



 KCS Country Risk & Threat Advisory

Grey Area Dynamics
A challenge of diagnosis and delivery

Latin America

September 2021

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Grey Area Dynamics

The corporate need

Target-specific due diligence is slowly becoming an accepted part of corporate strategy. This is diligence conducted against a handful of entities, be they individuals or companies, on a strict set of terms aimed at clarifying any potential issues of concern about the targets before a particular deal, partnership, or project. It is (for the most part) specific, focused, and refined. But there is also the need for businesses entering new markets, whether for the first or fiftieth time, to understand the whole host of variables at play, and the likelihood and impact of each.

Crucially, these variable risks may not always be immediately apparent to diagnose, or specific to a given issue: they are the inherent, general problems posed by a market; the grey area dynamics that can significantly affect every aspect of a business' finances and reputation. So-called, because they represent change and activity (not always for the better) and have deciding says in markets that are never always entirely black and white. It is in the grey area that a client's chances of success or failure may be decided.

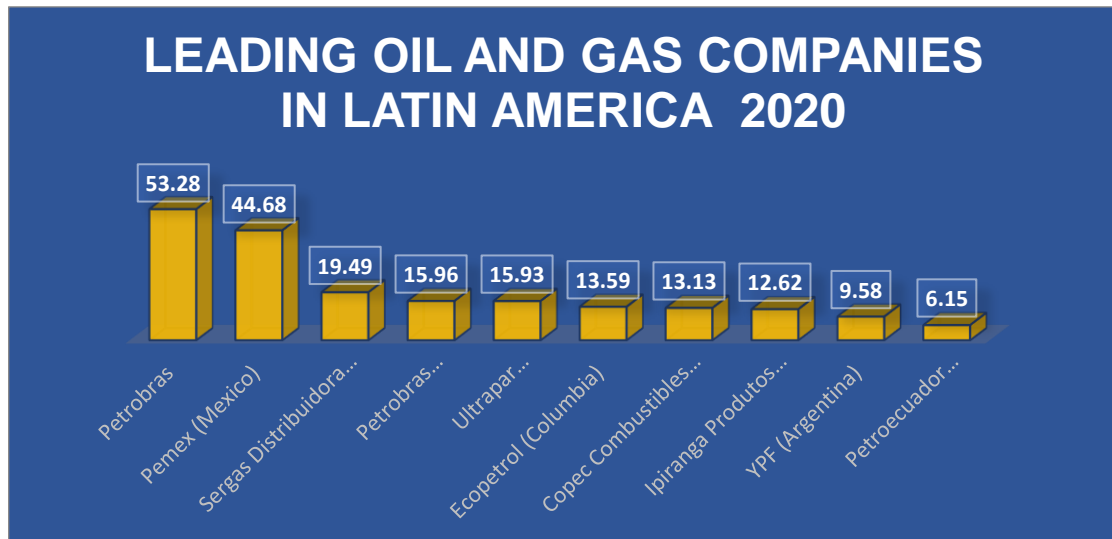
Moreover, there is never a one-size-fits-all solution. Understanding to a very granular degree where the risk lies, and in what direction, can be of inestimable benefit in a client deciding where to commit, how much to invest, and the extent of their risk appetite. But as with any danger, to be able to face it you must first know where it lies; and the more you know about the form it takes, so much the better. The challenge is therefore, creating a mechanism that transmits the nature, severity, and impact of these GADs to the Client in a manner which considers the multitude of risks at a granular level, but which is still packaged in an easily understandable framework which is actionable and appropriate.

Latin America: Focusing on Brazil, Venezuela, and the Fuel Industry

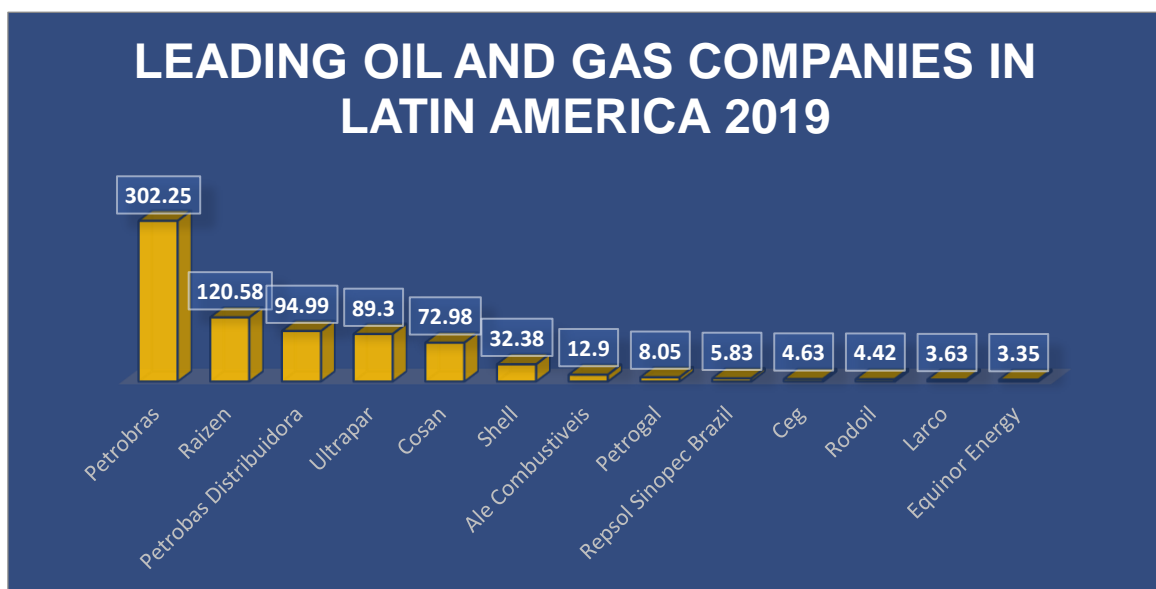


1.0 Latin America's fuel industry

In 2020, Brazilian state-owned company Petrobras still leads in the oil and gas industry in Latin America, based on annual sales, with more than \$53bn worth of revenue. Mexican national oil corporation Petróleos Mexicanos (Pemex) ranked second, with almost \$45bn of sales revenue. The fuel industry is recovering post pandemic and from the mismanagement by government.



