



## Country Analysis Framework

This framework takes the nation as the unit of analysis. Effective managers must be able to analyze systematically the national and international environments in which they operate. This note presents a framework to help them do this.

Since government actions shape business environments, that is the starting point for country analysis. In this view, nations have strategic purposes, the capacity to mobilize resources, and the power to affect their economies. The country analysis framework has three interrelated components: strategy, performance, and context. Each of these has economic, political, and social dimensions.

All governments have a national strategy composed of explicit or implicit goals and a set of policies to achieve those goals. These lead to performance, which can be judged by assessing how well the country is doing economically, politically, and socially. These outcomes also depend on a country's context, which has domestic aspects (economic, political, social, institutional, and ideological) and international aspects (trading relationships, political links, multilateral institutions, global industries). In turn, the outcomes affect the context for future strategies. Thus, strategy, performance, and context are interdependent. Country analysis can therefore begin with any of the three components, but requires examining all of them.

Country analysis is not a mechanistic or deterministic process; it requires critically interpreting data, analyzing causal relationships, and assessing options. One can begin with the descriptive question: What is the country's strategy, performance, and context? But full analysis requires follow-on questions such as: Why did the government choose its strategy? How well did the country do (relatively, absolutely)? Why did these results occur? What caused what? Did the government's policies have the effects it sought? If not, why not? What was the influence of the different contextual factors?

Country analysis uses a historical perspective and takes a dynamic rather than static view. To understand a country's environment, it is necessary to view its evolution. Probing a country's past and present strategy, performance, and context better equips the manager to understand and analyze the possible future environment.

Ultimately the manager will interpret the phenomena in the macroenvironment in terms of their implications for his or her industry and firm. These implications will depend on the specific characteristics of each industry and company. However, a prerequisite for moving from the macro to the micro is the ability to analyze and understand the larger country environment. The country

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analysis framework enhances that ability. We now examine in more detail the framework's three components.

## Strategy

A government's national strategy is seldom delineated clearly and completely. The country analyst must deduce the strategy from various government statements and actions. Also, strategy is rarely wholly consistent, for it is generally the outcome of conflict or compromise between contending actors. Strategy analysis addresses the following general questions:

- What is the government's strategy (goals and policies)?
- What are the relative priorities among the goals?
- How are the policies interrelated? Are they contradictory or reinforcing?
- How will the policies contribute to achieving the goals?

## Goals

Governments' economic goals commonly include such things as GNP growth, price stability, full employment, and rising consumption. Political goals might include sovereignty, stability, preservation of a particular type of political system, or survival of a specific regime. Social goals might include improving the population's educational levels or health status, reducing income inequalities, or increasing housing. Sometimes governments set precise targets for these goals as part of national development plans. In other cases the goals may be vague or implicit.

It is important to assess the relative priorities among goals. Some economic goals may be more important than others (e.g., inflation vs. unemployment). Political goals might take precedence over economic goals; economic price tags are often forgotten when issues of independence or political survival are on the table. Sometimes social goals have high priority. Costa Rica, for example, chose education over defense by abolishing its army with the slogan "More teachers than soldiers." Country analysis requires assessing such tradeoffs.

## Policies

To achieve its goals, a government formulates and implements a set of policies. These can be usefully grouped into five categories: fiscal, monetary, incomes, foreign trade and investment, and sectorial (economic and social). The task is not simply to identify the policy components of the strategy but to analyze their logic and interrelationships.

- (1) *Fiscal Policies.* The government's budgetary policies can have far-reaching macro-economic effects. Tax cuts or spending programs have often been centerpieces in governments' economic strategies. One needs to examine which aspects of the economy will be affected (such as investment or consumption) and how. The ramifications of aggregate deficits or surpluses need to be analyzed. Specific tax and spending measures may reveal shifts in priorities and produce varying effects on particular groups or industries.
- (2) *Monetary Policies.* A government's influence over the money supply, banks, and credit affects consumption, savings, and investment behavior. Japan, Korea, and

other countries have used their control over credit allocation to promote the selective development of key industries. It is important to analyze how monetary policy is reinforcing or contradicting fiscal policy.

