A Novel Country Classification System for Choosing International Business Locations

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Abstract

This paper introduces a novel country classification system that rates the political economy risks of countries for the purpose of conducting international business. It is intended to provide investors, multinational companies, and business researchers a quick and efficient way of gauging the extent of political, economic, and legal risks associated with doing business in different countries. The study covers over 170 countries and identifies 24 country types. At the extremes are Type 1 countries (least risky) and Type 24 countries (most risky). Overall, the new classification system suggests that political economy risks associated with doing international business are relatively mild in Type 1, Type 3, and Type 4 countries. However, international businesses should temper their investment decisions with caution in Type 19, Type 20, Type 22, Type 23, and Type 24 countries due to high political, economic, and legal risks, especially Types 23 and 24 where these risks are excessive. At the same time, international businesses may want to refocus their attention to Type 11 countries who are now havens for international investments due to drastic reduction in political, economic, and legal risks associated with doing business. The twenty-four country types identified in this new classification system are time-invariant. Thus, countries may move up or down due to improvements or deteriorations in certain aspects of their political economy.

Keywords: legal, international business, political, economic, risks, classification

1. Introduction

Countries have different political, economic, and legal systems. In each country, these systems collectively constitute the political economy. Political economy of a country can either facilitate or hinder multinational companies' ability to conduct business in that country (Gomez and Jomo 1999; Hamilton and Webster 2018; Haggard 2000; Henisz and Zelner 2003; Hill 2016). While international businesses repeatedly demand multifaceted information about the political, economic, and legal systems of countries, existing country classifications treat these systems as mutually exclusive and categorize countries based on one system at a time (Ball 1988; Brooker 2000; Collier 1999; Heilbroner and Boettke 2018; Economist Intelligence Unit 2019; Juri Globe 2019). For instance, Brooker (2000) focuses on political systems and distinguishes between non-democratic and democratic regimes. Heilbroner and Boettke (2018) focus on economic systems and classify countries into free market systems and centrally planned systems. Juri Globe (2019) focuses on legal systems and categorizes countries into five different legal systems. These siloed classification systems, though useful in some settings, are often fragmented and inefficient for international businesses. For instance, if a business in one country plans to expand its operations into another country, the business has to scramble for information from copious sources to determine the nature of political economy of that country and associated risks. The time and resources used to sift through these fragmented sources of information ultimately increases transaction costs.

The purpose of any classification system is to allow users to access information in an efficient and timely manner with the least amount of frustration as possible (Bruno and Richmond 2003). Thus, the goal of this paper is to reorganize the existing siloed classification systems to develop a more composite country classification system based on the political economy of countries. In particular, the study proposes a simple framework that classify countries depending, simultaneously, on the type of political, economic, and legal systems to provide international businesses a quick and efficient way of gauging the extent of political, economic, and legal risks associated with doing business in different countries.

The rest of the paper is organized as follows. Section 2 discusses the different political, economic, and legal systems. Section 3 describes the methodology for classifying countries. Results from the classification system are also presented and discussed in Section 3. Section 4 concludes.

2. Political, Economic, and Legal Systems

2.1 Political Systems

The political system of a country is the set of formal institutions that constitute a government or a state (Heslop 2018). The most common political systems are republic, democracy, monarchy, communism, and totalitarianism. Some are variants of others (democracy from republics) while others are antithesis to others (totalitarianism antithesis to democracy). Furthermore, each has its strengths and weaknesses and possess different types of risks and challenges to international businesses.

Because globally countries are moving towards democracy, the political system of a country is often defined by the extent of democratic principles prevailing in that country. The Economist Intelligence Unit Democracy Index (EIU-DI) provides a snapshot of the current state of democracy worldwide for 167 independent countries. This covers almost the entire population of the world and the vast majority of the world's countries. The EIU-DI is based on five categories: electoral process and pluralism, civil liberties, the functioning of government, political participation, and political culture. Based on a country's scores on a range of indicators within these categories, the country is then itself classified as one of four types of regimes: full democracy, flawed democracy, hybrid regime, and authoritarian regime. Full democracies are countries in which basic political freedoms and civil liberties are respected. Full democracies are also characterized by a political culture conducive to the flourishing of democratic principles. Flawed democracies are countries that have free and fair elections. Even if there are problems (such as infringements on media freedom), basic civil liberties are respected. Hybrid regimes are countries in which elections have substantial irregularities that often prevent them from being both free and fair. Also, government pressure on opposition parties and candidates may be common. In countries with authoritarian regimes, political pluralism is absent or heavily curtailed. Many countries in this category are outright dictatorships.[1]

