

**CERAM Sophia Antipolis**

European School of Management

**Academic Year 2005/2006**

**Semester 2**

# **MScIF Programme**

**Contry Risk Assessment**

**COURSE CODE**

**3 credits**

**Course Leader : Michel Henry BOUCHET**

# *Syllabus*

**Professor:**

*Dr. Michel Henry Bouchet<sup>1</sup> Office #265*

<http://globalfinance.org>

e-mail : [michel.bouchet@ceram.fr](mailto:michel.bouchet@ceram.fr)

... ☎ 0493954481

Faculty coordinator:

Mrs. Sandrine Charron, office 271- ☎ 4419

## **1. Course Objectives**

### **1.1 - General Objectives :**

Country risk is a broad concept that comprises an underlying combination of economics, finance, geopolitics, sociology, and history issues. As the new global economy raises the level of uncertainty and complexity for the international firm's cross-border strategy, country risk analysis has become today an essential component of strategy decisions regarding export, investment, partnership, mergers, as well as takeovers. Since 09/11, global terrorism shows there is no safe sanctuary, even in the world's largest economy. The course aims at providing students with a solid understanding of the concepts, historical perspectives, theoretical debates and methodologies surrounding country risk assessment in the global economic system. Risk analysis and forecasting will be approached as management tools. The course is composed of lectures, case studies, briefings by group mates, and debates.

At the end of the three-month course, the students will be expected to gauge the risks and opportunities of financial globalization regarding emerging markets.

### **1.2. Specific Goals**

Understanding the multi-faceted dimensions of cross-border risk

Assessing the main sources of risks and opportunities arising from the growing integration of international financial markets from the firm's standpoint;

Apprehending the range of risk-analysis methodologies, and their respective pros and cons

Understanding the various approaches to country risk hedging, starting with up to date reliable information and intelligence.

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<sup>1</sup> Dr. Michel Henry Bouchet is Professor of Finance at CERAM; Scientific Director of the MS in International Finance and coordinator of the Chair "Global Finance"; Consultant World Bank; He is also Senior Partner of Finconet.

### 1.3. Student's responsibilities

Students who join the course will be expected to read the prescribed references and all other recommended material, to make oral presentations on current international finance and emerging market risk topics, to follow closely the financial press on a weekly basis, to be involved in work group situations, and to be active participants in the debates and discussions in class (mobile phones off during the class!)

## 2. Course Organization

The course is composed of twelve sessions of three hours. Lectures, exercises, case studies. Each class will start with a press review where students will be expected to summarize and discuss the salient features of the week regarding country risk issues (not the 8 o'clock news!) Students are expected to be active participants.

PowerPoint-assisted lectures will be accompanied by documents to shed light on the various topics of the course. Power Point slides will be available on the web site of the Glob@l Finance Chair. <http://globalfinance.org> as well as on Webintec.

## 3. Assessment

### 3.1 Course assessment :

A final single letter grade will take into account both continuous assessment and the final assignment.

Class Participation, weekly reviews and oral presentations 25%

Quiz and Mid-term 35%

Final Project 40%

### 3.2 Grading system :

Course passed (credits earned)

A : Excellent

B : Very Good

C : Good

D : Satisfactory

E : Sufficient

Course failed (no credits)

Fx : Marginal Fail (Resit exam authorized)

F : Bad Fail (Course to be followed again)

## 4. Course Books

### 4.1 – Reference course book :

Bouchet M., Gros Lambert, B. and Clark, E. “Country Risk Assessment”, Wiley, 2003.  
Bouchet M., Gros Lambert, B, “Governance & Risk in Emerging Markets”, edited by Sima Motamen-Samadian, Palgrave, London: 2005.

### 4.2 – Selection of recommended books, articles or web-sites :

Peter L. Bernstein, “Against the Gods”, Wiley, 1998.

Bouchet Michel Henry, “The Political Economy of International Debt”, QUORUM/Praeger

Bouchet Michel Henry, “La Deuda de la Naciones: Que, Quien, Como, Cuanto y Por Que?”, FELABAN, Colombia.

Kindleberger, 1985, "Historical Perspective on Today's Third World Debt Problem", Cahiers de l'ISMEA, série MO n°5, tome XIX, n°9, Presses Universitaires de Grenoble, septembre, pp.109-134.

