JEL Classification: A12, D01, E2, F4, H56. https://doi.org/10.35945/gb.2022.13.007

FOREIGN DIRECT INVESTMENTS DURING THE CORONOMIC CRISIS AND ARMED CONFLICT IN THE NEIGHBOURHOOD, CASE OF GEORGIA

VAKHTANG CHARAIA

PhD in Economics, Associate Professor,
Business and Technology University, Georgia
vakhocharaia@gmail.com

MARIAM LASHKHI

Associate Professor,
Business and Technology University, Georgia
mariam.lashkhi@btu.edu.ge

MARIAM LASHKHI

Financial Analyst
TSU Centre for Analysis and Forecasting, Georgia
mariam.lashkhi09@gmail.com

Abstract. Paper provides an analysis of FDI challenges and their impact on the service sector of Georgia, under the covid-19 global pandemic, along with the armed conflict factor in Eastern Europe, between Ukraine and Russia. The article also discusses such issues as public debt, economic growth, employment, international rankings, trade, tourism and etc. Since the cases of different countries vary according to their economic structure, political reality, and even the readiness to overcome those newest and unprecedented challenges, the case of Georgia provides a great example of a small, democratic, developing economy, which significantly depends on foreign direct investments both inward and outward, regional stability and not the least - western cooperation and support.

KEYWORDS: COVID-19 GLOBAL PANDEMIC, ARMED CONFLICT, FOREIGN DIRECT INVESTMENTS, GEORGIA, SERVICE SECTOR.

For citation: Charaia, V., Lashkhi, M., & Lashkhi, M. (2022). Foreign Direct Investments during the Coronomic Crisis and Armed Conflict in the Neighbourhood, Case of Georgia. *Globalization and Business.* 13, 51-56. https://doi.org/10.35945/gb.2022.13.007

INTRODUCTION

Covid-19 global pandemic, also known as Coronomic crisis (Papava, Charaia, 2020), has changed the global FDI picture, as well as the impact on different sectors of economy, especially in the service industry. The Coronomic crisis has already caused a widespread economic crisis (Geller et al, 2020), transforming from healthcare challenge, towards an „economic pandemic" (Riley, 2020) with disruptions in global supply chains, an extreme increase of public debts, a mass increase of unemployment, unprecedented lockdowns, innovative restrictions on business and society and etc. (Papava, Charaia, 2021). At the same time, the Russian-Ukrainian war (Kirby, 2022) has put extra stress on investment making in the Eastern European Region and Georgia in particular.

Because of the change of standard ways of doing business before and after covid-19, investors from all over the world were also pushed:

- To concentrate on unusual business circumstances;
- To consider the pandemic experience of last years;
- To reflect spontaneous governmental policies in general causing business restrictions;
- To study the changes in consumer behaviour related towards covid-19 reality;
- To consider the factors of inflation and devaluation of local currencies simultaneously;
- To push towards more digitalization and etc.

These factors, in most cases, were hindering economic activities, including international investments and trade, leading towards recession in around 90 percent of countries worldwide in 2020 (Papava, Charaia, 2021), with the fragile recovery in 2021 (Roubini, 2021) and probably significant challenges for the next years as well. What is needed to overcome at least from the financial point of view is not simply more investments to inject, but also a better delivery system (Miliband et al, 2021), as well as synergy in spending for healthier global results.

On top of those issues mentioned above, the war factor in the Eastern Europe puts an extra challenge for the markets of those countries belonging to the region including Georgia. Such ones could be:

- The factor of possible war theatre expansion to the neighbouring countries (Soros, 2022);
- Economic deterioration of the Russian Federation as a result of unprecedented international sanctions (Ben-David, 2022);
- The damage for the region, including the monetary consequences (Eichengreen, 2022), partial gap in supply chains (Segal, 2022) and scarcity of specific products (Puma, & Konar, 2022) and etc.;
- Risks of higher inflation than expected in the Western countries and the predictions of much larger inflation in Russia, affecting latest's neighbouring countries, including Georgia and the rest of the world (Ip, 2022);
- The risk of damaging Russia's neighbouring developing countries (Ghosh, 2022), which became especially vulnerable after the war which followed the Cornomic crisis.

Both Covid-19 and the war have the potential of significantly weakening the economic potential of the East European region. However, on the other hand, a significant portion of political, economic and also military support from the West should not be underestimated as well. However, so far it is hard to predict if the benefits will overcome the losses (from the economic point of view) or vice versa.