In this study, we used the EIU-DI (2019) to define the degrees of democracy, i.e., more democratic and less democratic. *More democratic countries* are full democracies plus flawed democracies. *Less democratic countries* includes hybrid regimes and authoritarian regimes. Political systems of 11 countries are not included in the EIU-DI. These countries are Greenland, Somalia, South Sudan, Falkland Islands, Grenada, Kiribati, Cape Verde, Vatican, Andorra, Western Sahara, and Kosovo. Thus, we rely on data from the 2019 CIA World Factbook (CIAWFB) to determine their respective political systems. According the CIAWFB (2019), the political system of South Sudan is in transition. For this reason, it is not included in the list. Also excluded from the list are the disputed territories of Western Sahara. Table 1 reports the list of 176 countries based on our simplified definition of political systems (more or less democratic).

2.2 Economic Systems

The study defines economic systems based on the degree of individual or government involvement in economic decision making. Thus, economic system is synonymous to the degree of freedom in a country. Relying on Freedom Houses Freedom in the World (FH-FIW) classification, we parsed countries into *market economy* (free), *command economy* (not free), and *mixed economy* (partially free). The data comes from the Freedom House (2019) FIW report which evaluates the state of freedom in 195 countries and 14 territories during calendar year 2018. Each country and territory is assigned between 0 and 4 points on a series of 25 indicators, for an aggregate score of up to 100. These scores are used to determine two numerical ratings, for political rights and civil liberties, with a rating of 1 representing the freest conditions and 7 the least free. A country or territory's political rights and civil liberties ratings then determine whether it has an overall status of free, partly free, or not free. The methodology is derived from the Universal Declaration of Human Rights and applied to all countries and territories, irrespective of geographic location, ethnic or religious composition, or level of economic development.[2] Comoros, Fiji, and Hong Kong are not included in the FH-FIW index. Thus, we used data from globalEDGE (2019) to determine their economic systems. Table 2 reports the list of countries by economic systems.

2.3 Legal Systems

Generally, there are three types of legal systems: common law, civil law, and theocratic law. Common law is based on tradition, precedent, and custom (Hill 2016). It is derived from the English common law and is found in many parts of the English-speaking world such as Australia, Canada, England, the United States, Wales, and

other countries (Sjuggerud 2018). Civil law is based on a detailed set of laws organized into codes. Its origin can be traced to Roman law and is found today in much of continental Europe, Central America, South America, and several other regions. Nations with civil law systems have comprehensive, frequently updated legal codes (USC Law 2019). Theocratic law is a legal system predominantly based on religious teachings. Islamic law (or Sharia law) is the most widespread theocratic law found in varying degrees in some countries in Africa, the Middle East, Central Asia, and South Asia. Other theocratic law systems include the Jewish law (Israel) and Christian law (Vatican).

Building on the three primary types of legal systems, JuriGlobe (2019), the most comprehensive world legal systems database defines five categories of legal systems: common law, civil law, customary law, religious law and mixed law systems; the latter referring to a combination of systems. Because customary laws are typically a subset of common law which broadly encompasses tradition, precedent, and patterns of behavior or customs, we combine customary law with common law and reclassify JuriGlobe's five legal systems into four: *common law*, *civil law*, *theocratic law*, and *mixed components law system*. Table 3 reports the country classification based on the four legal systems.[3]

Table 1. Political Systems (by country)

More Democratic			Less Democratic		
Austria	Greenland	Panama	Afghanistan	Gabon	Nicaragua
Argentina	Grenada	Papua New Guinea	Albania	Gambia	Niger
Australia	Guyana	Paraguay	Algeria	Georgia	Nigeria
Andorra	Hong Kong	Peru	Angola	Guatemala	North Korea
Belgium	Hungary	Philippines	Armenia	Guinea	Oman
Botswana	Iceland	Poland	Azerbaijan	Guinea-Bissau	Pakistan
Brazil	India	Portugal	Bahrain	Haiti	Palestine
Bulgaria	Indonesia	Romania	Bangladesh	Honduras	Qatar
Canada	Ireland	Senegal	Belarus	Iran	Russia
Cape Verde	Israel	Serbia	Benin	Iraq	Rwanda
Chile	Italy	Singapore	Bhutan	Ivory Coast	Saudi Arabia
Colombia	Jamaica	Slovakia	Bolivia	Jordan	Sierra Leone
Costa Rica	Japan	Slovenia	Bosnia Hercegovina	Kazakhstan	Sudan
Croatia	Kosovo	Somalia	Burkina Faso	Kenya	Swaziland
Cyprus	Kiribati	South Africa	Burundi	Kuwait	Syria
Czech Republic	Latvia	South Korea	Cambodia	Kyrgyzstan	Tajikistan
Denmark	Lesotho	Spain	Cameroon	Laos	Tanzania
Dominica	Lithuania	Sri Lanka	Central African Republic	Lebanon	Thailand
Dominican Republic	Luxembourg	Suriname	Chad	Liberia	Togo
Ecuador	Malaysia	Sweden	China	Libya	Turkey
Estonia	Malta	Switzerland	Comoros	Macedonia	Turkmenistan
Falkland Islands	Mauritius	Taiwan	Congo Brazzaville	Madagascar	Uganda
Finland	Mexico	East Timor	Cuba	Malawi	Ukraine
France	Mongolia	Trinidad and Tobago	Dem. Rep. of Congo	Mali	United Arab Emirates
Germany	Namibia	Tunisia	Djibouti	Mauritania	Uzbekistan
Ghana	Netherlands	United Kingdom	Egypt	Moldova	Vatican
Greece	New Zealand	United States of America	El Salvador	Montenegro	Venezuela
	Norway	Uruguay	Equatorial Guinea	Morocco	Vietnam
			Eritrea	Mozambique	Yemen
			Ethiopia	Myanmar	Zambia
			Fiji	Nepal	Zimbabwe

