHOSE INSTITUTIONAL FRAMEWORK IS TOO WEAK TO MAINTAIN SOCIAL COHESION THROUGHOUT THE PROCESS OF DEVELOPMENT

INSTITUTIONAL WEAKNESSES, CONSEQUENTLY, GENERATE A CRISIS OF SOCIAL MEDIATIONS WHERE PARTIES, UNIONS, SOCIAL INSTITUTIONS AND LOCAL ELITES LOSE CREDIBILITY FOR ADDRESSING SOCIAL FRUSTRATION AND DEMANDS, HENCE RISING TENSIONS.

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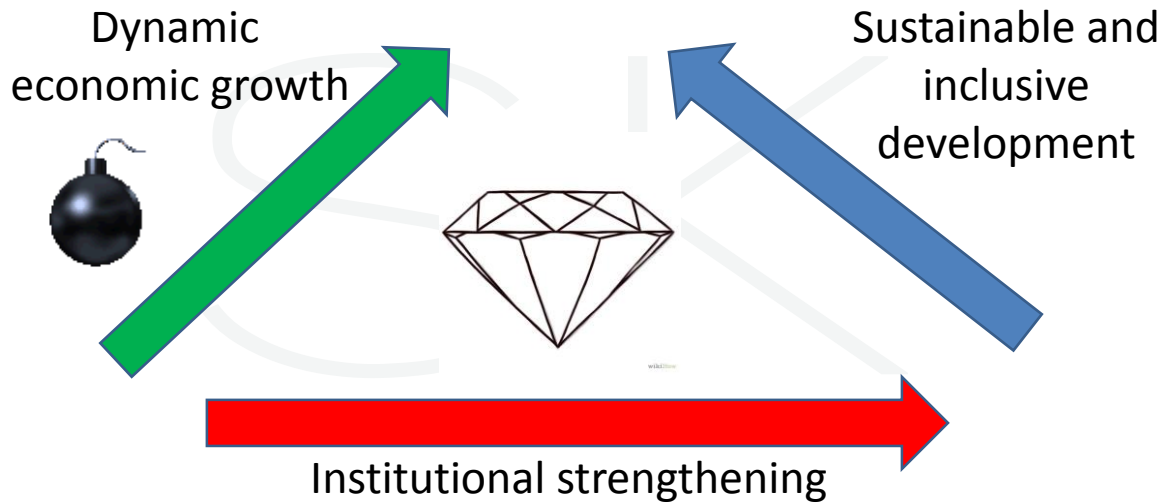
THE UNFOLDING OF STATE FAILURE



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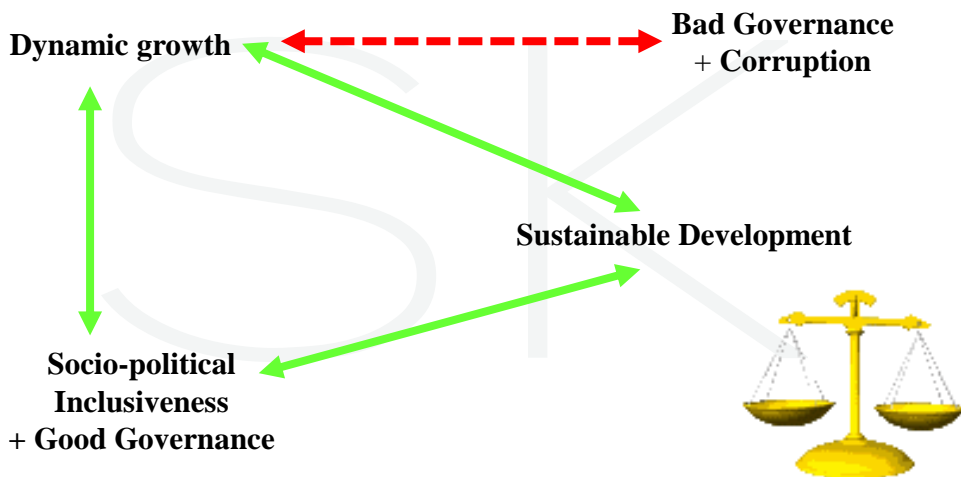
THE REQUIRED POLITICAL STABILITY TRIANGLE



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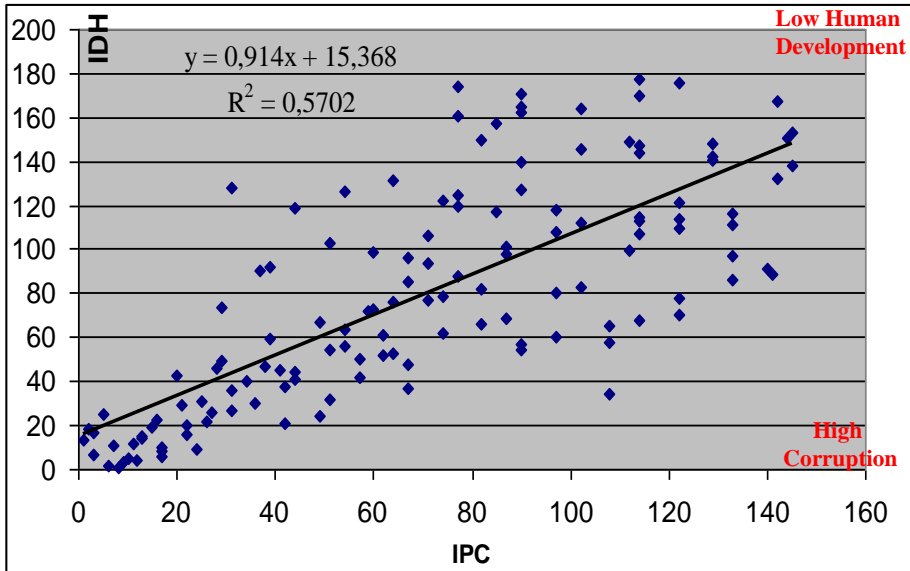
TRILEMMA OF GROWTH AND DEVELOPMENT?



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CORRELATION HUMAN DEVELOPMENT /CORRUPTION



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A FEW FACTS REGARDING DEMOCRACY AND DEVELOPMENT



1. Political regimes have **little** impact on **GDP growth rate**
2. **GDP per capita growth does breed democracy**
3. Economic growth provides legitimacy to dictatorships (while increasing demand for political change)
4. **Per capita income grows faster under democracy** (due to human capital and because population rises less fast than under dictatorships)
5. Growth is influenced less by the type of regime than by regime instability: **Democracy provides a stable political environment, hence a positive impact on sustainable growth!**

Since 1980, of the 124 EMCs that have managed to sustain a 5% growth rate for a full decade, 52 % were democracies. What matters is not the implementation of key reforms for growth and development.

