

# ASSESSING GEOPOLITICAL RISK: A MULTI-LEVEL APPROACH FOR MANAGERS OF MULTINATIONALS<sup>1</sup>

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**Abstract:** Geopolitical risk is a major concern for managers of multinationals around the globe. However, managers often find it challenging to assess how geopolitical risk can impact their multinational's operations. Hence, this article offers a multi-level approach for the holistic assessment of geopolitical risk that can help managers identify their multinational's degree of real exposure. This multi-level approach integrates insights of over one hundred managers of multinationals, and involves conducting a tailored examination at the supranational, international, national, industry, and firm levels of analysis to factor geopolitical risk more effectively into strategic decision-making.

**Keywords:** Geopolitics, Geopolitical risk, Risk assessment

## INTRODUCTION

The Russia-NATO conflict and U.S.-China strategic competition highlight the importance of geopolitics in international business. Because geopolitical issues, such as these, tend to create disruptions to international relations, supply chains, and trade, which impact multinationals' operations. As the world shifts from a unilateral order to a multipolar system, geopolitical issues are expected to rise (Kobrin, 2015, 2017). According to the U.S. National Intelligence Council's report *Global Trends 2040: A More Contested World*, "no single state is likely to be positioned to dominate across all regions or domains, and...[states] will compete to advance their ideologies, goals, and interests" (U.S. NIC, 2021: 92). Thus, geopolitical risk—the likelihood that wars, terrorist acts, and tensions between states affect the normal and peaceful course of international relations, and in turn, international business (Caldara & Iacoviello, 2018)—is likely to increase in the next two decades.

This setting makes geopolitical risk a major concern for managers of multinationals around the globe. However, managers often find it challenging to assess how geopolitical risk can impact their multinational's operations. One reason is that routinary assessments of risk exposure tend to focus on local political conditions. Another reason is that geopolitical risk is complex. Hence, this article goes beyond local politics and tackles geopolitical complexity by offering a multi-level approach for the holistic assessment of geopolitical risk.

This multi-level approach integrates insights of over one hundred managers of multinationals, who have been and continue to be challenged by geopolitical risk. These managers collaborated in co-creation workshops for advancing the assessment of geopolitical risk. During these workshops, by sharing their insights, these managers identified relevant factors to evaluate at multiple levels of analysis, which in turn, were structured into a multi-level approach for assessing geopolitical risk.

## WHY A MULTI-LEVEL APPROACH FOR ASSESSING GEOPOLITICAL RISK?

A multi-level approach for assessing geopolitical risk is pertinent as it enables the consideration of unique characteristics of a multinational's operations to provide a tailored analysis of its exposure (De Villa, Rajwani, & Lawton, 2015). As managers explained, "*through a multi-level approach, we can overcome general assessments of geopolitical risk designed to serve all by developing a customized assessment that best serves the case of our particular multinational.*" This is key as all multinationals are not exposed to the same degree of geopolitical risk, since their unique characteristics can either increase or decrease their degree of real exposure (Kobrin, 1982, 2017). In other words, while a geopolitical issue can generate a high level of risk for some multinationals, and

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be portrayed as posing a threat, other multinationals may experience a low level of risk or even encounter opportunities.

One example within the U.S.-China strategic competition, is the ban installed in 2019 by the U.S. government over Huawei. The U.S. government accused Huawei of using its products to spy on other countries, generating possible security threats due to its deep ties with the Chinese government. As a result of the ban, Huawei smartphones were suddenly unable to offer Google apps. Despite by 2018 Huawei had conquered the second position in the worlds’ smartphone market ahead of Apple, the ban disrupted Huawei’s success, causing at least US\$30 billion in annual losses to its smartphone business (Pan, 2021). In contrast, other multinationals benefited from the ban. Samsung’s operating profit for 2020 rose nearly 60% to its highest level in two years (Song, 2020), and Apple became the top-selling smartphone brand in China in 2021, reaching the world’s largest smartphone market leadership for the first time since 2015 (Bloomberg, 2022).

**APPLYING A MULTI-LEVEL APPROACH FOR ASSESSING GEOPOLITICAL RISK**

As the case of the Huawei ban illustrates, assessing the degree of real exposure of a multinational to geopolitical risk is key to identify challenges and opportunities. Over one hundred managers concluded that, “*this can be achieved by applying a multi-level approach that involves the examination of the supranational, international, national, industry, and firm levels of analysis,*” as summarized in Figure 1. To assess each of the factors included at the different levels of analysis, examples of practical questions and potential sources of information are provided in Table 1.

