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Master’s thesis

A comparative analysis of country risk of Bosnia and Herzegovina, Croatia, Serbia and Slovenia

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U skladu sa članom 54. Pravila studiranja za I, II ciklus studija, integrisani, stručni i specijalistički studij na Univerzitetu u Sarajevu, daje se

IZJAVA O AUTENTIČNOSTI RADA

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Sarajevo, 12. juli 2023. Potpis studenta/studentice: Nejla Huskić

ABSTRACT

Country risk has become a major concern for the international financial community and investors due to political changes and the spread of globalization. Country risk analysis began in the 1970s when countries began to expand their businesses and activities to other countries. This led to losses due to default due to war conflicts, mismanagement, and political instability. With the advancement of technology, country reports were more detailed and statistical techniques were used to create a "score" or rating for each country. Different tools and agencies have been developed to measure and forecast country risk and assist investors in making decisions. Rating agencies are considered to be of great help in today's world, as any investor can give a loan to anyone anywhere in the world. Besides private companies, rating agencies also assess the creditworthiness of government and public institutions. Some of the numerous ways to measure and evaluate country risk include credit rating agencies, economic indicators such as inflation, growth rates, level of unemployment, level of corruption. All these measures can provide information on a country's stability, political stability, governments, and social stability of a certain country. In addition, expert opinions such as analysts and mark participants can help assess country risk based on their knowledge and experience and by using qualitative and quantitative data they have. There is also a multivariate analysis which uses a combination of indicators and data from a variety of sources to generate a comprehensive measure of country risk.

One of the terms often mentioned while researching the topic of country risk is country risk premium (CRP). The country risk premium is a key component of country risk analysis. Country risk analysis helps investors to make informed decisions about where to invest their money and helps to manage the risk of investment by considering a range of economic, political, and social factors that can impact the stability and sustainability of the national economy. The results of country risk analysis are used to determine the country's risk premium, which provides a valuable tool for managing investment risk in a rapidly changing global economy. The purpose of the paper is to analyze and compare country risks for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia, highlighting the importance of country risk evaluation and its assessment in global markets. It looks at country risk reports and analysis for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia. It also looks at credit rating agencies' reports and rates for these four countries. It focuses on strengths and weaknesses of each country, compares them to political, economic, and financial factors, and looks into country risk premium calculated by Damodaran.

KEY WORDS: Country risk, political risk, financial risk, economic risk, rating agencies, country risk premium

SAŽETAK

Rizik zemlje postao je glavna briga međunarodne finansijske zajednice i investitora zbog političkih promjena i širenja globalizacije. Analiza rizika zemlje počela je 1970-ih kada su zemlje počele širiti svoje poslovanje i aktivnosti na druge zemlje. To je dovelo do gubitaka zbog neizvršenja obaveza zbog ratnih sukoba, lošeg upravljanja i političke nestabilnosti. Sa napretkom tehnologije, izvještaji o zemljama su bili detaljniji, a statističke tehnike su korištene za kreiranje "skora" ili ocjene za svaku zemlju. Razvijeni su različiti alati i agencije za mjerenje i predviđanje rizika zemlje i pomoć investitorima u donošenju odluka. Rejting agencije se smatraju od velike pomoći u današnjem svijetu, jer svaki investitor može dati kredit bilo kome bilo gdje u svijetu. Pored privatnih kompanija, rejting agencije ocjenjuju i kreditnu sposobnost državnih i javnih institucija. Neki od brojnih načina mjerenja i procjene rizika zemlje uključuju agencije za kreditni rejting, ekonomske indikatore kao što su inflacija, stope rasta, nivo nezaposlenosti, nivo korupcije. Sve ove mjere mogu pružiti informacije o stabilnosti zemlje, političkoj stabilnosti, stabilnosti vlasti i društva određene zemlje. Osim toga, mišljenja stručnjaka poput analitičara i učesnika u ocjenjivanju mogu pomoći u procjeni rizika zemlje na osnovu njihovog znanja i iskustva i korištenjem kvalitativnih i kvantitativnih podataka koje imaju. Postoji i multivarijantna analiza koja koristi kombinaciju indikatora i podataka iz različitih izvora kako bi se stvorila sveobuhvatna mjera rizika zemlje.

Jedan od pojmova koji se često spominju prilikom istraživanja teme rizika zemlje je premija za rizik zemlje (CRP). Premija rizika zemlje je ključna komponenta analize rizika zemlje. Analiza rizika zemlje pomaže investitorima da donesu informisane odluke o tome gde da ulože svoj novac i pomaže u upravljanju rizikom ulaganja uzimajući u obzir niz ekonomskih, političkih i društvenih faktora koji mogu uticati na stabilnost i održivost nacionalne ekonomije. Rezultati analize rizika zemlje se koriste za određivanje premije rizika zemlje, što predstavlja vrijedan alat za upravljanje rizikom ulaganja u globalnoj ekonomiji koja se brzo mijenja. Svrha rada je analizirati i uporediti rizike zemlje za Bosnu i Hercegovinu, Hrvatsku, Srbiju i Sloveniju, naglašavajući važnost procjene rizika zemlje i njegove procjene na globalnim tržištima. U njemu se razmatraju izvještaji o riziku zemlje i analize za Bosnu i Hercegovinu, Hrvatsku, Srbiju i Sloveniju. Također se razmatraju izvještaji agencija za kreditni rejting i stope za ove četiri zemlje. Fokusira se na snage i slabosti svake zemlje, upoređuje ih sa političkim, ekonomskim i finansijskim faktorima i razmatra premiju rizika zemlje koju je izračunao Damodaran.

Ključne riječi: Rizik zemlje, politički rizik, finansijski rizik, ekonomski rizik, rejting agencije, premija za rizik

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1. INTRODUCTION

1.1. Topic and problem of the research

The topic of this research paper is country risk, more precisely a comparative analysis of country risk of Bosnia and Herzegovina, Croatia, Serbia, and Slovenia. Throughout the years, country risk has become one of the main topics of concern for the international financial community and investors. Political changes, which arose because of the fall of communism and the beginning of globalization, resulted in an immense amount of external capital flowing into the emerging markets of Africa, Asia, Eastern Europe, and Latin America (Ramcharran, 1999). All of this led to a faster spread of globalization and greater interconnection and allowed for an increase in foreign direct investments, international lending and new capitalist countries started to operate on an international scale. However, investors realized that an open market and increased mobility of the capital can be risky and could lead to bigger problems in the international financial sector. Given all of this, country risk and its assessment became vital for all international businesses across the globe. Hence, different tools and agencies started to measure and forecast country risk and various instruments to assist investors in making their decisions.

As we were trying to find similar works and country analysis for these countries, we realized that actually, this topic has not been researched enough and detailed assessment of country risk as such has not been conducted for the chosen countries. It can be difficult to find current and accurate information on various risk factors for different countries. Research papers are less accurate and reliable when there is not enough data, or data is inconsistent. We frequently came across papers that had nothing to do with economics when looking up country risk. This is one of the issues with this kind of research because the term "country risk" is still not widely accepted and because different words are frequently used to describe the same or similar terms.

Another problem is that country risk analysis involves a lot of subjective judgments and assessments, and different researchers and institutions have a different methodology and approach to country risk analysis. This subjectivity can lead to variations in the results and make it challenging to compare, as everyone has a different judgment on these factors. Additionally, country risk is rapidly changing and is constantly facing various challenges across the countries. Factors such as economic fluctuations, political instability, geopolitical events, even natural disasters can all affect the country risk of a certain country. The challenge of trying to predict and forecast these changes remains a challenge. The last problem, which is tied with the issue of subjective judgment is that there is no standardized methodology for doing the country risk analysis and assessing the country risk. Lack of standardization leads to different results which cannot be compared.

1.2. Goal of the thesis and hypotheses

Goals of this paper are to research the literature on country risk, analyze and compare country risk analysis for BiH Croatia, Serbia and Slovenia, analyze all components of composite country risk, political, economic, and financial risk, define which one is predominating, and to see how country risk has changed for Croatia and Slovenia since they entered EU. Based on the defined problem and subject of research, we defined the following three hypotheses for this research:

1. BiH has higher country risk than Croatia, Serbia, and Slovenia.
2. Political risk is predominant in BiH and Serbia.
3. Country risk of Croatia started to decrease once they became EU member state.

1.3. Methodology

In this research paper, we will analyze country risk of Bosnia and Herzegovina, Croatia, Serbia, and Slovenia. Main methods are quantitative and qualitative analyses. We will assess three risk indices - the political, economic, and financial. We will define more in detail these risk ratings later in the paper. For this research, the main source of information and secondary data will come from reliable sites such as The World Bank, Coface, The World Factbook (CIA) and other reports and articles from various rating agencies, which are stated in references section. To make these analyses more transparent, we will take into consideration a longer period. So, we will investigate the data from 2007 until today, looking more closely at 2007, 2013 and 2021 as the reference years. This period will include Global Financial Crisis, but also entrance of the Croatia into European Union. We will see more in detail developments of these countries but also their downturns.

1.4. Thesis Structure

This research paper consists of five parts. In the first part of the paper is the theoretical part in which we will define risk, country risk and look a bit more into risk classification and risk assessment and also see why investors decide to invest outside their country and we finally, we define country risk. In the second part of the paper, we talk more about country risk analysis, ways to measure country risk and techniques of assessing country risk. We also discuss country risk assessors, rating agencies and define country risk premium. The third part of this paper is the literature review, where we see how and what have different research throughout the years found out about the country risk and country risk analysis and in what way have, they conducted country risk analysis.

The fourth part is the main part of the paper, the empirical research. We discuss reports and analysis of country risk for these four countries and see what the key strengths and weaknesses of each country are. Besides country risk reports and analysis for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia we also look at credit rating agencies’ reports and their rates for these four countries. In the tables below we see the score for each country done by Standard and Poor’s (S&P), Moody’s. After looking at different aspects of these four countries we compare them and show closely political, economic, and financial factors which are taken into consideration when calculating country risk for a specific country. We look closely at these factors and take 2007, 2013 and 2021 as reference years as this will give us a more comprehensive picture of the situation in each country.

We also compare data for country risk premium calculated by Damodaran, as an important aspect of country risk for these four countries. Finally, we present results and findings from all the collected and presented data and discuss the set hypothesis. We draw conclusions about the abovementioned hypothesis and discuss possible shortcomings and limitations we encountered while doing this research. In the end, we also shortly discuss potential directions which can be used for expanding this research.

2. RISK, RISK CLASSIFICATION AND RISK ASSESSMENT

What is risk? How many risks are there? How can we avoid the risk? The human race deals with different kinds of risk on an everyday basis. It is an inevitable and indispensable detail of everyday life, whether private or business. The intensity of risk may be small or big and the consequences insignificant or fatal. We deal with risk in various life situations, such as insurance, health, information technology, human services, finances and more. Risk is often defined as a possibility of loss or harm occurring from some type of internal or external exposure. There are various definitions of risk, but they all have two things in common: uncertainty of outcome and potential loss, as one of the possible outcomes. Often risk is identified to have the same meaning as uncertainty; however, there is a difference between these two terms: if we do not know for sure what will happen, but we know the probability of it happening, then there is a risk. However, if we do not know the probability, then there is uncertainty. Risk presents the possibility that things which we planned will not happen.

For example, if you are investing in stocks, risk is the possibility of losing your investments. Therefore, what you expected to gain can be different from what you gained.
Figure 1. presents one of the most important and essential concepts in finances: in order to have a higher return, you need to take on a bigger risk. The lower the risk, the lower potential return is. From Figure 1, we can see that even when risk is equal to zero, there is still some return.

Figure 1: Risk-return relationship

Source: MI Research Team (2018.), The Risk-Return Trade-Off, Retrieved from: https://modelinvesting.com/articles/the-risk-return-trade-off/

As we deal with risk in various situation, different types of risk can arise. However, in financial theory risk that affects value of asset is divided into systematic and unsystematic risk. Systematic risks, also known as un-diversifiable risk and market risk, can have an impact on the entire economic market and not just on a particular asset, company, or industry. Measure of systematic risk is beta. Market beta is always equal to one and we cannot eliminate nor decrease this risk by ourselves.