HOW MOVING FROM GROWTH TO SUSTAINABLE AND INCLUSIVE DEVELOPMENT?

Assumption n°1

- ▶ Primacy of **human capital for both growth and democratization**: human and social capital shape both institutional and productive capacities of a society.
- ▶ Growth in **income and human capital** causes institutional improvement with better political institutions even with pro-market dictators: **policy choices matter** while institutional quality rises as a country grows richer
- ▶ Economic growth and human capital accumulation cause institutional improvement, rather than the other way around

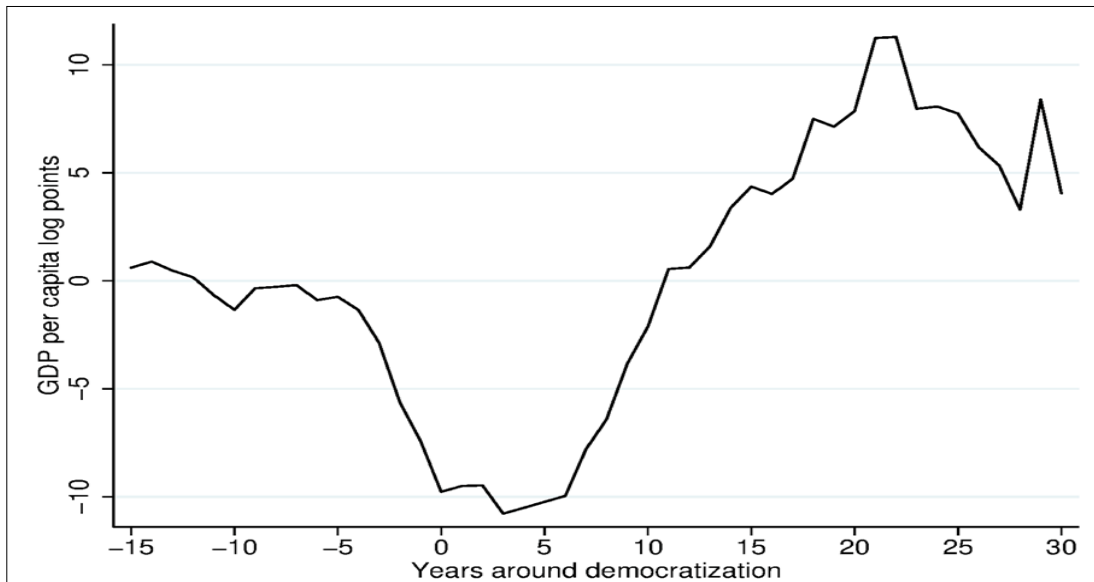
Assumption n°2

- ▶ **Democracy** and other checks on government are the **key mechanisms for securing property rights and boosting growth**
- ▶ **Good and stable institutions will enhance the pace and quality of economic growth**
- ▶ **Robust institutions and good governance matter!**

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DEMOCRACY BREEDS GDP PER CAPITA GROWTH WHILE ECONOMIC GROWTH LEADS TO DEMOCRACY (ACEMOGLU & ROBINSON)

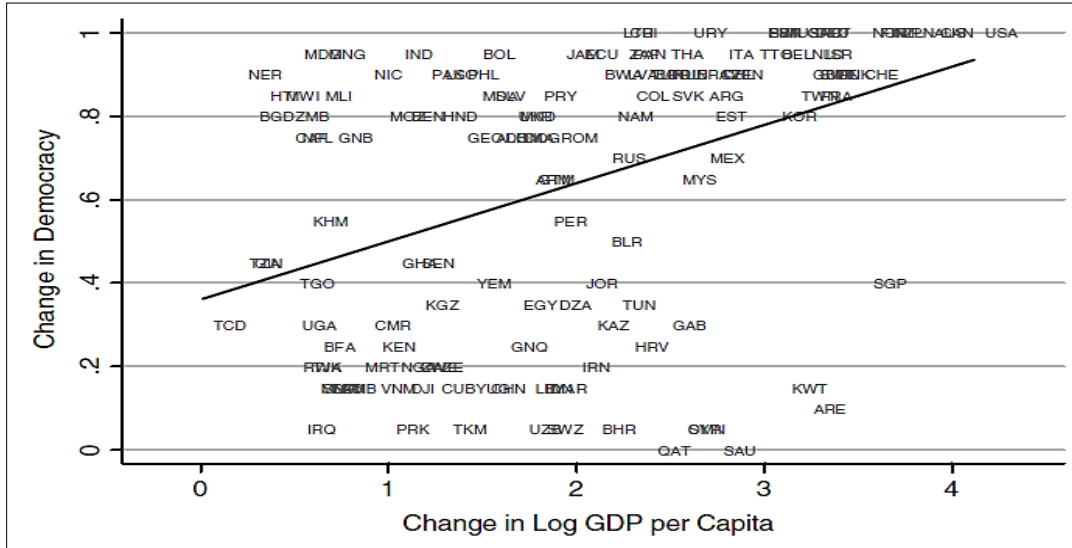


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DEMOCRATIZATION AND INCOME GROWTH 1500-1995

INCOME PER CAPITA AND DEMOCRACY ARE CORRELATED BECAUSE ECONOMIC AND SOCIO-POLITICAL INSTITUTIONS TRANSFORM GROWTH INTO SUSTAINABLE AND INCLUSIVE DEVELOPMENT

