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# INVESTIGATION INTO RISK TYPES FOR INVESTORS IN EMERGING MARKETS

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## ABSTRACT
Due to the numerous compelling reasons that draw investors to emerging economies, an increasing number of investors are concentrating on these areas. Identifying risk types for emerging market investors was the aim of this study. To analyse the data, descriptive statistics were employed. Exchange rate risk, nation risk, market risk, inflation risk, interest risk, financial risk, credit risk, liquidity risk, legal risk, and technology risk were the risk categories for investors in emerging markets, according to the data. Furthermore, it was shown that the top five risk types were technological risk, market risk, nation risk, exchange rate risk, and inflation risk. When making investments in emerging economies, investors want to take these risk categories into account. This study added to the corpus of information and gave developing market investors fresh perspectives on different kinds of risk. To ensure a structured strategy when investing in developing markets, it is therefore advised that investors who choose to do so take into account the risk categories found in this study as well as the top five risk factors.

## KEY WORDS
Risk types, investors, emerging markets, financial markets.

For investors, making money in emerging markets can be both profitable and risky. Rapidly expanding economies and more investment opportunities are features of emerging markets, but investors also need to be aware of several hazards (Baatwah, Almoataz, Omer & Aljaaidi, 2024). These risks fall into several categories, such as political, economic, currency, and liquidity concerns. Volatile economic conditions, such as high rates of inflation, erratic interest rates, and unpredictable government actions, are frequently associated with emerging markets. Because they can cause abrupt changes in asset prices and investor returns, these economic uncertainties can have a substantial effect on the performance of investments in emerging markets (Haroon & Rizvi, 2021). Changes in foreign currency rates can have a substantial positive or negative influence on the value of investments made in foreign currencies. Furthermore, if exchange controls or other limitations are in place, investors may encounter difficulties when trying to repatriate their money from emerging market investments (Wasiuzzaman, Chong & Ong, 2022). The financial markets and trading infrastructure in emerging nations may be less developed, which can make it challenging for investors to buy or sell assets swiftly and fairly. Investors may be more at risk of losing money as a result of this lack of liquidity, particularly in volatile market conditions. For investors looking for high returns and diversification, investing in emerging markets might present appealing options (Giaquinto & Bortoluzzo, 2020). Notwithstanding, it is imperative for investors to comprehend and meticulously evaluate the diverse hazards linked to investing in developing economies, including economic, political, currency, and liquidity hazards. As a result, research in this field is crucial and needs more attention. Studies on the many risk factors that investors need to take into account before making an investment in emerging economies are scarce. Nevertheless, established markets were the focus of a small number of noteworthy studies that examined different risk categories ( Proksch, Stranz & Pinkwart, 2018; Giaquinto & Bortoluzzo, 2020). As a result, this study is significant when considering emerging markets. Determining the risk categories that investors in emerging economies should take into account is the objective of this study.

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## LITERATURE REVIEW

According to Leeds (2015), an emerging market is one that is sufficiently open to the world economy to support free commerce between nations while also granting access to its bond and stock markets for foreign investors. Not every emerging market makes for a profitable investment, claims Amadeo (2017). Certain emerging markets have used the increase in commodity prices during the 2008 financial crisis to boost their economies. Certain developing nations chose to use their excess cash for government employment and subsidies rather than infrastructure investment (Abiad et al., 2012). Their people bought a lot of imported goods as a result, which caused their economies to grow swiftly and inflation to become an issue.

Following the 2008 financial crisis, emerging market shares have outperformed US stocks significantly, despite the fact that inflation has begun to rise. If the currency keeps declining, some market analysts predict that US equities will outperform them much more (Gundlach, 2017). If investors begin to rally behind emerging market currencies, Gundlach (2017) cautions that developing markets will probably continue to outperform the US. Consequently, this might be a good moment to invest in emerging markets. Strong US dollar values are frequently seen negatively by emerging nations since they lower the value of their commodities and increase the amount of debt denominated in US dollars (Sanchez, 2017). The features of emerging markets are the subject of the following section.

Cerutti, Claessens, and Puy (2015) state that rising markets share five common traits. They are poorer than average in terms of per capita income. Since it encourages the second crucial characteristic—rapid growth—low income is the first important characteristic. High volatility is the third attribute that results from rapid expansion. Natural disasters, external price shocks, and unstable domestic policies are the three main causes of high volatility (Kuepper, 2016). The need for significant investment capital is an emerging market's fourth attribute. The fifth feature—a high return on investment for investors—can also result from an emerging market's quick growth if an investment there is effective.