Krugman, 1994, The Myth of Asia's Miracle, Foreign Affairs, Nov.

John Kenneth Galbraith, 1994, A Short History of Financial Euphoria

### 4.3 – Additional useful Readings: (cont)

International Monetary Fund, Annual Report 2005, Part I: The Global Economy

World Bank, « Global Development Finance », Part 1, Volume I, 2005

World Bank; World Development Report 2005

Euromoney (monthly) & Institutional Investor (monthly)

Financial Times, Les Echos (daily)

Web sites : World Bank, IMF, BIS, OECD, CIA, Coface, S&P, Moody's, Fitch IBCA

## 6. Detailed Course Plan

### CLASS 1

#### Introduction: Course presentation

**Definition, Presentation: The various types of cross-border risk**

**Information sources**

**Illustration: Risk analysis of Peru**

## CLASS 2

### The history of risk analysis and risk management

#### The process of economic development: an historical perspective:

Peter Bernstein, K. Marx, the Dependency School, W. Rostow, The Liberal School, Joe Stiglitz, Paul Krugman, Jeff Sachs ...  
Bolivia Case

## CLASS 3

### IMF & World Bank: The role of International financial organizations as

1. providers of economic intelligence and information for country risk analysis
  2. providers of monitoring and surveillance
  3. providers of investment insurance and cofinancing
  4. providers of structural adjustment financial support
  5. providers of external debt relief
- The IMF's approach to the balance of payments adjustment

## CLASS 4

### Country Risk assessment: Information and intelligence gathering

1. Public information sources:
  - IFIs & Regional development banks
  - National sources and central banks
2. Private sources:
  - Risk rating agencies (Coface & others)
  - Private commercial and investment banks
  - Specialized agencies and think tanks

## CLASS 5

### Country Risk : Assessment Methodologies I

#### Political risk analysis: analysis of structural and institutional deficiencies

##### The Prince Model

##### The rating approach to political risk

Frost & Sullivan, EIU, CIA, Credit Risk International, Transparency International, Heritage Foundation...

## CLASS 6

### Country Risk : Assessment Methodologies II

- Balance of payments approach and country risk assessment
  - Solvency and liquidity ratios
  - Case study: Solvencia

## CLASS 7:

Mid-Term examination

**CLASS 8**

**Country Risk : Assessment Methodologies III**

The rating approach : usefulness and pitfalls  
Moody's, S&Ps, Euromoney, Institutional Investor, Transparency International, BERI...

**CLASS 9**

**Country Risk : Assessment Methodologies IV**

The Asian crisis and the regional contamination risk  
Country Risk case study

**CLASS 10**

**Country Risk : Assessment Methodologies V**

- "threshold" breaking points
- Principal component analysis (CDC)

**CLASS 11**

**Debt crisis and Investment opportunities**

- Origins and recent developments of the secondary markets in bank claims
- Price and discount determination, trading techniques, volume, liquidity and volatility
- A new vehicle for investment and hedge funds
- Debt conversion transactions

Preparation: World Bank-Annual Report, EMTA

**CLASS 12**

**Conclusion: Final Presentation of the Group Projects**

## **Main Sources of Country Risk Intelligence**

[www.grai.com](http://www.grai.com) (Global Risk Assessment, Inc. - Country Risk Services )  
Political and Economic Risk Consultancy, Ltd.- PERC Gateway to news & country data  
BERI (Business Environment Risk Index)  
Credit Risk International  
Frost & Sullivan  
Institute for International Economics (Washington)  
Institute of International Finance Inc. (Washington, D.C.)  
The Economist Intelligence Unit (London)  
The Davos World Economic Forum  
The Harvard Institute for International Development (Boston)  
Morgan Stanley Capital International Data  
International Finance Corporation Data (World Bank: source for emerging markets data)  
COFACE  
Bradynet Info and data on emerging fixed income markets.  
Political Risk Services (country risk indices).  
Euromoney Magazine (Country risk indices).  
Institutional Investor Magazine  
Global Finance Magazine  
International Finance Review (London): secondary market prices & bond issues  
Oxford Analytica Inc. On-line daily analysis and custom country risk services.  
Transparency International (corruption & governance)  
Rabid Tiger Project Jeff Deutsch's Political Risk Consulting and Related Research  
Dr. Nouriel Roubini's web site (NYU)  
Dr. Harvey Campbell 's site (Duke University)  
[www.imf.org](http://www.imf.org)  
[www.worldbank.org](http://www.worldbank.org)  
[www.cia.us](http://www.cia.us)  
[www.ifc.org](http://www.ifc.org)  
<http://www.iadb.org/>  
(Handbook of Economic Statistics. Washington, DC: Central Intelligence Agency)  
For macroeconomic data:  
IFC Emerging Stock Market Factbook 1999 (available at the library)  
Web sites of central banks (<http://www.zagury.com/cbanks.htm>)  
[www.bis.org](http://www.bis.org)  
<http://www.ntu.edu.sg/library/statdata.htm>