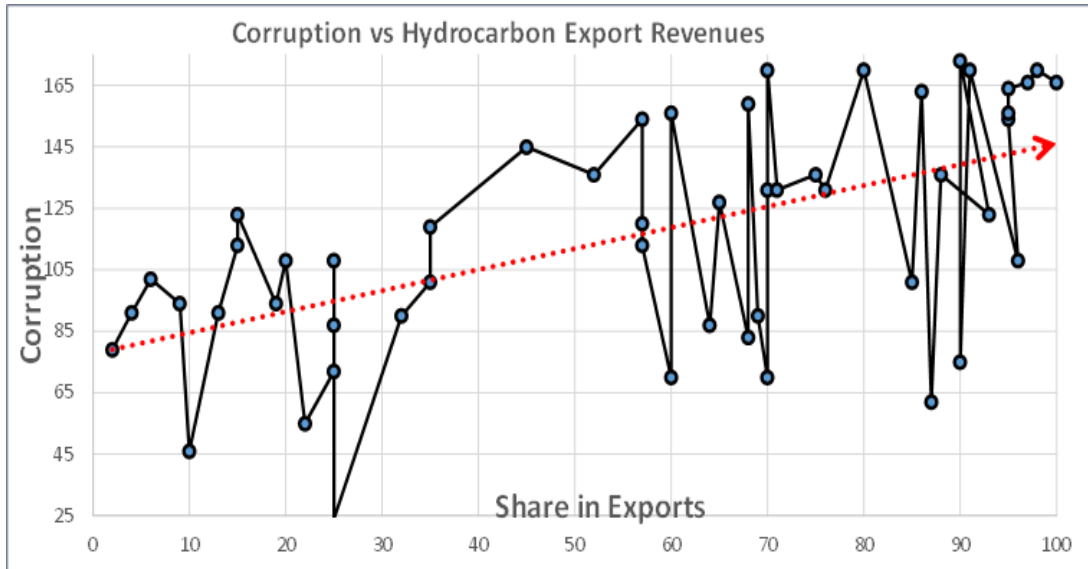


J. Robinson, 2006

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OIL-BASED GROWTH LEADS TO POWER AND WEALTH CONCENTRATION, AND CORRUPTION (EXCEPTED IN NORWAY!!?)



Source: Bouchet & alii Palgrave 2019

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DEVELOPMENT = ECONOMIC GROWTH + KEY CONDITIONS THAT MAKE IT SUSTAINABLE!

	CHILE	COSTA RICA	RUSSIA	GABON
GDP/per capita	\$15,000	\$11,000	\$15,000	\$14,000
Life Expectancy	79	80	67	61
HDI Rank	40	62	55	106

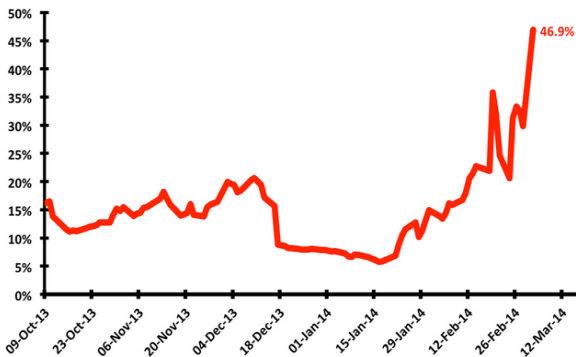


	ARMENIA	SRI LANKA	CONGO	ANGOLA
GDP per capita	\$5000	\$5000	\$5000	\$5000
Life expectancy	74	75	57	51
HDI Rank	87	97	142	148

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YIELD ON 6-MONTH UKRAINE GOVERNMENT BOND



UKRAINE:

THE PRICE OF POLITICAL RISK IN THE WAKE OF THE REVOLUTION AND THE RUSSIAN INVASION OF CRIMEA IN 2014



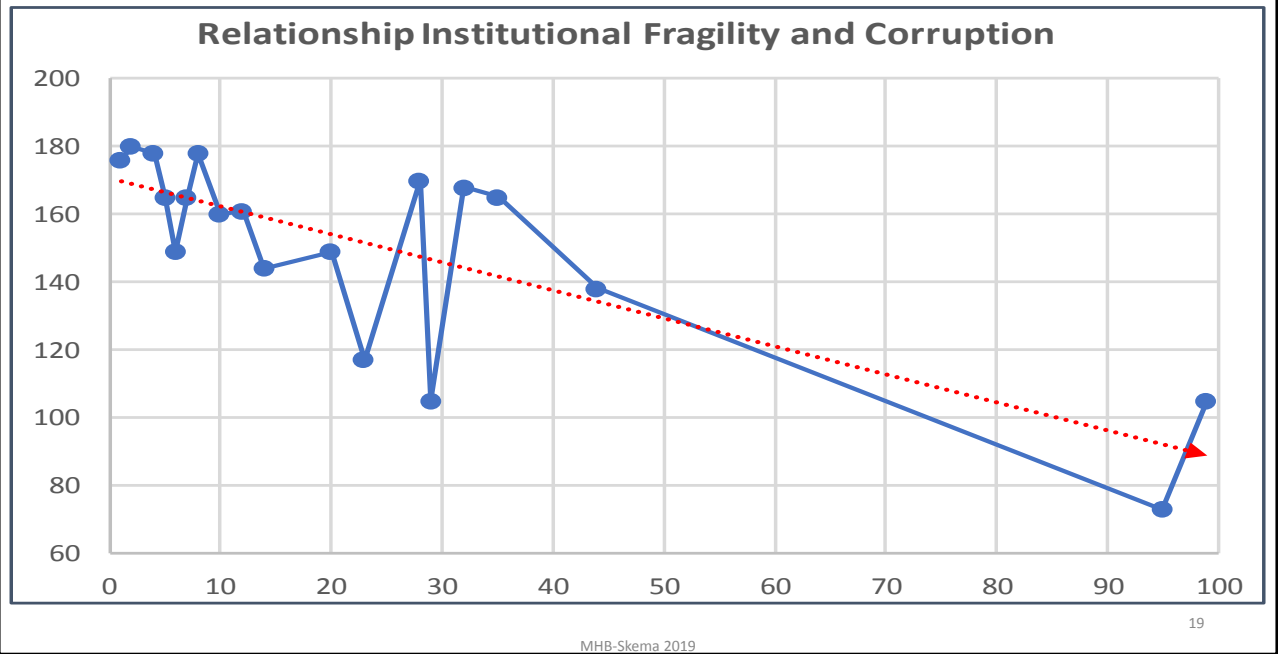
Sept 2017: back to market access?

bond swap with \$3 billion global bond issue over 15 year, with 7,375% in exchange for bonds maturing 2019-20