The majority of investors disagree about how different risk categories are. It is important to precisely identify and evaluate each risk category as well as any possible impact on investments in emerging markets, notwithstanding the opinion of some that this discussion is pointless. Investors should be able to manage risk and recognise it proactively, safeguarding their capital, with this awareness. Chapman (2013) and Saunders and Cornett (2018) identify the following as the primary risk types that should be examined when thinking about making an investment in emerging economies.

The unpredictability of returns for an investor purchasing securities denominated in a foreign currency is known as exchange rate risk (Salvatore, 2015). This idea is also occasionally referred to as "currency risk." The phrase "exchange rate risk" is utilised for this investigation. Exchange rate risk, according to Madura (2017), is a type of risk brought on by changes in the value or price of one currency relative to another. According to Saunders and Cornett (2018), exchange rate risk is the possibility that shifts in exchange rates will have an impact on the value of an investor's foreign currency-denominated assets and obligations. Exchange rate risk affects investors and businesses whenever they hold assets or conduct business internationally.

Exchange rates are subject to significant fluctuations based on changes in economic conditions, including import and export trends. According to Madura (2017), depreciation is the term used to describe a decrease in a currency's value and appreciation to describe a rise. According to Godi (2013), if a foreign currency's spot rates are compared at two different times. If the percentage change is positive, it indicates an increase in value of the foreign currency, and if it is negative, it indicates a decrease in value. When purchasing foreign assets or investments, emerging market investors may benefit from currency appreciation. However, a strong domestic currency might be unfavourable when emerging market investors expropriate returns, meaning the rewards will be much smaller than an expropriation when the currency is weak. Depreciation of currency will have the opposite effect.

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Mensi, Hammoudeh, Yoon, and Nguyen (2016) assert that the concept of country risk is ancient and is incorporated into the evaluation of risk and return in global operations. It was rarely distinguished from currency risk and was typically perceived as being closely tied to conducting business overseas (Madura & Fox, 2014). Rather, it was believed that currency risk and country risk were two sides of the same coin. Nonetheless, in the 1960s and 1970s, the idea of country risk underwent a significant evolution. In particular, this was a reaction to the global banking industry's attempts to quantify and characterise its exposure to losses from cross-border lending (Shmuel, 2015).

Different countries have different levels of country risk; some have very high hazards that deter foreign investment (Burnell et al., 2014). An investor may eventually be able to recover at least some of its initial investment when the assets of the defaulted firm are liquidated or restructured, for instance, if a domestic corporation is unable or unwilling to repay a loan. This is typically handled by the domestic bankruptcy courts (Frenkel et al., 2004). Most frequently, due to poor political circumstances and shortages of foreign currency, the government of the nation where the firm is headquartered may restrict or outright forbid debt payments (Burnell et al., 2014). The investor has little, if any, recourse to the local bankruptcy courts or an international civil claims court in the event that sovereign governments impose such limitations, reschedule, or outright forbid the payment of debt obligations (Saunders & Cornett, 2018). An investor's primary tool for guaranteeing or boosting payback amounts and probabilities is its control over the future flow of capital or loans to the relevant nation. However, in the face of a falling currency and a nation's government, such leverage can be extremely weak (Saunders & Cornett, 2018).

According to the literature and this study, market risk is the exposure resulting from unfavourable fluctuations in a financial instrument's market value. It is also evident that a wide range of factors, such as the reference asset's price, volatility, current interest rates, and time, influence market risk. As a result, if any of the above listed criteria changes, the risk and the investment asset's value will also alter. For instance, advantageous adjustments may result in earnings, whereas unfavourable ones may cause a loss.

Since it's such a broad term, there are situations when it gets confused with other threats. Some of the most prevalent kinds of market risks are listed by Banks and Dunn (2003) and include spread, basis, correlation, time decay, directional, volatility, and curve risks. Buraschi, Trojani, and Vedolin (2014) define directional risk as the possibility of losing money if the underlying assets move negatively. The forces of supply and demand, which determine asset prices through negotiations between buyers and sellers, are what create shifts in market direction. Volatility risk is the chance of losing money as a result of a volatile market. A market's volatility is a gauge of its degree of turbulence or calm.

