

WHAT IS COUNTRY RISK ALL ABOUT?

IN AN AGE OF GLOBALIZATION, PANDEMIC & GEOPOLITICAL THREATS?



CIFE SEMINAR ROMA-NICE 2024-25
MICHEL-HENRY BOUCHET

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«YESTERDAY'S» COUNTRY RISK

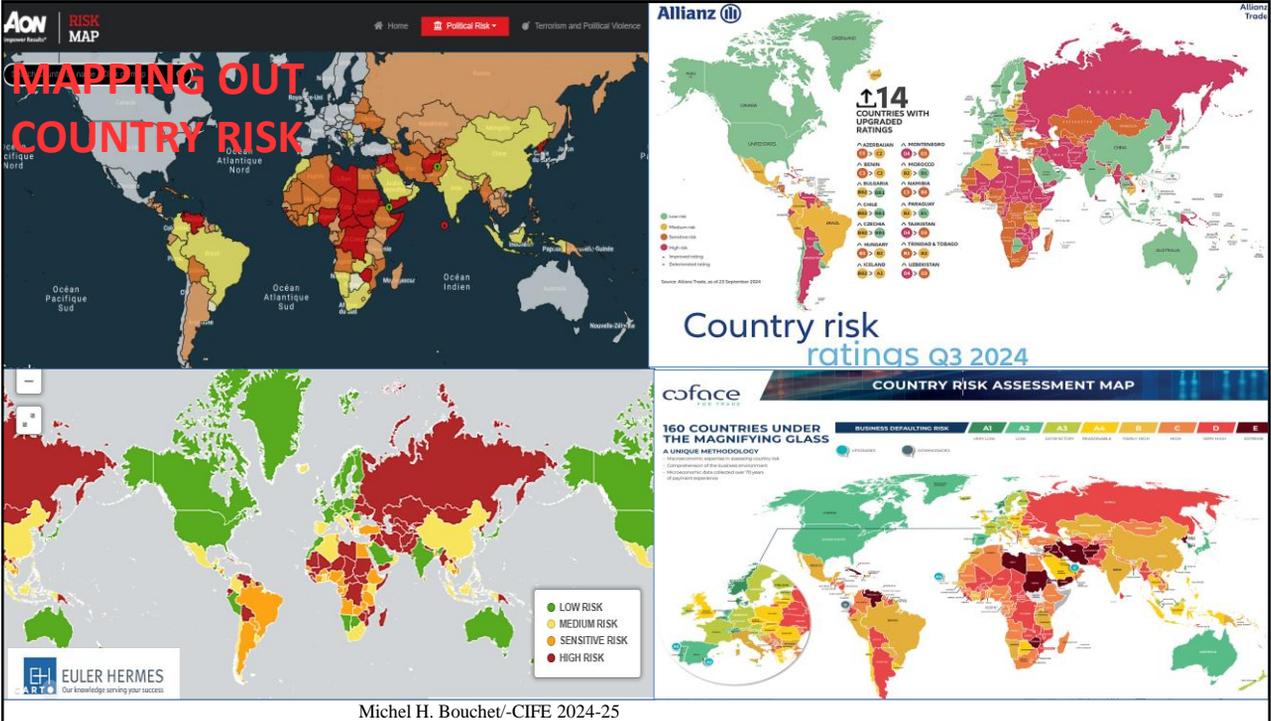
► Cross-border risk =

Assessment of a foreign entity's ability and willingness to meet its external obligations in full and on time

Foreign entity? Private firm, debtor country government, bank, investment fund, supplier, client, partner...

Country risk is composed of a complex combination of
political, financial and macro-economic risk

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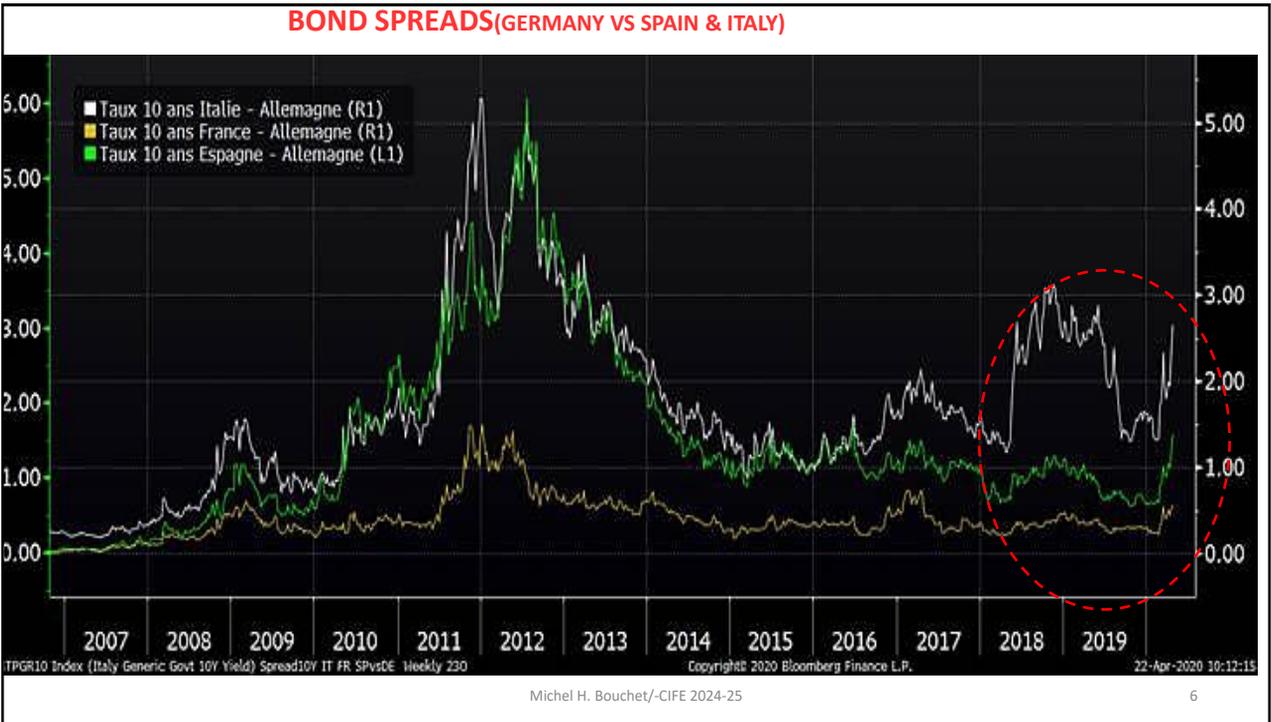
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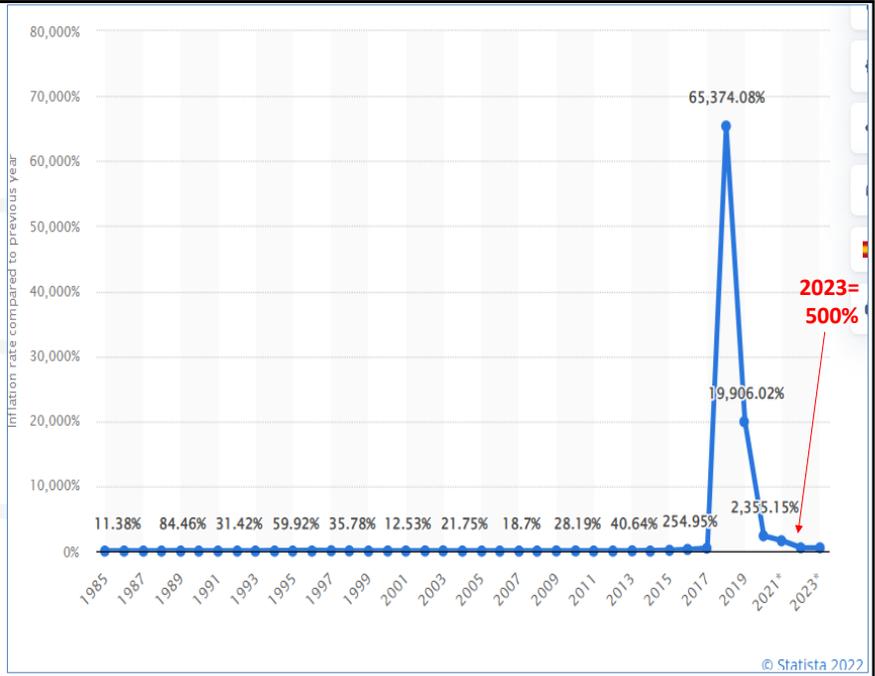