Systematic risk includes following types of risk:

- interest rate risk - risk that interest rates will fluctuate, i.e., rise and drive down the value of a security. For example, imagine we want to borrow money from the market, but interest rate has increased. This means we will now have to pay higher interest than before, and this investment will now cost more than originally planned.
- inflation risk – risk that the future real value of your investment will decline due to inflation.
- currency risk – or exchange rate risk, is a risk of the change in price of one currency against another.

- liquidity risk - is the risk of not being able to trade your assets without a loss, and
- country risk which we will explain more in detail in the next part of the paper.

We cannot change these types of systematic risk nor diversify them, and therefore investors try to avoid it as much as possible or try to protect themselves against these risks. On the other hand, we have unsystematic risk which can be reduced with diversification i.e., by investing in a range of different companies, assets or industries which do are not directly connected, and therefore is also often called "diversifiable" risk. Unsystematic risk is sometimes also called specific or residual risk because it affects specific company, asset, or industry. There are two categories within unsystematic risk: business and financial risk. Business risk is associated with a particular company and relates to its ability to reach set goals, while financial risk is associated with demographic risk, liquidity, and credit risk, etc. For examples, unsystematic risk includes losses caused by labor problems, entry of a new competitor into a market, workers strike in the company, or even due to weather conditions.

2.1. Defining country risk

As explained in the previous part of the paper, country risk belongs to the group of systematic risks. But how do we define it? Defining country risk is not as easy as one would think. The problem arises from the fact that there is no agreement on what makes up the overall country risk. It gets even more complicated because of the confusion between the meanings of political risk, country risk and sovereign risk.

There are many definitions of country risk. For example, Cosset *et al.* (1992) stated that country is the probability that a country will fail to generate enough foreign exchange and will not be able to pay its obligations which has towards foreign creditors. According to Jeff Madura (2011) country risk is the potentially adverse impact of a country's environment on a multinational corporation's (MNC) cash flows. Other researchers thought that the country risk has to be defined in a broader way so it can show all of its characteristics. Shapiro (1999) defined country risk as the general level of political and economic uncertainty in a country that affects the value of loans or investments made in that country. Calverley (1990) defined country risk as the possible economic and financial loss due to the difficulties that arise from the macro-economic and/or political environment of that country. When viewing the literature, we can see how the definitions of country risk and its components change. Due to the faster spread of globalization and greater interconnection, there was an increase in foreign direct investments, international lending and companies started to operate on an international scale and took their business abroad. However, investors realized that an open market and increased mobility of the capital can be risky and could lead to bigger problems in the international financial sector. Given all of this, country risk and its assessment became vital for all international businesses. So naturally, many defined country risk as several different challenges, which they face when investing in a foreign country. In table 1 we have put together some of the definitions and terminologies of risk used by various researches through time.

Table 1: Various approaches in the literature on country risk

Terminologies	*Definition of risk*	*Sources of risk*	*Nature of the investment*	*Methodology*
Political risk	Performance variance	Sovereign interference	Foreign direct investment	Qualitative
Country risk	Negative outcome	Environmental stability	Banking commercial lens	Quantitative
Sovereign risk	Foreign exchange	Credit institutions	Portfolio investment	Quantitative
Cross-border risk	Foreign governments	Volatility of consumption	Banking loans	Quantitative

Source: Sviderske T. (2014) Country Risk Assessment in Economic Security and Sustainability Context, Doctoral Dissertation.

A comprehensive definition of the country's risk is still in progress. However, so far literature and researches are indicating the implied assumption that imbalances or shortcomings in the financial, economic, social, and political areas, where we are investing, can lead to an increase of the risk of investing. Political, economic, and financial risk are frequently used and defined as overall country risk (Wynn *et al.* 1999), and we will define each of these components more in detail in the following part.

2.2. Political risk

Political risk is generally seen as a non-business risk encompassing various changes and components that may have a negative impact on investors. As we saw, researchers had different interpretations when defining country risk and same thing is happening with the political risk. Madura (2012) argues that political risk refers to the actions and changes of foreign government in their regulations that may have impact on multinational corporation's (MNC) investment. Banks and other MNC's have defined political risk as one of the factors which has an impact on the profitability of their international ventures (Shanmugam, 1990).

According to Ghose (1988), the political risk is similar to sovereign risk and lies within the wider context of country risk.

According to Madura (2012), political risk emerges from various events such as terrorist attacks, internal and external conflicts, currency inconvertibility, inefficient bureaucracy and changes in government, wars, and ethnic tensions within the country. He also states that inefficient bureaucracy may seem irrelevant, but it represents a factor that can complicate the business of MNC's. He mentions that in some countries, government employees can expect different kinds of "gifts" of "privileges" before accepting and approving MNC's application. Shanmugam (1990) introduced external reasons such as war, cross-border conflict, and foreign pressures as a further political aspect of country risk. For example, if you are investing in a country, which is next to a country that is at war at that moment, the risk level of that country will be higher than if the neighboring country was at peace. Although they might not be directly involved in the conflict, risk is still high as there is a chance of a spillover effect or perhaps inflow of the refugees from the neighboring country could affect the economic conditions in that country (Juttner, 1995). There is one tool that measures how peaceful a country is, and it is called Global Peace Index. In the table below, we can see the top 10 most peaceful countries in 2023. It is an index made of 23 quantitative and qualitative indicators and it measures how peaceful a certain country is. Indicators such as jailed population, violent demonstrations, political terror, political instability, neighboring country relations and so on, are taken into consideration and weighted on a scale from one to five. The lower the rank, the more peaceful the country is.

We can see from table below that Slovenia is ranked 8th, which is quite high and has score of 1.334. In the empirical research we will show data for other countries in question as well and discuss more the overall political risk of each country.

Table 2: Global Peace Index 23: Top 10 peaceful countries in 2023.

Rank	Country	Score
1	Iceland	1.124
2	Denmark	1.31
3	Ireland	1.312
4	New Zealand	1.313
5	Austria	1.316
6	Singapore	1.332
7	Portugal	1.333
8	Slovenia	1.334
9	Japan	1.336
10	Switzerland	1.339

Source: Global Peace Index 2023, https://www.visionofhumanity.org/maps/#/

In table 3, we can see the 10 least peaceful countries where due to war and conflicts these countries have found themselves at the bottom of this list. At the bottom of this list, we have Syria, Yemen, and Afghanistan.

Table 3: Global Peace Index 23: The least peaceful countries in 2023.

Country	Score
Iraq	3.006
Sudan	3.023
Somalia	3.036
Ukraine	3.043
Russia	3.142
Democratic Republic of the Congo	3.241
South Sudan	3.221
Syria	3.294
Yemen	3.35
Afghanistan	3.448

Source: Global Peace Index 2023, https://www.visionofhumanity.org/maps/#/

One of the examples of political risk which is often mentioned is related to the pharmaceutical company Bayer Ag, i.e., their painkiller Aspirin. They received patent for it both in Germany and United States and this worldwide known product presented one of the biggest revenues for the company. However, in the First World War, United States united with European allies and fought against Germans. Once the war finished, United States decided to drop Bayern, and the company lost its trademark status not only in the US, but also in the France and United Kingdom. United States expropriated several other German companies in order to be able to pay for reparations, and this meant that they were not able to be sold in the United States. This dispute was resolved later in 1994, where Bayer got full rights on the brand and are able to use today Aspirin under this name, but also to use their now famous logo and brand which is the “Bayer cross”.

Many companies and business do assessment of these risks, for example Transparency International ranks countries based on the level of corruption by using corruption perception index (CPI). Countries are categorized and results go from zero, which indicates a highly corrupt country, up to one hundred, which is very clean i.e., not corrupted. Below in table 4., we have an example for year 2022, a list of the ten least and the ten most corrupt countries. Top three countries with highest scores i.e., lowest level or corruption are Denmark, Finland, and New Zealand.

Table 4: Most and Least Corrupt Countries in 2022

Least corrupt		***Most corrupt***	
Country	***Score***	***Country***	***Score***
Denmark	90	Somalia	12
Finland	87	Syria	13
New Zealand	87	South Sudan	13
Norway	84	Venezuela	14
Singapore	83	Yemen	16
Sweden	83	Libya	17
Switzerland	83	North Korea	17
Netherlands	80	Haiti	17
Germany	79	Equatorial Guinea	17
Ireland	77	Burundi	17

Source: Transparency International: https://www.transparency.org/en/cpi/2022/

Some researchers, for example Damodaran (2021) also mentions the level of physical violence as an important determinant of political risk. He states that countries which are in the middle of internal or external physical conflicts, can expose investors to the risks of those conflicts and that cost arising from such risk are not only economic but can also relate to employees and managers and them being harmed.

2.3. Economic risk

Besides political factors, another important aspect to look at when analysing the country risk of a certain country are the analysis of financial and economic risks. Country with high economic and financial risks is more likely to face a financial crisis and thus be riskier for investments. Economics risk presents the possibility that investment could be affected by various macroeconomic conditions. Economic risk rating provides an assessment of a country's current economic strengths and weaknesses. If a country has a lower economic risk, it indicates that country's strengths outweigh the weaknesses, while higher economic risk would suggest the opposite. Economic risk is one of the reasons why international investing carries more risk than domestic investing does. It is also often too difficult to foresee the economic risk. It might seem that the opportunities of investing in foreign country are promising and high, but things can rapidly change and thus leave us with a loss. Some of the economic factors mentioned in various research are nominal gross domestic product – GDP at current market prices, real GDP, inflation, budget balance as percentage of GDP and current account as percentage of GDP. Glova *et al*. (2020) state that gross domestic product per capita (GDP) per capita is a measure of the economic degree of social and economic development. M. Teixeira *et al*. (2008) see the Gross Domestic Product Growth as a very important variable and indicator of economic conditions in a certain country. Higher economic growth is linked to a better relationship between government debt and GDP, meaning less risk for that country. Current account as percentage of GDP presents the balance of the current account (sum of net exports of goods and services, net primary, and secondary income) in a country divided by GDP. The more deficits, the riskier the country is. According to Asiri (2014) current account deficit is equal to the amount of funding required and thus countries with large current account deficits are less credible. In order to become more stable and decrease their country risk, countries have to bring their current account to a surplus and in that way decrease the probability of default. One of the other factors mentioned for economic risk is the inflation rate. According to Min (1998) and Teixeira *et al*. (2008), inflation rate presents status and conditions of country's economy. They contend as well that the perception of risk among economic actors is higher when the inflation rate is higher and the level of uncertainty regarding the nation's economic situations.

Some other researchers would also include financial risk in these analysis. Ramady (2013) stated that the aim of financial risk assessment is to see a country's ability to finance its commercial and debt obligations. Financial risk is everywhere, and it can affect everyone, from businesses and governments to individuals. For example, financial risk for individuals is when they make decisions, which can negatively influence their income, for governments it is perhaps when they default on bonds or cannot control their monetary policy. Market risk, credit risk, liquidity risk, operational risk, and legal risk are all examples of financial risk. The factors that structure a country's financial risk according to Bouchet *et al*. (2003) include foreign debt or external debt as a percentage of GDP which is an amount that one country owes to either an institution in another country or to another country. The higher the ratio, the riskier the country. According to Glova *et al*. (2020) total debt service as percentage of exports of goods and services which presents the sum of principal repayments and interest actually paid in currency, goods, or services on long-term debt, interest paid on short-term debt and repayments to the IMF should also be examined. However, due to lack of data for these factors, in the empirical part of the paper, we will go more through real figures and data which were available related to these factors for BiH, Croatia, Serbia and Slovenia and see how each country is standing.

