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MASTER'S THESIS

**THE CHARACTERISTICS AND EFFECTS OF FOREIGN DIRECT
INVESTMENT IN SLOVENIA**

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LIST OF ABBREVIATIONS

sl. - Slovene

bn – billion

CEE – Central and East European States

GDP – Gross Domestic Product

GVC – Global Value Chain

tn – trillion

EU – European Union

FDI – Foreign Direct Investment

m – million

MNE – Multinational Enterprise

M&A – Merger and Acquisition

n.a. – not available

OECD – Organization for Cooperation and Development

RS – Republic of Slovenia

SPIRIT – Public Agency for Entrepreneurship, Internationalization, Foreign Investments and Technology

SURS – Statistical Office of Slovenia

TNI – Tuje neposredne investicije

UNCTAD – United Nations Conference on Trade and Development

USD – United States dollar

WIR – World Investment Report

INTRODUCTION

Foreign Direct Investment (FDI) and its role in globalization and economic development has been debated in academia and policy making for many decades. International business activity is by no means a recent phenomenon, yet, the concept of FDI remains elusive, as the characteristics of cross-border investments have evolved over time. As FDI began to emerge, it stood for a flow of capital typically streaming from big multinational enterprises (MNEs) from developed, industrial economies to developing countries. Traditionally, the objective of cross-border investment was to exploit natural resources of the latter, or simply to substitute trade as a mean to serve domestic consumption markets (Qiang, Echandi, & Krajcovicova, 2015). The overall expectation of this simplified business equation was that the gains from FDI in terms of economic growth and business performance would be easily identified and measured empirically, however, over time this has proven to be elusive (Castro, 2000).

Today, FDI represents an integral part of an open and effective international economic system and a major catalyst to development (OECD, 2002). Contrarily to other forms of cross-border investment (i.e. foreign portfolio investments), FDI seeks to establish a long-term relationship in a country of investment. The long-term link with a foreign affiliate means creating a relationship that is not as easily breakable and as consequence-free as merely investing excess funds into a prospective foreign enterprise. Choosing a host country to invest in is a complicated process, involving looking at a bigger picture than just a momentarily return on investment. Additionally, the established relationship works both ways. Not only the investing company, but also the host country where the investment is made can benefit and profit or be negatively affected from the link (Chen, 2019). The correlation between FDI inflows into host countries and economic development has been subject to extensive studies ever since the emergence of FDI. However, the theoretical and empirical literature have not yet reached a conclusion as to whether and how foreign investment affects the host economies and companies. Various researches have proven FDI yields economic effects, both positive and negative, though it has also been proven that these effects are conditional. The existing relevant studies commonly suggest that the benefits of FDI do not occur and accrue automatically and evenly across countries, sectors and local communities (Buzdugan & Tuselmann, 2018).

FDI is perceived as an important factor in economic growth also in the Slovenian economy. General orientation of Slovenia as a host country is openness to foreign investors and incoming FDI. According to the Bank of Slovenia, the value of foreign investments in Slovenia has been continuously growing over the last 30 years. This growth in value of inward FDI can be attributed to the stability of the business environment and macroeconomic indicators, a stimulating investment environment and regulated legislation in the area (Bank of Slovenia, 2019). However, to this day, the levels of inward FDI in Slovenia are still relatively low in comparison to other comparable countries, in terms of size and development. Nevertheless, so far, FDI in Slovenia has

shown to have a relatively important positive influence on the development of Slovenian economy. The survey results on participation of foreign equity firms in the Slovenian economic environment, carried out by Center of International relations (CIR) from Faculty of Social Sciences, University of Ljubljana and commissioned annually by the Slovenian Public Agency for Entrepreneurship, Internationalization, Foreign Investments and Technology (SPIRIT), continuously suggest that, on average, foreign-owned companies mostly grow faster in comparison to the Slovenian average in terms of sales revenue, exports, number of employees and added value per employee (Jaklič, Koleša, & Knez, Tuji investitorji o slovenskem poslovnem okolju 2018, 2018). Inward FDI however still remains a point of debate in Slovenian political and economic environment, with no consensus on the impacts on the national economy.

The goal of this master's thesis will be to analyze FDI trends, benefits it can generate and also the potential negative effects FDI can bring to the host country, applied to the case of Slovenia. The purpose of the thesis is to prepare managerial and policy implications that will support faster productivity growth and economic development by exploiting the benefits of FDI, while considering also possible drawbacks. Key research goal of this master's thesis is to answer the question about what type of investment and what types of companies foreign investors choose when deciding to invest in Slovenia and what are the effects arising from the inward FDI.

The theoretical part of the thesis firstly focuses on definition of FDI, FDI effects as defined in the economic theories, current FDI trends, most commonly cited FDI effects on the host countries, supported by the selected empirical researches of various case studies. Following, the theoretical part presents an overview of current state of FDI and its characteristics in Slovenia as a host country. The described research, based on relevant secondary data, serves as a foundation for understanding of the research problem and as a support for the empirical part of the thesis. The empirical part consists of analysis of the data gathered from the existing statistical databases. The data was used to test existing theoretical opinions about FDI on a case of Slovenia and to measure trends identified in the theoretical part of the thesis. The limitations of my research are connected to the availability of data, especially regarding more recent information, as the majority of publicly available statistical data is published with a certain delay in years. Furthermore, different statistical offices apply different methodologies when collecting the data on number of companies in foreign ownership in Slovenian corporate environment and their performance, which results in quite significant discrepancies in collected data. Due to limitations related to the accessibility of the data for the purpose of the quantitative research on the effects of FDI on domestic companies, the research in the empirical part is also based on survey results gathered by another organization – SPIRIT Slovenia in cooperation with CIR, Faculty of Social Sciences. The results of the quantitative research are interpreted in conclusion of this thesis, and the obtained findings summarized in light of the fundamental goal of this master's thesis.

1 THEORETICAL FRAMEWORK AND OVERVIEW OF EMPIRICAL LITERATURE

1.1 Definition of FDI

FDI represents a form of cross-border investment aimed not only at moving capital to a prospective enterprise and earning a return on the investment but establishing a lasting link with a foreign enterprise. The OECD definition states that FDI is a '*category of cross-border investment made by a resident from one economy with the objective of establishing a lasting interest in an enterprise that is resident in an economy other than that of the investor. The 'lasting interest' implies the existence of a long-term relationship between the direct investor and the direct investment enterprise and a significant degree of influence on the management of the latter*' (OECD, 2008). Contrarily to foreign portfolio investments that can be easily adjusted to the changing short-term conditions in the host country, FDI is much less flexible in terms of withdrawing the investments from the unfavorable business environment.