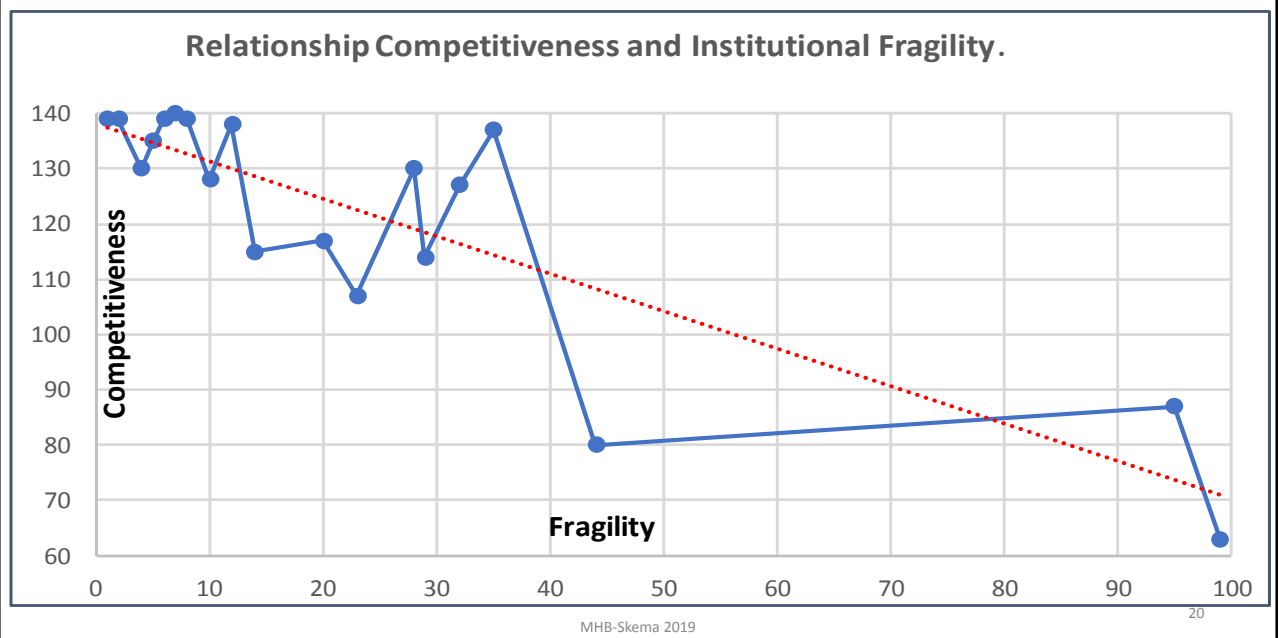
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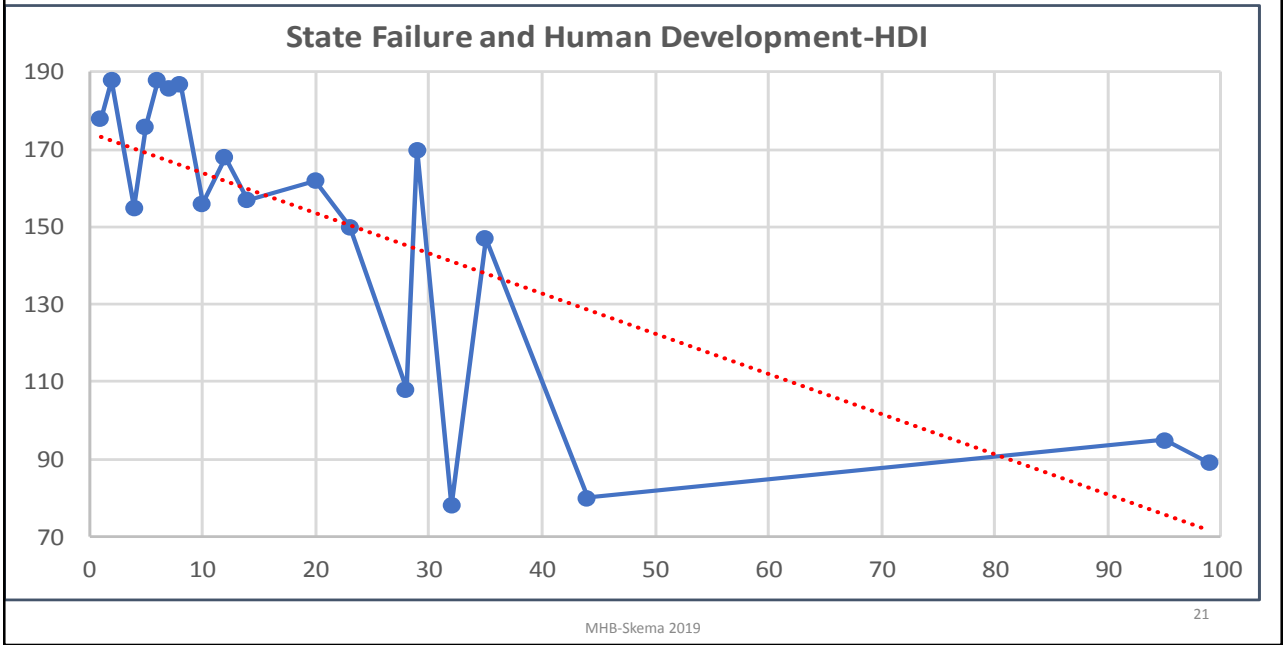
INSTITUTIONAL FRAGILITY AND CORRUPTION





INSTITUTIONAL FRAGILITY AND COMPETITIVENESS (WEF)



INSTITUTIONAL FRAGILITY AND HUMAN DEVELOPMENT (UNDP)



BETTER OFF IN TUNISIA OR IN ALGERIA ?

TUNISIA	ALGERIA
▶ GDP Per capita = \$10500	▶ GDP Per capita=13500
▶ HDI= 97	▶ HDI= 83
▶ Life expectancy f = 77	▶ Life expectancy= 75
▶ Infant mortality= 13	▶ Infant mortality= 22/1000
▶ Gender inequality: 0,28	▶ Gender inequality: 0,43
▶ Doing Business= 77	▶ Doing Business= 156
▶ Corruption = 75	▶ Corruption = 108

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MEASURING SOICO-POLITICAL RISK