According to Burschi et al. (2014), there is less volatility in a quiet market and more volatility in a tumultuous one. The risk of loss brought on by time decay is known as time decay risk. Derivatives, which derive part of their value from the period in effect, are the main source of this risk. Generally speaking, a contract's value increases with the amount of time left until it matures and vice versa (Banks & Dunn, 2003). The danger of losing money as a result of an unfavourable shift in the maturity structure, such as the interest rate, asset price, or degree of volatility (Leschhorn, 2014), is known as curve risk. Distribute the risk. This is the danger of losing money if two reference assets—such as risk-free assets and—undergo unfavourable adjustments. According to Banks & Dunn (2003), the gap between the two assets is constantly changing due to factors such as supply and demand, market and liquidity conditions, and credit events. The danger of loss resulting from unfavourable changes between two reference assets is known as basis risk, just like spread risk. The reference assets in this instance are somewhat comparable to one another but not exactly the same. A gain or loss may result from certain situations that cause the price of one to rise and the other to fall (Leschhorn, 2014). The risk of losing money as a result of a negative shift in the price linkages and correlations between markets and assets is known as correlation risk. It is evident from the financial price history that assets occasionally trade in tandem or against one another.

These correlation-based price correlations are frequently the foundation for investing or hedging (Banks & Dunn, 2003). One important part of the spread and basis risks mentioned above is correlation risk, which is genuinely present in assets and hedge connections. An investment manager may decide to purchase one asset and sell the other after analysing the past price movement of two assets and determining that there is a good chance that the prices will converge. The investment manager may experience a loss if the asset prices decouple because the historical correlation between the two diverges (Leschhorn, 2014).

Given that market risk encompasses several risks that are either categorised, integrated, or embedded within it, it follows that managing market risk in its diversity is vital. Furthermore, Waddell (2009) suggests that interest rate risk and market risk are strongly related. Prices fall as interest rates rise and vice versa. Therefore, changes in market risk factors may result in a decrease in the value of an investment. These factors are listed by Waddell (2009) as equity risk, which is the risk that stock prices will fluctuate; interest rate risk, which is the risk that interest rates will fluctuate; and currency risk, which is the risk that foreign exchange rates will fluctuate; commodity risk is the chance that the price of commodities (such metals and grains) will fluctuate; equity index risk is the chance that the price of stocks or other indexes will move negatively.

The history, terminology, and risk factors associated with inflation risk are the main topics of this section. Inflation, or an increase in the price of goods and services, lowers the value of a currency since investors can't buy as much with the same amount of money as they did before, claim García and Werner (2010). The rand's purchasing power has declined, for instance, if it could now only buy two candy bars instead of three as it could last year. A currency's purchasing power rises during times of falling prices, or deflation.

Inflation is defined in this study as a persistent rising price trend that detracts from an investment's value. Demand inflation and cost-push inflation are the two forms of inflation (Gustke, 2014). Demand inflation is the result of an excess of money in the economy relative to the amount of goods and services available. Prices rise as a result. Cost-push inflation occurs when input costs rise due to a variety of factors, including rising labour expenses and a declining exchange rate (Gitman et al., 2016). When evaluating inflation risk, investors in emerging markets should consider the following risk elements.

Interest rate risk in developing markets is the main topic of this section. Whittaker (2009) states that the interest rate is the amount owed on a loan. This rate is compounded in a variety of ways and is applied to the loan principle (Drechsler, Savov & Schnabl, 2017). Interest rates, for instance, can be compounded every day, every week, every month, or every year. Interest rate risk, according to Sharpe (2013), is the overall rise or fall in market interest rates as a function of the central bank's monetary policy. The banking industry modifies its own prime and other lending rates in accordance with the central bank's adjustment of its general lending rate (Whittaker, 2009). Because changes in interest rates have an impact on cash, bonds, and stocks, this has a knock-on effect that affects all economic activity. The interest rate risk risk factors are the subject of the following section.

Understanding interest rates' significance in investing can occasionally be challenging. Generally speaking, rising interest rates hurt investors because they hurt the bottom lines of the businesses they invest in (Bodie et al., 2018). Investors must comprehend interest rates as well as the methods by which interest rate risk elements are ascertained. If investors expect an increase in interest rates, this could assist them in modifying their investment portfolio and financial plan to account for the higher rates, and vice versa.

Bond investors are especially curious about the level of interest rates in the future because they want to know how they might affect price fluctuations (Sharpe, 2013). Because bond prices directly affect investors' financial gains and losses, it is crucial to be able to predict interest rate swings as accurately as feasible. Gitman et al. (2016) state that examining the most significant economic elements can help explain the forecasting of the variables and the overall level of interest rates.

Investors must comprehend the implications of risk for the company's operations (Olson & Dash Wu, 2015). This basically implies understanding if risks contribute significantly to revenue generation or whether they hinder, enhance, or complement corporate

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operations. For example, a typical bank's business is taking risks and making money by extending those risks. A bank's concept should support actions pertaining to the wise management of risk exposures since risk activities should align with the overall objectives.

