

The Role of Multinational Enterprises' Investments in Emerging Country's Economic Development, Case of Georgia

V. Charaia

Abstract—From the strategic point of view, not all Foreign Direct Investments (FDIs) are always positively benefiting the host economy, i.e. not all Multinational Enterprises (MNEs) are promoting local/host economies. FDI could have different impact on different sectors of the economy, based not only on annual investment amount, but MNE motivations and peculiarities of the host economy in particular. FDI analysis based only on its amount can lead to incorrect decisions, it is much more important to understand the essence of investment. Consequently, our research is oriented on MNE's motivations, answering which sectors are most popular among international investors and why, what motivated them to invest into one or another business. Georgian economy for the last period of time is attracting more and more efficiency seeking investments, which could be translated as - concentrating production in a limited number of locations to supply various markets, while benefiting local economy with: new technologies, employment, exports diversification, increased income for the local economy and so on. Foreign investors and MNEs in particular are no longer and not so much interested in the resource seeking investments, which was the case for Georgia in the last decade of XX century. Despite the fact of huge progress for the Georgian economy, still there is a room for foreign investors to make a local market oriented investments. The local market is still rich in imported products, which should be replaced by local ones. And the last but not the least important issue is that approximately 30% of all FDIs in Georgia according to this research are "efficiency seeking" investments, which is an enormous progress and a hope for future Georgian success.

Keywords—Investments, MNE, FDI motivations, Georgian economy.

I. INTRODUCTION

AT the best possible scenario, MNEs can significantly contribute to sustainable and inclusive economic development of the host country [1]. Especially in developing countries it is their role to build a healthy business environment through responsible business practices (which is not a reality for every case).

For the past decades international business environment has significantly modernized and faced real structural changes. Countries in all continents started to open their markets, businesses embraced new opportunities, FDIs are welcomed and supported.

MNEs through job creation, human capital development, efficient capital distribution, knowledge, technology, financial

Prof. Vakhtang Charaia, PhD in Economics, is a Director of the Center for Analysis and Forecast at Ivane Javakhishvili Tbilisi State University (e-mail: vakhocharaia@gmail.com).

and skills transfers – have significantly contributed to global development and economic growth of both home and host countries, though increasing global economy and bringing closer geographically the most distant places closer. However, not each and every FDI case is perfect for the host economy's sustainable economic development, which could be analyzed through the MNE motivations in a three alternative (sometimes motivations could be merged) ways: market seeking, efficiency seeking and resource seeking investments.

II. WHY TO INVEST IN GEORGIA - ACHIEVEMENTS

Georgia possesses a decade of fast economic growth, balanced tax and labor codes, business friendly atmosphere, low criminal and high security indicators [2]. Georgia signed the association agreement with the EU in 2014 [3] and gets visa free regime starting from the first half of 2017 year [4].

According to 2017 report, The World Bank rated Georgia as the 16th easiest place in the world (among 190 countries) for doing business [5] and also named it as a Top Global Improver [6]. Heritage Foundation ranked Georgia 13th (among 180 countries) for its economic freedom in 2017 year's country ranking [7]. Standard and Poor and Fitch Ratings has affirmed Georgia's Long-Term Foreign and Local Currency Issuer Default Ratings at 'BB-' with Stable Outlooks, for 2017 [8]. According to the Global Competitiveness Index, Georgia is one of the best performers for the last decade. In addition to simplified tax code with only 5 taxes with one of the lowest rates in the world, the Estonian Model of Income Tax was introduced since January 2017, thus corporate income tax is paid only in case of profit sharing. If a company reinvests its income no income tax is paid [9].

Progress of Georgian state could be proved by the following results:

- GDP per capita in Georgia in 1995 was less than 600 USD, which increased more than 6.5 times for less than a quarter of the century in 2016 [10].
- Bank Assets increased approximately 110 times for last two decades from 276 million in 1995 up to 30 billion USD in 2017 [11].
- FDIs increased from less than 4 million USD in 1996 to 1.6 billion USD in 2015 [12].
- An average wage increased 66 times from 13.5 GEL in 1995 to 900 GEL in 2016. The same period saw drastic growth of the volume of export (13 times) from 155 million USD to 2.1 billion USD [13].
- In 2003 Georgia was one of the most corrupted countries

in the world. By 2016 it had moved up to 44th place out of 176 countries [14].

- Georgia clashed against criminal and shaped the best police force in the ever seen in the region. Georgia is the leader country according to the Safety Index 2016 [15].
- According to the Frazer Institute's Economic Freedom of the World: 2016 Annual Report, Georgia got 5th place for the Economic Freedom Ratings [16].

These and many other achievements have contributed to Georgia's progress.