- (3) *Incomes Policies.* Concerns about inflation or income levels sometimes lead governments to control price and wage levels directly. Government intervention may deal with transitory economic disruption or have more basic income goals (e.g., minimum wage laws). A critical analytical issue is the interplay between such government intervention and market forces.
- (4) *Foreign Trade and Investment.* The international flow of goods and capital has risen dramatically during the last three decades. Export-led growth has been central to many countries' national development strategies. Foreign loans, direct equity investments, and technology flows have also played important roles in many countries' strategies. It is important to analyze the trade-offs involved in relying on such external resources. Tariffs, quotas, administrative requirements, subsidies, trade agreements, foreign-exchange rates, and capital controls are common policy instruments used to influence trade and investment flows.
- (5) *Sectorial Policies.* Government policies can also be aimed at specific economic sectors such as agriculture, heavy industry, and natural resources, and at social sectors such as education, health, and housing. Examples include fiscal subsidies to farmers, allowances for retraining workers in declining industries, and special credit facilities for home mortgages. In some countries a key sector is the focal point for the overall national strategy. The analyst should understand the role of each sector in the larger country strategy and the interrelationships among the sectors.

Government actions affect industry structure and dynamics and can have differential effects across industries and among firms within industries. Governments can erect barriers to entry through import protection or restrictions on the number of firms allowed in an industry. They can affect the intensity of rivalry within an industry by giving preferential access to resources (e.g., credit) to some firms and not others. Potential substitutes may be encouraged through government-funded research (e.g., alternative energy sources). Government influence over access to supplies (e.g., imports) may affect the bargaining power between buyers and suppliers.

## Performance

Analyzing a country's performance requires assessing how well it did and, more important, what gave rise to those results. Understanding causal relationships deepens the manager's ability to judge future actions and outcomes. The questions addressed in performance analysis include the following:

- What has been the country's economic, political, and social performance?
- What led to these outcomes?
- What are the implications of these outcomes for future strategy and performance?

## Performance Indicators

A number of *economic* indicators reveal distinct dimensions of an economy's performance. Changes in real GNP indicate aggregate economic growth, and shifts in GNP per capita relate this to average changes at the individual level. Price indices measure inflation. Unemployment and capacity utilization rates indicate resource usage. Wage and output levels reveal productivity and unit labor cost changes (for the whole economy or specific sectors). Balance-of-payments data can show international competitiveness and financial position with the external economy.

*Political* indicators might include the nature of the regime, frequency of changes, responsiveness of government to its citizens' concerns, incidences of civil unrest, the degree of external political dependence, and the preservation of human rights. Social indicators might be literacy levels, infant mortality rates, life expectancy, nutritional status, housing availability, and income distribution patterns.

## Performance Analysis

Analyzing performance involves interpreting these indicators and their relationships to reference points. Did the government accomplish what it set out to do? Is it doing better than before? The choice of an appropriate reference time period becomes an important consideration. Is the country doing better than other countries? Such cross-country comparisons can be useful but conclusions must take into account differences among countries' situations and analyze why the differences occurred.

To assess fully a country's strategy, it is necessary to judge to what extent the government's policies caused the performance. Links between specific policies and outcomes can be complex. Nonetheless, understanding these causal relationships and the public policymakers' perspectives is important to a manager's ability to evaluate and predict effects of government policies. This causal analysis requires probing the underlying variables. For example, to explain why a country's GNP grew at 8% annually, one could first examine what happened to the components of GNP (consumption, investment, government spending, and exports and imports). This might reveal, for example, that investment was experiencing the largest growth. Next, one could ascertain whether specific government policies were stimulating investment. This might reveal that investment tax credits had been used for this purpose along with lower interest rates. Understanding such multiple causality is part of the complexity of performance analysis. In some instances such analysis will reveal that different policies are inconsistent and have offsetting effects, thereby impeding desired outcomes. Performance is affected not only by policies but also contextual factors, to which we now turn.

## Context

A country's context includes domestic and international aspects. Contextual factors create constraints and opportunities for government policymakers. The key questions for contextual analysis are:

- What contextual factors shape the domestic environment?
- What are the key factors in the international environment?
- How do these factors influence national strategy?

- How do these factors influence country performance?