In 2019, Petrobras generated 302bn in revenues. Raízen generated a revenue of 120.6bn. Petrobras was still the leading fuel distributor in Latin America in most sectors it operated in. Petrobras do have rivals in the sectors of gasoline and diesel fuel - Raízen and Ipiranga each held one fifth of the market in 2019. During the past decade, smaller players have benefited from a small but continual market increase.



Brazil's fuel industry has continued to improve since, 2020 and according to Brazil's National Agency of Petroleum, Natural Gas and Biofuels – show that in July 2021, the country produced on average \$3.9 million barrels of oil which had increased by 4 percent from June 2021.

Venezuela's crude oil reserves as of 2021 stand at \$304bn bbl. Average crude oil is priced at \$49.13bbl. Crude oil exports are \$847k bbl. Petr6leos de Venezuela, S.A. (PDVSA) is the state-owned leading oil and gas production in Venezuela. Venezuela's oil and gas industry have suffered a double-edged sword having been mismanaged internally by government, suffered corruption, and losses of import and export due to the pandemic. Externally, Venezuela's fuel industry has suffered enormous loss of import/export profit due to the US sanctions which have also made foreign investment a difficult affair.

In February of 2020, Trinidad and Tobago had cancelled an agreement with Venezuela for the joint development of a natural gas field spanning their maritime border. The US efforts to undermine the Maduro regime of oil revenues has exacerbated the humanitarian crisis in Brazil and Venezuela. The sanctions have inadvertently increased the role of Russian energy in the US Gulf Coast, and the embargo on Venezuelan oil and gas has shifted the flow of fuel generating opportunities for growth of Russian petroleum exporters such as Russia's oil giant, Rosneft. The US persists on threatening Rosneft for its trade with Latin America's PDVSA. US sanctions have exacerbated Venezuela's humanitarian crisis, and as such has created market opportunities for countries like Russia, Iran, and China to bolster their presence in Latin America.

In July of 2021, sources revealed a Chinese logistics firm had emerged as a central player in the supply of sanctioned oil from Iran and Venezuela, despite it being blacklisted by Washington two years ago for handling Iranian crude oil. China Concord Petroleum Co., (CCPC) had been sanctioned by the US in September 2019 for trading with Iran. Of recent months however, CCPC have been moving oil out of Venezuela and Iran. Over the past year, China has invested in fourteen tankers to ship crude oil out of Venezuela and Iran.

In April 2020, the Brazil-Russian relationship had further cemented their trading partnership with contractual cooperation agreements in areas of health, education, energy, food, and security. This is good news for Venezuela, who had shut down their last drilling rig back in 2020.

As well as China seizing the opportunity of a mutually beneficial relationship with Venezuela, sources revealed the US owned subsidiary of Venezuela's state-held firm PDVSA, namely Citgo Petroleum; expects to act as a bridge role in the country's transition once US sanctions are lifted. Venezuela has some of the world's largest oil reserves and at one time the country had potential as an economic superpower with regards to its fuel economy.

Brazil, however, and its state-owned Petrobras is not out of the shadows of the "Car Wash". Brazil's largest ever corruption investigation. The Car Wash probe exposed a web of corruption across Latin America, rocking the political and economic business world in several countries. The investigation resulted in nearly 180 convictions. Several heads of state, particularly in Brazil and Peru were implicated. The investigation had been ongoing until February 2021, when Bolsonaro shutdown the taskforce behind the investigation, claiming corruption had been eliminated. However, a more likely reason for the prevention of investigation is that Bolsonaro himself wishes to evade a prison term.