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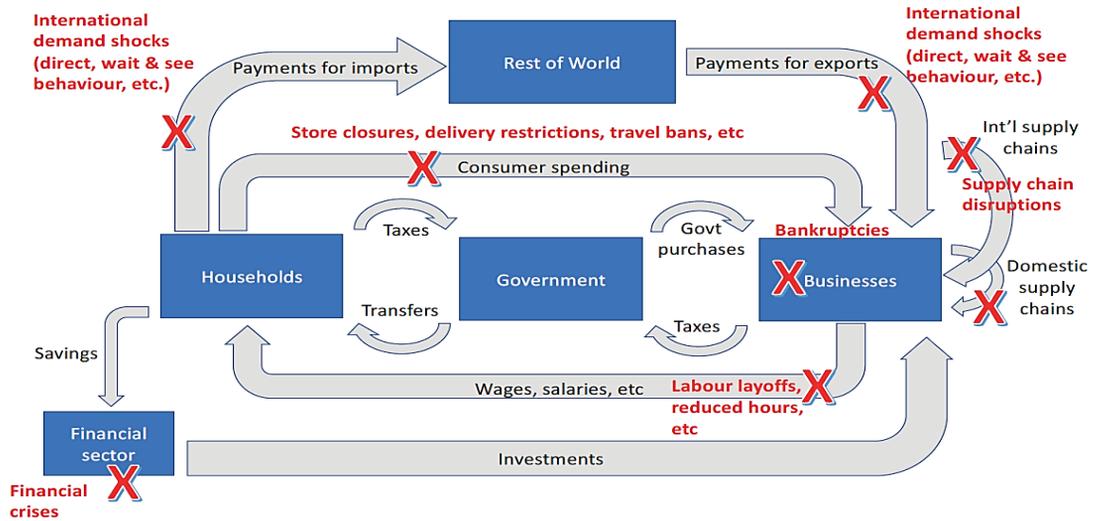
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CHAVES + MADURO = HYPERINFLATION!



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GLOBAL PANDEMIC = SYSTEMIC + COUNTRY RISKS DEPENDING ON THE GOVERNMENT'S RESPONSE TO THE SANITARY THREAT: COVID19'S MULTIPLE STRIKES IN THE CIRCULAR FLOW OF INCOME DIAGRAM



Source: Based on Baldwin (2020b).

« TODAY'S » COUNTRY RISK IN THE AGE OF GLOBALIZATION

Operational definition:

Set of interdependent factors, specific to a country in the global economy, which can affect both foreign and domestic agents

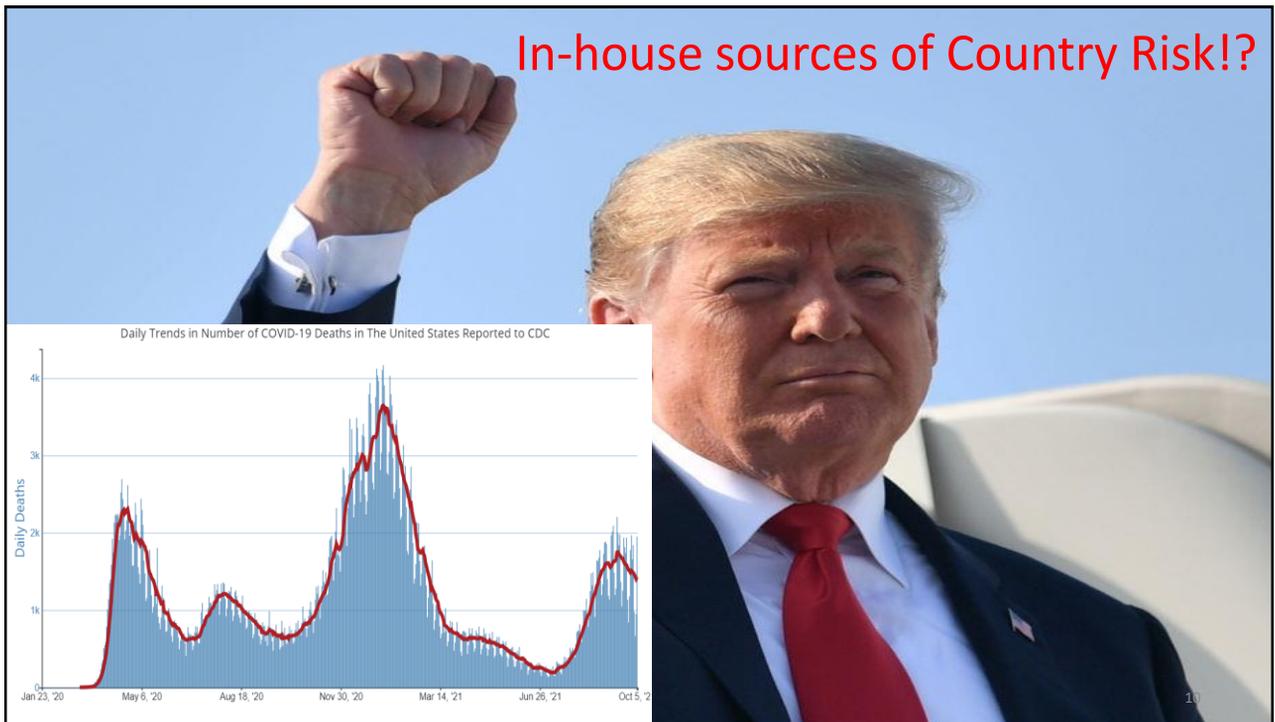
- Factors? Economic, financial, environmental, sanitary and socio-political
- Domestic agents? Private firms, households, banks, merchants, fund managers, exporters and importers, students...
- Foreign agents? Debtor country government, central bank, bank, supplier, client, partner...
- Country risk is composed of a complex combination of threats that must be assessed in the globalized system

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In-house sources of Country Risk!?



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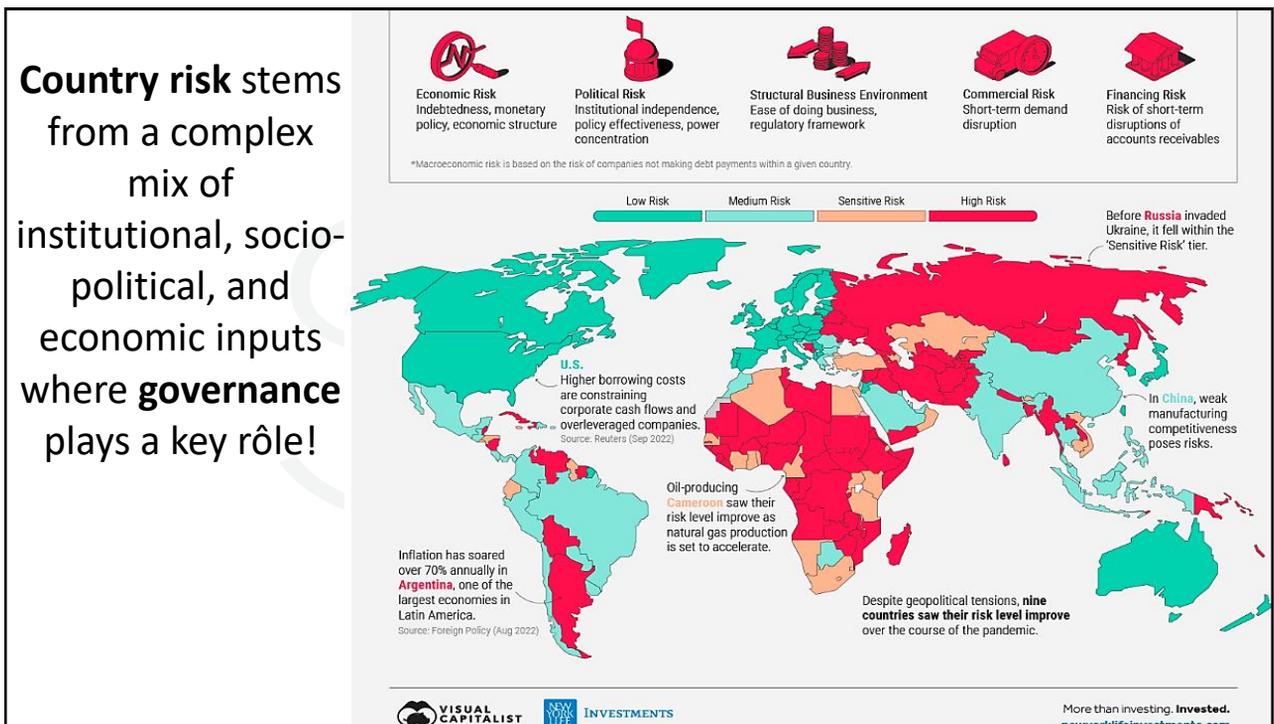
WHAT COUNTRY RISK IS NOT

- Country risk is **not** a monopoly of foreign creditors, exporters, importers, or investors
- Domestic residents (households, investors, corporate sector) also face country risk from their own country's socio-economic and political situation: the country's government can take **arbitrary** decisions that will affect the residents' well-being
- The country can be **contaminated** by adverse regional or global forces
- A deterioration in the risk perception by capital markets and rating agencies will **feedback** on domestic residents' environment = downgrading + capital flight!

