
Article

Intergroup Biases in Assessing Political Risk: The Role of National Identity

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Geopolitics are back as a subject of inquiry in international business and have increased the threat of political risk for MNEs and domestic firms globally. However, firms may struggle to assess political risk accurately due to the social identity processes within top management teams that influence information seeking and processing. This article offers a brief introduction to an intergroup bias which can harm political risk assessments, namely managers filtering risk through a national identity lens. Focusing on the consequences of identity bias, we suggest ways in which political risk assessment may be made more effective for managers – and accurate.

INTRODUCTION: THE HUMAN FACTOR IN POLITICAL RISK ASSESSMENT

The international business literature is unanimous in acknowledging that geopolitics, dormant during the globalization of the 1990s and early 2000s, are back (Ciravegna, Hartwell, Jandhyala, Tingbani, & Newburry, 2023). The increase in sanctions, trade disruptions, the ongoing Russian invasion of Ukraine, and military escalation in the Middle East have brought back political risk to its Cold War footing (Table 1), forcing firms to reassess and update their political risk algorithms from the threats of the 1990s (Sottilotta, 2016) to include the threats of the 1970s (Jarvis & Griffiths, 2007). However, despite the long pedigree of political risk in the international business literature (Kobrin, 1979), even new scholarship such as De Villa (2023) fails to take into account a crucial factor in how firms assess geopolitical realities: the human factor in risk management and the socio-constructivist reality behind risk assessment.

The purpose of this article is to introduce the concept of intergroup bias in political risk assessment in Multinational Enterprises (MNEs) and to highlight its influence on firm decisions. We focus specifically on risk mitigation strategies but also note how bias may affect a panoply of other international business areas such as firm entry/exit, modes of entry, and internationalization – and how to overcome these biases. We argue that top management teams or even entire organizations (as conduits of identity) may interpret environmental signals from foreign markets through the lens of national identity, defined as a sense of belonging to a community with shared nationalistic roots, along

with associated national interests, history, ideologies and cultural stereotypes (Vaara, Tienari, & Koveshnikov, 2021). National identity is not limited to “nationality” but is instead a shared understanding among managers of what it means to be a citizen of their respective nations (in-group) (Monzani et al., 2024) as opposed to foreign nations (out-group); it is the difference between understanding what a “country” is and what a “nation” is. However, this socially constructed reality can also apply to clusters of nations such as “we – emerging” versus “they – from advanced countries,” engendering similar loyalties.

National identity can thus encompass traditionally used views of (psychic, cultural, geographical) distance (Harzing, 2003; Vaara et al., 2021) as a proxy for high uncertainty and political risk but adds an additional dimension to understanding political risk. We argue, however, that firms which are associated with a specific national identity related to the home market often interpret signals from hosts markets – and make decisions – similar to other firms associated with this national identity, biasing basic decisions for an MNE. This concept of national identity, and how it filters through a firm, is thus crucial to explaining biases in risk assessments and helping to improve risk assessments in an increasingly more uncertain world.

THE SOCIAL IDENTITY APPROACH TO RISK

A land war in Europe which Russia began in 2014 and escalated in 2022, a pandemic which was unleashed on the world by an authoritarian state and whose provenance remains disputed, and an eruption of war in the Middle East supported by rogue states has provided MNEs with disrupt-

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Table 1. Main Sources of Political Risk by Decade

Decade	Main Sources of Political Risk
1950s-1960s	Interstate warfare, confiscation/expropriation/nationalization
1970s	Interstate warfare, nationalization, internal strife (civil war), terrorism
1980s	Interstate warfare, terrorism, political uncertainty (including revolution)
1990s-2000s	Terrorism, political uncertainty, institutional change, civil war
2010s-2020s	Terrorism, political uncertainty, institutional change, pandemics
2020s-?	Interstate warfare, terrorism, political uncertainty

Source: Adapted from the text in Hartwell and Devinney (2022).

