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DOMESTIC INVESTMENT POTENTIAL: A NEW DIMENSION OF A NATION'S ECONOMIC POWER

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ABSTRACT

In macroeconomics textbooks and research papers, authors traditionally try to cover the role of investments in economic growth, especially through econometric modeling FDI, GDP, exports, unemployment, etc. An overwhelming majority of relevant studies have shown that investments, whether they are foreign or not, have a significant impact on the growth of GDP. Consequently, these findings are now serving as a toolkit for policymakers while conducting national investment policy. However, according to Marxist theory investment policy is merely a superstructure constructed on the base – sources of investments and investment relations. This paper aims to investigate those sources under the new category "domestic investment potential". Our findings indicate that domestic investment potential is a quantitative economic indicator that should play a role in the process of investment policymaking.

KEYWORDS: *Investment Potential, Resource-Based Approach, Investment Resources, Investment Opportunity, Investment Climate, Investment Attractiveness.*

INTRODUCTION

Investments are one of the most important determinants of a country's economic growth in both the short and long run.To examine this notion thousands of researches have been conducted all around the world. For example, research using 210-country panel data by Sarwar et al (2017) **[1]** revealed that there is a bidirectional causal relationship between domestic investments and GDP growth. A similar finding of Choi and Yi (2017) **[2]** in the example of 105 countries showed that domestic investments cause economic growth. To sum up, there are a large number of arguments to deduce that the positive causal relationship between domestic investments and GDP is peculiar to the whole developing world with rare exclusions.

We can express the same judgment regarding FDI. Empirical studies of Tiwari and Murascu (2011) **[3]** over 23 Asian countries showed that FDI has a positive impact on economic growth. Anwar and Cooray (2015) **[4],** Li and Liu (2005) **[5],** Samargandi (2015) **[6]** and others, obtained identical results. Moreover, te Velde and Xenogiani (2007) **[7]** using panel data on 11 countries found that FDI contributes to the improvement of skills in the host country. According to Feriduni(2013) **[8],** a rise in the volume of FDI leads to more urbanization, energy consumption, and economic growth. Although FDI presents a myriad of economic effects to receiving countries, its instability in terms of yearly values may create particular risks. For example, if a country receives significantly fewer FDI in a year than the previous this may negatively affect the growth of GDP in coming years.

Hypothetically, the potential amount of FDI a nation can attract within a year may be easily assessed by averaging the values observed in a particular period in the past. However, when it comes to domestic investments the task becomes more complicated due to the diversity of investors and their anticipations of investment opportunities. Domestic investors have more accurate information about the local business climate than do foreign investors (Lautier and Moreau, 2012) **[9]** and thus they send a “signal” to their foreign counterparts (Ndikumana and Verick, 2008) **[10]** that may encourage or discourage the inflow of FDI into the country. Therefore creating a domestic investor-friendly business climate is a task of high priority before governments in the light of contracting global flows of FDI.

Any decrease in FDI inflow can be compensated by an increase in domestic investments through which stable paces of economic growth may be attained. However, as any economic resource domestic investments are also scarce. A part of national wealth that can transform into investments is the main source of domestic investments. By calculating it we get 2 important inferences: the capability of domestic investment to compensate FDI shrinkage (1) and effective investment policy measures for stimulating domestic investors (2). In recent literature authors are using a new term “investment potential” to describe those 2 facets of national wealth. Given a number of approaches to define investment potential, we can indicate a common feature of them, that is all definitions include both FDI and domestic investments. In other words, investment potential refers to a maximum amount of foreign and domestic investments a nation may see within a certain period of time. As aforementioned, this feature doesn’t allow to estimate domestic investment potential separately. From this viewpoint, it is important to develop a definition that will have a methodological significance in assessing the money value of domestic investment potential.

METHODOLOGY

To define domestic investment potential we first analyze existing definitions of investment potential. Meanwhile, we will try to identify the core of each definition in order to select the most appropriate approach to define domestic investment potential. Theoretically, the selected approach should point out the way of calculating the domestic investment potential.

