# International Political Risk Management: Perspectives, Approaches and Emerging Agendas

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**This paper reviews the extant and emerging perspectives on, and approaches to, political risk management, particularly in the context of foreign direct investment. The authors identify and classify the various theoretical lenses in the domain of political risk management, and suggest a future research agenda. The paper contributes by conceptually categorizing and mapping the extant research onto three approaches to the management of political risk. Through conducting a narrative literature review, the authors suggest three theoretical perspectives on political risk management: institutions; resources and capabilities; and resource dependence. They argue that the institutions approach to political risk management is reactive, responding to external stimuli, whereas the resources- and capabilities-based approach is proactive, preparing and acting in anticipation. The resource dependence domain offers an intermediate approach – the active management of political risk. The authors also suggest that the effectiveness of the domains' approaches may vary across different national contexts.**

## Introduction

The often unpredictable and hard to measure nature of political risk makes it difficult to anticipate and manage ((Lawton *et al*. 2014; McKellar 2010). For managers, financial, operational and other forms of risk can also arise unexpectedly and have a significant impact on business structure and strategy. But how do you manage the risk to your organization and assets associated with sudden regime change, an unexpected policy shift by government or the political instability caused by a terrorist attack or civil unrest? Despite the range and scale of impacts that political risk can have on companies, many top management teams continue to ignore, avoid or underestimate its strategic importance (Bremmer and Keat 2010; Czinkota *et al*. 2010; Lawton *et al*. 2014). Setting aside extractive industries and other sectors prone to frequent political intervention, firms typically deal with political risk in a tactical and defensive mode (Lawton *et al*. 2014). The extant literature on political risk management reflects this reactive and avoidance-oriented tendency (Butler and Joaquin 1998; Ellstrand *et al*. 2002; Henisz and Zelner 2003; Henisz *et al*. 2010; Jiménez 2010; Jiménez *et al*. 2014; Kobrin 1979; Moran and West 2005; Mortanges and Allers 1996; Slangen and van Tulder 2009).

In this paper, we challenge this predisposition and show there are other approaches that are proactive and more strategic in managing political risk. We draw on diverse research threads and theoretical perspectives to advance a comprehensive assessment and classification of political risk management scholarship, particularly in the context of foreign direct investment (FDI). We subsequently map these perspectives onto three approaches to the management of political risk: reactive, proactive and active.

As a mode of foreign market entry, FDI – particularly through greenfield investments and international acquisitions – entails greater voting shares (a 10% threshold) and control over the operations and organization in a host country (*Financial Times* 2016). Yet it

also implies greater resource commitment, higher potential losses and fewer possibilities to remove assets from the host country (Feinberg and Gupta 2009; *Financial Times* 2016). This conundrum stimulated our interest in research on the determinants of FDI decisions. Much of the extant research focuses on market and corporate determinants such as resource factors, including financial, managerial and knowledge (Erramilli 1991; Herrmann and Datta 2002; Lecraw 1993), organizational capabilities such as networking and timing (Chen and Chen 1998; Chen *et al.* 2004; Isobe *et al.* 2000; Li *et al.* 2008; Luo 2001), company size (Moran 2012; Terpstra and Yu 1988), degree of diversification (Doukas and Lang 2003; Mudambi and Mudambi 2002), prior acquisitions (Harris and Ravenscraft 1991), age of the enterprise (Moran 2012; Mudambi and Mudambi 2002), level and extent of FDI experience (Benito and Gripsrud 1992; Chan *et al.* 2006), and governance and ownership structures (Cui and Jiang 2012; Lien and Filatotchev 2015; Meznar and Nigh 1995; Woodcock *et al.* 1994). Some studies have also explored how FDI decisions depend on factors determined by the industrial and national systems of host and home countries (Jensen 2008). Examples include: industry resources, size and structure (Denekamp 1995; Moran 2012; Yu and Ito 1988); national economic, legislative, administrative and political systems (Buckley *et al.* 2007; Chan *et al.* 2008; Globerman and Shapiro 1999; Habib and Zurawicki, 2002; Li and Resnick 2003); and market dynamics such as size, demand and competition (Anand and Kogut 1997; Galan and Gonzalez-Benito 2001; Kim and Lyn 1987; Sethi *et al.* 2003; Tsang 2005). Moreover, some authors refer to FDI decisions as being influenced by the activities of international institutions such as the World Bank or the World Trade Organization (Lawton and McGuire 2005; Lawton *et al.* 2009) or being determined by international relations, particularly home–host country agreements and relations (Bieler *et al.* 2004; Lundan 2004; Schuler and Brown 1999).

We argue that these FDI determinants cannot be fully understood without considering the moderating effect of the political environment (De Villa *et al.* 2015), and without factoring in the risk arising from actions or inactions in this political context (Bremmer 2005). Hence our interest in the political risk factor in FDI decision-making. Spar (2001) stresses that FDI is inherently political, and political risks remain the key determinant of FDI decisions. This perspective is supported by studies such as Brewer (1981, 1985), Kobrin (1979), Oetzel (2005), and Zhuang *et al.* (1998) that support the idea of political risk as a significant determinant of FDI decisions. Moreover, political risk has implications not only at the pre-investment stage, but also when the FDI is in place (Feinberg and Gupta 2009; Oetzel 2005). In this paper, we revisit the link between political risk and firms' overseas investments by reviewing and classifying the relevant literature. We place an emphasis on the role of political risk management in this interconnection.

For our purposes, political risk refers to the possibility that a specific action or inaction in the political environment will directly or indirectly, on a regular basis or episodically, induce negative or positive changes in the economic outcomes of firms at macro and micro levels. This study considers political risk particularly in an international context, and examines it as one of the most important determinants of FDI choices. We define the political environment as a complex multi-level construct composed of: firm–government relations (firm-level); trade associations, unions and interest groups (industry-level); policies, norms and regulations, and political history in host and home countries (national-level); supranational entities, international agreements of, or between, a multinational enterprise's (MNE's) host and home countries, and political relations between an MNE's host and home countries (international-level) (De Villa *et al.* 2015; Doh *et al.* 2012).

Since earlier studies (Baglini 1976; Carlson 1969; Eiteman and Stonehill 1973; Green 1972; Green and Korth 1974; Weston and Sorge 1972) and two subsequent reviews (Fitzpatrick 1983; Kobrin 1979), research into political risk and its management has moved forward in different strands. As more countries around the world opened to FDI as the result of shifting from import-substitution industrialization to market-friendly strategies (Ramamurti 2001), new literature streams emerged in the mid-1980s that challenged the traditional perspective on political risk management, which assumed the authority of government (Poynter 1982; Root 1968; Truitt 1970) and the passivity of firms in the political environment (Faber and Brown 1980). This work also challenged the view that political risk has exclusively negative implications, should be avoided, and cannot be managed by firms (Green and Smith 1972; Root 1968; Root and Ahmed 1978). We learned from these studies that political risk does not always have purely negative implications (Jiménez *et al.* 2014) and that, if able to adopt a more active stance in the political environment (Dieleman and Boddewyn 2012; Getz and Oetzel 2009) and thereby influence government

(Blumentritt and Rehbein 2008; Holtbrügge *et al*. 2007), firms can actively manage and reduce political risk (Holburn 2001; Oliver and Holzinger 2008; Puck *et al*. 2013; Shaffer 1995). However, we have a limited understanding of the overall political risk research terrain, where these new perspectives could be documented relative to existing approaches to political risk management. Our contribution addresses this knowledge deficiency by categorizing extant literatures into discrete domains, each advancing a distinct approach to the management of political risk, particularly in the context of FDI. Through exploring these domains, we intend to develop a more robust understanding of managerial approaches to political risk strategies for FDI, shed light on their possible complementarities, and suggest a future research agenda. We pursue these objectives through conducting a narrative literature review.

Compared with systematic reviews (e.g. meta-analysis), narrative reviews are particularly valuable where, as in our case, there is the need to integrate advances in a certain research field by reinterpreting and interconnecting many publications on different topics and with diverse methodological approaches (Baumeister and Leary 1997). Moreover, narrative reviews are preferred where, as in our sample, analytical aggregation is impossible owing to a diversity of methodologies in the studies (Baumeister and Leary 1997). Narrative reviews do not always suffer from subjectivity (Hammersley 2002; Jones and Gatrell 2014). Instead, a scholar may enhance the objectivity of a narrative review by borrowing the more rigorous approach of systematic reviews, as well as by attaining a high level of transparency in sample development (Hammersley 2001; Jones and Gatrell 2014).

The remainder of the paper is structured as follows. First, we outline a methodological approach to the review, and propose research domains. Then, we present the research domains and their approaches to political risk management outcomes. We subsequently discuss the results of our review and the implications for future research agendas.

## Methodology

To increase the objectivity of this review and the credibility of the analysis, we adopt a methodological approach based on the transparency of procedures in relation to the selection of studies to be included in the review. To increase the research transparency, we discuss conceptual boundaries, establish thematic and disciplinary parameters, outline the review process, and present survey results by detailing the sample quality and proposing a review framework.

### *Establishing conceptual boundaries*

The boundaries as to what constitutes political risk are based on a synthesis of existing definitions. As shown in the introduction, we propose a broad definition of political risk as the possibility that a specific action, or inaction, in the political environment will directly or indirectly, on a regular basis or episodically, induce negative or positive changes in the economic outcomes of firms at macro and micro levels. We envisage several conceptual implications of this definition. These are summarized in Table 1. It is worth noting in our definition of political risk how we reflect the evolution of the concept by capturing new challenges for firms in modern political environments. For example, in contrast to earlier definitions of political risk (Kobrin 1979; Robock 1971), we emphasize that the economic consequences of political risk are not always negative. In line with Robock's (1971) early classification, we emphasize that political risk may be regular/continuous or episodic/discontinuous. Indeed, as the frequency, magnitude and geopolitical implications of terrorist attacks, violent conflicts and civil unrest increases, there is a need to develop an enhanced understanding of not only potentially manageable systematic political risks, but also exposure to less controllable discontinuous political risks (Oetzel and Oh 2015).

In this review, we consider political risk in the context of FDI into a host country. Our focus is on studies that discuss the link between political risk in host and home countries, and the FDI of firms in host countries. Earlier studies assumed that political risk originates in a host country context. However, subsequent discussions questioned this assumption by suggesting that, being an open system, an international firm is also exposed to political dynamics in its home country (Duanmu 2014; Kobrin 1979; Li and Vashchilko 2010; Murtha and Lenway 1994; Simon 1984; Soule *et al*. 2014).

It is worth noting at this point what this paper considers to be beyond the concept of political risk. Table 1 details what political risks are not.