Note. Political systems are defined based on the degree of democracy and classified using the 2019 Economist Intelligent Unit Democracy Index (EIU-DI). More democratic are full democracies plus flawed democracies. Less democratic includes hybrid regimes and authoritarian regimes. Political systems of countries not included in the EIU-DI were determined using data from the CIA World Factbook (CIA-WFB). These includes Greenland, Somalia, South Sudan, Falkland Islands, Vatican, Andorra, Western Sahara, and Kosovo. According the CIA WFB, the political systems of South Sudan is in transition. For this reason, it is not included in the list. Also excluded from the list is the disputed territory of Western Sahara.

Table 2. Economic Systems (by country)

Market Economy			Command Economy		Mixed Economy	
Austria	Guyana	Slovakia	Afghanistan	Qatar	Albania	Lesotho
Argentina	Hong Kong	Slovenia	Algeria	Palestine	Armenia	Liberia
Australia	Iceland	South Africa	Angola	Russia	Azerbaijan	Macedonia
Andorra	India	South Korea	Bahrain	Rwanda	Bangladesh	Madagascar
Belgium	Ireland	Spain	Belarus	Somalia	Bhutan	Malawi
Benin	Israel	Suriname	Burundi	Sudan	Bolivia	Malaysia
Botswana	Italy	Sweden	Cambodia	Swaziland	Bosnia Herzegovina	Mali
Brazil	Jamaica	Switzerland	Cameroon	Syria	Burkina Faso	Mexico
Bulgaria	Japan	Taiwan	Central African Republic	Tajikistan	Colombia	Moldova
Canada	Kiribati	East Timor	Chad	Thailand	Comoros	Montenegro
Cape Verde	Latvia	Trinidad and Tobago	China	Turkey	Cuba	Morocco
Chile	Lithuania	Tunisia	Congo Brazzaville	Turkmenistan	Djibouti	Mozambique
Costa Rica	Luxembourg	United Kingdom	Dem. Rep. of Congo	United Arab Emirates	Dominican Republic	Myanmar
Croatia	Malta	United States of America	Egypt	Uzbekistan	Ecuador	Nepal
Cyprus	Mauritius	Uruguay	Equatorial Guinea	Venezuela	Fiji	Niger
Czech	Mongolia	Vatican	Eritrea	Vietnam	Gambia	Nigeria
Denmark	Namibia		Ethiopia	Yemen	Georgia	Pakistan
Dominica	Netherlands		Gabon		Ghana	Papua New Guinea
El Salvador	New Zealand		Iran		Guatemala	Paraguay
Estonia	Norway		Iraq		Guinea	Philippines
Falkland Islands	Panama		Kazakhstan		Guinea-Bissau	Saudi Arabia
Finland	Peru		Laos		Haiti	Serbia
France	Poland		Libya		Honduras	Sierra Leone
Germany	Portugal		Mauritania		Hungary	Singapore
Greece	Romania		Nicaragua		Indonesia	Sri Lanka
Greenland	Senegal		North Korea		Ivory Coast	Tanzania
Grenada			Oman		Jordan	Togo
					Kenya	Uganda
					Kosovo	Ukraine
					Kuwait	Zambia
					Kyrgyzstan	Zimbabwe
					Lebanon	

Note. Economic system is defined based on the degree of individual or government involvement in economic decision making. Using the 2019 Freedom House Freedom in the World (FH-FIW) classification, countries are parsed into market economy (free), command economy (not free), and mixed economy (partially free). FH-FIW assigns each country and territory a score between 0 and 4 points on a series of 25 indicators, for an aggregate score of up to 100. These scores are used to determine two numerical ratings, for political rights and civil liberties, with a rating of 1 representing the most free conditions and 7 the least free. A country or territory's political rights and civil liberties ratings then determine whether it has an overall status of Free, Partly Free, or Not Free. Comoros, Fiji, and Hong Kong are not included in the FH-FIW index. Thus, we used data from globalEDGE to determine their economic systems.