## **Standard Country Risk Assessment Fact Sheet**

(prescribed format for country risk assessment work)

### **1. Introduction: Map and graphs**

(History, political system, ethnical features, culture and religion)

### **2. Survey of geographical features, raw material, human and natural resources**

[www.UNCTAD.org](http://www.UNCTAD.org)

UNDP [www.undp.org](http://www.undp.org)

World Bank [www.worldbank.org](http://www.worldbank.org)

### **3. Macro-economic analysis**

Sector analysis, adjustment, trade strengths and weaknesses (partner/product composition),

Inflation, savings/investment ratios

GDP growth..., relative importance of underground economy...

IMF/WB/regional development banks: IADB/AfDB:AsDB/EBRD

<http://www.ntu.edu.sg/library/statdata.htm>

### **4. Balance of payments analysis**

Trade balance, current account, reserves, E&O

[www.IMF.org](http://www.IMF.org)

IMF:IFS

### **5. Debt Flows & Stock Analysis**

Liquidity and solvency indicators

World Bank/OECD/BIS/IMF

[www.bis.org](http://www.bis.org)

Secondary market discounts: Bradynet, EMTA/IFR

### **6. Legal and regulatory framework conducive to private investment**

### **7. Ratings**

[www.Euromoney.com](http://www.Euromoney.com)

[www.fitchibca.com](http://www.fitchibca.com)

[www.moodys.com](http://www.moodys.com)

[www.standardandpoors.com/ratings](http://www.standardandpoors.com/ratings)

Institutional Investor

Transparency International

UNDP/HDI Index

### **8. CONCLUSION: risk and opportunity assessment**

## **TERMINOLOGY AND DATA SOURCES**

**Population:** A midyear estimate of the total number of people living in the country (World Bank: The Little Data Book-1999, IMF: International Financial Statistics, World Factbook, World Almanac).

**Area:** The total area of the country in square kilometers (World Bank: The Little Data Book-1999, World Almanac).

**Constitution:** The date of promulgation of the country's current constitution (World Almanac, World Factbook, Background Notes).

**Legislature:** The types of national legislative bodies and the distribution of seats among the major political parties (\*foreign embassies, data files, World Factbook). **Elections:** The election schedule and terms of office, as well as the date of the last and next scheduled elections for national offices (\*foreign embassies, data files).

**Currency Exchange System:** A description of the exchange characteristics of the currency (\*International Financial Statistics, data files).

**Exchange Rate:** The value of the currency in relation to the US dollar on the most recent date available. The dollar is reported in relation to the deutsche mark (\*International Financial Statistics, data files).

**Social Indicators :** (World Bank: The Little Data Book-1999, UNDP, UNCTAD)

**Energy, Per Capita Consumption:** The amount of energy consumed per person in kg. oil equivalent (World Development Report).

**Annual Population Growth Rate:** The average annual percentage change in the population over the last five years (\*International Financial Statistics, World Development Report).

**Infant Deaths per 1,000:** The number of deaths of children under one year of age per 1,000 live births in a calendar year (UNDP Human Development Index, CIA, World Development Report).

**Urban Population:** The percentage of the population living in urban areas (World Bank: World Development Report, World Almanac, CIA, World Factbook).

**Urban Growth:** The average annual percentage change in the urban population of the country (World Development Report, World Factbook).

**Literacy:** The percentage of persons age 15 and over who can read and write (UNDP, World Bank: World Development Report, World Almanac).

**Ethnic Groups:** Groups with which significant percentages of the population identify themselves (\*World Almanac, World Factbook, Background Notes).