Challenges on the Coronomic side

With Paul Krugman believing that weird times are calling for weird economic thinking (Krugman, 2021), coronomic crisis has overturned the whole economic order ever known before, requesting new approaches both in SME and MNE sectors (Zhan, 2020) and heating transition economies harder than other regions (UNCTAD, 2020).

According to the World Investment Report (2020), global flows of FDI were significantly affected by the COVID-19 pandemic and fell down by around 40 percent in 2019, followed by another 35 percent downturn, reaching - $1 trillion or around 20 percent below the level achieved in 2009, immediately after the global financial crisis of 2008 year.

With varying details in different regions, the service sector investments, such as tourism and related industries and also new infrastructural projects, has been heated significantly, with developing countries affected the most. Postponing progress for some time in the future.

Negative effects of Covid-19 hit FDI flows to the transition economies of South-East Europe, the Commonwealth of the Independent States and Georgia tougher than markets in most other regions. FDI decrease halved the previous year's results down to $24 billion, with around 70 percent decrease for the Russian federation (UNCTAD, 2020).

FDI depended Georgia, which exports around half of its exports by the companies with foreign investments, employs around 1/4 of its working power and etc. (Sikharulidze, Charaia, 2018), has been affected by the Coronomic crisis significantly. FDI outflow, which shows the strength of local economy, has decreased by 12 times in 2020, down to $23 million (UNCTAD, 2021).

On the other hand, FDI inflow has shrunk by 57 percent, down to $572 million (GEOSTAT, 2022) in 2020, around 15 percent below 2009, when the country was suffering from the double disease: post-war period and global financial crisis. The situation is dramatic, but from a positive point of view, reinvestments for the same year made an unprecedented 87.5 percent.

Those results mentioned above are simultaneously signalling different issues, both positive and negative ones:

- Foreign investors already familiar with Georgia do trust this economy and its perspectives;
- Foreign investors unfamiliar with Georgian economy prefer to wait until better times to invest into this market;
- Local companies with (beforehand) enough financial, technical, institutional and etc. competencies are nowadays facing hard times and/or prefer to postpone their investments, since the vast majority of such businesses preferred to invest into neighbouring countries, which nowadays are facing serious coronomic challenges.

On the structural side of in-flowed FDI picture is also vague:

- Investments in the financial sector which usually used to be around 15 percent, has reached an unprecedented 70 percent, 404 million in absolute numbers;
- Investments in such service sectors as: transport, construction, health and social work has decreased by around 50 percent in average;
- Hotels and Tourism industry has suffered the most, decreasing from positive $123.4 million in 2019, to negative $249.5 million in 2020.

Of course, not all of those trends or at least not totally were caused by covid-19, but had significant links to this global phenomenon.

Overall, because of coronomic crisis or issues around it, Georgia occurred in a reality with:

- Decrease Foreign investments, both direct and indirect;

- Significant increase in unemployment almost in all areas of the economy;
- Higher public debt rate to GDP, exceeding international standards and local regulations;
- Increased budget deficit which limited new programs from IFIs;
- Increased inflation, especially increased priced on medicine and food;
- Decreased salaries almost in all industries all over the country;
- Different restrictions on economic activities, such as the ban on specific industries, limiting working hours and so on;
- Increased pressure on the state budget coming from foreseen and unforeseen challenges of coronomic crisis;
- Meaningless expenditures, for instance, paid for vaccines, while the majority of society is not willing to vaccinate because of conspiracy theories (Charaia et al, 2020);
- Challenges in political and social stability, which from time to time push the government to undertake populistic decisions in some directions and etc.

After the critical 2020, foreign direct investments grow more than two times in 2021, exceeding $1.15 billion. This fact could be explained by strong messages from the Georgian market that it stays on the right path of development, despite the pandemic ambiguity and the second, trust of local and foreign investors in the market with huge perspectives unrealized so far.

To overcome a current (coronomic) crisis government has to change the structure of its economic development, moving from the dominantly service-oriented ones, toward more local production-oriented ones (Stiglitz, 2021). And we do believe that this should be the case for Georgia as well. However, statistics show that this idea is neglected by international investors globally (UNCTAD, 2021), as well as in Georgia (diagram 1). Thus, making it possible to overcome the crisis even without a dramatic shift in industries, however putting it under even more stress for the future.