Table 3. Legal Systems (by country)

Common Law	Theocratic Law	Civil Law			Mixed Components		
Australia	Afghanistan	Albania	Germany	Serbia	Algeria	Jordan	Sri Lanka
Andorra	Saudi Arabia	Angola	Greece	Slovakia	Bahrain	Kenya	Sudan
Bhutan	Vatican	Argentina	Greenland	Slovenia	Bangladesh	Kuwait	Swaziland
Canada		Armenia	Guatemala	Spain	Botswana	Lebanon	Syria
Dominica		Austria	Haiti	Suriname	Burkina Faso	Lesotho	Taiwan
Falkland Islands		Azerbaijan	Honduras	Sweden	Burundi	Libya	Togo
Fiji		Belarus	Hungary	Switzerland	Cameroon	Madagascar	Tunisia
Ghana		Belgium	Iceland	Tajikistan	Chad	Malaysia	United Arab Emirates
Grenada		Benin	Italy	Thailand	China	Mali	Yemen
Hong Kong		Bolivia	Kazakhstan	Turkey	Comoros	Malta	Zimbabwe
India		Bosnia Herzegovina	Kosovo	Turkmenistan	Congo Brazzaville	Mauritania	
Ireland		Brazil	Kyrgyzstan	Ukraine	Cyprus	Mauritius	
Jamaica		Bulgaria	Laos	Uruguay	Dem. Rep. of Congo	Mongolia	
Kiribati		Cambodia	Latvia	Uzbekistan	Djibouti	Morocco	
Liberia		Cape Verde	Lithuania	Venezuela	East Timor	Mozambique	
Malawi		Central African Republic	Luxembourg	Vietnam	Egypt	Namibia	
Myanmar		Chile	Macedonia		Equatorial Guinea	Niger	
Nepal		Colombia	Mexico		Eritrea	Nigeria	
New Zealand		Costa Rica	Moldova		Ethiopia	North Korea	
Papua New Guinea		Croatia	Montenegro		Gabon	Oman	
Sierra Leone		Cuba	Netherlands		Gambia	Pakistan	
Tanzania		Czech	Nicaragua		Guinea	Palestine	
Trinidad and Tobago		Denmark	Norway		Guinea-Bissau	Philippines	
Uganda		Dominica Republic	Panama		Guyana	Qatar	
United Kingdom		Ecuador	Paraguay		Indonesia	Rwanda	
United States of America		El Salvador	Peru		Iran	Senegal	
Zambia		Estonia	Poland		Iraq	Singapore	
		Finland	Portugal		Israel	Somalia	
		France	Romania		Ivory Coast	South Africa	
		Georgia	Russia		Japan	South Korea	

Note. The legal systems classification is based on a reclassification of JuriGlobe's five legal systems into common law, civil law, theocratic (religious) law, and mixed law systems. Common law is based on tradition, precedent, and custom. Common law includes customary law. Theocratic law is a legal system predominantly based on religious teachings. Civil law is based on detailed set of laws organized into codes. Mixed law systems refers to a combination of two or more of the other legal systems. Table A1 in the Appendix summarizes the mixed systems components. JuriGlobe database contained no information about the legal system of Kosovo. The information is thus obtained from the European Union Rule of Law Mission.

2.4 Summary of Political, Economic, and Legal Systems

Table 4 summarizes the different types of political, economic, and legal systems described in Sections 2.1 to 2.3. These are the two political systems (more democratic and less democratic), three economic systems (market, command, and mixed), and four legal systems (common, civil, theocratic, and mixed components).

Table 4. Political, Economic, and Legal Systems Summary

Political Systems	Economic Systems	Legal Systems
More Democratic	Market Economy	Common Law
Less Democratic	Mixed Economy	Theocratic Law
	Command Economy	Civil Law
		Mixed Components

Note. Political systems are defined based on the degree of democracy and classified using the 2019 Economist Intelligent Unit Democracy Index. More democratic are full democracies plus flawed democracies. Less democratic includes hybrid regimes and authoritarian regimes. Economic system is defined based on the degree of individual or government involvement in economic decision making. Using the 2019 Freedom House Freedom in the World (FH-FIW) classification, countries are parsed into market economy (free), command economy (not free), and mixed economy (partially free). The legal systems classification is based on a reclassification of JuriGlobe's five legal systems into common law, civil law, theocratic (religious) law, and mixed law systems. Common law is based on tradition, precedent, and custom. Common law includes customary law. Theocratic law is a legal system predominantly based on religious teachings. Civil law is based on detailed set of laws organized into codes. Mixed law systems refers to a combination of two or more of the other legal systems.