## Domestic Factors

**Economic.** A country's natural resources are critical determinants of its economic development. The discovery of oil in Saudi Arabia, for example, created a very different set of policy options for the government than existed before. The scarcity of natural resources in Japan confronted its government with options very different from those facing the U.S., a resource-rich country. Human capital is another key resource. Managers should analyze how these human resources and demographics facilitate or constrain a country's economic development.

**Political.** It is important to understand how a country's type of political system shapes its political processes. Differences can be drawn between democracies and authoritarian regimes, and within democracies one can distinguish between presidential and parliamentary structures and electoral systems. Political dynamics are driven partly by the underlying ideological and institutional factors discussed below.

**Social.** The social fabric of a society is often shaped by its ethnic composition. India, for example, has 14 major languages, 3,000 different dialects, and religious groups with deep-rooted differences. Such divisions can affect political processes and economic organization. Cultural values may also affect work behavior, business organization, and business-government relations.

**Institutional.** The country analyst should examine how the nature and interactions of a nation's economic, political, and social institutions affect government strategies and country performance. The organization, roles, relationships, and relative power of business, government, and labor are central. To understand the policy process, one may have to examine the roles and interactions of specific institutions such as political parties, trade unions, business groups, the military, or religious sects. How do these affect which policies are chosen and how they are implemented? How do they enhance or hinder performance?

**Ideological.** Ideology is the "set of beliefs and assumptions about values that the nation holds to justify and make legitimate the actions and purpose of its institutions."<sup>1</sup> There may be competing ideologies within a country. One should analyze how basic beliefs about the appropriate role of the state influence government actions and business-government-labor relations. Values concerning community welfare, individual freedoms, and property rights can influence a government's strategy.

## International Factors

**Trading Relationships.** On the international economic side, trading relationships with other countries are key. Sometimes geographical location is a determining factor; the shared borders of Canada and Mexico with the United States, for example, have made them primary trading partners, and it is similar with the European countries. In other instances historical political ties with former colonies have produced preferential economic relationships, for example, between Britain and France and many African countries. Political and cultural factors also sometimes influence trade.

**Multilateral Institutions.** A country's strategy or economic performance can be significantly affected by international agencies such as the International Monetary Fund (IMF) and the World Bank, international agreements such as the General Agreement on Tariffs and Trade (GATT), and

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<sup>1</sup> George C. Lodge, "Introduction: Ideology and Country Analysis," in George C. Lodge and Ezra F. Vogel, eds., *Ideology and National Competitiveness: An Analysis of Nine Countries* (Boston: Harvard Business School Press, 1987), p. 2.

economic groups such as the Organization of Petroleum Exporting Countries (OPEC) and the European Economic Community (EEC).

**Global Industries.** Lastly, many industries cut across national boundaries. Their dynamics can greatly affect countries whose economies are linked to them as buyers or suppliers, as the oil shocks of the 1970s and 1980s revealed. Understanding the nature and extent of a country's interdependence with global industries is critical to assessing strategy and performance.

## Conclusion

The country analysis framework assists managers in examining systematically a nation's strategy, performance, and context. **Figure A** presents a summary of the framework's data categories. It is essential to reiterate that country analysis consists NOT simply of assembling data, but rather critically interpreting information, analyzing historical patterns, understanding causal relationships, and assessing future scenarios and options.

Government actions can influence the competitive situation within a country and the competitiveness of national firms in international markets. Thus, central to the issue of national competitiveness are the relationships between business and government, between company strategies and country strategies, and between national economies and the international economy. The country analysis framework will help managers deepen their understanding of these critical relationships.

**Figure A** Country Analysis: Illustrative Data Categories

Context	Strategy	Performance
<p><b>Domestic:</b> Economic resources Political system Social structure Institutions Ideology</p> <p><b>International:</b> Trading relationships Multilateral institutions Global industries</p>	<p><b>Goals:</b> Economic growth Full employment Price stability Consumption Exports Political stability, sovereignty Educational, health, welfare improvements</p> <p><b>Policies:</b> Fiscal Monetary Incomes Trade and investment Economic sectors Social sectors</p>	<p><b>Economic:</b> GNP Unemployment Inflation Balance of payments Capacity utilization</p> <p><b>Political:</b> Independence Regime changes</p> <p><b>Social:</b> Literacy Health status Housing levels Income distribution</p>