Initiated by the start of the globalization process, FDI introduced the emergence of global companies, i.e. MNEs, that consist of parent company and one or more domestic or foreign affiliates owned and controlled by the parent. FDI is closely linked to MNEs, as it is MNEs that typically generate FDI flows, through a variety of different ways. These include opening of a subsidiary or associate company in a foreign country (i.e. greenfield investment), by means of merger, joint venture with a foreign company or by acquiring a controlling interest in an existing foreign company. The generally accepted, though variable, threshold for FDI to establish a controlling interest or gain an active role in a foreign enterprise is at a minimum of 10% ownership, as determined per guidelines of OECD and International Monetary Fund (IMF) (Johnson, 2005)

FDI can spur wider effects than solely on the company that receives the investment and can help contribute to the efficiency and growth of the recipient country's economy. It can help foster and maintain economic growth, both for the recipient country and for the country making the investment. The most commonly cited positive contributions of inward FDI to the development of the recipient country are additional resources and abilities in the form of capital, technology, organizational, management and other skills and access to foreign markets brought by foreign investors (Zeilhofer & Zobavnik, 2015).

Different types of FDI are likely to have varying impacts on the host economy and it is pertinent to understand and identify them separately. The distinction by type usually offers insight not only in terms of FDI volume, but also into its likely economic effects. According to Bruno and Cipollina (2014) impacts FDI can produce on the host economy are conditional upon the:

- mode of entry (greenfield, merger and acquisition or takeover),

- type of FDI (horizontal, vertical, or conglomerate)
- reasons why MNEs make such an investment (market seeking, resource seeking, efficiency seeking, or strategic assets seeking FDI) and
- the nature and capacity of the host country (absorptive capacity) (Bruno & Cipollina, 2014).

By mode of entry, FDI takes place either when ownership (at least 10%) of existing enterprise is transferred to a foreign investor or FDI can serve as a mean for direct investor to establish a new enterprise in a host country. The initial investments into target country, when a foreign parent company builds and operates a new venture to produce goods locally, are referred to as greenfield investments. They generally mean establishing of a new subsidiary of an existing foreign enterprise, which enables the highest integration into the foreign market for the investor. In this case, there is typically no existing suitable candidate for takeover on the market. On the other hand, establishing a business relationship with an already existing target on the market through means of merger and acquisition (M&A) allows quicker access to foreign market for the acquired domestic affiliate (Chen, 2019). Takeover is also commonly done through M&A, with the acquirer of the company taking over the majority stake in the target. Advantages of this strategy from the investor's perspective are acquisition of existing customer base, suppliers, sales channels, already trained personnel, equipment, reputation and brand of the acquire (Johnson & Turner, 2010). From the perspective of the host country it is generally considered that M&As do not bring significant changes in the performance of the acquired target in the host country (such as production, employment, turnover etc.), unless in certain cases of restructuring. A sharp distinction is therefore drawn between greenfield investments, which provide fresh capital, additional jobs and instantaneous introduction of new technology, and M&As that typically target the already strategic sectors and 'national champions' which ultimately leads only to change in ownership in an existing corporate entity (OECD, 2008). On the other hand, when it comes to FDI's influence on other domestic firms, that are not in foreign ownership, entry through M&A is expected to generate wider inter-sectoral linkages with domestic firms than greenfield investment, due to domestic affiliate's pre-integration in the local economy (Crespo & Fontoura, 2005).

FDI by type, is commonly categorized as horizontal, vertical or conglomerate and defines also channels through which FDI effects trickle to domestic economy. A horizontal investment refers to investor establishing the same type of business operation in a foreign country as it operates in a home country. A vertical investment refers to establishment or acquisition of business activities in a foreign country that are different from the investor's main business, however, still related to it. Finally, a conglomerate type means a foreign investment is made into a business that is unrelated to investor's existing business in its home country (Chen, 2019).

Diving into more fundamental reasons, why FDI is initiated in the first place and how it affects the host country, we notice that any investment is strongly contextual in a sense of the country or region of the investing firms and the ones in which they are seeking to invest, the industry and the nature of the value-added activity in which the firms are engaged. Based on this contextual variable, scholars have identified four main types of foreign based MNE's activity:

- Market-seeking or demand oriented investment,
- resource-seeking or investment made to gain access to natural and other resources,
- efficiency-seeking investments that aim to increase their cost efficiency by transferring production to low labor costs locations or exploit other comparative advantages of host country; and finally
- strategic asset seeking FDI that uses assets acquired abroad to enhance the operations of the investor in other markets (Dunning, 2000).

Any type of FDI under certain conditions can provide means for creating direct, stable, and long-lasting links between foreign investors and host economies. Foreign investment can influence growth by raising productivity and the efficiency of resource use in the recipient economy, beyond what domestic investment would normally trigger. The existence and size of FDI effects vary across different contexts. Theoretical considerations suggest that different kinds of FDI may each have different economic, social, and environmental impacts, which are primarily connected to host country's predispositions, notably for different levels of development supporting different types of FDI, typically referred to as absorption capacity (Meyer & Sinani, 2005). The fundamental question is whether a certain type FDI represents an efficient path toward economic development and industrial upgrading for a particular host economy (Bruno & Cipollina, 2014).

1.2 Impact of FDI on economic growth

Under the right circumstances, FDI can have important complementarities with local industries that stimulate development in host economies (Gugler & Brunner, 2007). Especially in developing countries which typically lack sufficient capital, FDI can have an important role acting as a foundation for economic growth. Consequently, participation of countries in the worldwide FDI has expanded steadily over the past three decades, especially with number of developing countries and countries in transition starting the processes of market liberalization. Thus, over the years the number of markets to which foreign investors were able to invest their savings has grown considerably. As developing economies became increasingly involved in the international competition, it became more important for their firms to compete with MNEs from other countries, both domestically and on foreign markets. However, competition in the market due to MNEs can either foster or suppress the domestic productive forces, as the levels of concentration

in host countries tend to increase and there is always the possibility of foreign firms out-competing local firms and forcing them out of the market. In the presence of crowding-out effect FDI can thus also cause negative externalities, as the negative competition effect dominates the positive effects of technology, know-how and other beneficial effects (UNCTAD, 2006).

When measuring the effects of foreign investment on the host economy, we distinguish between effects tied to the foreign ownership of affiliates or subsidiaries and so-called spillover effects on the broader local economic environment. In other words, the impact can be direct (on the foreign subsidiary) or indirect (on fully domestic firms), with the latter dividing further in horizontal (intra-industry effect) or vertical (inter-industry). Vertical effects also subdivide into forward linkages (downstream domestic customers) and backward linkages (upstream domestic suppliers) (Bruno & Cipollina, 2014). Direct FDI contribution to the economic growth typically occurs through additional capital inflows, transfers of technology, know-how and management skills and direct access to foreign markets provided by the foreign investor. On the other hand, prerequisite for the indirect effects of knowledge spillovers from foreign affiliates on domestic firms is adequate absorption capacity of the domestic economy and enterprises (Damijan, Knell, Majcen, & Rojec, 2003). In other words, the positive effects of FDI spillovers grow with local skills and competition (Blomstrom & Kokko, 2001).

