

Competitive Advantages of the Economy of Bosnia and Herzegovina as Precondition for Attracting Foreign Direct Investments

Vitomir Starčević

University of East Sarajevo, Faculty of Business and Economics, Bijeljina, Republic of Srpska

Slobodan Subotić

University of East Sarajevo, Faculty of Traffic and Transport, Dobo, Republic of Srpska

Abstract

Implementation of economic activities in the world market is one of the key elements of every country's development. In order to be present in the world market it is necessary to develop competitive abilities of particular economic subjects, branches of economy and national economy in general. The globalization process generated the period of global economic competition which requires the difference between micro and macro competitiveness to be made. Competitiveness has become a dominant economic topic of every country, particularly of those in transition. It is the main factor in attracting FDI, growing export and GDP. Foreign direct investments depend on the quality of macroeconomic, business and legal environment, whereas export and GDP growth can be achieved by increasing demand for domestic products. The level of BiH competitiveness is determined by the comparative analysis of the global competitive position of the Western Balkan countries. Comparing the economic competitive position of Bosnia and Herzegovina and that of the Western Balkans, we tend to determine to what extent such competitiveness is applicable for attracting FDI, while simultaneously taking macroeconomic, business and legal environment into account with the analysis, as highly significant factors.

Keywords

Competitiveness, global competitiveness, economy of Bosnia and Herzegovina, gross domestic product, foreign direct investments.

Introduction

Competition acts as the main regulator of the market. It represents a contest or rivalry for the purpose of achieving the best results. It contributes to innovation, better business performance and overall economic growth. However, in case the competitiveness in the labour market is scarce, it directly affects the national economy in an adverse manner. This usually leads to protectionism, non-transparent government subsidies and barriers to entering the world market. Therefore, boosting productivity and overall competitiveness must be the leading principle in implementing economic policies of any country.

Competitiveness is the ability of a country to ensure a sustainable growth of productivity, employment and quality of life in the conditions of globalization. Education, business environment, quality of business sector, infrastructure, and environment represent integral parts of foundations of competitiveness. These elements enable sustainable growth through productivity growth, export, investment efficiency and cost effectiveness (Vuković, 2007, p. 6). Macro competitiveness refers to a nation state's ability to produce, distribute and service goods or services in the international economy in competition with goods and services produced in other countries, and to do so

in a way that earns a rising standard of living. The foundations of competitiveness are formed in such a way that a country benefits from an increased export which compensates for the import of goods and services while simultaneously maintaining and expanding domestic real income, which enables the country to meet the test of competition (Porter, 1990, p. 23). Microeconomic competitiveness or market success of a company is of crucial importance for achieving national competitiveness. Therefore, the central question of the competitiveness of an enterprise is its position in relation to the profitability of an industry. This means that the favourable position of the company allows above-average industrial profits in the long run.

Competitiveness of a country is influenced by many direct and indirect factors. (Kitson, Martin & Tyler, 2004) However, the most important aspect with respect to the competitiveness of a country is the competitiveness of its enterprises as the bearers of economic development. Therefore, the enterprises are commonly placed in the foreground compared to many other indicators that characterize macroeconomics. Certainly, the macro-economic, business and legal environment should be neglected by no means, considering their effect onto the competitiveness of any economic sector.

1. Competitive position of Bosnia and Herzegovina (economy) compared to other countries in the region

Exploiting Bosnia and Herzegovina's own resources was not sufficient for successful introduction and competitiveness in the international market at the very beginning and during the transition process, which was largely the case with the remaining countries of the Western Balkans as well. The economies of the Western Balkans were struck by an internal economic crisis stemming from several factors, such as economic transformations implemented in the above countries, macroeconomic instability, poor economic management by their governments, but also due to political reasons, such as wars, sanctions and the like. Numerous sectors of the economy failed to survive due to altered conditions in the world market. Some successful sectors have been privatized, but not in a way that would increase their efficiency. This caused major changes in the structure of foreign trade flows of the Western Balkan Countries.

One of the indicators of non-competitiveness

of the Western Balkan Countries is *unfavourable quantitative ratio of exports of goods and services to GDP*. This ratio was significantly increased in all the Western Balkan Countries from the period of mid-last decade of the XX century to 2008. Based on the fact that the Western Balkans received a vast amount of foreign capital through privatization, new loans, current transfers and foreign direct investment (*greenfield, brownfield and portfolio*), it was expected that these countries would achieve high GDP growth rates. That is, that the economic growth of the Western Balkan Countries would export-oriented and would therefore generate a very dynamic growth of export coefficients in each of them, particularly in the smallest countries (Montenegro, Albania and Macedonia).