According to the official statistics import dependence in Georgia is around 3-4 times higher than export, while a great number of imported products are possible to produce locally, not only for the local but also regional markets.

A great advantage for the Georgian market is its free trade agreements (FTA) with the world's biggest economies, such as China, EU and others. This specific advantage could be used not only for trade, but also investment attraction to produce goods and services in Georgia and export them further to different countries and regions with the favourable free trade regimes or avoiding double taxing.

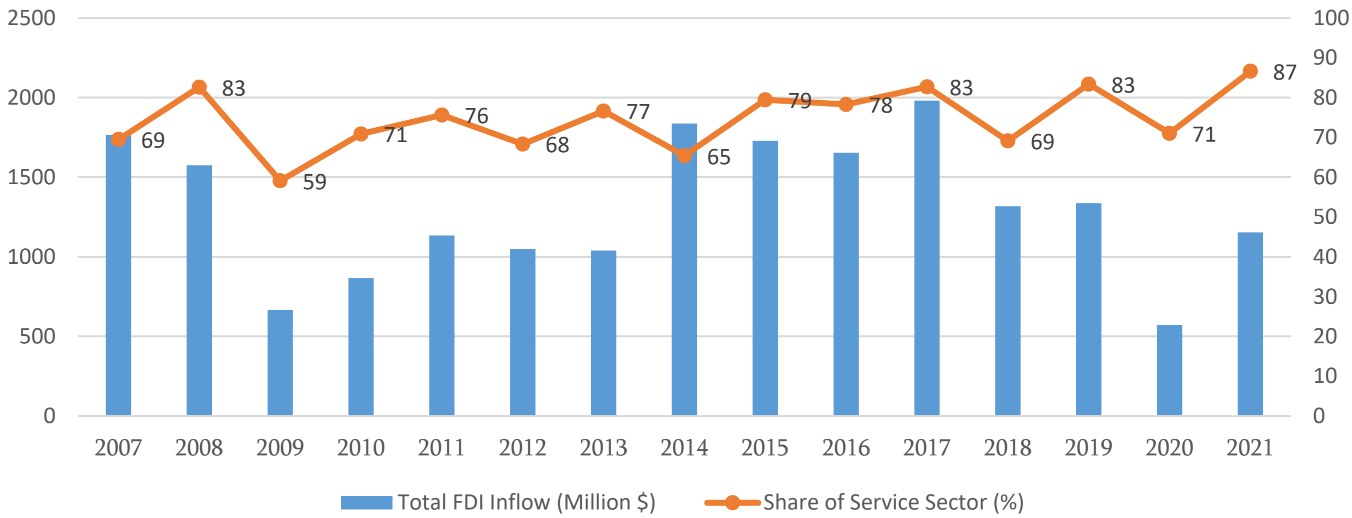
Cost of conflict and recommendations

To support the stable, inclusive and diversified economic development of the Georgian economy, it should constantly maintain progressive reforms and closely cooperate with its local and international associates, including partner countries, international organizations, business sector representatives and etc. However, we see that the factor of peace, could be at least no less important than, those legislative and globalization aspects of business making. Russian aggression/war in Ukraine (Allison, 2014) and war with Georgia in 2008, are great examples.

Since the Georgian economy is closely interlinked with the economies of Russia, Ukraine and also Belarus, all of which are under huge stress nowadays, Georgia will also face significant stress. Based on the official statistics:

- Georgia exported more than 14% of its goods to the Russian market in 2021, while all those three countries were a market for more than 23% of total Georgian exports (almost $1 billion) (GEOSTAT, 2022);
- Georgia was importing more than 10% of all foreign

Diagram 1. Amount of FDI (million USD) and the share of the Service sector (%)



Source: GEOSTAT. https://geostat.ge/media/43843/FDI_Eng-sectors.xlsx

goods only from Russia, while all three countries combined were reaching the 15% level ($1.5 billion) in the previous to the war year (GEOSTAT, 2022);
- Georgia was receiving from 5 to 10 percent of its foreign investments ($50-100 million) annually for the last years, from the given three countries combined, but dominantly from Russia (GEOSTAT, 2022);
- Georgia received 18% of its remittances from Russia ($411 million) and 4% from Ukraine ($93 million) for the 2021 (NBG, 2022);
- Georgia received 19% in pre-pandemic 2019 (1.472 million trips) and 12% of its international visitor trips (213 thousand) from Russia in 2021; for the same years the number of Ukrainian trips to Georgia raised from 3 to 8%; Belarus from 1% to 3%. However, should be noted that in 2021 Georgia received only 1.72 million international visitor trips, while in pre-pandemic 2019 the result was 7.73 million (GNTA, 2022).