Common suggestion of the relevant economic theory is that any type of FDI under certain conditions can become a source of financial stability, new ideas, technologies and working practices for the host country. The consensus of the literature studying the FDI effects is that countries differ in terms of market potential, needs of customers, level of income, economic development, labor productivity, technology level, competition intensity, infrastructure etc. The benefits from internationalization are thus different for each country. Essentially, this means that the policies to make the most of FDI certainly need to be context-specific. The challenge for each host country is to establish a favorable environment to attract and retain the right type of FDI and at the same time focus on promoting upgrade of the activities and investments of existing FDI. The latter consists of pursuing development of the right labor force to engage with the new activities, investing into relevant infrastructure to support reliable supplier networks and adapt legal and policy framework in a way that facilitates establishment of long-term relationships between foreign investors and local firms (Buzdugan & Tuselmann, 2018). Host countries' governments and other relevant parties thus need to create a transparent and effective enabling policy environment for foreign investments and foster human and institutional capacities to implement them (OECD, 2002).

Without regulations, FDI can gain a lot of market power and control on the domestic market of the host country, especially in cases of weaker regulatory capabilities of a government in a host country (Gachino, 2007). A study by Buzdugan & Tuselmann (2018) argues that it is not about the volume of inward FDI, but the quality of both

attracted and existing FDI, which can only be properly managed with the appropriate industrial policy. Evidence shows that solely liberalization of trade and investment alone has been insufficient in promoting economic growth. In this context the term industrial policy refers to state intervention with attempt to promote FDI more actively on micro and macro level. This is especially important for low and lower-middle income countries that are at risk of harming development and upgrade of their domestic production, especially if their production is dominated by low value activities (Buzdugan & Tuselmann, 2018)

There are several channels through which FDI can affect economic growth of the host country. A common starting point of theoretical studies is suggestion of higher productivity of foreign firms in contrast to their domestic counterparts, which can then benefit from the connection with MNEs and their foreign affiliates. However, theoretical studies present contradicting results in terms of positive and negative effects of FDI on host economies. The purpose of detailed overview of channels through which FDI can have an impact on economic growth presented in Table 1 below, is to determine the net effect a country hosting FDI can expect.

Table 1: Channels through which FDI can have an impact on economic growth

Channel	Influence description	Selected references
Capital increase	Adding to the capital stock, supportive or complementary role to local investments opportunities for other companies	Early studies by Caves in 1974 on Australian and by Globerman in 1979 on Canadian manufacturing sector found evidence of positive effects on positive correlation between foreign presence and sectoral productivity of local firms (Caves, 1974, Globerman 1979, as cited in Gachino, 2007). It is, however, disputed that early models from late 1970 failed to distinguish the role played by FDI from own economic development of host country.
Integration into global value chains (GVCs)	Enabling direct access to foreign markets through established networks of foreign investor, integration into GVCs, diversification of exports	Case studies show that many developing countries that have been successful in upgrading and diversifying their exports through inward FDI, achieved higher growth rates on the long run in comparison to those that simply keep trying to expand with goods and services that

(table continues)

Table 1 Channels through which FDI can have an impact on economic growth
(continued)

		were traditionally their comparative advantage in terms of exports. The experience of different developing countries such as China, the Czech Republic, Costa Rica, Malaysia, Mexico, the Philippines and Vietnam, are such examples of how FDI has been a key initiator of integration into GVCs and achieving higher growth rates (Moran, 2014).
Technology transfers	MNEs typically possess superior technology and skills that can be transferred through foreign investment either directly to the firm receiving the investment or indirectly through downstream or upstream linkages to domestic competitors, suppliers or customers.	Studies by Damijan, Knell, Majcen and Rojec (2003) and Damijan, Rojec, Majcen and Knell (2008) focusing on impact of FDI on productivity of transition countries from CEE region identified higher productivity of foreign owned firms due to technology transfer to previously domestically owned companies. Damijan, Knell, Majcen and Rojec (2003) also identified positive backward vertical technological spillovers to local firms in Czech Republic, Poland and Slovenia. On the other hand, Javoricik and Spartareanu (2003) found that positive technology spillovers to domestic firms are generated only by firms partially owned by foreigners.
Human capital enhancement	Direct effect of creating additional jobs and indirect effect through training of local workforce, implementation of advanced management skills	Evidence on direct effects found in studies by Girma and Görg (2006) and Conyon, Girma, Thompson & Wright (2002), both identifying higher productivity of foreign firms in comparison to domestic in the UK, based on findings that foreign

(table continues)

Table 1 Channels through which FDI can have an impact on economic growth
(continued)

		acquisition had positive effects on labor productivity of acquired firms.
Increased competitiveness	Incentive for domestic firms to increase their productivity and efficiency, to be able to compete better with foreign counterparts. On the other hand, foreign firms can also cause a negative competition effect by out-competing local firms and forcing them out of the market	Aitken and Harrison (1999) found negative impact from foreign presence on domestically owned firms in the same sector in Venezuela due to market stealing effect.

Source: Own work.

1.2.1 Increase in capital for investment

As researched by Amighini, McMillan and Sanfilippo (2017), FDI can play an important role in financing of development in host countries, both directly as an external source of capital, and indirectly through its impact on domestic capital formation (Amighini, McMillan, & Sanfilippo, 2017). The capital investment, in the context of FDI, is thought of as a direct, debt-free way of adding to the capital stock of the host economy. Capital inflow in its essence causes direct accumulation of more capital in the receiving companies and countries. Due to its long-lasting interest factor, FDI is a more stable source of capital in comparison to other forms of private equity flows, which is especially relevant for the emerging and developing markets, where capital is relatively scarcer (Gachino, 2007).

By acting as a stable source of capital, FDI can spur industrial development and play a supportive or complementary role to local investments. It can provide direct financing for acquisition of new plants and equipment and be an important catalyst for economic restructuring. Helping enterprises to get started can lead to creation of additional jobs which can lead to increase in general household income levels and thereby increased consumer demand. This type of development can often lead to opportunities for other companies, helping to further induce economic growth of the receiving country (Bruno & Cipollina, 2014).

The positive impact of foreign capital on the recipient economies can, however, be conditional on the kind of business activities carried out by foreign affiliates. Direct effects of FDI can be in many cases fully internalized by foreign affiliates (firms receiving the foreign capital) (Hale & Xu, 2016). Thus, it is important for host countries, to attract and retain the type of FDI that is more likely to foster domestic capital accumulation (Amighini, McMillan, & Sanfilippo, 2017).

1.2.2 Integration into the global economy

Through globalization process and accompanying decrease in trade barriers, easier access to foreign markets, uniformizing consumer tastes and progress in transport and communication, FDI introduced the fragmentation of supply chains and the emergence of global companies. Nowadays, the international dispersion of tasks and production processes represents complex network systems, typically coordinated by MNEs. These systems are commonly referred to as GVCs (UNCTAD, 2013). In an increasingly interdependent international economy, prosperity of countries and their enterprises depends highly on the participation in GVCs (Echandi, Krajcovicova, & Qiang, 2015).

