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THE MOTIVES AND IMPEDIMENTS TO FDI IN THE CIS

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ABSTRACT

This paper examines the motives behind foreign direct investments in a group of the CIS countries (Ukraine, Moldova, Georgia and Kyrgyzstan) based on the survey of 120 investors. The results indicate that non-oil MNEs are predominantly oriented at serving local markets. On average, MNEs in the CIS operate as ‘isolated players’, weakly cooperating with local CIS firms, but strongly linked to their parent companies. The surveyed firms secure very little percentage of supplies locally. For this reason, the possibility for spillovers arising from the cooperation with foreign-owned firms in the CIS is rather low at the moment. There is a lack of efficiency-seeking investment that poses further concern about the nature of FDI in the region. The most important problems in every day operations of surveyed foreign firms are volatility of the political and economic environment, ambiguity of the legal system and corruption.

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1. INTRODUCTION

The importance of transition economies as investment sites for multinational corporations has drastically increased over the last decade. With economic liberalization of Central and Eastern European countries, former Soviet Union republics, and hefty developments in People's Republic of China and East Asian economies, vast market and production opportunities have opened up for multinational businesses. Although a number of multinational corporations have successfully managed to capitalize on these opportunities, a number of firms have been significantly less successful in their internationalization efforts. Various internal and external factors were shown to considerably affect success of multinational businesses in transition economies setting (Peng and Heath 1996; Khanna and Palepu 1997; Sullivan 1998; Luo and Peng 1999; Isobe et al 2000; Peng and Luo 2000; Uhlenbruck and De Castro 2000).

Among the transition economies, the region of the Commonwealth of Independent States (CIS) experienced boom in foreign direct investment in recent years. The magnitude of capital inflows resembles FDI attracted to the Central and East European countries in the 1990s. FDI coming to the CEE and to the SEE countries had contributed to the major growth of productivity of local industries and services, acting as important sources of modern technologies and managerial knowledge.

The aim of the current analysis is to explore the motives for FDI in the smaller CIS countries (Ukraine, Moldova, Georgia and Kyrgyzstan), as well as to analyse how business and industry environment in the countries affects the foreign investors. The study targets three groups of investors with potentially different investment motives: market-seekers, resource/labour-seekers and efficiency-seekers (Dunning, 1993). This analysis will complement earlier results (which mostly were centred on Russia (Rogacheva & Mikerova, (2003), Ledayeva (2007)) by showing what aspects of investment climate are of particular concern to investors into the larger CIS. Also it will deepen our understanding of the problems which investors are facing in the CIS through differentiation among various investment types, which is a novel feature of this analysis.

We approach this task by conducting a survey foreign-owned companies located in the four CIS countries (120 firms in total). The survey took place in 2007-2008 in Georgia, Kyrgyzstan, Moldova and Ukraine. Non-oil and resource-attracting countries were dropped from the analysis. In this way we were able to see the analogies with the CEE or SEE countries, which have attracted mainly non-oil FDI.

The paper is organized as follows. First part presents the basic theoretical and empirical studies on the motives for FDI in general and in the CIS/CEE setting in particular. The next section offers some key facts about FDI flows into the region. In the subsequent section we investigate the survey findings followed by the econometric analysis of the data. The last section concludes the paper and offers some suggestions to policy makers.

2. INVESTMENT MOTIVES

The literature on FDI identifies three most common investment motivations: resource-seeking, market-seeking and efficiency-seeking (Dunning, 1993).

Availability of natural resources, cheap unskilled or semi-skilled labor, creative assets and physical infrastructure promotes resource-seeking activities. Historically, the most important host country determinant of FDI has been the availability of natural resources, e.g. minerals, raw materials and agricultural products.

Even when it was prominent as an FDI determinant, the presence of natural resources by itself was not sufficient for FDI to take place. Comparative advantage in natural resources usually gave rise to trade rather than to FDI. Investment took place when resource-abundant countries either lacked the large amounts of capital typically required for resource-extraction or did not have the technical skills needed to extract or sell raw materials to the rest of the world. In addition, infrastructure facilities for getting the raw materials out of the host country and to its final destination had to be in place or needed to be created (UNCTAD, 1998).

Labor-seeking investment is usually undertaken by manufacturing and service MNEs from countries with high real labor costs, which set up or acquire subsidiaries in countries with lower real labor costs to

supply labor intensive intermediate or final products. Frequently, to attract such production, host countries have set up free trade or export processing zones (Dunning, 1993).

Market-seeking investment is attracted by factors like host country' market size, per capita income and market growth. For firms, new markets provide a chance to stay competitive and grow within the industry as well as achieve scale and scope economies. Traditionally, market size and growth as FDI determinants related to national markets for manufacturing products sheltered from international competition by high tariffs or quotas that triggered "tariff-jumping" FDI (UNCTAD, 1998, 107). Apart from market size and trade restrictions, MNEs might be prompted to engage in market-seeking investment, when their main suppliers or customers have set up foreign producing facilities and in order to retain their business they need to follow them overseas (Dunning, 1993, 58).

The motivation of efficiency seeking FDI is to rationalize the structure of established resource based or market-seeking investment in such a way that the investing company can gain from the common governance of geographically dispersed activities. The intention of the efficiency seeking MNE is to take advantage of different factor endowments, cultures, institutional arrangements, economic systems and policies, and market structures by concentrating production in a limited number of locations to supply multiple markets (Dunning, 1993, 59). In order for efficiency seeking foreign production to take place, cross-border markets must be both well developed and open, therefore it often flourishes in regionally integrated markets (Dunning, 1993, 59).

However it is worth noting that many of the larger MNEs are pursuing pluralistic objectives and most engage in FDI that combines the characteristics of each of the above categories. The motives for foreign production may also change as, for example, when a firm becomes an established and experienced foreign investor (Dunning, 1993, 56).

3. DETERMINANTS OF FDI IN THE CIS

Resource-seeking investors

The abundance of natural resources in the CIS has been one of the most important determinants of FDI. Shiells (2003) showed that FDI in the CIS up to the early 2000s were related to the extraction of natural resources, to the construction of pipelines transporting these energy resources, large privatizations, and to debt/equity swaps to pay for energy supplies. The disappointing level of FDI at that time reflected weak investment climate in the region, particularly because of incomplete structural reforms. Campos and Kinoshita (2003) also find resource-seeking to be the key motivation for FDI in the CIS, whereas this factor had no effect for non-CIS countries.

Tondel (2001) stressed that, according to IMF estimates, between 75% and 82% of total FDI in Azerbaijan were in oil and gas industry. Besides, 30 cents of each dollar invested in other parts of economy was related to investments in oil and gas industry (Tondel 2001). Up to 2006, vast majority of incoming FDI in Georgia was related to the pipeline transportation. In Kazakhstan, which recorded the highest FDI per capita in the CIS (second only to Azerbaijan), most investments have also been directed towards the natural resource sector. The abundance of energy resources in Russia were also quoted as an important determinant of FDI (Rogacheva and Mikerowa 2003, Ledayeva 2007). Ledayeva (2007) found that after the 1998 Russian financial crisis the importance of large cities, availability of oil and gas resources, and legislative risk has increased, while the importance of sea ports and political risk has decreased. Also, the study showed that costs of production in Russia did not attract FDI.

Market-seeking investors

A number of studies on FDI in the CIS point to the paramount importance of market-seeking motivation for the investors. The earliest of this kind is by Collins and Rodrick (1991). The access to domestic FSU markets was reported to be a major motivation for investment just at the time when the Soviet Union was falling apart. The survey was conducted among 54 larger companies operating in the USSR in 1990-91. The second important motivating factor was named a proximity to the European Community.

Market-seeking motive was also demonstrated to be of high importance in later studies. Tondel (2001) reports high relevance existence of both market-seeking and natural resource-seeking motives in the CIS. The more recent results of Johnson (2006) also suggest that FDI in the CIS have been both market- and resource-driven. GDP of the CIS countries per capita (market size) and oil dummy were positive and significant in Johnson's equations, while wages were negative.