### *Establishing thematic parameters*

*Political risk management and corporate political activity.* We distinguish between the literature on

*Table 1. Conceptual boundaries and implications of political risk*

| Boundaries | Implications |
|---|---|
| 1. Political risk is the possibility that political actions or inactions trigger changes in economic outcomes. | Our definition combines political risk as a construct whose probability can be estimated, and as a construct whose probability is unknown (political uncertainty). The difference between the two constructs was first discussed by Knight (1921), Robock (1971) and Haendel *et al*. (1975). Since then, some researchers have drawn a clear line between political risk and political uncertainty (Bremmer and Keat 2010; Brink, 2004; Kobrin 1979, 1982; Miller 1992), whereas others have used the two terms interchangeably (López-Duarte and Vidal-Suárez 2010). The two ideas have several differences cutting across normative and positive views. Normatively, drawing on some earlier works (Haendel *et al*. 1975; Knight 1921; Robock 1971), scholars have assumed that, unlike political uncertainty, political risk can be measured because its probability can be estimated (Baird and Thomas 1985; Boyacigiller 1990; Bremmer and Keat 2010; Brink, 2004; Daniels *et al*. 1985; Fitzpatrick 1983; Kobrin 1979; 1982; Oetzel *et al*. 2001). They further surmise that information is what makes the two constructs different. That is, information about the political environment helps managers to convert uncertainty to risk that may be measured, forecast and, consequently, avoided. Yet some authors continue using the terms 'political risk' and 'political uncertainty' interchangeably. For instance, political risk is considered as a proxy of uncertainty in the political environment in López-Duarte and Vidal-Suárez (2010). These authors make an implicit assumption that, as with political uncertainty, political risk is difficult to estimate and, for this reason, is nearly impossible to manage and avoid. Indeed, the two terms may converge in the conditions of high political instability where, owing to the lack of information, it is almost impossible to provide accurate estimates of political risk and to control its economic implications (Miller 1992). |
| 2. Political risk is a function of not only political action, but also political inaction. | Many early conceptualizations of political risk assumed that it is triggered by political actions (Schmidt 1986; Shapiro 1981; Smith 1971). However, later studies referred to political risks as consequences of political inactions on the part of host and home governments and foreign firms (Oetzel 2005; Wells, 1998). The unwillingness of governments to take an active stance in regulatory policies or elsewhere in the political arena may substantially change conditions of FDIs and affect their performance (Henisz 2002). For example, the reluctance of a government to take measures against pollution from foreign manufacturers may occasionally escalate environmental protests and nationalistic movements and put at risk the operations of foreign manufacturers (Lawton *et al*. 2014). Similarly, the reluctance of firms to cooperate with governments on political matters may occasionally result in the adoption of policies and regulations putting at risk the performance of their FDIs (Lawton *et al*. 2014). |
| 3. Political action or inaction may be triggered not only by governments and their intervention, but also by other actors in the political environment. | Political action or inaction may be taken not only by governments and their intervention – governmental risk (Poynter 1982) – but also by other actors (rebel groups, transnational advocacy groups, non-governmental organizations, and individuals) in the political environment,[a] i.e. societal risk (Iankova and Katz 2003; Ting 1988). This allows the inclusion of a broader range of political risks in our analysis. That is, apart from expropriation, corruption, breach of contract, discriminatory taxation, repatriation of profits, currency controls and other types of governmental risks (Butler and Joaquin 1998; Habib and Zurawicki 2002; Poynter 1982), we consider risks that are indirectly related to government policies. For example, such political risks may be associated with terrorism and violence (Globerman and Shapiro 2003), revolutions (Nigh 1985), civil wars (Nigh 1985), international conflict (Nigh 1985), economic embargoes (Fatehi and Safizadeh 1994), and nationalism and social unrest, such as strikes and demonstrations (Bremmer 2005). |
| 4. Political risks may be regular or episodic. | Political risks may be regular (continuous) or episodic (discontinuous) (Oetzel and Oh 2015). Regular political risks are associated with policy uncertainty and corruption (Oetzel and Oh 2015). By contrast, episodic risks lead to discontinuities ranging from terrorist attacks to violent conflicts, which also influence the political environment but are difficult to anticipate and predict (Oetzel and Oh 2015). |
| 5. The economic implications of political risk may be direct and indirect. | The implications are direct if they have an immediate impact on the profits of firms. They are indirect if they are mediated by changes in managerial policies (Henisz and Zelner 2003; Siegel 2007). For example, firms may respond to the risk of expropriation by engaging in lobbying and by forging international alliances against expropriation legislation and practices, which, if successful, helps to secure profits and, if unsuccessful, undermines profitability (Henisz and Zelner 2003; Siegel 2007). |
| 6. Political risks may induce both positive and negative economic changes. | The economic outcomes do not necessarily have to be negative. Instead, political risk may occasionally create political opportunities and even improve the performance of firms (Alon and Herbert 2009; Holburn and Zelner 2010). For example, corruption in a host country may put foreign firms with little or no knowledge of dealing with corrupt governments at a disadvantage, but it may help those firms with prior experience of high levels of corruption (Holburn and Zelner 2010). |
| 7. Political risks have macro and micro effects on economic outcomes. | We do not limit political risk to either macro effects spanning all firms or micro effects pertinent only to certain firms, firms in specific industries, and firms with certain approaches to branding (Alon and Herbert 2009; Kobrin 1979; Robock 1971). For instance, firms in strategic national sectors may be more sensitive to political risk (Alon and Herbert 2009). Similarly, firms whose corporate brands are closely associated with states leading anti-terrorist initiatives are more exposed to risks of terrorist attacks (Alon and Herbert 2009). |

*Table 1. Continued*

| Boundaries | Implications |
|---|---|
| 8. What political risks are not. | We distinguish political risks from economic (e.g. debt level, inflation and GNP), exchange (e.g. volatility of foreign exchange rates), financial (e.g. interest rates), cultural (e.g. cultural distance), social (e.g. strikes and ethnic conflicts), informational (e.g. cyber-attacks and intellectual property loss) and environmental risks (e.g. explosions, pollution and natural disasters) (Grosse and Trevino 1996; Kobrin 1976; Meschi and Riccio 2008; Quer *et al*. 2007; 2012; Shan 1991; Siegel *et al*. 2013). Yet, in some cases, the border between political and other risks may be thin (Boddewyn 1988). For instance, a risk of government default on payments does not always have a purely economic nature; rather, it may have political motivations. Given this potential overlap, this review distinguishes political risks from other risks by taking account of the motivations behind actions or inactions in the political environment. |

*Note*: [a]Political environment is a complex multi-level construct, which includes: firm–government relations (firm-level); trade associations, unions and interest groups (industry-level); policies, rules of the game and political history in host and home countries (national-level); supranational entities, international agreements of, or between, an MNE's host and home countries, and political relations between an MNE's host and home countries (international-level) (De Villa *et al*. 2015; Doh *et al*. 2012).

political risk and its management, and research into corporate political activity (CPA). First, the two literature streams emphasize different origins and implications. Political risk is situated in the firm's environment (e.g. political uncertainty in the international environment of business) or at the intersection of the environment and the firm (e.g. nationalization) (Kobrin 1979; Lawton *et al*. 2013a). Despite being triggered by events, processes and routines in the market and non-market environment, CPA originates within the firm, hence the focus on legal and illegal political behaviors of firms, including lobbying, fostering political ties, corruption and bribery (Kobrin 1979; Lawton *et al*. 2013a).

As for the implications, strategic management and international business research into the political risk of FDI primarily considers the repercussions for firms and their aggregates, particularly industries (Lawton *et al*. 2013a). However, CPA studies are interested in the political risk effects, not only on firms, but also on other actors in the non-market environment, including host and home governments and non-governmental organizations (NGOs) (Lawton *et al*. 2013a).

Second, the two literatures emphasize different objectives: political risk management focuses on estimating political risk and managing the implications for firms; CPA incorporates strategies and tactics that facilitate political risk assessment and control for performance implications, but it is a broader domain (Lawton *et al*. 2013a). For instance, CPA may aim to foster political ties with home and host governments (Sun *et al*. 2012), or focus on securing first-mover advantages for the foreign investor (Frynas *et al*. 2006).

*Political risk management and non-market strategy.* Political risk management is not only a dimension of CPA, but is also an element of the broader non-market domain (Kingsley and Vanden Bergh 2015; Lawton *et al*. 2014; Liedong *et al*. 2014; Mellahi *et al*. 2016; Oetzel and Oh 2015; Oliver and Holzinger 2008). A closer look at the research into non-market activity suggests that the discourse on political risk cuts across three major streams in this wider literature: non-market factors; non-market strategies; and outcomes of non-market strategies (Lawton *et al*. 2014; Mellahi *et al*. 2016). The first literature stream considers political risk as a factor originating in the non-market environment of firms. It stems from political events (e.g. corruption, expropriation, nationalization, repatriation of profits and international political conflicts) triggered by socio-political actors such as societal groups, NGOs, firms, and home and host governments (Doh *et al*. 2012; Kingsley and Vanden Bergh 2015).

With its emphasis on non-market strategies, the second literature stream identifies political risk management as being closely intertwined with corporate social strategy (Detomasi 2008), part of corporate political strategy (Keillor *et al*. 2005; Murtha and Lenway 1994), and integrated into overall non-market strategy (Hadani and Coombes 2015; Liedong *et al*. 2014; Oetzel and Oh 2015). For instance, Liedong *et al*. (2014) and Hadani and Coombes (2015) argue that firms manage policy risks through an interplay of two pillars of non-market strategy – corporate political strategy and corporate social strategy. For example, governments, especially those with developmental needs, tend to trust firms engaged in both lobbying and philanthropic activities to fill funding gaps (Liedong *et al*. 2014). Such trust helps to make

relationships between firms and governments more predictable, and hence lower the policy risks for firms (Liedong *et al.* 2014).

Finally, in the third literature stream, political risk appears as a factor that moderates outcomes of non-market strategies and affects the implications of their alignment or misalignment (Lawton *et al.* 2014; Mellahi *et al.* 2016; Oliver and Holzinger 2008). No matter how well thought through political uncertainties are, there will always be some types of political risk that firms fail to incorporate into their non-market strategies (Lawton *et al.* 2014; Mellahi *et al.* 2016). It is this risk which may distort the desired outcomes of socio-political activity of firms (Lawton *et al.* 2014; Mellahi *et al.* 2016).

In sum, this paper considers political risk management as a dimension of CPA, as well as an element of the broader area of non-market strategy.

### *Establishing disciplinary boundaries*

Most studies of political risk and its implications for FDI are in the field of public policy and management. These studies are beyond the scope of our review. This is because, for the most part, they examine international political risk management through the lens of national and supranational public policy. They do not address the role of political risk in our primary unit of analysis – international firm strategy making (Baccini and Urpelainen 2014; Gehlbach and Keefer 2012; Malesky 2008).

A firm perspective on political risks to FDI is most evident in strategic management and international business research. Hence our focus on studies in these two disciplines (Ghoshal 1987; Holburn and Zelner 2010; Li 1995; Makhija 1993; Rice 1986; Ring *et al.* 1990; Ruefli *et al.* 1999; Simon 1984; Stevens *et al.* 2015). Indeed, political risk, particularly connected with FDI, is a distinct research field in international business (Boddewyn and Brewer 1994; Fitzpatrick 1983; Henisz *et al.* 2010; Kobrin 1979; Miller 1992; Simon 1984). Similarly, political risk is a theme within strategic management research, originating at the intersection of the environment and the firm, and affecting managerial decisions and the economic outcomes of firms (Clarke and Varma 1999; Holburn and Zelner 2010; Kobrin 1982; Ring *et al.* 1990).

Through focusing on these two disciplines, our review integrates discussions about political risk and FDI implications from a firm perspective. This adds value in two ways. First, we synthesize discussions on how firms cope with the strategic challenges of political risk to FDI in an international business environment. Second, we integrate advances in, and suggest directions for, political risk theory development in both disciplines.

### *Research process*

Our focus is primarily on research published in academic journals and books since the seminal works of Knight (1921) and Fainsod (1940). We consider these two studies as the basis for research into the link between political risk and FDI. Even though these scholars did not focus on political risk management in an international setting, their studies shed light on the essence of risk in the political environment and its role in investment decisions, and have stimulated discussions in our area of interest.

Using ProQuest and EBSCO databases, we selected books and papers that discuss the political risk of firms, and have been cited at least once in a peer-reviewed journal. In addition, we included newer articles (2012–2016), some of which have not yet been cited. The selected papers were published in English-speaking journals within the disciplinary boundaries of our study: strategic management and international business.

Focusing on studies with methodological and theoretical rigor, we opted for publications from higher-ranked journals. We referred to the most recent and extensive international rankings of English-speaking journals in strategic management and international business (ABS 2015, ABDC 2013 and Thomson Reuters 2015). We combined the three quality rankings to develop the journal sample. This included journals with rankings rated 3 and above in the ABS system, A* and A in the ABDC rankings, and an impact factor greater than 1.000 in Thomson Reuters Journal Citation Reports in business and management categories. The list of journals in our sample is shown in Table 2.

