

"Responding to Global Crises: New Development Paths"

Inputs received

New Approaches to Investment Strategies: Using Sustainable Methods

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Abstract

Tourism represents one of the main sources of income for many developing countries and tourism related investment plays an important role in economic growth. Our study of assessing the influence of governmental policies on tourism related investment, detected that good governance indicators of the World Bank are accurate predictors of high future investments and represent increasing regulatory quality and low control of corruption. The findings suggest that in the first place, a positive investment climate is essential in attracting tourism related investment. But perhaps an even more relevant conclusion is that where a country has an anti-corruption policy and closes corruptive pathways, but fails to build-up a positive atmosphere for investments, the result in the short-term will be a decrease of foreign direct investment (FDI) flows. This may be expected to have negative consequences on the country's economy and perhaps even affect the final success of anti-corruptive efforts.

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Introduction

In the present global economy, FDI has been adopted as a method of economic growth (World Bank, 2005). Although the allocation of world FDI in tourism is rather small (10 percent) compared to the level of FDI in other economic activities, FDI has been acknowledged as an essential avenue for developing countries to build-up their tourism industry (UNCTAD, 2007). The economic contribution of the tourism industry accounts for about 10.6 percent of the world's GDP (UNCTAD, 2007). Tourism represents one of the main sources of income for many developing countries (World Tourism Organization, 2008) and for some nations, tourism contributes up to 95 percent to their GDP (World Travel and Tourism Council, 2007). Over the years, tourism has been experiencing continuous growth, becoming one of the fastest growing sectors in the world. Although there are a growing number of studies that have uncovered the contribution of tourism to a country's economy (Burchell & Listokin, 1978; Frechtling, 1994; Honey, 1999), the topic of investment in the tourism industry is very limited. This interdisciplinary research intends to contribute to addressing this; keeping in mind that FDI and especially tourism related FDI plays an important role in economic development and can be very beneficial to developing countries.

Brief Description of Data and Results

Two datasets have been used in this study: the Good Governance (GG) indicators of the World Bank (World Bank, 2009) and Tourism Gross Capital Formation (TGCF) from the World Travel and Tourism Council (WTTC, 2009). Modeling has been performed on a relatively small set of 30 countries, but of those we had 10 developed, 10 developing, and 10 emerging tourism destinations in our dataset (Rios-Morales *et al.*, 2010). The countries have been ordered in respect to the relative increase of TGCF in the period 2000-2004. The model has been built using absolute and relative values of the GG data in the period 1996-2000. The modeling has been performed by intelligent data analysis approach based on subgroup discovery (Gamberger and Lavrac, 2002). The obtained model states that a high increase of TGCF can be expected for countries with *increasing slope of the rank of regulatory quality*⁵ (> 0.12) or *low absolute rank of control of corruption* (< 47). The model is illustrated in Figure 1 by countries not used in the modeling process and for predicting changes in TGCF in the period 2004-2008 that is different from the period targeted in the modeling.

The obtained result is relevant because it demonstrates that increasing regulatory quality is the main and the first choice for attracting investments in the tourism industry. However, the model also

⁵ Regulatory quality is one of the six good governance indicators of the World Bank. Regulatory quality measures the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.

demonstrates that when stimulating regulatory quality is not present, investors are prepared to use corruptive pathways in cases when investments go to countries that have favorable investing costs and/or exceptionally high rates of return.

	Regulatory quality slope 1996-2004	Control of corruption rank in year 2002	TGCF slope 2004-2008
Venezuela	-3.45	9	0.58
Belarus	-0.23	21	0.52
Romania	2.03	45	0.47
Lithuania	1.17	64	0.36
Indonesia	-4.04	8	0.31
Croatia	2.24	63	0.21
Syria	0.31	48	0.18
New Zealand	-0.31	99	0.14
Barbados	-0.79	89	0.08

Table 1: Illustration of the prediction quality of the positive Tourism Gross Capital Formation (TGCF) changes in the period 2004-2008 (last column) based on significantly increasing regulatory quality ranking in the period 1996-2004 (second column) or low absolute control of corruption ranking in the year 2002 (third column).

Fighting Corruption by Building Positive Atmosphere for Investments

The model presented in the previous section demonstrates that investors need either a positive atmosphere for investment, which in our model is detected by increasing slope of the regulatory quality, or they are prepared to use corruptive pathways if they exist and if rewards are high enough. The model also shows that the absolute level of regulatory quality is not decisive for this process, but rather the determination of the government to create a positive atmosphere for investment which is reflected in improving regulatory quality. Although these findings are for investment in the tourism industry, they may be generalized to any investment.

Corruption has been recognized as the most relevant long-term factor that may prevent development (Mauro, 1995; Oman, 2000; Church, 2002). In spite of corruption, some countries were able to attract foreign investment (Kolstad and Villanger, 2004) suggesting that a low level of control of corruption presents an open pathway for TGCF. Our findings support these results. The recognition of this pathway in no way contradicts previous studies or the general recognition that corruption is detrimental to long term development. Specific relevance of our findings is in the integration of increasing regulatory quality with low control of corruption in the model for predicting high FDI in tourism industry. This model suggests that one of the potentially effective approaches for fighting corruption and closing the corruptive pathways, may be building a positive atmosphere for investment.

Conclusions and Recommendations

The underlying motivation for this study was to examine the influence of governmental policies on FDI. Two main conclusions can be drawn from our analysis. The first is that creating a positive investment climate is important for attracting future inward FDI. Investors will place their capital in such countries and will try not to use corruptive pathways. The second conclusion is that a country which uses positive anti-corruption efforts and closes corruptive pathways, but at the same time does not build-up a positive atmosphere for investments, will in the short-term, decrease its FDI flows. This decrease of FDI may have a negative consequence on the country's economy and perhaps even on successfully reducing corruption. For that reason, building a positive atmosphere for investments is the paramount direct and indirect approach for long-term, anti-corruption prevention and sustainable FDI.

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