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3 main country risk triggers:

1. DIRECT "HARD RISKS"

2. INDIRECT "SURROUNDING RISKS"

3. "COLLATERAL DAMAGES"

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COUNTRY RISK IN THE AGE OF DONALD TRUMP

Direct «Hard Risks»

- **Risk materialization directly hurts US business:** outbreak of a military conflict US-North Korea; sharp rise in interest rates and fall in bond prices; fall in oil prices; pandemic corona crisis; stock market crash; large weakening of USD; trade retaliation by Mexico, China, and Canada; mounting trade and geopolitical tensions with China and Russia



Indirect «Surrounding Risks»

- **Risk materialization stems from a more hostile environment:** protracted Corona virus crisis; stalemate between White House and Congress regarding budgetary policy and National Security Strategy; ongoing saber-rattling with North Korea, Iran, and Pakistan; regional crisis in the Western Hemisphere and in the Middle East; protracted failed NAFTA renegotiations

Collateral «Soft Risks»

- **Risk materialization as byproduct of unfavorable interactions between power groups:** Impeachment of Donald Trump; global protectionism; geopolitical volatility; mounting wealth gap; pressure groups and hostile NGOs; lagged institutional reaction to covid-19 crisis

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TACKLING COUNTRY RISK

COUNTRY + RISK

- ▶ **Country** = sovereign entity, culture and values, geographical distance, national laws and regulations, socio-political parameters
- ▶ **Risk** = lack of perfect information in real time, spill-over effect, abrupt changes



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5 MAIN APPROACHES TO COUNTRY RISK ASSESSMENT

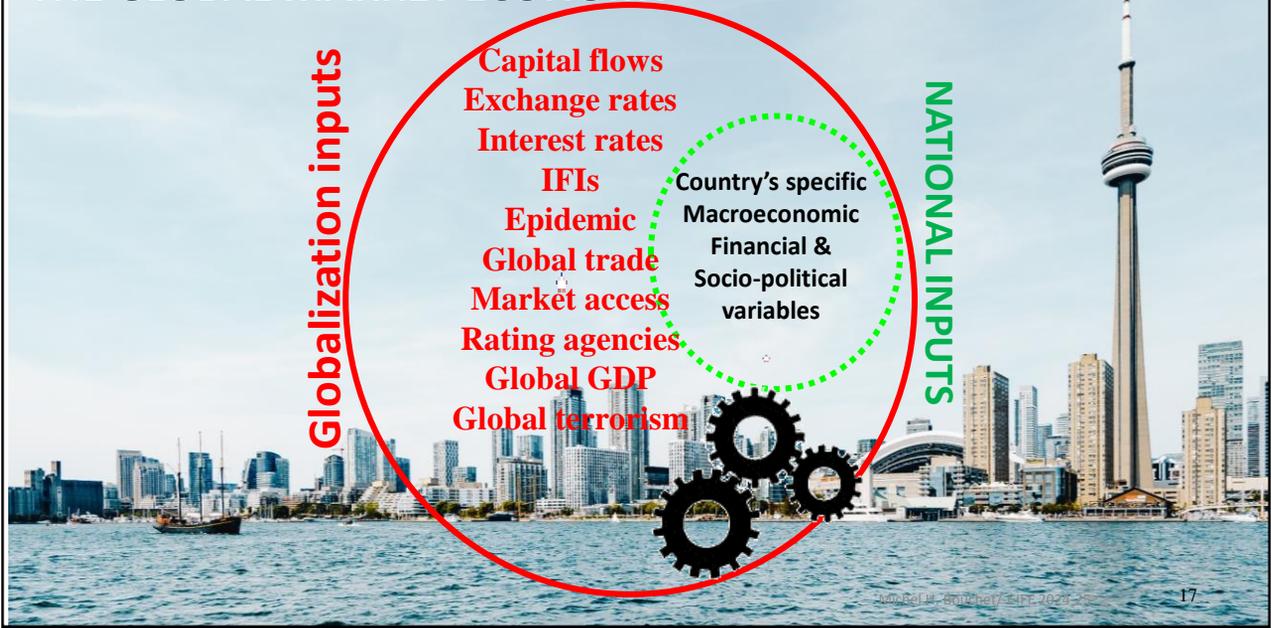
- 1. Qualitative « macro » approach:** financial, macroeconomic, legal, regulatory, environmental (incl. sanitary) and political parameters
- 2. Balance of payments and external debt analysis:** Liquidity + solvency
- 3. Quantitative approach :** rating, ranking, and scoring
- 4. Market signals:** inflation, exchange rates, yields, spreads, CDS, Vix
- 5. Econometric approach and modelization** (early warning signals, incl. Capital flight!)

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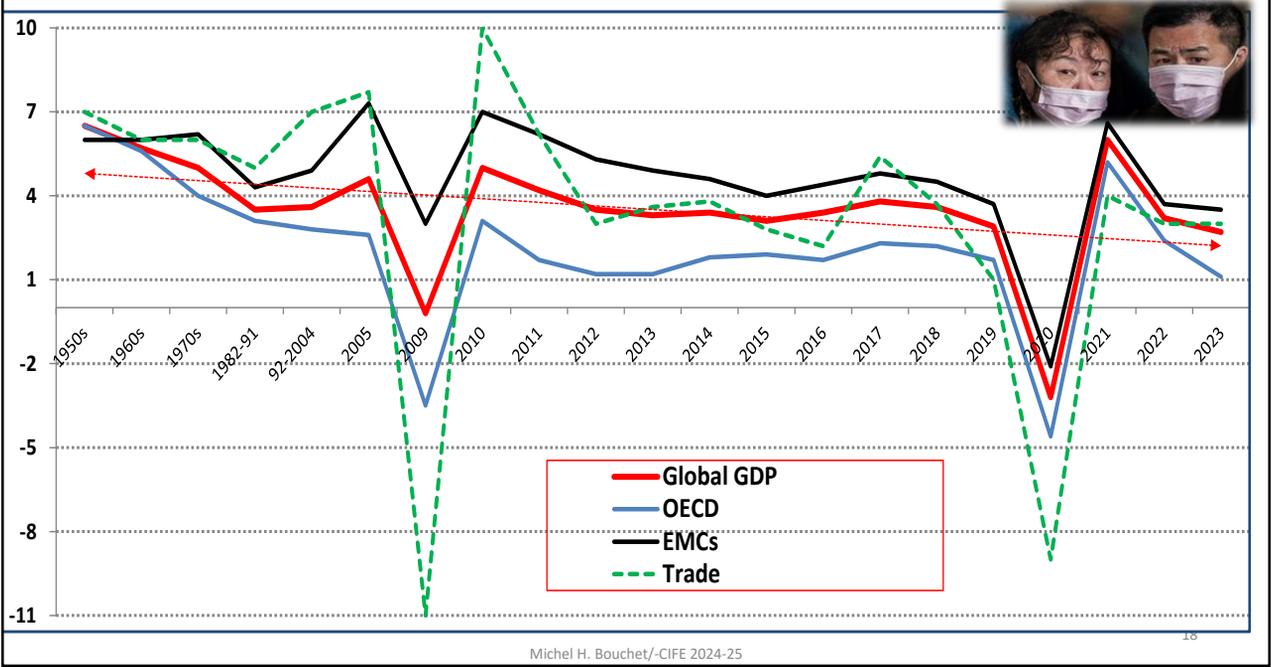
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INTERPLAY OF COUNTRY RISK WITH THE GLOBAL MARKET ECONOMY



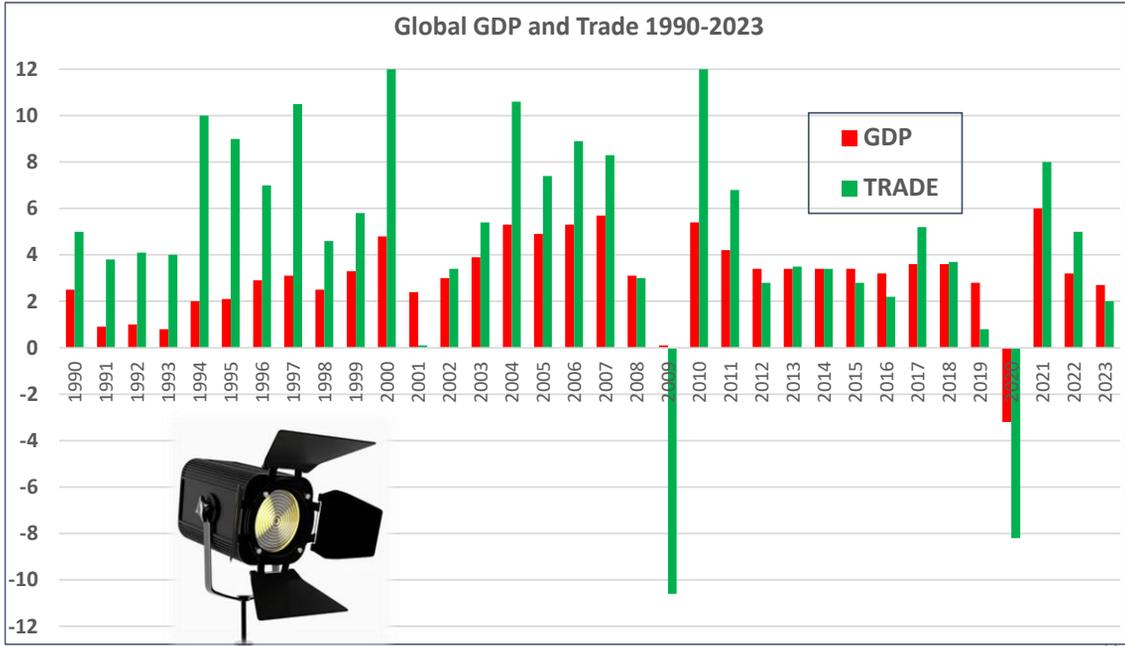
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1950-2023 Secular stagnation: A full decade of growth and trade slowdown



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PANDEMIC + GEOPOLITICAL CRISIS = GLOBAL MACROECONOMIC IMPACT



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THE THREAT OF GLOBAL SECULAR STAGNATION INCREASES COUNTRY RISK!