LITERATURE REVIEW

The concept of “investment potential” is multifaceted due to its economic nature. For this reason, authorsuse different approaches to define it. In particular, Lakhmetkina (2011) **[11]** suggests 3 types of approaches to define the investment potential:

- cost-based: the ability of the territory or economic entity to “swallow” capital;

- resource-based: the potential amount of investment resources, which is determined by the sum of opportunities and available resources;

- result-based: cumulative return on the used resources, or an assessment of economic efficiency of economic activity.

Golaydo (2008) **[12]** together with the resource- and results-based approachesusessectors of industry and ratings as a viewpoint to define investment potential:

- industrial sector-based: investment potential is equated to the development potential or level of development of the high value-adding industries;

- rating-based: investment potential is based on the structuring of investment potential, the assessment of its components, and their reunification.

Many authors define investment potential based on a single approach. The analysis shows that their definitions are consistent with one of the above-mentioned approaches. In particular, Tumusov (2000) **[13]** considers the investment potential as a sum of total investment resources, emphasizing that it can obtain the form of potential investment demand in the money market and transform into real investments. This definition refers more to a resource-based approach and provides the necessary clarity for the concept of investment resources. That is, the calculation of investment potential does not take into account the absolute volume of investment resources, but the part of this volume that can be transferred to production.

According to Katasonov (2005) **[14],** the investment potential is the sum of all resources that have emerged as a result of previous investment activities and will be used to fund future investment activities. Being a good example of the result-based approach,this definition reduces the scope of investment resources by embracing only a business profit and depreciation costs. This allows regardinginvestment potential as a synonym of the investment resources of the enterprise.

Some authors consider the investment potential as an integral part of economic independence. In particular, Beznos (2014) **[15]** describes the investment potential as the ability of a region to satisfy its needs for investment resources without attracting additional sources of financing. There is a valid reason to note that this definition also refers to the resource-based approach. It focuses on meeting the need for investment at the expense of domestic investment resources. That is if we consider the need for investment as a part of the investor's goal (for future profit), then all the internal (existing) resources needed to finance that goal can be considered as the sum of investment resources. Another peculiarity of this definition is that, when interpreted at the macro level, it means domestic investment potential.

Furthermore, many authors see investment potential as acomponent of the investment climate, the essence of which is explained by the presence of factors that stimulate investing. In particular, Asaul (2008) **[16]** emphasizes that the investment climate consists of investment potential and investment risk. In this case, the investment potential is explained by "... a set of objective economic, social, natural-geographical and other factors that encourage investment". Reasoning from the author's point of view, we can conclude that the concept of investment potential by its definition is very close to the concept of investment attractiveness.

A large number of approaches to defining the investment potential makes it necessary to bring them into a single and holistic concept. This requires an in-depth understanding of the essence of this economic category, especially its etymological and semiotic aspects.

DISCUSSION AND RESULTS

The word "potential" is derived from the Latin word "potentia" (power), which has two definitions in the dictionary (ABBYY, 2014):having or showing the capacity to develop into something in the future (1), and latent qualities or abilities that may be developed and lead to future success or usefulness (2).The word "potential" is international and is similarly expressed in many languages. To understand the accurate meaning of this word from an economic perspective, it is necessary to refer to the dictionaries of other languages.

In particular, Soglyanik (2004) definesthe concept of “potential” as a sum of monies, reserves, and other sources that can be used to achieve a certain goal when needed. A similar definition is given by Ozhegov (2008) where potential means the degree of power in a given relationship, as well as the set of tools needed for something. In addition, the Oxford Dictionary (1995) defines the word potential in a nutshell as “available resources”, while the second meaning of the word is “opportunities for use or development”. The Cambridge Dictionary (2008) also explains the word “potential” as the ability of a person or thing to develop, to achieve a goal, or to succeed. It can be concluded that in all the dictionaries reviewed, the potential is interpreted in the sense of “a set of resources or opportunities”.Consequently, in economic discussions,we would prefer to understand the word “potential” based onthe resource-based approach.

Now let’s define the words “investment” and “domestic”. It isobvious that the word “investment”as an adjective in all abovementioned dictionaries is interpreted as “related to investments”, and the word “domestic”stands for “relating to or occurring within a home or a country”. Thus we can summarize the meaning of the concept “domestic investment potential”:

- Potential– the sum of all resources and opportunities necessary to achieve a goal;

- Investment potential – the sum of all available investment resources and opportunities to achieve a particular goal;

- Domestic investment potential – the sum of investment resources and opportunities available in the country to achieve a particular goal.

