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A LITERATURE REVIEW ON THE RELATIONSHIP BETWEEN FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH IN BALKAN COUNTRIES

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Abstract
The process of globalisation has made the world a single global village. This process is now irreversible; it was primarily caused by trade and investment across economies resulting in strong worldwide market for goods, services and capital. Foreign Direct Investment is one of the important outcomes of globalisation. The world is full of development opportunities, covering the entire range from countries that have just begun to modernise to the richest countries. FDI help countries secure financing for their economic growth. These investments promote economic growth in both the host country and the country of origin. The host country benefits from FDI by financing projects planned, developing new technologies and generating new jobs. Investing companies benefit from the expansion of markets and, consequently, the growth of their shares in international markets. This paper targets and discusses the main theoretical aspects of existing literature pertaining to FDI. It starts with some definitions given by different institutions or authors regarding FDI, continuing with a history of foreign direct investments from ancient times to the present.

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Keywords: (FDI) Foreign Direct Investment, Economic Development/Growth, Balkan Countries International Trade

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1. Introduction

"Foreign direct investment (FDI) is defined as an investment involving a long-term relationship and reflecting a lasting interest and control of an enterprise resident in an economy other than that of a foreign direct investor (FDI enterprise or affiliate enterprise or foreign affiliate) by a resident entity originating from another economy (foreign direct investor or parent enterprise)."

The topic of FDI and economic growth is very popular in conditions of development of the contemporary world and modern economics. FDI seems to be an irreplaceable factor for growth Additionally, the benefits of FDI cannot arise automatically.

The region's current socio-economic conditions provide an impetus for Balkan State governments to induce more foreign investment as a mechanism for fostering economic growth However, regardless of common incentives to attract more FDI inflow, some state-governments vary in their capacity to effectively do so. Foreign Direct Investment (FDI) helps countries secure financing for their economic growth.

FDI promotes economic growth in both the host country and the country of origin. The host country benefits from FDI by financing projects planned, developing new technologies and generating new jobs. Investing companies benefit from the expansion of markets and, consequently, the growth of their shares in international markets. The world is full of development opportunities, be it for countries that have just begun to modernise to the richest countries. While central banks control money levels in the economy and politicians control fiscal affairs, these two groups often cannot drive economic growth without external help.

According to the World Bank, foreign direct investment worldwide has had a general upward trend from 1970 to 2020. This growth has been fed by increasingly close integration of national economies, driven by worldwide competitive pressures, economic liberalisation, and the opening-up of new areas to invest in.

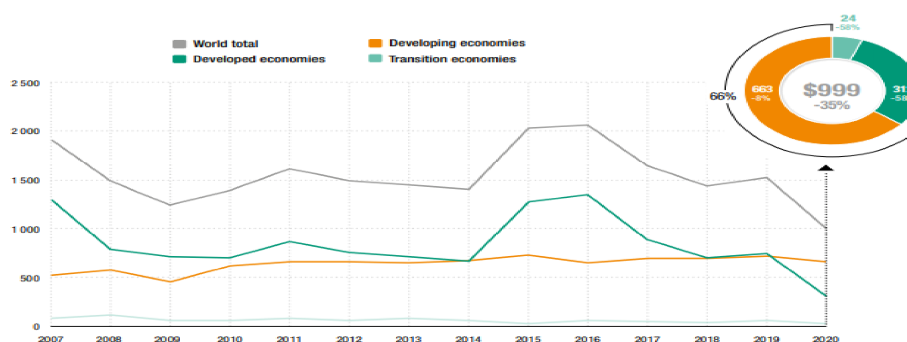
FDI is often vulnerable to economic and various other types of shocks. Past studies have noted the negative effects of financial crises (Dornean, Işan, and Oanea 2012; Dornean and Oanea 2015; Poulsen and Hufbauer 2011; Stoddard and Noy 2015).

In my paper, I will deal with FDI in the Balkan region for the 2000-2022 period. For this period FDI inflows, global and by group of economies, plummeted in developed and transition economies, falling by 58% in both. In developing economies FDI decreased by a more moderate 8% (UNCTAD, 2021).r

According to the World Bank, after 2007, we noticed some significant declines in FDI values, as a result of economic shocks. In 2008 we saw a decrease in FDI, which is explained by the financial crisis the world went through in that period. In 2018 there was also a significant decrease in FDI. In that year global trade spats, rising interest rates and Brexit uncertainty affected most stock indices in their worst

year since global financial crisis. In 2020 foreign direct investment was severely hit by the COVID-19 pandemic. Globally, FDI flows in 2020, fell by one third to $1 trillion, well below the low point reached after the global financial crisis a decade ago. Among the developed markets, Europe was hit hard The decline of foreign direct investments is a big concern, because international investment flows are vital for sustainable development in the poorer regions of the world.