These numbers are clearly explaining the challenges the Georgian economy will face because of the Russian invasion into Ukraine, as a result of sanctions on Belarus, unprecedented sanctions imposed on Russia and damaged Ukrainian economy. It will be challenging for the Georgian economy to face that economic hit, especially after the fight with covid-19. Georgia could face challenges not only in trade, tourism and remittances, but the pressure on inflation and exchange rate could become more severe. However, on the other hand, US and EU support to Georgia is also strong, which has a strength to decrease the stress level for Georgian economy.

To provide state of the art reforms vital for covid and also post-covid realities, as well as considering the war effect, Georgia should undertake a significant wave of reforms, including but not limited to:

- Concentrating on the post-covid trends already obvious from nowadays, for instance, such as digitalization;
- Improving educational system, including schools, universities and professional education/training;
- Popularization / active support for the jobs of the future, already predicted by different international organizations;
- Developing modern financial system, with a proper balance between the banking sector, capital market, fintech (Charaia et al, 2021) and other interested players on the market;
- Assisting business with the qualified labour force, to minimize the supply and demand mismatches;
- Improving local infrastructure, including energy efficiency and security;
- Supporting export-oriented and import substitution aiming local production in different areas;
- Providing political stability and predictable legislative base, guaranteeing reforms according to the best practices;
- Support market diversification in terms of trade, tourism and investments to guarantee a negligent dependence on particular markets, especially on Russia.

Georgia's chance to overcome both the coronomic and war challenges simultaneously is in forming reliable partnerships with the global players from all over the world, oriented on mutual benefits and stability (Charaia, Lashkhi, 2020; 2021), supporting innovation and development (Benashvili, 2017; Shatakishvili, 2021), cooperation with the international organizations and close allies in the West.

CONCLUSION

FDI motivations and their impact on service sector during Covid-19 global pandemic in case of Georgia shows that there are more challenges, than opportunities for the given moment, but different prospects for creating a modern economy.

Coronomic crisis has changed the decision-making process of the business sector all over the world at large, but still seeks for the best deals which country is able to offer and there the need of reforms and modern approaches arise.

Georgian case, as an average representative of the developing world, with a small population and market opportunities, import and FDI depended economy, significantly involved in globalization and thus affected by both, its positive and negative impacts, has shown that global investors are more careful with their investment decision nowadays.

Without significant reforms and modernization, developing countries like Georgia are doomed to failure, or at least for freezing their progress.

Coronomics proved that the way some countries had chosen before the pandemic (developing, service-oriented and import depended consumer economy), will not work after the pandemic, however there is still much time for action and reforms guaranteeing supplementary success, restored reputation, increased attractiveness, social stability, sustainable and inclusive growth.

Trade, tourism, remittances and also investment numbers are clearly showing the level of challenge for the Georgian economy, it will face because of the Russian invasion into Ukraine, as a result of sanctions on Belarus, unprecedented sanctions imposed on Russia and damaged Ukrainian economy.

It will be challenging for the Georgian economy to face that new wave of economic hit, especially after the fight with covid-19. Along with the direct economic hits through trade, tourism, remittances and investments, the inflation and exchange rate will become more vulnerable.

Georgia can stand strong against both the coronomic and war challenges only through systematic reforms, supporting innovation and close cooperation with the West and international organizations.

REFERENCES:

Allison, R. (2014). Russian – deniable - intervention in Ukraine: how and why Russia broke the rules Get access Arrow. *International Affairs*. 90, (6), November 2014, 1255–1297, https://doi.org/10.1111/1468-2346.12170

Benashvili, G. (2017). Boosting Entrepreneurship in Georgia Development of Fab Labs. *PressAcademia.* 4, (1), 29-33. http://pressacademia.org/archives/pap/v4/4.pdf

Ben-David, R. (2022). Unprecedented' scale of sanctions, boycott took Russia by surprise, experts say. *The Times of Israel*. https://www.timesofisrael.com/unprecedented-scale-of-sanctions-corporate-boycott-take-russia-by-surprise/