1. Ability of supranational organizations to mediate and resolve political tensions or conflicts between countries	<b>Supranational level</b>
2. Political relations between countries	<b>International level</b>
3. Dependence between countries on natural resources, food supplies, technologies, and others	
4. Development by countries of technologies, weapons, or others that can redefine their power and influence	
5. Political orientations and agendas of governments	<b>National level</b>
6. Business-government relations	
7. Effects throughout value chain	
8. Stakeholders	<b>Industry level</b>
9. Types of operations	<b>Firm level</b>
10. Political capabilities	

**Figure 1: Multi-level Approach for Assessing Geopolitical Risk**

At the supranational level, managers agreed that, “*a critical factor is the ability of supranational organizations to mediate and resolve political tensions or conflicts between countries, as this affects the likelihood of escalation of geopolitical risk.*” For instance, the United Nations (UN) is committed to maintaining international peace and security, and developing friendly relations among nations. However, the extent to which this organization is able to effectively mediate and resolve

political tensions or conflicts between countries has been different in each case. For example, in Iraq’s occupation of Kuwait in 1990, the UN used resolutions and armed forces, and achieved the liberation of Kuwait. However, in Russia’s assault on Ukraine in 2022, Russia used its UN veto to defend its assault. This weakened the UN’s ability to counter Russia’s aggression.

At the international level, managers explained that, *“political relations between countries play an important role in augmenting or mitigating the effects of political tensions or conflicts on multinationals.”* For instance, upon the threat of China’s invasion of Taiwan and the cutting of supply of Taiwan’s Semiconductor Manufacturing Corporation (TSMC), political ties between Taiwan, the U.S., and Japan enabled this multinational to open plants in the U.S. and Japan. This shows how cooperative political relations between countries can mitigate potential geopolitical risk, in this case, for TSMC and semiconductor reliant multinationals. At the international level, managers also highlighted that, *“dependence between countries on natural resources, food supplies, technologies, and others, can pose challenges for multinationals.”* For example, Germany’s dependence on Russian gas enabled the Russian government to use Gazprom, the Russian majority state-owned energy multinational, to affect Germany by reducing its gas supply in retaliation to sanctions imposed on Russia for its assault on Ukraine. This challenged multinationals operating in Germany, such as Mercedes-Benz and BASF, to implement measures to reduce and replace gas consumption.

At the national level, managers suggested that, *“tracking how the development by countries of technologies, weapons, or others, can redefine their power and influence is important.”* For instance, Russia and the U.S. possess over 90% of all nuclear weapons. Yet, China is confirmed by the Federation of American Scientists to be in a substantial expansion of its nuclear weapons arsenal. This developing change in the balance of power and influence among countries may have implications for multinationals around the globe. At the national level, managers also pointed out that, *“the political orientations and agendas of governments play a critical role in the intensification or weakening of political tensions or conflicts between countries.”* For example, in Russia, political power is concentrated in the authoritarian government of President Vladimir Putin. He leads an expansionist agenda, which caused political tensions between Russia and Ukraine to escalate into Russia’s assault on Ukraine. This affected businesses in both countries, and had consequences for multinationals worldwide. At the national level, managers also recognized that, *“understanding business-government relations and their effects on multinationals is useful.”* For instance, in response to foreign firms massively leaving Russia after its assault on Ukraine, the Russian government reacted with a plan to nationalize foreign firms that intend to close their operations in Russian territory. Nationalization increases the immediate costs for foreign multinationals considering leaving Russia.

**Table 1: Examples of Practical Questions and Potential Sources of Information**

Levels of Analysis	Factors	Practical Questions	Potential Sources of Information
Supranational level	1.Ability of supranational organizations to mediate and resolve political tensions or conflicts between countries	To what extent are the countries and actors involved in political tensions or conflicts willing to have mediation, comply with terms of settlement, and resolutions from the United Nations or other supranational organizations?	United Nations (articles on the effectiveness of the UN’s mediation, settlements, resolutions, and interventions in past conflicts)  Countries’ membership status and past commitment to supranational organizations
International level	2.Political relations between countries	What is the distance in relations between the governments of the countries where the MNE has operations and the governments of the countries experiencing political tensions or conflicts?  To what extent does the level of distance in political relations augments or mitigates the effects of geopolitical issues on the MNE’s operations?	Media coverage on political relations between countries (useful to check media outlets from the different countries involved to contrast perspectives)  Assessments from internal staff