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KEY FEATURES OF FAILED AND FRAGILE STATES

	n/178	Index TI/180 UNDP/188	Index **	WEF 140	KF/GDP%	human flight **	%	% (3 year av.)		
Weak States	Ranking	Corruption **	HDI **	GINI	Competitiv.	Capital flight	& Brain drain	Unempl.	Invest/GDP	Ext Debt/GDP%
Yemen	1	176	178	38	139	2%	7,3	35	12	30%
Somalia	2	180	188	39	139	1%	9,5	6	10	75%
Syria	4	178	155	36	130	3%	8,4	50	10	16%
Congo DR	5	165	176	49	135	39%	7	15	12	20%
CAR	6	149	188	44	139	4%	7,1	7	13	36%
Chad	7	165	186	43,3	140	2%	8,5	6	16	27%
South Sudan	8	178	187	35	139	1%	6,5	15	11	111%
Zimbabwe	10	160	156	43	128	5%	7,6	10	12	77%
Haiti	12	161	168	61	138	3%	8,4	15	25	30%
Nigeria	14	144	157	49	115	3%	6,9	23	15	70%
Uganda	20	149	162	42	117	3%	7,3	5	24	40%
Pakistan	23	117	150	33,5	107	1%	6,8	6	16	31%
Libya	28	170	108	42	130	22%	6,3	20	15	20%
Côte d'Ivoire	29	105	170	42	114	2%	7,3	5	16	37%
Venezuela	32	168	78	40	127	23%	6,1	35	14	33%
Angola	35	165	147	43	137	11%	6,9	9	24	57%
Lebanon	44	138	80	32	80	17%	5,6	9	20	200%
Tunisia	95	73	95	40	87	5%	5,9	16	21	90%
Peru	99	105	89	44	63	5%	7,1	10	21	35%

* Nonbank private deposits in international banks/BIS A6-1

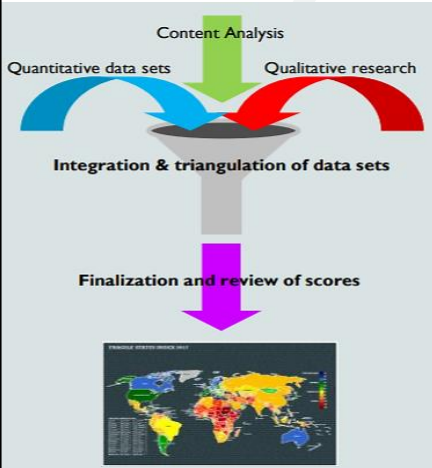
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** the higher, the worse

THE METHODOLOGY BEHIND THE FRAGILE STATES INDEX

The Fragile States Index produced by The Fund for Peace is a critical tool in highlighting not only the normal pressures that all states experience, but also in identifying when those pressures are outweighing a states' capacity to manage those pressures.



Annual ranking for 178 countries with 12 political, economic and social indicators and >100 sub-indicators, coupled with qualitative analysis and expert validation:

Economic decline, uneven development, brain drain, state legitimacy, public services, human rights, demographic pressures, refugees, external intervention, rule of law...

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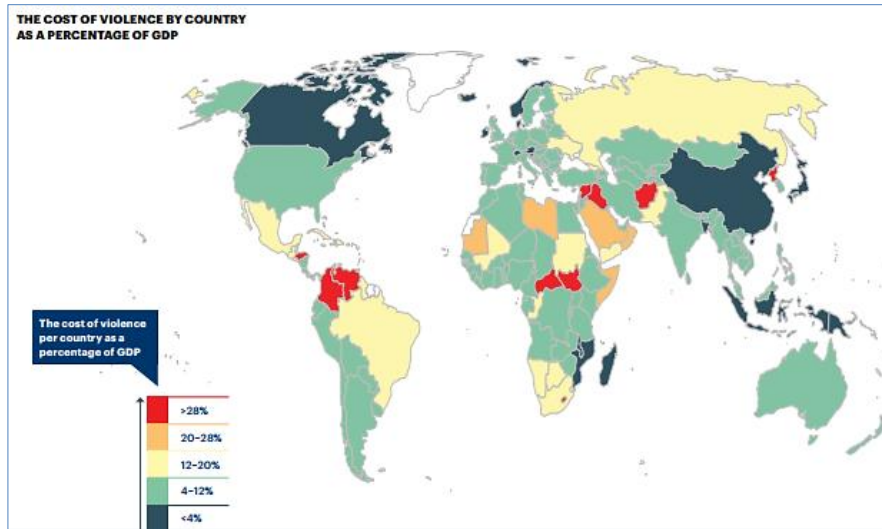
RANKING OF TOP RISKS REPORTED BY FTSE 100 FIRMS (FT JULY 2017)



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THE COST OF VIOLENCE IN % OF GDP (WORLD ECON FORUM: THE ECONOMIC VALUE OF PEACE REPORT)

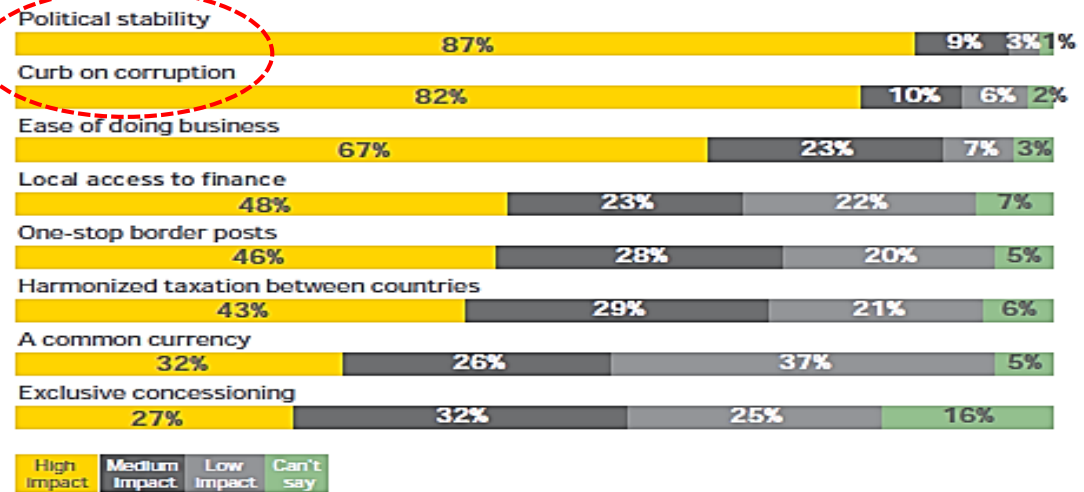


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BOOSTING FDI IN AFRICA?

What impact would the following changes have on Africa attractiveness?



Source: Ernst & Young's 2012 Africa attractiveness survey. Total respondents: 505.