The real sector of the Western Balkan countries' economy is characterised by very low exports, either in absolute terms or in relation to the population, with the numbers lower than other countries undergoing transition. In fact, unlike many smaller countries in transition that have accomplished very high growth in export coefficients (from 60 to 70 percent), this is not the case in the Western Balkans. To support such statement regarding the low coefficients of the Western Balkan countries, the following data indicate that, for example, Slovakia increased its export ratio from 5% in 1995 to 83% in 2012, Hungary from 45% to 81%, the Czech Republic from 51% to 77%, and Slovenia from 50% to 70% in the same time period. (Olsen, 2013)

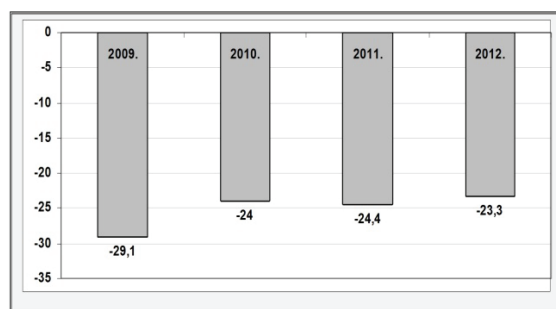


Chart 1 Trade balance of West Balkan Countries (% GDP)
Source: The World Bank, 2013a. p. 9

According to the data presented in Chart 1, based on research by the World Bank, it is evident that the Western Balkan countries recorded a negative trade balance in the observed four-year period. The negative trade balance of these countries was reduced in 2010 by 5.1% compared to the year 2009, only to be increased by 0.4% in 2011. In 2012, the Western Balkan Countries

managed to reduce the negative trade balance by 0.9%. The reason for such trends should be sought in a reduced demand in the European Union for goods from the Western Balkans, especially in 2009, which was then continued in 2010 and 2011. According to the research made by the World Bank, a sharp decline in export was registered in Serbia, Bosnia and Herzegovina and Montenegro, while their import continued to increase moderately.

Foreign trade deficit is one of the major problems of *Bosnia and Herzegovina's* economy, with the exception of high unemployment rate and low level of GDP per capita. Such high foreign trade deficit is a result of the weak competitiveness in the international market and high import-export dependence. The cause of such scarce export from Bosnia and Herzegovina can be seen in the lack of conformity of products and standards with applicable international standards, lack of export support funds and aggravated export procedures. The export problem lies not only with its low level, but is equally caused due to its poor structure. In other words, export includes raw materials and semi-products whose prices keep dropping at the world market, thus taking an increasingly smaller share of total world exports. Therefore, it is necessary to instigate change in the export structure, primarily by investing in technology and education, consequently enabling prerequisites for attracting foreign direct investment.

Table 1 Foreign trade indicators of BiH in the period 2008-2012. (in billion BAM)

Parameter	2008	2009	2010	2011	2012
Export of goods	6,711,690	5,530,377	7,095,505	8,222,112	7,857,962
Change in export	13.1%	-17.65	28.3%	15.9%	-4.45
Import of goods	16,286,056	12,348,466	13,616,204	15,525,428	15,252,942
Change in import	17.2%	-14.2%	10.3%	14.0%	-1.8%
Trade balance (I-E)	-9,574,366	-6,818,089	-6,520,699	-7,303,316	-7,394,980
Trade balance change	20.3%	-28.8%	-4.4%	12.0%	1.3%
Total trade exchange. (E+I)	22,997,746	17,878,843	20,711,709	23,747,540	23,110,904
Change in total trade exchange.	15.9%	-22.35	15.8%	14.7%	-2.7%
Coverage Import/Export	41.2%	44.8%	52.1%	53.0%	51.5%

Source: Bosna i Hercegovina, Vijeće Ministara, Direkcija za ekonomsko planiranje, 2013. p. 41.

Table 1 compares the foreign trade indicators of Bosnia and Herzegovina in the period from 2008 to 2012. Exports accomplished in 2012 from BiH amounted to 7.857 billion BAM, which is

4.4% less than the situation from the year 2011, in which the export of Bosnia and Herzegovina reached 8.222 billion BAM. Level of export was also lower by 17.6% in 2009 compared to 2008, while an increase in export of 28.3% was registered in 2010 when compared to the year before. The highest level of import was recorded in 2008, amounting to 16.286 billion BAM, which dropped dramatically by 24.2% in the following year, being only 12.348 billion BAM. In the coming years a continual growth in import was registered, so that it totalled to 15.252 billion BAM in 2012. If we observe the export-import ratio, it can be stated that the best results were made in 2011, amounting to 53%, although such percentage was considered as very unfavourable for the economy and the current account. The lowest ratio of import to export was recorded in 2008, being only 41.2%, while in 2012 this ratio increased to 51.5%, a decrease of 1.5% compared to the year 2011.