Having defined the sample, we went on to review publications. The review process was initiated by searching for publications using 'political', 'risk', 'uncertainty' and 'foreign direct investment' in their topic, as these terms are typically used by authors to discuss the link between political risk and FDI. We repeated the search several times, each time by substituting 'foreign direct investments' with the exact type of FDI in terms of entry ('greenfield', 'mergers' and 'acquisition') and ownership ('wholly owned subsidiary' and 'joint venture'). In total, the search

*Table 2. Journals included in the sample*[a]

| N | Journal[b] | ABS ranking[c] | ABDC ranking | Thomson Reuters JCR impact factor |
|---|---|---|---|---|
| 1 | Academy of Management Review | 4* | A* | 7.817 |
| 2 | Journal of Management | 4* | A* | 6.862 |
| 3 | Academy of Management Journal | 4* | A* | 4.974 |
| 4 | Journal of International Business Studies | 4 | A* | 3.597 |
| 5 | Journal of Management Studies | 4 | A* | 3.277 |
| 6 | Management and Organization Review | 3 | A | 3.277 |
| 7 | Strategic Management Journal | 4* | A* | 2.993 |
| 8 | Asia Pacific Journal of Management | 3 | A | 2.742 |
| 9 | International Journal of Management Reviews | 3 | A | 2.673 |
| 10 | Administrative Science Quarterly | 4* | A* | 2.394 |
| 11 | Long Range Planning | 3 | A | 2.111 |
| 12 | California Management Review | 3 | A | 1.944 |
| 13 | British Journal of Management | 4 | A | 1.909 |
| 14 | Journal of World Business | 4 | A | 1.907 |
| 15 | Strategic Organization | 3 | A | 1.853 |
| 16 | Harvard Business Review | 3 | A | 1.831 |
| 17 | Business & Society | 3 | A | 1.804 |
| 18 | Strategic Entrepreneurship Journal | 4 | A | 1.744 |
| 19 | Journal of Management Inquiry | 3 | A | 1.594 |
| 20 | International Business Review | 3 | A | 1.489 |
| 21 | Journal of Business Research | 3 | A | 1.306 |
| 22 | Management Learning | 3 | A | 1.245 |
| 23 | Journal of International Management | 3 | A | 1.096 |

*Notes*: [a]The journals are ordered by the Thomson Reuters JCR impact factor.
[b]In Europe, the ABS rankings were published by the British Association of Business Schools in February 2015 (Harzing 2015). It is worth noting that we decided not to use other European ranking systems because these considered fewer journals, reflected views of academics from only one institution, and included national non-English-speaking journals. In Asia and Oceania, the rankings corresponding to our criteria were represented by the ABDC (2013) edition developed by the Australian Business Deans Council (Harzing 2015). The composition of these rankings overlapped substantially with that of the ABS rankings. In the USA, the journal rankings were developed by Thomson Reuters in the Journal Citation Reports in 2013 (Thomson Reuters 2015).
[c]Owing to the selection process, we excluded several 3-AJG and 'A' journals found in the strategy and international business sections of the ABS and ABDC journal quality lists but not ranked in Thomson Reuters Journal Citation Reports. These journals were *Theory, Culture and Society*, *Global Strategy Journal* and *Management International Review*. We excluded 142 journals listed in Thomson Reuters Journal Citations Reports, but not specializing in the disciplines of our interest: strategic management and international business. Those were journals whose primary themes were marketing, research methods, management science, cross-cultural management, human resources, psychology, organizational behavior, logistics, innovations, management information systems, accounting and finance.

generated 1324 results. Based on the relevance to the political risk–FDI link and conceptual boundaries, we further refined this list to 164 publications. Of these, 74 studies belonged to larger domains. These selected publications are marked with the * symbol in the Reference list.

## Study results

### *Sample quality*

A closer look at our sample of studies reveals three issues about its quality. First, there is a disciplinary divide between studies focusing on external public policy implications and internal corporate impact. Having gained substantial attention among public-policy scholars, external public policy implications such as policy change and policy maintenance remain largely beyond the scope of strategic management and international business research. Instead, the political risk scholarship in strategic management and international business tends to cluster around internal corporate impact. For example, work on the corporate impact of political risk cuts across decisions about FDI – such as decisions about when and how to enter overseas markets – and the performance outcomes, including market growth and share, revenue, profits and market capitalization, and security of human assets, intellectual property and facilities.

The disciplinary divide has implications for the quality of our sample. Because our major field of interest is at the intersection of strategic management

and international business, our sample is biased to studies centering on internal corporate impacts. The selected studies fail to address the relationship between external public policy and internal corporate impact. An interdisciplinary research approach is needed to address this deficiency.

Second, there is a theoretical divide among studies in our sample. For the most part, prior to the early 1980s, research into political risk and its implications for FDI was theoretically weak (Simon 1984). However, advances in strategic management and international business research meant that subsequent studies benefited from a broad range of theoretical perspectives, including agency theory, institutional theory, the resource-based view, resource dependence theory, bargaining power theory and stakeholder theory. Our review suggests that an institutional perspective on political risk management emerged from three different approaches: new institutional theory (DiMaggio and Powell 1983); new institutional economics (North 1990); and national business systems (Jackson and Deeg 2008). We identified 41 studies using these theoretical lenses. Moreover, a growing interest in the resource-based view (Wernerfelt 1984) triggered research into the role of resources and capabilities in the political risk management of FDI. We found 16 studies in this field. Similarly, applications of bargaining power (Bacharach and Lawler 1981; Pen 1952; Wagner, 1988) and stakeholder approaches (Freeman 1984) revitalized discussions about the role of resource dependence (Pfeffer and Salancik 1978) in the exposure of FDI to political risk. Our search suggested 19 publications in this stream. Studies adopting other theoretical perspectives are relatively limited (Table 3).

### Research framework

We began the development of the research framework by searching for commensurability, or criteria (e.g. assumptions) that would allow evaluation of studies from different theoretical perspectives (Willmott 1993). We found most studies structured their analyses by addressing three major assumptions in the traditional view of political risk (Figure 1). Using these assumptions, we discovered three broader literature domains, which we label as institutions, resource and capabilities, and resource dependence. The three domains also have the largest frequencies of studies in the sample.

The domains shape political risk management outcomes such as (external) public policy and (internal) corporate impact. With external public policy, a firm aims to enhance its competitive position by changing or maintaining existing policy. The external public policy may have an internal corporate impact manifest in the firm's market performance (e.g. market growth and share), financial dynamics (e.g. revenue, profits and market capitalization) and security of assets (e.g. safety of human capital, security of facilities and protection of intellectual property). The subsequent sections discuss the three domains in detail.

### *Domain 1: Institutions*

The institutional perspective on political risk and FDI decisions in international business is well established (Dahan *et al.* 2006; Green 1972; Kassicieh and Nassar 1986; Moran 1973; Nigh 1985). The earlier mentioned scope and multidimensionality of the institutional perspective (DiMaggio and Powell 1983; Hotho 2014; North 1990; Whitley 2007) facilitates understanding of international business phenomena in general (Hotho and Pedersen 2012), and of non-market strategies in particular (Doh *et al.* 2012). Following Hotho and Pedersen (2012) and Doh *et al.* (2012), we also refer to the three approaches – new institutional economics, neo-institutional perspectives and national business systems – to address the complexity of the institutional domain of political risk research. We present key studies in Table 4.

As with many studies in the non-market strategy field (Doh *et al.* 2012), new institutional economics contributes to political risk management research by focusing on how political and regulatory uncertainty shapes the decisions of firms. Studies in this stream are mostly concerned with deterring the effects of instability in regulatory institutions, and the risk posed to FDI by changes in home and host country institutional environments, as well as moderating factors (Cherchye and Verriest 2016; Delios and Henisz 2000, 2003a,b; Henisz and Delios 2001, 2004; Slangen and van Tulder 2009; Witt and Lewin 2007). Most studies agree that risks associated with uncertainty due to opaque regulatory environments, underdeveloped judicial and financial systems, corruption and engagement in inter-state political conflicts increase the costs of and, therefore, discourage FDI (Chung and Beamish 2005; Delios and Henisz 2000; Desbordes 2007; Fatehi-Sedeh and Safizadeh 1988; García-Canal and Guillén 2008; Gaur and Lu 2007; Habib and Zurawicki 2002; Henisz and Delios 2001; Hiatt and Sine 2014; Holmes *et al.* 2013; Kobrin *et al.* 1980; Lee and Hong 2012; Li and Vashchilko 2010;

*Table 3. Themes in the sample*

| Themes[a] | Studies | Supporting studies[b] |
|---|---|---|
| Institutions (41studies) | Arregle *et al*. (2013) | New institutional economics (North 1990) |
| | Blake and Moschieri (2017) | New institutional perspective (DiMaggio and Powell 1983) |
| | Cherchye and Verriest (2016) | National business systems (Hotho 2014; Whitley 2007) |
| | Christmann *et al*. (1999) | Environmental determinism (Hannan and Freeman 1984, 1989) |
| | Chung and Beamish (2005) | |
| | Click (2005) | |
| | Delios and Henisz (2000) | |
| | Delios and Henisz (2003a,b) | |
| | Desbordes (2007) | |
| | Duanmu (2014) | |
| | Fatehi-Sedeh and Safizadeh (1988) | |
| | García-Canal and Guillén (2008) | |
| | Gaur and Lu (2007) | |
| | Guillén (2003) | |
| | Habib and Zurawicki (2002) | |
| | Henisz and Delios (2001) | |
| | Henisz and Delios (2004) | |
| | Hiatt and Sine (2014) | |
| | Holmes *et al*. (2013) | |
| | Kolstad and Wiig (2012) | |
| | Kwok and Tadesse (2006) | |
| | Lee and Hong (2012) | |
| | Li and Vashchilko (2010) | |
| | López-Duarte and Vidal-Suárez (2013) | |
| | Lu *et al*. (2014) | |
| | Meschi and Riccio (2008) | |
| | Mudambi *et al*. (2013) | |
| | Murtha and Lenway (1994) | |
| | Quer *et al*. (2012) | |
| | Ring *et al*. (2005) | |
| | Robertson and Watson (2004) | |
| | Rodriguez *et al*. (2005) | |
| | Rothaermel *et al*. (2006) | |
| | Salomon and Wu (2012) | |
| | Slangen and van Tulder (2009) | |
| | Soule *et al*. (2014) | |
| | Tallman (1988) | |
| | Witt and Lewin (2007) | |
| | Xie and Li (2017) | |
| | Zheng (2012) | |
| Resources and capabilities (16 studies) | Alon and Herbert (2009) | Proactive approach to political strategizing (Hillman and Hitt 1999) Resource-based view (Barney and Arikan 2001; Wernerfelt 1984, 1995; Peteraf 1993) |
| | Demirbag *et al*. (2011) | |
| | Frynas *et al*. (2006) | |
| | Getz and Oetzel (2009) | |
| | Hadani and Schuler (2013) | |
| | Holburn (2001) | |
| | Holburn and Zelner (2010) | |
| | Jiménez (2010) | |
| | Jiménez and Delgado-García (2012) | |
| | Jiménez *et a*l. (2014) | |
| | Mellahi *et al*. (2011) | |
| | Moon and Lado (2000) | |
| | Oetzel and Oh (2013) | |
| | Oliver and Holzinger (2008) | |
| | Poynter (1982) | |
| | Puck *et* al. (2013) | |