Figure 1. FDI inflows, global and by group of economies, 2007-2020 (Billions of dollars and per cent)



Source: UNCTAD

As we can see from Fig.1, in the years 2008, 2018 and 2020 global foreign direct investment (FDI) flows decreased. In 2020, foreign direct investment globally reached $1 trillion, from $1.5 trillion in 2019 (Figure1). This is the lowest level since 2005 and almost 20% lower than the 2009 trough after the global financial crisis. Foreign investment in developing economies and transition economies has been more constant over the last ten years compared to developed economies. Aggregate inflows in Europe plummeted by 80% reaching only $73 billion in 2020 compared to 2019 (UNCTAD, 2021). In the conditions of the decline of foreign direct investments in 2020 and 2021, some notable developments took place in terms of the international investment agreement (IIA). These developments include the entry into force of EU's agreement to conclude all intra-EU bilateral investment treaties and the emergence of new regional IIAs.

Following the international investment agreement, on November 10, 2020, six economies of the Western Balkan endorsed the Regionally Accepted Standards for Negotiating International Investment Agreements, (UNCTAD 2021). This agreement includes the 6 countries of the region, namely, Albania, Bosnia and Herzegovina, Kosovo (United Nations Administrative Region, Security Council Resolution 1244 (1999)), Montenegro, North Macedonia, and Serbia.

Saul Estrin and Milica Uvalic explore the impact of foreign direct investment on the economies of Western Balkans during their transition to a market system. They have argued, on the basis of numerous indicators, that institutional, economic and political features of Western Balkan countries have probably restricted potential FDI spillover. Furthermore, spillover effects may have been limited because this region has attracted relatively small amounts of FDI and because relatively little FDI has gone into manufacturing as the main sector responsible for these countries' exports. In their paper, Bilal Sucubasi, Borce Trenovski, Berkan Imeri and Gunter Merdzan (2021) have confirmed that foreign direct investment inflows in the Western Balkans, as well as real economic growth affect domestic investments, both significantly and positively.

1.1 The purpose and research methodology of the paper

The purpose of this paper is to assess the relationship between foreign direct investment (FDI) and socio-economic environment variables in Balkan countries. The paper develops a data set and an econometric model to analyses FDI flows, poverty and socio-economic relations at the macro-level panel data set.

Research Questions: The questions raised for dealing with the actual FDI situation in Balkan countries, are:

- What is the impact of FDI on economic growth in Balkan Countries?
- Is there suitable socio-economic environment for attracting FDI into these countries?
- Which factors influence FDI flows?
- How does FDI affect developing countries?
- What are the main FDI determinants in the two countries involved?
- What are the common features and the major differences in behaviour observed concerning the FDI these countries received over the 2000s and 2020s?

Methodology: The paper starts with a theoretical treatment of FDI to continue with an empirical analysis of the effect of FDI on economic growth in the countries of the Western Balkans.

At the centre of the theoretical treatment are the models of economic growth in the field of economic sciences. However, first, as seen in Figure 1, developing countries have a more stable fluctuation of FDI, even in the theoretical treatment; very little is discussed about small developing countries, leaving a gap regarding the importance of FDI in such places. For this reason, I was prompted to conduct an empirical study regarding the effect of FDI on the countries of the Western Balkans. From the empirical analysis in this paper, we expect that the generalising opinions or conclusions about FDI are in line with economic theory.

For the realisation of this paper, I will rely on theoretical approaches by combining two main tools for study: the theoretical models of FDI in economic growth, e.g., Solow model, Borenstein, De Gregorio & Lee model, Mankiw model, Easterly model, and econometric analysis with secondary data obtained from sources such as World Bank, UNCTAD and EUROSTAT.

2. Literature review and some data collections

This part targets and discusses the main theoretical aspects of existing literature pertaining to FDI. It starts with some definitions given by different institutions or authors regarding FDI, continuing with a history of foreign direct investments from ancient times to the present.