III. THE ROLE OF MNEs IN GEORGIA

MNE motivations and the driving force could be different in different countries, as well as they could be different even in the separate sectors of the same economy. Relatively higher added value production (such as electronics and engineering) is characterized by geographic concentration, proximity to the customers and high quality control demand. These fields are attracting Efficiency oriented FDI's. While, areas as: textile, food processing and other relatively low-tech service oriented fields.

Georgia is one of the post-communist countries where FDI's played tremendous role in the transformation of the local economy in last two decades, however there are still a lot of questions to the quality of these investments and answers are not on the horizon.

Complexity and strongly competitive nature of international business are pushing MNEs with unique and specific challenges, which often span multiple countries and many cultural, legal, and regulatory environments. Not in all, but at least in some cases especially at developing countries, MNEs demonstrate a respect for highest standards of business conduct. At circumstances where regulatory, legal and institutional frameworks are underdeveloped or fragile MNEs are more careless to sustainable economic growth of the environment where they work. Such companies are usually bringing a negative attitude toward all the rest of MNE's reputation, which is not fair toward all the players.

What are the MNE motivations and their influence on the Georgian economy; how much it is assisting development and modernization of different economic sectors in Georgia and how deep MNE's are integrated into the different fields of Georgian Economy? These are the questions which are most interesting for scientific point of view, as well as practical approach.

Based on Eclectic Paradigm, Dunning classifies the motivations of FDI into resource based, market seeking, efficiency seeking, and strategic asset seeking [17]. Each of them has different impacts on host economy. The goal for the host economy is to get as much benefits as possible, out from the MNE created assets. However, it is very much depended on governmental policy and motivations of foreign investors. The less there is a connection between host economy and MNE, the more it is unclear what host economies really need out of those FDI's, i.e. FDI's has the possibility to improve the

competitiveness of the host economy, but its impacts are different:

- Generally it seems to be much easier to attract FDI than to derive macroeconomic benefits from FDI;
- Countries with highly qualified human resources will benefit more from transmitting MNE's business related modern technologies;
- Openness of the economy is vital, since MNEs are followed by Complex Integrity Strategy, i.e. elimination of restrictions for intermediary products at all levels of the production cycle;
- Transfer of technologies is widely depended on the institutional development of the host economy.

All above-mentioned factors are closely related to the FDI motivations and have different growth effects on the host economy. For instance, Market-Seeking FDI is providing the host economy with technological assistance and staff trainings. Also modern technologies and import of intermediate products provide additional benefits for the local economy. Finally, rising competitiveness is pushing local firms to innovation. Otherwise the "crowded out" effect is expected, since foreign firms are highly competitive. Market-Seeking FDI's oriented on concurring local markets are less involved in export-oriented activities. In a long run it could result a crisis for balance of payments, since such FDI's cannot provide inflow of financial assets from the export-oriented activities.

Country with unfavorable characteristics are hardly attracting Market oriented FDI's in the service sector, when Location attractiveness is determined by the GDP per capita parameter. However, if we concenter the pectoral distribution in Georgian case, it is obvious that service is one of the dominant sectors in terms of FDI attractiveness: financial and energy sectors, trade and tourism sectors, transport and communications; thanks to the privatization process happened in Georgia for last decades in the respective sectors. However, this Market oriented investments in Georgian service sector are less efficient in terms of economic growth and exports; they are characterized with limited capabilities.

Recourse-seeking FDI's are attracting mainly large sums of capital inflows, are promoting technological upgrade and knowhow transfers, also providing economic with the stable currency inflows. Such investments are most often concentrated in the enclave formations, with weak ties to local commodity and labor markets. Also, one of the negative side effects could be the corruption promotion on macro level by the local elite.

Despite the fact that Georgian GDP per capita parameter does not seem to be the world's top performing one (approximately 4 thousand USD in 2016), still it is attracting a big portion of efficiency seeking investments, however the leader is the Local Market Seeking investments which consists of: Energy sector, construction, hotels and restaurants, health and social work, real estate, financial sector and other (see Table I) [17].

