FOREIGN DIRECT INVESTMENT AND THEIR CHARACTERISTICS IN BOSNIA AND HERZEGOVINA

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Abstract: Foreign investment is a key factor in the development of a modern economy, the trade, the most important means of enterprise business, the organization of production, supply of goods and services worldwide. Through foreign investment, companies organize production on a global scale, provide an efficient supply of raw materials, energy, labor, and then sell their products and services in the most important markets in a profitable way. Based on such a business, companies can optimally utilize its advantages in technology, knowledge, and economies of scale.

Developing countries due to debt and unfavorable economic conditions are showing interest in foreign investment, especially when various loans and financial help stop arriving. Transition countries integrate into the world economic system, negative economic tendencies can be overcome by international capital movements. Developed countries faced to a financial crisis, are also interested in the sizeable input of foreign capital, where foreign investment becomes the most important element of development strategies. This work gives special attention to the input of foreign direct investments and their effects in Bosnia and Herzegovina.

Key words: FDI, Bosnia and Herzegovina, economic development, effects and features.

INTRODUCTION

One of the important features of the world economy in the last three decades has increased the volume of foreign investment. Capital moved to different forms of foreign direct investment to classical borrowing in international financial markets. Foreign direct investment is a major form of private equity investments in developed countries to developing countries. The direct foreign investments is a form of investment in which the investor provides the right of ownership, control and management of the company to which the funds are invested, in order to achieve a long-term economic interests. Through this form of investment, the foreign investor acquires its active role in the work and operations of the company in which the funds were invested. Foreign direct investment are generating according to the statistics of the Convention IMF, when residents of one country become the owner of ten percent or more of a company in another country. The investment agreement is based on debenture and legal relations between investors. The contract is concluded between entities belonging to different states, or on the applicable law differently. It is a contractual relationship with a foreign element. The main characteristics capital of the movement in the world, in large part, reflect the format and quality of input in transition countries, including Bosnia and Herzegovina. Efficiency, height and structure of investment in Bosnia and Herzegovina are, without a doubt, the assumptions of a successful restructuring to strengthen export competitiveness and to achieve sustainable high growth rate in the long run. The key question is, how effective is foreign investment used in Bosnia and Herzegovina and its contribution to economic development. In the mid nineties, there was a sudden increase in capital inflows to the country, which was accompanied by a decline in the share of public capital to total funds, and reciprocally increased significance of private equity investments, particularly FDI investments. Foreign direct investment is defined as a form of capital, whose investment in a specific company, acquired ownership control over it. (Pušara, 2004).
1. The development of foreign investment

The beginnings of foreign investment dating back to the 16th century in Europe, where beginning to create real trade which extend throughout Europe, and their offices are opened in major shopping centers. As for the company's industrial revolution had a profound influence on their development. The capacity of the companies is increasing, creating a new organization, and they become stronger on the world market. This enabled the faster creation of multinational companies that in time to come, will become the locomotive which pull forward investments worldwide. At this stage, it is invested in foreign markets, primarily in commercial companies with the aim of obtaining a more favorable raw materials and sale of finished products. In the interwar period investments were steadily. Multinational companies have started to invest more strongly in oil sources, especially in the colonies. After World War II, in contrast to earlier investments, which were mainly motivated by providing resources, it begins to invest in new technologies, knowledge management and new markets.

In the Period till 1960. was characterized by a strong dominance of U.S. investment, as about 3/4 of investments came from the United States. The characteristic of the 70s is to strengthen European multinationals and their stronger investment worldwide. The beginning of the eighties was characterized by significant investments in TNCs in developing countries, where the main motive of investors was cheap labor force. The characteristics of 90s, is that empowered and already sufficiently developed some of the developing countries emerge as major global investors. Through this brief review, we see that the beginnings of investments are linked to the beginnings of world trade, and that the real development of foreign investment are linked to the beginnings of modern industry. In the process of economic competition in a globalized world market, major world countries and their transnational corporations „eat“ small and under-developed countries. (Petković, 2009).