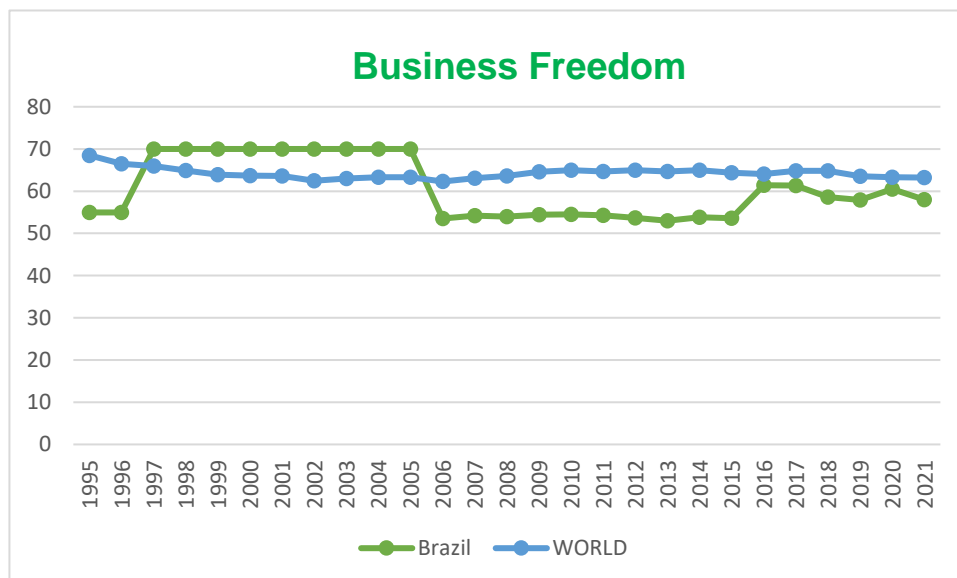
2.0 Brazil

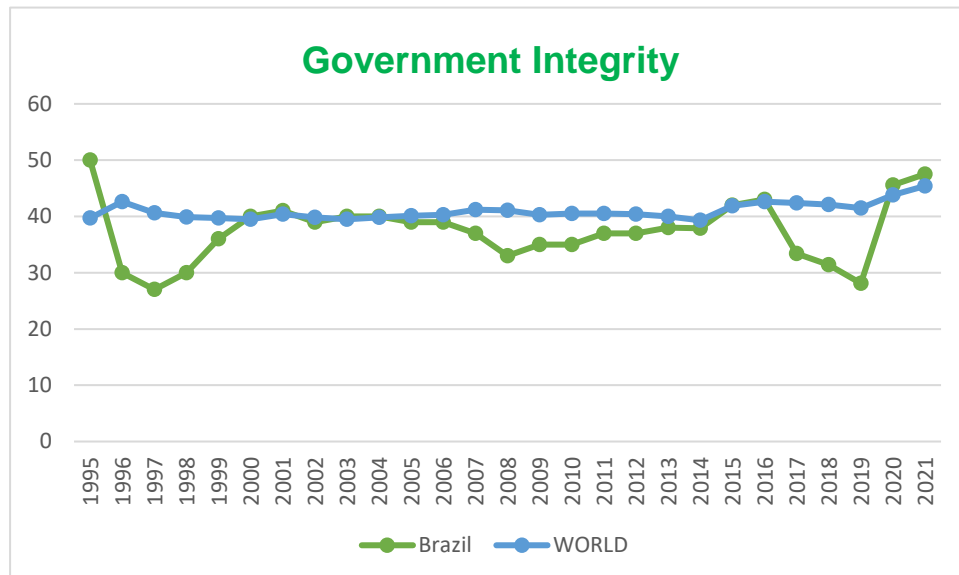
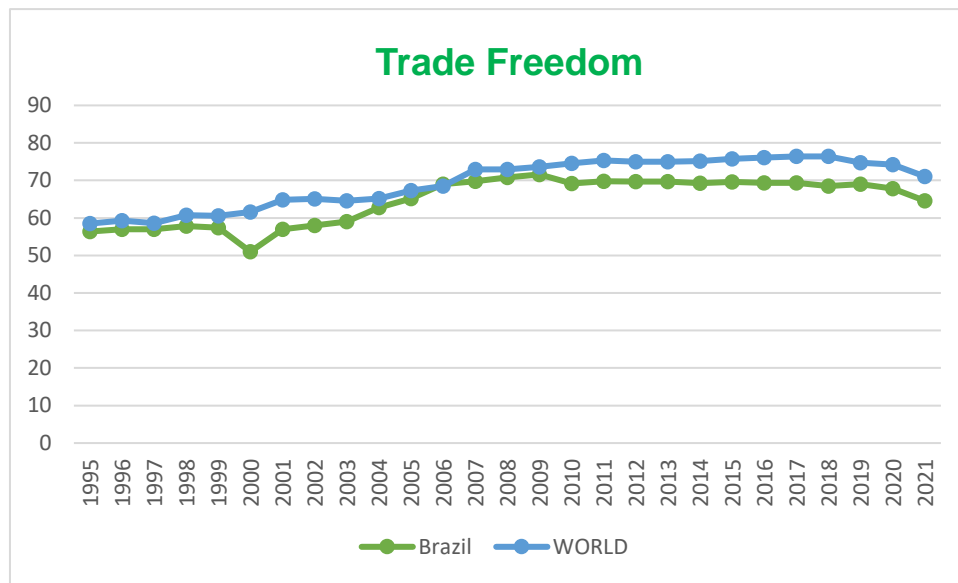
Country	Brazil
Population:	211.0m
GDP:	3.5tn USD (2021)

Brazil has a possible risk score of 4

As the world's ninth largest economy and fifth largest country, Brazil is more commonly known for its diverse population, iconic festivals, lush beaches, exquisite waterfalls, oil reserves, and of course, its jewel in the crown - the Amazon rainforest. Today, Brazil suffers two pandemics, the Covid-19 which has been disastrously handled by the Brazilian Government, and two consecutive Presidents who have brought the country to its knees.

The Index of Economic Freedom measures economic freedom of 184 countries based on business freedom, investment freedom, economic freedom, and property rights. As of 2021, Brazil scores 53.4 (a decrease of 0.3 from the previous year) with a world ranking of 143. Although trade freedom has declined in Brazil, it is slowly improving, with the oil industry seeing a mini boom between June and July 2021. However, its overall score is below the regional average. Brazil has one of the most complex and burdensome tax systems consuming an estimated 33 percent of GDP. The graph data below provides insight into the decline of business freedom, trade freedom and to the decline of government integrity (much like many countries) – between 1995 and 2021 the country data is visualized alongside the data for the rest of the world.





2.1 Political Landscape

In October of 2018, Far-Right presidential candidate Jair Bolsonaro had won the presidential election, becoming the peoples present. Some citizens of Brazil fell foul to the empty promises of fighting crime and corruption by Bolsonaro, and assisted his electoral campaign. The people were vulnerable, craved democracy, needed change and Bolsonaro had all the answers. It is common knowledge that Bolsonaro, with the help of his administration; secured presidency by fraudulent means. However, the 2nd of October 2022 presidential election is just around the corner.

Brazil's Bolsonaro, fearful of perceived impending loss in the coming election, engaged the news media with a petulant argument that the coming election may be fixed. So therefore, statistics would suffer fraudulent outcomes due to elections being counted digitally. Bolsonaro warns he may not accept the outcome (unless of course he emerged as the winner).

While considering travel to Brazil, the Foreign and Commonwealth Office warn (as of September 2021) that Brazil remains in the red at level 4 (do not travel), due to Covid-19 and violent crime. Areas most dangerous to human life are within 150km of Brazil's borders with Venezuela, Columbia, Bolivia, Guyana, Peru, Suriname, French Guiana, and Paraguay. Other areas to avoid include Brazil's favelas, Vilas and comunidades (informal housing developments).

In addition to the above locations, Brazil's administrative regions commonly known as satellite cities should also be avoided, such as Ceilandia, Santa Maria, Sao Sebastiao and Paranoa (especially after sundown). The most common crimes inflicted in Brazil are violent crimes such as homicide, kidnapping, carjacking, armed robbery, and Organised Crime Group Activity (OCG's).

As of 2020, Brazil scored 38/100 on the Corruption Perception Index (the lower the number, the higher the corruption). 54 percent of the public surveyed in Brazil thought corruption had increased between 2019 – 2020. 11 percent of public service users admitted to paying a bribe between 2019 – 2020. The highest levels of corruption are pervasive within the Brazilian customs administration, posing significant risk at border crossings. Companies moving into the Brazilian market, have reported inefficiency within customs administration in areas of unpredictable time management of business needs, requests for bribes, clumsy import procedures, and corruption.

The port of Santos is known to be the main departure point for class A drug smuggling bound for Asian, European and African markets. Although this is common knowledge, only 7 percent of South America's cocaine seizures take place at the port due to bribery and corrupt officials. Similarly, corruption is endemic within Brazil's law enforcement. External influence, corruption and violence is prevalent throughout the police force. In 2016, Newton Ishii, a key investigator and prominent police officer, was arrested on corruption charges. Threat level of corruption and bribery within Brazilian law enforcement remains at high.