TABLE I
FDIs BY ECONOMIC SECTORS, BY YEARS [18]

	2007	2008	2009	2010	2011	2012	2013	2014	2015
Mining	86	18	15	53	40	5	44	43	88
Agriculture, fishing	16	8	22	9	15	16	12	12	15
Manufacturing	312	188	125	175	120	168	100	205	67
Transports and communications	417	423	98	215	127	73	140	434	585
Energy sector	363	295	-2	22	204	179	245	190	124
Construction	172	57	105	5	48	42	50	317	111
Hotels and restaurants	242	182	38	17	23	18	-13	125	139
Health and social work	0.5	0.5	0.3	1	17	18	0.7	-10	140
Real Estate	31	278	147	119	225	53	42	139	90
Financial sector	158	11	50	107	168	163	166	115	179
Other sectors	219	104	60	90	131	178	156	188	28
Total	2016	1564	658	813	1118	913	942	1758	1566

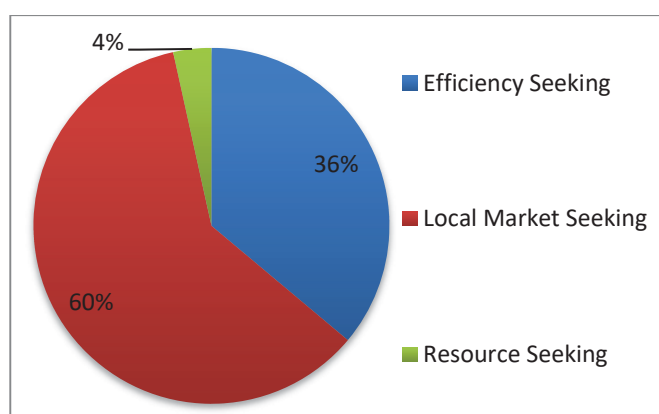


Fig. 1 Distribution of investments by motivations

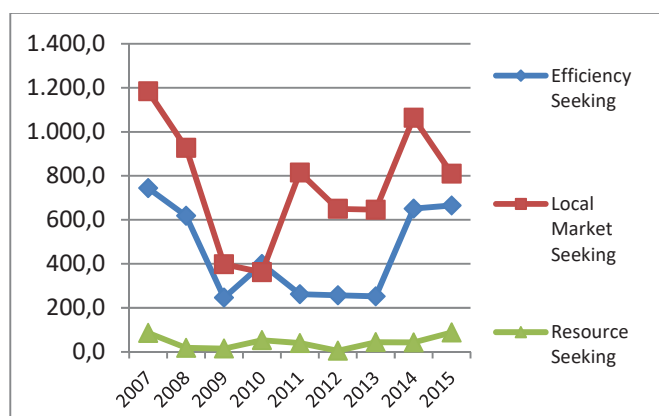


Fig. 2 Distribution of investments by motivations

According to the research done by the author on macro level, it is obvious that investments done during 2007-2015 years were mostly market oriented investments – 60%; second place was taken by efficiency seeking investments – 36%; while resource seeking investments took only third place with 4%, taking even less in a previous years (see Figs. 1 and 2). In other words, Georgian economy is still weak and needs further development to attract more FDIs in such efficiency seeking sectors as: Agriculture, manufacturing and communications. Such investments will fasten the economic growth and lead to higher life standards. However taking into account the

peculiarities of Georgian territorial problems, not all trade [18], transport and communication related projects can benefit Georgia, neither financially, nor politically, including the railway project through its breakaway region [19]. Financial losses based on the Georgian Territorial problems are huge [20] and are hindering possible future development of the whole country [21].

According to the analysis, FDIs in Georgia for the last three years are becoming more efficiency oriented, which could be explained by the country's progress [22] and its deeper inclusion to the regional and global economic projects [23], transit corridors and export oriented manufacturing industry development. However still one of the biggest problems for investment attraction is high interest rates at Georgian commercial banks, which pushes back long term sustainable business oriented investors [24].

IV. CONCLUSION

Research findings are essential to understand MNE motivations on the macro level, however not enough to deepen into the micro level incentives and to analyze the impacts of those investments on the local economy.

Upward trend of efficiency seeking investments in Georgia is a combination of important economic reforms and interest of foreign investors in Georgian economy and its progress, which leads to the prosperity on the both ends.

REFERENCES

- [1] OECD, Responsible Business Conduct in Georgia, p. 10. <http://www.oecd.org/countries/georgia/RBC-in-Georgia-2014.pdf> (last seen on 26.02.2017).
- [2] Deloitte, Guide to Taxation and Investment in Georgia 2016. <https://www2.deloitte.com/content/dam/Deloitte/ge/Documents/tax/Guide%20to%20Taxation%20and%20Investment%20in%20Georgia%202016.pdf> (last seen on 26.02.2017).
- [3] EU/Georgia Association Agreement. https://eeas.europa.eu/headquarters/headquarters-homepage_en/9740/EU/Georgia%20Association%20Agreement (last seen on 26.02.2017).
- [4] Visa-free Europe Coalition <http://visa-free-europe.eu/2017/02/georgia-visa-waiver-approved-by-parliament/> (last seen on 26.02.2017).
- [5] The World Bank, Doing Business 2017. <http://www.doingbusiness.org/data/exploreeconomies/georgia> (last seen on 26.02.2017).