*Table 3. Continued*

| Themes[a] | Studies | Supporting studies[b] |
|---|---|---|
| Resource dependence[c] (17 studies) | Arnoldi and Villadsen (2015)[RDT] | Resource dependence theory (Hillman *et al*. 2009; Pfeffer and Salancik 1978; Ramamurti 1986) |
| | Blumentritt (2003)[RDT + BP] | Stakeholder approach (Donaldson and Preston 1995; Freeman 1984; Frooman 1999) |
| | Blumentritt and Rehbein (2008)[RDT + BP] | Bargaining theory (Bacharach and Lawler 1981) |
| | Boyacigiller (1990)[RDT] | Obsolescing bargaining power (Vernon 1971) |
| | Brewer (1992)[RDT + BP] | |
| | Choudhury and Khanna (2014)[RDT + BP] | |
| | Dieleman and Boddewyn (2012)[RDT + BP] | |
| | Holtbrügge *et al*. (2007)[RDT + ST] | |
| | Inkpen and Beamish (1997)[RDT + BP] | |
| | Kim (1988)[RDT+BP] | |
| | Liu *et al*. (2016)[RDT] | |
| | Nebus and Rufin (2010))[BP + ST] | |
| | Poynter (1982, 1986)[RDT + BP] | |
| | Ramamurti (2000)[RDT+BP] | |
| | Ramamurti (2001)[BP + ST] | |
| | Ramamurti (2003)[RDT + BP + ST] | |
| | Vachani (1995)[RDT + BP] | |
| | Yan and Gray (2001)[RDT + BP] | |
| Transaction costs and real options (6 studies) | Ahsan and Musteen (2011); | Transaction cost approach (Williamson 1981) |
| | Brouthers and Brouthers (2003) | Transaction cost approach to CPA (Sawant 2012) |
| | Brouthers *et al*. (2008) | |
| | Fisch (2011) | |
| | Hennart (1988) | |
| | Meschi (2009) | |
| Agency view (2 studies) | Boubakri *et al*. (2013) | Positive political theory of agency research into political risks (Holburn and Bergh 2008) |
| | Ellstrand *et al*. (2002) | |
| Eclectic paradigm (2 studies) | Loree and Guisinger (1995); | Eclectic paradigm (Dunning 1980) |
| | Schollhammer and Nigh (1986) | |
| Political business cycles (1 study) | Vaaler (2008) | Political business cycles (Nordhaus 1975) |
| Firm behavior (1 study) | Alcantara and Mitsuhashi (2012) | Behavioral theory of firm (Cyert and March 1963) |
| Individual behavior (2 studies) | Amariuta *et al*. (1979) | Microfoundations (Marquis and Raynard 2015) |
| | Maitland and Sammartino (2015) | Frynas and Stephens (2015) |

*Notes*: [a]The sample is biased to studies discussing institutions, resources and capabilities, and resource dependence. Nonetheless, there is the lack of studies adopting transaction cost/real options and agency theories. Also, there are very few studies adopting other frameworks and theoretical lenses: political business cycles, eclectic paradigm, firm behavior and microfoundations. These studies may stimulate the emergence of new domains in political risk research in the future.

[b]These studies are not in the sample.

[c]Studies marked with RDT use the resource dependence theory. Studies marked with RDT + BP complement resource dependence theory with bargaining power theory. Studies marked with RDT + ST complement resource dependence theory with stakeholder theory.

Lu *et al*. 2014; Mudambi *et al*. 2013; Tallman 1988). These risks can even cause subsequent divestment of FDI (Blake and Moschieri 2017; Soule *et al*. 2014).

Yet some studies have shown how firms are not always repelled by political risk in a specific host country. First, firms may opt for a less risky mode of entry (Delios and Henisz 2003a; López-Duarte and Vidal-Suárez 2013; Slangen and van Tulder 2009). Second, firms with previous experience in politically hazardous or culturally similar contexts are more likely to invest in politically hazardous regions (Delios and Henisz, 2003b; Kolstad and Wiig 2012; Meschi and Riccio 2008). Finally, there exist non-firm, or external environment, factors at industry and country levels that moderate the negative effects of political risk on FDI. At the industry level, political risks are more acute in highly regulated sectors (Desbordes 2007; García-Canal and Guillén 2008). At the country level, political risk is moderated by home country institutions and relations between home and host countries. For instance, FDI into other politically risky contexts may be triggered by the need to escape home country institutional constraints, i.e. institutional escapism (Witt and Lewin 2007). Alternatively, politically risky contexts may be more attractive because of gravity model factors such as larger host country economic

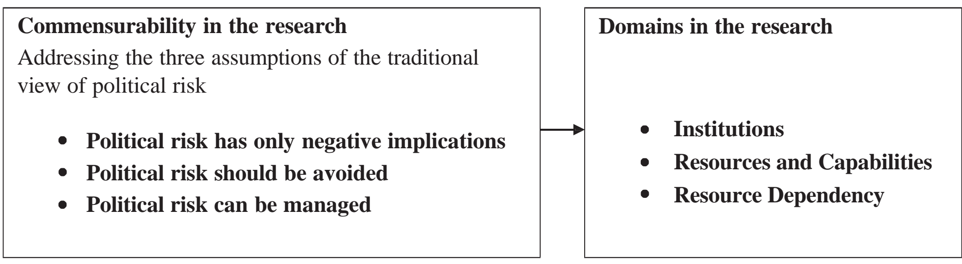


*Figure 1. Ontological Framework*

mass (or higher development) and smaller distance – cultural difference, dissimilar governance principles, and different economic cost structures – from the home country (Arregle *et al*. 2013; Kolstad and Wiig 2012; Li and Vashchilko 2010; López-Duarte and Vidal-Suárez 2013; Rothaermel *et al*. 2006).

Although the new institutional economics perspective places specific emphasis on the reactions of firms to political instability and associated risks, some studies contributed to the discussion around how firms can take a more proactive approach to politically uncertain contexts by influencing institutional structures (Duanmu 2014; Henisz and Delios 2004; Kwok and Tadesse 2006). Nonetheless, the new institutional economics view remains skeptical about the efficacy of influencing tactics such as lobbying and donations in politically unstable environments. Henisz and Delios (2004) contend that the efficacy of influencing strategies is a decreasing function of political instability. Indeed, politically uncertain contexts are susceptible to regime change, which can negate the investment in political influence. Scholars adopting a new institutional economics perspective prefer to concentrate on firms' market entry decisions – location, entry mode and investment sequencing (Delios and Henisz 2003a) – and on firms' market exit decisions (Blake and Moschieri 2017; Soule *et al*. 2014), without considering how firms manage political uncertainty when in the market.

While the new institutional economics viewpoint focuses on the role of institutional structures, the new institutional perspective (DiMaggio and Powell, 1983), also known as organizational sociology, contributes to political risk management research by placing an emphasis on social structures and relationships within societies and on how pressures emanating from them influence organizations and their responses to political risk stimuli. This stream informs how societal norms and practices underpin investment climates and governmental policies and, most importantly, how they shape firms' decisions in host countries with higher political risk. A distinctive feature of studies in this stream is the assumption that firms' responses to political risk are socially embedded in softer aspects (e.g. culture and history) and harder aspects (e.g. formal rules and enforcement systems) of institutions (Granovetter 1985; Jackson and Deeg 2008; Lawton *et al*. 2013a).

In assuming the social embeddedness of firms in institutional environments, the new institutional approach to political risk research suggests that institutions exert mimetic, normative and coercive pressures that trigger similar responses among firms and, therefore, lead to homogeneity, or isomorphism, in their organizational field. For instance, firms may become homogeneous owing to mimetic isomorphism, or through emulating the responses of other firms to political risk stimuli in host markets. In some cases, such responses ignore economic rationality in favor of normative rationality, which takes for granted the legitimacy of decisions made by more successful firms (trait-based emulation) or by most firms (frequency-based emulation). For example, when considering entry into a country with high political risk, a multinational firm may not always follow a less risky, staged entry approach where a joint venture precedes a wholly owned subsidiary. Instead, it may opt for a wholly owned subsidiary if the entry mode is adopted by most multinational firms (Guillén 2003). In parallel, Xie and Li (2017) and Zheng (2012) contend that, in a restrictive environment where political risk events such as expropriation and forced exit are more probable, foreign firms are more likely to choose entry modes of previously successful entrants to the host market. Also, Rodriguez *et al*. (2005) argue that, having entered a specific host market, foreign firms reduce political risks such as corruption by imitating the approaches of successful local firms.

Similarly, similar responses to political risk may occur owing to normative pressures to conform to the

*Table 4. Sample studies in the domains*

| Author | Year | Summary of key papers |
|---|---|---|
| Institutions domain (ID) | | |
| New institutional economics | | |
| Delios and Henisz | 2000 | The study suggests negative implications of political hazards on FDIs. Nonetheless, it may be considered as a bridge to the resources and capabilities domain. This is because it views experience as a factor of capabilities needed to cope with political hazards. |
| Habib and Zurawicki | 2002 | This paper examines the relationship between corruption and FDI. |
| Henisz and Delios | 2004 | The study agrees that political instability has negative implications for FDIs. It also contends that the efficacy of influencing strategies is a decreasing function of political instability. |
| Slangen and van Tulder | 2009 | This paper examines how soft institutional factors (e.g. culture) influence political risk for firms. |
| Li and Vashchilko | 2010 | The study examines the susceptibility of vertical and horizontal FDIs to political risks by considering institutional configurations of home and host countries. |
| Lu et al. | 2014 | This paper questions the assumption of negative effects of institutions. It examines how decisions about FDIs are affected by home country government support and host country institutions. |
| New institutional perspective | | |
| Henisz and Delios | 2001 | Looking at the example of Japanese MNCs, the authors explore imitation among firms as a political risk reduction strategy. |
| Rodriguez *et al*. | 2005 | This study argues that, having entered a host market, foreign firms reduce political risks such as corruption by imitating the approaches of successful local firms. |
| Zheng | 2012 | This paper suggests that, in a restrictive environment, where political risk events such as expropriation and forced exit are more probable, foreign firms are more likely to choose entry modes of previously successful entrants to the host market. |
| Guillén | 2003 | The author concludes that firms are likely to opt for a wholly owned subsidiary if this entry mode is adopted by a majority of other multinational firms. |
| New business systems approach | | |
| López-Duarte and Vidal-Suárez | 2013 | The paper examines how differences in configurations of soft institutions of home and host countries affect FDI modes (joint ventures vs. wholly owned subsidiaries). |
| Quer et al. | 2012 | The authors discuss how political risks stemming from institutional differences between home and host countries influence decisions about FDI location. |
| Salomon and Wu | 2012 | The study explores how political risks originating in institutional differences between home and host countries trigger isomorphic decisions about FDI. |
| Resources and capabilities domain (RCD) | | |
| Moon and Lado | 2000 | Building on the resource-based view, this study discusses how firms reduce uncertainties arising from the firm–host government bargaining relationship and attain desired outcomes by using resources and capabilities (e.g. managerial competencies, technological know-how and reputation). |
| Frynas *et al*. | 2006 | This paper shows how firms deploy political resources to generate first-mover advantages from investments in countries with high levels of political uncertainty caused by opaque regulations and legal voids. |
| Oliver and Holzinger | 2008 | The authors discuss how political strategies enable the mobilization of firm capabilities to either avoid or reduce political risks (value maintenance objective) or take advantage of political risks (value creation objective). |
| Holburn and Zelner | 2010 | The paper defines political resources and capabilities and explains their role as sources of sustainable competitive advantage and factors helping to reduce, and benefit from, political risks. |
| Sun et al. | 2011 | The paper draws attention to destructive effects of personal ties to political officials in the process of and after political regime changes. |
| Puck *et al*. | 2013 | This study suggests that political strategies of financial incentives, information and constituency building do not necessary mitigate exposure to, or generate value from, political risks; rather, they may occasionally lead to a competitive disadvantage. |
| Jiménez *et al*. | 2014 | The authors conclude that previous experience of exposure to political risk helps to develop capabilities (e.g. negotiation and lobbying) needed for future investments into other politically risky countries. |
| Resource dependence domain (RDD) | | |
| Boyacigiller[a] | 1990 | The study draws attention to the intra-organizational interdependencies of US MNEs exposed to high levels of political risk in host countries. The study argues that such interdependencies coupled with high political risk may have negative implications for firms and their performance. The papers further suggest that effective management of such interdependencies will require more flexible coordination mechanisms – those where staff members will be recruited from the home country (USA). |