Market-seeking motive was also found to be determining FDI in Russia. According to the results of the survey by Rogacheva and Mikerova (2003), the main motive for investment in Russia was market potential (obtained 9 points of 10). Natural resources were also important in view of significant investment (6 points) in Russian energy field. Strategic location (1 point) was the main concern for the multinational companies doing business all over the world. Low costs (1 point) were recognized as insignificant. Interestingly, political and economic situation in Russia was named stable enough to invest. Market-seeking motive in Russia was also confirmed by Ledayeva (2007).

Table 1 compares the studies of FDI motivations into the CIS and current new EU member states (NMS) This simplified review shows that foreign investors seek markets both in the CIS and in the NMS. The difference is that natural resource-seeking factors prevail in the CIS, while factors that relate to the efficient use of labour and cross-border efficiency are important in the NMS setting.

Table 1. The relation between FDI determinants and the character of investment decision

Group of countries	Variables determining FDI inflows
CIS	<p>Resource-seeking factors <u>Abundance of natural resources</u> Campos, Kinoshita, 2003 Johnson, 2006 Merlevede, Shoors, 2004 Shiells, 2003</p> <p>Market-seeking factors <u>Market size (growth)</u> Tondel, 2001 Johnson, 2006 Merlevede, Shoors, 2004</p> <p>Efficiency-seeking factors N/A</p>
Current new EU members and Western Balkans	<p>Resource-seeking factors <u>Labour</u> Horwath, Ribakova, Wu, 2005 Smarzynska, Wei, 2002 Merlevede, Shoors, 2004 Lansbury, Pain and Smidkova, 1996</p> <p>Market-seeking factors <u>Market size (growth)</u> Johnson, 2006 Merlevede, Shoors, 2004 <u>Population</u> Johnson, 2006</p> <p>Efficiency-seeking factors <u>Institutions</u> Campos, Kinoshita, 2003 <u>Transition progress</u> Tondel, 2001 <u>Agglomeration</u> Campos, Kinoshita, 2003 <u>Privatization method</u> Merlevede, Shoors 2004 Botric, Skuflic 2005</p>

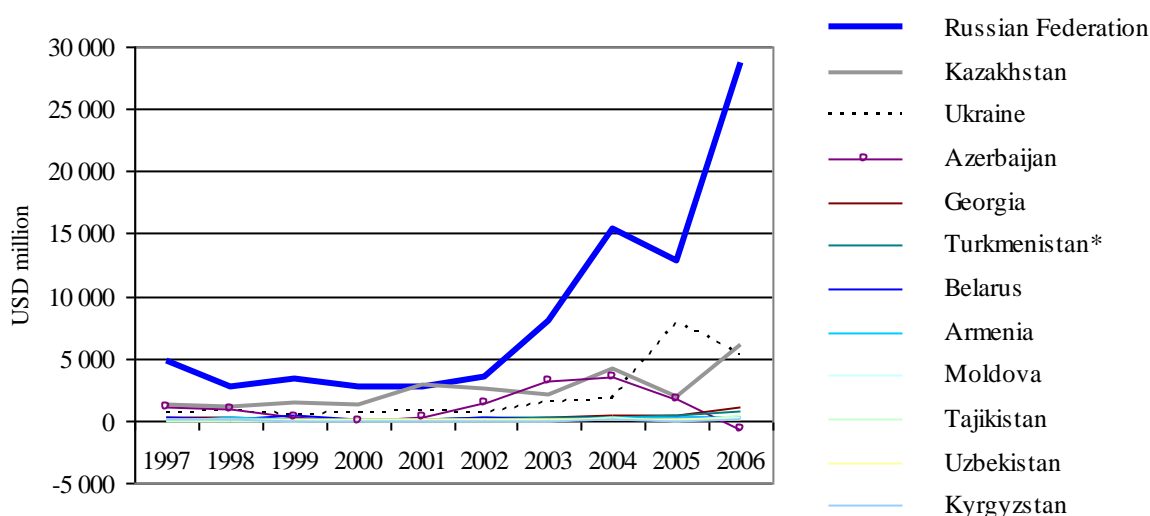
Source: own elaboration

4. FDI INFLOWS IN THE CIS

FDI inflows to the whole CIS region averaged in 2000-2006 about USD 19bn a year. Over half of it (USD 11bn a year on average) was coming to the Russian Federation (see Figure 1). This investment was mainly directed to the extraction and transportation of the energy resources. Two other CIS countries with abundant energy-resources, i.e. Kazakhstan and Azerbaijan, attracted USD 3bn and USD 1bn per annum respectively during 2000-2006.

If compared to the Central and Eastern European countries, the eight CEE countries which joined the EU in 2004¹ recorded total USD 25bn FDI inflows per annum on average in 2000-2006. The largest country of this group, Poland, attracted the average of USD 9bn per year mainly due to the development of the financial intermediation and manufacturing sectors in this period. Poland was followed by the Czech Republic that attracted USD 6bn on average in 2000-2006.

Figure 1. FDI inflows to the CIS, 1997-2006



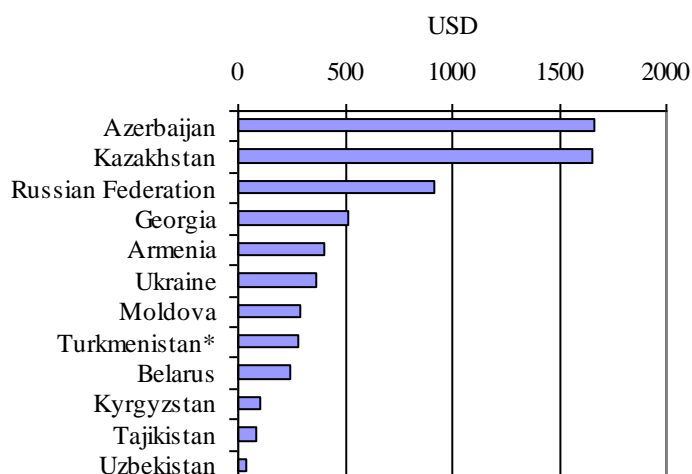
Source: UNCTAD

Note: * - Turkmenistan was in the CIS in 1991-2005; associate member since 2005

In terms of the accumulated FDI stock per capita, energy-resources and/or energy transit CIS countries lead (see Figure 2). Azerbaijan and Kazakhstan accumulated over USD 1,500 per capita in FDI stock in 2005. FDI stock per capita in Russia is close to 1,000 USD, and that of Georgia is about 500 USD. To compare, per capita FDI stock in Croatia in 2005 was 2,800 USD, and those for Romania and Bulgaria were over 1,000 USD. FDI per capita in the CEE countries were ranging from 2,700 USD in Poland to 9,400 USD in Estonia.

¹ The Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia.

Figure 2. FDI stock per capita in the CIS in 2005



Source: UNCTAD

Note: * - Turkmenistan was in the CIS in 1991-2005; associate member since 2005

Some of the CIS economies are very FDI-dependent, although FDI per capita is not high at all. Tajikistan has been the extreme example of it. FDI inflows in the 2000s accounted for the majority of all investment in the country, which basically reflect the lack of domestic resources. Over 1/3 of overall investment in the resource-rich Azerbaijan and Kazakhstan and in the consumption-driven Moldova were made by foreigners during 2000-2006. On the other hand, Uzbekistan, Belarus and Russia are very little FDI-dependent. Less than 10% of all investment in these countries was made by foreign firms.

In general, the CIS countries are on average less FDI-dependent than the CEE and SEE countries.² The average share of foreign firms in total investment in the CEE countries³ in 2000-2006 was around 23%, and in the SEE countries⁴ – 26%. It also reflects the fact that on average the CIS countries are still less open to FDI than their Eastern/Central and Southern European neighbours.

² Although there are exceptions of resource-rich Tajikistan, Azerbaijan and Kazakhstan.

³ The Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia.

⁴ Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Romania, Serbia and Montenegro.