Albania is the only country in the Western Balkans which, statistically speaking, accomplished a modest economic growth throughout the previous period, mainly due to its extreme poverty and its very low statistical base in terms of GDP level. Unlike Albania, other Western Balkan countries had a level of GDP in 2012, equal or below the level of the year 1989. According to the Transition Report from 2012, Albania had about 72% higher level of GDP than in 1989, while Croatia and Former Yugoslav Republic of Macedonia (FYROM) recorded approximately the same level of GDP as 23 years earlier. The three Western Balkan countries: Serbia, Bosnia and Herzegovina and Montenegro had a considerably lower level of GDP in 2012 compared to the year 1989. Thus, Montenegro's GDP was 14% lower in 2012 than 23 years ago, Bosnia and Herzegovina's GDP was 15% lower than the one in 1989, while Serbia's GDP was 30% lower in 2012, than in 1989. At the same time, some countries in transition, such as the Baltic states (Latvia, Estonia and Lithuania), Poland, the Czech Republic, and Slovakia recorded much higher levels of GDP in 2012 than they have in 1989. Some countries, which were considered as underdeveloped 25 years ago, such as Turkey and, in particular, China, managed to achieve an incomparably higher GDP growth within the same period (Olsen, 2013). Assessing the competitiveness of the Western Balkan Countries and taking into account the foregoing, it can be easily concluded that their economies are largely uncompetitive and as such

can hardly compete with other countries in transition.

The *World Economic Forum (WEF)* defines Competitiveness as *the set of institutions, policies and factors that determine the level of productivity of a country*. Indicator of the competitiveness level is called **Global Competitiveness Index (GCI)** and refers to averaging of multiple macroeconomic and microeconomic components. Statistical factors of competitiveness, which are included in the ranking are grouped into twelve pillars, reflecting various aspects of complex economic reality. The twelve pillars of competitiveness are grouped into three subindexes, which are the key to different methods of economic management, namely: (1) basic factor of a driven economy, (2) efficiency of a driven economy, and (3) innovation of a driven economy. Rating the global competitiveness of the Western Balkan Countries is presented in the following table:

Table 2 Overview of the Global Competitiveness Index (GCI) of Western Balkan Countries for the period 2010-2013

Country	2010		2011		2012		2013	
	133	index	139	index	144	index	148	index
Albania	88	3.9	78	4.1	89	3.9	95	3.8
Bosnia and Herzegovina	102	3.7	100	3.8	88	3.9	87	4.0
Montenegro	49	4.4	60	4.3	72	4.1	67	4.2
Macedonia	79	4.0	79	4.1	80	4.0	73	4.1
Serbia	96	3.8	95	3.9	95	3.9	101	3.7
Croatia	77	4.0	76	4.1	81	4.0	75	4.1

Source: World Economic Forum, 2009, 2010, 2011, 2012

Based on the values of Competitiveness Index presented in Table 2, it can be noted that some of the Western Balkan Countries have managed to record growth, while others recorded a drop in its value throughout the observed three-year period. Therefore, **Bosnia and Herzegovina** recorded permanent growth of Competitiveness Index from 2010 to 2013, through which it reached the value of (4.0), with the country being ranked as 87 out of 148 countries on the research list. Serbia recorded a decline in the Competitiveness Index in 2013 compared to 2012, dropping from 3.9 to (3.7) as well as recording the drop in ranking from 95 to 101 position. Albania registered a drop of Competitiveness Index in 2013, as well as a decrease in position on the table by 6 places. Croatia, Macedonia and Montenegro registered the growth of their Competitiveness Indexes in 2013, implying a better ranking out of 148 countries.