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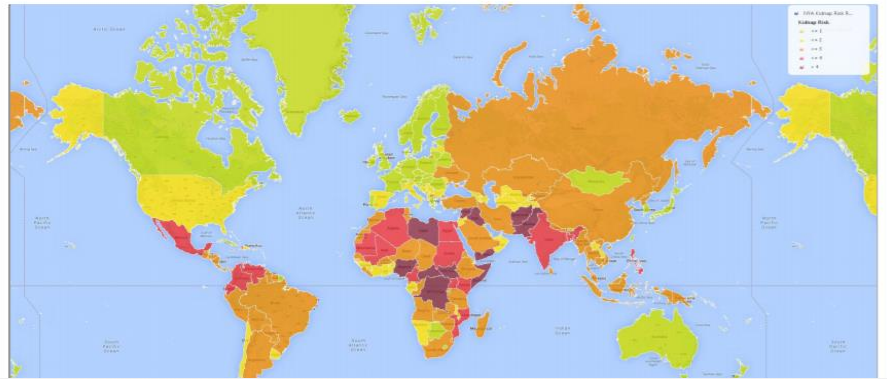
TOP 20 KIDNAP RANKING



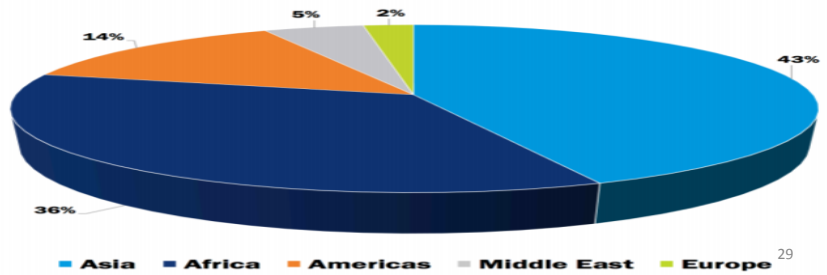
1. South Africa
2. Pakistan
3. Mexico
4. India
5. Nigeria
6. Venezuela
7. Lebanon
8. Philippines
9. Afghanistan
10. Colombia
11. Iraq
12. Syria
13. Guatemala
14. Yemen
15. Libya
16. Egypt
17. Brazil
18. Kenya
19. Nepal
20. Malaysia

: >7,770 kidnaps for ransom!

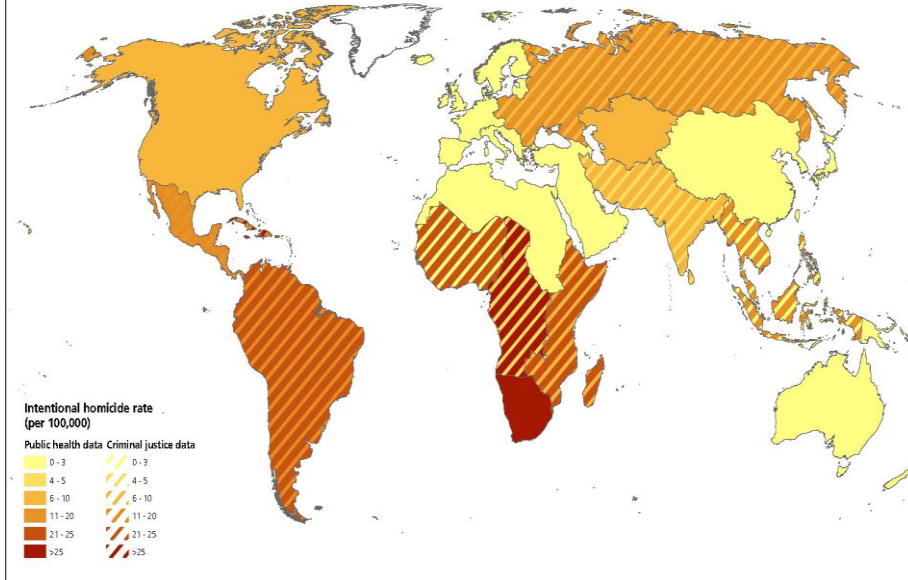
Source: Hiscox Group/FT/ AIG



**KIDNAPPING INCIDENTS BY REGION
JANUARY – DECEMBER 2017**



Intentional homicide rate by sub-region and for two sources, latest available year

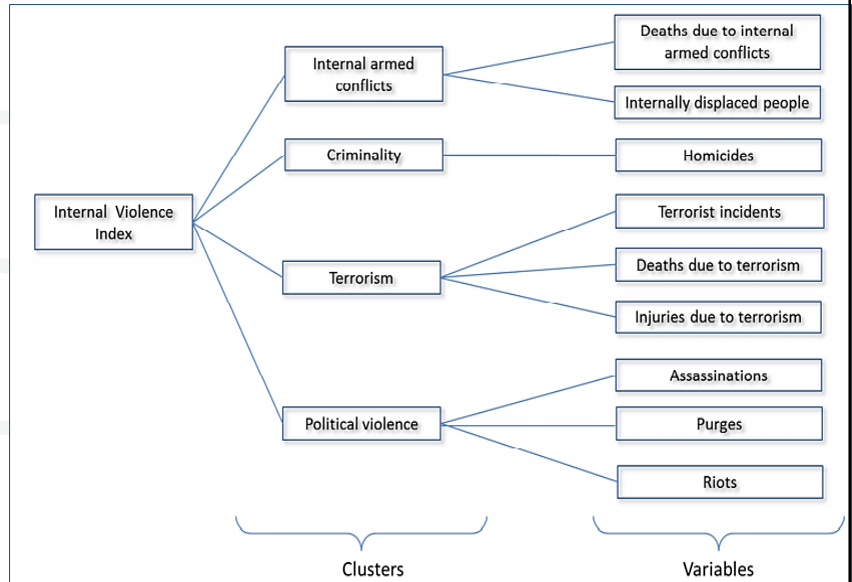


[HTTP://WWW.UNODC.ORG/UNODC/INDEX.HTML?REF=MENUTOP](http://www.unodc.org/unodc/index.html?ref=menutop)