*Table 4. Continued*

| Author | Year | Summary of key papers |
|---|---|---|
| Arnoldi and Villadsen | 2015 | The study refers to theory of resource dependence to consider political ties of MNEs in politically risky contexts. It suggests that governmental ties may help an MNE to manage its resource dependence and exposure to political risk in a host country. Specifically, thanks to central governmental ties, an MNE in China can gain access to critical resources, strategically important information, preferential treatment and benefits in the host country as well as to reduce the risk of government intervention. |
| Liu et al. | 2015 | Using the resource dependence theory, this study considers localization decisions of MNEs as ways to reduce resource dependence on host countries and manage political risks and their impacts on firm performance. The paper finds that localization does not help to reduce political risks and their impacts on firm performance. |
| Bargaining power approach[b] | | |
| Poynter | 1986 | The paper revisits the role of resource dependence and bargaining power of MNEs vis-à-vis host governments in political risky less developed economies, including Brazil, Tanzania, Zambia, increase bargaining power vis-à-vis, host governments in order to reduce exposure to the risk of government intervention. |
| Kim | 1988 | This study discusses the bargaining power of MNEs vis-à-vis host governments as an instrument helping to reduce exposure to political risk (e.g. government intervention). The paper argues that greater corporate political responsiveness enhances bargaining power and reduces the political risk exposure of MNEs entering highly competitive markets. |
| Brewer | 1992 | The author discusses political risks emanating from host government interventions. The study takes a closer look at how resources dependence and changes in bargaining power of MNEs affect their exposure to host government interventions in strategic industries. |
| Vachani | 1995 | The study discusses resource dependencies of MNEs on host governments from the perspective of obsolescing bargaining power. Using longitudinal firm-level data, this paper shows that, if able to reduce their resource dependence on host governments, firms can avoid the problem of obsolescing bargaining power. The ability to maintain bargaining power helps to reduce political risk (e.g. host government intervention). |
| Inkpen and Beamish | 1997 | The study refers to the theories of resource dependence and of bargaining power to discuss the exposure of firms to political risks due to instability in foreign firm–host partner firm relationships. The paper argues that the ability of an MNE to maintain or even reduce resource dependence on its host partner may help it to avoid undesirable shifts in, and ultimate obsolescence of, its bargaining power vis-à-vis its host partner and, therefore, reduce exposure to political risk in the host country. |
| Ramamurti | 2000 | The paper revisits the host government–MNE relationship in emerging economies from the perspective of resource dependence and bargaining power. Using examples of MNEs in a newly deregulated sector – telecommunications – in Latin American countries, it discusses possible outcomes of first-mover strategies on bargaining power and exposure to political risk. It concludes that first-mover market entry strategies create sustainable competitive advantages for MNEs, strengthen their bargaining power vis-à-vis host governments and reduce their exposure to regulatory risk. |
| Yan and Gray | 2001 | The study draws on ideas of resource dependence theory and bargaining power theory to explain bargaining between MNEs and their host–partner firms in contexts where political risk stems out of government influence. |
| Choudhury and Khanna | 2014 | The study revisits ideas of resource dependence and bargaining power to discuss FDIs of MNEs from politically risky countries. It argues that some firms make FDIs abroad to increase bargaining power and reduce resource dependence in their home countries. |
| Stakeholder approach[c] | | |
| Holtbrügge *et al.* | 2007 | Linking ideas from resource dependence and stakeholder theory, this study suggests that MNEs experience multiple interdependencies, which shape their exposure to international political risk. The paper further discusses the role and impact of interdependencies on various stakeholders of German MNEs investing to China, France, India, Russia and the US. |
| Bridging bargaining power and stakeholder approaches[d] | | |
| Ramamurti | 2001 | The study stresses the need to revisit the traditional approach to MNE bargaining in host countries. It criticizes the traditional model in the context of politically risky developing economies. It stresses that the model has a shortcoming: it discusses bargaining as an outcome of negotiations between two parties – MNEs and host governments – but without consideration of possible impacts of other actors in the diverse political environment. The paper suggests a new |

*Table 4. Continued*

| Author | Year | Summary of key papers |
|---|---|---|
| | | model where an MNE can reduce its political risk by building its bargaining power vis-à-vis host governments, as the result of its relationships not only with the host government but also with various entities in its home country, and with international organizations, including the World Bank, the IMF and the WTO. |
| Ramamurti | 2003 | This study draws attention to the role of resource dependence and multiple stakeholders in bargaining outcomes and dynamics of MNEs in politically unstable developing economies. Specifically, it argues that an MNE's bargaining power does not necessary obsolesce over time. Instead, an MNE can enhance constraints on the host government reneging and managing its bargaining power by controlling resource interdependencies with various stakeholders, including international organizations and public and private institutions in home and host countries. The study discusses possible applications of the new model using an example of Enron's Dabhol power project in the Indian state of Maharashtra. |
| Nebus and Rufin | 2010 | The study revisits discussions about bargaining power and resource dependence under conditions of political risk (e.g. government intervention and governmental uncertainty during privatization). It argues that the traditional bargaining model fails to address multiple interests and stakeholders in bargaining processes. It further suggests a new model, which takes account of a network of stakeholders whose political behaviors affect the market and non-market performance of firms. |

*Notes*: [a]These studies only use resource dependence theory.
[b]These studies complement resource dependence theory with bargaining power theory.
[c]These studies complement resource dependence theory with stakeholder theory.
[d]These papers cannot be easily assigned to either the bargaining power or stakeholder approach. However, insights from these studies may help to integrate, or bridge, the two approaches in future research.

same ethical codes of professional practice and education systems. However, even if existing literatures acknowledge a possibility of normative isomorphism in firms' responses to political risk, there is a lack of empirical research about the role of normative factors and processes in firms' behavior in politically risky contexts. For example, little is known about the role of internal normative pressures – those that stem from the norms adopted by a parent organization. Meanwhile, it is possible that subsidiaries follow the norms of their multinational parent when coping with political risk. For example, firms may follow homogeneous political risk assessment procedures established by centralized political risk intelligence units. Indeed, as the increasing globalization of MNEs reduces the autonomy of subsidiaries (Birkinshaw and Morrison 1995), many international factors, including political risk, are becoming strategic domains of parent organizations (Christmann *et al*. 1999).

Also, there is a lack of understanding of external normative pressures originating from sources beyond the parent organization. For instance, it is not known whether firms engage in similar political risk management practices because of being exposed to the recommendations of leading professional service firms and political risk consultancies. Similarly, it is not clear whether and how education systems influence political risk management practices. For example, very little is known about how different political risk measurement approaches advocated by consultancy agencies and universities determine the international investment decisions of firms.

Finally, firms may become like each other, owing to coercive isomorphism, which presumes compliance with the same legislation on corruption, tax systems, nationalization and other sources of political risk in a host country. For example, designed to reduce corporate bribery, the US Foreign Corrupt Practices Act (FCPA 1977) and its enforcement system have led to isomorphism in how companies registered in the US or trading shares on a US exchange respond to corruption in foreign markets. Rodriguez *et al*. (2005) argue that firms that are eager to comply with the FCPA provisions are more likely to prefer to enter host markets with a high risk of corruption by using arm's-length entry modes such as joint venture instead of FDI (particularly wholly owned subsidiaries).

The national business systems perspective overlaps with the new institutional economics and the new institutional theory approaches to the political risk of FDI. However, it shifts the focus from institutional and social structures to differences among national economic systems (Doh *et al*. 2012). The central hypothesis is that there exist relations between societal institutions and economic and societal

outcomes, particularly non-market outcomes such as political risk management (Hotho 2014; Whitley 1992, 1994, 1999, 2007). Research examined how cross-national distinctions in institutional configurations shape the reactions of firms to political risk (López-Duarte and Vidal-Suárez 2013; Quer *et al*. 2012; Salomon and Wu, 2012). The focus is on how and why firms with different soft (e.g. culture) and hard (e.g. ownership control regulations) institutional backgrounds may develop competencies for, and become equally effective in, avoiding or minimizing political risk exposure. Furthermore, the new business systems perspective examines how differences in national institutional organizations contribute to variations in the exposure of firms to political risk and approaches to its management (Salomon and Wu 2012).

Nonetheless, empirical research in this stream suffers from methodological constraints. Owing to measurement difficulties, it fails to capture institutional systems by taking account of national differences across a limited set of institutional aspects, such as national culture (Jackson and Deeg 2008; López-Duarte and Vidal-Suárez 2013). For instance, it leaves out such factors of national institutional configurations as state dominance, burden of regulations and union density, among others.

The domain makes two major contributions to political risk research. First, it informs us about political risk choices at a macro level. Second, it revisits assumptions of the traditional view of political risk. It agrees that political risk has negative implications for FDI and, therefore, should be avoided. It also agrees that, in most cases, firms cannot control political risk. Yet, there are studies that challenge this view. In new institutional economics, such studies argue that firms do not always reject investments; rather, they enter politically unstable contexts with less risky modes of entry or by targeting a host country with support from and/or good relations with the firm's home country (Delios and Henisz 2003a; López-Duarte and Vidal-Suárez 2013; Slangen and van Tulder 2009). In new institutionalism, firms do not adopt any systematic approach to political risk management, and their control over political risk is the outcome of isomorphic decisions (Rodriguez *et al*. 2005). Some decisions may occasionally help to gain control over political risks. In the national business systems approach, control over political risk is possible if firms enter countries with similar institutional frameworks, where they may benefit from existing approaches to political risk management (Quer *et al*. 2012).

Nonetheless, the domain has limitations. It de-emphasizes the micro-effects of institutions on the political risk strategies and practices of firms. Furthermore, its greater emphasis on the macro-context at the expense of the micro-context is linked to the conceptualization of institutions as sources of political risk and of firms as actors that react passively to political risk, but cannot influence the political environment and avail of its opportunities. Apart from Robertson and Watson (2004), this perspective implicitly follows the idea of environmental determinism (Hannan and Freeman 1984, 1989), suggesting that environments determine firms and the latter cannot control the former.

The national business systems perspective takes for granted the negative role of political uncertainty in institutions. Indeed, the empirical research in this domain lags the wider institutional scholarship in its conceptualization of institutions (such as governments, regulatory systems and cultures) as constraints, and not instruments that create value, in the political environment. This view dominates research into institutions such as trade associations and NGOs (Dahan *et al*. 2006; Doh and Teegen 2002; Lawton *et al*. 2017; Rajwani *et al*. 2015; Tan and Wang 2011). However, with few exceptions (e.g. Murtha and Lenway 1994; Ring *et al*. 2005), political risk studies remain silent about the positive effects of institutions (Duanmu 2014; Kwok and Tadesse 2006).

Neither does the domain question the need to avoid political risk (Chung and Beamish 2005; Habib and Zurawicki 2002; Mudambi *et al*. 2013). Consequently, political risk strategies are considered mainly at the level of market entry decisions, without elaborating on what happens when firms have already made investments and must stay in a specific host country (Desbordes 2007; García-Canal and Guillén 2008; Lu *et al*. 2014).

Finally, studies claiming that political risk can be controlled are in a minority (Kolstad and Wiig 2012; Meschi and Riccio 2008). Consequently, the question as to how firms invest into, and remain in, political risky countries, has not been fully addressed.

### *Domain 2: Resources and capabilities*

Some scholars have explored political risk management via the lens of resources and capabilities (e.g. Alon and Herbert 2009; Demirbag *et al*. 2011; Frynas *et al*. 2006; Getz and Oetzel 2009; Hadani and Schuler 2013; Holburn, 2001; Holburn and Zelner 2010; Jiménez 2010; Jiménez and Delgado-García

2012; Jiménez *et al*. 2014; Mellahi *et al*. 2011; Moon and Lado 2000; Oetzel and Oh 2013; Poynter 1982) (see Table 4). A common feature of studies in this domain is that they place an emphasis on firms and their internal sources of political risk management. The importance of incorporating political risk into firm strategy is not novel. For example, Kobrin (1979, 1982) suggested that firms should conduct systematic assessments of political risk to make more accurate decisions about future investments. Yet it is the resources and capabilities perspective which turned to the internal environments of firms as a starting point of systematic political risk management.