3. Methodology and Results

Having carefully delineated the different types of political, economic, and legal systems in the previous section, the study proceeds to classify countries into composite groups. A simple classification system is implemented; one that combines each of the political system with all other economic and legal systems to classify countries. More specifically, with 2 political systems, 3 economic systems, and 4 legal systems, the study identified 24 variant combinations. These variant combinations are referred to as *types*, with Type 1 representing the least risky political economy conditions and Type 24 the most risky political economy conditions. Table 5 shows each of the 24 types with their corresponding countries.

Type 1 countries are more democratic, lean towards market economy, and operate on common law system. Also, they are mostly technology-driven. Type 1 countries include Australia, Canada, Ireland, New Zealand, United Kingdom, United States, Hong Kong, India, and few islands in the Caribbean and Virgin Islands regions. These countries are of the least risk politically, economically, and legally for international business investments. Type 1's polar opposite is Type 24 countries who are less democratic, lean towards command economy, and operate on mixed legal systems. Type 24 countries are quite diverse and include Algeria, Bahrain, Burundi, Cameroon, Central Africa Republic, Chad, China, Congo Brazzaville, Democratic Rep. of Congo, Egypt, Eritrea, Ethiopia, Gabon, Guinea-Bissau, Libya, Mauritania, North Korea, Qatar, Rwanda, Sudan, Swaziland, Syria, Equatorial Guinea, United Arab Emirates (UAE), and Yemen. Except for Bahrain, China, Qatar, UAE, Swaziland, and Cameroon, all Type 24 countries have, at least, in the last decade experienced political instability that have stifled economic growth and thrown their legal systems into disarray making them extremely risky for international business investments. The situation is however changing in Egypt, with a new government and Rwanda with the rise of Paul Kagame as an international hero for reforming the country and making it one of the most attractive FDI destinations in Africa. Other countries, such as North Korea, though it has not experienced political instability, is known for its notorious authoritarian regime. Also, geographically, unlike Type 1 countries that are concentrated in the northern hemisphere, Type 24 countries are spread all over the world.

Between the two extremes are different interesting combinations that includes, for example, Type 11 countries – Colombia, Dominican Republic, Serbia, Hungary, Kosovo, Ecuador, Paraguay, and Mexico – that are more democratic, maintain a mixed economic system, and run on civil law. The political economy of these countries are not the best but they are not the worst either. Also, there are Type 3 countries that are more democratic, operate on market economy and a civil law system. Type 3 contains the largest share of countries: one-fifth of the 176 total. These countries are Argentina, Austria, Belgium, Brazil, Bulgaria, Cape Verde, Chile, Costa Rica, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Greenland, Iceland, Italy, Latvia,

Lithuania, Luxembourg, Netherlands, Norway, Panama, Peru, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Suriname, Sweden, Switzerland, and Uruguay. Type 3 countries are similar to Type 1 countries in so many respects. However, the principal difference is that Type 3 countries are mostly located in Europe and operate on the civil legal system. Furthermore, though risk factors of Types 1 and 3 do not differ much, international investors looking for countries with less litigation costs may want to consider Type 3 countries since their codified legal system makes their laws relatively clear and precise.The full disclosure not only reduces investor uncertainty but also allow investors to be fully aware of ramifications of the laws.

Also similar to Type 1 is Type 9 countries which include Ghana and Papua New Guinea. These countries are more democratic, maintain mixed economy, and operate on common legal system. Their principal risk factor is strong government presence in the economy. While Ghana could also qualify as Type 1 country because Freedom House FIW classification places it under free market economy, Ghana's economy is at best a mixed economy. Indeed, our closer examination of Ghana reveal that the degree of government intervention is quite strong. For instance, the price of goods and services in the country are heavily dictated by the price of petroleum products. The government sets the price of petroleum products and the price of everything else follows accordingly. In 2005, Ghana initiated a petroleum price deregulation policy but till date the government maintains significant control in the pricing of petroleum products. Consequently, we classify Ghana as Type 9 country and not Type 1.