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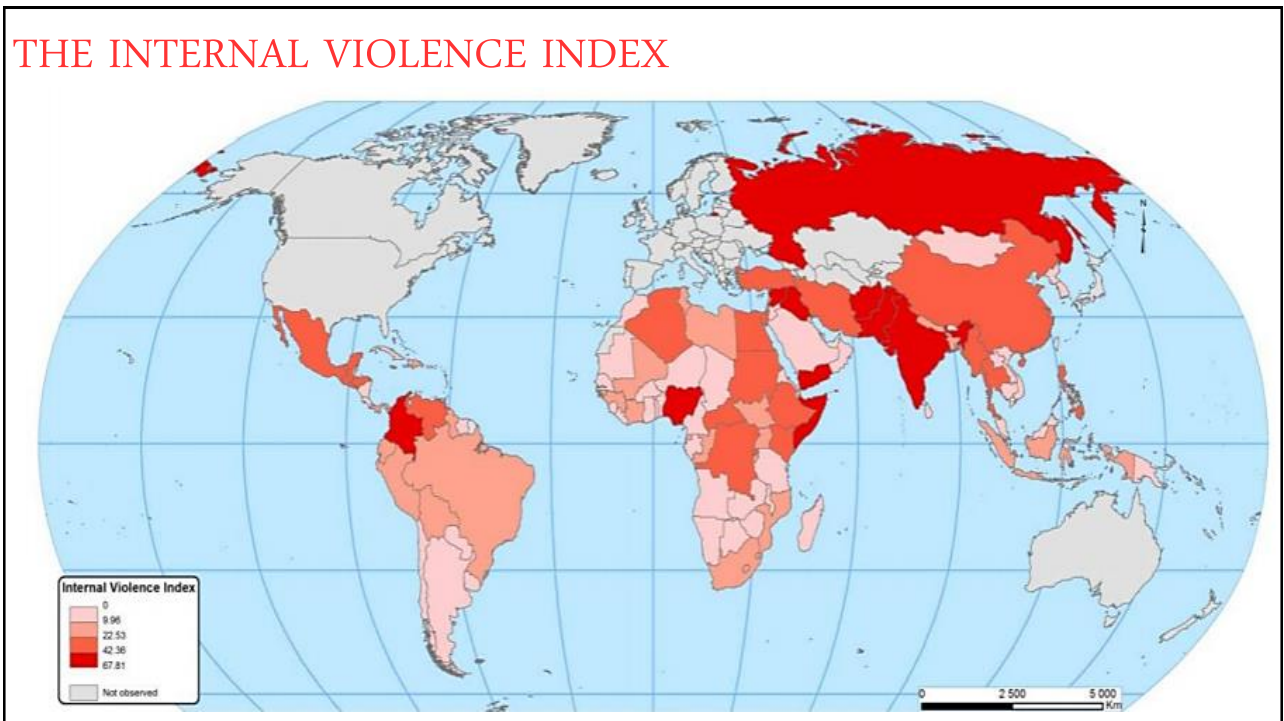
THE INTERNAL VIOLENCE INDEX

The composite index measures a narrow concept of fragility for 130 developing countries through their level of violence in its many different forms: internal armed conflicts, criminality, terrorism, and political violence: Iraq, Pakistan, Afghanistan, Yemen, Syria, and Nigeria.



MHB-Skema 2019 SOURCE: FERDI April 2016: Feindouno / Goujon /Wagner

THE INTERNAL VIOLENCE INDEX

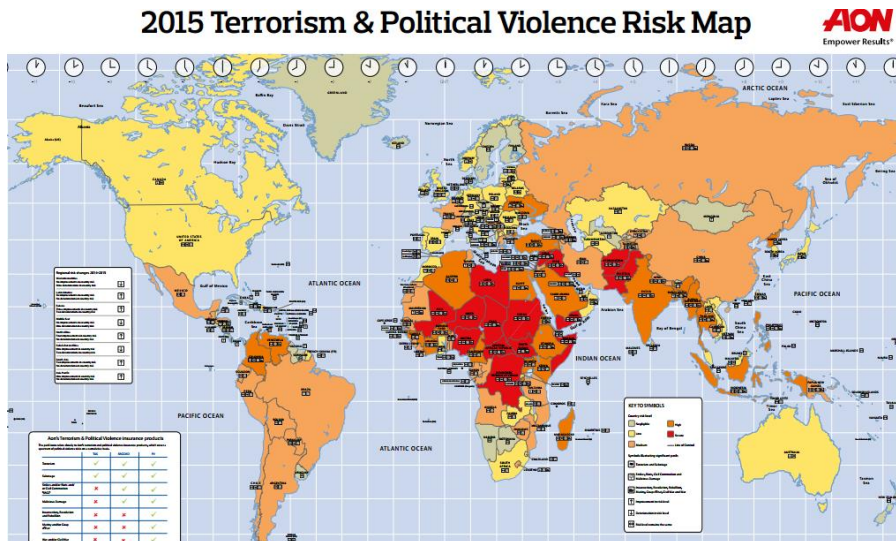


AON POLITICAL RISK MAP

- ▶ The Aon Political Risk Map measures political risk in 163 locations and territories.
- ▶ Risk ratings are standardized across each location, on a six-point scale ranging from low to very high, with all risks updated once per quarter.
- ▶ EU and OECD countries are not rated in the map!!
- ▶ Political risk is calculated as a simple average of six core risk measures :
 1. • Political Violence
 2. • Exchange Transfer
 3. • Sovereign Non-Payment
 4. • Political Interference
 5. • Supply Chain Disruption
 6. • Legal & Regulatory

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MAPPING OUT POLITICAL RISK: FRANCE AS RISKY AS BRAZIL?