Table 2. FDI inflows in percent of domestic investment in CIS, 1997-2006

Countries	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Commonwealth of Independent States (CIS)	8.9	9.8	13.4	8.4	9.0	10.5	14.2	17.7	13.3	17.1
Tajikistan	11.1	16.9	3.7	39.6	11.6	48.3	13.0	100.0**	27.5	100.0**
Azerbaijan	71.7	60.0	27.2	2.5	16.8	65.5	83.9	72.0	30.7	-
Kazakhstan	36.7	33.1	53.9	40.5	53.9	43.8	29.4	36.9	11.9	27.6
Moldova, Republic of	20.5	20.2	17.5	64.1	41.7	31.0	20.1	27.1	28.0	29.7
Georgia	37.4	28.7	11.3	17.4	15.2	20.1	32.3	33.6	24.0	54.5
Armenia	19.5	72.0	40.3	29.6	18.7	22.1	18.7	27.2	19.0	16.4
Turkmenistan*	9.8	4.8	8.2	8.9	11.8	22.1	17.5	27.0	24.3	40.2
Kyrgyzstan	37.9	51.7	22.6	-	1.9	1.8	17.4	54.4	11.3	45.7
Ukraine	6.3	9.1	8.2	9.7	10.6	8.5	13.8	11.7	43.0	21.0
Russian Federation	6.6	6.3	11.7	6.2	4.7	5.6	10.0	14.3	9.2	16.3
Belarus	9.9	5.1	13.9	4.5	3.4	7.7	3.8	2.6	4.0	3.4
Uzbekistan	3.2	3.1	2.6	2.3	3.2	3.0	3.3	7.0	3.0	5.4

Source: UNCTAD

Note: * - Turkmenistan was in the CIS in 1991-2005; associate member since 2005

** - own estimate

In our subsequent research, oil and resource-attracting countries were dropped from the analysis as we would like to capture possible analogies with the CEE/SEE countries (which have attracted mainly non-oil FDI). Those FDI in the CEE/SEE countries contributed to the major growth of productivity, and this is why this kind of investment is of the highest interest here in this paper. Taken together, the survey covers countries that attracted about 16% of overall FDI flows to the CIS in 2006.

5. SURVEY RESULTS

Survey design

This section presents the results of the survey of 120 foreign owned-companies located in Georgia, Moldova, Kyrgyzstan and Ukraine. The representatives of the companies in each country were asked a set of identical questions about the reasons to invest in the CIS, their business environment and impediments for their everyday activities. The survey was conducted in 2007-2008.

While drafting the questionnaire, existing findings on the investment motives in the CIS, CEE and SEE (described in the preceding part of this paper) were considered. The questions about the business environment of foreign-owned firms were formulated in such a way that allowed to conclude about the nature of production chains and check for the existence of various linkages between foreign-owned and local firms. There is evidence that the existence of such linkages (especially of the vertical type) has facilitated knowledge spillovers from the foreign-owned to domestic firms in some of the current new member EU states in the 1990s. The most relevant examples may be those of Romania and Lithuania (see Javorcik and Spartaneu 2006, Altomonte and Pennings 2006, Smazynska-Javorcik 2004). Therefore, it was interesting to check whether such spillovers can be detected in the CIS as well.

Description of the sample

The sample consisted of 30 foreign-owned companies from Ukraine, 30 foreign-owned firms from Moldova, 30 foreign-owned companies from Georgia, 29 from Kyrgyzstan and 1 from Kazakhstan. Most foreign companies operating in these countries started their business in the 1990s. The median company has been in business for 8 years, has revenues of about USD 4.7mn, and employs 145 people. Company profiles differ among the countries significantly. The Ukrainian companies are the largest in the sample with average annual revenues exceeding 5 times those of Moldovan companies, who still earned twice as much as Kyrgyz companies, which are the smallest in the sample. Average market share of the Georgian companies is less than 20%, whereas it is higher at 28% in Ukraine and Kyrgyzstan. Still, it is the Moldovan foreign-owned companies which hold leading positions on the local market with average market share of about 47%.

Most foreign companies operating in these countries started their business in the 1990s. For Ukraine and Kyrgyzstan, average time period is 8 years. Average time period for Moldova is much longer (17.8 years ago on average), as there are two companies working in food industry that established their business in Moldova more than 100 years ago.

Table 3. Sample statistics

	Profile	Min	Max	Average
1.	Years in the country			
	Ukraine	2.0	18.0	8.4
	Moldova	2.0	134.0	17.8
	Kyrgyzstan	2.0	15.0	7.7
	Georgia	1.0	17.0	6.2
2.	Annual revenue (turnover) of the subsidiary, million USD			
	Ukraine	0.03	1,233.0	80.7
	Moldova	0.009	121.1	13.8
	Kyrgyzstan	0.3	30.0	6.8
	Georgia	0.3	280.0	43.7
3.	Total amount of capital invested, million USD			
	Ukraine	0.06	600.0	67.1
	Moldova	0.0004	112.4	21.0
	Kyrgyzstan	0.2	50.0	8.7
	Georgia	0.15	160.0	39.9
4.	Personnel employed			
	Ukraine	7	3,500	502
	Moldova	10	1,653	370
	Kyrgyzstan	6	1,200	232
	Georgia	12	1,200	237
5.	Domestic market share,%			
	Ukraine	0.5	100.0	28.8
	Moldova	0.4	99.1	46.6
	Kyrgyzstan	5.0	100.0	28.7
	Georgia	0.0	100.0	19.6

Source: survey results

Note: Numbers are simple averages.

On average, companies differ significantly among countries in the scope of their business. Foreign companies invested much more in Ukraine compared to Moldova and Kyrgyzstan, thus gaining higher revenues. Annual revenue of companies investing in Ukraine is about USD 80mn, which is more than 5 times higher than Moldovan companies, while the amount of capital invested exceeds the average investment of Moldovan companies by almost three times. The foreign companies working in Kyrgyzstan that participated in our research were the smallest in terms of the scope of their business.

As for personnel employed, Ukrainian foreign companies are also the largest (about 500 employees on average), followed by Moldovan (370), Georgian (237), and Kyrgyz companies (232). The distribution of companies according to the personnel employed seems to be close to the normal distribution with an exception of the ‘thick tail’ in the upper end. Thick tail is made of several big companies employing over 1,000 workers.

The industry structure of the interviewed companies reflects FDI distribution by industries in the countries (compare Table 5 below with Appendix 3). Most companies are working in financial services, food industry, trade, transport & communications and construction. These activities are developing very fast in the CIS countries, giving high revenues and thus attracting foreign investors. At the same time, substantial investment inflow is the key reason behind the rise of these sectors.

Table 4. Distribution of surveyed companies by sector

Industry	Ukraine	Moldova	Kyrgyzstan	Georgia	Total
Agriculture	1			1	2
Food industry	4	4	7	4	19
Woodworking, pulp and paper industry, publishing	1		1		2
Textile and leather industry	1		1	1	3
Oil refineries		3	1	2	6
Production of chemicals	2		1	1	4
Machinery and equipment	2		1		3
Mining	1			2	3
Energy		1		3	4
Financial services	4	7	4	8	23
Retail and wholesale trade	7	2	4	1	14
Transport & Communications	3	4	4	1	12
Construction	1	4	4		9
Other activities	3	5	2	6	16
Total	30	30	30	30	120

Source: survey results

Factors attracting investors into cis

One of the main objectives of this survey was to explore the nature of FDI coming to the CIS countries. As we have mentioned before, investment motives are often classified either as market-seeking (when investing firm wants to supply products and services to a recipient country market) or as resource-seeking (intending to benefit from cost-efficient production in a recipient country) and/or as efficiency-seeking (looking for labour-productivity advantage or local specific creative assets).

We have tested the investment motives by asking interviewees to answer several questions: about the strategic role of the subsidiary established in the host CIS country, directly about their investment motives, and about the share exported production (for details, see Appendix 1).