ECONOMIC FORECASTS

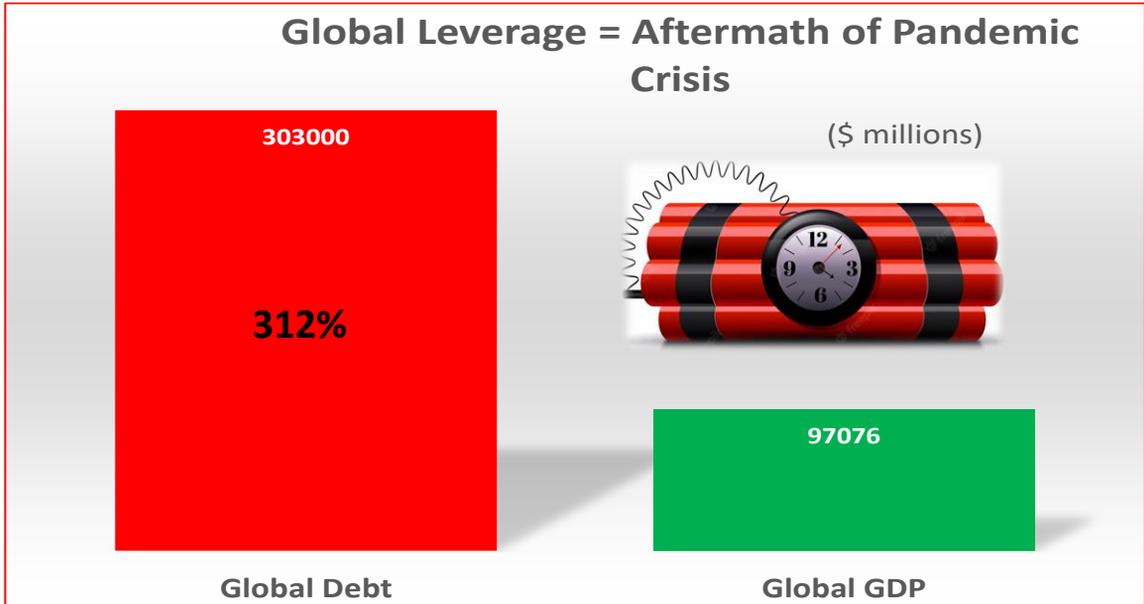
	GDP (yoy, %)			Consumer price (yoy, %)			Current account (% of GDP)		
	2022	2023	2024	2022	2023	2024	2022	2023	2024
United States	1.9	2.1	0.7	8.0	4.2	2.7	-3.8	-3.2	-3.0
Japan	1.0	2.0	1.2	1.1	3.9	1.9	1.7	2.0	1.3
Eurozone	3.4	0.5	0.9	8.4	5.6	3.0	1.2	2.1	1.9
Germany	1.9	-0.4	0.5	8.7	6.1	2.9	4.0	3.9	3.3
France	2.5	0.9	1.0	5.9	5.8	3.1	-2.0	-0.5	0.1
Italy	3.8	0.7	0.6	8.7	6.1	2.7	-1.3	1.1	2.3
Spain	5.5	2.2	1.7	8.3	3.6	3.5	0.5	2.0	1.2
Netherlands	4.4	0.4	0.7	11.6	4.3	3.4	9.2	6.3	5.2
Belgium	3.2	0.9	1.0	10.3	2.3	2.5	-3.6	-0.9	-0.5
Other advanced									
United Kingdom	4.3	0.4	0.7	9.1	7.4	3.1	-3.1	-3.9	-4.5
Canada	3.3	1.1	0.9	6.9	3.7	2.3	0.7	0.5	0.2
Australia	4.0	1.9	1.6	6.5	4.5	2.5	0.9	-0.2	-0.4
Switzerland	2.1	0.6	1.4	2.9	2.5	1.5	6.5	5.8	6.3
Sweden	2.9	-0.8	0.1	8.5	3.0	2.1	4.8	2.5	1.8
Norway	3.2	1.4	0.8	5.8	5.5	3.1	30.3	27.0	26.0
Asia	4.2	4.9	4.6	3.5	2.4	2.5	1.4	1.1	1.0
China	3.0	5.1	4.5	2.0	0.4	1.8	2.2	1.8	1.2
India	6.7	6.1	5.8	5.7	5.8	4.0	-2.6	-2.8	-2.5

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RISING GLOBAL DEBT THREAT

Global Leverage = Aftermath of Pandemic Crisis



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THREE-FOLD RISK SOURCES

Climate Change, the Great Displacer

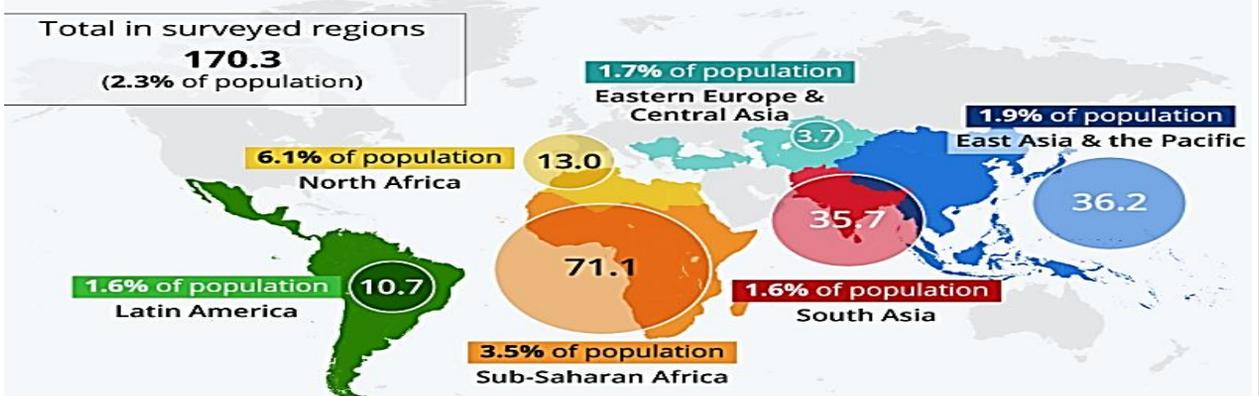
Average number of internal climate migrants by 2050 per region (in millions)*



Total in surveyed regions

170.3

(2.3% of population)



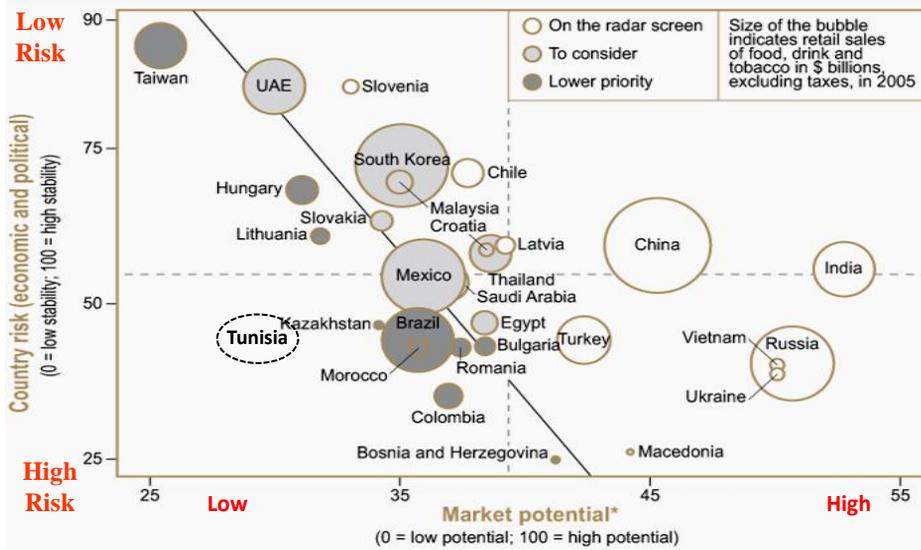
* Modeled on pessimistic reference = High emission & unequal development scenarios concerning water availability, crop productivity and sea-level rise

Source: World Bank

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MOST ATTRACTIVE EMERGING MARKETS?