Table 3 The World Bank's Doing Business 2013 (ranked 185 countries)

COUNTRY	Albania	Serbia	BiH	Croatia	FYROM	Montenegro
Doing business rank	85	86	126	80	23	51
Starting a business	62	42	162	67	5	58
Dealing with construction permits	185	179	163	143	65	176
Getting electricity	154	76	158	56	101	69
Registering property	121	41	93	102	50	117
Getting credit	23	40	70	48	23	4
Protecting investors	17	82	100	133	19	32
Paying taxes	160	149	128	32	24	81
Trading across borders	79	74	103	100	76	42
Enforcing contracts	85	103	120	48	59	135
Resolving insolvency	66	103	83	94	60	44

Source: The World Bank, 2013b

The World Bank's *Doing Business 2013*, presented in Table 3 shows that **Bosnia and Herzegovina** is placed on 126 of 185 ranked countries in the world, thus occupying the worst position of all the other Western Balkan Countries. Among the countries of the region, FYROM is the best ranked one, being at the 23rd position, followed by Montenegro on 51st position. Croatia is located at 80th position, while Albania is just a single position above Serbia, which is located at 86 place of world ranking list. Major difference with respect to **Bosnia and Herzegovina's** ranking when compared to other Western Balkan Countries can be noted by comparing some indicators used to define Doing Business rank. For example, it takes 162 days to start a business in **Bosnia and Herzegovina**, while the same activity in Macedonia takes only 23 days, or 86 days in Serbia. To obtain cross-border trade permission it takes about 120 days in **Bosnia and Herzegovina**, while the same procedure in Croatia lasts only 48 days or 103 days in Serbia. The procedure for getting a credit in Bosnia and Herzegovina usually lasts for 70 days, while the same activity in Montenegro takes only 4 days, 23 days in Macedonia and Albania, 40 days in Serbia, and in Croatia 48 days are required for the same procedure.

2. Impact of competitiveness of Bosnia and Herzegovina to attracting FDI

The complexity of business operation in terms of globalization and internationalization emphasizes

the issue of the problem of foreign direct investment as one of the current issues of international economic scene. The above issues have long been the subject of various observations and criticism. However, governments of many countries, particularly of developing countries and those undergoing transition, have adopted the position by which foreign direct investment is a key prerequisite for economic development of any country. Even more so as foreign direct investment, in addition to the transfer of capital enable the transfer of technology, managerial skills, and provide opportunities for new jobs, education of staff, etc.

Bearing in mind that most investors come from developed countries (USA, Japan, Germany, France and others) the overview of the key factors that determine their decision to invest in a particular country or region appears as quite interesting. The pursuit of transnational companies from developed countries for the implementation of foreign direct investment in developing countries and countries in transition is determined by various 'push' and 'pull' factors. The most important 'push' factors are the following: avoiding trade barriers, reducing dependence on the domestic market, increase of production costs in the home country, competitive pressure of companies from developed countries, lack of key resources and inputs necessary for implementation of the production process and others. 'Pull' factors are manifested in the form of various incentive measures through which the governments of the capital recipient countries seek to attract foreign capital in order to, on its basis, manage to strengthen their economic competitiveness. (Sinanagić, 2008, p. 155.)

Net inflow of foreign capital was achieved by all countries in transition, to a lesser or greater extent, although the results of capital inflows were different. Some of these countries managed to significantly increase their export competitiveness and to engage in international production and technological trends. In other countries, the inflow of foreign capital largely resorted to disinvestment or financing various forms of domestic consumption. The transition process of the Western Balkan Countries was also accompanied by an inflow of foreign capital. Foreign investors bought domestic enterprises, thus enabling capital inflows through privatization. That way, foreign direct investment has become the main source of covering the growing current account imbalances of the countries from the region.

Table 4 Balance on Current Account in the Western Balkan Countries from 2005 to 2011 (percent of GDP)

Country	2005	2006	2007	2008	2009	2010	2011	2012
Albania	-8.7	-11.4	-10.7	-15.4	-15.4	-9.2	-12.3	-12.8
BiH	-15.6	-7.2	-9.3	-13.3	-6.6	-5.5	-8.8	-8.0
Montenegro	-8.6	-24.7	-29.4	-50.7	-30.1	-17.0	-19.5	-19.8
FYROM	-2.7	-0.4	-7.6	-12.8	-6.9	-3.9	-2.7	-4.0
Serbia	-8.7	-10.1	-15.7	-17.9	-5.6	-9.6	-9.5	-11.0
Croatia	-5.5	-6.9	-7.6	-9.2	-5.2	-3.8	-1.0	-1.2

Source: Kovačević, 2012, p. 244; International Monetary Fund, 2013.