Public services are laden with excessive bureaucracy as well as bribery, and according to GAN Integrity, the threat level here is at medium.

Within the land administration sector, corruption is cited to be medium-high. The rich, powerful and corrupt have significant influence on Brazil's law enforcement, as well as the Judiciary. Corruption takes shape in the form of falsified 'legal land documents' and OCG's taking land by force using the threat of armaments. Brazil's Judicial system scores high on the list of corruption. Companies operating in Brazil may encounter corruption at local levels of the Judiciary where political, economic and local interests have a heavy influence.

Public procurement is another sector in the red. Favouritism, cronyism and nepotism are included in the corruption of Brazil's public procurement sector. Public money is misappropriated, and foreign investment may suffer significantly without in-country assets on a local level to negotiate business and examine the market.

According to the Global Peace Index (GPI), Brazil's overall score was 2.4/5 (the lower the score, the more peaceful the country). Of the 23 indicators measured, those scoring the highest were criminality in society (3.9/5), homicides (5/5), violent crime (5/5) and political terror (4.5/5). According to the Global Terrorism Index (GTI), Brazil scored 2.4/10. Terrorism incidents have remained very few in Brazil (two over the last five years), however, extremist groups known to operate in Brazil are neo-Nazi groups such as Carecas do Subúrbio, Carecas do ABC, and White Power. Isis and Hezbollah are also known to operate within the region, particularly Hezbollah whose criminal activities within Brazil are used to finance their operations.

2.2 Economy and climate landscape

Brazil's current GDP is at 1.4tn (USD). It had receded by up to 7 percent during the recession, however, despite this, Brazil is making a steady recovery with expected GDP growth of 3.7 percent in 2021. Brazil's most lucrative market sectors remain petroleum processing, cement, iron and steel production, chemical production, automotive, machinery production and aerospace.

From an ecological point of view, Brazil scores low on the ETR, with an overall score of 1. Flooding was the main ecological concern with a score of 4.2/5 followed by droughts with a score of 2.8/5 (the higher the number, the higher the threat). Brazil remains the largest Latin American source of FDI in the United States. Brazil's main export countries as of 2019 were the US, China, Argentina, the Netherlands, and Japan.

Top products exported were soybeans of which Brazil was the world's biggest exporter (\$26.1b), Crude petroleum (\$24.3b), iron ore (\$23b), corn (\$7.3b) and sulphate chemical wood pulp (\$7.3b).

Top imports for Brazil were refined petroleum (\$12.4b), vehicle parts (\$6.1b), crude petroleum (\$4.3b), integrated circuits (\$3.8b), and pesticides (\$3.7b). Imports were mainly from China with a value of (\$36.3b), United States (\$32.6b), Germany (\$11.3b), Argentina (\$10.3b), and South Korea (\$4.83b). In July 2021, Brazil exported \$25.5b and imported \$18.1b, resulting in a positive trade balance of \$7.39b. Between July 2020 - July 2021 the exports of Brazil had increased by \$6.07b.

2.3 Social and legal climate

The Covid-19 pandemic hit hard on Brazil which currently has the second highest death rate (behind America). Bolsonaro faces the fall out of an angry population of Brazil and media backlash in relation to 584k deaths thus far. Brazilian citizens and foreign governments hold Bolsonaro responsible, accusing him of inflicting genocide for his mishandling of the pandemic.

Bolsonaro refused to acknowledge the pandemic initially, and so therefore refused to implement lockdown, social distancing measures or any other crisis contingency to safeguard Brazilian citizens; until it was too late and then he had implemented the barebones necessary advised to him by his health and safety ministers. This is despite the fact that he himself had contracted the virus in July 2020. During May 2021, thousands of people took to the streets of Brazil to protest the handling of the pandemic by Bolsonaro. Citizens demanded his impeachment.

According to the World Bank's 2021 Ease of Doing Business report, Brazil scored 124 out of 190. Brazil can be a challenging business market due to a clumsy, complicated and at times corrupt regulatory environment. Businesses had reported that commodities such as electricity have become complicated and expensive to source and take longer to obtain a connection. Construction permits have also increased in price, despite Bolsonaro's promises of reforming Brazil's labour market. The government do however provide heavy subsidies for the production of agriculture and subsidise hundreds of state-owned enterprises. Lessons from the pandemic seem to have reverberated around the world in terms of trading partnerships.

In October 2020, Brazil strengthened their trade relationship with the US by signing a protocol to bilateral agreement on trade and economic cooperation. In 2019, Brazil passed the Regulatory Agencies Law and the Economic Free Trade Law. In June of 2020, Brazil published Decree 10,411, which implements the regulatory impact analysis established by the Economic Freedom and Regulatory Agencies Law.

As of the 7th of September 2021, Bolsonaro implemented a new law restricting social media sites from policing content. *“The Provisional Measure issued by the Brazilian government forbids the removal of content that may result in any kind of censorship of political, ideological, scientific, artistic or religious order”*. Bolsonaro acts impulsively, has little regard or understanding of the consequences of his actions and his myopia on the matter of a ‘free for all’ uncensored internet/social media space may have catastrophic consequences to society at large.

Bolsonaro’s actions will encourage the propagation of political, ideological and religious extremist groups. It will exacerbate the proliferation of cybercrime. It will inadvertently invite the depraved and unwanted behaviours of bad actors and leave the young and the vulnerable exposed. OCG’s will conduct their business and communications unchallenged, and groups will gather in numbers to encourage hate, dehumanisation and engage in terroristic mischief and recruitment. There will be deep fake news and propaganda, and this will encourage terrorism by way of an uncensored media outlet which terrorist’s crave as their world podium.

The power of propaganda should not be taken lightly. History is an attestment to this. There are several levels and types of propaganda (extremist groups use them well). The most important of which is the propaganda of integration, which is to promote a collective among citizens of acceptance and support for that system of which it propagates and infiltrates into societies. Expressed succinctly *“Extreme propaganda must win over the adversary and at least use him by integrating him into its own frame of reference”* (Ellul, 1973).

Moreover, Bolsonaro does not envision his actions may just work against him. A group or individual may exploit his new law by way of character assassination, election intervention, and opposition campaigns. This, all brought about because he had once had his social media account suspended.