There are many different types of risk that are thought to be included in the definition of financial risk. According to Chapman (2013), these risks include, but are not restricted to, capital risk, foreign investment risk, funding risk, interest rate risk, currency risk, systems risk, outsourcing risk, and liquidity risk. Risk to liquidity brought on by a brief incapacity to pay bills, including rent, employees' salaries, and business suppliers. Credit risk is the result of items delivered to the company on credit not being paid for. Interest rate risk has an impact on consumers' disposable income, which deteriorates commerce.

Currency risk is the possibility that changes in exchange rates will negatively impact the anticipated cash flow from foreign investments. Funding risk for borrowers in terms of having to pay fixed charges on corporate assets and not being able to meet capital repayment criteria (plus interest). Risks associated with foreign investments include limitations on the ability to repatriate money, high rates of taxation on earnings made abroad, temporary bank account balance freeze, and/or asset expropriation. Risk associated with derivatives stems from market speculation or hedging through forward purchases of commodities at a discount to the going rate. Systems risk is the possibility of suffering losses as a result of company procedures, processes, systems, or controls breaking down. outsourcing risk resulting from a counterparty's default owing to liquidation, late delivery of goods, or violation of contract terms. capital risk brought on by the possibility of losing one's initial investment (Chapman, 2013).

The aforementioned financial risks ought to be minimised when thinking about investing in emerging markets. Aggarwal (2005) defines financial risk management as the process of generating economic value for a company by using financial instruments to control risk exposure, especially credit and market risk. Foreign exchange, shape, volatility, sector, liquidity, and inflation risks are some other risk categories. Financial risk management necessitates determining its sources, quantifying it, and implementing risk-reduction strategies, much like general risk management.

Transfers of either equity or credit are typically necessary for the movement of financial capital between nations. The reputation or creditworthiness of the investor who assumes responsibility for the funds is a determining factor in credit. The primary risk to take into account while investing in an emerging market is credit risk, which is the subject of this section.

Netting agreements and collateral determine actual credit losses. Collateral taken may, in certain (but not all) cases, be liquidated upon default to offset losses, and a netting arrangement collapses a portfolio of agreements into a single amount payable or receivable.

Credit risk can take two forms, according to Banks and Dunn (2003): trading credit risk, which is the risk of loss resulting from a counterparty defaulting on a bilateral obligation, such as derivatives or repurchase agreements; and direct credit risk, which is the risk of a counterparty defaulting on the direct, unilateral extension of credit, such as a loan, security, receivable, or deposit; credit risk that is not guaranteed. which is the chance of suffering a loss if a counterparty defaults on a potential loan extension in the future; Correlated credit risk raises the amount of possible loss and is present in several financial transactions; Settlement risk is the loss resulting from a default following the delivery of securities to a counterparty or the payment of foreign exchange, but prior to receiving a comparable exchange from the same counterparty; sovereign risk, on the other hand, refers to the possibility of suffering a loss as a result of decisions made inside a nation's financial system. This can happen through devaluation and exchange controls. For instance, a rule that forbids players from exchanging and potentially withdrawing local cash, or a significant decline in the value of a local currency.

When evaluating credit risk from a single counterparty, an investor needs to take default likelihood, credit exposure, and recovery rate into account (Rose and Hudgins, 2013). The default probability measures the chance that the counterparty will not fulfil its obligations for the duration of the obligation or for a predetermined period of time, like a year. The

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predicted default frequency is the value that is determined over a period of one year. Credit exposure evaluates the amount of outstanding debt at the time of default as well as the credit exposure in such scenario. The recovery rate denotes the possibility of recovering a portion of the exposure through bankruptcy procedures or other forms of settlement in the case of a default (Rose & Hudgins, 2013).

Although credit scoring is included in the phrase "credit risk," it is more frequently used to describe procedures that need human judgement. Investors in emerging markets should evaluate and examine counterparty information. This could include the income statement and balance sheet of the counterparty, as well as recent developments in the business sector and the overall status of the economy. Another plausible explanation for why the needed rate of return isn't always achieved is credit risk. Bonds in default are ones that show a lack of interest payment or where the interest is past due. When the return of the capital sum, in whole or in part, is at risk, investors may perceive insolvency as a major problem. The issuer has fulfilled its commitments under the agreement when the required rate of return equals the actual rate of return (Rose & Hudgins, 2013).

Any time during market hours, a liquid asset can be sold quickly, conveniently, and with little loss of value (Banks & Dunn, 2003). A liquid market's primary feature is the constant presence of willing and able buyers and sellers. Investing in liquid assets has two benefits. First off, in the event that investors experience a cash flow issue, banks are more inclined to grant a credit line because they favour liquid assets. Second, investors have the option to sell the assets themselves, regardless of the bank's opinion (Rahman & Banna, 2015). Historically, it has been extremely difficult to compare highly illiquid and non-traded investments to typical investments, such as venture capital, leveraged buyouts, and private real estate (Gitman et al., 2016). When investors think about how to include these assets into a conventional asset portfolio, this becomes more troublesome.