Data presented in Table 4 demonstrate that, until 2008, all Western Balkan countries registered increasing deficits of their current account (as a percentage of GDP). The largest current account deficit was recorded in Montenegro in 2008, with a record of -50.7%. In the same year, Serbia had significantly lower current account deficit being -17.9% of GDP. The lowest current account deficit in 2008 was in Croatia amounting to -9.2%. The year after (2009), all Western Balkan Countries recorded a reduction of their current account deficit. However, some of these countries recorded a decline in their current account deficit in 2009 and 2010, with an increase in 2011. Therefore, Albania recorded a decline in current account deficit which increased from -9.2% in 2010 to -12.3% in 2011 and to -12.8% in 2012. The situation is similar with *Bosnia and Herzegovina*, where the current account deficit rose from -5.5% in 2010 to -8.8% in 2011, being reduced to 8% in 2012. Of all the Western Balkan Countries, only Croatia registered a continuing decline in their current account deficit throughout the three-year period, which amounted to only 1% at the end of 2011, with a slight increase of 0.2% in 2012.

As for the Western Balkan Countries, foreign direct investment dates back to the early 1990s. The first beneficiaries of foreign investment in the area were Croatia and Albania, since 1992 to be exact. Throughout the next few years, as recipients of foreign direct investment, other Western Balkan Countries such as Serbia, Montenegro, *Bosnia and Herzegovina* and Macedonia were included. Available data indicate a low level of foreign investment flows in the Western Balkan Countries. Inflow of foreign direct investment in the early 90s of the last century was negligible, due to the war across the region. Establishment of relative political and economic stability, the inflow increased significantly (about 10 times) and reached a level of 3-4 billion USD at the regional level in the period from 1995 to 2000. Such funding level remained until 2004 with a minimum

deviation. The expansion of capital flows on a global level in the period from 2005 to 2007, caused a significant increase in capital flows to the Western Balkan Countries. Inflows of foreign direct investment were significant and had a positive effect on the entire economic and political environment of the countries of the region. Single largest absorber of foreign capital was Croatia, as the most developed country in the region with the best integration results. Significant foreign capital inflow was also registered in Montenegro, which had the highest inflow of foreign direct investment per capita in Europe.

Table 5 Dynamics of FDI inflow in the Western Balkan Countries from 2001 to 2011 (in million USD)

Year	Albania	BiH	Croatia	Montenegro	FYROM	Serbia	West Balkans
2001	206	119	1,313	5	447	177	2,262
2002	135	265	1,071	76	106	567	2,144
2003	178	381	1,989	39	118	1,406	4,072
2004	346	704	1,179	42	323	1,028	3,580
2005	264	613	1,825	322	97	2,051	4,850
2006	325	766	3,468	252	424	4,968	9,951
2007	662	2,077	5,023	377	699	4,382	12,843
2008	988	1,064	6,140	916	587	2,995	12,690
2009	979	501	2,065	1,311	248	1,920	7,024
2010	952	408	354	689	191	1,204	3,798
2011	891	734	1,258	481	365	2,339	6,068
Total	5,926	7,632	25,685	4,510	3,605	23,037	69,282

Source: Grgurević, 2013

According to The World Bank (2013b), *Bosnia and Herzegovina* was ranked 95th in 2007, 110th in 2011, 125th in 2012 and 126th in 2013 Doing Business rank. In addition to the continuing deterioration of its Doing Business rank and the worst ranking (126) in 2013, compared to the other Western Balkan Countries, Bosnia and Herzegovina is in the third place regarding foreign direct investment inflow. Based on the data presented in Table 5, foreign direct investment in Bosnia and Herzegovina amounted to 7.632 billion USD in the period from 2001 to 2011. On the basis of foreign direct investment, *Bosnia and Herzegovina* is ahead of three other Western Balkan countries: Macedonia, Montenegro and Albania. Croatia is located in the first place with regards to the amount of foreign direct investment in the region, with the influx of 25,685 billion USD, while Serbia is in the second place with 23,037 billion of foreign direct investment.

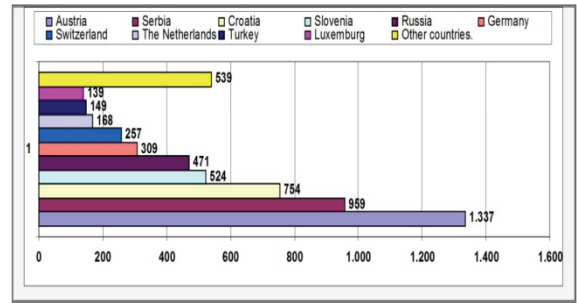


Chart 2 Most important countries investing in BiH from 1994-2012 (in million EUR)

Source: Centralna banka Bosne i Hercegovine, 2013

Chart 2 includes ten major foreign investors in *Bosnia and Herzegovina* in the period from May 1994 to December 2012. The most considerable investor throughout the nineteen-year reporting period is Austria, which invested 1.337 billion of the total amount of foreign direct investment - being 5.605 billion EUR. Foreign direct investment from Serbia to Bosnia and Herzegovina amounted to 959 million EUR, while Croatia invested 754 million EUR in Bosnia and Herzegovina. Likewise, Russian investments in Bosnia and Herzegovina are also quite considerable, amounting to 471 million EUR. Germany and Switzerland invested a slightly lower amount in relation to Russia, i.e. 309 million and 257 million EUR. Foreign direct investment of Turkey to Bosnia and Herzegovina amounted to 149 million EUR, while the other countries invested 539 million EUR of foreign direct investment in total.