Market seeking

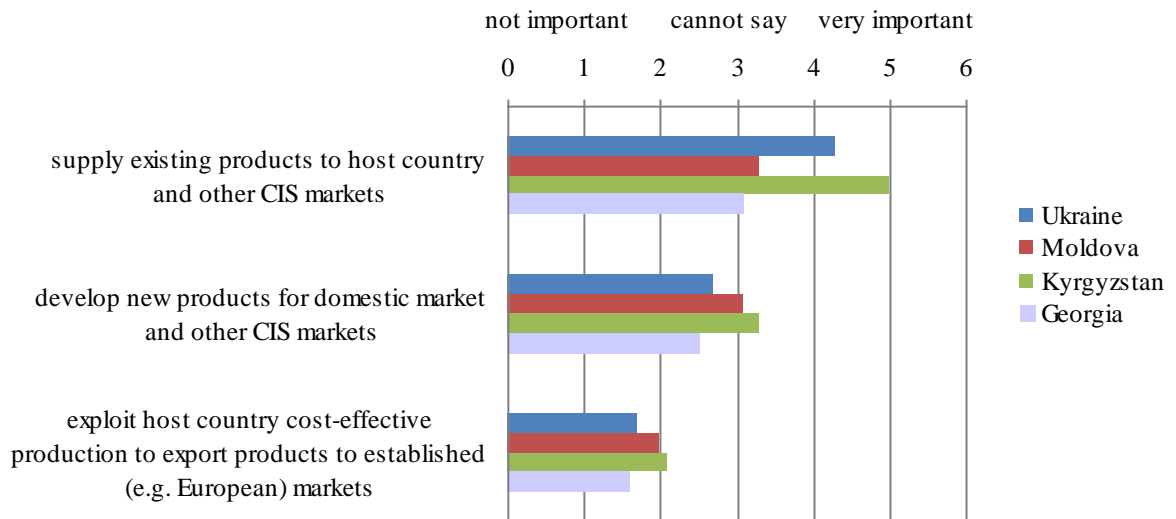
This motive clearly comes out as a dominant one in the sample. The companies that participated in the survey hold substantial share of the recipient country's market. Average domestic market share for Ukrainian and Kyrgyz firms is close to 30%, while Moldovan investors hold leading positions with average market share of about 47%. This means that the surveyed firms managed not only to supply their host markets but they also managed to secure dominant positions at these markets.

Percentage of local production of final and intermediate goods that is exported is rather low at 17% and 30% on average (see question 7; Appendix 1). About 70% of all the production of final goods is destined for the local markets. Some companies even mentioned that they faced a lot of problems when trying to export their products to other countries, particularly to Russia.

The role of the CIS affiliates in the operations of the parent companies as a supplier of existing products to the host country market and to other CIS markets was assessed on average as rather important (see Figure 3). The companies noted that the growing markets produce high demand, which is very positive for further expansion of their businesses.

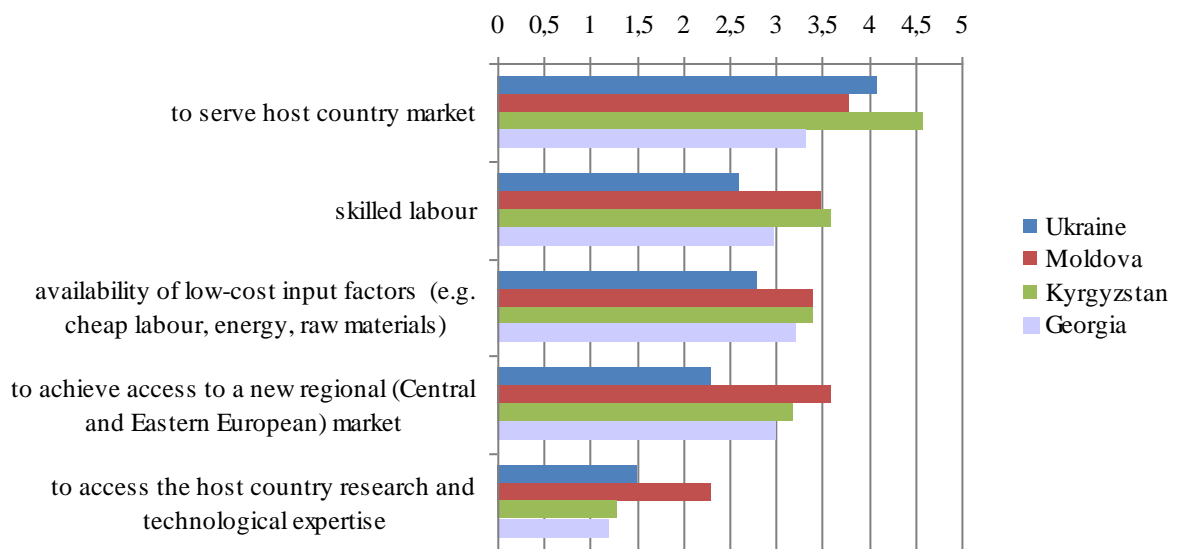
This outcome is supported by the results of the assessment of investment motives. The interviewees were asked to grade reasons for opening business activity in the CIS by ranging each of options from 1 (unimportant) to 5 (very important). Most companies mentioned the ability 'to serve the host country market' as the most important motive in all three economies (see Figure 4). On the top of it, companies in Moldova and Kyrgyzstan mentioned ability to avoid import duties while supplying domestic market as another reason to invest.

Figure 3. Strategic roles of CIS subsidiaries in operations of their parent companies



Source: survey results
 Note: Numbers are simple averages.

Figure 4. Reasons to invest in the CIS



Source: survey results
 Note: higher number indicates that a given reason is more important. Numbers are simple averages.

Resource-seeking

The second and third most important investment motives varied across the countries, although they were predominantly concentrated around the use of low-cost factors of production (including natural resources) and skilled labour. In Ukraine, the second most important motive was the availability of low-cost input factors, i.e. cheap labour, energy and raw materials. This is explained by the availability of rich natural resources along with cheap labour force and by the close proximity to the EU. The desire to use Kyrgyz skilled labour, followed by the availability of low-cost input factors were also behind the decision to invest in Kyrgyzstan. Interestingly, the second most important motive for investing in Moldova was the ability to access the new regional market (Central and Eastern European), which can be attributed to country's proximity to the 'new' EU states. This motive can be also attributed to the willingness to exploit Moldovan labour and other resources (graded as the third most important motive).

Efficiency-seeking

Access to country's research and technological expertise was assessed as the least important reason to invest in the CIS (see Figure 4), which suggests that investors do not yet seek efficiency in the CIS. This is also confirmed by the answer that the exploitation of the cost-effective production in the CIS for the purpose of exporting products to the EU was not important for the strategy of the parent companies. Moreover, the surveyed firms export on average rather small volumes of intermediates (17% of the production of firms producing intermediate goods is exported), which means that they are weakly integrated in vertical production chains.⁵

The results of the survey indicate that the predominant motive for investing in the three CIS countries has been market-seeking. The second important reason is resource-seeking. Foreign investors in the surveyed CIS firms do not seek efficiency there yet.

Major impediments

In order to check the investor's attitude towards investment climate in the countries against the conclusions of our theoretical part, we asked respondents to assess the importance of the major problems creating difficulties for doing business in the host countries. Each of the responders ranked the importance of the problem from 1 to 5 (1 – the least important, 5 – the most important).

Based on our analysis, the most urgent problems in the surveyed CIS countries are the volatility of the political environment, uncertainty of the economic situation, ambiguity of the legal system and corruption. However, the top three ones differ among countries. Political and economic instability are of particular concern for the foreign companies operating in Kyrgyzstan. The next most important obstacle is the lack of physical infrastructure. All other problems are relatively less important in the light of the three mentioned above. Ukraine and Moldova are more stable in political terms and foreign investors perceive there extensive bureaucracy, corruption and uncertainties connected to domestic legislations as the main obstacles for their businesses. This means that neither difficulties connected with establishing the Ukrainian government in late 2007, nor problems with the uncertain status of Transnistria in Moldova are important obstacles for expanding business activities by foreigners in the two European CIS countries.

High level of corruption in the CIS, which is acknowledged to be a serious deterrent to FDI inflows, is confirmed by Corruption Perception Index 2006, where Ukraine is ranked 104th and Kyrgyzstan 145th out of 163 developed and developing countries of the world (Transparency International, Global Corruption report 2007). Interestingly, the perception about corruption in Moldova, although still high, is much lower. Moldova ranked 81st on that list (Transparency International, Global Corruption report 2007).

⁵ With the exception of the Moldovan companies. Foreign subsidiaries producing intermediates in Moldova export over 50% of their production.