2.1 What Is Foreign Direct Investment?!

Nowadays, domestic capital is not sufficient for fast economic development and competition in foreign markets. History has shown us that countries need foreign financing to ensure sustainable, long-term economic growth. Countries need Foreign Direct Investments as a means of financing the construction of new infrastructure and the creation of jobs. On the other hand, multinational companies benefit from FDI by expanding their footprint in international markets. In this context, Foreign Direct Investments can be a very important alternative for a faster and more competitive economic growth.

The term Foreign Direct Investment (FDI) is used to describe a category of cross-border investment in which an investor resident in one economy establishes a lasting interest in and a significant degree of influence over an enterprise resident in another economy (OECD).

Lasting interest means the existence of a long-term relationship between the direct investor and the direct investment company as well as a significant degree of influence on the latter.

The terms “direct investor” and “direct investment enterprise” are defined by the IMF and the OECD as follows: A direct investor can be an individual, a legal or natural person, a public enterprise, a government, a group of individuals or legal entities and/or individuals, who own a direct investment enterprise active in a country outside the direct investor’s country of residence. A direct investment enterprise is a legal or physical entity of which a foreign investor owns 10% or more of the shares or - has the voting power of a commercial company or the equivalent of a partner.

According to the same source, the importance of FDI is very crucial because:

a. FDI is a key-element in international economic integration because it creates stable and long-lasting links between economies.

b. FDI is an important channel for the transfer of technology between countries, promotes international trade through access to foreign markets, and can be an important vehicle for economic development.

According to the EU Statistics Office (EUROSTAT), FDI is the category of international investments that reflects the objective of realising sustainable interest by an investor of one economy from an enterprise resident in another economy. A direct investment enterprise is one in which a direct investor owns 10% or more of the ordinary shares or voting rights (for an incorporated enterprise) or the equivalent (for an unincorporated enterprise).

According to the World Bank (WB), foreign direct investment is the net inflow of investment to realise sustainable management interest (10% or more of the voting shares) from the enterprise operating in an economy other than that of the investor's. This is the sum of equity capital, reinvestment of earnings, other long-term capital and short-term capital, as shown in the balance of payments

Foreign direct investment (FDI) is an ownership stake in a foreign company or project made by an investor, company, or government from another country (Adam Hayes, 2022).

Foreign investment can be defined as the transfer of movable or immovable assets in whole or in part, from the country of origin to the host country for the purpose of using it to improve the welfare of the host country, under the control of the owner (Sornarajah, M. 2010).

Foreign direct investment can be defined as a long-term investment made by a firm or an individual in one country, into business interests located in another country, with all risks and profit opportunities (Emre Koluman, 2020).

If we have to give a certain definition of what FDI is, we will see that it is difficult to give an exhaustive answer. Due to the fact that foreign investors in different countries have different characteristics and operate in accordance with the legislative and regulatory framework of their countries, this causes the definition of FDI to change. FDI is much more complex in nature than portfolio investment, as it often involves the transfer of basic assets, such as technological know-how, and managerial and organizational skills. Consequently, the definition of FDI cannot practically be considered in isolation from the definition of multinational companies, which is also difficult to define. The main definitions of FDI can be found in the Balance of Payments Manual of the International Monetary Fund and the 1999 World Investment Report of the United Nations.

2.2 Historical Development of Foreign Direct Investments

The great accumulation of capital in world centres leads to the expansion of investments in other parts of the globe. One of the earliest examples of foreign direct investment dates back to 1500BC in the Phoenicians civilization. The Phoenicians

traded with the countries around the Mediterranean Sea, setting up outposts in those countries. These lasting outposts are to be accepted as a permanent presence in foreign countries. A few centuries after the Phoenicians civilization, the Silk Road trading routes was built to connect Europe with Asia, and this is considered a foreign investment in the countries it passed through. In the early fifteenth century and onwards, Western European states began to establish permanent colonies in the locations they had previously visited because of their trade missions. These can be described as the world's first multinational corporations.

FDI started in the beginning of the 19th century. In that period FDI started to grow at a faster pace. This growth has been influenced by a number of factorsthe most important of which is probably the change of the market in which the firms operated. The stock of FDI in 1914 was valued at around $14 billion and the UK was the largest source of investment, followed by the United States and Germany; on the other hand, the United States was also the largest recipient of FDI. (International Finance Corporation 1997).

Table 1. The Global Stock of Foreign Direct Investment by Recipient Area ($ billion)

	1914
Developed Countries	5.2 (37.2)
Developing countries	8.9 (62.8)
World	14.1

Source: Dunning, (198 Table 3.2)

At the beginning of the 20th century, a large part of the world's infrastructure was developed by foreign direct investment. Some examples of such investment are electric power in Brazil, telecommunications in Spain, and German chemical companies expanding outside Germany. British firms invested even earlier in manufacturing consumer goods abroad.