Brazil's Amazon rainforest. Between 2019 – 20, Pará accounted for 40 percent of illegal deforestation in the Brazilian rainforest. In response to this illegal deforestation being brought to the fore – Bolsonaro's administration relaxed inspection requirements for timber exports and facilitated individuals securing lands by force in indigenous territories that awaited official recognition from the Government. Bolsonaro's new legislation has allowed construction of major projects such as roads, railways, and dams, and has granted amnesty to land grabbers.

The new law facilitates deforestation of indigenous lands for the implantation of dams, mining, industrial farming, and oil exploration. This has destroyed several protected areas of the rainforest, and he had also allowed new deforestation on private land. The amazon rainforest is the most important ecological system in the world, not only for its part in the carbon cycle regulation but also for its diverse and endangered species of flora and fauna. Yet again, Bolsonaro's short sightedness threatens the eco system.

2.4 Representative Grey Area Dynamics

Economically, Brazil is slowly coming back from the brink. It has a lucrative market, especially given its current vulnerability with the need for FDI and trade relationships to strengthen its economy. Brazil's dark side, however, must be navigated prudently and with due diligence. The Grey Area Dynamics (GADS) identified in Brazil's market include that of political and economic corruption (deeply endemic), a high crime rate, and unfair trade and competition.

GAD business risks:

Corruption – bribery patronage, nepotism, cronyism and favouritism, political and economic corruption, vested interests and disguised beneficial ownership.

Bureaucracy – navigating vested interests, deliberate and/or enforced delays, political influence and government interference/action.

Cultural issues – cultural perspectives of business, navigating corporate culture of bribes, extortion, and civil unrest.

Legal safeguards – government policies, customs and border issues, regulations and tax.

Organised crime – kidnap, extortion and syndicate criminal threat (firearms).

Unfair trade – hidden barriers to entry (documents, waiting time and apathetic insufficient/corrupt staffing) and unfair pricing.

Unfair competition – vested interests, favouritism, and local government interference.

Asset security – pilferage, threat to life, premises and assets, and OCG's extortion and activity.

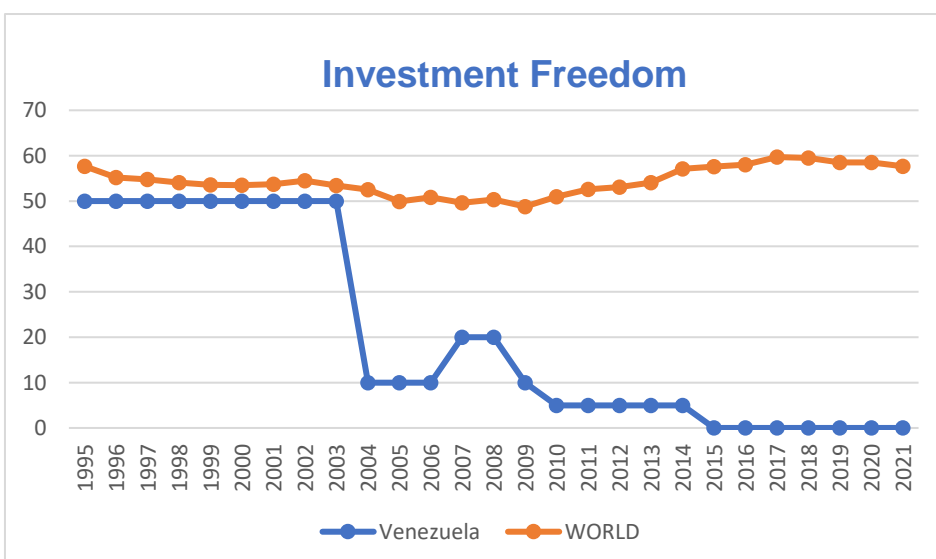
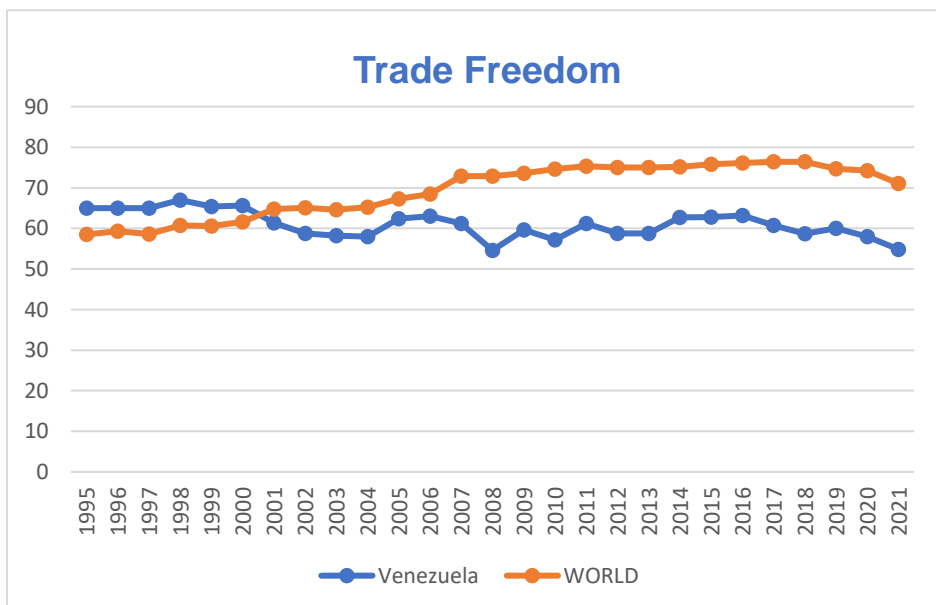
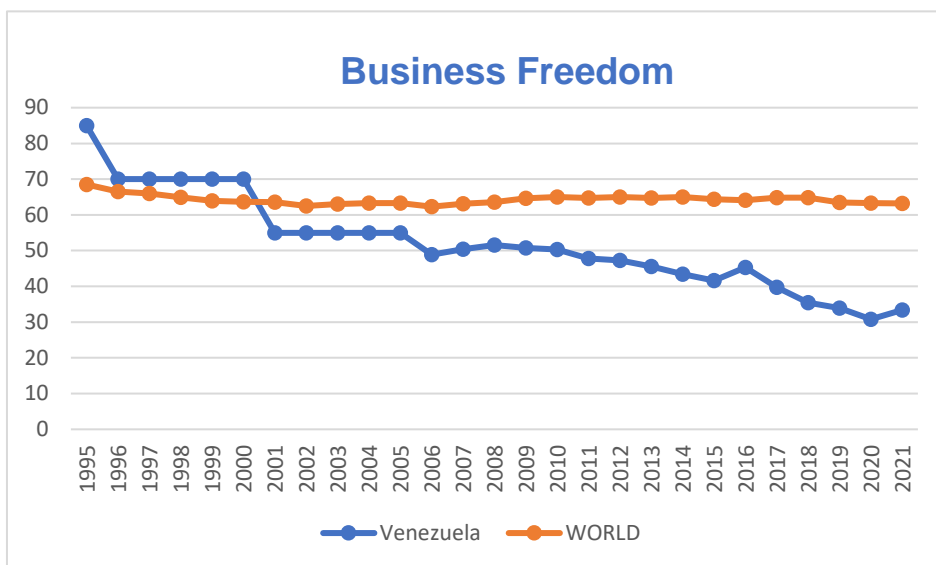
3.0 Venezuela