Another characteristic of this domain is the possibility to use political resources and capabilities in political risk management. This idea is not new, as it was first suggested in relation to industries. Specifically, Fainsod (1940) concluded that political resources, such as building political coalitions, help industries to attain their goals. However, the resources and capabilities domain applies this idea to the management of political risk in firms.

The preponderance of scholars in the resources and capabilities stream structure their analyses around a resource-based view (Barney and Arikan 2001; Penrose 1959; Peteraf 1993; Wernerfelt 1984, 1995). This assumes that firms are bundles of political resources and capabilities. The former is defined as 'stocks of available political factors to which the firm gains access' (Holburn and Zelner 2010, p. 1291). Frynas *et al*. (2006) suggest that, like other resources, political resources may fall into three broad categories: physical capital resources (e.g. a firm's nationality as a proxy of the extent of home government protection); human capital resources (e.g. experience of managers in dealing with government officials in emerging economies); and organizational capital resources (e.g. relations between the firm's managers and public-policy-makers).

Political capabilities refer to a 'firm's capacity to deploy or leverage its political resources on an on-going basis' (Holburn and Zelner 2010, p. 1291). For example, access to key policy-makers may be conceived of as an organizational political resource (Frynas *et al*. 2006), whereas an ability to use this access by identifying key political actors and their preferences is a political capability (Holburn, 2001; Holburn and Zelner, 2010; Lawton and Rajwani 2011). Similarly, experience in dealing with government officials is a human political resource (Frynas *et al*. 2006). However, a capacity to use this experience by developing ties with, and exerting sufficient pressure on, government officials to initiate or maintain certain policies, is a political capability (Holburn and Zelner 2010).

The resource-based view of political risk management assumes heterogeneity of political resources and capabilities among firms. Holburn and Zelner (2010) argue that multinational firms differ in political capabilities linked to risk assessment and the management of policy-making processes. The idiosyncrasies in political resource and capabilities endowment stem from the unique experiences of firms (Holburn and Zelner 2010; Jiménez *et al*. 2014; Lawton *et al*. 2013b).

The central argument of the resource-based view suggests that, given their heterogeneity, resources and capabilities affect sustainable competitive advantage and the performance of firms (Barney 2001). Political risk studies suggest that key political resources may be conceived of as sources of superior performance and sustainable competitive advantage because they are valuable, rare and costly to imitate (Holburn and Zelner 2010). Indeed, the most effective political behaviors and experiences are typically covert in nature and, therefore, difficult to emulate (Boddewyn and Brewer 1994; Getz and Oetzel 2009; Oetzel and Oh 2013).

The resource-based view of political risk management addresses the central suggestion via two themes. The first focuses on the effectiveness of political strategies in converting resources and capabilities into outcomes (Jiménez *et al*. 2014; Moon and Lado 2000; Oliver and Holzinger 2008; Puck *et al*. 2013). For example, Oliver and Holzinger (2008) discuss how four political strategies allow for mobilizing firm capabilities to either avoid or reduce political risk (value maintenance objective), or take advantage of political risk (value creation objective). Specifically, firms reduce political risk exposure by following reactive and defensive strategies. With reactive strategies, firms align with the political environment by complying with regulatory standards. With defensive strategies, firms foster influence capabilities to protect their interests through political ties. In contrast, firms seeking to create value from political risk are likely to adopt anticipatory and proactive political strategies. Anticipatory strategies require internal capabilities such as environmental scanning, and predictive capabilities to anticipate public policy changes and resultant opportunities. Proactive political strategies entail influence capabilities, which enable a firm to create value out of political risk by shaping the non-market environment. For example, redefining norms and establishing standards to redefine existing legislation.

Nonetheless, some empirical studies question assumptions of the resources and capabilities domain. First, it seems political resources and capabilities such as experience in a political environment do not always lead to decisions in favor of entering politically risky markets (García-Canal and Guillén 2008). Second, political strategies do not necessarily improve performance. For example, Puck *et al*. (2013) found that strategies of financial incentives, information and constituency-building in emerging economies do not necessary mitigate exposure to, or generate value from, political risk. Rather, they may occasionally lead to a competitive disadvantage.

The second theme of the resource-based perspective cuts across an evolutionary approach by focusing on the process whereby the resources and capabilities of firms change over time (Barnett *et al*. 1994; Karim and Mitchell 2000; Levinthal and Myatt 1994; Oliver and Holzinger 2008; Teece *et al*. 1997). It is worth noting that the first literature stream places greater emphasis on resources and lower-order capabilities whereas, in the second, discussions revolve mainly around higher-order, or dynamic, capabilities needed to sustain competitive advantage in fast-moving market and non-market environments.

The resources and capabilities domain has made several contributions to political risk management research. For instance, it provides the micro-view of political risk. Indeed, the resource-based view complements the earlier focus of industrial organization economics and internationalization studies in the business environment by taking a closer look at political risk via the lens of the firm (Holburn 2001).

Also, the domain reconsiders the traditional view of political risk. It argues that political risk does not necessarily deter investment. Instead, it may be a source of opportunities (Jiménez *et al*. 2014). Therefore, political risk should not be avoided (Holburn and Zelner 2010) and firms can manage political risk to transform it into opportunities (Holburn and Zelner 2010). Indeed, as the center of attention shifted from the macro (business environment) to the micro level (firm), the resource-based view made it possible to question the assumption of multinational passivity in engaging government, and to consider firms as proactive managers of political risk (Holburn 2001; Jiménez 2010; Jiménez and Delgado-García 2012; Jiménez *et al*. 2014). This broadened the scope of research from enquiries into how firms react to political risk (Baglini 1976; Carlson 1969; Eiteman and Stonehill 1973; Green, 1972; Weston and Sorge 1972) to studies of why and how some firms gain advantage through investments in high-risk contexts (Getz and Oetzel 2009; Holburn and Zelner 2010; Oetzel and Oh 2013).

Also, with its assumption about the proactive role of multinationals, the resource-based view has changed the approach of practitioners to political risk management to one of a tool to create and maintain business value (Oliver and Holzinger 2008).

### *Domain 3: Resource dependence*

The resource dependence domain considers the political risk management of a foreign firm in terms of its relationships with and dependence on the resources of other organizations (Holtbrügge *et al*. 2007; Kim 1988), including host governments (Arnoldi and Villadsen 2015; Blumentritt 2003; Blumentritt and Rehbein 2008; Dieleman and Boddewyn 2012; Moon and Lado 2000; Poynter 1982, 1986; Ramamurti 2001; 2003; Vachani 1995), host-country partner firms (Inkpen and Beamish 1997; Liu *et al*. 2016; Yan and Gray 2001), parent firm (Boyacigiller 1990) and NGOs (Nebus and Rufin 2010). Table 4 shows key studies in the domain.

Drawing on resource dependence theory (Hillman *et al*. 2009; Pfeffer and Salancik 1978), this domain makes the following assumptions. First, it assumes that firms are not autonomous (Blumentritt and Rehbein 2008; Dieleman and Boddewyn 2012; Inkpen and Beamish 1997; Liu *et al*. 2016; Pfeffer and Salancik 1978). Instead, they are elements of a network of interdependencies with other organizations (Inkpen and Beamish 1997; Liu *et al*. 2016).

Second, this domain assumes that firms are constrained by their environment (Dieleman and Boddewyn 2012; Hillman *et al*. 2009; Pfeffer and Salancik 1978). It is a source of political uncertainty that has negative impacts on the performance of FDI (Liu *et al*. 2016). Aiming to reduce their political uncertainty, firms are motivated to change their environments (Dieleman and Boddewyn 2012).

The third assumption is that firms can affect their environments to make them more favorable for their economic activities (Hillman *et al*. 2009; Pfeffer and Salancik 1978). They do so by responding to government regulations and decisions (Arnoldi and Villadsen 2015; Blumentritt 2003; Blumentritt and Rehbein 2008; Dieleman and Boddewyn 2012; Moon and Lado 2000; Poynter 1982, 1986; Ramamurti 2001; 2003; Vachani 1995), managing relationships with host-country partner firms (Inkpen and Beamish 1997; Liu *et al*. 2016; Yan and Gray 2001), headquarters (Boyacigiller 1990) and NGOs

and transnational advocacy groups (Nebus and Rufin 2010).

The discussions in the domain revolve around two broad themes. The first examines how resource interdependencies influence political risk effects. Authors agree that resource dependence on host partners poses greater risks to economic outcomes of FDI in contexts with institutional ambiguities, ineffective regulation enforcement and low policy credibility (Blumentritt and Rehbein 2008; Liu *et al.* 2016; Inkpen and Beamish 1997; Nebus and Rufin 2010).

The second discusses how managers cope with political risk by managing resource interdependencies (Arnoldi and Villadsen 2015; Dieleman and Boddewyn 2012; Holtbrügge *et al.* 2007; Inkpen and Beamish 1997). Studies in this domain suggest firms tend to reduce their political risk by following two approaches to the management of interdependencies: a bargaining power approach and a stakeholder approach. The former complements the resource dependence theory (Pfeffer and Salancik 1978) with bargaining theory (Bacharach and Lawler 1981). Studies center on bargaining power as a factor that allows the choice of more effective bargaining strategies (Blumentritt 2003) and helps to attain desired outcomes (Yan and Gray 2001). It considers bargaining power in a dyadic interdependence relationship between the firm and a host-country organization such as government or a partner firm (Blumentritt and Rehbein 2008; Inkpen and Beamish 1997). In this relationship, the firm's bargaining power and resource dependence are the obverse of each other (Choudhury and Khanna 2014; Yan and Gray 2001). Bargaining power increases as the foreign firm gains greater control over vital resources and its resource dependence decreases (Choudhury and Khanna 2014; Yan and Gray 2001). By contrast, the firm's bargaining power becomes weaker when its control over vital resources drops and its resource dependence increases (Choudhury and Khanna 2014). As in the case of firms, bargaining power of host organizations reflects their control over vital resources and their resource dependence (Inkpen and Beamish 1997). To this end, the firm–host organization bargaining is an ongoing resource interdependence relationship whose outcomes depend on resources the two parties have and require from each other (Behrman and Grosse, 1990; Brewer 1992; Inkpen and Beamish 1997).

In comparison, the latter approach combines resource dependence theory (Pfeffer and Salancik 1978) with stakeholder theory (Freeman, 1984). This allows a shifting of the focus from the issue of power in a dyadic relationship, to the complexity of dependence relationships with multiple actors – stakeholders – in the political environment (Donaldson and Preston 1995; Holtbrügge *et al.* 2007; Nebus and Rufin 2010; Ramamurti 2003). The stakeholder approach suggests that dependence on valuable resources and capabilities and its implications for FDI into politically uncertain environments are outcomes of a dialogue with internal and external stakeholders controlling these resources and capabilities (Holtbrügge *et al.* 2007). Such stakeholders may be home governments (Choudhury and Khanna 2014), national and international NGOs such as Greenpeace (Holtbrügge *et al.* 2007), and supranational organizations such as the European Union (Holtbrügge *et al.* 2007).

Both dyadic and multiple interdependencies can be managed by two strategies: risk aversion and risk taking. The former implies firms avoid investing into higher interdependence projects (Liu *et al.* 2016). That is, they opt not to invest in a host country where access to crucial resources depends on a politically unstable government or a partner firm with low credibility (Liu *et al.* 2016). This option echoes the institutional perspective, suggesting that political risk deters FDI. Alternatively, firms undertake FDI with lower interdependence, suggesting greater chances to control critical resources. Lower interdependence may be achieved by reducing links with the resource-controlling entity (e.g. fewer staff and localization of marketing), and developing internal capabilities such as networking and building coalitions for the supply of crucial resources (Inkpen and Beamish 1997; Liu *et al.* 2016; Nebus and Rufin 2010). Nonetheless, risk aversion strategies may result in the loss of business opportunities, raising doubts about the need to reduce political risk (Liu *et al.* 2016). These doubts bring us back to the question of whether political risk should be reduced. To benefit from opportunities, firms may need to accept political risk.