2. Characteristics of foreign investment

The main aim of the investment is profit. The most important sub-goals, which are basically, aimed at maximizing conception of a firm are: the pursuit of new markets, lower labor cost, insurance, regular source of supply, and so on. The pursuit of new markets is one of the most important motives of foreign investors. If the entry of a company to some interesting market, difficult by macro-economic policy of the state or of the competitive environment in this market, it will try to enter that market by investment strategy. When it comes to the country in which to invest, then the interest is mainly the rapid development of the foreign capital invested in the country. For investors it is to conquer the new ones, or to expand existing markets in order to increase profit as the main objective of all investment. The lower cost of labor as a factor of investment has encouraged multinational corporations to using cheap labor to organize production at significantly lower costs, which contributed their products become more competitive on the world market. Foreign investor, in order to ensure regular supply of raw materials necessary to its production, invests in a foreign country while, at the same time, there are cheaper and better raw materials, which ultimately affects the reduction of the total cost or cheaper product which thus acquire a better position in the market. In an attempt to answer the question of why, how and where to get foreign direct investment can serve OLI theory. (Sauvant, 1993). According to this theory, the motive for initiating direct investment occurs when fulfilled three conditions: first, when there are ownership advantages for possession of specific intangible assets (ownership advantages-O), and second, when the benefits of their own production and the internationalization of higher benefit brought by selling licenses (internalization-I), and third, if there are advantages of the location (location-L).
The recipient countries, demanding for the input of foreign direct investments, are mainly motivated by the social benefits of foreign direct investment, which originate primarily from the transfer of technology, knowledge and skills and their influence to the rest of the economy and the positive impact of foreign trade, employment growth and investment in the local economy.

3. Distribution of Foreign Investment

Foreign investments are classified as portfolio investment and foreign direct investment. Portfolio investments include investments in which a foreign investor, as a rule, does not participate in the governance and management but it is focused on gaining profits, dividends and interest. The direct foreign investments is a form of investment in which the investor provides the right of ownership, control and management of the company to which the funds are invested in order to achieve a long-term economic interests.

The direct foreign investment can be divided further, based on the interdependence of investment in the recipient to substantive and additive. The substantive direct foreign investments lead directly or indirectly to the suppression of local investors. If direct foreign investment are additional to the size of investment in the recipient country, then it is the additive investments.

Based on fitting into enterprise, investments are divided into horizontal, vertical and conglomerate. (Sarajčić, 2006).

The horizontal mean investments in which the investment in the recipient country produces the same product as the provider of investment land, then we say that it is a vertical investments. If direct investments are not in any kind of production and economic connection with the provider of investment land, then we say that it is a conglomerate or diversified investments.

When the parent company of certain parts of the production and marketing related to a product distributed by affiliated institutions and in different countries, we say that it is a vertical investments. If direct investments are not in any kind of production and economic connection with the provider of investment land, then we say that it is a conglomerate or diversified investments.

There are three common ways of origin of foreign direct investment: (Burnazović, 2007).

- Green field operations are building a brand new plant in the foreign market.
- Majority acquisition means taking the company through the purchase of a majority stake.
- Merger (fusion) is merging partners.

In the modern world there has been a massive centralization and concentration of capital in the hands of a small number of giant corporations that allocating the investments to a large number of countries were able to eliminate the threat of big risks. TNCs are the main carrier of the globalization of the world economy, which, among other things, can be seen from the fact that during the 1999, 63,000 parent companies owned at about 690,000 of its affiliates worldwide. Increasing FDI increases the number, but also the role of foreign affiliates as part of the modern global economy with FDI and TNCs are inextricably linked. All this confirms that the TNC now represents the generator of globalization and foreign direct investment. The special feature of the global economy is the fact that the TNC in its business use affiliates more than traditional export to serve basically foreign markets. TNC concept is fundamental intention that foreign investment is being made, rather than in the form of Loan Capital (indirect investment), in an entrepreneurial capital (direct investment).

The main characteristics of foreign direct investment are:
- The ability of foreign investors to set up a company (or buy already existing) and to control it,
- A foreign investor makes profit directly, depending on the business success of the company (and not in the form of interest as in the case of Loan capital).

Constant excess capital with limited investment opportunities in developing countries, is to request new opportunities for export. The export of capital is an objective necessity for developed countries. Global Strategy TNCs tries the most of the funds needed for their operations, to provide in the developing countries and at the same time to take the most of the profit out of these countries.

TNC use three main sources of financing in developing countries:

1. own assets that generate their affiliates in host countries (reinvestment of profits and depreciation),
2. funds that are provided in local capital markets,
3. funds derived from the native country.