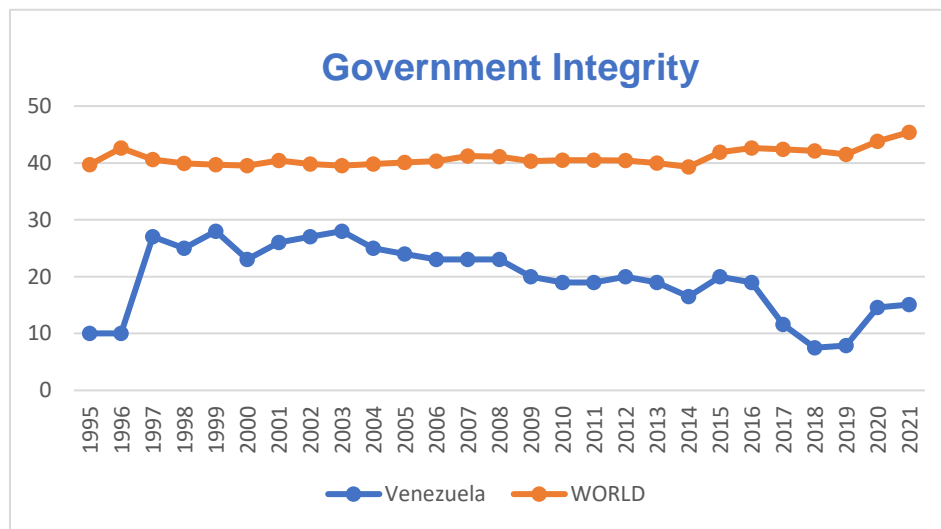
Country	Venezuela
Population:	28.7m
GDP:	240.0bn USD (2021)
	Venezuela has a possible risk score of 5

Venezuela is home to a diverse population, beautiful waterways, and a once thriving tourism industry. Venezuela has the world's largest oil reserves and the second largest natural gas reserves. It is home to the beautiful and highest Angel Waterfall and the Canaima National Park. However, Venezuela is suffering two epidemics, Covid-19, and the humanitarian crisis.

Venezuelan citizens are swept up in a socio-political crisis, and poverty and injustice at the hands of their despotic state. Officials (foreign and domestic), citizens and opposition suffer persecution of political appointments, torture and arrests. President Nicolás Maduro's dictatorial bullish regime is systemic and widespread. The Venezuelan Government uses all means available at their disposal, including the military and intelligence services to persecute and control their citizens. Maduro, Chávez's successor continues the path of destruction of democratic institutions and has replaced them with an authoritarian dictatorship which breeds difficult ground for business and investment.

Venezuela's Economic Freedom Index as of 2021 scores a low of 24.7 and the 177th freest economy. It had also declined by 0.5 percent due to a decline in government investment. Venezuela ranks last among 32 countries and is well below the regional averages. By the end of 2021, economy is forecast to contract by 25.0 percent. Below is a visualization of the decline in business freedom, trade freedom, government integrity and investment freedom.





3.1 Political landscape

Police are ranked the highest institution for corruption in Venezuela. Companies entering into the Venezuelan market report they have no confidence in the police to protect them from crime or to enforce the law. Police officers are underpaid, underfunded, and poorly trained. Impunity is the corruption of choice among officers and, acceptance into the Venezuelan police force is a matter of who you know and not what you know. Favouritism and nepotism form the curriculum vitae for police officers.

The Venezuelan Judicial system ranks high regarding corruption. When former President Hugo Chávez was in power, he favoured loyalists within the Judicial halls and so it became politicized. In 2013, 94 percent of cases ruled in favour of the government due to fear of reprisals. Chávez took over the Supreme Court in 2004 and had politicised it. Businesses report that although Venezuela is less time consuming when it comes to arranging contracts, it is more expensive on enforcing them. Due diligence must be exercised when considering entering the Venezuelan market to avoid being targeted for extortion and treated with bias from either the Venezuelan government, competitors, or other individuals.

Customs Administration and Public Procurement have similarities to the Brazilian methods of corruption, with officials expecting gifts or money in return for favourable treatment and expedition of documentation. Similarly, corruption within the fuel industry manifests by way of government officials expecting payments.

Crime in Venezuela is exacerbated by the state sanctioned abuse of Human Rights. Crime types inflicted by the state and OCG's are kidnapping, and torture (including waterboarding, electric shock, suffocation, and severe beatings). Organised Crime Groups (OCG's) and "syndicates" operate with little or no policing, and some are even supported by the state. OCG's are mainly operating in border states including (but not limited to) the National Liberation Army, Patriotic Forces of National Liberation, and fractured groups which have evolved from the Revolutionary Armed Forces of Columbia.

Venezuela scores 3.7/10 on the Global Terrorism Index (GTI) and has an overall score of 2.93 on the Global Peace Index (GPI). Areas of concern remain criminality in society (4.6/5), homicides (5/5), violent demonstrations and crime which both scored 5/5, political instability which scored 4.2/5 and political terror which scored 5/5. Displaced people scored 4.5/5 and access to weapons and internal organised conflict scored 4/5.

The UK government warns against travel to Venezuela due to high levels of crime. The US Government have issued a level 4 warning (do not travel) due to civil unrest, high levels of crime, poor health infrastructure, kidnapping and arbitrary arrest and detention. Venezuela has one of the highest incidences of violent deaths in the region and the world. Areas of concern is the state of Miranda which ranks as the most violent state in Venezuela, with Bolivar in second place. The violence in Guarico state has increased to such a degree that it is now among the five most violent states in the country.

