

The Political and Legal Environment

Learning objectives:

- To learn how differing types of political system function, in terms of governmental processes, societies and business interactions.
- To gain a critical appreciation of democracy's progress in differing national environments.
- To assess political risk, both internally and internationally.
- To appreciate the nature and significance of diverse national legal systems, as well as their interactions with both regional and international legal frameworks.
- To assess legal risk for international managers, including both national and international implications.

■ Authoritarian government rests on rule by a political elite that has power for the time being. Such a regime usually holds on to the power by suppressing dissent, often by force. Democratic governments tend to be accountable to the people, instead, by relying on free and fair elections. The will of the leadership thus dominates in an authoritarian regime, whereas democracy relies on representative institutions like the elected legislatures.

■ Political risks comprise the uncertainties associated with location and exercise of power within a country as also from the forces outside its borders. There are two kinds of political risks, therefore:

- **Internal political risks** include corruption, weak rule of law, social fragmentation etc. that are common in developing economies. Since most economic opportunities too arise in these countries, many international businesses balance the extra costs associated with these risks against the potential benefits such opportunities offer.



and especially operate in strategic sectors such as energy) and "state-controlled" enterprises with varying ownership structures, some are listed companies others with the state as the majority shareholder. State players are a growing force in the global economy, notably China and the resource-rich Middle Eastern states.

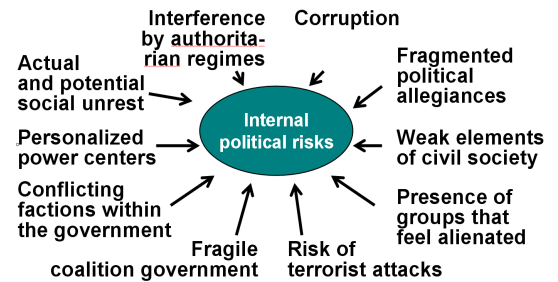
Legal framework, from national to international:

- The **national legal system** provides the substantive law and court structure which most directly affect businesses.
- MNEs operating in different countries are subject to the national law in each. Legal systems in democratic societies where the rule of law prevails tend to be more transparent than those in authoritarian countries.
- **Regional frameworks** and **international law** overlap with national law in several spheres, such as environmental protection

Legal risk internationally

- **Legal risk** arises when a company needs to launch legal action (such as to enforce a contract) or when it must defend itself against legal action.
- In FDI and outsourcing strategies, the MNE is involved in webs of legal relations in foreign environments, e.g.,
 - Contracts with suppliers, customers, subcontractors
 - Liability under environmental protection law
 - Liability for dangerous products
 - Liability for industrial accidents
 - Liability under employment law and health and safety law

Authoritarianism	versus	Democracy
Power determines law; constitution on paper only	Rule of law	Constitutional framework; equality before law
Detention without charge; few rights for accused; imprisonment for political dissent	Civil rights	Right to a fair trial; no detention without charge; torture prohibited
Restrictions on association, expression and any activity contrary to the official line	Political rights	Right to vote and stand for office; freedom of association and expression
Elections with little or no choice of the candidates	Elections	Regular elections; one person/one vote; monitoring for irregularities, intimidation
Courts are an administrative arm of government	Court system	Independent judiciary; transparent process
Press controlled by the state; restricted reporting	Freedom of the press	Editorial and reporting independent from government



- **External political risks** concern inter-governmental relations and include benefits like trade agreements and investments as also the risks such as disputes that affect transborder trade and business. Terrorist threats too would be included here. By informing themselves of a country's historic relations with others, international managers can manage the range of possible external risks.

■ **Role of governments in economic activities:** Traditional liberal market view is one of minimum intervention, but recent financial crises have prompted direct financial support by US, European and the other governments worldwide. These are in addition to the "state-owned" enterprises (they are limbs of the government