FDI should not be perceived as a substitute for trade but as a mean to integration into the global economy. UNCTAD (2002) finds that MNEs can help enhance and sustain export competitiveness of the host country. For example, through diversification of exports, improvement of technological and skill content of export activity, enlargement of local firms to meet the global demand, reduction of entry costs to foreign markets for local firms accessing foreign markets through MNEs, gaining access to MNE's distribution networks, GVCs and marketing knowledge (UNCTAD, 2002).

Thus, FDI effects on trade must be measured in terms of broader perspective than the direct impact of investment on increase of imports and exports. The main trade-related benefit of FDI lies in the increased outward orientation. Foreign affiliates tend to be more outward oriented than fully domestic companies, as they are being more aware of the opportunities of foreign markets. As countries develop, through development and strengthening of international networks, FDI can help with their further integration into the global economy (OECD, 2002).

1.2.3 The transfer of new technologies and know-how

Technology transfers are perceived as one of the most important channels through which MNEs can positively impact the host country with their presence (OECD, 2002). To compete in the highly competitive arena of international trade, firms need to constantly improve their performance and efficiency. Due high competition on the international markets, MNEs are compelled to make continuous changes, more than the local firms, in order to compete. These changes relate to MNEs production process, quality of their products, management skills and continuous technological innovations (Gachino, 2007). Therefore, a commonly accepted analytical starting point regarding positive effects of FDI is presumption that MNEs possess superior technology and skills. As MNEs are perceived as more skill-intensive and more productive than local firms, it also perceived that they are able to produce more sophisticated products (Pham, 2016). For MNEs, this represents the competitive advantage, which helps to them to compete successfully with the local firms, that typically have the advantage of having superior knowledge of local markets, consumer preferences and business practices (Torlak, 2004).

Regrading different channels, benefits to the host economies in a form of technology transfer arise from foreign firms demonstrating new technologies to competing or complementary companies in the same industry, providing technological assistance through vertical linkages to their local suppliers and customers, training workers who may subsequently move to local firms and the internationalization of R&D. Through FDI, skills of international competition are also likely to be transferred to local firms. Consequently, local firms are forced to learn and introduce new approaches to be able achieve technical efficiency and enhance their competitiveness. All of this can introduce new technologies to the local firms earlier than if it would be happening with own technological development (Fan, 2002).

The technology spillover effects, however, depend on the relevance of the foreign technologies transferred for the host country business sectors. Further relevance is also assigned to the size of the technology gap between domestic enterprises and foreign investors, as it should not be too big for FDI to have a positive impact (OECD, 2002).

1.2.4 Enhancement of human capital and knowledge transfer

The enhancement of human capital is a consequence of and a complement to technology transfer (Gugler & Brunner, 2007). As previously indicated, the transfer of technology from MNEs to domestic firms, does not only take place by transfer of machinery and equipment. A considerable contribution to the transfer is also realized through the training of local employees and implementation of advanced management skills. Besides the direct effect of creating additional jobs, MNEs must train employees so that they are able to follow the practices or technology in the affiliate company. Once individuals are employed by MNEs' subsidiaries, their knowledge and skills may be enhanced through training and on-the-job learning. As experienced workers leave the foreign firms, the enhanced human capital becomes available also to domestic firms. Thus, a major factor in knowledge and technology transfer is movement of labor within the foreign company and between foreign and domestic companies. Most of the recipients of training are employed in the MNEs' own affiliates, however employees among the MNEs' suppliers, subcontractors and even customers are also included (Blomstrom & Kokko, 2001).

The overall effect of FDI on national economic performance is argued to depend upon whether recipient countries have already attained minimum levels of human capital and technological development. This means that the domestic firm already needs to already sustain technological knowledge and human capital at a certain level. Considering effects on the national economy, for example, countries with higher levels of human capital may be more attractive to technology intensive foreign MNEs that can significantly contribute to further development of labor skills. On the other hand, host economies which have weaker initial conditions in terms of labor and technology are likely to attract foreign firms that will likely use simpler technologies when entering on the market and thus have lesser effect on local learning and development of skills (Blomstrom & Kokko, 2001).

1.2.5 Increased competitiveness in domestic industry

There is still no unanimous answer in the literature regarding the question about the nature of competition effect of FDI. Specifically, whether the pressure arising from entrance of foreign firms should be seen as positive or negative with regards to impact on the productivity of the competitive national firms in the host economy (Torlak, 2004). Pressure on domestic competition initiated by the presence of foreign enterprises may have a positive effect on economic development by initiating higher productivity, lower prices and more efficient resource allocation. The foreign competition might operate with better technology or more efficient managerial and business processes, which encourages domestic firms to upgrade their methods to reach a similar standard of development. This way, the competition effect works by setting a set of expectations for the host country's firms to meet. Increased rivalry forces local firms to act and to innovate (OECD, 2002).

However, competition in market due to MNEs can also suppress the domestic productive forces. There is always the possibility of FDI out-competing local firms forcing them out of the market and causing negative externalities when the negative competition effect dominates a positive technology effect. The entry of MNEs tends to raise the levels of concentration in host-country markets, which can also hurt domestic competition. In the presence of crowding-out effect, domestically-owned firms have lower levels of productivity as their fixed costs are spread over a smaller scale of production (OECD, 2002). Supporting this theoretical assumption on the need for pre-existing levels of economic development prior to the FDI inflows, Pham (2016) points out that based on the empirical research evidence shows that the possibility of MNEs crowding out the local firms in host country is higher in developing than in developed countries, due to the higher technology gap between domestic firms and foreign affiliates in the developing countries.

The main conclusion that can be drawn from the theoretical literature overview is that the economic benefits connected to FDI activity do occur, however are not triggered automatically by the foreign presence. While it has been observed that FDI can have various positive effects on formation of human capital, technology transfers, enterprise restructuring and increased competition, the intensity of these effects depends on the efforts of the host country in the fields of raising education levels, investments in relevant infrastructure and improvement of domestic business sectors (OECD, 2002).

1.3 Case specific empirical evidence of FDI impact on host economies

As concluded in the previous section, benefits of FDI do not occur and accrue automatically and evenly across countries, sectors and local communities. By looking at number of empirical studies based on FDI impacts in countries on different levels of development, the purpose is to assess their experience and challenge the theoretical conclusions. For the purpose of this thesis, the focus will be on the FDI inflows, thus the empirical papers investigating the outward FDI flows are not taken into consideration.

Studies regarding FDI effects on the host economy usually examine the correlation between the productivity of domestic firms (i.e. firm efficiency and output, labor productivity etc.) and their linkages with foreign affiliates. The goal is to answer two main questions:

- whether foreign equity participation is associated with an increase in the FDI-firm's productivity (i.e. direct effects of FDI), and
- whether foreign ownership in an industry affects the productivity of domestically owned firms – i.e. whether there are positive or negative spillovers to domestic enterprises, either on horizontal or vertical basis (i.e. indirect effects of FDI).

While the theoretical literature is consistent with the idea that FDI steers the economy of a host country towards production of more sophisticated goods, promotes exports and incorporates low and lower-middle income countries into higher levels of GVCs, introduces more advanced technologies and thereby also increases the demand for skilled labor, we find that despite a large theoretical consensus on positive effects from FDI, case-specific empirical evidence is relatively rare and contradictory.