The major contribution of the resource dependence domain is that it revisits the traditional view of political risk from the perspective of resource interdependencies. It agrees that political risk has mainly negative implications for FDI. But it concludes that firms can control political risk by managing interdependence. Furthermore, the approach cautions against opting for risk aversion without consideration of business opportunities (Liu *et al.* 2016).

## Discussion and directions for future research

Our review identifies three distinctive research domains in political risk management: institutions; resources and capabilities; and resource dependence. In Table 5, we compare the three domains and suggest that differences in conceptual assumptions lead to variances in applied approaches to political risk, particularly in the institutions and resources and capabilities domains. However, the resource dependence domain has some common features with both the institutions and resources and capabilities perspectives.

The effectiveness of approaches to political risk management within the three domains may vary across contexts. Table 6 shows how some approaches may be more effective in one environment, whereas others may work better under a different set of conditions. Table 6 also provides examples of how political risk managers may benefit from the three approaches in different contexts.

Our findings also identify shortcomings in existing literature on political risk management, and suggest resultant directions for future research. These limitations stem from four problems: first, theoretical, contextual and structural biases in FDI outcomes of political risk management; second, partial fulfilment of political risk research objectives in each domain; third, failure to establish links and integrate suggestions across the domains; and fourth, the limited scope of research challenging the traditional view of political risk management. We next discuss these four problems, and propose how they may be resolved in future research.

### *Biases in outcomes of political risk management*

*Theoretical biases.* The theoretical perspectives emphasize different outcomes. For instance, most studies deploying an institutional lens (70%) provide empirical evidence of negative impacts, whereas positive impacts account for the largest portion of findings drawing on the resource-based view (63%). In the institutions domain, scholars might explore if, how, when and why the institutional embeddedness of firms and their reactive approaches to political risk influence FDI policies. Borrowing methodologies from similar institutional studies in other disciplines such as economic geography, finance, economics and politics, scholars could benefit from spatial analysis, historical analysis, case studies, longitudinal research, cross-sectional studies and panel data analyses (Henisz 2000; Krifa-Schneider and Matei 2010; Qiu 2005). Future research may also benefit from integrating theoretical lenses from other disciplines. For example, public choice theory in political science could inform how public policy outcomes depend on firms' capabilities in detecting the incentives and constraints of public officials (Chin *et al*. 2000; Getz 2001). Similarly, the resource dependence domain does not explain how the management of resource interdependencies influences public policies (Arnoldi and Villadsen 2015; Blumentritt 2003; Dieleman and Boddewyn 2012; Ramamurti 2001). Future research might benefit from collective action theory in economics to explain how firms not only gain access to critical resources, but also avoid a free riding problem by blocking competitors' access to these resources (Olson 1971 [1965]; Oström and Oström 1977).

*Contextual biases.* Empirical research on the implications of political risk for FDI is skewed towards advanced economies (Hadani and Schuler 2013; Jiménez 2010). Studies drawing data from emerging and developing economies are in a minority (Frynas *et al*. 2006; Holburn 2001). This lack of focus on emerging and developing economies may be due to methodological challenges related to the covert nature of political activities in these contexts. The lack of transparency in the political sphere in these economies hinders idiosyncrasies of political resources and capabilities affecting FDI outcomes of political risk (Hadani and Schuler 2013). The relative lack of insight on emerging and developing economies stems from methodological issues. Most research questions are examined through quantitative analyses of secondary data. Obtaining such data can be problematic in the context of emerging and developing economies. For instance, it is not always possible to apply existing indices of political risk. They do not fully capture complexities and salient elements of political systems in emerging and developing economies. For example, Henisz's (2016) Political Constraints' Index measures the likelihood of changes in the policy regime, but does not tap into other aspects of political risk such as terrorism, inter-country political and military conflicts, and nationalism. Also, the existing indices of political risk may contain no entries for some emerging and developing economies. For instance, drawing on a data set of 100 countries, Global Political Risk Services Index (Political Risk Services 2016) does not report data for several economies in Central and

*Table 5. Comparing the domains*

| ID[a] vs. RCD[b] | ID vs. RDD[c] | RCD vs. RDD |
|---|---|---|
| Assumptions | | |
| Conceptualization of political risk<br>ID: equates political risk with political uncertainty – a construct whose probability is unknown.<br>RCD: political risk is a source of opportunities. | Conceptualization of political risks<br>ID and RDD envisage political risk as political uncertainty – a construct whose probability is unknown. | Conceptualization of political risks<br>RCD: political risk is a source of opportunities.<br>RDD: equates political risk with political uncertainty. |
| Origin of political risk<br>ID and RCD: disagree about the origin of political risks.<br>ID: the political environment is the major source of political risk.<br>RCD: a portion of risk originates within the firm too and, therefore, may be triggered by the internal factors including internal activities and resources and capabilities (e.g. relations among employees and managers, political intelligence and monitoring of non-market environment). | Origin of political risk<br>ID and RDD: agree that political uncertainty comes from the external environment of firms.<br>ID: political uncertainty originates in the institutional field.<br>RDD: political uncertainty is a factor of relationships of a foreign firm with other actors in the political environment (e.g. host governments, host partner firms, competitors, society) that influence its access to strategically important resources (e.g. government contracts, license agreements, legitimacy and reputation). | Origin of political risk<br>RCD and RDD: disagree about the origin of political risks.<br>RDD: the external environment is the major source of political uncertainty due to resource interdependencies; yet, it ignores the role of the internal environment.<br>RCD: a large portion of political risk originates in the external environment. However, some risks may be triggered by the firm, be outcomes of its internal processes and heterogeneity of its resources, and be a result of its actions. |
| Implications of political risk<br>ID and RCD: disagree about the implications of political risk.<br>ID: political risks have negative implications.<br>RCD: political risks contain opportunities and, therefore, may have positive effects on firms. This assumption is linked to another assumption: resources and capabilities are assets rather than liabilities of firms. | Implications of political risk<br>ID and RDD: agree that political uncertainty has deterring effects on FDI. | Implications of political risk<br>RCD and RDD: disagree about possible implications of political risks.<br>RCD: political risks may have not only negative, but also positive effects on FDI. Firms may turn risky situations to their favor and generate competitive advantage even in highly unstable markets.<br>RDD: political uncertainty is likely to have negative implications for FDI. |
| Firm–environment interaction<br>ID and RCD: disagree about firm–environment interaction.<br>ID: political environment dominates firms; these can only passively respond to pressures of the environment, but cannot control it; hence, the unidirectional relationship between firms and their environments.<br>RCD: the firm–environment relationship is bidirectional, and firms can influence their political environment too. | Firm–environment interaction<br>ID and RDD: disagree in their conceptualization of the firm–environment interaction and its role in the reduction of political uncertainty.<br>ID: assumes a one-directional relationship between foreign firms and institutional environments. Firms are embedded into their institutional environments, but cannot influence them. The institutional environments affect firms and their FDI. Opaque regulatory environments and underdeveloped judicial and financial systems, corruption and engagement in political conflicts, increase political uncertainty.<br>RDD: assumes a bidirectional relationship (interdependence) between a foreign firm and its political environment. The firm is dependent on other actors in the political environment because those determine its access to important resources. Other actors are not autonomous either and may be dependent on the firm too. | Firm–environment interaction<br>RCD and RDD: agree that firms influence their political environment and therefore manage their exposure to political risks. |
| Approaches | | |
| Having different assumptions about the firm–environment interaction, the two domains follow different approaches to political risk management. | Having different assumptions about the firm–environment interaction, the two domains suggest different approaches to political risk. | Having different assumptions about the implications of political risks, the two domains have different approaches to political risks. |
| ID: Unable to influence their political environment, firms react to political risks but cannot control them; hence political risk management is *reactive* and its primary function is to support market entry–exit decisions only.<br>RCD: being able to influence their environment, firms adopt a *proactive* approach to political risk management. Firms can not only avoid political risk but also benefit from it. | ID: takes a *reactive* approach to political risk. Unable to influence their environments, firms react to, but cannot manage, political risk.<br>RDD: proposes a more *active* approach to political risk. Organizations may attempt to reduce their political uncertainty by managing external interdependencies. However, these attempts may not necessarily be successful and may occasionally lead to new patterns of interdependencies. | RDD: firms aim to reduce their political uncertainty through the management of resource interdependence with other organizations.<br>RCD: adopts a more *proactive* view of the firm's objective. Firms are not necessarily concerned with how to avoid or reduce political risks; instead, they may use political risks in order to avail of opportunities in the non-market and market environments. |

*Notes:* [a]Institutions domain (ID); [b]Resources and capabilities domain (RCD); and [c]Resource dependence domain (RDD).

*Table 6. The impact of approaches to political risk management*

| Reactive approach (Institutions) | Proactive approach (Resources and capabilities) | Active approach (Resource dependence) | |
|---|---|---|---|
| Decisions based on the institutional approach may be more effective in contexts where institutional systems are relatively well-defined and homogeneous across different parts of a country.<br>The approach may be less useful in areas where institutions are very loose (e.g. less developed African economies) and where there is variance of structure and process across different parts of a federal systems (e.g. USA, Germany, Australia or Canada). | The resource-based view of political risk management is likely to bring in better results where the context is highly volatile with weak governmental structures and the institutional system is not clear or is in transition: e.g. in the process of devolution of powers from the central authority units (e.g. national governments), to the lower level administrative units (e.g. states, provinces and counties). | The use of the resource dependence approach makes sense in a context where there exist resources and (inter)dependence relationships between an MNC and other entities in the environment.<br>Dyadic interdependence<br>The approach may be valuable where, owing to factors such as federal structure, ethnic and religious division, and historical development, there is a relative lack of central authority and, thus, norms and behaviors, as well as enforcement of rules and regulations, vary substantially across different parts of a country. In such countries, bargaining of local authorities helps MNCs to integrate into the regions of interest. | Multiple interdependence<br>The approach may also be helpful where an MNC has resource interdependence relationships with multiple stakeholders in the political environment.<br>While considering a FDI in a specific sub-national region of a host country, an MNC may need to bargain not only with the state's local government, but also to consider the interests of other stakeholders in the political environment, such as local communities. |
| Examples: Russia and China<br>The two countries have relatively strong central government authorities and national institutional systems with significant homogeneity across regions. The political risks for a foreign MNC will depend on its integration, or embeddedness, into the host institutional systems. For instance, despite the steadily increasing importance of local governments, the performance of MNEs in China has been highly dependent on their connections to the central government (De Fouloy 2014; Shen 2004). Similarly, the federal reform in Russia strengthened the power of the central government vis-à-vis federal governments by aggregating them into federal districts with envoys directly appointed by the president of the Russian Federation (Kordonsky 2016). | Examples: Venezuela, Ecuador, Nicaragua, Ukraine and the UK.<br>Reliance on resources and capabilities (e.g. adaptive capability) may be particularly effective in volatile contexts (e.g. Venezuela, Ecuador, Nicaragua and Ukraine) (De Villa *et al*. 2015).<br>Also, the approach may be helpful for MNCs operating in the UK, owing to devolution-driven transitions in the institutional systems of Scotland, Wales and Northern Ireland (O'Neill 2014). | Examples: India and Mozambique<br>In India, each state has its unique institutional organization (Aggarwal, 2005; Sridharan, 2003). In Mozambique, provinces differ in terms of political orientation. Some provinces (e.g. those in the center of the country) are under greater influence and control by the political opposition to the central government and the ruling party (Beck 2014). MNCs may reduce political risks surrounding their direct investments in these contexts by accruing bargaining power vis-à-vis local governments. A failure to reach a bargain with local authorities may result in withdrawal of investment. | Example: India and Mozambique<br>Consider the example of Coca Cola, which had to shut down a bottling plant in Mehdiganj. Following protests from the local community against Coca Cola's industrial waste discharge and its use of scarce groundwater resources, the local government revoked its permission for the company to run bottling operations in the area (*Ecologist*, 2014). To ensure continuance of its onshore gas exploration operations in the Inhaminga, Pande and Temane areas of central Mozambique, South African company Sasol designed a project to engage with local communities in creating biofuels, e.g. oil from Jatropha plants (Borras *et al*. 2013). |

Eastern Europe (e.g. Slovenia, Estonia, Latvia, Lithuania, Belarus and Moldova) and Africa (e.g. Mozambique, Madagascar, Burundi, Somalia and Guinea-Bissau).