Table 5. Assessment of problems faced by foreign investors in the CIS

Problem	Ukraine	Moldova	Kyrgyzstan	Georgia	Total average
volatility of the political environment	3.4	3.3	4.5	2.8	3.5
uncertainty about the economic environment	3.3	3.4	4.4	2.9	3.5
ambiguity of the legal system	3.9	3.5	3.5	2.7	3.4
corruption	4.0	3.9	3.1	2.1	3.3
bureaucracy	3.9	3.9	3.1	2.0	3.2
lack of physical infrastructure	2.5	2.8	3.9	2.9	3.0
backward technology	2.4	2.9	3.1	2.4	2.7
lack of business skills	2.4	2.6	3.1	2.7	2.7
finding a suitable partner	2.5	2.9	2.3	2.8	2.6
problems in establishing clear ownership conditions	3.2	2.9	1.7	2.4	2.6

Source: survey results

Note: higher number indicates that a given impediment is more important. Numbers are simple averages.

Problems in establishing clear ownership rights came up to be relatively important obstacle faced by firms operating in Ukraine and Moldova, but not very much for those located in Georgia or Kyrgyzstan. Existing infrastructure, technologies and management skills of the local workforce do not seem to be much of a problem for foreign investors operating in Ukraine and in Moldova, however it is perceived as the biggest obstacle in Georgia. Finding a suitable partner seems not to be a problem neither in Ukraine nor in Kyrgyzstan, whereas it is a relatively important obstacle in Moldova and Georgia. Among other impediments, investors mentioned were problems with tax administration, which involves difficulties in paying taxes, VAT refund, complicated tax regulations.

Business environment of foreign firms

When analyzing industry-specific FDI determinants, we relied upon Jacobides (2006) who assumes that the similarities and dissimilarities in the use of factors of production in the vertically integrated production chain among countries shape the globalisation prospects and the effects that FDI may produce in a host country. Hence, the second part of our questionnaire was designed to reveal the impact of FDI in a recipient country. The companies were asked to estimate the extent to which their business can be divided into separate components and the degree of similarity of vertical and horizontal value-chain structures between home and recipient country, as well as give feedback on the performance of their CIS subsidiary. Also, some additional questions let us draw the conclusions on the importance of industry-level FDI determinants.

The recipients estimated the similarity of industry value-chain structure at 3.4 points (according to 1-5 scale, where 1 – not similar at all, 5 – very similar) by this indicating that the structures are somewhat similar. Country averages did not differ much, though the answers of Moldovan FDIIs suggested a higher degree of similarity. When asked to distinguish between the differences/similarities in vertical and horizontal industry structures (referring to vertical structure as the way of the systems of in-bound logistics, manufacturing, outbound logistics, organised sales), and horizontal industry structures (defined as the number of industry participants, their functions and market shares), the respondents gave similar answers. Interestingly, vertical value chains structures are more similar to home countries value chains than the horizontal ones (3.3 and 3.1 points respectively, total average across countries).

The differences between home and host country value-chain structures were not perceived as a significant impediment for business expansion in the recipient country. The total average was estimated at 2.0 points, while the results vary among countries (see Question 21 in Appendix 1). Foreign companies that established their business in Kyrgyzstan estimated the impact of different structures as insignificant (1.2 points), Ukrainian and Georgian ones as rather insignificant (2.1 and 2.0 points correspondingly), while it had some impact on Moldovan subsidiaries (2.8 points).

Interestingly, companies that have invested in Kyrgyzstan assessed the performance of local subsidiaries as very good (4.5 points). Foreign firms in Ukraine and Moldova were also perceived by their representatives as performing relatively well (Ukraine – 4.3 points and Moldova 4.1 points) while Georgian subsidiaries were rated as performing worse of all at 3.7 points.

The activity of foreign affiliates to a large extent depends on the parent company's multinational business. Firstly, 42% of the company's value chain components are supplied from the home countries, while only 17% are provided by local suppliers (see Question 15 in Appendix 1 for details). Especially large share of value chain components (about 60%) are imported by Ukrainian foreign affiliates, whereas Moldovan and Kyrgyz companies import only 21% and 39% respectively. Ukraine's reliance on imports can be explained by a big number of companies engaged in retail trade among firms which took part in the survey.

The largest part of imported value chain components are parts and technologies and know-how (42% of total), the second are materials (23.9%), components parts take about 20% each and final products account for about 14% (see Question 8 in Appendix 1). As for the open option, the majority of Ukrainian companies reported on marketing technologies brought from parent companies to be of large value. Also, in all countries financing and working capital were named as an important resource received from a parent company. Among other resources mentioned were consulting services with regard to major business processes and equipment.

Secondly, the companies were asked to comment on the success of their business depending on the performance of local and multinational partners. As it turned out, on average the success of the operations of a subsidiary depends more on the performance of international industry participants (3.4 points) than on the performance of local industry participants (3.0 points). This confirms the earlier findings about the importance of parent company and the multinational links to the subsidiaries. Unfortunately, the local environment is not sufficiently developed to offer companies products of the necessary quality for their business, so they have to maintain close links with their international partners.

Thirdly, the average number of key local suppliers among all four countries was significantly below the number of key local customers/distributors (18 and 74 respectively, total average among four countries). The last finding supports the earlier described outcome of our research on the market-oriented nature of investment in the CIS countries. While much of the resources are supplied from abroad, the final products are targeted to the internal markets, which stipulates for the significant number of local distributors and customers.

Overall, the results suggest rather pessimistic implications for the influence of technological spillovers over the productivity of domestic firms. It was shown in studies examining CEE data that the highest productivity-increasing gain for local firms takes place when foreign-owned technologically superior firms buy local supplies, teach suppliers and make them acquire new technologies. Then we may talk about positive technological spillovers arising from the activities of foreign-owned companies. However, in the case of this sample, it seems that spillovers from FDI, even if exist, are rather limited to certain firms and/or sectors of economic activity. Moldova has the most favourable suppliers to customers ratio, which suggests that the potential for spillovers may be the highest there. But even in Moldova, the average number of domestic customers of a foreign subsidiary is three times higher than the average number of local suppliers. Foreign firms in the surveyed CIS markets seem to buy supplies locally only when it is necessary, and concentrate on capturing domestic demand.

6. ECONOMETRIC ANALYSIS

In this section we will present findings from the subsequent econometric analysis we have conducted based on the survey results. In particular, we were interested to see whether there were any differences among the three different types of investors (market-seekers, resource-seekers and efficiency-seekers) with respect to the levels of their satisfaction with their CIS operations, problems they were encountering in their countries of operation, and particularities of their modes of operation.

To estimate our models we employ ordered logistic analysis (based on a maximum likelihood estimation) as we are working with the categorical data. This method is the most appropriate for this type of data as it allows obtaining consistent, efficient, and powerful estimates (see Greene, 2002; Agresti, 2002 and Allison, 1999). We use STATA 9.0 to conduct estimation.

Dependent variables

We employ a number of dependent variables in this study. Our first dependent variable is a manager's perception of the subsidiary's performance. This and all other variables in our survey were measured on a five-point Likert scale. More specifically, the question was, "Please evaluate the performance of your [the country where the subsidiary is] subsidiary". This, of course, is not a true measure of performance as such, but a satisfaction effect, which is also subject to individual biases. However, by analyzing managers' satisfaction with the performance of a subsidiary we are in a position to gauge which factors contribute to higher or lower satisfaction with performance.

The other dependent variables employed are the various problems the survey participants are encountering during their operations in the host countries. We have tried all 10 individual problems specified in the questionnaire. However, we report only six of them (the ones which yielded significant results). These variables are: 1) volatility of the political environment, 2) uncertainty of the economic environment, 3) ambiguity of the legal system, 4) corruption, 5) difficulties in finding a suitable partner, and 6) problems in establishing clear ownership conditions. With these dependent variables, we analyze how different investment motivation/orientation of a subsidiary and other firm-specific and industry-related variables affect the perceived problems of operating in the respective countries.

Independent variables

This study employs a number of independent/explanatory variables in order to explain possible differences in the perceived performance and problems of operating in a particular country. As we have already mentioned, the key independent variables employed are related to the investment motive/orientation of the subsidiary. These are the answers to the question 10 of the questionnaire 'Why did you choose to invest in [the country where the subsidiary is]?' The following five options were considered: 1) cheap input factors; 2) skilled labor; 3) local market; 4) regional market; and 5) local R&D expertise.