2.4. Country risk analysis and techniques of country risk analysis

Country risk analysis, like most things, needed time to develop and reach current status. It all started when countries began to expand their businesses and activities to other countries and started with cross-border lending. Back in the days, information on needed data could not be so easily obtained and technology was not there to help, so often countries did not have all the necessary knowledge and experienced losses because borrowers were not able to repay back the money. There were many reasons for default, for example expenses due to the war conflicts, mismanagement, and political instability in the region or even harvest failures. Solberg (2002) says that with the advance in technology in the 1970s, country risk analysis also started to evolve, and it resulted in a greater use of quantitative approaches. Country reports were then more detailed and contained information not only on historical trend, but also balance of payment, external debt, and international reserve stocks. Analysts began to use various statistical techniques, as well as weighted and unweighted checklists which allowed them to create a "score" or rating for each country. These risk ratings were used then to rank countries and see which one had the best score and was worth investing in. Civil war in Lebanon which occurred in the end of 1970s emphasized the need to also include political factors into these country risk analysis.

Although there were significant improvements in the methodology and country risk analysis, some issues were still present. Not everyone would use these developments and information such as data on external assets and liabilities was still lacking and a lot of investment decisions were made despite presented country risk issues. Solberg (1992) explains how at this time many decisions were made only due to desire to "book international assets". During these times, many countries just started to have and take advantage of large and powerful companies and so literature most often described what kind of impacts country risk can have on these multinational corporations (MNCs). Khan (2023) described issues with international lending, for example effects of political risk and how it can have a negative impact on the cash flow of the company. However, even with all the research that has been done many authors such as Kobrin (1979), Brewer (1981), Fitzpatrick (1983), Desta (1985), Howell and Chaddick (1994) could not still agree was actually "political risk" is and how could they measure it and get precise results.

2.4.1. Measuring country risk

There is no single method for calculating country risk because different approaches may be more appropriate for various types of investments and business operations. Measuring country risk presents evaluating the likelihood that certain events in the country, such as political, economic, or financial, will have a detrimental impact on investment in that country.

Before describing the most used techniques in assessing country risk, we should mention there are macro and micro-assessment of a country risk. A macro-assessment of a country risk is focused on a comprehensive risk assessment of a country. It includes all variables that might impact country risk and can be used for each country. However, it does not take into consideration the business of multinational corporations. While on the other hand, micro-assessment does. Therefore, MNCs will use this type of measuring country risk, as it relates to their business directly and it can be of more help to them and to their MNC. The aim of micro-assessment is to define and determine what kind of impact particular macro environmental factors can have on those MNCs in question.

Some of the numerous ways to measure and evaluate country risk includes: credit rating agencies, economic indicators such as inflation, growth rates, level of unemployment can provide information on country's stability, political stability indicators including level of corruption, government's stability, social stability which includes the level of ethnic and religious tensions and the availability of resources such as water and food, regulatory and legal environment in the country including stability of the legal system, easiness of conducting a business, expert opinions such as analysts and mark participants who can help assess country risk based on their knowledge and experience and by using qualitative and quantitative data they have. There is also a multivariate analysis which uses a combination of indicators and data from a variety of sources to generate a comprehensive measure of country risk. For example, a study by Berneche and Chinn (2010) used a multivariate model to evaluate the level of country risk for a sample of countries during the 2008 financial crisis. Companies, investors, and financial institutions can benefit from multivariate analysis of country risk when making investment decisions and determining the degree of risk involved with doing business in a specific nation.

Regardless of the method used, it is important to consider a range of factors when evaluating country risk. This may include political stability, economic conditions, the regulatory and legal environment, and social stability. Additionally, it is important to regularly update risk assessments, as country risk can change over time due to events such as political upheaval, natural disasters, or changes in the global economy.

2.4.2. Techniques of Assessing Country Risk

In this part we will discuss more in detail some of the most used techniques are a qualitative method, checklist approach, a Quantitative analysis, Delphi technique, inspection visits and finally a combination of these techniques.

- A Qualitative method which presents an assessment of a country's political, social, cultural, and economic conditions and it investigated country's evolution. However, one of the setbacks was that could not compare different countries. Political risk index, which Business Environment Risk Intelligence (BERI) provides, is one of the examples of the qualitative method.
- The checklist approach involves analysing a country's risk based on rating and weighting a set of identified factors that include financial, political, and economic criteria and consolidates them afterwards in order to get a full picture of the assessment. All of these factors are weighted and scaled from lowest one to the highest one. An example of this method is the CRS Group's International Country Risk Guide (ICRG). This method is also used for forming a country profile, which is comparable to other regions, and over different periods. Most factors in this method are measured from actual data, for example GDP which can be found in available data, but political factors must be defined subjectively. You cannot find available measure for probability of one country entering a war or something similar, so you would have to give your subjective thought and measure to get country risk for a certain country.

- A Quantitative analysis uses different economic and statistical methods in analysing country risk. A large number of countries are compared with this method, however researchers often argued that it had narrow focus, as it mainly looked at economic data. Despite being able to quantify the effect of variables on one another, it does not foresee country's problems before they occur.
- The Delphi technique is a bit different from the abovementioned methods. Here, we collect different opinions of the experts and try to get the right answer through consensus. Of course, the results highly depend on the chosen experts and their quality (Burmester, 2000). Even though this technique is often said to be methodologically unscientific, it can and is still used as a good communication tool in gaining expert opinions (Benn *et al*., 2009).
- Inspection visits method is what it sounds like. It includes visiting a definite country and meeting with consumer, business officials and especially the government, in order to create an assessment and settle any ambivalent issues with that country.
- Combination of techniques – and of course, in the end, one can use a combination of all of these techniques in order to achieve a more detailed assessment of countries and their ratings. For example, one technique can be used to assign ratings to the identified factors, while another one to develop an overall country risk rating of a certain country.

In conclusion, there are various methods for measuring country risk, and investors should consider using a combination of these methods to get a comprehensive understanding of the risks associated with investing in a particular country.

2.5. Country risk assessors

In this part we will discuss country risk assessors, their role and different rating scores they use. The concept of rating agencies goes back to the beginning of 19th century, and it is related to financial disclosure. Katavic (2015) explains that agency called Mercantile, was one of the first credit agencies in 1841 that used a network of intermediaries to collect data on operational statistics, business ability, and the creditworthiness of the business and then spread this information to others. Rating agencies are considered to be of great help in today's world, as any investor can give a loan to anyone anywhere in the world. Besides private companies, rating agencies also assess the creditworthiness of government and public institutions. By using credit rating, you can also determine the credibility of a certain country. It has become particularly important for countries to have high credit rating, as those with lower one, are only able to take less loans at a higher rate of interest than they would normally if they had higher credit rating.

Various agencies combine qualitative and quantitative methods in defining political, economic, and financial risk measures and provide detailed country risk analysis (CRA) and combine it all into the composite risk ratings. The most famous three rating agencies in the world are Standard and Poor's (S&P), Moody's and Fitch rating. These big tree rating agencies have been criticized as one of the main causes of the financial crisis that happened in Greece, but also a source of the financial problems in Spain, Portugal, and Ireland. Alsakka *et al*. (2011) says they were also accused of not alerting the risks related to mortgage-backed securities. So, how do these agencies work and collect the necessary data?

Standard & Poor's Financial Services (S&P) started all the way back in 1860. Their rating is a credit score that describes the general creditworthiness of a company, city, or country that issues debt. The Standard and Poor's company rates how likely will a debt be repaid. If S&P gives a country, rating from AAA to BBB then that country is characterized as an investible country, while on the other hand if the government gets a credit note with rating from BB to D, then it is considered to be speculative. Following Standard & Poor's Financial Service, the second largest rating agency is Moody's. Its credit rating ranges from a maximum Aaa to a minimum C. Countries which are rated from Aaa-Baa are good for investment, but others are more speculative and not investible. The third biggest credit agency is Fitch, which was founded in 1914. The rating is similar to S&P and Moody's, so countries graded from AAA to BB are characterized in a positive way and considered investible. On the other hand, those which are graded from B to D, are not considered a good choice and have a high default risk.

In table 5, we can see rating scales and rating description for Moody's, Standard & Poor's, and Fitch, the three most known credit rating agencies.

Table 5: Rating Scales of Different CRA's

Moody's	**S&P**	**Fitch**	**Rating Description**
Aaa	AAA	AAA	Prime
Aa1	AA+	AA+	High grade
Aa2	AA	AA	
Aa3	AA-	AA-	
A1	A+	A+	Upper medium grade
A2	A	A	
A3	A-	A-	
Baa1	BBB+	BBB+	Lower medium grade
Baa2	BBB	BBB	
Baa3	BBB-	BBB-	
Ba1	BB+	BB+	Non-investment grade
Ba2	BB	BB	Speculative
Ba3	BB-	BB-	
B1	B+	B+	Highly speculative
B2	B	B	
B3	B-	B-	
Caa1	CCC+	CCC+	Substantial risk
Caa2	CCC	CCC	
Caa3	CCC-	CCC-	
Ca	CC	CC	Extremely speculative
C	C	C	Default imminent

Source: Author creation based on agencies' official websites: Moody's https://www.moodys.com/, S&P https://www.spglobal.com/ratings/en/, Fitch https://www.fitchratings.com/.

Other various rating agencies, which are also used all around the world, are Business Environment Risk Intelligence (BERI) Control Risks Information Services (CRIS), Economist Intelligence Unit (EIU), Euromoney Country Risk, International Country Risk Guide (ICRG). According to Business Environment Risk Intelligence (BERI) website is a company which provides ratings, analyses, and forecasts for more than 140 countries. Their services are designed to assist executives in risk assessment when making decisions about entering foreign markets or setting up operations abroad. Political, security, and integrity risk are the focus of the international risk and strategic consulting firm Control Risks Information Services (CRIS). According to Kenton (2019), Economist Intelligence Unit (EIU) provides country, industry and risk analyses based on the work, research, and insights of a worldwide network of economic, political, and business experts. The online community of economic and political experts known as Euromoney Country Risk (ECR) offers real-time ratings in categories related to political, structural, and economic risk. Euromoney establishes an overall score for countries using nine weighted categories. The International Country Risk Guide (ICRG) was created in 1980 and today is one of the world's largest risk assessments and databases. It serves as important information on potential risk for business operations to investors, banks, businesses, traders, and more. The ICRG assesses three risk indices - political, economic, and financial. Each index has several variables adding up to twenty-two in total. The financial risk index is based on fifty points, as well as economic risk, while political risk is based on one hundred points. A formula is used to combine the three independent risk ratings into a single overall country risk score.

One of the downfalls of these agencies is that there is no standardization. Each one uses its own methods and way of showing results, which can lead to a bit of confusion as well. In addition to the lack of standardization, another limitation of these rating agencies is that often there is data missing, as they do not provide ratings for every country in the world. We will see it especially in the case of Bosnia and Herzegovina, Croatia, Serbia, and Slovenia, where data for some years is missing. Damodaran (2011) also notices some downfalls related to these agencies, such as lack of transparency when it comes to used methodologies in assigning the country ratings, and there is lack of providing comparability among countries, as measures are linear. Naumoski (2012) emphasized that for example, a country that has a risk score of 40 is not twice as risky as a country with a score of 20.

2.6. Country Risk Premium

One of the terms most often found in research related to the country risk is the country risk premium (CRP). In addition to country risk analysis, country risk premium can also be used as an additional tool. This term describes the additional return that investors demand to make up for the increased risk involved with investing in a specific country. The anticipated risk of investing in a particular country affects the size of the country risk premium. For instance, investors may demand a higher return if a country has more political instability than a country with a stable political climate to offset the higher risk. In addition to the return, they would receive from a risk-free investment, an investor must pay a country risk premium in order to invest in a particular country which covers the additional social, political, and economic risks associated with investing in that particular country.

Using country risk premium makes it simpler to make well informed decisions regarding various investments. Investors are arable to calculate the expected return on a certain investment by taking into consideration particular risks which are in connection with that country and the premium. When determining and calculating risk premium for a certain country, factors such as political and economic stability, infrastructure, currency risk are all taken into consideration.