Nor is it always possible to design new indices of political risk in emerging and developing economies. Indeed, corporate political activities in such economies are rarely institutionalized (e.g. reported) formally, and scholars may have no secondary data to work with (Lawton *et al*. 2013a). However, where secondary information is not readily available, a possible solution might be using data from reports published in advanced economies on the political activities of their multinational corporations (MNCs) in emerging and developing economies (Lawton *et al*. 2013a).

Resource dependence research appears less contextually biased than studies with an institution or resources and capabilities lens. A possible reason is that many of the phenomena in this domain (for instance, obsolescing bargaining power and high resource dependence on coercive regimes) are more salient in emerging and developing economies. Studies of Enron's Dabhol power project and US and European MNEs in India (Ramamurti 2003; Vachani 1995), on the Salim Group in Indonesia (Dieleman and Boddewyn 2012), on Unión Fenosa's electricity distribution subsidiaries in the Dominican Republic (Nebus and Rufin 2010) and MNEs in China (Arnoldi and Villadsen 2015) support this view. Meanwhile, some studies caution about possible methodological challenges for future enquiries in some emerging and developing economies (Dieleman and Boddewyn 2012; Ramamurti 2003; Vachani 1995). For instance, it may be difficult to address the complexity and dynamics of resource dependencies in economies where scholars do not have connections with key political actors and where political activity has not been institutionalized (Dieleman and Boddewyn 2012). For example, Dieleman and Boddewyn (2012) demonstrate how their longitudinal case study benefited from unique access to the key political decision-makers in one of the largest corporations in Asia – Salim Group.

*Structural biases: external outcomes.* Only two studies reported information on external outcomes. In both cases, the external outcomes were represented by changes in levels of corruption (Kwok and Tadesse 2006; Robertson and Watson 2004). We suggest that future research might address questions such as: How does political uncertainty stimulate firms to engage in CPA intended to change or secure specific public policy outcomes? And how do differences in institutional configurations determine corporate political strategies? Future studies adopting a resources and capabilities lens might explore whether and how political resources and capabilities help firms to influence public policy outcomes. Also, how are political resources and capabilities deployed within a broader set of non-market initiatives?

External outcomes received less attention in the resource dependence domain. Only one study explored how firms may influence the decisions of policy-makers (Vachani 1995). Future studies might explore how complex and changing resource dependencies between firms and their environments factor changes in the public policy environment (e.g. corruption) and decisions to change or maintain public policies.

*Structural biases: internal outcomes.* Scholars explored how political risk affects FDI decisions around entry, mode of entry, ownership and exit (Arregle *et al*. 2013; Desbordes 2007; Gaur and Lu 2007; Mudambi *et al*. 2013) and organizational performance (e.g. Cherchye and Verriest 2016; Li and Vashchilko 2010). However, this literature stream has not fully considered organizational performance. Several internal indicators were explored, including market performance (Christmann *et al*. 1999), the security of assets – the protection of human resources and intellectual property and the defense of facilities – (Li and Vashchilko 2010), and financial performance (Cherchye and Verriest 2016; Lee and Hong 2012). However, external indicators were overlooked. Future studies might consider external dimensions of organizational performance suggested in Mellahi *et al*. (2016). For instance, organizational reputation, stakeholder relationships, positive investor assessment, consumer loyalty and attractiveness to perspective employees.

### *Partial fulfilment of objectives in domains*

Of the three domains, the institutions approach has been discussed more frequently by scholars, whereas the resources and capabilities and resource dependence perspectives require greater research attention. Also, our review suggests that each of the three domains does not fully address its objectives in political risk research. For example, the institutions domain does not fully address its objective to explain the role

of institutions in exposure to and management of political risk (Cherchye and Verriest 2016; Delios and Henisz 2000; Witt and Lewin 2007). Similarly, the resources and capabilities domain renders only partial explanation of the role of political resources and capabilities in exposure to and management of political risk (Holburn and Zelner 2010; Jiménez *et al*. 2014). Similarly, the resource dependence domain does not fully explicate the role of resource interdependencies in the effects of political risk on FDI performance (Arnoldi and Villadsen 2015; Holtbrügge *et al*. 2007; Liu *et al*. 2016; Vachani 1995). We argue that effective political risk management depends on how successfully firms balance their internal and external interdependencies.

### *Failure to integrate the domains*

Rousseau *et al*. (2008) suggest it is difficult to know what we know, because research communities often do not, and sometimes cannot, talk to each other. As in the wider domain of non-market strategy research (Mellahi *et al*. 2016), this problem stems from the lack of multi-theory or multi-domain inquiries. We argue that, despite different perspectives, the political risk management research domains are not in conflict. Instead, their insights are complementary. The resources and capabilities domain can inform the institutions domain about how firms might use political resources and capabilities to avoid negative, and activate positive, impacts of institutions on FDI in politically risky contexts. The resource dependence domain can inform the institutions domain about possible effects of resource interdependencies on institutions. Also, resource interdependencies may lead to isomorphic practices. Further work is needed to understand these effects.

### *Challenging the traditional view*

The traditional view of political risk management suggests that political risk has negative implications for FDI, is difficult to control, and should be avoided (Green and Smith 1972; Root 1968; Truitt 1970). The three domains identified in this paper adopt different approaches to this traditional perspective. Except for a small number of studies (Delios and Henisz 2003b; Kolstad and Wiig 2012; Meschi and Riccio 2008), the institutions domain largely aligns with the traditional view that exposure to political risk undermines FDI performance and, therefore, should be avoided (Habib and Zurawicki 2002; Hiatt and Sine 2014; Lee and Hong 2012; Li and Vashchilko 2010; Soule *et al*. 2014). Furthermore, it concludes that political risk is difficult to control (Blake and Moschieri 2017; Lu *et al*. 2014). However, this skeptical view of political risk limits the overall scope of research inquiries. First, FDI decisions (usually not to invest) were discussed mainly at the market entry stage, without consideration of how firms use institutions to deliver FDI, create value and remain in politically risky contexts. Second, FDI decisions were discussed via the lens of political risk, without considering the role of business opportunities. In practice, firms must balance political risk with business opportunities. Firms avoiding investment in politically risky contexts may lose business opportunities (Shrader *et al*. 2000). We argue that addressing these issues will broaden the scope of future research in the institutions domain.

The resources and capabilities domain diverges from the traditional view of political risk management. It contends that political risk has positive implications for FDI, and can be managed by taking advantage of political resources and capabilities (Holburn and Zelner 2010; Jiménez *et al*. 2014; Oliver and Holzinger 2008). This approach mainly considers situations where firms benefit from political resources and capabilities and take political risks while entering, and staying in, host countries. However, it does not discuss situations where political resources and capabilities transform from assets into liabilities, and firms opt not to invest or decide to divest (Sun *et al*. 2011). To broaden the scope of future research, scholars need to revisit assumptions about the positive value of political resources and capabilities (García-Canal and Guillén 2008; Puck *et al*. 2013).

The resource dependence domain only partially diverges from the traditional view. For instance, political risk has negative implications for FDI (Liu *et al*. 2016; Vachani 1995). Also, political risk should be avoided, provided this does not cause the loss of opportunities (Liu *et al*. 2016). Furthermore, firms can and should control political risk by managing resource dependencies (Holtbrügge *et al*. 2007; Inkpen and Beamish 1997; Nebus and Rufin 2010). This moderately skeptical view limits the research scope to either situations where firms opt for risk aversion strategies and reject FDI with high resource dependencies (e.g. Inkpen and Beamish 1997; Liu *et al*. 2016; Nebus and Rufin 2010) or situations where firms take risks and accept FDI with high resource dependencies in politically uncertain contexts, but over time become more exposed to political risks, e.g. obsolescing bargaining power (Liu *et al*.

2016; Vachani 1995). However, further work is needed to explore situations where high resource interdependence does not increase political risk over time. For example, political risk is likely to remain at the same level, or even lower, when the host and home governments decide to cooperate. Consider a case where a firm's access to critical resources depends on a politically unstable host government. Nevertheless, its risks due to this dependence may reduce over time if the home government offers the host government critical resources such as funding, market access, and support in international negotiations.

## Conclusions

This paper focuses on political risk research, exposure and management in relation to FDI. We use a strategic management lens and an international business context. We contribute to the literature by integrating research advances that challenge traditional views: political risk has negative implications, should be avoided and cannot be controlled (Faber and Brown 1980; Green and Smith 1972; Root 1968; Truitt 1970). We argue that these advances may be organized into three theoretical domains – institutions, resources and capabilities and resource dependence – that have implications for FDI decisions.

The institutions domain does not substantially challenge the traditional view of political risk. As it centers on macro-effects of political risk, it assumes greater power of institutions over firms, such that institutions influence firms, but firms lack control over institutions and political risk stemming from the institutions (Habib and Zurawicki 2002; Hiatt and Sine 2014; Lee and Hong 2012; Li and Vashchilko 2010; Soule *et al*. 2014). Because this domain assumes that firms cannot control political risk, it places greater emphasis on risk aversion decisions such as avoiding investments into, or exiting, politically risky markets (Blake and Moschieri 2017; Lu *et al*. 2014). We argue that this domain follows a reactive approach to exposure to, and management of, political risk in FDI.

In contrast, the resources and capabilities domain

tive. As it takes a micro-view of political risk and its management, the focus shifts from institutions to firms, suggesting greater power of firms (Holburn and Zelner 2010; Jiménez *et al*. 2014; Oliver and Holzinger 2008). Consequently, firms have the possibility to influence the political environment and manage their political risk (Holburn 2001). This suggests that firms may not necessarily be repelled by political risk (Levinthal and Myatt 1994; Moon and Lado 2000). Instead, they may take advantage of it as an opportunity for future growth (Oliver and Holzinger 2008). This domain informs us about how firms mobilize political resources and capabilities to evade and, where possible, benefit from political risk. It explains why some firms invest in politically risky markets instead of avoiding them, as suggested in the institutional domain. We argue that this domain adopts a proactive approach to political risk management.

The resource dependence domain partially disagrees with the traditional view. In common with the institutions domain, it assumes that firms are embedded into, and constrained by, the political environment (Liu *et al*. 2016; Vachani 1995; Yan and Gray 2001). Following this assumption, it suggests that political uncertainty has negative implications for firm FDI and, as such, should be avoided (Dieleman and Boddewyn 2012; Ramamurti 2001; 2003; Vachani 1995). Nonetheless, like studies in the resources and capabilities domain, this school of thought assumes that firms can affect their environment too and, therefore, can control their political risk (Arnoldi and Villadsen 2015; Blumentritt and Rehbein 2008; Dieleman and Boddewyn 2012). It further informs us how firms control political risk by managing their resource interdependencies with other actors in the political environment. We suggest that this domain follows an active approach to political risk management.

Finally, we argue that the efficacy of the three approaches may vary across different national contexts. In some countries where institutional systems are well defined, the institutions approach may work better. In contrast, managers may abstain from embeddedness into institutional systems by opting for the resources and capabilities approach in highly volatile contexts. Alternatively, the resource dependence approach may be preferred where firms find themselves in a situation of resource interdependence with other actors in the political environment.

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