1.3.1 Direct effects of FDI

Looking through existing literature on direct effects FDI, we firstly notice, there is a scarce amount of information – especially in comparison to the number of studies on indirect effects. However, contrarily to the contradicting nature of the conclusions drawn from the case studies on indirect effects, that will be addressed later, most papers considering empirical evidence on direct effects conclude with the same message – if direct effects of foreign ownership are present, they are strongly positive.

Number of studies, that are presented in the continuation of the thesis, have compared the performance of foreign-owned and domestic firms, identified superior financial performance among the foreign owned firms (for example Harris and Robinson (2003), Conyon, Girma, Thompson and Wright (2002), Girma and Görg (2006)). Association of foreign ownership with higher productivity of FDI firms has been found in developed and developing countries, irrelevant of type of FDI. Positive effects mostly related to direct technology transfers through FDI and in terms of higher productivity levels and growth. These findings confirm the theoretical suggestions on higher productivity of foreign firms due to their proprietary technology, superior know-how and management techniques as well as ability to attract superior labor force.

Empirical evidence for developed countries, that are typically acting as a source of outward FDI, are rare but consensual. Examples of positive effects on higher productivity were found in a study by Harris and Robinson (2003) concentrating on foreign owned manufacturing plants in the United Kingdom (UK). However, the study also provides empirical evidence that shows foreign investors tend to acquire firms with higher productivity (Harris & Robinson, 2003). A study by Conyon, Girma, Thompson and

Wright (2002) supplies the same result of higher productivity of foreign firms in the UK, based on findings that foreign acquisitions had positive effect on the labor productivity of acquired firms. While Girma and Görg (2006) reached the same conclusion while examining domestic firms in the UK acquired by foreign ones, they also noted that the pre-acquisition productivity of the target plays a role in the rate of technology transfer from the acquiring MNE.

FDI acting as a source of foreign technology transfer and productivity growth, has proven to be particularly important for firms in transition economies, as these were more in need of restructuring. Looking at empirical evidence, Konings (2000) focused on comparison of firm-level data from transition economies Romania, Bulgaria and Poland for the years 1993 - 97. In his study, he found evidence of foreign firms performing better only in Poland, which was the more advanced transition economy in his sample. For other two countries, he suggested, that potential reason for lack of positive direct effects might be that it takes time for ownership effects to have an effect on performance, due to lags in restructuring (Konings, 2000). On the other hand, a more recent study by Damijan, Knell, Majcen and Rojec (2003) investigated impact of FDI on productivity in eight CEE countries from 1995 – 1999: the Czech Republic, Slovenia, Estonia, Slovakia, Latvia, Lithuania, Poland and Romania. The results have found that in 5 of the studies transition countries, FDI acted as an important vehicle of direct technology transfer to domestic firms. In Estonia, Hungary and Slovenia foreign affiliates grew much faster in terms of total factor productivity as compared to local firms, no matter the size of investment, while in Lithuania and Romania faster productivity growth was observed only in the majority owned foreign affiliates. In line with the previous study of Damijan, Knell, Majcen and Rojec from 2003, a study by Damijan, Rojec, Majcen and Knell (2008) focused on data from 10 transition countries from 1995 – 2005 (Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania, Slovenia, Croatia and Ukraine). The study confirmed that direct effects of foreign ownership on firm performance, related to faster growth, are mixed. While they were significantly positive in three countries Czech Republic, Latvia and Slovenia, for other countries, the growth rate of affiliates was also higher than that of domestic firms, but not significantly. However, only in Czech Republic and Slovenia foreign owned firms persistently outperformed domestic firms in terms of total factor productivity growth, as in both countries, firms have shown to make long term productivity improvements after the ownership change. In other countries from the sample, productivity gains were only observed in first year after the change in ownership and seemed to dissipate afterwards (Damijan, Rojec, Majcen, & Knell, 2008).

While the results of empirical studies on direct effects of FDI show mixed results or impacts on performance of firms in foreign ownership versus their domestic counterparts, they generally support the theoretical idea of MNEs possessing superior knowledge and know-how. While the results of FDI effects, when identified, are strongly positive, it has also been noted that ownership effects might take time to have an impact on performance

due to lags in restructuring and that the positive effects are also dependent on productivity of domestic firms before FDI (Konnings, 2000). The positive direct effects of FDI are thus more noticeable in the already developed countries.

1.3.2 Indirect effects of FDI

Spillover effects are defined as transfer of know-how and technology from a firm in foreign ownership to local firms. Empirically, spillover effects are studied at the horizontal level (intra-industry) or vertical level (inter-industry), with the vertical effect subdividing also in downstream effect to domestic customers or upstream to domestic suppliers. More precisely, the channels through which FDI may spillover from foreign affiliates to domestic firms in host country are identified as imitation/demonstration, movement of workers and competition (Bruno & Cipollina, 2014).

According to insights gathered from literature regarding spillover effects, many of the early studies found significant positive effects from the presence of foreign firms on domestic firms' performance in the same industry (Gachino, 2007). Early theoretical models on foreign capital and spillover started to emerge in late 1970 and were pioneered by Caves in 1974 on Australian and by Globerman in 1979 on Canadian manufacturing sector (Caves, 1974, Globerman 1979, as cited in Gachino, 2007). Theirs and other similar earlier studies on FDI spillover effects were focused on horizontal productivity spillovers, i.e. spillovers from foreign presence in the same industry. These industry level studies all identified a positive correlation between foreign presence and sectoral productivity of local firms. Their theoretical approach proposed that the large presence of foreign subsidiaries in host countries leads to increases in the rate of technology transfer and diffusion, increasing the productivity of locally owned companies by enhancing their technical efficiency. The common proposition was that the presence of foreign firms has positive impact on domestic firms' performance, by diffusion of positive externalities or spillovers to the domestic firms through their interaction with foreign firms (Gachino, 2007).

The major critique of the standard model however is that it failed to distinguish the role played by FDI in a country's development from the own economic development of the host country. If positive relationship existed between productivity of local firms and share of foreign firms in a particular industry, that was interpreted as a positive spillover effect of FDI (Gachino, 2007). It might also possible that this positive association is caused by the fact that MNEs tend to target high productivity industries rather than by genuine productivity spillovers. Not only that, one of the possibilities of increased productivity in a certain sector, might be the negative effect from FDI. This means, that by forcing less productive domestic firms to exit the market, MNEs increased their market share, and by being more productive rose the average productivity in the industry (Smarzynska, 2003).