The two other employed independent variables are related to the similarities/differences in the industry's value chain structures between host and home countries. These factors have been shown to affect the investor's behavior to a significant extent (see Jacobides, 2006). The corresponding two variables are called 'Sector Similarity' and 'Sector Modularity', which are the answers to questions 20 and 16 of the questionnaire respectively.

The next two independent variables are linked to the subsidiary's embeddedness/

dependence on the host/home country environment a propos the links with the local/global value chain partners. The corresponding variables are called 'Local Relationships' and 'Foreign Relationships' and constitute the answers to questions 13 and 14 of the questionnaire respectively.

The remaining variables are measured on a continuous scale and relate to basic firm characteristics, e.g. turnover (annual, USD mn), years of operation, personnel, investment (initial, USD mn), market share (per cent, in a host country). Also, we add country dummy variables to control for country effects.

The results

The results of our analysis are reported in Table 6. It shows 7 specifications with the dependent variables described. The first specification (S1) analyzes the factors which influence performance of the foreign owned companies in the CIS. We find that having market-, skilled labor-, and cheap input-orientation affects the performance positively with market-orientation having the strongest impact in the absolute value. Hence, we find that market-seeking companies are performing better in our sample of the CIS countries. Also, the value chain similarity and modularity are shown to affect positively the performance of the subsidiaries.

Although the relationship between the local and foreign relationships and performance is insignificant at 10% level, it is worth noting that foreign links have a positive effect on performance, whereas local links have a negative one. It further points towards the point that there are no massive spillovers between local companies and foreign affiliates, and those which exist tend to be of detrimental value to the investors. Hence, unsurprisingly, the foreign-owned companies try to have as little involvement with local businesses as possible.

The other variables turned out to be insignificant apart from the dummy for Georgia (with a negative sign) reflecting that the companies operating in Georgia are showing lower performance than their peers in other countries.

The other 6 specifications analyze factors which affect the perceived problems of MNE's operations in the CIS countries. Differentiating among the different investment orientations, we find that the ambiguity of the legal system and problems in establishing clear ownership rights are the most important for investors who seek cheap inputs in the CIS. As legal matters are one of the key factors which determine success of resource-seeking operations, i.e. all contractual arrangement related to the use of the key resource, we find them to be of paramount importance for this type of investors.

At the same time, investors who are seeking skilled labor are most affected by the uncertainty of the economic environment. We would expect these investors producing something relatively sophisticated for the local market/exports, and since economic uncertainty amplifies all business-related risks, then this problem becomes of the highest concern to them.

Interestingly, market-seeking investors do not seem to have a specific problem to be of more importance to them than the rest. The situation is somewhat different with the investors who are trying to access the regional market: for them the problems in finding a suitable partner are of the highest significance. And finally, corruption and the uncertainty of the economic environment are the most significant problems for investors who are seeking to tap in into R&D expertise in the CIS region.

Out of the other variables, sector similarity appears to be one of the most important alleviators of problems which are encountered in the CIS by foreign investors (as all coefficients have negative signs) – hence the similarity of the value chains helps to overcome the problems investors are experiencing in the region. This is in line with the global expansion logic put

Table 6. Estimation Results

<i>Independent Variables</i>	Dependent Variables						
	<i>Perfor mance</i>	<i>Political Environm.</i>	<i>Economic Environm.</i>	<i>Legal System</i>	<i>Corruption</i>	<i>Finding a partner</i>	<i>Ownership Rights</i>
	S1	S2	S3	S4	S5	S6	S7
FDI Motives:							
Cheap factors	0.39* (0.10)	-0.11 (0.62)	-0.25 (0.27)	0.43** (0.05)	0.04 (0.85)	-0.40 (0.51)	0.47* (0.07)
Skilled labour	0.49* (0.07)	0.19 (0.45)	0.45* (0.09)	0.14 (0.58)	0.14 (0.57)	0.28 (0.28)	-0.11 (0.69)
Local Market	0.53* (0.07)	-0.5 (0.84)	0.19 (0.47)	0.09 (0.67)	0.05 (0.82)	0.28 (0.23)	-0.04 (0.87)
Regional Market	0.17 (0.327)	0.20 (0.19)	0.19 (0.47)	0.23 (0.12)	0.21 (0.15)	0.32** (0.04)	0.11 (0.51)
R&D expertise	0.09 (0.797)	0.38 (0.19)	0.35** (0.03)	0.23 (0.37)	-0.57** (0.04)	-0.07 (0.76)	0.42 (0.12)
<i>Other Variables</i>							
Local relationships	-0.23 (0.33)	-0.09 (0.23)	-0.19 (0.41)	-0.38* (0.06)	-0.20 (0.32)	0.12 (0.58)	-0.07 (0.74)
Foreign relationships	0.15 (0.48)	0.06 (0.75)	0.42** (0.05)	0.11 (0.59)	0.22 (0.28)	-0.24 (0.23)	0.14 (0.53)
Sector similarity	0.64** (0.02)	-0.28 (0.23)	-0.75*** (0.00)	-0.13 (0.55)	-0.05** (0.03)	-0.33 (0.15)	-0.47** (0.05)
Sector modularity	0.42** (0.05)	0.06 (0.38)	-0.58** (0.02)	-0.013 (0.95)	-0.32 (0.11)	0.07 (0.74)	0.23 (0.34)
Turnover	-0.01 (0.34)	0.00 (0.97)	-0.01 (0.18)	-0.02** (0.04)	-0.01 (0.56)	0.01 (0.58)	0.01* (0.07)
Years of operation	-0.01 (0.97)	-0.01 (0.72)	-0.03 (0.16)	-0.03** (0.04)	0.01 (0.57)	0.00 (0.90)	-0.01 (0.58)
Personnel	-0.00 (0.97)	0.00 (0.29)	-0.01 (0.17)	-0.01* (0.09)	0.00 (0.97)	0.00 (0.72)	-0.001 (0.31)
Investment	0.01 (0.27)	0.01 (0.62)	0.01 (0.18)	-0.01 (0.24)	-0.01 (0.91)	-0.001 (0.86)	-0.001 (0.36)
Market Share	0.01 (0.19)	-0.01 (0.79)	-0.01 (0.55)	-0.02** (0.05)	0.01 (0.39)	0.004 (0.66)	-0.004 (0.61)
D-Ukraine	0.61 (0.462)	-2.89*** (0.00)	-1.15 (0.16)	1.79** (0.02)	2.11*** (0.00)	0.69 (0.39)	4.33*** (0.00)
D-Georgia	-1.58* (0.05)	-3.98*** (0.00)	-3.59*** (0.00)	-1.76** (0.02)	-1.72** (0.02)	1.76** (0.20)	3.04*** (0.00)
D-Moldova	-1.32 (0.15)	-3.39*** (0.00)	-1.83** (0.02)	1.33* (0.08)	2.19*** (0.00)	1.58** (0.040)	3.91*** (0.00)
Pseudo R-squared	0.26	0.23	0.35	0.19	0.20	0.09	0.21
LR chi2	49.25	59.63	81.40	47.31	55.64	24.18	55.70
Number of observations	87	88	88	88	88	88	88

* p-values in parentheses

forward in Jacobides (2006). Sector modularity, on the other hand, is only helping to alleviate the uncertainty of the economic environment to investors into the CIS.

The local value chain embeddedness affects negatively the difficulties caused by the ambiguity of the legal system, whereas close links with foreign value chain partners amplify the problems caused by the uncertainty of the economic environment. As we already mentioned, significant involvement with local partners creates a number of situations where legal matters can potentially arise, which then should be resolved within highly imperfect local legal systems. As to the latter finding, it can be explained by the fact that the closer the links with the foreign partners are the more a firm relies on import/export operations which make it dependent on macroeconomic stability in the host country, in terms of the exchange rate stability, inflation, monetary policy etc.

A number of firm-level variables appeared to correlate significantly with the problems caused by the ambiguities of the legal system also. The number of years of operation in the CIS is negatively related to the difficulties caused by this ambiguity, i.e. younger companies are more severely affected by this problem. The companies which had been in the country for a few years had already developed some capabilities which help them in dealing with this ambiguity, which younger companies lack.