Multinational companies began to gain their position in foreign markets not only through trade but also by investing in those countries in the form of foreign direct investments. Globalisation allowed these firms to exploit all world markets, and, with the help of new technology, it became possible for FDI to spread rapidly. Although some scholars see FDI as a solution to various global problems, on the other hand, other scholars think that FDI is the very instrument through which global calamities are caused.

Nowadays, the effects of globalisation are re-dimensioning the way governments, businesses and families are organising their life activities. Regardless of the

recognition of this phenomenon and its importance, globalisation remains among the most important debates regarding the impact it has on the economy, society, and politics.

Multinational companies are the business form that carries globalisation around the world, and FDI is an important method firms use for their global growth strategies. Multinational companies can enter a foreign market through foreign trade by exporting, which is the simplest and least risky way by which a firm can enter the foreign market. When companies enter a foreign market through direct investments in production or in other ways and exercises significant control, then we are dealing with FDI (Shenkar, 2007).

Shenkar (2007) describes the difference between FDI Flow and FDI Stock:

1. The flow of FDI refers to the amount transferred during a certain period of time. FDI is outgoing when it leaves a country, while it is ingoing when its flows into a country, i.e., when foreign firms undertake direct investments in the host country.
2. FDI stock refers to the total accumulated value of foreign-owned assets at a given time.

According to Ivy Panda, (2020) the labour market is greatly affected by the effects of globalisation. On the one hand, it negatively affects the competitive labour markets of a country by bringing workers from other countries but, on the other hand, it also has a positive effect because it redistributes offer, thus providing more homogenisation. Both of these opposing viewpoints can be supported by Foreign Direct Investment. In order to see how FDI affects the labour market, specific studies should be done. At the beginning of the 20th century, developing countries focused on exploiting their natural resources and building national infrastructure. To finance these investments, more and more foreign direct investments were required.

The rise in prices in the 1970s had an impact on foreign direct investment by encouraging the growth of FDI in the hydrocarbon sector. On the other hand, the surplus in the balance of payments in these countries helped them provide their own means to finance their projects and to recycle money in developing countries through loans. Under these conditions, countries are more attracted towards loans than towards attracting FDI.

In 1980, the prices of goods and services began to fall, interest rates increased, countries were beginning to feel the first effects of the economic review consequent to the debt crisis. Countries that at the beginning of the 1970s had a domestic economic orientation were suffering the consequences of low productivity, lack of competition and isolation from the global economy. Under these conditions, these economies began to draft new policies for a more sustainable economic development, turning their economies towards the private sector, international trade, and competition. A series of measures were taken to make these policies effective, such as reduction of tariffs, drafting policies to attract FDI and facilitating conditions for the development of private business. All these led to the increase of foreign direct investments after the 1980s.

In the 1990s, the privatisation of public properties and the opening to foreign markets led to an increase in the stock of foreign direct investments throughout the world.

After 1990, foreign direct investment (FDI) flows continued to set new records in 1999 when global inflow reached $865 billion. This global increase of 27% was not balanced in the three-country group/three country-groups. FDI flows to developing countries reached a value of 208 billion, an increase of 16% in 1998 (UNCTAD, 2000). Looking at it from a short-term perspective, the main reason for the increase in foreign direct investments is attributed to the opening of markets as a result of the removal of economic borders between countries. Looking at it from a long-term perspective, the increase in foreign direct investments is attributed to international production — production under the common governance of transnational corporations.

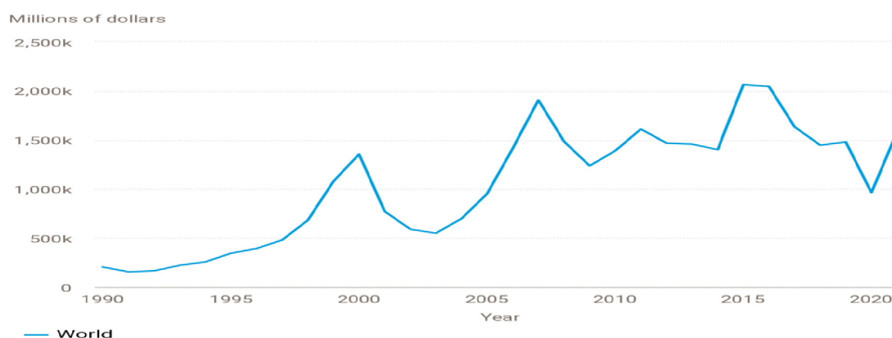
In this period, the global gross product gross world product attributable to foreign was about one-tenth of the global GDP, compared to 5 in 1982. The ratio of the stock of FDI to global GDP increased in that period from 6%to 16%.