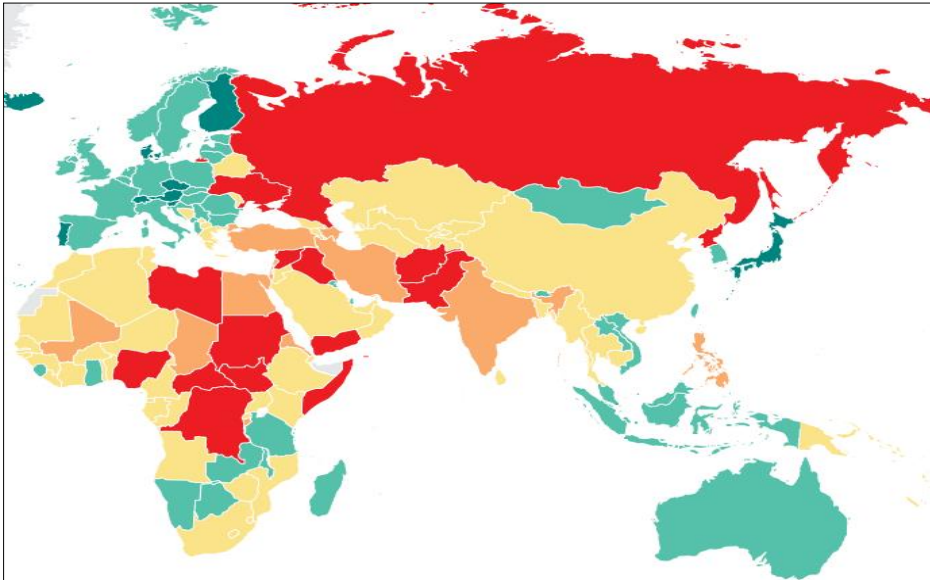


<http://www.aon.com/terrorismmap/2013-Terrorism-Map-14-05-2013.pdf>

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34

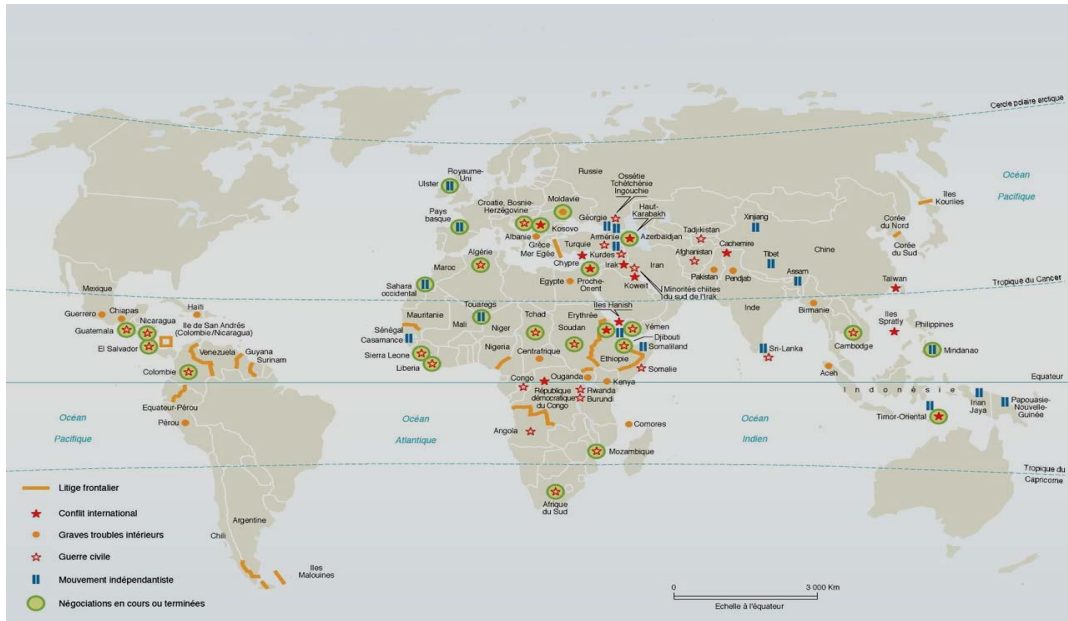
PEACE AND SECURITY INDEX



http://www.visionofhumanity.org/sites/default/files/Global%20Peace%20Index%20Report%202016_0.pdf
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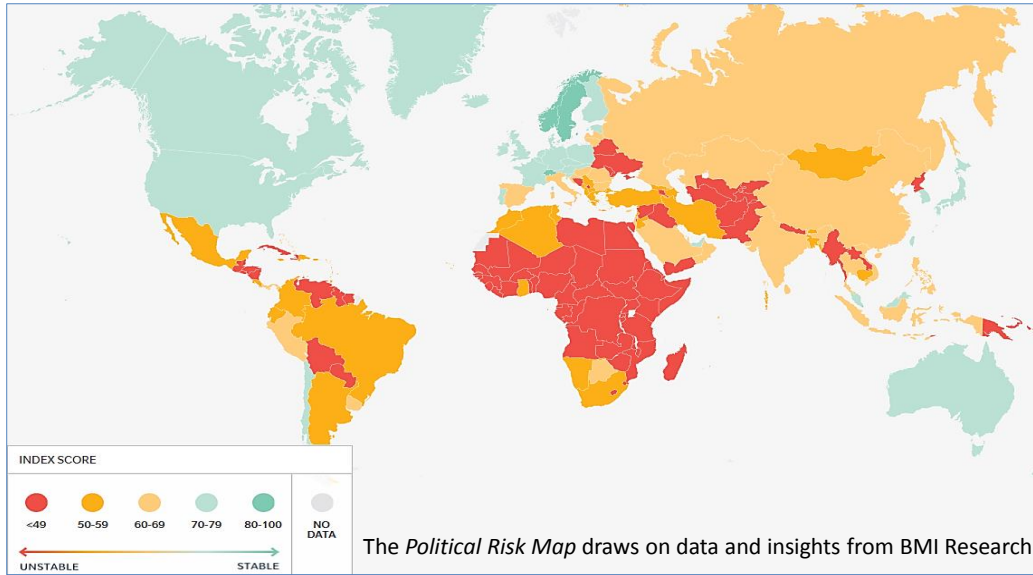
Wars and armed conflicts all over the world



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MARSH POLITICAL RISK MAP



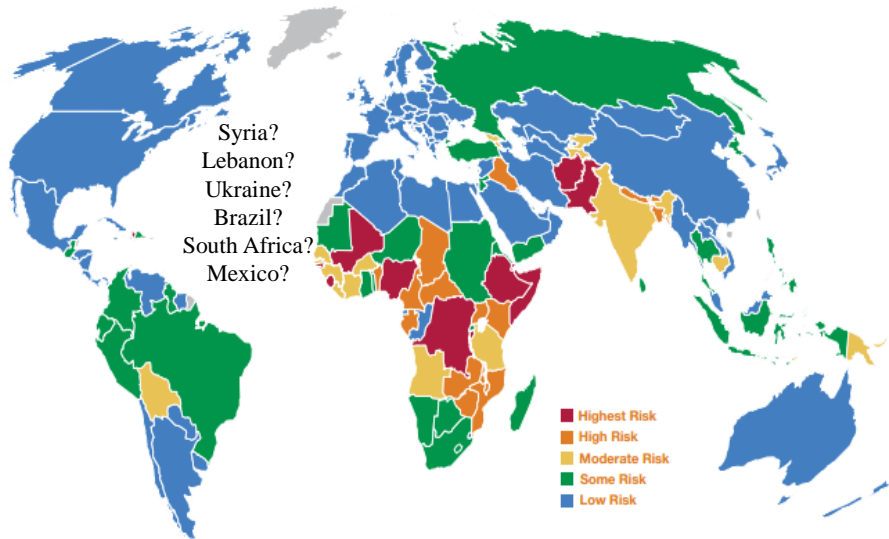
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37

BLINDNESS? RISK OF FUTURE POLITICAL CRISIS 2010-12

SOURCE: UNIVERSITY OF MARYLAND CENTER FOR CONFLICT MANAGEMENT

Figure 2.1 Risk of Future Instability, 2010-2012



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38