Charaia, V., Chochia, A., & Lashkhi, M. (2020). The impact of FDI on Economic development: The Case of Georgia. *TalTech Journal of European Studies*. 10 (2), 96-116. https://sciendo.com/article/10.1515/bjes-2020-0017

Charaia, V., Chochia, A., & Lashkhi, M. (2021). Promoting Fintech financing for SME in S. Caucasian and Baltic States during the Covid-19 Global Pandemic. *Journal of Business Management and Economics Engineering.* 19 (2). https://journals.vgtu.lt/index.php/BME/article/view/14755

Charaia, V., & Lashkhi, M. (2020). Georgia and China: The Economic Ties that Could One Day Bind. A Sea Change? China's Role in the Black Sea, 26. https://mei.edu/sites/default/files/2020-11/A%20Sea%20Change%3F-China%27s%20Role%20in%20the%20Black%20Sea.pdf

Charaia, V., & Lashkhi, M. (2021). COVID-19 effect on FDI motivation and their impact on service sector: Case of Georgia. In C. Cobanoglu, & V. Della Corte (Eds.), *Advances in global services and retail management*. 1-11. USF M3 Publishing. https://www.doi.org/10.5038/9781955833035

Charaia, V., & Lashkhi, M. (2021). Economic cooperation between Central Caucasus, China, and EU, under COVID-19 challenges. In C. Cobanoglu, & V. Della Corte (Eds.), *Advances in global services and retail management*. 1–9. USF M3 Publishing. https://www.doi.org/10.5038/9781955833035

Charaia, V., & Lashkhi, M. (2021). *Strategic cooperation between China and the South Caucasus countries.* China and Eurasia: Rethinking Cooperation and Contradictions in the Era of Changing World Order. Routledge. https://www.taylorfrancis.com/chapters/edit/10.4324/9781003109259-14/strategic-cooperation-china-south-caucasus-countries-vakhtang-charaia-mariam-lashkhi

Eichengreen, B. (2022). The Monetary Consequences of Vladimir Putin. *Project Syndicate.* https://www.project-syndicate.org/commentary/russia-financial-sanctions-will-change-currency-reserves-by-barry-eichengreen-2022-03?a_la=english&a_d=6229cf8fef1af2dec478e263&a_m=&a_a=click&a_s=&a_p=homepage&a_li=russia-financial-sanctions-will-change-currency-reserves-by-barry-eichengreen-2022-03&a_pa=latest&a_ps=&a_ms=&a_r=

Geller, A., Wiseman, P., & Rugaber, C. (2020). Outbreak Starts to Look More Like Worldwide Economic Crisis. *Herald Tribune*. February 28.

GEOSTAT. (2022). External Trade. https://www.geostat.ge/en/modules/categories/35/external-trade

GEOSTAT. (2022). Foreign Direct Investments. https://geostat.ge/media/43842/FDI_Eng-countries.xlsx

Ghosh, J. (2022). Putin's War Is Damaging the Developing World. *Project Syndicate.* https://www.project-syndicate.org/commentary/ukraine-war-economic-damage-for-developing-countries-by-jayati-ghosh-2022-03

GNTA. (2022). International Travel (Residence). (2021). https://gnta.ge/wp-content/uploads/2022/01/2021-ENG.xlsx

Ip, G. (2022). War in Ukraine Fans the Flames of Global Inflation. *The Wall Street Journal.* https://www.wsj.com/articles/war-in-ukraine-fans-the-flames-of-global-inflation-11646922368

Kirby, P. (2021). Why has Russia invaded Ukraine and what does Putin want? *BBC*. https://www.bbc.com/news/world-europe-56720589

Krugman, P. (2021). Pandemic Economics: Stay Weird. *The New York Times*. February 16. https://static.nytimes.com/email-content/PK_sample.html

Lashkhi, M., & Charaia, V. (2017). Investment Development Path and Motivations for Foreign Direct Investment in Georgia. World Academy of Science, Engineering and Technology. *International Journal of Economics and Management Engineering*. 11, (11), 3213.