This way we have developed the “mechanical” meaning of domestic investment potential. However, to give it an economic character, we have to take into account the definitions of investment potential given by above mentions authors. At the same time, it should be noted that in those definitions, the investment potential has not been studied in terms of domestic and foreign (external) types.

To understand the true economic meaning of the domestic investment potential, it is necessary to identify the components of investment resources. In this regard, authors usuallyuse financial and value-based approaches to detail the structure of investment resources. According to the financial approach, investment resources are all financial assets involved in funding investment projects. Yuzvovichet al. (2016) suggest that investment resources include:

- Own funds: net profit, depreciation reserves;

- Funds raised: funds of other investors, insurance coverage, funds of partners, budget allocations, initial public offering (IPO);

- Loans: loans, loans from commercial banks, tax credits, leasing, forfeiting, franchising, project financing.

According to this approach, investment resources have become equivalent to the category of sources of investment financing. The investment resources indicated in this approach can also be perceived as a synonym of a company’s investment resources. This is because the fact that they are divided into groups such as own, raised, and borrowed funds means that the issue is being considered at the level of an enterprise. Thus we can conclude that this approach is only suitable for use in microeconomic research.

In turn, the value-based approach treats investment resources to be all values that can be included in investment projects. Some authors define investment resources more precisely by stating them as“all types of material and intellectual property”, “all types of real and financial assets”, “aggregate of material, labor, and financial resources". For example, Lakhmetkina (2011) emphasizes the following as investment resources:cash;land areas;buildings, constructions, and utilities for them;equipment (installed and not installed);vehicles;subsoil and minerals;forest funds and water resources;patents, ownership of industrial designs;new technologies;trademarks;certificates, etc.

Article 7 of the Law of the Republic of Uzbekistan “On Investments and Investment Activity” (2019)similarly defines investment resources. According to the law, investment resources include:

- cash (including foreign currency) and other financial resources, including loans, shares, stocks, and other securities;

- movables and immovables (buildings, constructions, equipment, machinery, and other valuables) and the rights to them;

- objects of intellectual property;

- the right to own and use land plots and other natural resources, as well as other property rights arising from property rights.

We canhence conclude that the value-based approach provides an opportunity to look at investment resources from the perspective of the region and the country, and is fully suitable for macroeconomic analysis.

Defining domestic investment potential is first of all a matter of methodology. Therefore, it is important to use this concept in its true meaning. At presentauthors and politicians often use investment potential as a substitute forthe concepts “investment climate”, “investment opportunities”, and “investment attractiveness”. As a result, researchers are facing the confusion of terms caused by the problem when two economists say the same words but meaning differently. Therefore, another key task should be to establish semantic borders between those similar concepts.

According to Alkhasov (2015), the investment climate is a set of financial, economic, social, political, legal, and cultural conditions in the region, and the level of potential risks arising from the inflow of capital.Vahabov et al. (2010) **[17]** describe investment climate as a set of economic, political, legal, and social factors that predetermine the level of risk of foreign capital investment and the possibility of their effective use in the country. The author emphasizes the indicators of investment climate including national legislation, economic conditions (crisis, growth, stagnation), customs regime, monetary policy, economic growth, inflation, exchange rate stability, and indebtedness.

From the above definitions, we can conclude that the investment climate is a macroeconomic conceptthat is based on two factors: risk and return on investment. The direction in which the factors change is determined by the economic, social, political, legal, and other conditions in the region.The category of the investment climate is often substituted for the concept of investment attractiveness as well. However, this is not the case. To explain the difference between these concepts, we use a unique metaphor used by Litvinova(2014) [**18].** According to the author, investment attractiveness and investment climate can be compared to the weather and climate in natural geography. In this case, the weather is a "snapshot" of the climate, and the climate is the statistical ensemble of the geographical area that consists of the average values of the weather for a long time.