= COMBINING RISK EXPOSURE + MARKET OPPORTUNITIES



* Based on weighted score of market attractiveness, market saturation and time pressure scores
Source: A.T. Kearney

AT KEARNEY FDI CONFIDENCE INDEX

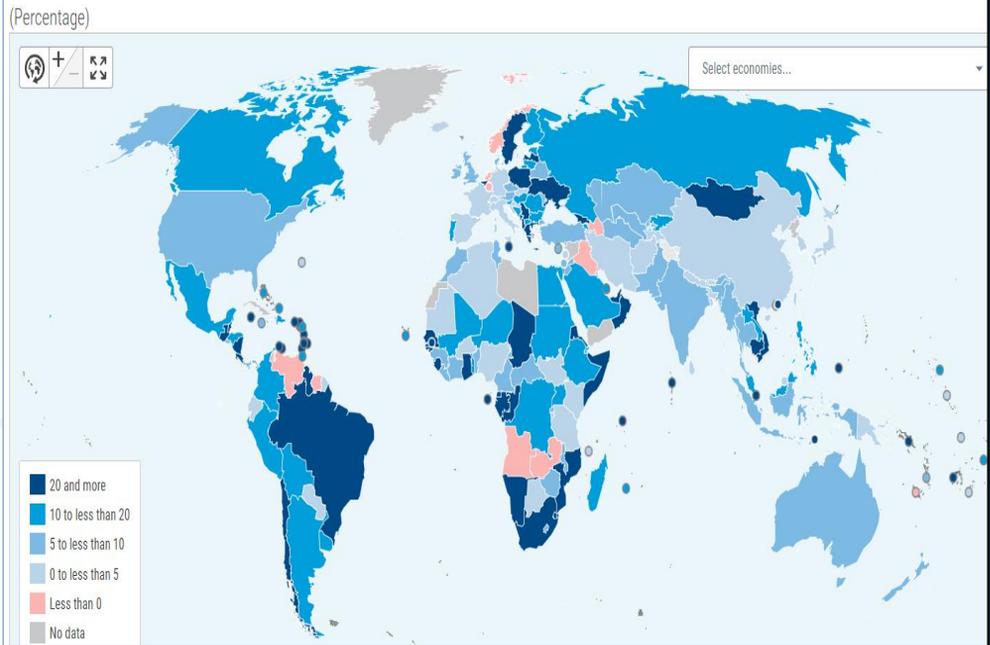
GOVERNANCE MATTERS!

Ranking			Score	
2017	2018	2019		
1	1	1	United States	2.10
2	3	2	Germany +	1.90
5	2	3	Canada -	1.87
4	4	4	United Kingdom	1.85
7	7	5	France +	1.79
6	6	6	Japan	1.78
3	5	7	China -	1.72
13	10	8	Italy +	1.67
9	8	9	Australia -	1.67
10	12	10	Singapore +	1.65
11	15	11	Spain +	1.62
14	13	12	Netherlands +	1.61
12	9	13	Switzerland -	1.59
-	20	14	Denmark +	1.58
15	14	15	Sweden -	1.55
8	11	16	India -	1.54
18	18	17	South Korea +	1.54
22	21	18	Belgium +	1.54
23	16	19	New Zealand -	1.52
20	19	20	Ireland -	1.52
24	24	21	Austria +	1.50
-	-	22	Taiwan (China) +	1.50
-	-	23	Finland +	1.50
-	23	24	Norway -	1.49
17	17	25	Mexico -	1.49

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**UNCTAD
TRADE AND
FDI FLOWS &
STOCKS**

Map 1. Foreign direct investment inflows as a ratio to gross fixed capital formation, 2021



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Table 1. Foreign direct investment flows by group of economies

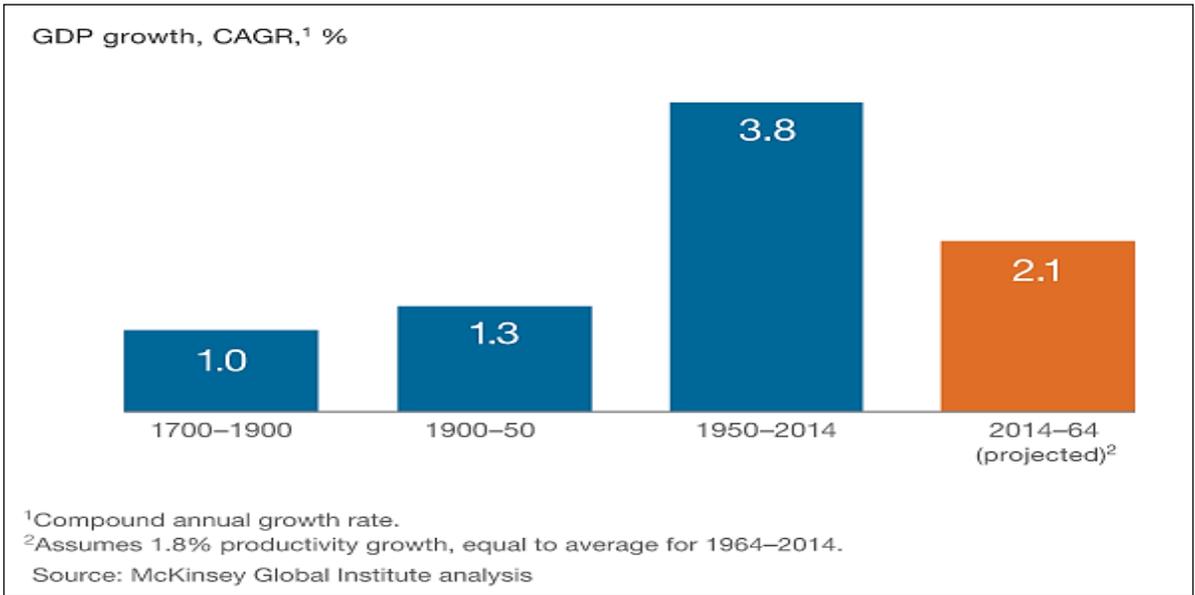
Group of economies	Inflows				Outflows			
	Value (Billions of US\$)		Annual growth rate (Percentage)		Value (Billions of US\$)		Annual growth rate (Percentage)	
	2020	2021	2020	2021	2020	2021	2020	2021
World^a	963	1 582	-35.0	64.3	780	1 708	-30.6	118.8
Developed economies	319	746	-58.2	133.6	408	1 269	-44.6	210.9
Developing economies	644	837	-10.1	29.9	372	438	-3.8	17.8
Developing economies: Africa	39	83	-14.7	113.1	-1	3	-112.7	-526.2
Developing economies: Americas	86	134	-45.7	56.0	-5	42	-110.0	-995.6
Developing economies: Asia and Oceania	519	619	1.4	19.3	378	394	12.6	4.3
Selected groups								
Developing economies excluding China	495	656	-14.0	32.6	219	293	-12.6	34.1
Developing economies excluding LDCs	621	811	-10.4	30.5	371	439	-4.5	18.3
LDCs	23	26	0.6	13.1	2	0	-250.1	-109.4
LLDCs	14	18	-35.9	30.7	-1	2	-271.4	-231.6
SIDS (UN-OHRLLS)	82	107	-28.9	30.5	31	48	-42.7	51.3
HIPCs (IMF)	24	32	-12.1	33.6	1	2	-44.0	65.3
BRICS	255	355	-13.3	39.2	157	247	-19.3	57.9
G20	757	1 104	-34.7	45.9	596	1 496	-38.8	150.9

Table 2. Foreign direct investment stock by group of economies

Group of economies	Inward stock				Outward stock			
	Value (Billions of US\$)		Share in world total (Percentage)		Value (Billions of US\$)		Share in world total (Percentage)	
	2020	2021	2020	2021	2020	2021	2020	2021
World^a	41 728	45 449	100.0	100.0	39 546	41 798	100.0	100.0
Developed economies	29 967	33 119	71.8	72.9	31 113	33 009	78.7	79.0
Developing economies	11 760	12 330	28.2	27.1	8 433	8 790	21.3	21.0
Developing economies: Africa	958	1 026	2.3	2.3	331	301	0.8	0.7
Developing economies: Americas	2 070	2 143	5.0	4.7	708	741	1.8	1.8
Developing economies: Asia and Oceania	8 732	9 160	20.9	20.2	7 394	7 747	18.7	18.5
Selected groups								
Developing economies excluding China	9 841	10 266	23.6	22.6	5 852	6 208	14.8	14.9
Developing economies excluding LDCs	11 367	11 915	27.2	26.2	8 410	8 767	21.3	21.0
LDCs	393	414	0.9	0.9	23	22	0.1	0.1
LLDCs	421	431	1.0	0.9	51	52	0.1	0.1
SIDS (UN-OHRLLS)	2 120	2 182	5.1	4.8	1 292	1 373	3.3	3.3
HIPCs (IMF)	379	403	0.9	0.9	25	26	0.1	0.1
BRICS	3 577	3 866	8.6	8.5	3 681	3 704	9.3	8.9
G20	32 394	35 256	77.6	78.7	32 883	34 919	83.2	83.5