One of the important aspects to look at while discussing country risk premium, is Damodaran's approach to the country risk premium. Damodaran is a prominent finance professor and researcher who has written extensively on the topic of country risk premium. He maintains a personal website (Damodaran online www.stern.nyu.edu/~adamodar) where he shares his research, valuation tools, and resources. His view on country risk premium is that it is a critical component of the cost of capital for international investments and plays an important role in the investment decision-making process. Damodaran (2012) argues that a country risk premium represents the extra return that investors demand to compensate for the added risk associated with investing in a particular country. He notes that the size of the country's risk premium varies depending on the perceived risk of investing in a particular country and that it should be incorporated into the cost of capital calculation for international investments.

In his research, Damodaran has developed a framework for estimating country risk premium that considers a range of factors, including political risk, economic risk, and sovereign risk. He also adds that factors such as political climate, corruption and financial and economic stability have an important impact on the country risk premium. Damodaran also writes about the two challenges which he has faced in calculating the country risk premium, one being the lack of available data and the other is a high level of subjectivity in country risk assessments.

3. LITERATURE REVIEW

A literature review on country risk analysis presents a comprehensive overview of the research and literature related to the assessment of the risk of investing in a particular country. It was not an easy task to search for literature related to country risk and country risk analysis, in particular country risk analysis for the region in question. However, we have managed to gather a few articles which were related to the topic and talked about country risk analysis, determinants, factors, and country risk premium.

3.1. Country risk assessment in the region

Glova *et al.* (2020) in their article "Determinant Effects of Political and Economic Factors on Country Risk: An Evidence from the EU Countries" analyze and provide country risk assessment based on political and economic factors which have an impact on the country risk. According to Glova *et al.* (2020) analysis, factors such as GDP per capita, inflation, rule of law, political control index of corruption are one of the main components affecting the country risk of the EU countries. This article also emphasizes the importance of governance quality and political stability within a country, in order to decrease the country risk and not just to achieve higher economic growth, but also to attract more of foreign investment into the specific country.

Naumoski (2012) in his article discusses methods and challenges which occur while determining country risk premium in emerging markets, with focus on North Macedonia. He uses different methods to estimate CRP such as country credit rating, equity risk premium method and sovereign spread. He also argues the importance of using more than one method in order to get a more precise result and talks about solutions for challenges he faced while estimating CRP for emerging markets which are a lack of transparency and unavailable data. Good thing about this article is that it is focused on a single country and also offers more information about history background and political and financial stability of North Macedonia.

The third article is written by Iloje (2015) where he explored the relationship between corruption index, foreign direct investment (FDI) and country risk assessment for the region of Central and Eastern Europe. He explains the relationship between country risk assessment and FDI and writes about the effect corruption has on FDI and provides with solution on how to deal with that corruption, as it most often has a negative impact on the inflow of FDI. He also argues that a more comprehensive approach is needed for country risk assessments, one which would involve a variety of factors including political, economic, financial, and social.

3.2. Country risk assessment in the world

Khattab *et al.* (2015) in their research paper discuss the issue of country risk management in developing countries. One of the highest risks for these countries are political, economic, and financial which affect the stability and growth. Authors highlight the impact of political risk as it leads to political instability, meaning changes in government policies, expropriation of assets. There are numerous examples of current political instability in countries such as

Iran, Iraq, Libya, Syria. Khattab *et al.* (2015) suggest that countries need to try to maintain a stable political environment, with a transparent policy framework. Besides political risk, economic and financial risk also play a huge factor for these countries. Economic risk and financial risk, according to Khattab *et al.* (2015), can result from fluctuations in the exchange rates, inflation, inadequate financial institutions, speculative investment and financing and lack of access to financing. In their study, Khattab *et al.* (2015) also conducted interviews on risk management with enterprises in developing countries. The results showed that the majority was not satisfied with the current approach for conducting country risk analysis in their enterprises.

Gur (2001), in his article “A Country Risk Assessment Model and the Asian Crisis”, discusses the Asian financial crisis of 1997-1998 and the importance of accurately assessing the country risk. In his research, Gur (2001) developed a country risk assessment model to try and identify the impact Asian crisis had on various countries in the region. This model consists of economic factors, political stability factors and institutional quality and is further tests for the ability to predict external debt crisis. The final results are then compared with the ratings from rating agencies, S&P and Moody’s. The study results show that Asian crisis did have a significant impact on the country risk of the affected countries and Gur (2001) highlights the need for ongoing monitoring and assessment of the country risk, in order to provide timely and accurate information.

In the research paper “Country risk and effects of foreign direct investment”, Petrovic and Stankovic (2009) examine the relationship between country risk and foreign direct investment (FDI) and argue that country risk is the critical factor which influences the decisions of foreign investors when choosing where to invest their capital. They also state that the effects of FDI on a country’s economy depend on the level of country risk, so higher level of risk will potentially lead to a lower level of investment in that particular country. Petrovic and Stankovic (2009) also discussed the benefits of FDI for countries which include creation of jobs, transfer of technology and an overall increase in economic growth. They also conclude that the relationship between country risk and FDI is not uniform across different countries, as some are more sensitive to changes in the country risk than others. Sviderske (2014) presents a study on country risk assessment in the context of economic security and sustainability. The author argues that traditional approaches to country risk assessment, which focus on macroeconomic indicators, are insufficient to capture the complex and dynamic nature of risk in a rapidly changing world. The author proposes a new approach to country risk assessment that considers both economic and non-economic factors, such as political stability and environmental sustainability, to provide a more comprehensive understanding of country risk. He argues that this approach can help to improve investments decisions and risk analysis as many of the approaches used are often based on pure judgment and therefore can show inaccurate estimates of the country risk.

As already mentioned in the beginning of the paper, Damodaran is a well-known academic and researcher in the field of finance, who has made significant contributions to the study of country risk. A lot of information about him can be found on his personal website (Damodaran online www.stern.nyu.edu/~adamodar) where he shares his research, resources, and valuation tools. Damodaran's research focuses on the assessment and management of country risk in the context of international investment and finance. He is one of the main researchers of country risk in the world and his research has been highly used in academic literature and helped shape the current understanding of this topic. Damodaran (2018) proposed a several frameworks for the assessment of country risk which involve a three-step process:

1. Identifying and quantifying political, economic, and financial risks which a country faces.
2. Assessing the impact of these risks on investments returns.
3. Developing strategies for managing and mitigating country risk through diversification and other risk-management tools.

Damodaran argues that country risk analysis should consider a range of factors and be regularly updated in order to reflect the changing condition of the country and the global economy, and that country risk cannot be entirely diversified.

4. EMPIRICAL RESEARCH

After going through theoretical part of this paper, we will now look at some of the reports and analysis of country risk for these four countries and see what all of this means in practice, as well as what are the key strengths and weaknesses of each country. Besides country risk reports and analysis for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia we will also take a look at credit rating agencies' reports and their rates for these four countries. As already mentioned, credit ratings done by credit rating agencies are also important and can be of immense value to investors. In the tables below we will see the score for each country done by Standard and Poor's (S&P), Moody's. Unfortunately, as already mentioned above, for some years there was no data from these credit rating agencies for these four countries. We will first discuss and focus on the strengths and weaknesses of each of these countries and see what the reports say about each country.

After looking at different aspects of these four countries we will compare them and show closely political, economic, and financial factors which are taken into consideration when calculating country risk for a specific country. We will look closely at these factors with focus on the current situation, but also for the years 2007 and 2013 as this will give us a more comprehensive picture of the situation in each country. We will also look into data for country risk premium calculated by Damodaran, as an important aspect of country risk for these four countries. Finally, we will draw conclusions from all the collected and presented data and discuss the derived hypothesis.

4.1. Bosnia and Herzegovina

Bosnia and Herzegovina are a relatively small country located in Southeast Europe in Balkans and has population of around 3.4 million citizens. It was one of seven states that belonged to the Social Federal Republic of Yugoslavia. During that time Bosnia's population amounted to 4,526,996 which made only 19% of the total population of Yugoslavia. BiH has the biggest border with Croatia, and also borders with Serbia, and Montenegro. There is a small coastline on the Adriatic Sea. In 1992, the country declared its independence which was followed by war, which ended in 1995 by the signing of Dayton Peace Accords in Paris and it was mostly supported by large donations. In 1998, national currency – Bosnian convertible mark (BAM) was introduced, and it has been pegged to the Euro. Since then, BiH is divided into two entities, Federation of Bosnia and Herzegovina and Republic of Srpska, and has one self-governing administrative unit Brcko District. BiH has three members of Presidency of Bosnia and Herzegovina, one representing Bosniaks, one Croats, and one Serbs. Each 8 months they are rotated, and one is the chairperson of the presidency. Since these happenings in the 90s, there has been strong presence of international community in BiH, and country has been trying to stay on its feet and recover. When it comes to the economy of Bosnia, revenues were earned mostly from different natural branches as BiH is a country filled with natural resources. The European Union (EU) is continuously trying to provide and assist BiH in its recovery process and is seen as mayor player in this process. Stabilization and Association Agreement (SAA) with the EU was signed in 2015, which provides formal mechanisms and timelines of reforms that will bring BiH closer to EU standards. In 2016, BiH submitted a formal application to become an EU member state. According to European Commission's report (2022), European Council confirmed once again its readiness to grant the status of candidate country to BiH and invites the European Commission to report on implementation of the 14 key priorities set out in its Opinion with special attention to those, which constitute a substantial set of reforms.

According to the Coface, French company which provides country risk classification, rated Bosnia and Herzegovina with a “D”, emphasizing high-risk political and economic situation in the country, as well as difficult business environment. In the table 6, we have summarized strengths and weaknesses defined by Coface (2022) for Bosnia and Herzegovina.

Table 6: BiH: Strengths and weaknesses

Strengths	**Weaknesses**
Significant transfers from expatriate workers	Only a few of the fourteen priorities set by the Commission have seen progress, accession negotiations pending since 2016
Stabilization and Association Agreement with the EU (2015) with pre-accession funds	Institutional, regulatory, economic and community fragmentation (50% Muslim Bosniaks, 33% Orthodox Serbs and 15% Catholic Croats)
Potential in tourism and hydroelectricity	Public investment is lacking in local transportation, education, and health.
BiH is a member of various trade agreements (CEFTA 2007, EFTA since 2015 and the Regional Common Market of 6 Balkan countries since November 2020)	Exports sector undiversified and exposed to commodity price movements
Free Trade Agreement under negotiation with Malaysia	Large dependence on neighboring countries for exports and remittances
Wage competitiveness	High presence of corruption, cronyism, administrative and judiciary delays, defective rule of law
	High emigration estimated at 50,000 people per year which also leads to lack of skilled workforce
	Large informal sector (one third of the economy), low labor force participation (47%), high youth unemployment (38%)
	Dependent on external funding

Source: Coface (2022) Bosnia and Herzegovina: Major Macro Economic Indicators. Available at: https://www.coface.com/Economic-Studies-and-Country-Risks/Bosnia-and-Herzegovina

The first strength is significant transfers from expatriate workers, which represents skilled workers or professionals, such as doctors, who took on a position outside of BiH. This phenomenon is quite popular in BiH, as many educated people leave for Germany, Austria, and Switzerland in search of better opportunities and send money to their families who stayed in BiH. Besides this, Stabilization and Association Agreement signed with the EU, which we already mentioned above. The EU has continued to support and give grants to BiH, but there is still a long way to get to EU membership. Trade agreements signed with other countries, such as Central European Free Trade Agreement (CEFTA) and European Free Trade Association reduce which reduce or abolish trade barriers, are also strength for BiH. On the other hand, for weaknesses Coface report (2022) mentions a lack of public investment, high emigration and lack of skilled workforce, high unemployment, corruption, and defective rule of law among other things. All these things are connected. Due to lack of opportunities, corrupted system and complicated political situation, people often seek for jobs outside of BiH, and see leaving BiH as a great accomplishment. Only older people actually stay in BiH, and cities, one by one, become ghost cities.