Illiquid asset classes need to be made comparable to liquid asset classes in order to be allocated as assets (Banks & Dunn, 2003). More precise assessment of the real risks and diversification advantages offered by illiquid asset classes may be possible with the use of an estimating approach. The method should give a clearer picture of the fluctuations in illiquid returns, despite the fact that it is predicated on certain assumptions. When acquiring an asset, an investor anticipates that it will either mature or be sold to a different investor (Rahman & Banna, 2015).

The investor anticipates that they will be able to cash in on the security and use the money for additional investments or for their own consumption in either scenario. The liquidity risk increases with the difficulty of this conversion (Gitman et al., 2016). When evaluating an investment's liquidity risk, an investor should take into account two factors: first, how long will it take to turn the investment into cash?, according to Rose and Hudgins (2013). and how certain is the amount that will be paid?

Young (2018) defines legal risk as the possibility of breaking the law or failing to comply with established norms, guidelines, rules, and moral principles. This risk also occurs when regulations or laws pertaining to specific goods or activities of an organization's clients are ambiguous or unproven (Young, 2018). Legal risk is defined by Chapman (2013) as the inability to follow the law, to be aware of one's legal obligations, to keep one's word when entering into a contract, and to work with the offshore firm to agree on remedies for compensation in the event of default. Consequently, the investor must provide proof that the institution has complied with the law or that it can identify and resolve legal risks (Gitman et al., 2016).

When an organisation violates the law, it may be subject to fines, financial penalties, damage payments, and contract voiding (Young, 2018). Additionally, it can result in a damaged reputation, a decreased value of the franchise, less commercial prospects, constrained developments, and the inability to uphold obligations (Chapman, 2013). In summary, investors can benefit from well-managed legal risk in the form of favourable returns, a solid reputation, and a competitive advantage in developing markets. The constant revision of trading rules and regulations by emerging market countries makes legal risk

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management a continuous exercise. Thus, risk mitigation strategies must be in place in case legal risks materialise.

In recent times, investors in emerging markets have grown increasingly concerned about technological risk (Saunders & Cornett, 2018). Since the 1980s, significant expenditures in computers, internal and external communications, and an expanded technology infrastructure have been made by banks, insurance companies, and developing market investment firms in an effort to increase operational efficiency (Gitman et al., 2016). When back-office support systems fail or current technology malfunctions, technological risk results (Saunders & Cornett, 2018). Technology risk, according to Chapman (2013), refers to risk factors that are thought to be included in the definition of technology.

Technology risk includes not investing enough in technology and losing out on competitive advantage; not managing technology, especially IT; not managing outsourcing; not aligning IT with business goals; not providing enough protection against viruses, hacking, and loss of confidential information; and not having enough production flexibility to economically produce small production runs. Inadequate technology may force investors in emerging markets to remove their foreign holdings due to their incapacity to compete, resulting in losses and frustration (Gitman, et al. 2016). When considering offshore investments, investors must make sure they have the financial means to purchase the equipment required to transact with their counterparts abroad.Staying ahead of the opposition's advances or at least not being outwitted by them is a crucial part of technological risk management. The three ubiquitous technologies of today are controls, communication, and information. These innovations have the power to boost growth, cut costs, and increase productivity. Therefore, in terms of market share and market development, technological advancements present both an opportunity and a threat. Furthermore, integrating technology into a company might expose it to a number of crippling risks that could substantially reduce profitability and competitive advantage, or even cause the company to fail. Investments in emerging markets may face both opportunities and risks from technological advancements. Consequently, in order to maximise profits and minimise dangers, investors should thoroughly investigate the technology that their offshore counterparts employ. An investment plan may fail if technology risk, or any other risk covered above, is not managed.

## METHODS OF RESEARCH

This investigation used an end-of-study research design. There are two categories of decisive research, according to Gaudet and Robert (2018): causal and descriptive. The study research kind is the most decisive of them, with the primary goal being the description of something (typically qualities or functions). In descriptive research, longitudinal and cross-sectional designs are used. This study used a cross-sectional research design, which is characterised by data collection from a sample of the population elements only once. Since the researcher was attempting to obtain impartiality through the use of a structured questionnaire to collect data from the participants, quantitative research was thought to be the appropriate research strategy for this study (Gaudet & Robert, 2018).