When it comes to the Western Balkan countries, with respect to foreign direct investment in Bosnia and Herzegovina, leading positions are occupied by Serbia and Croatia. These two countries, with negligible participation of Montenegro, make about one-third of foreign direct investment in Bosnia and Herzegovina. On the other hand, if the investor countries are grouped into categories, it can be said that EU Member States account for about fifty percent of the foreign direct investments in Bosnia and Herzegovina. Unlike the European Union member countries, Islamic countries as foreign investors accounted for 6% with Russia's participation being about 5% of the total foreign direct investments in Bosnia and Herzegovina.

Among the Member States of the European Union, Austria and Slovenia, which can be regarded as nearby countries, are particularly noted as countries providing the highest level of foreign direct investment, while the significant presence of the Slovenian capital can be explained by the

recent historical ties. The high investment level from the European Union to Bosnia and Herzegovina unequivocally confirms the strategy of the future inclusion of Bosnia and Herzegovina in the European integration process. Therefore, such economic presence of the member states of the European Union in BiH is entirely understandable, particularly regarding the nearby member states. *This justifies the Bosnia and Herzegovina's third place regarding foreign direct investment despite, despite its worst competitive position among the countries of the Western Balkans.*

3. Macro-economic, business and legal environment as a key factor for attracting FDI in Bosnia and Herzegovina

Macroeconomic stability and economic growth were recorded in Bosnia and Herzegovina in the period from 2005 to 2008. Gross domestic product increased by 5.6% per annum within the given period. Such economic growth was caused by the expansion of domestic demand and export. Domestic consumption was stimulated by the growth of wages and income per capita, as well as by the inflow of remittances from abroad. The expansion of bank loans directed to private enterprises and households was also registered within the given period. Export growth was potent, although it was exceeded by imports in each year, which ultimately resulted in the growing *negative trade balance*.

The global financial crisis led to a drop in stock markets indices and to market capitalization in 2008 in Bosnia and Herzegovina, while its actual impact was not reflected to the real economy until 2009. This led to a decline in real GDP by 3% in 2009, while the economic recovery was very slow with almost non-existing growth in 2010. The economic crisis quickly evolved into an employment crisis that began in late 2008, which was reflected as the decline in paid employment in the formal sector, growth of unemployment and poverty. The financial crisis in Bosnia and Herzegovina was transferred through two global channels: (1) *export demand* and (2) *through financial sector*. There was a decline in export, which accounted for as a very important item of the GDP in Bosnia and Herzegovina, since its major trading partners, such as Germany and Italy, recorded their lowest growth in the last 20 years.

The *banking sector* was another sector struck by the crisis in Bosnia and Herzegovina. This oc-

curred due to profound relations of Bosnia and Herzegovina's banks with banks from the west, and not because of any internal factors. The largest banks, owned by Western European banks, were affected by the lack of funds for loans, which caused a slowdown in credit growth in mid-2008. This directly reflected onto loan-dependent industries such as construction, automotive, mechanical, etc. Reduced activities in these industries expanded to their supplying sectors, such as metal, civil, energy and others. In addition to financial and export sectors, there was a decline in remittances from abroad and in *foreign direct investment*.

The banking sector in Bosnia and Herzegovina is liquid and well capitalized today, although the level of non-performing assets is currently being increased. It should be noted that foreign banks currently hold more than 90% of total assets in the banking sector of BiH. Despite that fact, the banking sector is not exposed to major credit outflows towards parent banks, meaning the system is still quite solvent. However, the level of non-performing assets in the banking sector is increasing considerably. By the end of 2012 it reached the level of 13.5% compared to 7.1% in 2010 and 5.9% in 2009.

Poor external and internal circumstances limited the economic growth of Bosnia and Herzegovina. Following the negative growth in 2012, economic recovery in 2013 was very modest. Some medium-term growth is expected in case the global and regional outlook is improved. However, the economy remains vulnerable on many fronts, not only because the whole region is facing a difficult situation, but also because of *internal complexity of the political structure of the country and a poor investment environment* are the main obstacles to *foreign direct investment*.