In the country report by Allianz Group (2022), BiH has been ranked with “D3” meaning sensitive risk for enterprises. It shows high economic, financing, and political risk. Among strengths are mentioned the stable exchange rate and comfortable level of foreign exchange reserves. As for weaknesses, Allianz (2022) emphasized high political instability of the country, high external debt stock, high vulnerability to external shocks and just overall weak business environment. The political situation which has been present in BiH for quite some time has been making it difficult for this country to move on and is putting the risk on any kind of investment. According to Trading Economics (2022), as being one of the least attractive countries for investment, foreign direct investment (FDI) in BiH, in the second quarter of 2022, had increased by 512.40 BAM million. Despite BiH being ready and wanting more foreign direct investments, many unfortunately do not see enough investment opportunities in the country. According to the report from U.S. Department of State (2021), legal framework does not discriminate against foreign investors but given the high level of corruption (score of 35 out of 100 according to Transparency), foreign investors can be at a significant disadvantage in relation to established local companies, especially those with formal or informal backing by BiH’s various levels of government.

In the table below we have shown ratings done by credit rating agencies for Bosnia and Herzegovina. But only data by S&P and Moody’s is shown, as Fitch’s rating could not been found.

Table 7: Country risk ratings for Bosnia and Herzegovina 2006-2023

Year	**S&P**	**Moody's**
2006	n/a	B2/Stable
2008	B+ / Stable	n/a
2010	B+/Stable	n/a
2011	B/Negative	B3/Negative
2012	B/Stable	B3/Stable
2016	n/a	B3/Stable
2018	n/a	B3/Stable
2019	B/Positive	B3/Stable
2020	B/Stable	B3/Stable
2022	n/a	B3/Stable
2023	B positive	n/a

Source: Country Economy (2022) Rating: Bosnia and Herzegovina Credit Rating. Available at: https://countryeconomy.com/ratings/bosnia-herzegovina & Trading Economics (2023) Bosnia and Herzegovina - Credit Rating. Available at: https://tradingeconomics.com/bosnia-and-herzegovina/rating.

Due to lack of data for 2007, we showed results for 2006 where according to Moody's, Bosnia and Herzegovina was scored with B2. This is characterized as highly speculative, meaning high risk. If we fast forward for a couple of years, the situation does not change drastically. In most years, for both S&P and Moody's, BiH has ratings B or B3, meaning it was still seen as a country with high risk, and unsafe for investment.

According to Central Bank of BiH, on 22nd July 2022, rating agency Moody's has affirmed sovereign credit rating on Bosnia and Herzegovina at „B3 with stable outlook ". The report mentions BiH's limited economic strength, high unemployment, and emigration. All these things are connected to as many young people as possible still each year due to limited opportunities decide to look and find jobs and better lives in other EU countries. Complex and fragile political structure as well as poor political situation also adds to this, as we are forced each day to listen and read about constant problems, corruption, differences and so on. Lack of cooperation on a state level who often threaten with war, only increases citizens' dissatisfaction. But, despite many negative things, BiH still managed to get "B3 with stable outlook" rate. Moody's report (2022) states that the economy has proved relatively resilient to the pandemic, with real GDP growth rebounding by 7.5% in 2021 from a contraction of

3.1% in 2020 supported by the recovery of domestic demand and strong export growth, in particular base metals and mineral products, exceeding pre-pandemic levels. They expect that Russia-Ukraine conflict which started in February 2022, despite what many think, will not have such a great impact on BiH. Strong and continuous presence of international community in BiH also adds to BiH's stability and growth as it continues to support BiH on its path to the EU and helps decrease some of the political tensions which are present in the country.

Despite some progress, from the data above, we ca see that BiH continues to face numerous economic and political challenges, which contribute to a higher level of country risk. Political challenges such as complex political system, overlapping levels of government, ethnic tensions between three main groups have led to both political and social instability making it quite difficult for BiH to move forward and create more stable environment for the citizens, and foreign investors. In addition to this, there is still a high unemployment rate as the country struggles to create new jobs and improve the standard of living. As already said above, more and more people each year search for better opportunities in the countries of EU, especially Germany. Also, the country's level of corruption is still high, and this creates a risk for investors and discourages them from investing. It also undermines the country's economic stability and lead to other issues such as mistrust in the government, lack of rule of law and so on. BiH also has a complex legal system and ineffective government which makes it difficult to address some of the challenges that country faces and to start with necessary reforms. Country's economy is heavily relying on exports which again makes it more vulnerable to economic fluctuations in other countries. High level of public debt put pressure on government's finances and pose a challenge to country's financial stability. BiH has a lot of challenges which need to be addressed in order to try and create a more economically stable country and to attract more investment which can be of great help for countries' economy.

4.2. Croatia

Croatia was also one of the countries that belonged to Social Federal Republic of Yugoslavia. In 1991, Croatia declared independence and today has population of around 4 million people. It has been a member of the EU since 2013 and is also a member of the United Nations (UN), World Trade Organization (WTO), The North Atlantic Treaty Organization (NATO) and Croatia is also a founding member of the Union for the Mediterranean. On January 1st, 2023, Croatia replaced its national currency – kuna, with euro and also joined the Schengen Area. By entering the Schengen Area, EU countries which are members of this area, eliminate any type of border control for these countries, but most importantly passport control.

From the Coface report (2022), we can see that long coastline and tourism are one of the biggest strengths for Croatia. Tourism remains the most important source of income, and that is why once pandemic Covid-19 started, they were in trouble as restrictions on all travelling were imposed for most of the countries. Before the pandemic, sales took up $11.97 billion, 19.24 percent of Croatia's gross national product (GDP). According to World Data Info (2020), in 2020 tourist receipts plummeted due to the Covid-19 pandemic of the $11.97 billion (2019), only $5.63 remained. This is a 53 percent decrease in Croatia. As for weaknesses, high youth unemployment is still present, and many of the Croatians have used the opportunity of Croatia becoming a member of the EU to go to other EU countries and work there which led to decline in educated workers and in population in general.

Table 8: Croatia: Strengths and weaknesses

Strengths	**Weaknesses**
Long coastline and high potential in tourism	Dependence on tourism which has strongly suffered from the pandemic
Oil and gas potential	High private and public debt
The country joined ERM II in 2020, joined the Eurozone in 2023	Institutional gaps: inefficient administration, health, and justice; overlapping administrative levels, corruption
Large support from the EU funds	Time-consuming and inefficient business insolvency procedure
Infrastructure has high-quality	Low industrial diversification i.e., lack of competitiveness
	High youth unemployment (20% in September 2021), low participation of women
	Due to skilled workers' emigration and a declining population, there are labor shortages

Source: Coface (2022) Economic Studies and Country Risks: Croatia
https://www.coface.com/Economic-Studies-and-Country-Risks/Croatia

Country risk assessment made by Coface ranked this country with "A4", meaning that there are some weaknesses present in economic and financial outlook, but the risk is still acceptable. Report also highlighted stabilization of Croatia in a political sense, but there have been strained and intense relations with other neighboring countries, BiH especially. The main disputes are related to geostrategic and political issues. One strong political issue that has been present for quite some time is related to the rights of Croats living in BiH and changes in Electoral Law of BiH, while geostrategic is related to the Peljesac bridge. Allianz's report (2022) ranked Croatia with B2 which represents medium risk. Financing risk was characterized as very low in contrast to economic and political risk.

Allianz report highlights good international relations that Croatia has as well as EU membership since 2013, but also a low inflation which is present and fast recovery from the pandemic Covid – 19. But what Croatia needs to worry about is the very high public and external debt. According to data from CEIC, Croatia National Government Debt reached 6.1 USD billion in August of 2022, and Croatia External Debt reached 48.2 USD billion July of 2022.

Table 9: Country Risk Ratings for Croatia from 2007-2023

Year	**S&P**	**Moody's**	**Fitch**
2007	n/a	Baa3/positive	n/a
2008	n/a	Baa3/stable	n/a
2009	n/a	n/a	BBB- /negative
2010	BBB- /negative	n/a	n/a
2012	BB+ stable	Baa3/negative	BBB-/negative
2014	n/a	n/a	BB/stable
2015	BB/negative	n/a	BB/negative
2016	BB/stable	Ba2/negative	n/a
2017	BB/positive	Ba2/stable	BB/stable
2018	BB+/stable	n/a	BB+/stable
2019	BBB-/stable	Ba2/positive	BBB-/positive
2020	n/a	Ba1/stable	BBB-/stable
2021	n/a	n/a	BBB/positive
2022	BBB+ (Stable)	Baa2/stable	BBB+ (Stable)
2023	BBB+ (Stable)	n/a	BBB+ (Stable)

Source: Country Economy (2022) Rating: Croatia Credit Rating. Available at: https://countryeconomy.com/ratings/croatia and Trading Econmics (2023) Croatia - Credit Rating. [online] Available at: https://tradingeconomics.com/croatia/rating.

In the table 9, we can see country risk ratings for Croatia from 2007 until 2023. Again, for some years data has unfortunately not been available. In 2007, Croatia according to Moody's has score of Baa3 which is the lower medium grade. In 2014, a years after its accession to the European Union, Croatia had score BB by Fitch – it is characterized as non-investment grade speculative. In 2023, the score by Fitch was improved to BBB + stable.

In July 2022, Moody's upgraded Croatia's ratings go Baa2, characterizing it as subject to moderate risk, which is a bit higher than in 2020 when Croatia was ranked with Ba1. According to Moody's report (2022), The main reason for this is Croatia's entering the euro zone with which it eliminated any foreign currency risk and reduced government liquidity risk. Croatia has furthermore earned this rating by recovering in the economic sense from the negative impacts of the pandemic, especially in the tourism section and if its continuous positive growth and decline in the public and external debt it can have a higher ranking in the following months and years. In 2023, Croatia remained with the same rating by S&P and Fitch, for both BBB+.

As we can see from data and analysis presented above, Croatia is considered to have a relatively moderate level of country risk. A member of the EU, Croatia has been able to have a functioning democracy and maintain a level of political stability. In addition to this, growing tourism sector and improved business environment are also one of the strengths of Croatia. On the other hand, Croatia still struggles with high level of youth unemployment, public debt, large trade deficit and corruption. These factors can pressure government's finances and increase economic volatility, leading to instability and uncertainty for investors and business. Also, the country is heavily dependent on tourism which can limit the country's ability to attract investment and create new jobs. Despite all challenges it faces, Croatia has managed to have stable country risk ratings for the last few years.

4.3. Serbia

Serbia is a country in Central and South-Eastern Europe that encompasses the central part of the Balkans. Bosnia and Herzegovina, Bulgaria, Croatia, Hungary, Kosovo, Macedonia, Montenegro, and Romania are its neighbors. Serbia has population of around 7 million people. For this country as well, history is a bit complicated, but we will mention the most important facts. In 2006, Serbia earned its independence after referendum and State Union of Serbia and Montenegro ceased to exist. Two years later, Kosovo, declared independence from Serbia. To this day, this is a disputed territory in the Balkans around which a lot of tension is present. In 2014, Serbia signed agreement with Kosovo to normalize relations and thus began discussions to become European Union member state. Serbia is also a member of the Central European Free Trade Agreement (CEFTA). Economy in Serbia is dominated by a large services sector (which make 61% of country's GDP). The strongest sectors are energy, automotive industry, machinery, mining, and agriculture. According to Guidance (2021) trade plays a major role in Serbian economic output with the main trading partners being the EU countries, Russia, China, and neighboring Balkan countries. In addition, foreign direct investments are also a priority for Serbia and biggest investors include EU countries (Germany, Austria, Italy, Norway), United States of America and China. The majority of these investments go to automotive industry, food and beverage industry, machinery, textile, and clothing, according to Guidance (2021).

Coface report (2022) ranked Serbia with a "C" which presents very uncertain economic and financial outlook, including unstable political context. In table 10., we have strengths and weaknesses presented by this Coface report (2022).

