



# **Examining the Political Economy of the Firm: The Dynamics of State Aggression in Georgian-Russian Trade, 1996-2014**

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# Research Problem: Firms at times export to national adversaries

- China-Taiwan Economic Integration (Lee, 2014)
  - Russia-Ukraine Trade (*Forbes*, 2015)
  - Japan-China Trade (*Time*, 2013)

But what about the “public good” of international stability (e.g, Kindleberger, 1986)?  
Firms care about this, no?



**Research Question:** How does state aggression influence a firm’s export decision?

# Theoretical Paradigms

## Hegemonic Stability Theory

- Iteration 1: Trade policy outcomes explained.
- Iteration 2: Peace → Stability → Certainty → Ability to do business → **Int'l trade** (Smith, Gilpin, Nye, Keohane, Kindleberger et al)
- **Missing: Firm-level analysis**

## International Trade Theory

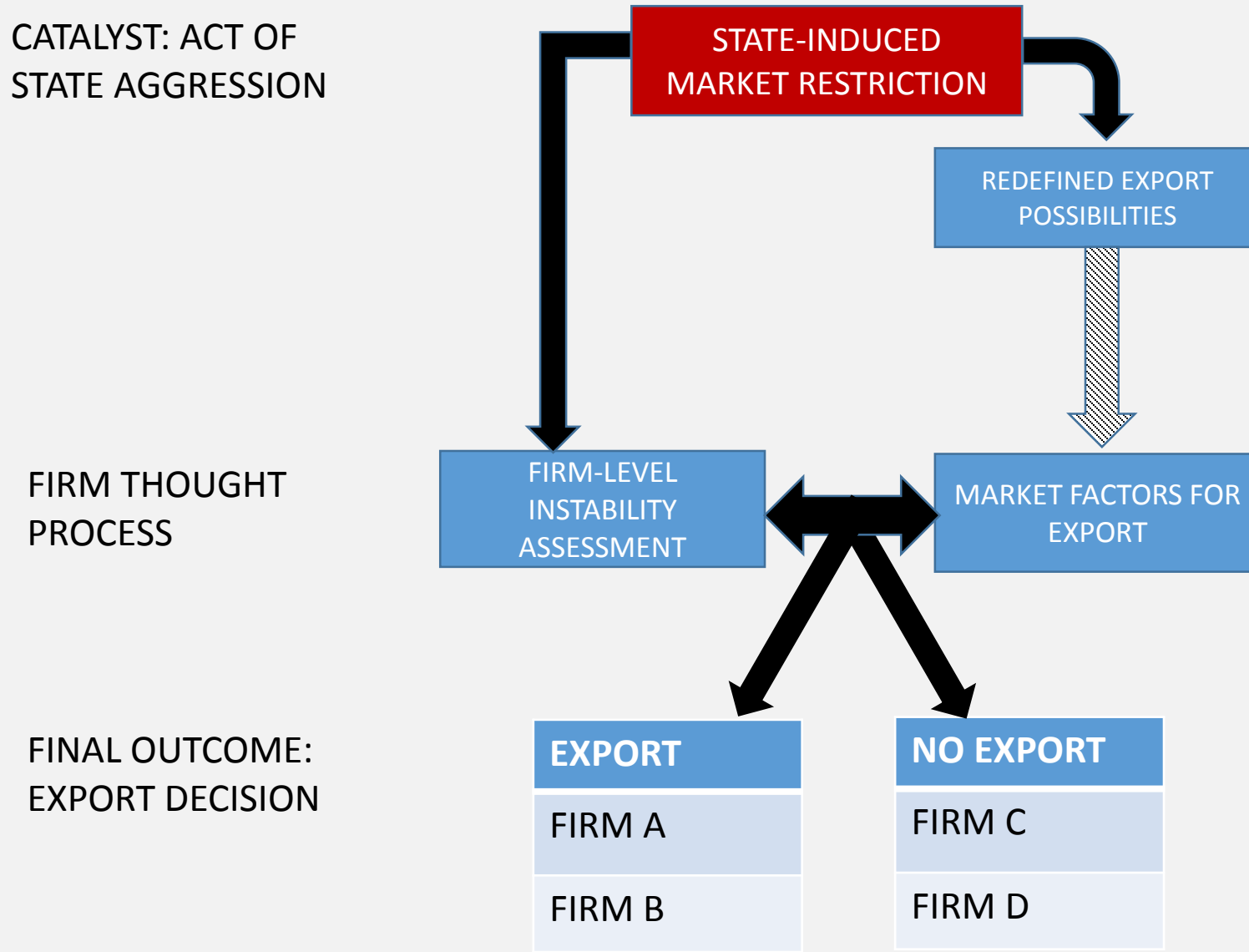
- Macro-level: Gravitationalism
  - Trade based on proximity and distance
  - Additional factors such as colonial ties matter
- Micro-level: Theory of the Firm
  - Productivity heterogeneities
- **Missing: *Political* heterogeneities among firms**