It was decided that the survey approach was most suited for the current investigation. Surveys, according to Leedy and Ormrod (2018), entail gathering data on one or more groups of individuals, possibly regarding their traits, beliefs, attitudes, or prior experiences, then tallying their responses. Because it is one of the nations with an emerging economy that draws the bulk of investors to the African continent, South Africa was chosen as the study region. Accordingly, a questionnaire was determined to be the best means of data collection given the goals of this investigation. The optimal data collection technique was determined to be a web-based questionnaire based on the pros and cons of the different survey delivery methods.

The method that was deemed most pertinent to this investigation was a purposeful non-probability sampling strategy. This choice was made because the study's data set comes from a particular target population. This group is limited to a particular class of asset managers and/or investors who can provide the necessary information. Asset managers

were the respondents best positioned to supply the information required. As to the 2019 report by the Financial Sector Conduct Authority (FSCA), a total of forty-four Collective Investment Schemes (CIS) were authorised to transact in developing economies. The best people to give information on the dangers they identified for investors in emerging markets were the asset managers overseeing these programmes.

Consequently, these asset managers received an invitation letter inviting them to take part in the study. These asset managers are important players in the global investing scene and have been at the forefront of investments. As a result, the desired sample size will include all 44 asset managers in South Africa who hold FCSA-issued trading licences for emerging markets. In this study, validity and reliability were also regarded as crucial concerns. In collaboration with a statistician, asset managers, and senior scholars from the University of South Africa who are specialists in the fields of finance, investments, and risk management, a draft questionnaire was pre-tested for validity, reliability, objectivity, and generality. This investigation examined content validity.

The degree to which a measurement accurately represents the particular intended domain of content is the foundation for content validity (Howell et al., 2005). Since the suggested questionnaire measured investors' attitudes and beliefs towards a predetermined set of emerging market risks, content validity was the most acceptable validity type for this study. The experts have affirmed that the study's questionnaire complies with academic research guidelines and is valid in terms of content. Cronbach's alpha was used in a reliability test to determine the questionnaire's level of dependability.

Thirty-three out of the forty-four questionnaires that were sent to asset managers in South Africa were returned, indicating a 75% response rate. Every questionnaire that was returned was appropriate for examination. To analyse the data, descriptive statistics were employed. To analyse data imported from a LimeSurvey, utilise SPSS software.

## RESULTS AND DISCUSSION

To assess the questionnaire's internal consistency and reliability, a reliability test was conducted. As a result, the coefficients for every risk factor found in emerging markets were calculated. Table 1 presents the Cronbach's alpha coefficients.

Table 1 – Descriptive statistics and internal consistency reliabilities

| | |
|---|---|
| Average inter-item covariance | 0.034456 |
| Number of items in the scale | 46 |
| Scale reliability coefficient | 0.761 |

Table 1 shows that the scales have an alpha coefficient of 0.761, indicating strong reliability given that 0.6 is the acceptable score. This is supported by De Souza and Dick (2009), who caution that in statistical analysis, any coefficient alpha value of 0.6 is deemed appropriate.

The primary aim of this research was to identify the various risk categories that investors in emerging markets face. Risk categories found in the literature were added to the questionnaire in order to accomplish these goals, and respondents assessed them appropriately.

Objective 1: To determine the risk types for investors in emerging markets.

The results of risk factors for developing market investors are shown in Figure 1.

Several risk categories in emerging markets were found, as seen in Figure 1. These findings are covered in more detail below.

The purpose of the question was to find out if investing in an emerging economy included a significant risk of exchange rate risk. Figure 1 demonstrates that while 27% (n = 9) and 9% (n = 3) agreed to a degree and to a partial degree, respectively, that exchange rate risk was important to take into account in an emerging market, the majority of respondents (64%, n = 21) agreed to a full degree.

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As a result, everyone who responded agreed that investment in emerging economies should take exchange rate risk into account. This suggests that when making investments in emerging markets, the majority of asset managers take exchange rate risk very seriously. According to some writers (Warner & Pierce, 2016), if the risk associated with a financial transaction denominated in a currency other than the home currency is not well handled, the value of the investment could be considerably reduced.