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PROSPECTS: ECONOMIC SLOWING DOWN IN THE NEXT 50 YEARS

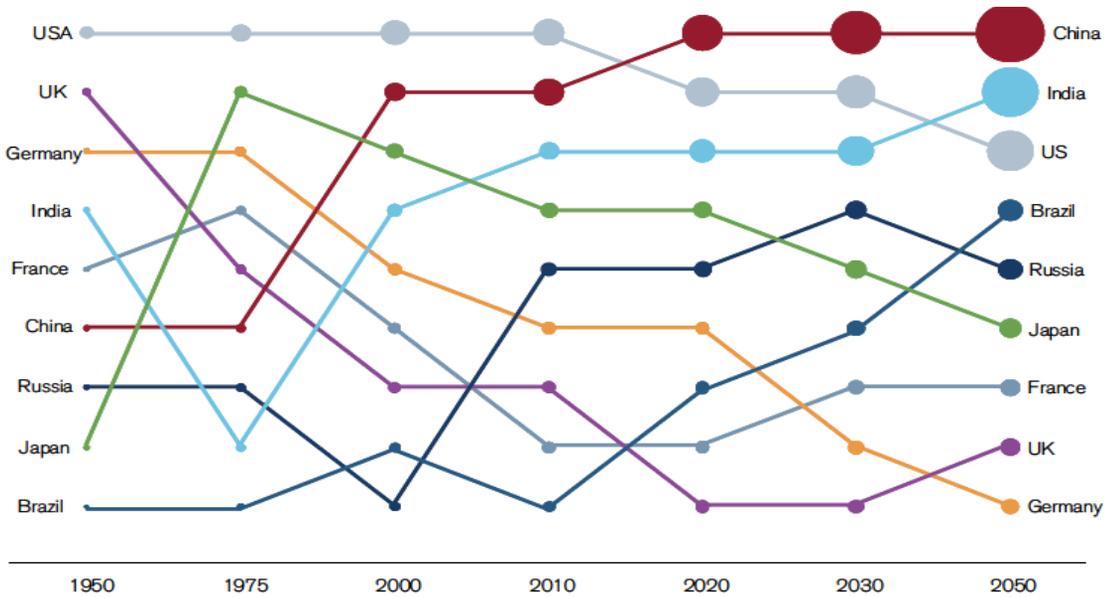


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THE TOP GLOBAL GDP 1950-2050?

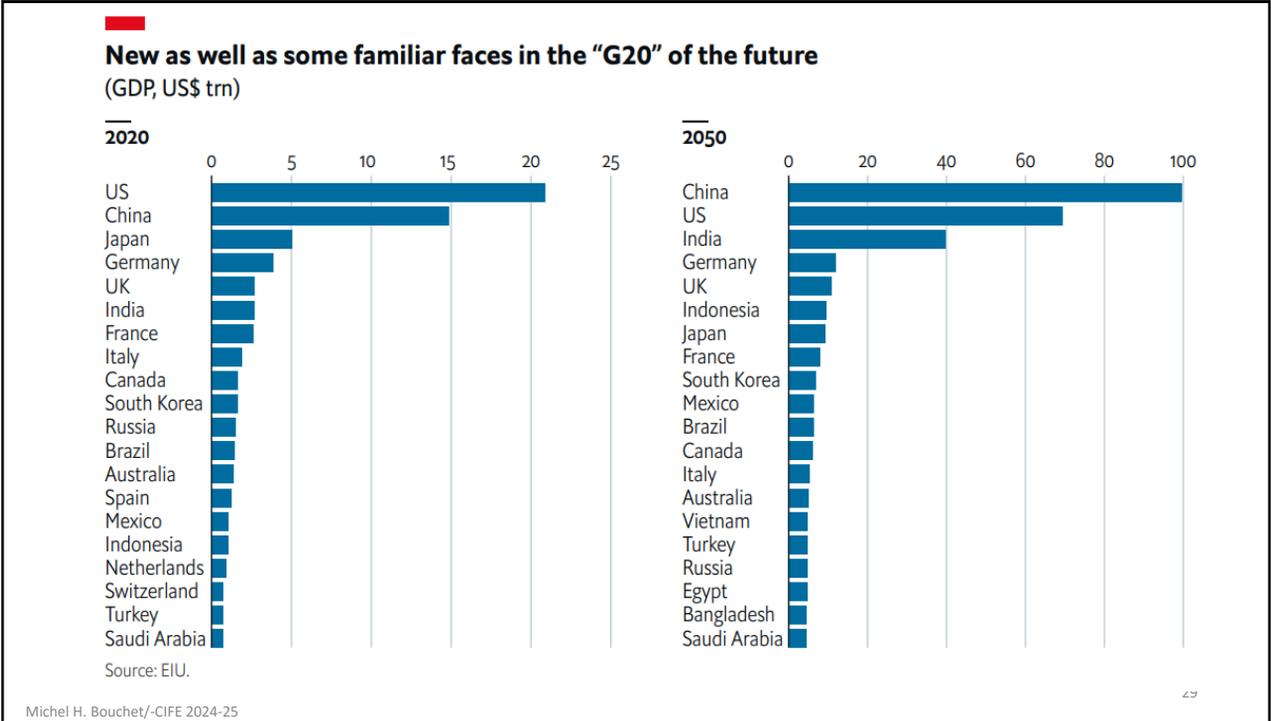


World Bank, PWCs, Credit Suisse

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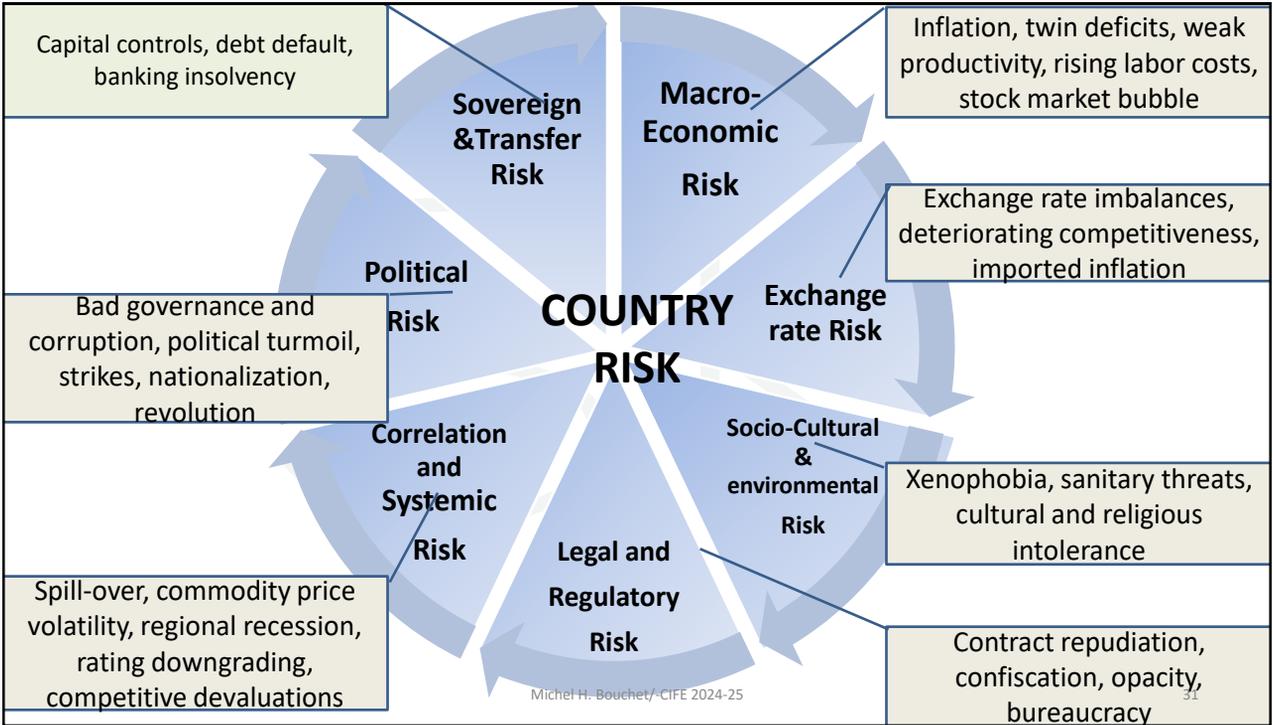


