Evgenia Prokhorova
Doctoral student Department of Geography University of Joensuu

FOREIGN GREENFIELD INVESTMENT AND COMMUNITY: THROUGH MUTUAL ADAPTATION TO SUCCESS.

This paper discusses foreign direct investment as a learning process and outline some practical application of such approach for a host territory. Foreign direct investments can be classified by their motivation, duration, mode of entry, etc. This paper is dealing with greenfield investment which refers to the investment into new facilities and the establishing of new entities through entry as well as expansion (UNCTAD 2005) as distinguished from brownfiled investments (investments into already existing facilities). According to UNCTAD (2005, 10), FDI enter developing countries mainly in form of joint ventures or greenfield projects in contrast to developed countries, where merges and acquisitions are more common mode of entry.

Foreign direct investment is nowadays a topical issue and opinions about FDI and its role in territorial economic development is far from being united. Foreign direct investment is praised as a mechanism of modernisation and development by some and accused for being exploitative by others. Bradshaw (2005, 13-14) sums up theoretical assumptions on positive impact of FDI on economic restructuring as following: FDI provides an access to capital sources beyond domestic economy, transfers technology (both in form of machinery and management know-how), brings international standards of corporate governance, provides income to the state through privatisation and taxation, increases foreign trade turnover. Bradshaw (2005, 14) points out that there are not so many studies on post-socialist countries, which would offer more critical point of view on impact of FDI. One of the exceptions is a research by Smith and Pavlinek on FDI in Czech Republic and Slovakia, which argues that FDI's positive effect on economic restructuring is less significant than it was assumed and it is weakened among others by limited upgrading skills of local workforce, limited effect on local employment, and small impact on local supply chains (Smith and Pavlinek 2000, from Bradshaw 2005, 14). It lies outside the scope of this paper to discuss thoroughly long-term effects of FDI upon economic development of a host territory. It is enough to state here, that FDI is not a panacea for economic restructuring, but it is an intrinsic part of healthy market economies and it is essential to understand mechanisms behind investment process in order to maximise benefits of all parties involved.

A citation from Dyker (1999, 22) is a good starting point of the discussion - "FDI is pregnant with possibilities of various circles of networking, technological upgrading and enhancement of human competences, but there is nothing automatic about these virtuous circles. Unlearning curves are as plausible as learning curves, and some elements of networking maybe so exploitive as to kill any possibility of creative mutual interaction". A host territory may receive benefits of FDI in various forms but following Dyker knowledge exchange and learning which occurs between actors involved is one of the most important benefits of FDI. Establishing of a new enterprise through greenfield investment requires development of multiple socio-economic interactions between parent company, newly established subsidiary, local development offices, employees, etc. Those relations create micro level of investment climate (Kuznetsov 1994, 79) and may play a decisive role in implementing, functioning and future expansion of the investment project. Those relations sprung from a single investment episode become valuable resources of development both for the company and the host territory because they are channels of mutual learning.

Why are interactions so important for learning? Learning through interactions is a key mechanism behind successful development for both company and region. Cook and Morgan (2000) offer a conceptual framework, which brings together institutional change and innovation (learning) based on interactions. Their framework is elaborated on theoretical insights of evolutionary political economy and interactive model of innovation. They define innovation as an interaction between different actors in which information and feedbacks are circulated in up and downstream flows (Cook and Morgan 2000, 12-13). Learning occurs not only through interaction between different actors, it can also be gained through indirect sources such as printed media. However, some forms of knowledge is possible to be acquired only through direct contacts between actors. Cook and Morgan (2000, 16) distinguish between first-order learning (doing things better) and second-order learning (doing better things). "While first-order learning can be achieved through better use of codified (tradable) knowledge, second-order learning is more difficult for firms, not least because novelty involves a great degree of tacit knowledge, which had been defined simply but effectively by 'we can know more than we can tell' (Polanyi, 1966 from Cook and Morgan 2000, 16). Because tacit knowledge is personal and context-dependent, it is difficult if not impossible to communicate other than through personal communication in a context of shared experiences." (Cook and Morgan 2000, 16). Relations established during investment process are able to channel valuable tacit knowledge exchange between partners involved.

What kind of learning occurs through investment episode and what implications might it have for a host territory? Well-established body of literature within organisational studies deals with ways companies are learning from their experiences at a new host territory. Very and Schweiger (2001) single out two types of learning, which foreign investors have to face during investing process[76]. The first type refers to acquiring knowledge about target company (in case of acquisition) or, more broadly, about business environment at the possible host territory (both in case of acquisition and of greenfield investment). Very and Schweiger call this type *target learning process*. This learning process is the most obvious one and as a rule host regions and their development offices do not have problems with realising immediate requirements of a potential investor and responding to them. Territorial development agencies should maintain intensive dialogue with each interested investors to collect data about their specific needs. Requirements of investing companies can vary considerably and have very specific characteristics, therefore, host territories should be flexible in their work with potential investor and react fast to meet specific requirements of potential investor (Young 2005, 105).