The negative impact is not reflected only in the immediate exploitation, which extracting extra value, the fact is that the limiting factor of TNCs is to influence the formation of characteristic dependent economy that is not able to develop on an independent basis. The entry of TNCs in the economies of developing countries has contributed to strengthen the economic dependence of developing countries to developed countries. TNK is an instrument of exploitation of underdeveloped countries, they lead to the concentration of capital and profits in a several number of leading industrialized countries, primarily the United States. Of course, one cannot deny that TNCs have also brought some benefits in some developing countries, but there are many more countries where the impact was negative and where the long-term, foreign capital has become obstacle to social, political and economic emancipation of developing countries. As for the positive impact of TNCs, we can state that: they bring to the host country needed capital, new technology, increase employment, contribute to the rise in exports, as well as the country's opening to the world. The capital is needed in developing countries in order to activate the existing resources, set the industrialization, because in some cases, modern technology can be provided only through cooperation with TNCs. Along with the development of cooperation with TNCs, it is necessary to strengthen the resistance of capital investment under exploitative conditions that allow the accumulation of most of the outflow from developing countries.
4. Advantages of FDI

The experience of many countries shows that foreign direct investment is better for accumulation the necessary foreign capital in relation to the taking of classical credits in international financial markets. Analyzing the state of the balance of payments and growth rates achieved in the seventies, we see that it is a group of countries which relied on foreign direct investment more develop. From a macro point of view, the benefits of foreign direct investment are the following: improving the trade and balance of payments of the country, there is a faster and more efficient incorporation of the domestic economy in the world market, improving the supply of the domestic market, the number of new jobs, etc.. At the micro level, domestic firms have the following benefits: faster and cheaper introducing the modern technology, also introducing modern organization of work, acquiring more modern knowledge of the marketing and so on. Foreign direct investment should represent additional factors to the economic development of developing countries in accordance to their development strategy. It should contribute to the transfer of appropriate technology, particularly the development of national scientific and technological resources, as well as increasing employment and staff training, and increasing demand for domestic raw materials and, in general, domestic production factors.

5. FDI in Bosnia and Herzegovina

Through foreign investment in the period from 1967. to 1990. Bosnia and Herzegovina has built a number of significant industrial capacity. These include TAS, which was built in Volkswagen's and UNIS investment, then factory office machines in Bugojno, factory bearings in Sarajevo, etc. The choice of foreign capital investment is essential for the country. Foreign investment facilitates faster rehabilitation and construction of the war-torn country. Foreign capital should be encouraged the restructure of those industries which Bosnia and Herzegovina has successfully stepped in the global market. Foreign investment should accelerate the transformation of previous social forms to private ownership. This will further reflect to a faster establishment of the money and capital markets, particularly stocks. Foreign investment could mitigate extremely high rate of unemployment relatively high skilled labor.

According to the Law on Foreign Direct Investment in Bosnia, in section 2 of says that the foreign direct investment "means the acquisition, creation or expansion of any business enterprise or any activity alone or with others at the same time or one after the other has the effect of permitting one or more foreign investors acquiring or increasing control over a company that control doing industrial, agricultural, commercial and financial activities and also activities related to real estate, services, or activities, or to facilitate the extension of the company that is already controlled by foreign investors ... ". (DEP BiH, 2010). "Foreign control" means any participation of more than 10% of capital and or the voting rights which are the direct agents of foreign investors or a local legal entity under such control. Bosnia and Herzegovina as most of the countries offer incentives for foreign investment. The point is, that foreign direct investment in the first ten years, do not pay tax income. Besides the tax relief that reduce production costs or increase the chances of long-term profits, Bosnia and Herzegovina should provide a good basic infrastructure, connectivity of the economy to other countries (Free Trade Agreement), political stability and the legislation of the country and the stability of the tax system.

According to the Ministry of Foreign Trade and Economic Relations of Bosnia and Herzegovina, investment in 2010. amounted to EUR 135.4 million, which represents a decrease of investments in the same period of 2009. by 71.4%.

It should be noted that there are possible variations in the amount of registered foreign investment due to the implementation of
amendments to the Law on Foreign Direct Investment in Bosnia and Herzegovina (published 7.14.2010.), so that the total amount FDI in BiH is slightly higher.

Under this law, foreign investors will continue to register only in a competent court, and this remains an obligation to inform the competent ministry. This stops the obligation of foreign investors to register their respective investment at the Ministry of Foreign Trade and Economic Relations. Hereby is greatly simplified and shortened the registration of foreign investors with local authorities, which should certainly help increase FDI in Bosnia and Herzegovina.