Similarly, the size of the company (measured by both turnover and number of employees) affects the legal ambiguity in the negative way also, i.e. the smaller the company is the more likely it is to suffer from legal problems. Again, smaller companies probably do not have enough resources to deal effectively with legal problems, whereas bigger companies have more leeway which allows them to overcome the related difficulties. The company's market share is also negatively related to legal ambiguities – we think that effect here is similar to the size effect as bigger companies typically have larger market share and vice versa.

On a contrary, the relationship between the size of the company (turnover) and problems in establishing clear ownership rights is positive. The bigger the size of the company, the larger effect these problems have on its business. It can be explained by the fact that ownership rights/corporate governance issues become more significant as the company grows larger, and given the shortcomings of the legal systems in the surveyed countries these problems are likely to amplify in significance at that stage.

The country effects prove to be one of the most significant factors affecting the various problems foreign companies are facing in the CIS. In general, Ukraine and Moldova are the countries where the analyzed problems (corruption, ambiguity of the legal system, problems in finding a suitable partner and establishing clear ownership rights) cause the largest difficulties for investors (apart from political and economic stability). At the same time, investors operating in Georgia seem to suffer less from the identified problems than their peers in other countries under analysis. The only problems which cause significant difficulties in Georgia are problems with finding a suitable partner and difficulties in establishing clear ownership rights.

7. CONCLUSIONS

This paper has been devoted to the analysis of the motives of FDI into the CIS focusing on the smaller CIS countries. It has also explored the problems which foreign investors incur in these countries. Furthermore, we analysed how different investors profiles (market-, resource- and efficiency-seeking) affected the problems they were encountering in their countries of operation, and particularities of their modes of operation.

Our analysis shows that:

- Market-seeking is a dominant motive for investors in our sample. The companies hold substantial share of the recipient country's market, with small part of their products being exported. The growing CIS markets produce high demand, which foreign investors are aiming to capture by further expanding their business. This motivation is similar to the motivation foreign investors into the CEE countries had in the early 1990s.
- The second and third most important investment motives vary across the countries, being predominantly focused on the use of low-cost factors of production (including natural resources) and

skilled labour. We expect that together with closer integration with the global economy (and particularly with the EU in the case of the European CIS countries) and the fall in overall protection, the cheap CIS labour will attract new waves of investments, similarly as it has been happening in the CEE and SEE countries. It is very important, though, that the skills of the CIS labour force could match the needs of the labour markets.

- Investors do not yet seek efficiency by producing in the CIS, which is one of the key reasons for investment in the CEE/SEE countries.
- There is a need to address the following impediments (so that they do not override possible profits from using cheap CIS labour): political instability in Kyrgyzstan, and extensive bureaucracy, corruption and uncertainties connected to domestic legislations in Moldova and Ukraine.
- Overall, the results suggest rather pessimistic implications for the influence of technological spillovers over the productivity of domestic firms. It was shown in studies examining CEE data that the highest productivity-increasing gain for local firms takes place when foreign-owned technologically superior firms buy local supplies, teach suppliers and make them acquire new technologies. Then we may talk about positive technological spillovers arising from the activities of foreign-owned companies. However, in the case of our sample, it seems that spillovers from FDI, even if exist, are rather limited to certain firms and/or sectors of economic activity. Moldova has the most favourable suppliers to customers ratio, which suggests that the potential for spillovers may be the highest there. But even in Moldova, the average number of domestic customers of a foreign subsidiary is three times higher than the average number of local suppliers. Foreign firms in the surveyed CIS markets seem to buy supplies locally only when it is necessary, and concentrate on capturing domestic demand.
- Our econometric analysis reveals that market-seeking orientation has the most positive effect on investment performance, followed by skilled labour- and cheap input orientations. Hence, serving local market is the most beneficial strategy for investors.
- The ambiguity of the legal system and problems in establishing clear ownership rights are of biggest concern for the investors seeking cheap factors of production in the CIS, whereas the uncertainty of economic environment is the most harmful for the investors seeking skilled labour. The latest problem is also the most significant for investors trying to tap in into the local R&D, hence improving macroeconomic stability should be of the primary importance to the government aiming to attract skilled labour- and R&D-seeking FDI, the types which are considered to bring the largest benefits to the host country development.
- The problems stemming from the ambiguity the legal system are also amplified if a foreign company has close links with local businesses, is of a smaller size and younger age. Hence, improving the legal system will help the foreign companies to develop their operations in the CIS countries with less trouble, and hence contribute to the host country's development much sooner.

Consequently, the policy makers could assist in attracting more and higher quality FDI into the CIS countries by working on the improvement of macroeconomic and political stability, and reducing the ambiguity of the legal system. Of particular concern is reported lack of efficiency-seeking investors in the region, as well as insufficient links of foreign owned businesses with local companies. Again, removing legal deficiencies could stimulate more active involvement of foreign companies with local businesses, as well as active policy directed on higher localisation of the value chain. The other impediment to the efficiency-seeking (R&D) investment was found to be high corruption levels – and this is the avenue where the governments can go a long way to help alleviating the problem, yet the political willingness is the key here as it will define effectiveness of any action taken in this respect.

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APPENDIX 1. DETAILED RESULTS OF THE SURVEY

Profiles						
Ukraine	Min	1st quartile	2nd quartile	3rd quartile	Max	Average
1. Years in the country	2.0	4.5	9.0	11.0	18.0	8.4
2. Annual revenue (turnover) of the subsidiary, million USD	0.03	3.1	10.5	67.7	1233.0	80.7
3. Personnel employed	7.0	38.0	136.0	272.8	3500.0	501.5
4. Total amount of your capital invested in the subsidiary, million USD	0.06	0.17	3.5	49.8	600.0	67.1
5. Market share in the country,%	0.5	15	22.0	27.0	100.0	28.8
Moldova						
1. Years in the country	2.0	7.0	9.0	12.0	134.0	17.8
2. Annual revenue (turnover) of the subsidiary, million USD	0.0091	0.3	1.8	5.2	121.1	13.8
3. Personnel employed	10.0	82.0	297.0	440.0	1653.0	369.2
4. Total amount of your capital invested in the subsidiary, million USD	0.0004	0.3	3.0	32.6	112.4	21.0
5. Market share in the country,%	0.3790	30.0	44.0	70.0	99.1	46.6
Kyrgyzstan						
1. Years in the country	2.0	4.0	8.0	10.8	15.0	7.7
2. Annual revenue (turnover) of the subsidiary, million USD	0.3	1.8	3.0	7.0	30.0	6.8
3. Personnel employed	6.0	50.0	120.0	300.0	1200.0	232.4
4. Total amount of your capital invested in the subsidiary, million USD	0.2	0.5	3.0	10.0	50.0	8.7
5. Market share in the country,%	5.0	10.0	20.0	30.0	100.0	28.67

Georgia						
1. Years in the country	1	3	4	10	17	6.2
2. Annual revenue (turnover) of the subsidiary, million USD	0.25	1.50	6.00	68.00	280	43.7
3. Personnel employed	12	35.00	120.00	302.50	1200	237.6
4. Total amount of your capital invested in the subsidiary, million USD	0.1500	7.10	20.00	66.25	160	39.9
5. Market share in the country,%	0.0	2.0	8.0	25.0	100.0	19.6

7.What percentage of the following is exported? Please indicate %.	Ukraine	Moldova	Kyrgyzstan	Georgia	Total	
- intermediate products	12.63	51.7	1.1	3.0	17.1	
- final products	10.63	58.6	28.8	23.7	30.4	
8.Which products the Ukrainian subsidiary receives from parent company? Please tick.	Ukraine	Moldova	Kyrgyzstan	Georgia	Total	% from total
- technology, know-how	17	22	26	21	86	41,95%
- materials	8	8	17	16	49	23,90%
- components parts	7	4	16	14	41	20,00%
- final products	10	7	11	1	29	14,15%
- others (please specify)						0.0%
Total	42	41	70	52	205	