Bozorov (2018) **[19]** argues that the investment climate is an objective reality, which has the property of accurate assessment. It is subjective and can be perceived differently by each investor. Tchiong (2005)indicates investment legislation, the stability of the banking system, the provision of tax benefits, protection of investors' rights, and openness of information as main conditions for investment attractiveness.

Based on the results of terminological analysis, we found that authors use the concept of investment attractiveness in two ways: the investment attractiveness of the national economy (at the macroeconomic level) and the investment attractiveness of the enterprise (at the microeconomic level). The definitions given by the above-mentioned authors reflect macro-investment attractiveness, while Podshivalenko(2010), Kreinina (2005), Thang (2009) studied the investment attractiveness of an enterprise or a particular project.

Being most often interchangeably used with investment potential,investment opportunitiesaremainly considered not as a characteristic of aregion, but as an aspect of an enterprise. Also, this economic category is approached differently in different parts of the world. For example, Kallapur (2001) describes it as a set of opportunities to invest in projects with positive net present value.A broader explanation by Dvoretskaya (2007) **[20]** defines investment opportunities as a set of alternative projects for the firm to create new products or to expand current production.According to the US Electronic Code of Federal Regulations, an investment opportunity means "anything, tangible or intangible, that is offered, offered for sale, sold, or traded based wholly or in part on representations, either express or implied, about past, present, or future income, profit, or appreciation.

These definitions of the investment opportunities can be generalized as follows: an investment opportunity is a set of projects in which a business entity can allocate investment resources under favorable conditions. Applying this concept to all subjects of the economy helps to evaluate total investment opportunities within a country. Therefore, investment opportunities at the macro-level are a set of all real and financial objects that can be invested by economic entities within a certain area.

The following table clearly shows the difference between chosen concepts at both micro- and macro-level:

Semantic delimitation of economic categories

Concept	**Meaning**	
	At micro level	**At macro level**
Investment climate	-	A set of economic, social, political, legal, and other conditions that affect the risk and profitability of an investment.
Investment attractiveness	An indicator of the economic efficiency of investing in a production facility or financial instruments.	The state of the investment climate at a certain time.
Investment opportunities	A set of projects in which a business entity can allocate investment resources under favorable conditions.	A set of all real and financial objects that can be invested by economic entities in a certain area.

Investment potential	The ability of the business entity to direct its investment resources to realize its investment opportunities.	The sum of all investment resources needed to realize the existing investment opportunities in the region.

Our studies have shown that investment potential is closely linked to investment opportunities, regardless of whether they are considered at the micro- or micro level. That is, when investment opportunities are not identified in a region or at the enterprise level, the existing investment resources remain stagnant. In addition, a favorable investment climate, ie high investment attractiveness, is a prerequisite for the full use of the investment potential.

It should be noted that the concept of domestic investment potential has not yet become the subject of in-depth research in economics. Therefore, to unify all approaches in a single one we suggest defining the domestic investment potential asa set of investment resources needed to fund the existing investment opportunities in the country without the use of foreign sources.

CONCLUSION

There are only a few nations that could build a strong and advanced economy from the bottom through the FDI development convention. Most emerging economies are remaining behind the industrial revolution happening in high-income countries. The lessons from history tell that this will lead to harsher inequality and disparity among nations causing more poverty, migration, and instability. To break the status quo in the way to the development emerging economies have to deal with the dilemma of capital deficiency. That is, to build up a high-value adding economy they need massive capital resources; meanwhile, without an advanced economy, it seems quite difficult to raise enough funds for strategic investments. At present most developing countries see FDI and foreign debt as a solution to this dilemma. However, recent literature has proven that FDI flows to the markets where domestic firms operate in best conditions seeing high returns on investments. Moreover, in most cases, the effectiveness of long-term foreign loans tends to be lower than expected because of factors such as centralized usage of funds, corruption, low skills. Thus to achieve the goal of sustainable economic growth, relying on domestic investments may serve as a “win-win” strategy for both the central government and private sector, where FDI and foreign loans play the role of supplementary instruments of funding. Designing an investment policy oriented towards domestic investors requires, first of all, the evaluation of the domestic investment potential. This makes it possible to diagnose where resources are deployed fully and where they are ineffective or stagnant.

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