

# Oppressive Regimes: A guide for investors

This briefing outlines the risks for investors with holdings in companies that operate or have supply chains in oppressive regimes. We highlight how investors can engage with companies to minimise these risks, and also ensure that their investments are not supporting the oppressive regime.

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## What is an oppressive regime?

There is no universally accepted definition of an 'oppressive regime', but the term is generally used to refer to countries where there are "laws, customs or practices that systematically produce inequalities that oppress specific groups within a society."<sup>1</sup> The systematic abuse of human rights is a common feature of oppressive regimes, and the regimes are often characterised by: leaders with a lack of democratic accountability; absence of the rule of law; arbitrary use of torture, execution and other harsh punishments; suppression of civil society and free media; lack of freedom of expression, religion or movement; and persecution of certain groups in society.<sup>2</sup>

## Which regimes are most oppressive at the moment, and where can that information be found?

As there are many different factors associated with oppressive regimes, it is not possible to produce a definitive ranking of how oppressive countries are. However, there are many reports which examine certain aspects of oppression and produce reports showing how different countries and regimes perform on these aspects.

One source of information is the annual Freedom House report, *Freedom in the World*,<sup>3</sup> which evaluates the level of freedom in countries and regimes around the world. Countries are awarded a score based on political rights and civil liberties, including electoral process, functioning of

government, freedom of expression, association and organisational rights, and individual rights. The lower the score, the more oppressive the country is considered to be. In 2016, Freedom House identified the 12 worst countries for political rights and civil liberties as: Syria; Tibet; Somalia; North Korea; Uzbekistan; Eritrea; Turkmenistan; Western Sahara; Sudan; Central African Republic; Equatorial Guinea; and Saudi Arabia.

Another relevant source of information is the Global Democracy Ranking, which scores countries according to how democratic they are (also taking in to account gender, economy, knowledge, health and the environment) – those achieving the lowest scores in 2015 were Yemen, Syria, Pakistan, Cote d'Ivoire, Togo, Egypt, Nigeria, China, Guinea and Mali.<sup>4</sup> Similarly, the Rule of Law Index examines how the rule of law is experienced in countries all over the world. It awards scores based on Constraints on Government Powers, Absence of Corruption, Open Government, Fundamental Rights, Order and Security, Regulatory Enforcement, Civil Justice, and Criminal Justice. The countries which were identified as having the worst rule of law in 2015 were Venezuela, Afghanistan, Zimbabwe, Cambodia and Pakistan.<sup>5</sup>

On press freedom, the Committee to Protect Journalists produces an annual report on attacks on the press, which identifies countries with a lack of press freedom. In 2015, the report identified Eritrea,

North Korea, Saudi Arabia, Ethiopia, Azerbaijan, Vietnam, Iran, China, Myanmar and Cuba as the most censored countries in the world.<sup>6</sup> On personal freedom, the Legatum Prosperity Index looks at personal freedom as one of its categories, and identifies Yemen, Sudan, Egypt, Syria, Haiti, Angola, Jordan, Algeria, Mauritania and Afghanistan as the 10 worst countries for personal freedom.<sup>7</sup>

The table in appendix 1 shows how countries are ranked by each index. As can be seen, whether a company or regime is defined as oppressive can depend on which factors are considered to be most significant. The list of countries which are defined as operating under an ‘oppressive regime’ may also change quickly if there is a sudden change in leadership, for example. However, it is possible to see that some countries are consistently identified as oppressive, so an investor may wish to pay particular attention to assets linked to these countries.

## How might an investor be supporting an oppressive regime?

Companies which operate, or offer services, in countries governed by oppressive regimes may be supporting the regime. These companies may do so indirectly if their presence supports the regime through creating economic and political stability. Companies may also indirectly support an oppressive regime if part of their supply chain is in that country. For example, companies with Uzbek cotton in their supply chain have been accused of indirectly supporting the oppressive government of Uzbekistan, which forces its citizens to pick cotton.<sup>8</sup> Another specific example is that of mining companies operating in Eritrea, which have been forced to use workers essentially enslaved by the state under strict national service requirements.<sup>9</sup>

Alternatively, a company may directly support the regime if its activities help the regime to implement its oppressive policies. For example, some companies support oppressive regimes by supplying these regimes with the tools they need to oppress citizens, such as surveillance systems or weaponry.<sup>10</sup> Similarly, technology companies that comply with government demands, for example shutting down internet or mobile phone networks during protests or providing data to governments on dissidents, are supporting the oppressive actions of the regime.

Investors which hold the sovereign bonds of countries which are oppressive, or which support other oppressive countries, are also likely to be

supporting the regime by providing it with financing through these bonds.

## What risks are associated with investing in oppressive regimes?

It is important for an investor to be aware of whether their investments may be linked to oppressive regimes, as there can be risks associated with this. Companies operating in oppressive regimes may face operational risks, leading to financial risks, if a government decides to close down the business or its services for a period. For example, the shutdown of internet services in Egypt by the Egyptian government in 2011 for five days resulted in direct costs of at minimum USD \$90 million due to lost revenue, according to the Organisation for Economic Co-operation and Development (OECD).<sup>11</sup> Situations such as these also result in senior management having to dedicate time to the incident, which reduces their focus on other parts of the business.