Another interesting group is Type 14, i.e., countries that are less democratic, lean towards market economy, and operate on theocratic laws. Only one country, the Vatican, fits this category. Type 14's counterpart is Type 22 countries who are also less democratic and operate on theocratic laws but maintain a command economic system. These countries are Afghanistan and Saudi Arabia. Risk factors for Afghanistan are however much higher compared to Vatican and Saudi Arabia. Yet another intriguing group is Type 23 countries. These are less democratic, maintain command economy, and mixed components legal system. They also share very similar characteristics to Type 24. However, a main difference is that unlike Type 24 countries, almost all Type 23 countries are oil producing countries heavily concentrated in Central Asia (Uzbekistan, Kazakhstan, Tajikistan, and Turkmenistan) and Eastern Europe (Russia, Belarus, and Moldova). Few Type 23 countries are in Latin America (Nicaragua and Venezuela) and Africa (Angola). The political economy of these oil export-dependent countries is extremely risky and corrupt, but it is unclear whether the presence of oil drives the political economy risks and corruption or whether the political economy risks and corrupt practices are inherent in the cultures of these countries.

Other types with wide dispersion of countries all over the world are Types 4, 12, 19, and 20. For instance, Type 4 countries are more democratic, run on market economy but maintain a mixed legal system. It includes countries such as Botswana, Mauritius, Namibia, Senegal, South Africa, and Tunisia (Africa); Cyprus (Europe); Israel (Middle East); and India, Japan, Mongolia, South Korea, Taiwan, and East Timor (Asia). Type 20 countries on the other hand are less democratic with mixed economy and mixed legal system includes Jordan, Kuwait, Lebanon, and Palestine (Middle East), Bangladesh, and Pakistan (Asia), and Burkina Faso, Comoros, Ivory Coast, Djibouti, Gambia, Guinea, Kenya, Madagascar, Mali, Morocco, Mozambique, Niger, Nigeria, Togo, and Zimbabwe (Africa). Political economy risk factors for Type 4 and Type 20 countries originates from occasional commodity price shocks, persistent red-taped legal practices, and diversified religious practices although these risk factors are more heightened in Type 20 countries than in Type 4 countries.

Some country types do not contain any country. These include Types 5 to 7, all of which combines democratic political system with command economic system, and different legal systems. In theory, democratic political systems are incompatible with command market economy. However, in practice it is likely to have cases where a more democratic country operates under a pseudo-command economy especially during periods of extraordinary circumstances. A case in point is the United States during the 1970s oil crisis when government took a strong role in the economy by rationing several basic necessities and directing private enterprises (Baumeister and Kilian 2016; Gray 1987; DeLong 1997; Ibrahim 1990). In 2018, no country experienced such extraordinary circumstances which perhaps explain why there are no entries in Types 5 to 7. The other exception to the incompatibility principle between democratic political system and command economic system is Somalia, a Type 8 country, which recently became a democratic country after several years of civil war but still maintains a command economy due to the fragile state of the economy. Other types that contain no country or a set of countries are Type 2 (more democratic, market economy, theocratic law); Type 10 (more democratic, mixed economy, theocratic law); Type 13 (less democratic, mixed economy, common law); Type 16 (less democratic, market economy, mixed components legal system); and Type 18 (less democratic, market economy, theocratic law). While Types 2, 10, 13, 16, and 18 contain plausible combinations of systems but currently do not have

countries that fit into them, it is conceivable that in future iterations of this new classification system some country may fall into one of these types.