## Risk-Aversion Literature

- Behavioral Economics
  - Systematic market irrationalities
  - Analysis of heuristics, e.g., overreaction, **risk-aversion**
- Application of behavioral principles to economics at level of market actors
- **Missing: International trade theory**

# A Dynamic Approach: Constructing the International Political Economy of the Firm

FIGURE 5.2: THE FLUID DYNAMIC OF EXPORT DECISION PROCESSES AS A RESPONSE TO STATE AGGRESSION



# Research Design: Case Selection, Methods and Data Overview

## Case Justification

- Processes & Mechanisms of export behavior
- Selection: Georgian exports to Russia, 1996-2014
  - “Good” case
  - Data-rich
  - State aggression presence
  - Embargo on agricultural goods, 2006-2012

## Mixed Methods Design

- Critical Juncture analysis of the embargo
  - Process-tracing of firm decision-making
- Economic analysis of Georgian trade flow pattern changes as result of embargo

## Data

- Qualitative:
  - Interviews with Seven Georgian Firms
  - Interviews conducted Summer 2015 in Tbilisi, Georgia & over email January 2016
  - Limitation: Sample size
- Quantitative:
  - Georgian export flows to Russia and other Post-Soviet countries
  - Source: UN Comtrade Database ([comtrade.un.org](http://comtrade.un.org))

Figure 1.3 Research Question Breakdown and Chapter Divisions

Research Question:

**How does state aggression affect firm export decisions?**

Sub-questions:

**Through what process do firms change their export practice in response to state aggression (e.g., in response to an embargo)?**

**How do firms factor political instability and the resulting risk into their export decisions in response to state aggression?**

Chapter and Method addressing sub-question:

**Chapter 4, Differences-in-Differences Quantitative Study**

**Chapter 5, Process-Tracing Analysis of Firm Interviews**

Explanatory factors:

