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## A TOOL TO MANAGE COUNTRY RISK

Ridzwan Aminuddin, manager, Country-Check, a recently launched initiative from World-Check; in an exclusive interview to CRO.

**CRO:** What were the major drivers for designing this service?

**Ridzwan:** During 2006, World-Check CEO David Leppan received several queries from compliance officers regarding a compliance-based jurisdictional risk indicator covering all countries and territories worldwide. Upon closer inspection, it seemed the general consensus was that there was no standardised way for financial institutions to gauge 'country risk', and that such a service could add value to a range of institutional risk management processes. Country-Check was thus engineered to meet the market demand for a jurisdiction-specific risk indicator.

Most institutions' in-house risk management models and processes have evolved over time. Traditionally, financial institutions that already have in-house country risk models in place use open-source information such as Transparency International's Corruption Index and Freedom House Press Freedom Report's values as source data. These and



Ridzwan Aminuddin

similar sources of information should work well as generally accurate indicators of country risk, however the means by which they are combined to obtain country risk scorings is often non-standardised and highly subjective. This leads to country risk ratings that are unable to withstand regulatory scrutiny or validation.

Country-Check seeks to overcome this problem by providing a service that enables users to aggregate information sources in

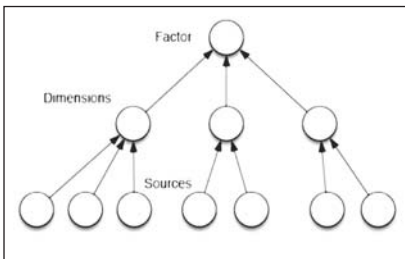
a standardised, methodologically verifiable and transparent manner. Our system methodically aggregates country data from 88 public sources found on the Internet. Users can tailor their focus by selecting or deselecting included sources, and use our aggregation engine to generate quality country risk ratings.

**CRO:** Who are the target clientele for this service?

**Ridzwan:** The service is so designed as to add value to all institutions that need to mitigate jurisdictional risk. It is presently being marketed to the financial industry, but we are already exploring other verticals as we move forward. Given the nature of country risk, the possibilities for targeting other industries are virtually endless.

**CRO:** Are all the risk factors that form the Country-Check Master Index obtained from established public sources, as in the case of World-Check database?

**Ridzwan:** Yes, it only uses data



from reputable and well established open sources of information available on the Internet. Sources range from data from the United Nations, CIA Factbook, Polity IV Democracy Ratings and Freedom House, to name but a few.

The number of sources currently being aggregated is 88, but this number is continually added to, as we scour the Internet for country-related information that meets our quality requirements. We have automated monitoring of all these 88 sources in real-time. This means that any changes in the original source values will be reflected in the Country-Check system very quickly, eradicating the need to manually monitor the sources for updates, as is the case when one uses a traditional in-house country risk model.

**CRO:** Your website talks about dimensions, factors and parameters. Could you please explain these?

**Ridzwan:** Our system derives a score (master index value) for each country based on the aggregation of all the source data available for this jurisdiction. Let me explain some of the key terms that are a part of our methodology.

At the lowest level is what we call a 'source' which is nothing but a country-specific public dataset published online by a specific

organisation. We only use that data which is either in a quantitative form or is in a form suitable to be transformed into a quantitative scale without any ambiguity or loss of precision. The system uses only those sources which have measures for more than one country. That is, we do not use sources that provide single measures for a single country.



David Leppan, CEO, World-Check

'Country-Check is the result of two and a half years of dedicated research and development work. World-Check is extremely pleased to be launching this groundbreaking country risk index in September, and remains committed to continue investing in similar projects to support the industry.'

We do have sources that measure the same attribute. These measures are normally independently observed, and therefore do not always use the same scale. For instance, one source may have counts of crude oil production in terms of how many thousands of barrels are produced per day, whereas the other might measure it by gallons

per year. Our transformation algorithms automatically transform and merge the two scales and its corresponding values. The resultant values (by country) are stored and referred to as dimension scores. A dimension is an abstract piece of terminology used to describe and hold the aggregated score of sources that essentially measure the same attribute. Examples of dimensions include civil rights, gross domestic product (GDP), number of terrorist attacks, etc.

Dimensions can be further aggregated upwards to a final 'factor level'. Again, factors are abstract placeholders that store the aggregated scores of dimensions that may be grouped according to a higher-level grouping. We currently feature three umbrella factors, namely political, economical/financial and security/criminality. All dimensions found in the system would fall under either one of these factors, and each dimension's scores would contribute to the parent factor's aggregated scores. The aggregation paths and functions of each of these entities are illustrated in our methodology graph. This graph explains how sources, dimensions and factors are aggregated and are finally combined to obtain a master index score for a particular country.

**CRO:** While reliable estimates for some of the factors like average earnings, country risk (export credits), country/public debt, GDP, military expenditure etc are easily available, how do you calculate a number for dimensions like economic freedom, competitiveness, sanctions, armed conflict, military

influence etc?

**Ridzwan:** Let me categorically state that Country-Check does not create or provide any source information. All of the raw data that is used by us originates from open-source information publishers, which I mentioned earlier.

There are sources which provide statistical or quantitative measures for traditionally qualitative dimensions that you mention. You can find sources that measure dimensions such as economic freedom and competitiveness. For example, The World Economic Forum features a 'Competitiveness Index' and Heritage Foundation provides an 'Economic Freedom Index' which serve as appropriate qualitative datasets. Country-Check continually scours the Internet to provide users with a plethora of country risk related sources provided by reputable organisations.

**CRO:** Why do you place so much emphasis on using open-source data?

**Ridzwan:** We believe that using open-source data brings about two distinct advantages.

The first is that we can be assured that the data is of high quality, as these organisations dedicate a lot of time, money and effort in

providing accurate and up-to-date information. Secondly, we believe that the use of a variety of reliable sources renders the resultant risk index values fair and, critically, highly bias free.

**CRO:** How do you assign default weights for arriving at index scores?

**Ridzwan:** Our beta version offers users the option to select the 'Country-Check Default Weight Set' for index calculations. This weight set has been calibrated to provide measures for overall risk, and acts as a starting point for many users, who wish to begin using the tool, but do not wish to analyse and weigh all sources provided individually. It also acts as a good starting point for users who wish to customise weight sets, but only wish to adjust selected sources or dimensions.

These weights have been generated using a proprietary algorithm that takes the following considerations into account namely published political and country risk theories, number of countries each source covers, the relative authority and reputation of a source and the entity publishing it. For instance, some sources have measures for only 5 countries, whereas some have measures for all 244 jurisdictions that we cover. Obviously the latter are assigned higher weight.

**CRO:** What has been the response from your existing customers?

**Ridzwan:** User feedback on our beta version has generally been very positive. The system has undergone rigorous testing by a group of key industry experts prior to the soft launch of the beta version. Within a month of the beta launch, more than 1,150 user accounts had been registered, confirming the demand for reliable jurisdictional risk intelligence.

**CRO:** What uses do you anticipate for this service?

**Ridzwan:** Anticipated uses include country profiling and analysis, foreign market expansion, credit risk management, and financial management and planning. For tax havens and jurisdictions that do not comply with international anti-money laundering (AML) and know your customer (KYC) standards, country risk becomes a critical risk indicator and an early warning system against credit, legal and reputational risk.

**CRO:** When is the commercial version expected to be released?

**Ridzwan:** Version 1.0 is to be released on September 10, 2008. Several of the academics involved in its development will be giving presentations at the launch event, which will be held in London. ■



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