

THE IMPACT OF POLITICAL ENVIRONMENT ON FOREIGN DIRECT INVESTMENT DECISIONS OF MULTINATIONAL COMPANIES

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Abstract

The paper is dedicated to the political environment and its influence on the foreign direct investment decisions of multinational companies. The aim of this paper is to provide an understanding of the significance of the environmental factors in the host country, especially the political factors, on the foreign direct investment decisions of multinational companies. It pays special attention to several main political factors that should be taken into consideration by multinational companies when deciding to invest in a certain host country, such as regional economic integration, government regulations, political risks, and corruption.

The applied methodology consists of qualitative research techniques, such as analysis, comparative analyses, and syntheses. On the basis of the obtained results, the contribution of the paper is reflected in the determination of the relevant political factors that affect the investment decisions of multinational companies. These factors affect the economic activity in a certain host country as well as on the activity of multinational companies operating within its borders. Therefore, multinational companies should be aware of the importance of the host country's political environment in their foreign direct investment decision process.

Keywords: political environment, multinational companies, government regulations, political risk, corruption

Results and Discussion

The main purpose of this paper was to understand the importance of political factors' influence on the foreign direct investment decision of multinational companies. Therefore, when deciding to invest in a certain host country, multinational companies should take in consideration the influence of political factors such as regional economic integration, government regulations, political risk, and corruption.

- The regional economic blocs create new opportunities as well as challenges for multinational companies. In order to benefit from a regional integration of a group of countries, such as smaller trade restrictions, many companies invest in a certain country to be able to sell their products and services in other member countries of the same regional economic bloc. Apart from the benefits of operating within a given regional economic bloc, multinational companies are faced with certain challenges as well.
- By imposing various regulations, local governments affect the current operation of multinational companies as well as their headquarters' decision-making and control implementation. Local governments have the power to support, but also to limit the activities of multinational companies. The regulations imposed by local governments for multinational companies can be classified into three categories: 1) regulations related to the financial decisions of multinational companies, 2) regulations related to the business decisions and 3) regulations related to the human resource management decisions.
- From a multinational company's point of view, political risk is considered as any government action or politically motivated event that could adversely affect its long-term profitability or value. Correspondingly, the political risk encompasses all changes in a political environment that could negatively affect the business operations of the companies. The political risk, also, may be a result of changes in government regulations, civil unrest, war or politically motivated terrorism. The intensity of the political risk differs among the countries.
- According to the general meaning, corruption implies an abuse of the position of the authority in order to acquire personal benefit. Political corruption defined by Transparency International, on the other hand, is a manipulation of policies, institutions, and rules of procedure in the allocation of resources and financing by political decision-makers, who abuse their position to sustain the power, status, and wealth. Multinational companies are mostly engaged in corrupt activities in order to prevent the loss of a government contract or the decrease of their competitive position on the local market. However, engaging in corruption adversely affects the company and may lead to the creation of bad reputation for the company.