Contrarily to the early studies of FDI, most more recent ones often fail to find evidence on positive correlation between foreign presence and productivity of local firms. There are several studies that find none or negative effects of the presence of multinationals on domestic firms. Aitken and Harrison (1999) conducted a study on Venezuelan plants in 1999 and found an overall negative impact from foreign presence on productivity of domestically owned firms in the same sector. They explain this trend by the fact that the net productivity effect from FDI is dominated by the negative market stealing effect from intensified competition after the entrance of foreign firms. Hence, while on the one hand the foreign presence in an economy may stir some learning processes and produce positive externalities for local firms, it can at the same time result in a negative demand effect, especially in developing countries where the gap in productivity between foreign and domestic firms is higher, which pushes the productivity of local firms automatically downwards (Aitken & Harrison, 1999).

Looking at evidence of FDI effects from European region, we find two studies overlapping in countries of interest and time frame after the year 2000, both coming to similar results. Firstly, a panel data research by Konings (2000) was conducted on 5000 firms in Poland, Bulgaria and Romania and secondly, a panel study by Torlak (2004), used more than 8000 firms in five transition countries: Hungary, Poland, Romania, Bulgaria and the Czech Republic, to observe effects of FDI on firm's productivity in host country. Both identified very little evidence on diffusion of technology from foreign domestic firms. In contrast, there were negative spillovers to domestic firms in Bulgaria and Romania, which indicates that the competition effect from the FDI was dominating the technology transfer spillover. Since Bulgaria and Romania were lagging behind other countries in terms of development, this occurrence might signal that if the technological gap was too large, this truly affects the possibility of spillovers. In Poland and Czech Republic there was weak evidence of technological transfers from spillover effects. Only in Hungary there were interesting positive results even on the national level, showing increased productivity. Torlak (2004) suggests that since FDI in Hungary has occurred a bit earlier than in other countries, this might mean foreign investment takes time to show and effect and also that through time this might be a case of market stealing by more developed foreign competitors. Domestic owned firms can improve their performance to some extent by learning from foreign companies. However, it is important to note that it is possible that they might be forced from the market due to high competition pressure from foreign owned companies before they can start learning from them (Torlak 2004; Konings 2000).

The majority of empirical results highlight the importance of the absorptive capacity of domestic firms, suggesting it to be the fundamental precondition for host countries for being able to capture the indirect benefits from FDI (Crespo & Fontoura, 2005). The question for domestic policy makers therefore does not seem to be whether to attract FDI, but rather how to connect it with domestic investments. One of the questions is also

whether to obtain FDI in sectors in which there is no domestic investment, since the prospects for generating sources of economic growth in this case are even more limited (Kokko, 1994).

While the empirical studies on horizontal spillovers focus on efficiency gains of domestic competitors of foreign affiliate, the studies of vertical spillovers focus on technology and knowledge transfers that occur through interaction of foreign owned firms with domestic suppliers (backward spillovers) and domestic buyers (forward spillovers). It is generally perceived that it is preferable to MNEs to prevent technology leakage within their industry (i.e. through horizontal spillovers). However, it is also perceived that backward vertical spillovers might have greater effects on host economies, as MNEs have an incentive to transfer their knowledge to local suppliers or buyers. Regarding forward vertical linkages, access to sophisticated inputs from MNEs (either products or knowledge), allows local firms to produce more sophisticated outputs. The effects of vertical (as of horizontal) spillovers, however, depend on many factors. One of the decisive roles is the technological gap between local firms and MNEs, as the host economies absorptive capacities are lower if the gap is too large (Huber & Eck, 2018).

There are several studies that cover spillover effects in transition countries. The study by Damijan, Knell, Majcen and Rojec (2003), that identified direct technology transfer to domestic firms as mentioned in section on direct effects of FDI, reported also significant positive backward vertical spillovers to local firms in Czech Republic, Poland and Slovenia (out of 10 countries studied). On the other hand, Konings (2000) found no spillovers in Bulgaria and Romania and significant negative spillovers in Poland. A study by Javorcik and Spatareanu (2003) in Romania, found that firms partially owned by foreigners generate positive backward spillovers, while the firms in full foreign ownership generate the opposite. They interpret these results are based on different types of FDI, as investors that enter with fully-owned greenfield investment are less likely to source intermediate inputs from local firms than those who enter in a form of a joint venture. Javorcik (2004) reached the same conclusion for Lithuania, where she found only significant positive vertical spillovers through backward linkages with suppliers, which were generated only by firms in partial ownership of foreign investors (Javorcik, 2004).

As with direct effects and horizontal spillovers, the empirical literature is inconclusive on the vertical spillover effects. However, the widely identified positive backward linkages of firms in foreign ownership with domestic supplier to some degree support the theoretical identified suggestion that the global production networks or GVCs can play an important role in facilitating knowledge transfer (Bruno & Cipollina, 2014).

Drawing conclusions from the literature on direct and indirect effects of FDI, we can observe that the technological spillovers do lead to positive effects on domestic firms, however highly conditionally. Especially in developing and transitional countries, there

is a high risk of competition effect working in the opposite direction. Several studies also addressed concerns about potential drawbacks for host economies. These potential drawbacks mainly reflect potential lack of positive linkages with local communities and the effect on competition in national markets. It seems that even some expected benefits may prove elusive. This is the case when the host economy, in its current state of economic development, is not able to take advantage of the technologies or know how transferred through FDI. Additionally, high presence of foreign competitors can lead to crowding-out effect. This effect has been mostly identified in developing and transition countries, where inefficient firms lost market share due to foreign competition.

While it is consensually documented that FDI firms i.e. joint ventures, firms receiving foreign investment and fully foreign firms are more productive than their domestic counterparts without foreign equity share, much of the evidence on FDI spillover effects points mainly to vertical spillovers – backward linkages to foreign affiliates’ suppliers and forward linkages to its customers. This indicates that the transmission of knowledge and technology through the channel of imitation or labor turnover does not appear as efficient as it is suggested by the theoretical assumptions. Contrarily to MNEs incentives to protect its advantages towards their local competitors and block leakages through imitation or labor turnover, in the case of backward and forward linkages foreign companies have more interest to increase the productivity of their local suppliers and/or distributors, to provide for high-quality intermediaries or for adequate distribution of products. These linkages to suggest that global production networks do play an important role in facilitating knowledge transfer.

2 FDI TRENDS: OVERVIEW OF FDI FLOWS

Global FDI flows and stock have been experiencing steady growth in volume in past decades. Since 1980 the world FDI stock increased from USD 698 billion (bn) to USD 1.5 trillion in 2019, as monitored by UNCTAD (UNCTAD, 2020).

While the global FDI flows started to show a declining rate in recent years, due to newly arisen protectionism politics, the year 2020 was also strongly marked by the unexpected COVID-19 pandemic. The uncertainty of future evolution of the pandemic and the growing restrictions in global investment policy environment led to a collapse of global FDI stock to an estimated USD 895 bn in 2020. Despite the projections for the global economy to recover in 2021, UNCTAD expects the effects of the pandemic will linger longer (UNCTAD, 2020).

For the purpose of this thesis, the focus will be on the trends of global FDI before the pandemic, while considering the predictions for the future that will be strongly marked by further developments of COVID-19 pandemic and global economy’s response to it.