tions which are unlikely to be captured in existing political risk algorithms. Unfortunately, political risk assessment and related decisions may be inaccurate not only due to inherent traits of risk assessment (i.e., asymmetric/incomplete information), but additionally due to biases in decision-making within the firm. Indeed, a number of cognitive biases may plague management in dealing with political risk, including the overuse of heuristics (Maitland & Sammartino, 2015) or reliance on tried-and-true cognitive styles despite their possible unsuitability in a specific situation: for example, a firm from a country with greater governmental involvement in the economy may be more attune to the risks of “state capitalism” and thus more accurately price risk than a firm without this background. At the same time, however, the experience of the firm in similar situations may instill overconfidence in the management team’s abilities to accurately estimate risk (or ignore other sources of risk beyond the familiar) and thus generate bias in assessment (Das & Yaghoubi, 2023).¹ Similarly, a firm from a developing country may have political connections which ease the cost of doing business, contributing to underestimation of risk in countries where these connections do not exist.²

Perhaps the greatest threat to accurately assessing political risk for a firm may come from a manager’s or a firm’s cultural surroundings and, in particular, their national identity. In intergroup situations, individuals might not act on the basis of their individual characteristics, but as a member of a pre-defined group; this is the core tenet of social identity theory (SIT), which posits that people’s behavior is shaped by their group membership and how this group relates to other groups (Tajfel & Turner, 1979), while self-categorization theory (SCT) explains how and when people define themselves as group members – as well as examining the impact of this variability on self-perception to better understand group behavior vis a vis other groups (“we” vs. “they”). In IB, there has been an emphasis on organizational identity (Raskovic & Takacs-Haynes, 2021) but less focus on how SIT applies for national identity, an oversight which can account for problems in the case of cross-

cultural confrontations or politicized and competitive relationships (Vaara et al., 2021).

This reliance on a social (national) identity can result in two, interrelated, intergroup biases in political risk assessment. First, **in-group/out-group derogation**, creates a shared understanding among managers about what it means to be a citizen of their respective nations, “who we are” (Monzani et al., 2024). Such a national identity encompasses culture and geography, but also is shaped and tempered by history. For example, although Colombia and Venezuela share a common language, familial ties across the country border, and the dominance of mestizo (mixed European/indigenous) ethnic groups, citizens from each country define themselves very differently; the countries have had many border disputes (even before they were formally countries), and they have ingrained stereotypes about each other. We argue that media framing, stereotypes, historical experiences, and even regular interactions frame one national identity vis a vis another. Identity divergence can happen even where formal institutions are similar across countries, explaining (for example) why employees of subsidiaries or acquired firms tend to identify more strongly with their local organization rather than global headquarters (Łupina-Wegener, Schneider, & Van Dick, 2015; Reade, 2001).

However, reliance on identity may also lead to overgeneralizing or underestimating specific risks to an entire country or region due to the in group/out group effect. A prominent example of this is emerging markets as a host market for MNEs: China was viewed as becoming increasingly democratic in the 2010s (Baack, Dow, Parente, & Bacon, 2015), while Russia in the 1990s was appreciated by US based MNEs for its apparent commitment to transitioning to a market economy (Puffer, McCarthy, & Zhuplev, 1998). This perception may have led to an underestimation of the true risk of doing business, as the illusion of narrowing distance was based on a national identity reference point i.e., “democracy,” or “market economy,” rather than reality (indeed, restrictions on foreign investment were quite stringent at this time in China, and corruption was very high

¹ Thanks to an anonymous referee for suggesting the framing of state capitalism.

² Thanks to the other anonymous reviewer who suggested this point.

in Russia). As a counterfactual, Finnish MNEs (with a complex historical relationship with Russia) displayed concerns about political risks in Russia even before 2022 (Koveshnikov, Vaara, & Ehrnrooth, 2016).