There are several reasons for the expansion and deepening of international production in that period according to UNCTAD; (a) liberalisation of FDI (and related) regimes and (b) the recognition that FDI can contribute to a firm's competitiveness.

2.3 Current Developments

Foreign direct investments are very important nowadays in the international arena. UNCTAD's World Investment Report (2022) shows that global foreign direct investment inflows (FDI) reached the value of $1.3 trillion in 2000, $1.9 trillion in 2007, $2 trillion in 2005, the highest value since 2008 crisis. Global foreign direct investment (FDI) grew 64% in 2021 compared to 2020, reaching nearly $1.6 trillion.

Figure 2. Foreign direct investment inflow, 1990-2021



Source: UNCTAD World Investment Report 2022

Starting from 2015 FDIs present a downward trend, for three consecutive years Global FDI flows also continued their slide in 2018, falling by 13% to $1.4 trillion from a revised $1.6 trillion in 2017. In the first half of 2019, global FDI flows also decreased by 20% compared to the last half of 2018. Despite this decline, direct investments are still one of the most important factors in the global economy for both developed and developing economies.

The Covid-19 epidemic had a devastating effect on countries' economies, quickly affecting all businesses. Developed and developing countries designed economic support programmes to deal with the crisis. According to UNCTAD, FDI fell dramatically in 2020 during the COVID-19 pandemic Global FDI flows dropped by 35% in 2020. This is almost 20% below the 2009 financial crisis level.

Developed countries took the biggest hit, where FDI inflows fell by 59%, while developing countries had a moderate decrease of only 9% in FDI flows.

This period was also significant for FDI: although the pandemic had a negative impact on FDI flows, it -also provided an opportunity to reflect on it.

2.4 Types of Foreign Direct Investment

FDI is one of the three components of capital flow, which are divided into two types, namely Foreign Direct Investment by target and by motive.

Types of Foreign Direct Investment by target -There are two main reasons that businesses become multinational: to serve a foreign market, thereby increasing their profits, and to obtain lower cost inputs. These two main reasons are used to distinguish between the two main types of FDI: horizontal and vertical.

a. Horizontal FDI. A company establishes the same type of business operation in a foreign country as it operates in its home country. This is called horizontal when companies duplicate the same business activity in other countries. The reason why these companies enter a foreign market is the high economic costs of exporting their products to those countries, e.g., transportation costs, customs fees, the distance from economic centres, etc. Yokota (2005), based on the view of Helpman (1984), Markusen (1984) and the empirical study of Hanson *et al.* (2001), analyses that horizontal FDI mostly aims to sell products in markets similar to the size of that in host countries, while vertical FDI aims to export products from the mother country to the host country.

b. Vertical FDI. Vertical FDI is also known as efficiency seeking and occurs when multinational companies invest in different countries, fragmenting production in order to produce at low cost. One of the main reasons for product fragmentation is the price of production or input factors. When prices of production factors or inputs are low in host countries, the company has an interest in investing a part of its product manufacturing there because it lowers the cost. For example, many companies carry out part of their production processes in countries that have a relatively cheap labour cost. Besides, vertical FDI seeks to use advanced technology if its use minimises the cost of production (Alma Zisi, 2004).

c. Merge and Acquisition. Cross-border merges occur when operations assets of firms from multiple countries are combined to establish a new entity. When firms are in financial difficulties or they want to become more powerful in markets, two or more firms may merge into one. The most common form of mergers and acquisitions is aimed at firms in developed countries. Large corporations make acquisitions of other firms (usually in host countries) for reasons of expansion. Mergers of firms mostly offer positive advantages, as they increase efficiency, reduce production costs, and provide opportunities to expand in the international market.
d. Investment. Greenfield investment is the main target of a host country. It can lead to linkages to the international marketplace. From the very beginning Investments aim to produce goods and services at the lowest cost, using the production capacities of the host country, and are supported by the latter, due to the creation of new jobs, providing further qualifications for employees and influencing the transfer and adaptation of technology. These investments also serve as an incentive for local companies in the host countries, impacting the increase of competition in the country. However, these investments transfer the largest percentage of the benefits they provide to their mother country, positively influencing its economic growth. This is seen as one of the earliest disadvantages of investments for the host country.