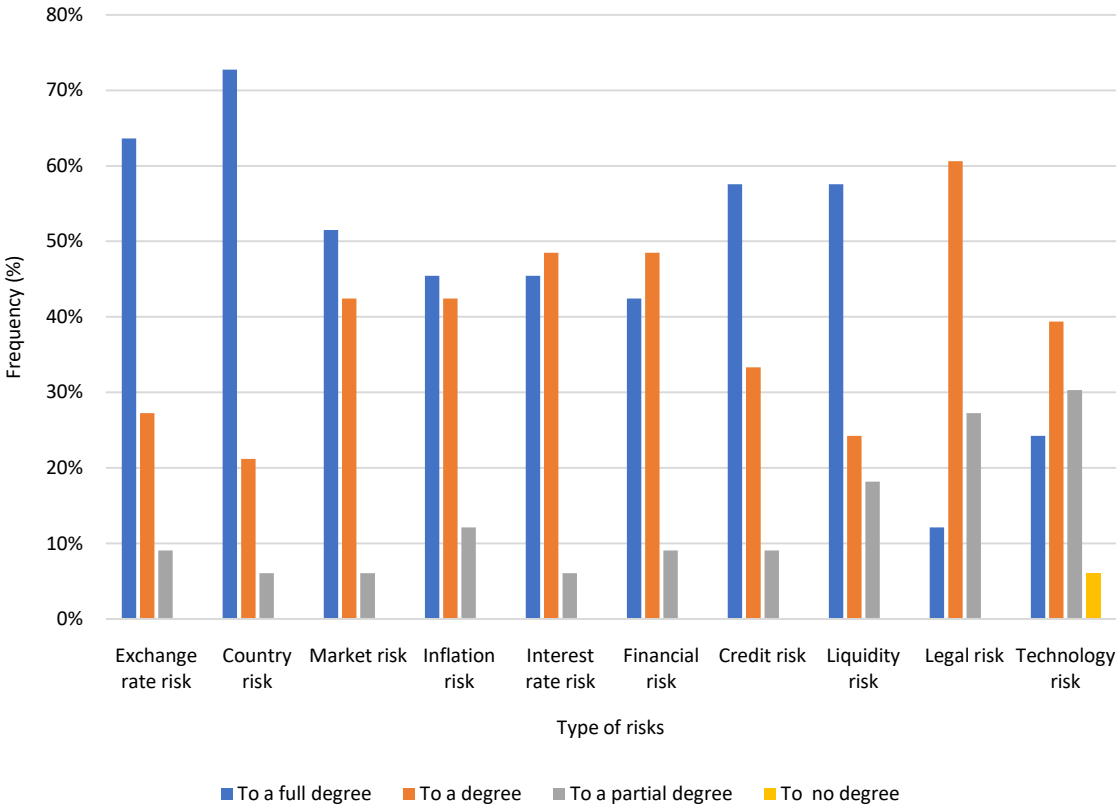


Figure 1 – Risk types in emerging markets

When it came to the importance of taking nation risk into account in an emerging market, the majority of respondents (73%) thought that it was very important, 21% agreed that it was somewhat important, and 6% agreed that it was only partially important.

Every responder expressed agreement that country risk should be taken into account, with many believing it to be crucial in developing nations. If country risk is not reduced, it will raise the level of uncertainty around investments made in a given nation, and more especially, the likelihood that such uncertainties would result in investor losses. Various factors such as political, economic, exchange rate, or technical effects might lead to uncertainty.

The purpose of this question was to ascertain how crucial it is to take market risk into account in developing markets. According to the graphic in Figure 1, more than half of the respondents (52%, n = 17) agreed that market risk is vital to take into account in developing markets to a full degree, 42% agreed to a degree, and 6% agreed to a partial degree.

Market risk is the chance that an investor will lose money as a result of events that have an impact on the financial markets they are involved in. Every respondent concurred that in emerging markets, this kind of risk needs to be taken into account.

The scores provided by respondents in Figure 1 are in line with the prevailing opinion that any investment should be managed for inflation risk because it raises the possibility that future changes in inflation-related buying power may result in an investment's cash flows

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losing value. Of the participants, 46% fully agreed, 42% mostly agreed, and 12% agreed to a lesser extent that inflation risk is crucial to take into account in emerging countries.

Increased costs for products and services are a sign of inflation. Purchasing power risk, another name for inflation risk, is the possibility that future returns on investments will not be as high as anticipated. It is crucial to consider the inflation rate since, if left unchecked, it might make an investment completely useless.

Of those surveyed, 46% fully agreed, 48% partially agreed, and 6% agreed to a lesser extent that interest rate risk should be taken into account while investing in emerging markets.

Nearly equal numbers of respondents believed that interest rate risk should be taken into account for both degrees and full degrees.

The cautionary statement by Bodie et al. (2018) that interest rate fluctuations affect the value of investors' stocks, cash, and shares is consistent with the significance of taking interest rate risk into account. Consequently, an investment's risk may rise in tandem with an increase in interest rates. Stock prices drop when risk rises, and investors run the danger of losing money.