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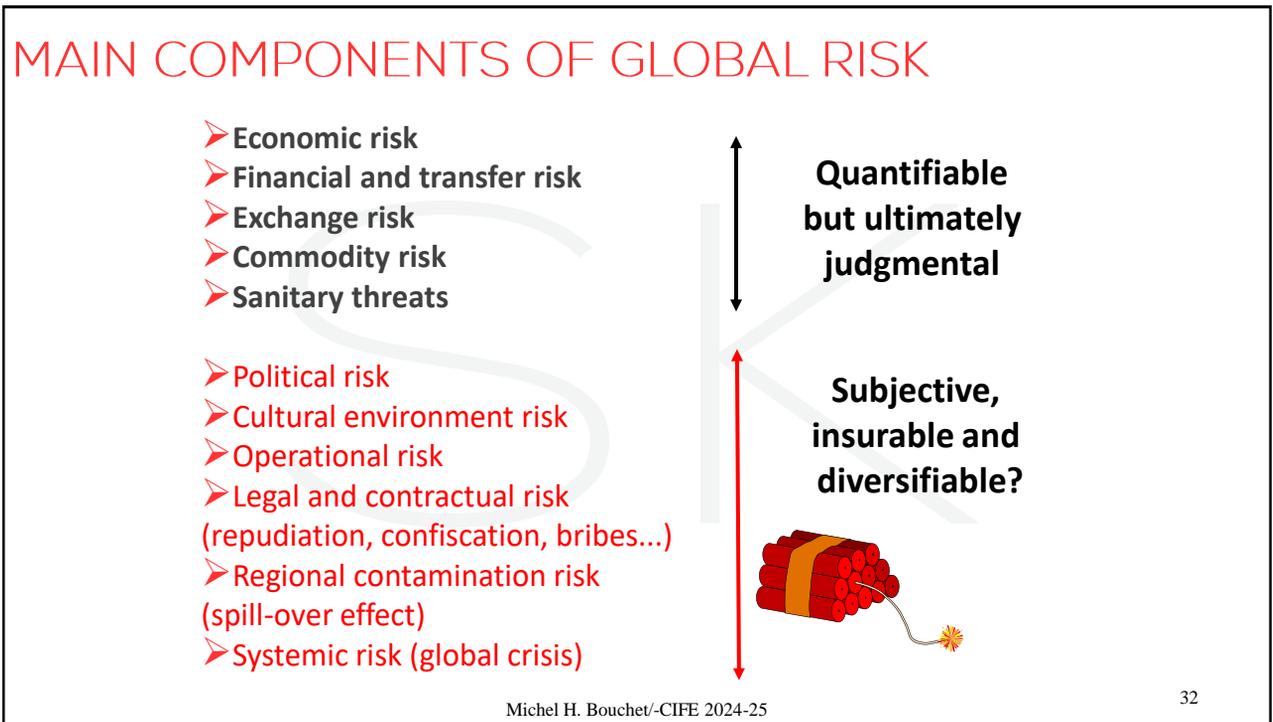
THE KEY COMPONENTS OF COUNTRY RISK?

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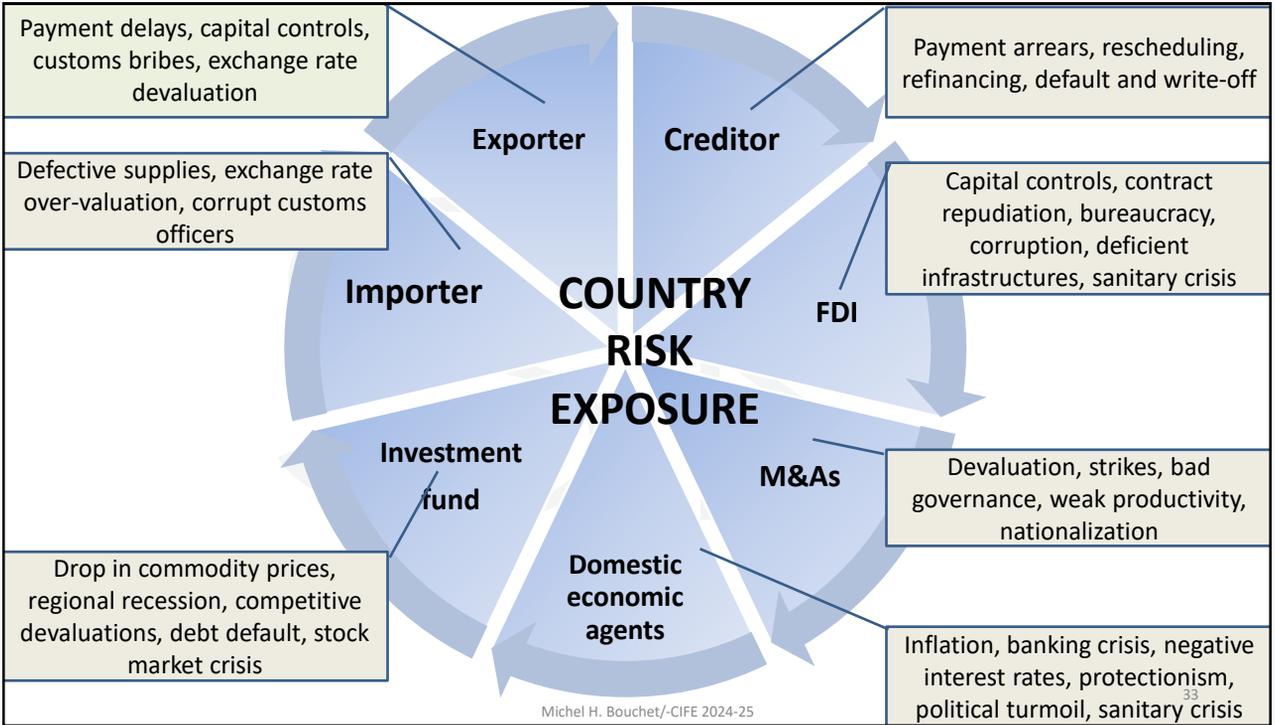


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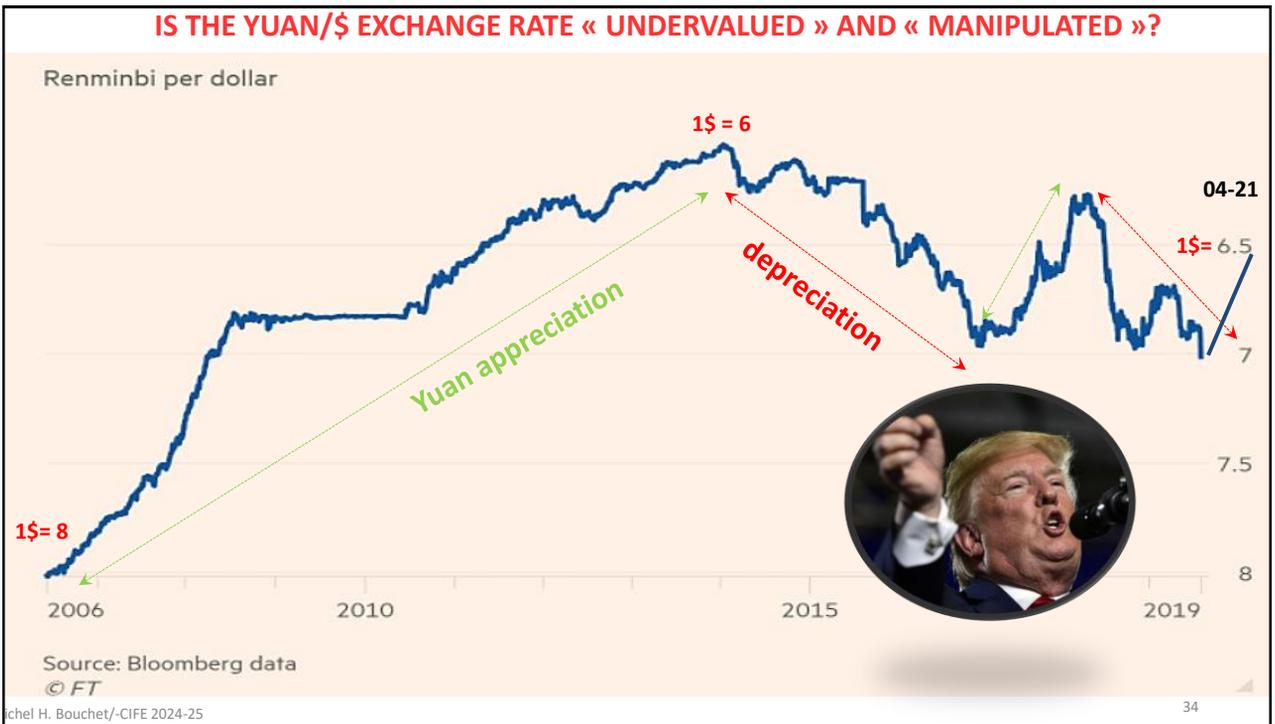