Table 5. Types with Corresponding Countries

Type	Countries
Type 1 (MD, ME, CML)	Australia, Andorra, Dominica, Falkland Islands, Grenada, Hong Kong, India, Ireland, Jamaica, Kiribati, New Zealand, Canada, Trinidad and Tobago, United Kingdom, United States of America.
Type 2 (MD, ME, TCL)	None.
Type 3 (MD, ME, CVL)	Argentina, Austria, Belgium, Brazil, Bulgaria, Cape Verde, Chile, Costa Rica, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Greenland, Iceland, Italy, Latvia, Lithuania, Luxembourg, Netherlands, Norway, Panama, Peru, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Suriname, Sweden, Switzerland, Uruguay.
Type 4 (MD, ME, MXC)	Botswana, Cyprus, East Timor, Guyana, Israel, Japan, Malta, Mauritius, Mongolia, Namibia, Senegal, South Africa, South Korea, Taiwan, Tunisia.
Type 5 (MD, CE, CML)	None.
Type 6 (MD, CE, TCL)	None.
Type 7 (MD, CE, CVL)	None.
Type 8 (MD, CE, MXC)	Somalia
Type 9 (MD, MXE, CML)	Ghana, Papua New Guinea.
Type 10 (MD, MXE, TCL)	None.
Type 11 (MD, MXE, CVL)	Colombia, Dominican Republic, Ecuador, Hungary, Mexico, Kosovo, Paraguay, Serbia.
Type 12 (MD, MXE, MXC)	Indonesia, Lesotho, Malaysia, Philippines, Singapore, Sri Lanka.
Type 13 (LD, ME, CML)	None.
Type 14 (LD, ME, TCL)	Vatican
Type 15 (LD, ME, CVL)	Benin, El Salvador.
Type 16 (LD, ME, MXC)	None.
Type 17 (LD, CE, CML)	Fiji
Type 18 (LD, CE, TCL)	None.
Type 19 (LD, CE, CVL)	Albania, Armenia, Azerbaijan, Bolivia, Bosnia Herzegovina, Cuba, Georgia, Guatemala, Haiti, Honduras, Kyrgyzstan, Macedonia, Moldova, Montenegro, Ukraine.
Type 20 (LD, CE, MXC)	Bangladesh, Burkina Faso, Comoros, Djibouti, Gambia, Guinea, Iran, Iraq, Ivory Coast, Jordan, Kenya, Kuwait, Lebanon, Madagascar, Mali, Morocco, Mozambique, Niger, Nigeria, Oman, Pakistan, Palestine, Togo, Zimbabwe.
Type 21 (LD, MXE, CML)	Bhutan, Liberia, Malawi, Myanmar, Nepal, Sierra Leone, Tanzania, Uganda, Zambia.
Type 22 (LD, MXE, TCL)	Afghanistan, Saudi Arabia.
Type 23 (LD, MXE, CVL)	Angola, Belarus, Cambodia, Kazakhstan, Laos, Nicaragua, Russia, Tajikistan, Thailand, Turkey, Turkmenistan, Uzbekistan, Venezuela, Vietnam.
Type 24 (LD, MXE, MXC)	Algeria, Bahrain, Burundi, Cameroon, Central Africa Republic, Chad, China, Congo Brazzaville, Democratic Rep. of Congo, Egypt, Eritrea, Ethiopia, Gabon, Guinea-Bissau, Libya, Mauritania, North Korea, Qatar, Rwanda, Sudan, Swaziland, Syria, Equatorial Guinea, United Arab Emirates, Yemen.

Note. Type is a scale that combines political, economic, and legal systems of countries to rate the associated political economy risks of doing business. The scale is from Type 1 (least risky) to Type 24 (highly risky). Political systems consist of More Democratic (MD) and Less Democratic (LD). Economic systems comprise of Market Economy (ME), Command Economy (CE), and Mixed Economy (MXE). Legal systems consist of Common Law (CL), Theocratic Law (TCL), Civil Law (CVL), and Mixed Components (MXC). Political systems are defined based on the degree of democracy and classified using the 2019 Economist Intelligent Unit Democracy Index. More democratic are full democracies plus flawed democracies. Less democratic includes hybrid regimes and authoritarian regimes. Economic system is defined based on the degree of individual or government involvement in economic decision making. Using 2019 Freedom House Freedom in the World (FH-FIW) classification, countries are parsed into market economy (free), command economy (not free), and mixed economy (partially free). The legal systems classification is based on a reclassification of JuriGlobe's five legal systems into four: common law, theocratic/religious law, civil law, and mixed components. Common law is based on tradition, precedent, and custom. Common law includes customary law. Theocratic law is a legal system predominantly based on religious teachings. Civil law is based on detailed set of laws organized into codes. Mixed components refer to a combination of two or more of the other legal systems.

4. Conclusion

Political economy risks associated with conducting international business abound and are difficult to measure or classify in a consistent manner. Existing classification systems are fragmented and often fraught with inconsistencies leaving investors and multinational businesses scrambling for information from copious sources to determine the nature of political economy risks associated with doing business in different countries. The

search of information from prodigious sources is not just inefficient but also expensive to investors and multinational businesses. This paper proposes a new composite country classification system that rates the political economy risks associated with doing business in countries all over the world. It is intended to provide investors and multinational companies a quick and efficient way of gauging the extent of political economy risks for the purpose of conducting international business.

The new system classifies countries into types, a rating scale that combines political, economic, and legal systems of countries to rate the associated political economy risks. The new system is operationalized using 2018 data on 176 countries. Twenty-four country types were identified. At the extremes are Type 1 countries (least risky) and Type 24 countries (most risky). Type 1 countries are more democratic, lean towards market economy, and operate on common law system whereas Type 24 countries are less democratic, lean towards command economy, and operate on mixed legal systems. On the spectrum between these two polar opposites are different intriguing combinations that includes, for example, countries that are more democratic, run on command economy and mixed legal systems (Type 8) and countries that are more democratic, maintain a mixed economy, and operate on civil law (Type 11). There are also Type 14 countries that are less democratic, lean towards market economy, and operate on theocratic laws; Type 15 countries that are less democratic, lean towards market economy, and run on civil law; Type 20 countries that are less democratic, operate on mixed economy and mixed legal system; and several other types.