	3. Dependence between countries on natural resources, food supplies, technologies, and others	In what degree are the MNE's countries of operations dependent on the resources, food supplies, or technologies of other countries?  What are the implications of such dependencies?	International trade data from national statistics agencies, trade promotion or industry associations, chambers of commerce, Trade Map  Assessments from external experts and internal staff
National level	4. Development by countries of technologies, weapons, or others that can redefine their power and influence	Are the countries involved in political tensions or conflicts, or other countries, developing technologies, weapons, or others that can redefine their power and influence?  How can this affect the geopolitical context, and in turn, the MNE's operations?	Technical Intelligence, Federation of American Scientists, Intelligence Resource Program, peace and security organizations, external experts
	5. Political orientations and agendas of governments	What are the political orientations and agendas of the governments of the countries involved in political tensions or conflicts, and of the governments of the countries where the MNE has operations?  How can their political orientations and agendas impact the geopolitical context and the MNE's operations?	The World Fact Book, media coverage, political programs and discourses, political analysis
	6. Business-government relations	How are the relations of government with the business sector in the countries involved in political tensions or conflicts?  Are foreign firms, firms from a specific home country or industry, likely to be targeted by any of the governments involved in political tensions or conflicts?	Media coverage on the enforcement of contracts and public policies, or the use of discriminatory policies and expropriation
Industry level	7. Effects throughout value chain	How can political tensions or conflicts between countries affect the value chain of the MNE's operations?  What alternatives can be identified to overcome potential disruptions in the MNE's operations?	Assessments from external experts and internal staff
	8. Stakeholders	What are the major concerns of shareholders in regard to political tensions or conflicts between countries?  What are the expectations of stakeholders regarding the responses of the MNE to political tensions or conflicts between countries?	Shareholder focus groups or meetings  Stakeholder focus groups, established communication channels, social media
Firm level	9. Types of operations	How can the different types of MNE operations be affected by political tensions or conflicts between countries?  What types of operations are vulnerable and how can they be made more resilient?	Assessments from internal staff
	10. Political capabilities	What political capabilities have been developed by the MNE?	Assessments from internal staff

		How can these be useful to mitigate threats or exploit opportunities derived from the geopolitical context?	
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At the industry level, managers highlighted that, “*it is key to identify how political tensions or conflicts between countries affect the value chains of multinationals.*” For example, Russia’s assault on Ukraine has led to shortages on the availability of fertilizers, affecting the food industry. This has driven many multinationals to actively search for alternative suppliers, while others like Dangote Fertilizer have seized this business opportunity. At the industry level, managers also suggested that, “*identifying stakeholders’ concerns and expectations in multinationals’ responses to political tensions or conflicts between countries is useful to inform choices.*” Indeed, in various industries, strong pressures from investors and consumers after Russia’s assault on Ukraine, influenced many Western multinationals’ choice to take out their investments or pause sales in Russia.

At the firm level, managers explained that, “*identifying how multinationals’ different types of operations can be affected by political tensions or conflicts between countries is necessary.*” For example, political tensions between Venezuela and Colombia due to divergent political ideologies between former Presidents Hugo Chavez and Alvaro Uribe, confronted Colombian multinationals in Venezuela with the risk of being the target of expropriation. Nonetheless, this risk was higher for production plants than for distributions offices. This was because production plants owned more assets, and in turn, their expropriation implied higher costs. At the firm level, managers also considered that, “*identifying the development of multinationals’ political capabilities is important to determine the extent to which they can be useful to mitigate threats or exploit opportunities derived from the geopolitical context.*” For example, Airbus managed through its well-developed political capabilities, during the establishment of sanctions to Russia for its assault on Ukraine, to have the EU avoid sanctioning Russian titanium while it accelerated searching for other suppliers.

## CONCLUSIONS

Applying this multi-level approach for the holistic assessment of geopolitical risk can help managers identify their multinational’s degree of real exposure, overcoming potentially misleading general assessments of geopolitical risk. In doing so, managers can respond to growing investor demands that are calling upon multinationals to assess the impact of geopolitical risk on the full scale of their operations (BlackRock, 2022; Thomas, 2022). Moreover, managers can factor geopolitical risk more effectively into strategic decision-making, to better address the challenges or pursue the opportunities they encounter.

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