The characteristics of registered FDI in 2010. in Bosnia and Herzegovina is their low rate and most of them are recapitalizations, increasing previously established companies capital that is about 54%, while the creation of new ones is about 46%.

The largest investments are related to the companies: (www.fipa.gov.ba, 2012).

- Intesa Sanpaolo Banka Bosnia and Herzegovina 44.2 million convertible Mark (Italy)
- Hypo Alpe Adria Leasing Ltd Sarajevo 20.5 million - an increase of capital (Austria)
- Hotel tourist enterprise Neum Ltd Neum 20.2 million - foundation (Netherlands)
- Brodomerkur Ltd Široki 16.7 million - foundation (Croatia)
- Hypo Alpe Adria Bank Mostar 10.0 million - an increase of capital (Austria)
- Kosig insurance Banja Luka 6.8 million (Serbia)
- Hypo Alpe Adria Bank ad Banja Luka 5.0 million (Austria)
- JP B & H Airlines Ltd 3.8 million (Turkey)
- Invest Inving engineering Ltd Prijedor 2.8 million (Cyprus)
- Hepok Ltd Mostar 2.5 million - an increase of capital (Serbia).

At the same time the greatest reduction in capital is related to:
- OMV BH Ltd 38.7 million loss of losses for accumulated company (Austria),
- Energoinvest reinforcement Ltd Sarajevo 9.0 million (Montenegro)
- Nelt Ltd Trebinje 1.2 million (Cyprus)
- Klimotehna Ltd Sarajevo, 9 million (Austria),
- Inter Bhutan Ltd Cazin 0.3 million (Slovenia)
- Velefarm Ltd. Banja Luka 0.3 million (Serbia) and
- The other smaller companies with a total reduction of approximately 2 million convertible Mark.

Figure 1. FDI in BiH, in 000 KM

Source: Agency for Promotion of Foreign Investment in the Bosnia and Herzegovina

The most significant investment by the investing in 2010. include:
- Italy 46.8 million,
- Croatia 29.8 million,
- Serbia 22.4 million,
- Netherlands 20.3 million,
- Slovenia 5.26 million,
- Turkey 4.6 million,
- Switzerland 3.4 million,
- Austria 2.26 million, which accounts for 99.6% of total investment in 2010.

Figure 2. Major investments by country in 2010.

![Diagram showing major investments by country in 2010](image)

Source: Agency for Promotion of Foreign Investment in the Bosnia and Herzegovina

According to the Central Bank, foreign direct investment in the 2011th amounted to EUR 566.9 million, or 2.2% of GDP. The structure of foreign direct investment in equity relating 389.3 million and other capital 185.1 million. In terms of geographical distribution, most investments were from Russia (142.6 million), Austria (106.2 million) and Serbia (98.3 million). Most of it was completed in the activities related to financial intermediation (about 162 million), followed by trade (about 96.5 million), and in companies that are registered in the real estate business in the amount of 74.3 million.

Figure 3. Condition of FDI by sectors of 1994-2011.

![Diagram showing condition of FDI by sectors](image)

Source: Central Bank of the Bosnia and Herzegovina

Bosnia and Herzegovina has attracted some, but not a sufficient amount of foreign investment. Most of the capital is invested by taking ownership of enterprises, privatization. There is a lack of new investments (greenfield-investment), especially in sectors of export. One of the reasons for the failure of the foreign investment is that there is no development strategy, objectives, and macroeconomic policy to implement the goals, and therefore neither height, nor the effects of investments have not reached the proper level.

**Conclusion**

Foreign direct investment increase exports and improve the balance of payments of the countries concerned, as well as the diversification of the national economic structure.

The reduction in foreign direct investment is the result of reduction in foreign interest caused by the still-present global economic recession and stopping the direct economic incentives that have given the government of the most developed economies around the world (mainly the U.S., Britain and Germany).

The process of privatization of state-owned shares in some strategic enterprises did not
begin, however in the most profitable ones (in the field of Telecommunications and Energy, has been postponed until further notice), it is evident the delay of major investments in the energy sector on the principle of joint investment with foreign partners. The participation of foreign partners in these projects could in the future significantly increase foreign direct investment in Bosnia and Herzegovina, and therefore becomes the main future initiator economic development of the country.

Increasing in foreign direct investment in the world, especially to developing countries and transition economies (where they first exceeded investment in developed countries), and moderate output of the crisis the most developed countries, provides a realistic base for the expectation of increasing investment of foreign direct investment to Bosnia and Herzegovina compared to the previous period.

REFERENCES