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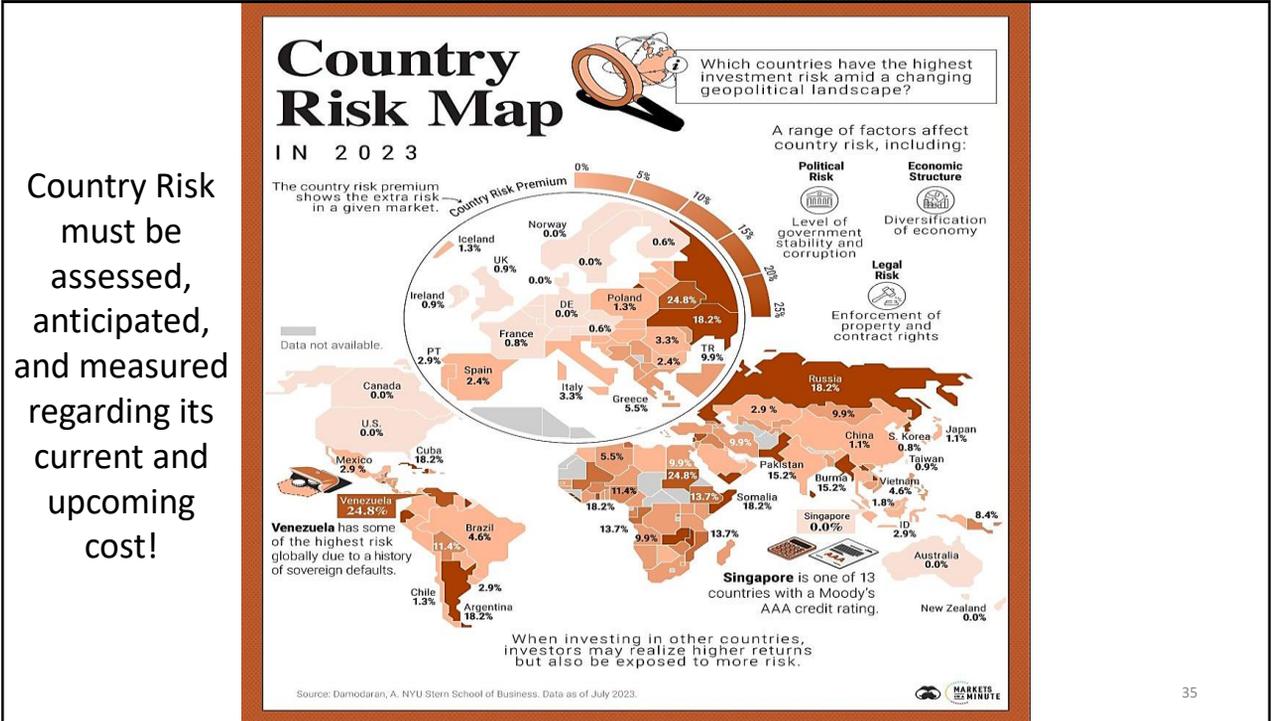
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Country Risk must be assessed, anticipated, and measured regarding its current and upcoming cost!



BETTER OFF IN TUNISIA, JORDAN OR BOLIVIA?



TUNISIA

- ▶ GDP Per capita = \$3700
- ▶ HDI= **101**
- ▶ Life expectancy f = 78
- ▶ CA/GDP%= - 8,5%
- ▶ Trade openness: 111%
- ▶ Doing Business= **78**
- ▶ Corruption = 87
- ▶ Shadow economy: **31%**
- ▶ Coface = **D/B**



JORDAN

- ▶ GDP Per capita = \$4600
- ▶ HDI= 99
- ▶ Life expectancy f = 75
- ▶ CA/GDP%= - 4%
- ▶ Trade openness = 80%
- ▶ Doing Business= **75**
- ▶ Corruption = 63
- ▶ Shadow eco. = 15%
- ▶ Coface = **C/B**



BOLIVIA

- ▶ GDP per capita = \$3800
- ▶ HDI = **120**
- ▶ Life expectancy= 71
- ▶ CA/GDP% = -1,5%
- ▶ Trade openness= 60%
- ▶ Doing Business = **150/190**
- ▶ CPI corruption= 133
- ▶ FDI = **minimal**
- ▶ Shadow ec. = **46%**
- ▶ Coface = C/B

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THE PRICE OF COUNTRY RISK = 5 YEAR CDS TUNISIA VS MOROCCO



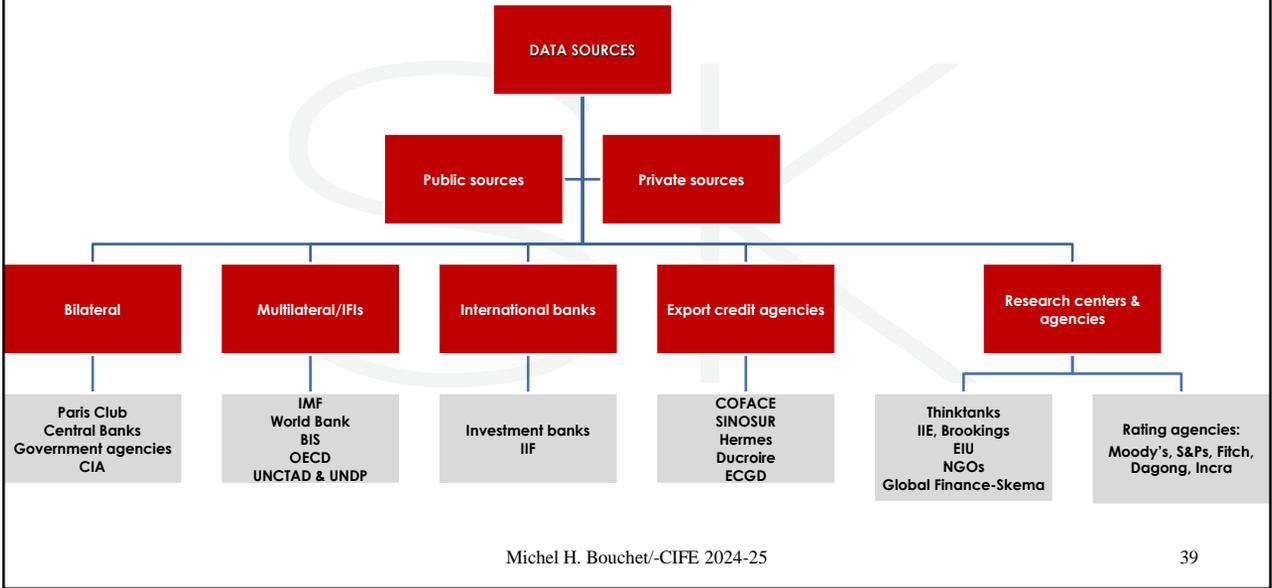
1000 5/01 17:44 NEWS ALERT/New York Governor Cuomo Holds Coronavirus Briefing:

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MAJOR SOURCES OF COUNTRY RISK INTELLIGENCE



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ANALYSIS AND INFORMATION SOURCES

IMF, World Bank, IFC & MIGA
UNCTAD & UNDP
Fed Reserve Bk of St Louis
BIS, OECD, EBRD, EIB
Coface, SACE, Euler-Hermes
Moody's, S&P, Fitch, Dagong
Euromoney, Institutional Investor
CIA & US State Dept, ICRG
Transparency International
Hiscox, AON, Control Group
DEFI www.developingfinance.org

DEFI DEVELOPING FINANCE
 OXFORD ECONOMICS
 AON Empower Results®
 EULER HERMES Our knowledge serving your success
 coface FOR SAFER TRADE
 INTERNATIONAL MONETARY FUND
 THE WORLD BANK BRD • ICA
 Country and Political Risk 2nd Edition EDITED BY SAM VEDON
 La globalisation Introduction à l'économie du nouveau monde Michel-Henry Bouchet
 Country risk assessment A Guide to Global Investment Strategy MICHEL HENRY BOUCHET EPHRAÏM CLARK BERTRAND GROS Lambert
 MANAGING COUNTRY RISK IN AN AGE OF GLOBALIZATION A PRACTICAL GUIDE TO OVERCOMING CHALLENGES IN A COMPLEX WORLD
 CONTROL RISKS

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A QUICK AND RELIABLE ACCESS TO COUNTRY RISK INTELLIGENCE? COFACE!

Short case study:
Compare the ratings and debt ratios of ... Italy, Germany, and Greece as well as socio-political prospects

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RATINGS AND DEBT RATIOS OF ... ITALY, GERMANY, AND GREECE AS WELL AS ECONOMIC AND SOCIO-POLITICAL PROSPECTS

COUNTRY	DEBT/GDP	RATING COFACE	Economic & Socio-Political
GERMANY	69%	A3/A1	Decline in the working population from 2020 onwards, despite immigration! Prominence of the automotive and mechanical industries, particularly in exports Capacity constraints, insufficient investment
ITALY	125%	B/A2+	Very high youth unemployment, hence brain drain Prevalence of small, low-productivity companies Strong exposure to pandemic-sensitive sectors Strong regional disparities
GREECE	192%	B/A2	Poorly diversified industry, overwhelming tourism dependence, Increasing security concerns vis-à-vis Turkey, low productivity L/Y

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