Business environment in Bosnia and Herzegovina continues to be the most complicated in the region. The past two years were marked by implementing certain reforms in order to reduce administrative barriers for the purposed of establishing new enterprises, through reducing the regulatory and tax burden and simplified registration of property. However, Bosnia and Herzegovina is still ranked very low on the basis of most business environment quality indicators. The latest World Bank Doing Business report ranked Bosnia and Herzegovina as the 126th out of 185 countries on the overall doing business rank, thus placing it beneath all the countries of Southeastern Europe and among the worst in the whole transi-

tion region. Bosnia and Herzegovina is particularly low ranked in indicators for obtaining a construction permit (163rd place), starting a businesses (162nd) and getting electricity (158th).

Bosnia and Herzegovina is somewhat better positioned according to the World Economic Forum (WEF) Global Competitiveness Index, being ranked as 87th out of 148 ranked countries. According to the WEF Global Competitiveness Index, quality of public institutions in Bosnia and Herzegovina is high compared to other countries in the region (Bosnia and Herzegovina is ranked as 79th with reference to this indicator, positioned worse than only two countries in South East Europe), despite its complex political environment. According to the indicators of the quality of macroeconomic environment, Bosnia and Herzegovina is ranked as 97th which is slightly below the average for the region of Southeast Europe. However, according to the quality of infrastructure indicators, i.e. transport infrastructure, Bosnia and Herzegovina is extremely poorly positioned, being ranked as 143rd, or the second last from a total of 144 countries covered.

According to the results of the *European Bank for Reconstruction and Development* and the *World Bank* from 2010, related to researching the business environment and to the successful operation of companies, entrepreneurs and managers specified the following as the main obstructions in business: (1) political instability, (2) High tax rates, (3) vast informal sector, and (4) difficult access to financing. Reports on the credit rating of well-known international rating agencies such as *Standard & Poor's* and *Moody's* provide stable outlook for Bosnia and Herzegovina. When it comes to economic freedom, *National Heritage* monitors economic trends of 179 countries, where Bosnia and Herzegovina is ranked as 104th, right below Nicaragua, Cambodia and Kenya. According to the Corruption Perceptions Index (CPI) of *Transparency International* Agency for the year 2012, Bosnia and Herzegovina is ranked as 72nd of 176 countries surveyed, although such ranking is quite favourable when compared to many regional neighbours.


Legal environment in Bosnia and Herzegovina is still a complex and problematic issue. Some significant reforms were made in the previous period, but it is necessary to do even more. Multilayered constitutional and political structure of the country still has a negative impact on legal reform. Problems of multilayered legal structure are visible in numerous areas of law. Corporate

governance is regulated at the entity level, thus causing emergence of two different systems of corporate governance, with each entity having its own primary and secondary legislation. In the judiciary sector, there are two separate legal systems and limited coordination at the state level. Legal framework for the securities market is regulated at the entity level, with each entity having its own Securities and Exchange Commission.

In theory, with reference to certain areas, Bosnia and Herzegovina's legislation is characterised by the laws which, in principle, comply or even exceed the standards in comparison to other countries. However, the implementation of such laws in practice is often poor due to incompetency of key institutions. For example, the law on bankruptcy and insolvency has been rated as a law of "high compliance" with international standards. However, in practice the insolvency regime is marked by weaknesses in implementing appropriate regulation of insolvency office holders. Likewise, the legal and regulatory framework for secured transactions is modern, but its enforcement is sluggish and susceptible to obstruction. Efficiency of the courts in Bosnia and Herzegovina is still marked as the weakest link of the system, enabling the debtors to obstruct the enforcement proceedings. The laws on concessions are complex and fragmented. Similar issued are regulated by a combined set of legislative acts that coexist at various levels. Thus, Bosnia and Herzegovina's prospects largely rely on the practical implementation of legal reforms and internal and regional integration.