Table 10: Serbia: Strengths and weaknesses

Strengths	**Weaknesses**
Due to Stabilization and Association Agreement with the EU which allows 93% of Serbian products to enter without customs duties	Landlocked with poor road infrastructure (roads, railways)
Ongoing EU accession process (18 out of 35 chapters have been opened, unchanged since October 2020)	Massive and inefficient public sector
Public sector reform in coordination with the IMF and EU	Slow judicial proceedings, customs harassment, corruption, lack of transparency in the government
Natural resources (coal, bauxite, copper, zinc, gold, lithium)	Large informal sector: 26% of GDP and 19% of employment
Rising automotive industry	Difficult relations with several neighboring countries (unresolved conflict with Kosovo, BiH and Montenegro)
	Brain drains (youth unemployment: 32% in Q1 2021)

Source: Coface (2022) Economic Studies and Country Risks: Serbia https://www.coface.com/Economic-Studies-and-Country-Risks/Serbia

One of the key strengths is definitely EU presence in the country, EU accession process and signed agreements with the EU which make trade easier for Serbia. On the other side we have poor infrastructure, high level of corruption in the country (according to Transparency in 2021 Serbia had score of 38), lack of transparency in the government, weak rule of law and lack of good governance, inefficient public sector, high youth unemployment rate and difficult political situation with neighboring countries.

In the Allianz report (2021), Serbia is assigned with “B2” which presents medium risks. However, they also emphasized the growing economic and political risk which could lead to bigger issues in the future. According to Allianz, Serbia besides political risk needs to work on public debt and inadequate infrastructure. As their strengths, Allianz (2021) points out the strong potential this country has, as well as the continued inflow of foreign direct investments into the country. According to the report from Standard Bank Group (2023), Serbia attracted around 4.4 billion USD of FDI in 2021.

In the table below, we can see country risk ratings from S&P, Moody’s, and Fitch for Serbia from 2007 until 2021. As these three countries share more than just geographical location, but also history and mentality it is perhaps not surprising that these ratings do not differ as much. In 2007, Serbia had rating BB- by S&P, which is non-investment grade speculative. Situation practically stays the same, as Serbia does not quite make a move out of this “non-investment grade speculative” zone. For 2021, we can see that ratings are by S&P is BB+, while Moody’s decided to give rank Ba3 with positive outlook. They explained that reason for this is because Serbia managed to react to after coronavirus shock in economic sense and earned medium growth, which is expected to resume, according to Moody’s. In the Moody’s report it is also mentioned that in general, Serbia entered the Covid - 19 crises with a better macroeconomic profile and lower external imbalances than in previous years. Low and stable inflation, a relatively stable exchange rate, adequate foreign exchange reserves, more balanced growth supported by increased economic diversification, and a stronger government balance sheet given the pre-pandemic marked fiscal consolidation are all part of the improved profile. Negative pressure on the rating would arise if the fiscal metrics deteriorated materially in comparison to peers due to a less prudent fiscal stance, the realization of contingent liabilities, significant exchange rate depreciation, or the growth outlook falling short of Moody's expectations. For 2023, S&P and Fitch both gave Serbia a rating of BB+, with stable outlook.

Even though Serbia has received good rating BB+, it still faces some challenges. One of the main concerns is definitely a high level of corruption which undermines the work of the government. Next would be difficult relations Serbia has with neighboring countries, especially with Kosovo which is a significant source of political risk as these two countries still have not reached a resolution on the status of Kosovo, i.e., Serbia did not recognize Kosovo a sovereign country. It is also important to mention a strong influence of foreign powers, such as from Russia, which pose a risk to the stability of the country but also affects if rode to the EU accession. Beside political risk, Serbia also deals with lower quality of infrastructure, weak rule of law and lack of good governance.

Table 11: Country Risk Ratings for Serbia from 2007-2023

Year	**S&P**	**Moody's**	**Fitch**
2007	BB-/stable	n/a	n/a
2008	BB-/negative	n/a	BB-/negative
2009	n/a	n/a	BB-/stable
2010	n/a	n/a	BB-/stable
2011	BB/stable	n/a	n/a
2012	BB-/negative	n/a	BB-/negative
2013	n/a	B1/stable	n/a
2014	BB-/negative	n/a	B+/stable
2015	n/a	n/a	B+/positive
2016	BB-/positive	B1/positive	BB-/stable
2017	BB/stable	Ba3/stable	BB/stable
2018	BB/positive	n/a	n/a
2019	BB+/positive	Ba3/positive	BB+/stable
2020	BB+/stable	n/a	n/a
2021	BB+/positive	Ba3/positive	n/a
2022	BB+		
2023	BB+ / stable outlook		BB+ / stable outlook

Source: Trading Economics (2023) Serbia - Credit Rating. [online] Available at: https://tradingeconomics.com/serbia/rating.

4.4. Slovenia

Slovenia is the fourth and final country that we will analyze. It is a small country in central Europe with a current population of around 2,125,000 people. Slovenia was part of Yugoslavia until 1991. After its independence, Slovenia moved closer to the politics of the EU countries and economy started to improve and Slovenia was politically stable country.

In 2004, Slovenia joined both North Atlantic Treaty Organization (NATO) and the EU. Three years later, Slovenia adopted the Euro. Joining the EU had many advantages for Slovenia and its citizens, starting from financial benefits but also Slovenia citizens now had the ability to travel and work in other EU member states. Thanks to the great strategic location between the Western Europe and the Balkans, excellent infrastructure, and a well-educated work force, Slovenia has achieved one of the highest per capita GDPs in Central Europe, despite having suffered a protracted recession in 2008-2009 in the wake of the global financial crisis, according to Know your country (2022) report. Slovenia’s main trading partners are of course the EU countries, such as Germany, Austria, Croatia, Italy, France, and Slovakia.

Coface (2022) reports ranked Slovenia with an “A3” rating, making it the best ranked country among these four i.e., with the lowest country risk. In table 12, we showed a list of strengths and weaknesses mentioned in this report. As strengths for Slovenia, Coface emphasizes the importance of being and EU member state as well as member of the Eurozone. Report also highlights Slovenia’s diversified economy and its external surplus, meaning that the amount of funds coming into the country is higher than the amount of funds going out from the country. On the other side, one of the challenges for Slovenia is a small domestic market, labor shortage inefficient state-owned companies and slow administrative and judicial procedures.

Table 12: Slovenia: Strengths and weaknesses

Strengths	**Weaknesses**
Member of the Eurozone since 2007	Small domestic market, open economy (exports of goods and services represent 80% of GDP in 2020)
Diversified economy (automotive, pharmaceuticals, electrics, electronics, tourism)	Ageing population and demographic growth at a standstill, resulting in a labor shortage
Integrated in the European production chain	Dependence on regional economic conditions and automotive
External accounts in surplus	Inefficient state-owned companies
Efforts to clean up the banking sector	Slow administrative and judicial procedures

Source: Coface (2022) Economic Studies and Country Risks: Slovenia
https://www.coface.com/Economic-Studies-and-Country-Risks/Slovenia

As for Allianz reports (2022), Slovenia is ranked with BB2 indicating medium risk. This report also highlights the importance of EU membership for Slovenia, which lead to good international connections and stable democracy in the country as well as membership of the Eurozone which bring forth lower convertibility risk. On the other side, downfalls elevated public debt and high gross external debt are mentioned in the Allianz report (2022). Gross external debt reached 124% of the GDP in 2014, while in 2021 decreased to 98% of the GDP, during the Corona virus crisis. Slovenia's EU membership is also seen in state's exports as it is mostly exporting to Germany, Italy, Austria, and Croatia.

And lastly, let's take a look at Slovenia and its country ratings from 2006 until 2022 in the table 13 below. As there is no data for 2007, we will start with 2006 when the rating by S&P was AA, and by Moody's Aa3 - both ratings are of high grade, meaning lower risk. Here is an immediate difference between Slovenia and BiH, Serbia and Slovenia. Throughout the years, Slovenia slightly shifts from high grade ratings to lower medium grades. However, in 2020, rating by Moody's and Fitch put Slovenia again in the list of countries with low risk, ranking it A3 with positive outcome. The reasons for this upgrade, according to Moody's report (2022) is firstly the improvement in debt burden but also Slovenia's resilience to the pandemic. In 2023, S&P ranked Slovenia with AA- rating with stable outlook, and Fitch with A rating, also stable outlook.

Table 13: Country Risk Ratings for Slovenia from 2006-2023

Year	S&P	Moody's	Fitch
2006	AA/stable	Aa3/positive	AA/stable
2007	n/a	n/a	n/a
2008	n/a	n/a	n/a
2009	n/a	Aa2/stable	n/a
2010	AA/negative	n/a	n/a
2011	AA-/negative	A1/negative	AA-/negative
2012	A/negative	Baa2/negative	A-/negative
2013	A-/negative	Ba1/stable	BBB+/stable
2015	A-/positive	Baa3/stable	BBB+/positive
2016	A/positive	Baa3/positive	A-/stable
2017	A+/stable	Baa1/stable	A-/stable
2018	A+/stable	n/a	A-/stable
2019	AA-/stable	Baa1/positive	A/stable
2020	n/a	A3/stable	A/stable
2021	n/a	n/a	n/a
2022	AA-/stable	A3 /stable	n/a
2023	AA-/stable	n/a	A/stable

Source: Country Economy (2022) Rating: Slovenia Credit Rating. Available at: https://countryeconomy.com/ratings/slovenia.

Slovenia, when compared to Bosnia and Herzegovina, Croatia and Serbia have a relatively low level of country risk. Financial and political stability, as well as the well-developed tourism industry and growing manufacturing sector contribute to this low risk. Slovenia has also made progress in reducing public debt and as it is a member of EU it has access to a large market for Slovenian businesses. On the other hand, Slovenia does still face some challenges such as dependence on foreign financing, exposure to the eurozone, and a weak banking sector. It is also exposed to geopolitical risk and has faced tensions with its neighboring countries in the past. However, taking all of this into consideration, Slovenia is a stable country which makes it open and suitable for more investment.

4.5. Comparative analysis of Country Risk: Bosnia and Herzegovina, Croatia, Serbia, Slovenia

As already mentioned, in this part we will take a closer look at political, economic, and financial factors related to country risk for Bosnia and Herzegovina, Croatia, Serbia and Slovenia. We will look into data related to the current state of these countries, but also take a look at data from 2007 and 2013 to understand and comprehend how each country was improving or worsening during this time period.

4.5.1. Political risk: Bosnia and Herzegovina, Croatia, Serbia, Slovenia

We already discussed political risk in the theoretical part of this paper and said that it emerges from various events such as terrorist attacks, internal and external conflicts, currency inconvertibility, inefficient bureaucracy and changes in government, wars, and ethnic tensions within the country according to Madura (2012). When it comes to wars and ethnic tensions within the country, Global Peace Index is a tool used worldwide to determine how peaceful a country is. The lower the score, the less violence there is in that country. In the table 14 we have results for BiH, Croatia, Serbia, and Slovenia.

Table 14: Global Peace Index: BiH, Croatia, Slovenia, and Serbia for 2023

	Country	**Score**
8.	Slovenia	1.334
14.	Croatia	1.45
61.	Bosnia and Herzegovina	1.892
65.	Serbia	1.921

Source: Global Peace Index https://www.visionofhumanity.org/maps/#/

We can see that Slovenia is ranked on 8th place, with score of 1.334. On the other hand, Croatia is ranked 14th, with score 1.45, while Bosnia and Herzegovina is ranked on 61st place with score of 1.892 and Serbia is on 52nd place with score 1.83 making it the least peaceful countries among these four. Within the Global Peace Index, Bosnia and Herzegovina got the highest score for political instability 3.25, while Croatia received score of 3.44 for security officers and police, and Serbia received 3 points for neighboring country relations.