Another particular risk for companies operating in, or supplying goods to, oppressive regimes is reputational risk. For example, Canada-based company Streit Group, received significant negative media coverage when it was discovered that it had been supplying armoured vehicles to the Libyan and South Sudanese governments, the supply of which has been linked to increased instances of human rights abuses in these countries.<sup>12</sup> Investors which invest in companies operating in oppressive regimes, or hold the sovereign bonds of oppressive regimes, may face reputational risks associated with these.

Companies operating in oppressive regimes may also face legal risks. For example, the UN recently issued a declaration stating that ‘internet kill switches’ are impermissible under international human rights law, so companies which are asked to shut down their services by governments might find themselves in breach of international law. Similarly, some companies may be breaking their own government’s laws by operating in oppressive regimes, if sanctions are issued. For example, in 2011 the EU passed a resolution which banned “overseas sales of systems that monitor phone calls and text messages, or provide targeted Internet surveillance, if they are used to violate democratic principles, human rights or freedom of speech.”<sup>13</sup>

## Should all investments associated with an oppressive regime be avoided?

If an investor wishes to avoid any investment that might support an oppressive regime, they may wish to divest from any company that itself operates in an oppressive regime, or whose supply chain operates in an oppressive regime. However, divesting from any company with part of its operations in an oppressive regime may seriously limit the available investment universe. There is also evidence that companies can play a role in reducing incidences of human rights abuses in countries where they operate. For example, a study found that introducing economic sanctions, which limit the activity of businesses in a country, usually increases the cases of human rights abuses in that country.<sup>14</sup> Investors may therefore wish to consider staying invested in companies operating in oppressive regimes, and engaging with them to encourage them to act in a way that reduces oppression. For example, a company operating in an oppressive regime may be able to lobby that government to improve their human rights practices. It has been suggested that whether or not a company operating in an oppressive regime is able to have a positive influence on the human rights situation will depend on the type of regime they are operating in. Under an authoritarian, but not totalitarian, regime companies may be able to raise standards through commercial and social investment, without supporting the regime. Under more totalitarian regimes however, it is likely that companies will end up assisting the oppressive regime.<sup>15</sup>

## What can investors do?

One option for investors is to avoid any investment associated with an oppressive regime, including sovereign bonds, and companies with links to oppressive regimes. An investor who wishes to do this may wish to add this screen to their investment portfolio. There are also indices, such as the MSCI Human Rights Index, which investors can utilise to avoid investing in companies that may be supporting oppressive regimes.

For investors who choose to remain invested in companies associated with oppressive regimes, it is important to engage with them to ensure they act in a way which benefits people rather than the regime. Investors should make sure that these companies have policies and practices in place to ensure that their activities do not support these regimes. For example, companies which are signatories to the UN Global Compact have committed to making sure they are not complicit in human rights abuses,

so investors could look for companies that have signed up to this. Investors can also engage with the companies they are invested in about improving their practices – for example, they could ask companies to publicly condemn the oppressive practices of the companies they operate in, and refuse to support state requests for assistance in repressing their population.

Below are some questions which an investor wishing to engage with this issue can ask their asset manager(s) and investee companies.

## Questions to ask companies

- Is any part of your operation taking place in a country defined as an 'oppressive regime'?
- If yes, what steps are you taking to engage with the governments of these countries about their treatment of citizens, if any?
- Have you issued a public statement condemning the oppressive practices of these companies? If not, would you be willing to do so?
- What policies and practices do you have in place to ensure that workers within your own company and supply chain are not forced labour?
- What assessment have you made of the financial risks of operating in countries with oppressive regimes?
- What assessment have you made of the risks to people of operating in countries with oppressive regimes?

## Questions to ask asset managers

- Do any of the companies in the investment portfolio have operations taking place in countries that are defined as oppressive regimes?
- What is your approach to engaging with companies about where they hold their operations? How are you making sure that companies have the necessary policies and practices in place to ensure that they are not supporting the activities of oppressive regimes?
- What is your assessment of the risks and benefits associated with companies operating in oppressive regimes, both financially and in terms of human rights?
- Do you engage with policy makers about oppressive regimes?

# Appendix 1

Country	Freedom in the World	Global Democracy Ranking	Rule of Law Index	Committee to Protect Journalists	Legatum Prosperity Index
Syria	1	2			4
Tibet	2				
Somalia	3				
North Korea	4			2	
Uzbekistan	5				
Eritrea	6			1	
Turkmenistan	7				
Western Sahara	8				
Sudan	9				2
Central African Republic	10				
Equatorial Guinea	11				
Saudi Arabia	12			3	
Yemen		1			1
Pakistan		3	5		
Cote d'Ivoire		4			
Togo		5			
Egypt		6			3
Nigeria		7			
China		8		8	
Guinea		9			
Mali		10			
Venezuela			1		
Afghanistan			2		10
Zimbabwe			3		
Cambodia			4		
Ethiopia				4	
Azerbaijan				5	
Vietnam				6	
Iran				7	
Myanmar				9	
Cuba				10	
Haiti					5
Angola					6
Jordan					7
Algeria					8
Mauritania					9

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