9. What is the strategic role of the subsidiary in your MNE group's operations?	Ukraine	Moldova	Kyrgyzstan	Georgia	Total
Please rank from 1 to 5 (1 – unimportant, 5 – very important):					
a) supply existing products to country's and other CIS markets	4.3	3.3	5.0	3.1	3.9
b) develop new products for country's and other CIS markets	2.7	3.1	3.3	2.5	2.9
c) exploit country's cost-effective production to export products to established (e.g. European markets)	1.7	2.0	2.1	1.6	1.9

10. Why did you choose to invest in the country? Please evaluate each of the reasons presented below.	Ukraine	Moldova	Kyrgyzstan	Georgia	Total
Please rank from 1 to 5. (1 – the least important, 5 – the most important):					
a) availability of low-cost input factors (e.g. cheap labor; energy; raw materials)	2.8	3.4	3.4	3.2	3.2
b) skilled labor	2.6	3.5	3.6	3.0	3.2
c) to serve country's market	4.1	3.8	4.6	3.3	4.0
d) to achieve access to a new regional (Central and Eastern European) market	2.3	3.6	3.2	3.0	3.0
e) to access the country's research and technological expertise	1.5	2.3	1.3	1.2	1.6
f) other (please specify)					
11. What do you think are the current problems investors face in the country?					
Please rank from 1 to 5. (1 – the least important, 5 – the most important):					
a) volatility of the political environment	3.4	3.3	4.5	2.8	3.5
b) uncertainty of the economic environment	3.3	3.4	4.4	2.9	3.5
c) ambiguity of the legal system	3.9	3.5	3.5	2.7	3.4
d) corruption	4.0	3.9	3.1	2.1	3.3
e) bureaucracy	3.9	3.9	3.1	2.0	3.2
f) finding a suitable partner	2.5	2.9	2.3	2.8	2.6
g) problems in establishing clear ownership conditions	3.2	2.9	1.7	2.4	2.6
h) lack of physical infrastructure	2.5	2.8	3.9	2.9	3.0
i) backward technology	2.4	2.9	3.1	2.4	2.7

j) lack of business skills	2.4	2.6	3.1	2.7	2.7
12. Does your parent MNE company have investments in other Eastern European countries?					
Yes	19	28	13	17	77
No	11	2	17	13	43

13. What is the extent to which the success of your operations in the recipient country depend on the performance of and relationships to other local industry participants (e.g. other supply chain partners, providers, etc)?	Ukraine	Moldova	Kyrgyzstan	Georgia	Total
Please rank from 1 to 5. (1 – very small, 5 – very substantial)	3.5	3.6	2.4	2.5	3.0
14. What is the extent to which the success of your operations in the recipient country depend on the performance of and relationships to other international industry participants (e.g. other supply chain partners, providers, etc)?					
Please rank from 1 to 5. (1 – very small, 5 – very substantial)	3.6	3.4	3.8	2.6	3.4
15. What part of the value chain components or activities are NOT produced in house by your subsidiary?, %	43.4	12.0	48.5	31.0	33.7
15 a. Imported to the country from the home country (or other subsidiaries), %	61.1	21.1	38.8	46.0	41.8
15 b. Supplied by local (recipient country) companies, %	26.1	13.8	10.3	16.0	16.6
16. How easy is it to break up the activities of your sector in separate components / modules? (i.e., to what extent are there or can there be firms specializing in each part of the value chain?)					
Please rank from 1 to 5. (1 – very difficult, 5 – very easy):	2.7	3.0	3.1	2.3	2.8
17. What is the number of your local key suppliers/partners?					
Please indicate	12.4	27.9	13.2	17.5	18.2

18. What is the number of your local key customers/distributors?					
Please indicate	53.4	82.4	85.8	71.9	74.3
19. Does your company have close relationships with buyers/suppliers in your home country?					
Please rank from 1 to 5. (1 – not at all, 5 – very close):	3.5	3.9	3.5	3.6	3.6

20. How similar is the structure of your industry in your home country to the structure of the industry in the recipient country?	Ukraine	Moldova	Kyrgyzstan	Georgia	Total
Please rank from 1 to 5. (1 – not at all, 5 – greatly):	3.2	3.6	3.1	3.7	3.4
20 a. The vertical structure of the industry in my home country is the same as in the recipient country. (i.e., there are similar segments along the value chain)					
Please rank from 1 to 5. (1 – not at all, 5 – greatly):	3.3	3.2	3.2	3.5	3.3
20 b. The horizontal structure of the industry in my home country is the same as in Ukraine (i.e., the industry participants in the recipient country are like those in the home country)					
Please rank from 1 to 5. (1 – not at all, 5 – greatly):	2.9	3.2	2.8	3.5	3.1
21. To what extent did differences in the structure of the value chain or the way firms in the industry collaborate pose a problem for your expansion?					
Please rank from 1 to 5. (1 – not at all, 5 – they are a great problem):	2.1	2.8	1.2	2.0	2.0
22. (If there were some problems due to the value chain / industry structure), we anticipated the differences in the industry structure in the recipient country					
Please rank from 1 to 5. (1 – strongly agree, 5 – strongly disagree):	2.4	2.7	3.9	2.6	2.9
23. How difficult was it for you to overcome the differences in the industry structure?					
Please rank from 1 to 5. (1 – quite easy, 5 – very difficult):	2.3	2.9	1.8	2.2	2.3
24. How easy is it for your company to work in the recipient country?					

Please rank from 1 to 5. (1 – very difficult, 5 – very easy):	3.2	3.2	3.7	3.5	3.4
25. Please evaluate the performance of your subsidiary.					
Please rank from 1 to 5. (1 – very poor, 5 – very successful)	4.3	4.1	4.5	3.7	4.2

APPENDIX 2. STATISTICS ON FDI IN CIS

Table 1 FDI stock in Moldova by economic activities, 2000-2005

	2000	2001	2002	2003	2004	2005
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Agriculture	3.4%	4.9%	5.7%	5.2%	6.0%	5.9%
Manufacturing	14.5%	26.7%	26.0%	31.8%	22.3%	21.0%
Production and distribution of energy	12.8%	17.6%	10.2%	8.8%	10.6%	7.9%
Construction	1.8%	1.4%	1.2%	1.3%	1.7%	2.6%
Wholesale and retail sale	9.0%	7.9%	6.5%	6.9%	15.4%	11.6%
Transport and telecommunications	43.8%	24.3%	31.1%	24.9%	22.5%	21.3%
Financial activities	1.3%	2.4%	2.6%	1.2%	1.4%	1.4%
Real estate transactions	7.1%	7.6%	8.2%	10.6%	12.6%	16.9%
Public administration	0.7%	1.0%	1.0%	1.7%	1.6%	3.8%
Education	2.1%	2.0%	1.8%	1.6%	1.1%	1.4%
Health and social assistance	0.3%	0.1%	0.3%	0.4%	1.5%	1.0%
Other sectors	3.0%	4.1%	5.4%	5.6%	3.3%	3.9%

Source: Moldovan National Bureau of Statistics

Table 2 FDI stock in Ukraine by economic activities, 2002-2006

	2002	2003	2004	2005	2006
Total, millions of USD	4 555	5 472	6 794	9 047	16 375
Total	100%	100%	100%	100%	100%
Agriculture, hunting and forestry	2%	2%	3%	2%	2%
Fishery	0%	0%	0%	0%	0%
Industry	54%	52%	50%	43%	31%
of which food industry and processing of agricultural products	18%	16%	15%	12%	7%
Construction	3%	3%	3%	3%	2%
Wholesale and retail trade	17%	17%	17%	18%	12%
Hotels and restaurants	3%	3%	3%	3%	2%
Transport and communication	7%	7%	8%	7%	5%
Financial activity	8%	8%	7%	8%	6%
Real estate	4%	4%	6%	7%	6%
State management	0%	0%	0%	0%	0%
Education	0%	0%	0%	0%	0%
Public health protection and social help	3%	2%	2%	2%	1%
Collective, civil and private services	1%	2%	2%	2%	1%
Investment undistributed by regions*	0%	0%	0%	4%	32%

Source: State Statistics Committee of Ukraine

Note: * Data on direct investment are obtained from the National Bank of Ukraine and State Property Fund of Ukraine (on difference between market and nominal value of shares, property, etc., not published in statistical reports of selected enterprises).

Data are for the beginning of a year.