Lashkhi, M., & Charaia, V. (2020). China in the South Caucasus: Economic Interests. *Silk Road 2020 (virtual) Conference*. 74-78. https://www.researchgate.net/profile/Kyrylo-Mieliekiestsev/publication/349670327_The_post-truth_era_and_its_effects_on_public_perception_of_Georgian_and_Ukrainian_history/links/603bb202299bf1cc26fbb270/The-post-truth-era-and-its-effects-on-public-perception-of-Georgian-and-Ukrainian-history.pdf#page=75

Miliband, D., Radin, E., & Eleftheriades, C. (2021). Fixing the Broken Pandemic Financing System. Project Syndicate. https://www.project-syndicate.org/commentary/fixing-pandemic-financing-system-by-david-miliband-et-al-2021-06

NBG. (2022. Money Transfers by Countries. https://nbg.gov.ge/fm/%E1%83%A1%E1%83%A2%E1%83%90%E1%83%A2%E1%83%98%E1%83%A1%E1%83%A2%E1%83%98%E1%83%99%E1%83%90/external_sector/eng/money-transfers-by-countries-eng.xlsx?v=17w5z

Papava, V., & Charaia, V. (2020). The coronomic crisis and some challenges for the Georgian economy. *GFSIS, Expert Opinion*. 136. https://www.gfsis.org/files/library/opinion-papers/136-expert-opinion-eng.pdf

Papava, V., & Charaia, V. (2021). Public Debt Increase Challenge under COVID-19 Pandemic Economic Crisis in the Caucasian

Countries. *Journal of Contemporary Issues in Business and Government.* 2021, 27, 3. https://cibg.org.au/article_10671.html.

Papava, V., & Charaia, V. (2021). The Problem of the Growth of Georgia's Public Debt during the Economic Crisis under the COVID-19 Pandemic. *GFSIS, Expert Opinion*. 152. https://www.gfsis.org/files/library/opinion-papers/152-expert-opinion-eng.pdf

Puma, M. J., & Konar, M. (2022). What the War in Ukraine Means for the World's Food Supply. *The New York Times*. https://www.nytimes.com/2022/03/01/opinion/what-the-war-in-ukraine-means-for-the-worlds-food-supply.html

Riley, C. (2020). Coronavirus is fast becoming an 'Economic Pandemic'. *CNN Business.* https://edition.cnn.com/2020/02/24/business/coronavirus-global-economy/index.html

Roubini, N. (2021). A Fragile Recovery in 2021. *Project Syndicate.* https://www.project-syndicate.org/onpoint/fragile-global-and-us-recovery-in-2021-by-nouriel-roubini-2021-01

Segal, E. (2022). Ukraine Crisis Creates New Strains On Global Supply Chains. *Forbes*. https://www.forbes.com/sites/edwardsegal/2022/03/06/ukraine-crisis-creates-new-strains-on-global-supply-chains/?sh=339781e910af

Shatakishvili, D. (2021). Economic Ties of Georgia with Central Asian Countries and Future Cooperation Perspectives. Inter*national Journal of Trend in Scientific Research and Development*. 5, (6), 305-314. www.ijtsrd.com/papers/ijtsrd46396.pdf

Sikharulidze, D., & Charaia V. (2018). Oli paradigm and investment position of Georgia. *Globalization & Business*. 71–78. https://www.eugb.ge/view_archive2.php?content=content&id=126&OLI%20PARADIGM%20AND%20INVESTMENT%20POSITION%20OF%20GEORGIA

Soros, G. (2022). Vladimir Putin and the Risk of World War III. *Project Syndicate.* https://www.project-syndicate.org/commentary/putin-ukraine-world-war-3-risk-by-george-soros-2022-03

Stiglitz, J. (2021). COVID-19 and Human Freedom. *Project Syndicate*. https://www.project-syndicate.org/commentary/covid19-spike-in-us-reflects-misunderstanding-of-liberty-by-joseph-e-stiglitz-2021-09?utm_source=Project+Syndicate+Newsletter&utm_campaign=1cbaf2a836-covid_newsletter_09_09_2021&utm_medium=email&utm_term=0_73bad5b7d8-1cbaf2a836-93567601&mc_cid=1cbaf2a836&mc_eid=e9fb6cbcc0

UNCTAD. (2021). Global foreign direct investment rebounded strongly in 2021, but the recovery is highly uneven. https://unctad.org/news/global-foreign-direct-investment-rebounded-strongly-2021-recovery-highly-uneven

UNCTAD. (2021). *World Investment Report.* https://unctad.org/system/files/official-document/wir2021_en.pdf

Zhan, X. (2020). Covid-19 and investment - an UNCTAD research round-up of the international pandemic's effect on FDI flows and policy. *Transnational Corporations*. 27 (1).