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How to manage political risk?



What is the difference between managing market risk and political risk?

Standard approach to market and credit risks:

- ❑ Measure
 - ...by volatility, beta, VaR, etc.
- ❑ Mitigate to the acceptable level
 - E.g. by hedging via derivatives

How to deal with political risk, which is hard to quantify?

- ❑ Ignore?
 - Focus on measurable risks
- ❑ Measure?
 - ...and aggregate together with market and credit risk
- ❑ Use special tools for framing and evaluating!
 - E.g., provide top management with alternative future scenarios

What is political risk?

- ❑ Risk of losses due to the exercise of power by the government and related groups
- ❑ Government action... or inaction
 - E.g. failure to issue the license
- ❑ Country-wide vs. firm-specific
 - Raising taxes
 - Company's expropriation / selective enforcement
- ❑ Political instability / war
 - Change of power at elections

What are the top political risks for investors in emerging markets?

THE TOP EMERGING-MARKET HAZARDS

THE MOST COMMONLY CITED POLITICAL RISKS IN DEVELOPING COUNTRIES OVER THE NEXT THREE YEARS



Source: Multilateral Investment Guarantee Agency survey of investors, 2010

How can foreign investors evaluate and manage political risk?

□ How to evaluate?

- Country ratings
 - E.g. Transparency Intl Corruption Index
- Experts / consultants
- News smart search
- Scenarios / stress tests
- War room: analyzing incentives and responses of political actors

□ How to manage?

- Legal contracts?
- Insurance?
- Financial instruments?

□ New tools

- Maintaining goodwill
- Framing investment
 - ...as fair, equitable,...
- Finding political pressure points

How can Russian companies deal with the risk of (new) sanctions?

What sanctions?

How to manage?

Thanks for your attention!