Taken together, the results from this new classification suggest that political economy risks associated with doing international business are relatively mild in Type 1, Type 3, and Type 4 countries. However, international businesses should temper their investment decisions with caution in Type 19, Type 20, Type 22, Type 23, and Type 24 countries due to high political, economic, and legal risks, especially Types 23 and 24 where these risks are excessive. At the same time, international businesses may want to refocus their attention to countries hitherto considered extremely risky and volatile for business but now have become havens for international investments due to drastic reduction in political, economic, and legal risks associated with doing business in those countries. Most of these countries are Type 11 countries. The results are descriptively valid because they represent the factual accuracy of the political, economic, and legal risks associated with doing business in different countries. In addition, the results satisfy conceptual validity because the conceptual framework and explanations developed from the study fits the data and are, therefore, credible and defensible. We should note however that while the twenty-four country types identified in this new classification system are time-invariant, countries may move up or down due to improvements or deteriorations in certain aspects of their political economy. Thus, a dedicated website accompanies this paper that updates the country list in all the twenty-four types on an annual basis.

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Notes

Note 1. For a full description of the EIU-DI methodology, see Economist Intelligence Unit (2019).

Note 2. For a full description of the FH-FIW methodology, see Freedom House (2019).

Note 3. Detailed composition of mixed components legal systems by country is provide in Table A1 in the Appendix. JuriGlobe database contained no information about the legal system of Kosovo. The information is thus obtained from the European Union Rule of Law Mission (2018).

Appendix

Table A1. Mixed Components Legal System

Country	Mixed Components	Country	Mixed Components	Country	Mixed Components
Algeria	Civil law/ Muslim	Iraq	Civil law/Muslim	Philippines	Common law/Civil law
Bahrain	Muslim/Civil law/Common law	Israel	Civil law/Common law/Jewish/Muslim	Qatar	Muslim/Civil law/Common law
Bangladesh	Muslim/Common law	Ivory Coast	Civil law/ Common law	Rwanda	Civil law/ Common law
Botswana	Civil law/Common law	Japan	Civil law/ Common law	Senegal	Civil law/ Common law
Burkina Faso	Civil law/Common law	Jordan	Civil law/Muslim/ Common law	Singapore	Common law/Muslim
Burundi	Civil law/ Common law	Kenya	Common law/Muslim	Somalia	Muslim/Civil law/Common law
Cameroon	Civil law/Common law	Kuwait	Muslim/Civil law/Common law	South Africa	Civil law/Common law
Chad	Civil law/ Common law	Lebanon	Civil law/Muslim	South Korea	Civil law/ Common law
China	Civil law/ Common law	Lesotho	Common law/Civil law	Sri Lanka	Civil law/Common law
Comoros	Civil law/Muslim	Libya	Muslim/Civil law	Sudan	Muslim/Common law
Congo Brazzaville	Civil law/Common law	Madagascar	Civil law/ Common law	Swaziland	Civil law/ Common law
Cyprus	Common law/Civil law	Malaysia	Muslim/Common law	Syria	Civil law/Muslim
Dem. Rep. of Congo	Civil law/ Common law	Mali	Civil law/ Common law	Taiwan	Civil law/ Common law
Djibouti	Civil law/Muslim/Common law	Malta	Civil law/Common law	Togo	Civil law/ Common law
East Timor	Civil law/Muslim/ Common law	Mauritania	Muslim/Civil law	Tunisia	Civil law/Muslim
Egypt	Muslim/Civil law	Mauritius	Civil law/Common law	United Arab Emirates	Muslim/Common law
Equatorial Guinea	Civil law/ Common law	Mongolia	Common law /Civil law	Yemen	Muslim/Civil law/Common law
Eritrea	Civil law/ Common law /Muslim	Morocco	Muslim/Civil law	Zimbabwe	Civil law/Common law
Ethiopia	Civil law/ Common law	Mozambique	Common law /Civil law		
Gabon	Civil law/ Common law	Namibia	Common law/Civil law		
Gambia	Muslim/Common law	Niger	Civil law/ Common law		
Guinea	Civil law/ Common law	Nigeria	Common law/Muslim		
Guinea-Bissau	Civil law/ Common law	North Korea	Civil law/ Common law		
Guyana	Common law/Civil law	Oman	Muslim/Common law/Civil law		
Indonesia	Civil law/Muslim/ Common law	Pakistan	Muslim/Common law		
Iran	Muslim/Civil law	Palestine	Civil law/Muslim		

Note. Mixed law systems is the fourth legal system and refers to a combination of two or more of the other three legal systems, i.e., common law, civil law, and theocratic law.

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