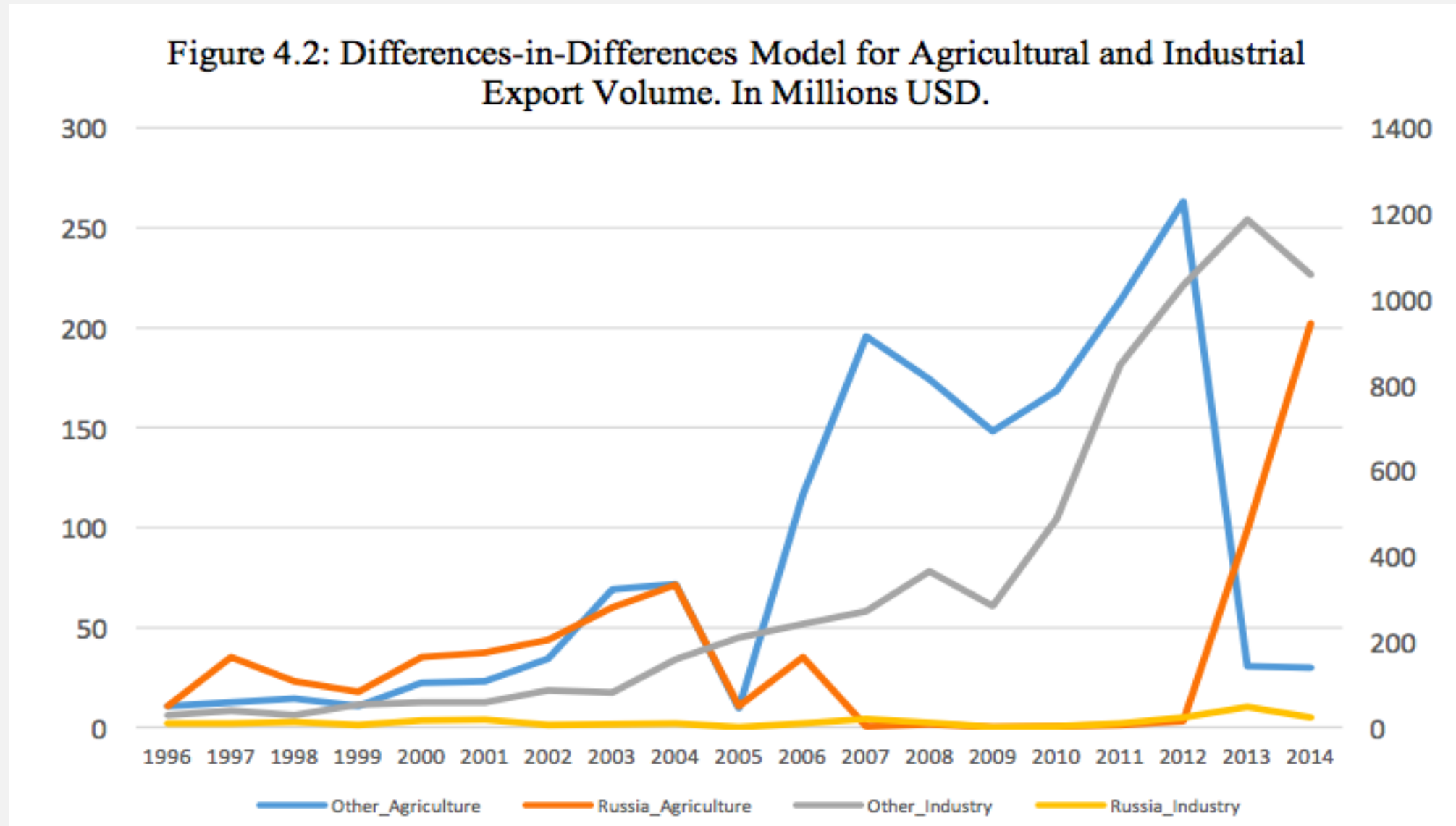
Factor x  
Factor y

Process A  
Process B

**EFFECT OF STATE AGGRESSION ON EXPORT DECISIONS**

# Results: Differences-in-Differences Analysis I: Treatment Basis Confirmation

- “Substitution” effect?
- Potential Drivers of substitution:
  - Business networks
  - Product familiarity in non-Russia countries
  - Post-Soviet connections



Source: Data from UN Comtrade Database

# Results: Differences-in-Differences Analysis II, Regression Results

Export Market	Substitution Coefficient ( $\theta/\lambda$ )	Sector Coefficient ( $\psi$ ) (in millions)	Constant ( $\kappa$ ) (in millions)
Ukraine	-0.81** (0.36)	50.7*** (16.9)	19.5* (10.6)
Moldova	-0.05* (.03)	3.22** (1.34)	0.98 (0.88)
Belarus	-0.1 (0.06)	8.65*** (2.99)	1.78 (1.89)
Estonia	-0.01* (0.004)	0.49** (0.19)	0.14 (0.14)
Latvia	-0.025* (0.01)	1.89*** (0.63)	0.69 (0.42)
Lithuania	-0.05 (0.04)	2.53 (1.89)	3.06** (1.21)
All of the Above Aggregated	-1.04* (0.56)	37* (22.7)	56.6 (29.6)

\*\*\*Significant at the 1 percent level.

\*\*Significant at the 5 percent level.

\*Significant at the 10 percent level.

