Foreign direct investment risks

Finance

Some of the factors that cause political instability include government interference, violence, and terrorism and guerilla groups.

According to Schmidt (1986), he defines political risk as applications by the host country's government that constrains the operation of an investment. He subdivided political risks into three different risks: Investors therefore always consider these factors before investing in a foreign country, a country with a history of persistent political instability will be avoided or if they feel that there is a possibility of occurrence of political instability.

An investor will consider the risk of business exposure in a foreign country; the investor may fear that there will be the risk of exposing the operations of a business in a foreign country which will lead to competition from other firms in the host country.

When skilled labor is available in a foreign country then the investor will invest in that country. The investor may be forced to train workers in the host country who may expose the operations of the firm leading to competition in that country.

In some other countries there will be the availability of cheap labor which will encourage investors to invest in that country, in some countries labor may be very expensive and the investor is not allowed to import laborers, this may be because the government of the host country has set these conditions.

Another factor to be considered before deciding on where to invest in the stability of a currency of a country, if a currency fluctuates against the major currency by a large range then it wouldn't be good to invest in that country. For a firm to invest in a foreign country it has to convert its capital currency into the currency of the host country, in case that countries currency

devalues against their own currency then they will lose a lot of money.

B. Infrastructure:

Good support infrastructure such as good transport network and communication will be an advantage to an investor such that if such support infrastructure exists the higher the possibility that there will be foreign direct investment in a country.

Foreign investors also fear that they may invest in foreign countries and lose a lot of money if they decide to close down their operations, an example is where a firm may invest much on infrastructures such as land and buildings and heavy machinery that may be difficult to liquidate once they want to close down their investment in the foreign country. Due to the fact that these assets cannot be moved from one country to another the investor loses.

In conclusion, we can say that political instability will cause a firm to not to invest in country, the firm will also consider the risk associated with exposure of the operations of the firm in the foreign country, the firm will not invest in country where it is required to hire laborers from the host country and train them for the operations of the firm. Most foreign investors prefer to employ laborers from their own country but this faced with conditions set by host countries.