Other areas of concern, particularly to individuals perceived as a political threat is the Western part of Libertador, such as the areas El Retiro, Blandin, La Vega, La Rinconada, Las Mayas, and Tazon. In the Eastern region, areas include parts of Sucre, Barrio Piritu, Barrio La Rubia, Barrio Altavista, Petare, Caucaguita, La Dolorita, Paulo Sexto and El Llanito.

3.2 Economic and climate landscape

Venezuela's GDP is estimated at \$240.0bn as of 2021. According to Trading Economics, it is expected to drop to £230bn by the end of 2022. Venezuela suffered a 30 percent decline during 2020 and a further drop is forecast of a 10 percent negative drop in 2021, followed by a five percent drop in 2022. Together with the pandemic, fluctuating oil prices and sanctions by the US, Venezuela's economic growth remains sluggish.

Venezuela's import of goods (2020) reached \$6.55bn and export of goods were \$5.02bn, with a deficit trade balance of \$-1.3bn. Ratio of government expenditure to GDP was 37.7 percent and national debt in relation to GDP was 26 percent. Between 2019 - 2020, the value of Venezuela's exported goods fell by -71.9%.

The top ten exports (2020) were mineral fuels including oil: \$3.3b, (68.9% of total exports) iron, steel: \$427m, (9%) organic chemicals: \$241.8m (5.1%) and fish: \$235.9m, (5%). Other exports included ores, slag, and ash: \$91m (1.9%) beverages, spirits, vinegar: \$67.3m, (1.4%) copper: \$51.4m (1.1%) fertilizers: \$45.9m (1%), aluminium: \$49.3m (1%) and Meat/seafood preparations: \$44.8m (0.9%)

Venezuela's most recent imports (2020) were mineral fuels including oil: US\$940.5m (15% of total imports) cereals: \$672.7m (10.8%) machinery, (including computers): \$642.8m (10.3%) electrical machinery: \$536.9m (8.6%) vehicles: \$268.2m (4.3%) and cereal/milk preparations: \$239.4m (3.8%). Additional imports were animal/vegetable fats, oils, and waxes: \$232.7m (3.7%), sugar/sugar confectionery: \$193.7m (3.1%), plastics: \$195.8m (3.1%), and pharmaceuticals: \$154.7m (2.5%).

Due to a decline in government spending, Venezuela's economic freedom score has suffered a reduction by 0.5 bringing the score to an overall 24.7. Venezuela is ranked last among 32 countries in the America's region and its overall score for the region is well below the regional averages. Under the Chávez and Maduro regimes, economic freedom has been stifled.

3.3 Social and legal climate

On the 6th of December 2020, Maduro's ruling party PSUV, claimed 90 percent of the seats through fraudulent legislative elections. The UK does not recognise the fraudulently elected parliament but rather, continues to recognise the National Assembly elected in 2015 and supports Juan Guaidó as the interim constitutional President.

According to the Rule of Law Index, Venezuela ranked last among 128 countries in the world Justice Project 2020. Venezuela's despotic state continues to destroy democracy. It would take transnational intervention to bring Venezuela back from the brink of a near collapse of economy, which is currently suffering hyperinflation, price controls, and a politicized Judiciary.

The fall out of which has embedded a culture of serious violent crime, corruption, favouritism, nepotism, cronyism, patronage, and a passive state of decision making based on fear of reprisals.

In March of 2020, the US government charged Maduro and 14 other officials with narco-terrorism, drug trafficking, and corruption – among other crimes. The Human Rights abuses by government and OCG's, starvation, serious lack of healthcare, the migrant crisis and soaring crime in Venezuela have created a volatile and explosive environment. Civil unrest is predicted to escalate and doing business in many regions of Venezuela would require a complex, sensitive exploration and analysis of due diligence to mitigate risk. From an ecological threat perspective, Venezuela scores low with an overall score of 1/8. The highest concern was the capacity for country resilience, followed by flooding and cyclones.

3.4 Representative Grey Area Dynamics

Never has there been a better time to seek investment into the Venezuelan market. The country is on its economic knees, and according to the World Bank, will get worse before it gets better. Investment would be of mutual benefit for prospective FDI, the Venezuelan economy and in turn, have a positive effect on Venezuelan citizens. Market opportunity in the oil and gas industry is wide open and could be an excellent place to invest with the country's rich reserves and capacity for production. However, Venezuela's dark side is exacerbated by its despotic state, and so businesses wishing to enter this market must explore the terrain armed with due diligence. Grey Area Dynamics (GADS) identified:

GAD business risks

Corruption – bribery patronage, nepotism, cronyism and favouritism, political and economic corruption, vested interests and disguised beneficial ownership.

Bureaucracy – navigating vested interests, deliberate and/or enforced delays, political influence and government interference/action.

Cultural issues – business and cultural perspectives of what is acceptable or not, navigating corporate culture of bribes, extortion, motivation and civil unrest.

Security – business/asset damage, threat to human assets.

Legal safeguards – government policies, customs and border issues, regulations and tax.

Organised crime – kidnap, extortion and syndicate criminal threat (firearms) and theft/robbery.

Unfair trade – hidden barriers to entry (documents, waiting time and apathetic insufficient/corrupt staffing) and unfair pricing.

Unfair competition – vested interests, favouritism, corporate espionage, and local government interference.

Extremism – terroristic activity, OCG's, left- and right-wing activity and civil unrest.

4.0 Appendix

4.1 What are GADs

Grey Area Dynamics (GADs) are all the risks, weakness and threats that have direct and measurable impact on businesses. They are a collective description of behaviours and factors that can at best disrupt a firm and at worst close it down. Ignorance of, or objection to, their impact has, on some occasions, even led to fatalities. The GADs methodology makes the invisible risks, visible, and serve to differentiate between different variables in each climate. For instance, the bureaucratic climate of a South American nation may be wholly different to that of an Asian nation; but this generalisation does not go far enough.

To even better understand the market, you need to consider the very specific types of bureaucratic indignities: inherent red tape, a culture of bribery, corruption from on high, the role of distributors – and so on. The deeper down you drill, the more likely you are to get to the core of an issue – which in today's business climate has never been more necessary.

Grey Area Dynamics are aptly named not only for the shades-of-grey approach, in seeing the variable plus and minus points, but also the dynamic nature of how these factors can and will impact a business. They identify and analyse not only the known risks, but the unknown ones too, setting out how the exact variant nature of a given situation (say the differences between an environment where threats are active and illegal, compared to passive and bureaucratic) matters in a manner which is practical and actionable.