**Religions:** The religious preferences of significant percentages of the population (World Almanac, Background Notes, World Factbook).

**Gross Domestic Product (GDP):** The nominal value of the total final output of goods and services the country's economy produced in a year, regardless of its allocation to domestic or foreign factors (IMF: International Financial Statistics, Trends in Developing Economies; OECD; World Bank: The Little Data Book- 1999).

**Per Capita GDP:** The ratio of GDP to population (World Bank: The Little Data Book- 1999; IMF: International Financial Statistics, Trends in Developing Economies, OECD Economic Surveys, data files).

**Real Growth Rate:** The annual percentage change in real GDP, adjusted by the inflation rate (World Bank: The Little Data Book- 1999; IMF: International Financial Statistics, Trends in Developing Economies, OECD Economic Surveys, data files).

**Inflation:** The annual percentage change in a consumer price index (IMF: International Financial Statistics, Trends in Developing Economies, OECD Economic Surveys, data files).

**Capital Investment:** The value of gross fixed capital formation (International Financial Statistics).

**Budget Revenues:** All nonrepayable and nonrepaying government receipts plus grants received from other governments - domestic or foreign, and international institutions (International Financial Statistics, Trends in Developing Economies, data files).

**Budget Expenditures:** All nonrepayable and nonrepaying payments by governments, plus government acquisition of claims on others (loans and equities) minus repayments of lending and sales of equities previously purchased (International Financial Statistics, Trends in Financial Statistics, Trends in Developing Economies, data files).

**Budget Balance:** The difference between (a) revenue and applicable grants received and (b) expenditure and lending, minus repayments (includes foreign lending) (International Financial Statistics, Trends in Developing Economies, data files).

**Money Supply (M1):** Total stock of money in the economy. Components of M1 include currency in circulation, commercial bank deposits, NOW accounts, credit union share drafts, mutual savings bank demand deposits, and non-bank travelers checks (International Financial Statistics).

**Change in Real Wages:** The annual percentage change in real (inflation-adjusted) wages (\*International Financial Statistics, Foreign Labor Trends).

**Foreign Direct Investment:** Investment by foreign citizens in domestic business; usually involves majority stock ownership of the enterprise (IMF: International Financial Statistics).

**Foreign Exchange Reserves:** Foreign currency (excluding gold) held by a central bank for purposes of exchange intervention settlement of intergovernmental claims (International Financial Statistics).

**Total Foreign Debt:** Gross indebtedness by private and public sector domestic borrowers to foreign entities (World Bank: World Debt tables; BIS/OECD).

**Long-Term external debt:** debt with an original maturity of more than one year and owed to nonresidents and repayable in foreign currency. (World Bank: World Debt Tables)

Disbursements: Drawings on loan commitments during the year specified. (World Bank)

Net Resource flows: sum of net debt flows plus non-debt creating flows (foreign direct investment).:World Bank

Net flows: Disbursements minus principal repayments. (World Bank)

Net Transfers: Net Flows minus interest payments (World Bank)

Debt Service: On-going payments of interest and principal on total borrowings which must be made on time by the borrower as and when they come due. (World Debt tables)

Debt Service Ratio (as a percentage of exports): The sum of interest and principal repayments on external public and publicly guaranteed debt as a percentage of exports of goods and services (Trends in Developing Economies, International Country Risk Guide).

Current Account: The balance of payments on goods and services and all transfer payments: the difference between (a) exports of goods and services, plus inflows of unrequited official and private transfers, and (b) imports of goods and services, plus unrequited transfers to the rest of the world (\*International Financial Statistics, Trends in Developing Economies, OECD Economic Surveys, data files).

Exports: The value of merchandise exports, measured free-on-board (f.o.b.) (IMF: International Financial Statistics, Trends in Developing Economies).

Imports: The value of merchandise imports, measured free-on-board (f.o.b.) (IMF: International Financial Statistics, Trends in Developing Economies).

Foreign Trade Balance: Exports as defined above minus imports as defined above (International Financial Statistics, Trends in Developing Economies).

Currency Change: The annual percentage changes in the national currency value in relation to the US dollar (International Financial Statistics).

Principal Exports: A list of the country's primary exports and main export partners (World Factbook, Background Notes, World Almanac).

Principal Imports: A list of the country's primary imports and main import partners (World Factbook, Background Notes, World Almanac).