In addition, a perception of a “safe” country in which to internationalize may also be colored by the relative status of the home to the host country (Yildiz & Fey, 2016), often reflecting geopolitical relations or overall stereotypes. For example, Russian firms in the 2000s internationalized *en masse* into the former Soviet republics in Eastern Europe and Central Asia, seeing their shared history and (for the most part) similar political trends – as well as the dominance of the Russian economy over these markets and the perception of these countries as rightfully in Russia’s sphere of influence – as benefits for the firm (Panibratov, 2015). However, this bias has led an ignoring of the political risk of countries attempting to move away from Russia’s political influence, such as Ukraine (most prominently) and Moldova, as well as creating overconfidence in Russian firms who wished to internationalize into Europe.

Second, an **in-group/out-group derogation might be reinforced by the intergroup sensitivity effect (ISE)**, namely the tendency of in-group members to be more receptive to criticism of their group but reacting more strongly to negative evaluations from members of an out-group (Hornsey, Oppes, & Svensson, 2002). ISE might lead risk management teams to a tendency to favor information or interpretations that confirm prevailing opinions while disregarding contradictory information, especially when it comes from out-group sources (including managers located in MNE subsidiaries), creating reinforcement within social “bubbles” (Vaara et al., 2021). Liang, Ullrich, Van Dick, & Lupina-Wegener (2021) reveal that, even in mergers and acquisitions (M&As) where learning is the motive, people tend to act more defensively toward criticism from an out-group, potentially jeopardizing the success of the M&As. They also show that even if the out-group criticism was perceived as constructive, the out-group critic was derogated, a case of “shooting the messenger.”

In this vein, studies indicate that firms from “Western” home markets with similar characteristics tend to exhibit similar patterns in their political risk assessments facing geopolitical tensions and subsequent market commitment decisions (Cui, Vertinsky, Wang, & Zhou, 2023). This bias is not limited to the Western bloc, however, as a key example of this predilection from a non-Western viewpoint is the reality that firms whose home country have autocratic governments tend to perceive host markets with autocratic governments as less risky (Clegg, Voss, & Tardios, 2018). If such decisions are grounded in national identity, then the pernicious effects of this cognitive bias can be more widely spread than just affecting one type of firm’s political risk and indeed represent a major distortion in firm thinking.

RECOMMENDATIONS: OVERCOMING – OR MINIMIZING – BIAS

Understanding decision-making biases is crucial to improve political risk assessments for firms but in particular for MNEs. This note has begun to shed light on some of these biases, highlighting that national identity implies an intergroup bias which can influence political risk assessments and create inaccuracies, both through distorting the lens via which another country is analyzed (and leading to harmonized perceptions) and by derogating information from out-groups. Although the awareness of bias does not necessarily lead to better decisions (Milkman, Chugh, & Bazerman, 2009), awareness may help to create a more realistic risk profile, if simply by forcing decision-makers to attempt to reduce the salience of national identity.

Apart from mere knowledge of the bias, firms can take specific actions to minimize its effects in political risk assessment and consequently strategic decisions such as new market entrance, market investment, or market exit, in addition to planning “normal” risk mitigation strategies.

With regard to *in-group/out-group derogation*, we recommend that firms:

1. PROMOTE CULTURAL AND NATIONAL DIVERSITY IN TOP MANAGEMENT AND RISK MANAGEMENT TEAMS (TMTS)

Members of TMTs should represent the key markets where a MNE operates, hiring managers from varied backgrounds and with varied viewpoints, as well as making international experience for local hires, especially in culturally distant countries, an important selection criterion. Particular attention needs to be put into status attributed to particular nationalities (e.g., racial majority or minority)⁵ and gender to mitigate biases in assessment (Park & Westphal, 2013). This might help firms better assess market entrance or investment decisions and help to break the role of the firm as a transmission belt for national identity bias.