- [6] The World Bank. Georgia among Top Global Improvers, Says Latest Doing Business Report. <http://www.worldbank.org/en/news/press-release/2016/10/25/georgia-among-top-global-improvers-says-latest-doing-business-report> (last seen on 26.02.2017).
- [7] Heritage Foundation Ranking, 2017 year. <http://www.heritage.org/index/ranking> (last seen on 26.02.2017).
- [8] Trading Economics, Georgia. <http://www.tradingeconomics.com/georgia/rating> (last seen on 26.02.2017).
- [9] Regulatory Impact Assessment on Estonian CIT Model Implementation in Georgia, 2016. http://pdf.usaid.gov/pdf_docs/PA00KXXW.pdf (last seen on 26.02.2017).
- [10] World Bank Group. GDP per capita (current US\$). <http://data.worldbank.org/indicator/NY.GDP.PCAP.PP.CD> (last seen on 26.02.2017).
- [11] National Bank of Georgia. <https://www.nbg.gov.ge/index.php?m=304> (last seen on 26.02.2017).
- [12] National Statistics Office of Georgia. FDI. http://geostat.ge/index.php?action=page&p_id=2231&lang=eng (last seen on 26.02.2017).
- [13] National Statistics Office of Georgia. Wages. http://geostat.ge/index.php?action=page&p_id=149&lang=eng (last seen on 26.02.2017).
- [14] Transparency International. <https://www.transparency.org/country/#GEO> (last seen on 26.02.2017).
- [15] Crime Index for Country 2016. <http://cbw.ge/georgia/georgia-ranked-among-top-6-safe-countries/> (last seen on 26.02.2017).
- [16] Economic Freedom of the World 2016 Annual Report. Frazer Institute. <http://www.freetheworld.com/2016/economic-freedom-of-the-world-2016.pdf> (last seen on 26.02.2017).
- [17] National Statistics Office of Georgia, Foreign Direct Investment by Economic Sector. http://geostat.ge/cms/site_images/files/english/bop/FDI_Eng-sectors.xls (last seen on 26.02.2017).
- [18] V. Charaia, Trans Inguri Trade Partnership. *4th International Conference on Global Business Environment. International Foundation for Research and Development (IFRD)*. Bangkok, 2014. Pp. 209-211. https://www.academia.edu/10505580/The_Positives_of_Cross-Cultural_Interactions_in_Multinational_Companies_and_Multicultural_Groups (last seen on 26.02.2017).
- [19] V. Papava, V. Charaia, Regional Railways in the Central Caucasus and Georgia's Economic Interests. *The Caucasus & Globalization*. Sweden. Volume 8, Issue 1-2. pp. 58-67. <http://www.papava.info/publications/regional-railways-en.pdf> (last seen on 26.02.2017).
- [20] V. Charaia, The Financial Side of the Conflict: The Case of the Georgian-South Ossetian Conflict. *Cost of Conflict: Core Dimensions of the Georgian-South Ossetian Context. George Mason University, 2016*, pp. 46-51. http://scar.gmu.edu/sites/default/files/global-documents/cpp/cost-of-conflict/Vakhtang%20Charaia_Eng.pdf (last seen on 26.02.2017).
- [21] V. Charaia, Economics of Conflict: Core Economic Dimensions of the Georgian-South Ossetian Context. *International Journal of Humanities and Social Sciences* Vol:3, No:10, 2016. <http://waset.org/abstracts/55987> (last seen on 26.02.2017).
- [22] V. Charaia, Foreign Direct Investment (FDI) Inflow in Georgia. *9th International Silk Road Conference on Business, Economics, International Relations and Education*, 2014, pp. 53-60. <http://silkroad.ibsu.edu.ge/previous/nineth/9th%20International%20Silk%20Road%20Conference.pdf> (last seen on 26.02.2017).
- [23] V. Charaia, Local Investment Climate and the Role of (Sustainable) FDI: The Case of Georgia, *International Journal of Social, Behavioral, Educational, Economic, Business and Industrial Engineering*, Vol:8, No:2, 2014, pp. 425-428. <http://waset.org/publications/9997562/local-investment-climate-and-the-role-of-sustainable-fdi-the-case-of-georgia> (last seen on 26.02.2017).
- [24] O. Anguridze, V. Charaia, I. Doghonadze. Security Problems & Modern Challenges of the Georgian National Currency. *Ivane Javakhisvili Tbilisi State University*. 2015. [http://press.tsu.ge/data/file_db/nashromebi/Security-Problems-Modern-Challenges-of-the-Georgian-National-Currency%20\(1\).pdf](http://press.tsu.ge/data/file_db/nashromebi/Security-Problems-Modern-Challenges-of-the-Georgian-National-Currency%20(1).pdf) (last seen on 26.02.2017).