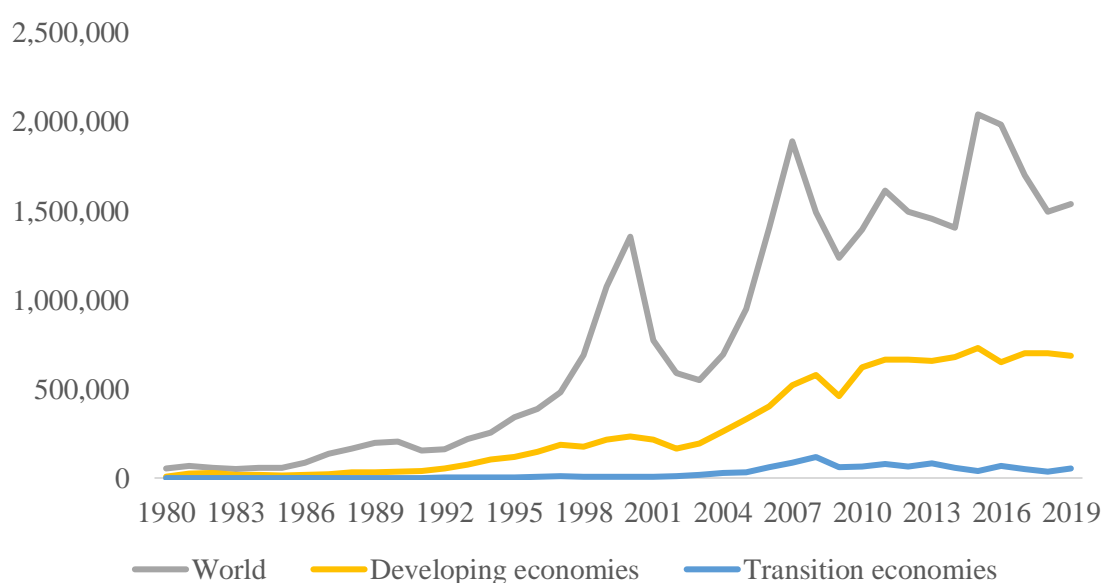
2.1 Global FDI trends and prospects

Since 1980, participation of countries in the worldwide FDI has expanded steadily. Not only developed countries but many developing countries and countries in transition have embarked on a process of market liberalization and the number of markets and industries to which international investors were able to allocate their savings has grown substantially. The growth in FDI volume until today reflects both an increase in the size and number of individual FDI transactions, as well as the growing diversification of enterprises across economies and industrial sectors (OECD, 2008).

Global FDI flows are highly dependent on the developments in the overall global economy. The top three factors influencing FDI decisions are political stability, macroeconomic stability and a country's legal and regulatory environment. Investor confidence decreases when the direction of policy making is unclear or unpredictable, the effect of which is also observable in the decline of FDI inflows. Negative trends effecting the FDI are important concern especially for policymakers when considering countries' efforts to stimulate economic development.

According to UNCTAD's statistics, global FDI flows began to exhibit a downward trend in recent years. As presented in Figure 1 below the downward trend in FDI flows was already noticeable starting from 2015, when FDI flows reached its first peak after the recession in 2008. The decline in FDI flows went hand in hand with other macroeconomic indicators such as gross domestic product (GDP) and trade, which were weighted down due to several factors concerning trade tariffs and other retaliatory measures that have a negative effect on global economic growth (UNCTAD, 2019).

Figure 1: Global inward FDI flows 1980 – 2019 (USD million)



Source: UNCTAD (2020a).

The interconnectedness of FDI flows with the turbulences in global economy has been most evident in year 2020, when the world was hit by the COVID-19 pandemic that has majorly disrupted global economic activity. Interestingly, as observed in Figure 1, historically developing and transition economies have proven to be more resilient to downturns in global economy in terms of FDI inflows, while developed world has experienced significant ups and down in FDI flows through the past three decades. However, according to UNCTAD's latest World Investment Report (WIR) from 2020, COVID-19 is not the only gamechanger for future FDI flows. It is predicted that the new industrial revolution, the policy shifts towards economic nationalism and sustainability trends will all have long-term effects on the configuration of international production in the decade to 2030 (UNCTAD, 2020).

2.1.1 Global trends in FDI flows

One of the most direct measures of FDI is total level of direct investments at a given point in time, i.e. FDI stock, which accounts for cumulative value of past outward and inward FDI flows. Looking at the data recording recent historical FDI flows (see Table 2), it is evident that the observed recent decline in global FDI flows was concentrated mostly in developed part of the world, while developing countries continued to increase their share as the recipients of FDI. According to UNCTAD WIR 2019, the decline in both FDI inflows and outflows in developed countries, that is especially noticeable in year 2018, is attributable to the fact that almost all developed countries introduced more rigorous screening of investment in strategic industry on the basis of national security considerations. UNCTAD also reports that the share of restrictive and regulatory measures against FDI is the highest it has been in more than 20 years and the primary drivers of this trend have been high-income countries (UNCTAD, 2019).

As observed in Table 2, although FDI inflows to developing economies declined more marginally, it is reported, that it nonetheless fell to its lowest levels in decades relative to GDP, due to the investment climate shifts. The transition economies also started to take part in being the recipients of the FDI inflows over the past decade, but were also affected by the changing climate in global economy and the decline in recent years is associated with geopolitical uncertainties (UNCTAD, 2019).

It is evident that due to rising protectionism and other uncertainties affecting investors' confidence, FDI inflows and outflows were already slowing down before the COVID-19 outbreak. The pandemic added an unprecedented risk to the already existing socio-economic and political factors that were already exerting pressures on global trade and FDI, sending business confidence to historic lows (Pazarbasioglu, 2020). Global Investment Competitiveness Report 2019-2020, which is based on large surveys of 2,400 global business executives in ten large middle-income countries, reported that within months of COVID-19 outbreak, more than two thirds of multinational investors were

reporting disruptions in supply chains, declines in revenues and falls in production (World Bank, 2020).

Table 2: FDI flows 2017 – 2019, by and region and level of development (in USD bn or %)

Year	FDI inflows			FDI outflows		
	2017	2018	2019	2017	2018	2019
Economy						
World (Total FDI flows) (USD bn)	1,700	1,495	1,540	1,601	986	1,314
<i>Annual growth rate (%)</i>	<i>-14%</i>	<i>-12%</i>	<i>3%</i>	<i>4%</i>	<i>-38%</i>	<i>33%</i>
Developed economies (USD bn)	950	761	800	1,095	534	917
<i>% of Total FDI flows</i>	<i>56%</i>	<i>51%</i>	<i>52%</i>	<i>68%</i>	<i>54%</i>	<i>70%</i>
Out of which:						
Europe (USD bn)	570	364	429	539	419	475
North America (USD bn)	304	297	297	379	-41	202
Developing economies	701	699	685	467	415	373
<i>% of Total FDI flows</i>	<i>41%</i>	<i>47%</i>	<i>44%</i>	<i>29%</i>	<i>42%</i>	<i>28%</i>
Out of which:						
Asia (USD bn)	502	499	474	417	407	328
Latin America (USD bn)	156	149	164	38	0.1	42
Africa (USD bn)	42	51	45	12	8	5
Transition economies (USD bn)	50	35	55	38	38	24
<i>% of Total FDI flows</i>	<i>3%</i>	<i>2%</i>	<i>4%</i>	<i>2%</i>	<i>4%</i>	<i>2%</i>

Source: UNCTAD (2020a).