Types of Foreign Direct Investment (by motive)

a. Resource seeking. Investment that seeks to acquire factors of production that are more efficient in the host country. It is a strategy that means the main aim of the company is acquiring in foreign markets particular types of resources not available in the home country, or available abroad at a lower cost (IGI Global).
b. Market seeking. It is a strategy that means companies invest to exploit the possibilities granted by foreign markets, motivated by investor interest in serving domestic or regional markets.
c. Efficiency seeking. FDI that comes into a country seeking to benefit from factors that enable the investor to compete in international markets.
d. Strategic asset seeking. First proposed by John Dunning (Dunning, 1993, Dunning & Narula, 1995),
it is a tactical investment to prevent the gain of resources by a competitor. Strategic asset seeking describes FDI by an emerging economy's MNEs (e.g., Deng, 2009; Rui & Yip, 2009; Cui, Meyer & Hu, 2014).

3. Conclusions

The analysis above shows that there is a positive correlation between FDI and gross domestic product (GDP) growth, but also between FDI and the state aid granted within the Balkan region. The growth trend of the GDP predicted the trend in FDI, while, with a time lag of two periods, the trend in the state aid granted predicts the trend in FDI.

In recent years, the process of economic development of countries helped by FDI has increased the opportunity for economic growth, improved the balance of payments, increased exports through improving the trade process and implementing a new knowledge environment, created a more skilled labour force and increased employment rate.

Countries in the region, including Albania, have had positive effects from foreign direct investments in their economy. FDI can be used as a powerful growth driver for the local economy because of increasing capital inflow into the country, introducing new technologies, increasing productivity, improving environmental conditions, creating jobs, raising living standards. Balkan countries still have high and underdeveloped potential in attracting FDIs in many sectors, such as manufacturing, agro - processing, agriculture, technology, tourism.

According to a report of the "Albanian Investment Development Agency", there are ten reasons why an investor should choose the Balkan region, including Albania, namely, strong economic performance, favourable geographical position, free market entry, business friendly legislation, high potential for investments, low taxes, labour force, increasing foreign investment flows, improving infrastructure and improving the quality of life; however, it still needs to create some capacities. One of the most important sectors with high potential for growth is agriculture and agro industry, which requires investments to develop and increase market competitiveness.

There are so many reasons why the study of FDI is important and some of them are presented below:

a. ***FDI is associated with the transfer of technology***. Thus, Moosa (2002) gives the main reasons why foreign direct investment should be studied, arguing that FDI is associated with the transfer of technology, as well as managerial, technical, and marketing knowledge.
b. ***Market size is related with foreign direct investment***. A special place is occupied by the main determinants of FDI. Chakrabati (2001), Walsh and Yu (2010) argue that market size is among the main determinants of foreign direct investment absorption.
c. ***Human capital is related with FDI***. In their works, De Mello (1997), Noorbakhsh *et al*. (2001) and Campos and Kinoshita (2002) argue that there is a positive relationship between FDI and human capital for countries that have a certain level of human capital. While Lipsey and Kravis (1982), Edwards (1990) and Easterly (2001) point out that the host country's infrastructure plays an important role in attracting FDI.
d. ***FDI affects wages***. Lipsey (2002) argues that FDI affects the wage level as a result of the entry of foreign firms or their participation in a certain industry. According to Wang (2009), FDI conveys positive effects as it transfers advanced technology.

e. ***FDI affects the flow of capital***. Moosa (2002), analyses the effects of FDI in host countries. According to him, FDI positively affects the flow of capital. Vernon's (1966) Product Cycle Theory explains nteractions between ownership-specific advantages and location-specific advantages, best describing the role of technology in international trade.
f. ***FDI affects financial markets.*** Aliber (1970) explained FDI through the relationship of financial markets where foreign investing firms have to cope with the imperfections of capital markets and exchange rates.
g. ***FDI is oriented towards the markets.*** Trajko Slaveski and Pece Nedanovsk, in their work on Balkan countries, point out that Bulgaria has been among the more successful Balkan recipients of FDI, while Greece has been a major source of FDI for the transition economies of the Balkan region. Greek investment is driven in part by the availability of low-cost labour in the neighbouring transition economies.

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