Conclusion

In the recent decade of the current century, competitiveness has become a dominant economic topic. The fact has been accentuated by the global financial crisis that has affected and still affects, the development of numerous countries in transition, particularly the Western Balkan countries. Recent research results have shown that all Western Balkan countries have very low export coefficients, thus having a negative trade balance expressed as a GDP percentage. Bosnia and Herzegovina is by no means different from other countries of the region. Namely, the trade deficit is one of the major problems of this country's economy, and is the result of weak competitiveness in the international market and high import-export dependence. Ranked as 87th, Bosnia and Herzegovina positioned as the third country in the region, placed above Albania and Serbia. However, when

it comes to doing business and starting business rank of 126th position, Bosnia and Herzegovina is by far the lowest ranked country in the Western Balkans. The subject of this survey is the competitiveness of the economy of Bosnia and Herzegovina in comparison to other Western Balkan countries and the impact of economic competitiveness to foreign direct investment in the country. Despite such poor competitiveness indicators, studies have shown that Bosnia and Herzegovina is still the third ranked country in the region in terms of inflow of foreign direct investment, right after Croatia and Serbia. Surely, such ranking is surely caused by the geopolitical and strategic position of BiH which investors such as EU countries, Islamic countries and Russia forward their investments in. Since macroeconomic, business and legal environment are essential factors for attracting foreign direct investment, Bosnia and Herzegovina still requires a fair amount of time to overcome the problems of transition and to improve elements of all three factors. By doing so, it would manage to compete with neighbouring countries when it comes to attracting foreign direct investment, thus bringing better competitiveness to its economy, reduction of its trade deficit and would increase the growth rate of its GDP and employment rate. 

References

- Bosna i Hercegovina, Vijeće Ministara, Direkcija za ekonomsko planiranje. (2013, April). *Bosna i Hercegovina, Ekonomski trendovi, Godišnji izvještaj 2012*. Retrieved January 28, 2014 from Direkcija za ekonomsko planiranje BiH: www.dep.gov.ba/dep_publikacije/ekonomski_trendovi/?id=1574
- Centralna banka Bosne i Hercegovine. (2013). *Godišnji izvještaj 2012*. Retrieved 2 February, 2014 from Centralna banka Bosne i Hercegovine: http://cbbh.ba/files/godisnji_izvjestaji/2012/GI_2012_bs.pdf
- Grgurević, N. (2013). *Uticaj stranih direktnih investicija na zemlje u tranziciji*. Retrieved February 2, 2014 from Univerzitet za poslovni inženjering i menadžment: <http://univerzitetpim.com/wp-content/uploads/2013/10/Grgurevi%C4%87-N>
- Grgurević, N. (2013). *Uticaj stranih direktnih investicija na zemlje u tranziciji*. Retrieved February 2, 2014 from Univerzitet za poslovni inženjering i menadžment: <http://univerzitetpim.com/wp-content/uploads/2013/10/Grgurevi%C4%87-N>
- International Monetary Fund. (2013, October). *World Economic and Financial Surveys, World Economic Outlook, Transitions and Tensions*. Retrieved February 2, 2014 from <http://www.imf.org/external/pubs/ft/weo/2013/02/pdf/text.pdf>
- Kitson, M., Martin, R., Tyler, P. (2004). *Regional Competitiveness: An Elusive yet Key Concept? Regional Studies* 38 (9), 991-999.
- Kovačević, R. (2012). *Međunarodno tržište kapitala*. Beograd: Ekonomski fakultet.
- Olsen, K. B. (2013). *Užas balkanske tranzicije*. Retrieved February 3, 2014 from Aurora: <http://www.aurora.hr/2386/uzasi-balkanske-tranzicije/>
- Porter, M. E. (1990). *The Competitive Advantage of Nations*. New York: Palgrave.
- Sinanagić, M. (2008). *Strategijske varijante ulaska na inostrano tržište*. Brčko: Gamma-X.
- The World Bank. (2013). *Southeast Europe - Periodic Economic Review No. 4*. Washington: The World Bank.
- The World Bank. (2013). *Doing bussines*. Retrieved February 3, 2014 from Open Knowledge Respository: <https://openknowledge.worldbank.org/>
- Vuković, D. (2007). *Quality and Competitiveness, Governance & Management, Consulting services*. Zagreb: incus Ltd.
- World Economic Forum. (2009). *The Global Competitiveness Report 2009-2010*. Retrieved February 2, 2014 from World Economic Forum: http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2009-10.pdf
- World Economic Forum. (2010). *The Global Competitiveness Report 2010-2011*. Retrieved February 2, 2014 from World Economic Forum: http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2010-11.pdf
- World Economic Forum. (2011). *The Global Competitiveness Report 2011-2012*. Retrieved February 2, 2014 from World Economic Forum: http://www3.weforum.org/docs/WEF_GCR_Report_2011-12.pdf
- World Economic Forum. (2012). *The Global Competitiveness Report 2012-2013*. Retrieved February 2, 2014 from World Economic Forum: http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

✉ Correspondence

Vitimir Starčević

Faculty of Business and Economics
Semberskih ratara bb, 76300, Bijeljina, Republic of Srpska

E-mail: nana.vitimir@gmail.com