Of those surveyed, 42% fully agreed, 49% mostly agreed, and 9% agreed to some extent that financial risk should be taken into account while investing in emerging economies. Since every respondent acknowledged the significance of financial risk, it follows that while making investments in emerging countries, one should manage one's exposure to unfavourable events that could reduce profitability or, in the worst case scenario, cause a business to collapse. This is consistent with the opinions expressed by Olson and Dash Wu (2015), who contend that investors must comprehend the implications of risk for their company's operations. This entails being fully aware of whether risks contribute significantly to income or serve to supplement, enhance, or undermine corporate operations.

The purpose of this question was to assess how crucial it is to take credit risk into account when making investments in emerging markets. Of those surveyed, 58% agreed fully that credit risk should be taken into account when making investments in emerging markets, 33% agreed to some extent, and 9% agreed to some extent.

The claim made by Chapman (2013) that credit risk is the oldest and, in terms of the magnitude of possible losses, the most significant risk is supported by the responses. A small number of major clients' defaults can result in significant losses and ultimately lead to insolvency. Investors in emerging markets must therefore reduce credit risk. Purchasing credit risk insurance, which is accessible to both domestic and foreign investors in many nations, can help reduce credit risk. Investors in emerging markets won't be exposed to liquidity or legal risk if credit risk is properly managed.

Two benefits of liquid investments have been mentioned in the literature: first, even if the bank disagrees, investors can always sell the assets themselves. Secondly, since banks like liquid assets, they are more likely to offer a credit line to investors in the event of a cash flow crisis. This topic aimed to evaluate how crucial it is to take liquidity into account when making investments in emerging economies. Of the participants, 58% (n = 19) fully agreed, 24% (n = 8) partially agreed, and 18% (n = 6) partially agreed that liquidity risk was crucial to take into account while investing in emerging markets.

One of the most important risks that an investor should take into account when making an investment in emerging markets is liquidity risk. In addition to ensuring that risks are minimised, managing liquidity will make sure that opportunities are taken advantage of.

Twelve percent of respondents agreed that legal risk should be taken into account in a developing market to the fullest extent possible, sixty-one percent agreed to a degree, and twenty-seven percent agreed to a partial degree. It may be inferred from the respondents' assessments of legal risk in Figure 5.4 above that when legal risk is not avoided in a foreign nation, investors' goals may be jeopardised. Young (2018) asserts that neglecting to control legal risk can lead to the termination of trading licences in severe circumstances, penalties, fines, and the cancellation of investment contracts, all of which will be harmful to the goals of investors in the global market.

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Regarding the degree to which technological risk should be taken into account in emerging countries, 24% (n = 8) of the respondents agreed (full), 40% (n = 13) agreed (degree), 30% (n = 10) agreed (partial), and 6% (n = 2) disagreed. When back-office support systems fail or current technology malfunctions, technological risk results. Investors in developing markets must be cautious of technological mishaps like service interruptions or information security breaches that could jeopardise their investments.

Chapman (2013) asserts that inadequate technology can force investors in emerging markets to pull out of the market due to an inability to compete, resulting in losses and frustrations. When considering an investment, investors must make sure they have the financial means to purchase the technology required to transact with overseas partners. The majority of respondents (94%) agreed that technology risk is a crucial risk to take into account when preparing to invest in developing economies, indicating that technological considerations should be taken into account before making an investment in these regions. When considering to invest fully or partially in a developing market, the majority of respondents stated that these risks should be taken into account.

## CONCLUSION

Identifying risk types for emerging market investors was the aim of this study. To analyse the data, descriptive statistics were employed. Exchange rate risk, nation risk, market risk, inflation risk, interest risk, financial risk, credit risk, liquidity risk, legal risk, and technology risk were the risk categories for investors in emerging markets, according to the data. Furthermore, it was shown that the top five risk categories were technological risk, market risk, nation risk, exchange rate risk, and inflation risk. When making investments in emerging economies, investors want to take these risk categories into account. For investors looking for portfolio diversification and growth potential, investing in emerging markets can be an enticing proposition. Investors must, however, thoroughly research the many risks connected to making investments in these dynamic, developing economies. Making wise investment decisions and safeguarding wealth in emerging markets require an understanding of and ability to manage these risks. Thus, it can be said that these risk categories can act as a reference for investors during the risk analysis process and guarantee that the analysis is done to guarantee sufficient risk mitigation and control methods. This study added to the body of knowledge and gave developing market investors fresh perspectives on different kinds of risk. In order to ensure a structured strategy while investing in developing markets, it is advised that investors who choose to do so take into account the risk types outlined in this study in addition to the top five risk factors.

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