The GADs system: a revived concept for a new era

At the turn of the century, KCS' Grey Area Dynamics system won the ACE Insurance Group's Innovative Risk Tool of the Year at the annual awards of StrategicRisk. It has now been extensively redrawn and refined in terms of input, mechanism and output, so as to better meet the considerable challenge of encapsulating wildly differing risks and threats while remaining concise and of value.

The system is underpinned by the dividing of risks into four categories as follows:

- Legal – concepts/activities that are permitted but which can be implicitly troubling to firms, or knowingly exploited by bad actors.
- Illegal – practices which clearly breach the law, but which occur regardless because of a permissive or actively mendacious business & governance culture.

- Active – issues that are the result of deliberate actions taken by bad actors to disrupt and damage businesses for their own benefit.
- Passive – factors that are in the background or which are ever-present, that are threats without being consciously brought to the surface.

Each Grey Area Dynamic can thus be placed in two of the four categories as follows:

	Legal	Illegal
Active	<ul style="list-style-type: none"> • Industrial & labour relations • Absence or effectiveness of legal safeguards • Government policy and nationalism • Overt and disguised/beneficial ownership • Bureaucracy and local government • Public or media hostility 	<ul style="list-style-type: none"> • Counterfeit & fraud • Pilferage • Unfair market competition • Product piracy • Ethics and corporate espionage • Organised crime • Threats to physical assets • Kidnap & extortion • Religious extremism • Terrorism • Civil unrest • Organised crime/Cyber Crime
Passive	<ul style="list-style-type: none"> • Language & dialects • Local customs & traditions • Local staff • Tribalism and integration • Cultural & local sentiment • Regulations, taxes and duties • Currency & capital exposure – payment methods and banking practice • Environmental hazards • Pressure groups • Media relations • Pandemics 	<ul style="list-style-type: none"> • Bribery & corruption • Vested interests and cronyism • Patronage bribery & corruption • Product diversion • Parallel trading • Hidden barriers to entry

Within these assorted umbrellas, are issues ranging from broad corruption and state-sponsored espionage to very localised industrial problems and social unrest. All are wildly different, and not all will be relevant every single time. The key is in discerning exactly where, and why, they are important to your market or sector.

The methodology

Having established the division of the grey area dynamics, these are then plugged in to a bespoke mathematical model that provides further insight into assessing the risks that businesses face when in-country. The evaluation of the GADs, when summarised by the model, produce an overall 'risk score' and threat level status. This is done as follows.

Stage 1. Produce periodic IMPACT data rate scores for each of the 35 GADs.

All 35 KCS GAD risks are graded for IMPACT from 1-100% (1% being the least severe and 100% being the most severe). For example, the Language & Dialects GAD is awarded 2% and the Pandemic GAD 100%. The impact scores are based on a combination of over forty years of expert analyst opinion on the severity of a GAD and its direct/indirect impact on personnel and business operating in a given country. These impacts are reviewed and updated quarterly.

Stage 2. Produce periodic FREQUENCY data rate scores for each of the 35 GADs.

The FREQUENCY of each and every GAD having occurred historically, is scored from 1-100% (1% being not frequent at all and 100% being all the time). The frequency scores are based on a combination of expert opinion and its historical commonality. These frequencies are similarly reviewed and updated quarterly.

Stage 3. Produce present day LIKELIHOOD threat level scores for each of the 35 GADs.

The LIKELIHOOD of a GAD being encountered, based on present day research and analysis is rated from 1 to 6, where 1 is almost unthinkable and 6 is a certainty. The likelihood scores are based on a combination of historical analysis, expert opinion, and a thorough understanding of the present-day situation. The likelihood scores are produced at any given time a country risk score is required.

Stage 4. Convert scores into GAD equation.

Begin with the following formula:

$$\text{RISK} = \text{IMPACT} \times \text{LIKELIHOOD}$$

And introduce a variable that accounts for the FREQUENCY (or commonality) of a GAD historically occurring, and multiply by the LIKELIHOOD of the same:

$$\text{RISK} = \text{IMPACT} + \text{FREQUENCY} \times \text{LIKELIHOOD}$$

Stage 5. Calculate the mean average.

The Standard Deviation statistical formula is employed to calculate the mean average GAD risk score. This is calculated by summarising the data and dividing the sum by the total number variables – in this case, 35.

Stage 6. Report the risk level score.

The country score is produced as a percentage, and a country is graded and reported as defined by KCS' six levels of severity:

<u>Severity</u>	<u>Grade</u>	<u>Consequence</u>
1 – Very low	0.00 – 0.16	The GADs pose virtually no risk to business.
2 – Low	0.17 – 0.33	A slight chance of risk posed by the GADs.
3 – Possible	0.34 – 0.49	A fair chance of risk posed by the GADs.
4 – Very Possible	0.50 – 0.66	A strong chance of risk posed by the GADs.
5 – High	0.67 – 0.83	A very high chance of risk posed by the GADs.
6 – Very High	0.84 – 1.00	A certain and serious risk posed by the GADs.

Value

The system thus works at both a micro- and a macro-level. The percentage figure and ranking offer a 'headline' as to the general level of risk posed by a market, with the deeper intimations of exactly where the threats will come from being obtainable from a breakdown of the statistics. Not only does this allow decision-makers to get an immediate idea of the threat level, but also a deeper breakdown of which specific Grey Area Dynamics are in play, their severity and frequency, and how the divisions of legal/illegal, passive/active are weighted. This kind of information offers a substantial degree of clarity over how the GADs can independently affect a client, and how they may intersect with each other to create the threat profile in a given business environment – thereby allowing a client to better refine or prepare their business plan to take account of where the threats are understood to lie.

This statistical modelling is of course backed up, in any report, by extensive comment and expert analysis on the given market and its dynamics, providing further and deeper comment on the key issues and delivering a comprehensive and effective assessment of the nature, and extent, of the risks that a business will face.

So, if you want to take a step, use Grey Area Dynamics to ensure that it isn't into the unknown.

KCS Group Europe won the European Service Provider of the Year, 1999-2000 at the European Risk Management Awards Magazine International Risk Management for their work on GAD's. In 2004, the company won an award for Product of the Year from Strategic Risk.