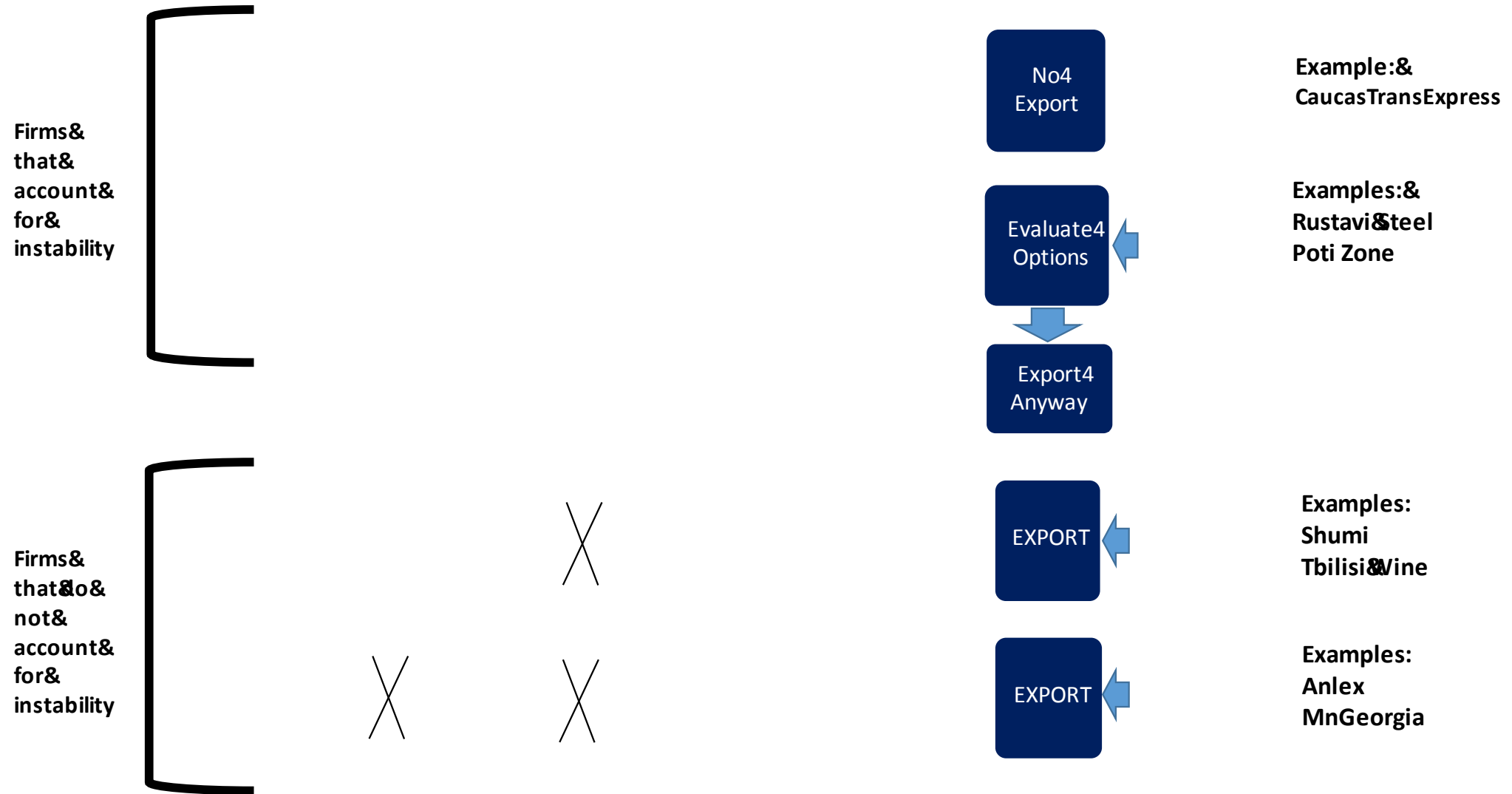


# Results: Firm Interview Decision-Making Matrix

Firm Name	Industry / Background	Market Factors For Export	Outlook on Russian Market	Non-Russian Export Markets	Embargo Experience	Outlook on Risk	Russia Export?
CaucasTransExpress	Transportation	Macroeconomics; contact relationships	—————	Rest of Former Soviet Union	no direct embargo exposure	Category I Risk-Type	NO
Rustavi Steel	Heavy metals	Good networking, strength of contacts	positive outlook	Azerbaijan, China, Ukraine, Turkey, etc.	no direct exposure	Category II Risk-Type	YES
Poti Free Industrial Zone	Logistics	Brand, scale	mixed outlook	Armenia, Azerbaijan, Central Asia etc.	direct exposure	Category II Risk-Type	YES
Shumi Wine Company	Agriculture / wine	Brand	positive outlook	Ukraine, Moldova, Japan, etc.	direct exposure	Category III Risk-Type	YES
Tbilisi Wine Cellar	Agriculture / Wine	Brand familiarity, volume	positive outlook	Ukraine, Belarus, Kazakhstan, etc.	partial exposure	Category III Risk-Type	YES
Anlex Logistics	Logistics	Network strength	Positive outlook	Armenia, Azerbaijan	no direct exposure	Category IV Risk-Type	NO
MnGeorgia	Chemical processing	Close business ties	Positive outlook	Hungary, Germany,	no direct exposure	Category IV Risk-Type	YES

# Results: Firm Interview Categorizations

Figure 5.1. The Four Risk Types of Export Decision Making Processes



# Implications

- Theoretical Significance
  - Market circumstances, personal outlook drive export decisions in consideration of state aggression
  - Nuance added to our theories of stability
- Methodological Contributions
  - Mixed methods, quantitative economics + process-tracing
  - Observation of fluid *dynamic* processes for firm decision-making
  - Further research within economics using mixed methods

**“Trade along with war has been central to the evolution of international relations.”**

**–Robert Gilpin**