The second type of learning refers to the fact that foreign investors draw their future plans on their past experiences. Very and Schweiger (2001) have named it *experience accumulating process*. Experience accumulating process partly determines future strategy of a company within a host region. Though a decision on further investment and

[76] Note that Very and Schweiger have constructed their model based on analysis of acquisition process but the same logic can be easily adapted to greenfield investments.

extending business activity at a host territory depends on other factors as well (such as international market trends, company's performance, corporate strategy, etc), the role of experience accumulating process should not be underestimated. It is essential for development agencies to establish and maintain long-term contacts with a company. One of the ways to keep long-term relations with investors is establishing of 'after-care team', which collects feedback of companies about their investment experiences in order to increase their satisfaction. (Young 2005, 112; Morgan 1997, 499). Moreover, small projects should not be neglected for their size and limited impact on regional economy, because they might have a good potential of growth in future.

Both learning processes discussed above are based on companies' own experiences. However, investors learn not only through own experience but also through cumulative experiences of other investing companies in particular host territory. This learning-by-others'-experience can be labelled as *experience spillover process*. Experience spillover process is of a particular significance at initiation stage of investment projects, when a company is choosing possible host territory for the location of its new unit. In other words, experience spillover process is a key element of place marketing and, thus, of future development trajectories of a territory. Foreign companies already established within a host region can be used for promotion of a territory as a favourable environment for investment. Successfully working company is a best advertisement for a region.

Paragraphs above have discussed three different ways in which companies learn during investment process and what implications those learning types have for local or regional development offices. But learning is not one-way street and development agencies can learn a lot from their work on each investment project. MNEs are carriers of international standards in business management as well as mirror of latest changes in business environment. The establishing of a subsidiary by MNEs gives a chance for a host region to learn and update its development strategy to requirements of a contemporary international business. The investment experience can be valuable source of information for local development bodies and the efficiency of this information can be increased through conscious approaching of investment episode as a process of learning. The most important result of learning occurs in sphere of investment management. Working with

MNEs, development agencies face challenge of meeting high standards of international business, direct experience, which is difficult to replace by information drawn from books. New knowledge received through implementation of investment project can be used for strengthening managing skills of staff in development agencies as well as improving regional investment and development strategy. This statement is supported by several empirical researches, such as Morgan's (1997) study of Welsh industrial economy. According to Morgan the necessity to meet requirements of foreign direct investors made regional development agency to revise its traditional regional development policy and to bring it nearer to needs of contemporary business. Renewed development strategy facilitates reinvestment and supports diversification of Welsh economy from domination of coal and steel industries into service and manufacturing based economy.

To conclude with, the ability of regional development agencies to learn and adapt flexibly to requirements of foreign investors is growing in importance all over the world. Globalisation demands MNEs to search for combination of low costs (labour costs and other) and high quality and efficiency of production (skilled labour, management, etc) (Fabry and Zeghni 2002). That has an important implication for territories competing for FDI. Strategies based on high quality of services provided for potential investors are more beneficial for regions than 'race to the bottom' strategy, which emphasises cheap labour, weak environmental or labour regulations, etc (Young 2005, 109). Thus, host territories' investment strategies should be more focused on concrete needs of each investor, and aimed at developing long-term relations with companies to facilitate reinvestment into regional economy, as well as to guarantee spillover of positive references from existing investors to potential ones.

References

1. Bradshaw, Michael J. (2005) Foreign Direct Investment and Economic Transformation in Central and Eastern Europe. In Turnock, David (ed) *Foreign Direct Investment and Regional Development in East Central Europe and the Former Soviet Union: A Collection of Essays in Memory of Professor Francis 'Frank' Carter.* Ashgate, Aldershot, pp. 3-19.
2. Cook, Philip and Kevin Morgan (2000) *The associational economy, Firms, regions and innovation*. Oxford University Press, New York.

3. Dyker, David A. (1999) Foreign Direct Investment in Transition Countries: A Global Perspective. In Dyker, David A. (ed) *Foreign Direct Investment and Technology Transfer in the Former Soviet Union*. Edward Elgar, Cheltenham, pp. 8-26.
4. Fabry, Nathalie and Sylvain Zeghni (2002) Foreign direct investment in Russia: how the investment climate matters. *Communist and Post-Communist Studies*, 35, pp.289-303.
5. Kuznetsov, Andrei (1994) *Foreign Investment in Contemporary Russia: Managing Capital Entry*. Houndmills, St.Martin's Press.
6. Morgan, Kevin (1997) The learning Region: Institutions, Innovation and Regional Renewal. Regional Studies, 31.5, pp.491-503.
7. Very, Philippe and David M. Schweiger (2001) The Acquisition Process as a Learning Process: Evidence from a Study of Critical Problems and Solutions In Domestic an Cross-Border Deals. *Journal of World Business*, 36 (1), pp.11-31.
8. UNCTAD (2005) *World Investment Report 2005: Transnational Corporations and Internationalisation of R&D*.
9. Young, Craig (2005) Place Marketing for Foreign Direct Investment in Central and Eastern Europe. In Turnock, David (ed) *Foreign Direct Investment and Regional Development in East Central Europe and the Former Soviet Union: A Collection of Essays in Memory of Professor Francis 'Frank' Carter*. Ashgate, Aldershot, pp. 103 - 121.