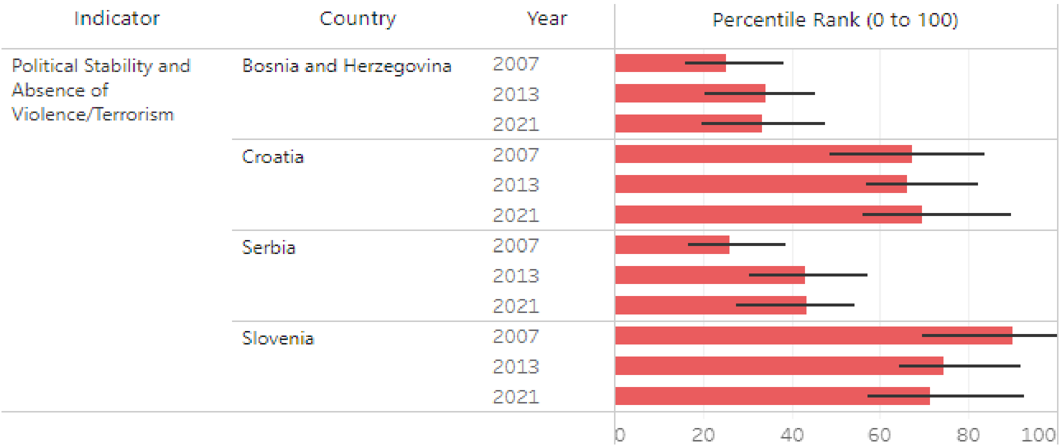
Many companies and business also assess risk by looking on the level of corruption in certain country, and that is measured by using corruption perception index (CPI). Countries are categorized and results go from zero, which indicates a highly corrupt country, up to one hundred, which is very clean i.e., not corrupted. As for countries which we are examining, the latest available data is for the year 2022, and they are ranked in this order:

- 41. Slovenia (score 56),
- 57. Croatia (score 50),
- 101. Serbia (score 36),
- and 110. Bosnia and Herzegovina (34).

By looking at these results we can see that Slovenia is ranked as “cleanest” i.e., lowest level of corruption, while Bosnia and Herzegovina and Serbia are ranked with higher level of corruption.

World Bank Data also offers ranks of the country with various government indicators. We took into consideration political stability and absence of violence/terrorism and government effectiveness. These indicators show a percentile rank which indicates the percentage of countries worldwide that rate below the selected country. Higher values indicate better governance ratings. A thin black line indicates this governance indicator's statistically likely percentile rank range. As Kaufman *et al*. (2010) explain that for instance, a bar of length 60% has the following interpretation: an estimated 60% of the countries rate worse and an estimated 40% of the countries rate better than the country of choice selected country. Political stability and absence of violence/terrorism indicators captures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically motivated violence and terrorism, according to Kaufman *et al*. (2010). From figure 2, we can see rankings for political stability and absence of violence/terrorism for these four countries in 2007, 2013 and 2021, unfortunately data for 2022 and 2023 are still unavailable. For Bosnia and Herzegovina, we can see slight improvement from the 2007, when the ranking was 25.12%, and it moved in 2021 to 33.49%. Croatia on the other hand, has been quite steady and in 2021 had percentile rank of 69.34, which is significantly better than Bosnia and Herzegovina. Serbia also had slight improvement. In 2007 percentile rank was 26.09, which is quite low while in 2021 rank was 43.40, which again is better than Bosnia and Herzegovina. Interestingly, Slovenia had a decrease from 2007 when the percentile rank was 89.86, which is quite good percentile rank and means that only 10.14% of countries had better rankings. In 2013 Slovenia’s percentile rank decreased to 74.41 while in 2021 it was 71.23%, which is still a better ranking and score than Bosnia and Herzegovina, Serbia, and Slovenia.

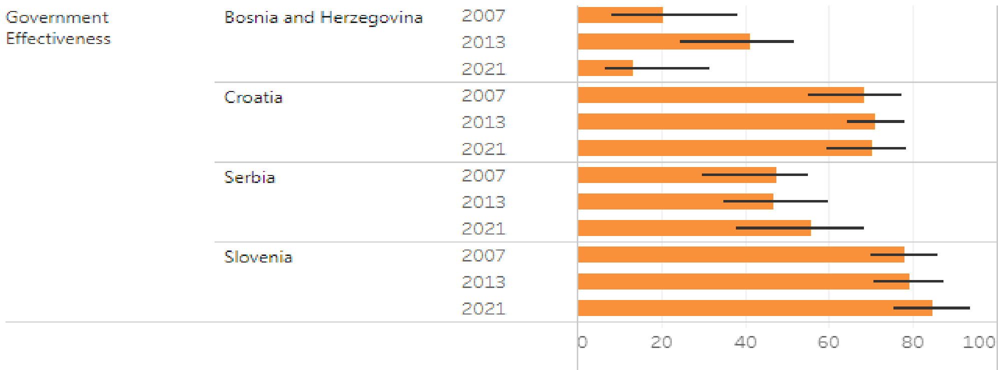
Figure 2: Political stability and absence of violence/terrorism



Source: Worldwide Governance Indicators. Available at: [*https://info.worldbank.org/governance/wgi/Home/Reports*](https://info.worldbank.org/governance/wgi/Home/Reports)

In figure 3, we see rankings for government effectiveness. Kaufman *et al*. (2010) also explain that this indicator captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

Figure 3: Government effectiveness

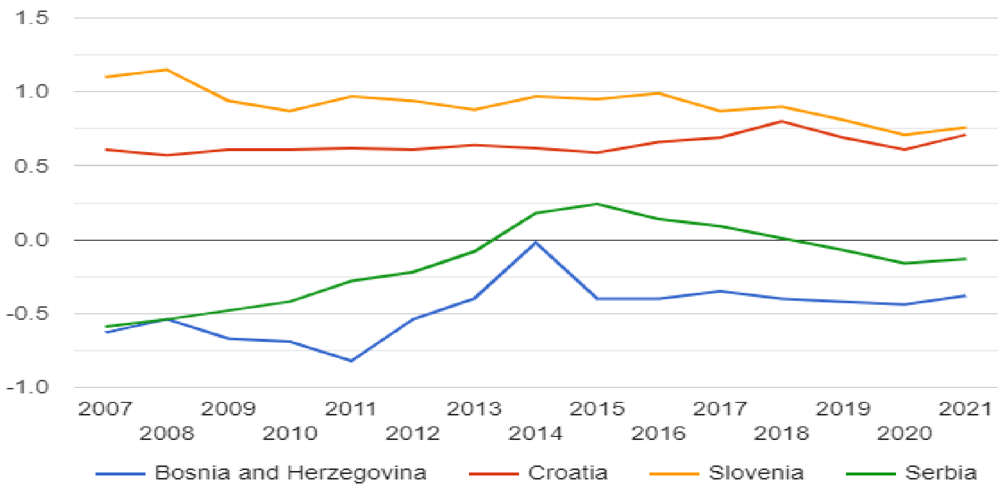


Source: Worldwide Governance Indicators. Available at: [*https://info.worldbank.org/governance/wgi/Home/Reports*](https://info.worldbank.org/governance/wgi/Home/Reports)

Bosnia and Herzegovina had a slight better ranking in 2013 where percentile rank amounted to 41.23, but in 2021 it decreased to 13.46 which is actually worse than in 2007 when it was 20.39. This means that in 2021, 86.54% of countries had better rankings than BiH and more effective government, better independence from political pressures and higher quality of public and civil services. As for Serbia, it had slight increase from 2007 when the ranking was 47.57% and in 2021 it was 55.77 which is higher than the ranking for Bosnia and Herzegovina. On the other hand, Croatia's ranking in 2021 was 70.19% and for Slovenia in 2021 84.62, which is significantly higher than Bosnia and Herzegovina's and Serbia's rankings.

In the Figure 4, we have collected data for political stability index for BiH, Croatia, Serbia and Slovenia from 2007 until 2021. Political stability index is ranged between -2.5 (weak) and 2.5 (strong). We can see for BiH that it has never actually gone beyond zero, so the political stability index has been week for all these years. While Croatia and Slovenia had better results, index has started to decrease in the few last years. In 2021, political stability index for BiH was -0.38, Serbia -0.13, Croatia 0.71 and Slovenia 0.76. This index shows the possibility of politically started and motivated violence, attacks and terrorism, and the likelihood of the government being overthrowned. Unfortunately for 2022 and 2023 data could not have been found.

Figure 4: Political stability index: BiH, Croatia, Serbia, Slovenia



Source: The Global Economy, Political Stability Index:
https://www.theglobaleconomy.com/compare-countries/

4.5.2. Economic and financial factors of Country risk: Bosnia and Herzegovina, Croatia, Serbia, and Slovenia

In this part we will take a look at some of the factors that are taken into consideration when calculating the economic and financial risk of a certain country. We will look at the data from 2007, 2013 and 2021 in order to get a more comprehensive and clearer picture of the situation in each of these four countries.

The first factor is the gross domestic product (GDP), which is a measure of a country's economic output per person. GDP shows us the economic development of a certain country and a higher GDP indicates that the economy is doing well. In tables 15 and 16, we have presented GDP per capita and real GDP growth for these four countries. We can see that Slovenia has the highest GDP per capita 29,291.4 USD, followed by Croatia with 17,685.3 USD. Both of these countries had a slight decrease in GDP per capita in 2013. On the other hand, BiH has the lowest GDP per capita, amounting to 7,143.3 USD and Serbia is not far behind with 9,230.2 USD.

Table 15: GDP per capita (USD): BiH, Croatia, Serbia, and Slovenia

	2007	**2013**	**2022**
BiH	3,936.9	5,025.1	7,585.4
Croatia	14,0469.3	13,871.3	18,413.2
Serbia	5,848.5	6,755.1	9,393.6
Slovenia	23,817.9	23,503.3	29,457.4

Source: The World Bank Data: GDP per capita (US$), Slovenia, Croatia, Serbia, BiH. Available at: https://databank.worldbank.org/reports.aspx?source=2&series=NY.GDP.PCAP.CD&country=BIH#

Interestingly, Croatia and Slovenia in 2013 had real GDP growth of -0.4% and -1% respectively, indicating that these two countries were in the period of economic recession and their economy had some difficulties. However, in 2022, they still had higher real GDP growth than BiH and Serbia.

Table 16: Real GDP growth: BiH, Croatia, Serbia, and Slovenia

	2007	**2013**	**2022**
BiH	5.9%	2.3%	3.9%
Croatia	5%	-0.4%	6.3%
Serbia	7%	2.9%	2.3%
Slovenia	7%	-1%	5.4%

Source: The World Bank Data: GDP growth (annual %) - Slovenia, Croatia, Serbia, BiH. Available at: https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=SI-HR-RS-BA&name_desc=false

According to the Trading Economics (2021), inflation rate is measured by the consumer price index (CPI) and reflects the annual percentage change in the cost to the average consumer of acquiring a basket of goods and services that may be fixed or changed at specified intervals, such as yearly. The study of Glova *et al*. (2020) states that "the higher the inflation rate, the higher the level of uncertainty about the economic environment of the country, and thus the perception of the risk of economic operators is higher." In the table 17, we have acquired data on inflation rates from the World Bank for BiH, Croatia, Serbia, and Slovenia. We can see that in 2013, BiH had a negative inflation i.e., deflation, meaning there was a decline in the prices. Investopedia (2022) says that this could happen due to an increase in productivity, a decrease in overall demand, or a decrease in the volume of credit in the economy. In 2022, inflation increased highly for all the countries, but the BiH had the highest inflation rate amounting to 14.0%. and Slovenia had the lowest one 8.8%.

Table 17: Inflation rates (annual %): BiH, Croatia, Serbia, and Slovenia

	2007	**2013**	**2022**
BiH	1.5	-0.1	14.0
Croatia	2.9	2.2	10.8
Serbia	6.4	7.7	12.0
Slovenia	3.7	1.8	8.8

Source: The World Bank Data: Inflation rates: Slovenia, Croatia, Serbia, BiH. Available at: https://databank.worldbank.org/reports.aspx?source=2&series=FP.CPI.TOTL.ZG&country=

Next factor which we collected data for is the current account as percentage of GDP. It presents the balance of the current account (sum of net exports of goods and services, net primary, and secondary income) in a country divided by GDP. The more deficits, the riskier the country is. Theoretically, the current account balance should be zero but that is impossible, so it indicates whether a country is in a surplus or deficit.