2. HIGHLIGHT “ATYPICAL” OUT-GROUP MEMBERS IN RISK ASSESSMENTS

Social psychological research (Yetkili, Abrams, Travaglino, & Giner-Sorolla, 2018) shows that out-group prejudice is reduced when in-group members are confronted with “atypical” or “anti-normative” out-group members. Risk management teams and TMTs should thus highlight such anti-normative policymakers or personalities during risk calculations in an attempt to both lessen national identity bias and improve the accuracy of risk assessment.

3 Thanks to an anonymous referee for suggesting we account for hierarchy, stereotyping, or status asymmetries.

3. INVOLVE INTERDISCIPLINARY AND INTERGENERATIONAL TEAMS TO CHALLENGE THE DECISIONS OF TOP MANAGERS

Beyond merely hiring diverse viewpoints, senior executives must listen to individuals within their organizations who may not align with the mainstream, creating procedures and mechanisms which can integrate diverse perspectives from those outside the core group to enhance the accuracy of assessments. While risk assessment often relies on various sources within and outside of the organization, the standard operating procedures of a firm may unwittingly homogenize the analysis of these sources along national identity lines. To avoid this reality, there needs to be a broader democratization of the process of assessing risks within an organization, so as to involve different viewpoints from front-line and customer-facing staff. This will provide a broader approach to quantifying risk, one not necessarily informed solely by national identity, particularly relevant for strategic investment decisions.

Similarly, there can be ways to deal with the *intergroup sensitivity effect*:

4. CONSTRUCTIVE CRITICISM FROM AN OUT-GROUP VIEWPOINT CAN HELP IDENTIFY BLIND SPOTS IN GROUP DECISION-MAKING

As constructive criticism from out-group members tends to be downplayed, being aware of the ISE could help managers to think twice when they are about to reject such criticism. Risk management teams might want to increasingly rely on inputs from boundary spanners, leaders who uniquely bridge gaps and interact with internal stakeholders, e.g., local subsidiaries and academics, bringing bring information directly from local players in the host markets to challenge/criticize head office risk assessments. Indeed, members of TMTs might want to seek information from policymakers in host markets themselves and have their information interpreted by local analysts and subsidiary managers rather than analysts from headquarters alone. As policymakers are the source of political risk, developing intelligence and outreach channels directly can help to cut through inaccurate perceptions and provide more real-time information. These local insights must be taken with humility – both at the managerial level and as part of procedure – a trait which can make managers “more amenable to divergent viewpoints” (Van Tongeren et al., 2016: 200).

5. PROVIDE CRITICISM FROM A SHARED IDENTITY

Those within the MNE who provide constructive criticism also need to be aware and sensitive to a range of variables wrapped up in group memberships, historical factors, and the overall intergroup context. For example, in host market risk assessment, subsidiary managers need to be aware of the social identity of the headquarters, the history, and the

context which might make national identity salient in intergroup dynamics (Hornsey & Esposito, 2009). This should translate into criticism being couched in firm identity terms – a shared “we” instead of an in-group/out-group dichotomy or a “we versus they” built along boundaries formed by national identities. Local managers also need to be proactive in identity leadership (Haslam, Reicher, & Plautow, 2011; Monzani et al., 2024), serving as a conduit between the MNE’s identity and the local identity (and back again), intentionally cultivating the identity of the MNEs within the local subsidiary.

CONCLUSIONS

As this article is only an opening salvo to bring together social psychology and political risk for IB, there is much still to be done. The policy literature, e.g., Stolwijk and Vis (2021), has begun to explore how the human mind grasps risk in a political setting, and these examinations need to be applied in the IB realm. We argued that a manager’s national identity can imply biases in risk assessments, something which can have large ramifications in a world characterized by geopolitical tensions and uncertainty. Our analysis relies on social identity theory to identify two intergroup biases and derive four recommendations on mitigating national identity salience, but we acknowledge that there is much work still to be done from both the research and the practical side, in particular in the design of political risk assessments to minimize these biases. Thus, this is not a conclusion but a beginning, hopefully pointing the way to more efficacious – and accurate – risk assessments in firms in the future.

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