Table 18: Current account as percentage of GDP

	2007	**2013**	**2022**
BiH	-9.2%	-5.3%	-4.5%
Croatia	-7.8%	-1%	-2.1%
Serbia	-17.4%	-5.8%	-7%
Slovenia	-4.2%	3.3%	-0.5%

Source: The World Bank Data: Current account balance (% of GDP) Available at: https://data.worldbank.org/indicator/BN.CAB.XOKA.GD.ZS?locations=SI

If we take a look at all of the four countries in Table 18, we will notice that in 2022 they had a negative current account balance. It indicates that they are running a deficit i.e., they are spending and borrowing more than collecting.

And lastly, we have collected data for foreign debt as a percentage of GDP and total debt service as percentage of exports of goods and services. The foreign debt-to-GDP ratio is a commonly used metric to assess a country's debt burden and its ability to manage and repay its external obligations. A higher debt-to-GDP ratio implies that a larger portion of a country's economic output is used to service its debt, which can have implications for the government's fiscal stability and the overall health of the economy. Unfortunately, we could not find relevant data for this indicator for these four countries. Also, for total debt service as percentage of exports of goods and services, we could not find any data for Croatia and Slovenia, so we cannot compare it to BiH and Serbia. From the table below, we can see that total debt service as a percentage of goods and services for both BiH and Serbia has decreased in 2021, meaning a positive development and suggests that the burden of debt on the country's economy is decreasing relative to its overall economic output. Unfortunately, data for 2022 nor 2023 is still not available.

Table 19: Total debt service as percentage of exports of goods and services

	2007	**2013**	**2021**
BiH	7.96	20.66	13.81
Serbia	27.3	43.6	16.45

Source: World Development Indicators | DataBank (worldbank.org)

4.5.3. Country risk premium: Bosnia and Herzegovina, Croatia, Serbia, Slovenia

We have examined and looked at different aspects of country risk related to Bosnia and Herzegovina, Croatia, Serbia, and Slovenia. Before we make any final conclusions, we will additionally take and compare country risk premium for the aforementioned countries. In order to do this, we will return to one of the most important researchers when it comes to this topic.

Damodaran, in his researches, says that country's risk premium (CRP) is the extra return that investors request in order to compensate for the additional risk related to investments in a certain country. He also stated that the country's risk premium varies depending on the perceived risk of investing in a particular country and that it should be incorporated into the cost of capital calculation for international investments. In his research, he has developed a framework for estimating country risk premium that considers a range of factors, including political risk, economic risk, and sovereign risk. He has also written about the challenges associated with measuring and estimating country risk premium, including the limited availability of data and the subjectivity of risk assessments. The relationship between country risk and country risk premium is important in determining the cost of capital for firms operating in a specific country. A higher level of country risk will lead to a higher country risk premium, as investors require a higher return to compensate for the increased risk of investing in that country. The country risk premium is a measure of the level of risk associated with a specific country and is influenced by a range of factors, including the level of economic stability, the political environment, the level of corruption, and the level of financial stability in the country. In table 20, we can see ratings by Moody's, and country default spreads and risk premiums according to Damodaran's latest data published on the first of the January 2023.

Table 20: Country Default Spreads and Risk Premiums: BiH, Croatia, Serbia, and Slovenia (2023)

Country	**Moody's rating**	**Rating-based Default Spread**	**Total Equity Risk Premium**	**Country Risk Premium**
Bosnia and Herzegovina	B3	7.95%	17.16%	11.22%
Croatia	Baa2	2.33%	9.23%	3.29%
Serbia	Ba2	3.68%	11.13%	5.19%
Slovenia	A3	1.47%	8.01%	2.07%

Source: Damodaran A. (2023) Country Default Spreads and Risk Premiums. Available at: https://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/ctryprem.html

As for Moody's ratings we can see that Slovenia has the best rating A3 indicating low risk of default while Bosnia and Herzegovina is again on the other end with a rating of B3, which means that BiH is considered to be a subject to high risk. In the second column, we have rating based default spread which evaluates the equity risk premium based on the average default spread of countries which have the same Moody's rating. In the third column, we have Damodaran's calculation for total equity risk premium (ERP) which represents the "insurance" that investors require in holding a portfolio composed by risky assets, according to Donadelli and Prosperi (2011). And in the fourth column, we have calculated country risk premium. As already explained, a higher level of country risk will lead to a higher country risk premium, as investors require a higher return to compensate for the increased risk of investing in that country.

According to Damodaran's calculations we can see that Bosnia and Herzegovina has significantly higher country risk premium than Croatia, Serbia, and Slovenia. The lowest country risk premium has Slovenia 2.07% and Croatia 3.29%, meaning that these two countries also have lower level of country risk making them more suitable and open for investments, as investors will not require a higher return since the risk is lower. This would imply that our first hypothesis which states that BiH has higher country risk than Croatia, Serbia, and Slovenia is correct. The best rated country is Slovenia, then Croatia and Serbia. We will deliberate more on the results in the next part of the paper.

5. RESULTS AND FINDINGS

In this part of the paper, we will look back at the empirical research and compare results and findings with hypothesis set in the beginning. The three main hypothesis which were defined are:

1. BiH has higher country risk than Croatia, Serbia, and Slovenia.
2. Political risk is predominant in BiH and Serbia.
3. Country risk of Croatia started to decrease once they became EU member state.

From the empirical part of the paper, we can see that we cannot reject the first one as BiH does have a higher country risk than Croatia, Serbia, and Slovenia. From Damodaran's (2023) Country Default Spreads and Risk Premiums, we could see that BiH had higher country risk premium than other countries, meaning that investors require a higher return to compensate for the increased risk of investing in BiH than in the other countries we examined. BiH was also ranked in January 2023 with B3 rating from Moody's, which indicates that BiH is a highly speculative country. It had the lowest rating amongst these four countries. Croatia was ranked as lower medium grade, Serbia as speculative and Slovenia was ranked with the upper medium grade meaning it was the least speculative country and had the best rating. If we take another look at the presented political, economic, and financial factors we will see once again that BiH had the lowest results i.e., it would be considered as the riskiest country.

The second hypothesis stated that political risk is predominant in BiH and Serbia. If we compare Bosnia and Herzegovina and Serbia with Slovenia and Croatia in terms of the political risk, we will see that political risk is more predominant in these two countries. Bosnia and Herzegovina and Serbia are ranked with higher level of corruption, are also the least peaceful countries among these four countries according to the Global Peace Index and have weaker political stability index in comparison to Croatia and Slovenia. From the data we presented above for political risk in BiH, we can see that despite some improvements the situation is still not satisfactory. As there have been onoging tensions for years in BiH and fears of new conflict in BiH, it is safe to say that political risk is predominant in BiH.

The final hypothesis states that country risk of Croatia started to decrease once they became EU member state. As we already mentioned above, EU membership did bring a lot of positive effects for Croatia and contributed to a lower country risk and improvement in economic, politicial and financial stability of the country. Croatia had to align its political institutions and legal system with the EU stanards which helped strengthen democractic processes and institutions. An important benefit of EU membership for Croatia has also been increased market access to EU member states, which led to expanded export opportunities. Croatia also gained access to different EU funds aimed at supporting infrastructure development and stimulating economic growth of the country. From the data we have presented above in the empirical research, we could have seen that certain aspects have improved for Croatia and we say that country risk started to lower once they became a member of the EU. However, there are still some challenges that Croatia faces which need to be addressed in order to maintain sustainable economic growth and strengthen the country.

6. CONCLUSION

In this paper we analyzed and compare country risks for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia and saw that each country has its unique risk profile which is influenced by history background, domestic policies, geopolitical situation, and global economic conditions. We highlighted the importance of country risk analysis and assessment in the global markets and discussed country risk reports and analysis for these four countries. In addition, we also looked at credit rating agencies' reports and rates in order to have a comprehensive picture of the country risk for these countries. We discussed strengths and weaknesses of each country, compared them, and also took into consideration a country risk premium calculated by Damodaran, a well-known academic and researcher in the field of finance, who has made significant contributions to the study of country risk.

In conclusion, a variety of opportunities and challenges are revealed by the analysis of country risks for Bosnia and Herzegovina, Croatia, Serbia, and Slovenia. Since the end of the war in the 1990s, Bosnia and Herzegovina has made significant progress, but there are still issues that affect the country's overall risk profile. The country's political stability is still a major risk factor. Political tensions can result from complex political structures, numerous ethnic groups, and decentralized governance, which can also impact sound decision-making.

Despite recent modest economic growth, BiH continues to struggle with structural problems like high unemployment rates, an unregulated economy, and regional inequalities. Serbia is experiencing the same problems as Bosnia and Herzegovina. Serbia is also dealing with slow and low economic growth, corruption, a lack of government transparency, and tense relations with several neighboring nations. However, we need to keep in mind that Bosnia and Herzegovina and Serbia also have some good sides. These two countries have valuable natural resources, knowledgeable labor force and through the EU accession process, they are trying to strengthen the institutions, enhance the business environment and conform to the EU standards.

On the other hand, we have Croatia and Slovenia, a two EU member countries which have gained a lot of benefits from this. Slovenia has the lowest country risk compared to these four and it has achieved economic growth, political and financial stability. Croatia has made progress since joining the EU in 2013. It has complied with the EU standards and the rule of law. However, despite the positive outlook, some challenges remain. For Croatia and Slovenia, it is important to continue the path they have started and to invest in infrastructure, create additional jobs and invest in tourism, in order to maintain their economic and financial development.

And finally, we cannot reject hypotheses set at the beginning:

1. BiH has higher country risk than Croatia, Serbia, and Slovenia.
2. Political risk is predominant in BiH and Serbia.
3. Country risk of Croatia started to decrease once they became EU member state.

The empirical analysis in the paper concludes that Bosnia and Herzegovina has a higher country risk compared to Croatia, Serbia, and Slovenia. Bosnia and Herzegovina does have a higher country risk premium, indicating that investors require a higher return to compensate for the increased risk of investing in BiH. Moody's gave BiH the lowest rating among the four countries, indicating that it is a highly speculative country. Croatia has seen a decrease in country risk after becoming an EU member state, which has brought positive effects such as improved political stability, economic integration, and regulatory environment. EU membership has also led to increased trade, investment, and access to EU funding programs for Croatia.

And finally, it is important to also discuss some limitations and challenges we have faced while writing this research. One of the primary and biggest challenges was definitely the availability and reliability of data. It was difficult to obtain accurate and up-to-date information for these countries. We are not sure if this is just the case with these four countries but there was not a single unique site that offered available data for country risk analysis for countries in question. We often stumbled on complete country risk analysis for these countries, but one would have to set a significant amount of money to get access to those reports.

As we already mentioned a couple of times, country risk is dynamic and changes rapidly due to political, economic, or social events across the world. Limitation, which we already mentioned in the beginning of the paper, is that researchers and analysts have different methods and opinions on the significance of certain factors. Often country risk assessments involved a degree of subjectivity and personal judgment making it hard to take that data into consideration or compare it with other results.

Country risk analysis is a wide topic, and there are definitely several potential directions which can be taken to explore and expand this research. The first that comes to our attention is to increase the number of indicators and reference years, in order to get more comprehensive and accurate results which would definitely provide more detailed progress of each country. Another direction is also to analyze the relationship between country risk and investment performance and try to determine how risk levels affect investment returns and how investors behave across different countries.

This research paper has managed to analyze country risk aspects of Bosnia and Herzegovina, Croatia, Serbia, and Slovenia and highlighted the importance of assessing more than just one factor. Economic, political, and financial factors play a vital role in country risk analysis. Each country we discussed has its own historical background, unique strengths and weaknesses, and space for improvement. These countries can all achieve higher economic growth, financial and political stability if they do address the challenges and seize the opportunities.

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