As presented in Table 3 below, the latest data on global FDI flows estimates that in 2020 FDI could decline to its lowest levels since the mid-2000s. With the predicted decrease in FDI inflows of 30 to 45 per cent, developing economies appear more vulnerable to the current crisis, as their productive and investment footprints are less diversified and thus more exposed to systematic risks. Developing economies are also more reliant on investments that are GVC intensive and extractive industries, which have both been severely hit during the pandemic outbreak. Additionally, developing economies are not able to grant the same economic support measures for recovery as response to crisis as developed economies (UNCTAD, 2020).

As per UNCTAD's predictions, despite the drastic decline in global FDI flows during the crisis, the international production system is expected to continue to play an important role in economic growth and development. While the global economy is expected to recover already by 2022, future implications for FDI flows have more lingering effects, that will also be noticeable in the structure of FDI flows in the following decade (UNCTAD, 2020).

Table 3: FDI inflows by region in 2019 and preliminary estimates for 2020 (USD bn)

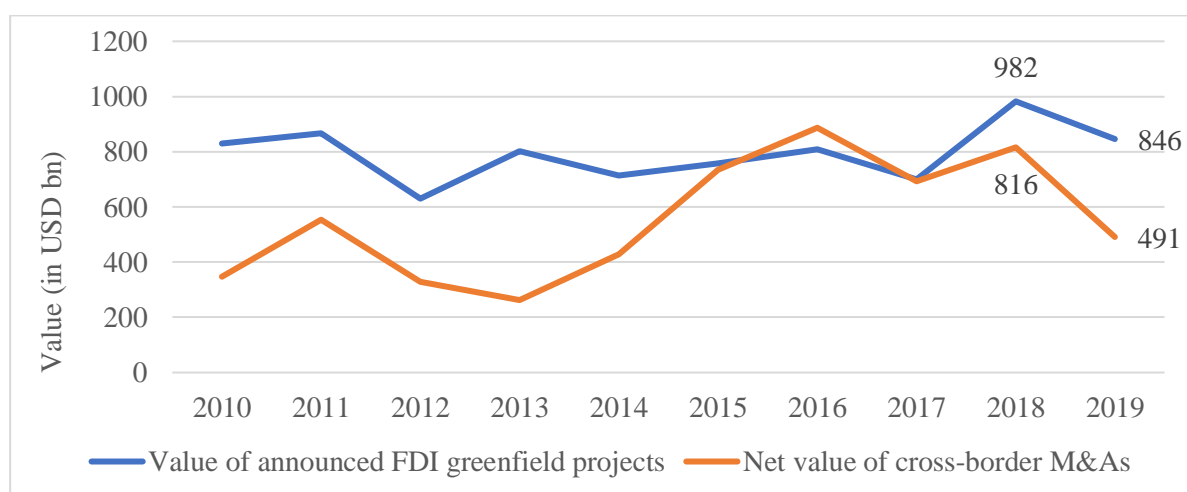
Year	FDI inflows		
	2019	2020*	Annual growth rate (%)
Economy		*Projections	
World	1,540	920 to 1,080	-40 to -30
Developed economies	800	480 to 600	-40 to -25
Europe	429	240 to 300	-45 to -30
North America	297	190 to 240	-35 to -20
Developing economies	685	380 to 480	-40 to -30
Asia	474	260 to 330	-45 to -30
Latin America	164	70 to 100	-55 to -40
Africa	45	25 to 35	-40 to -25
Transition economies	55	30 to 40	-45 to -30

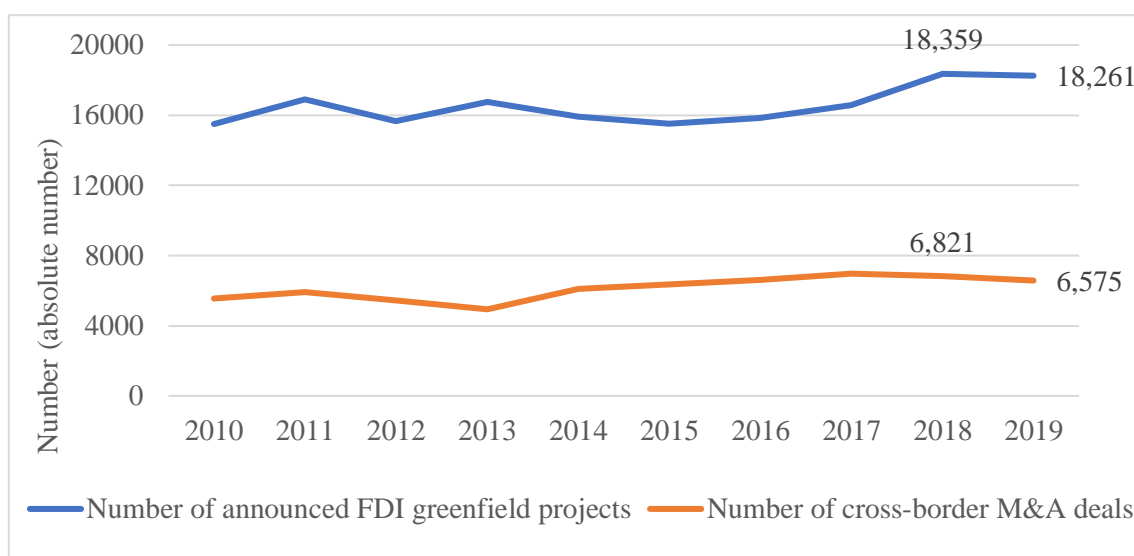
Source: UNCTAD (2020a).

2.1.2 Investment trends by type and region

Besides FDI stock, announced cross-border M&A, greenfield investments or project financing can also serve as an indication of future intensity of FDI projects. Already in 2019, the number and value of announced cross-border M&A deals and greenfield investments decreased in comparison to historical values (see Figure 2). However, the decline was primarily driven by decrease in value of FDI greenfield projects and cross-border M&As, as the number of announced cross-border investments did not decrease significantly in 2019 in comparison to the preceding year.

Figure 2: Value (upper panel) and number (bottom) of cross-border M&As and announced greenfield FDI projects, 2010-2019 (USD billion and number)





Source: UNCTAD (2020a).

The decrease in FDI activity was more evident among M&A announcements, than among greenfield announcements. As presented in Table 4, the decrease in announced M&A activity was concentrated in developed part of the world, while the developing and transition economies recorded an increase in number of announced M&A deals in 2019. Similarly, the decrease in greenfield investments was concentrated mostly in developed economies and partially in transition economies.

Table 4: Number of cross-border M&As and greenfield FDI projects by region, 2017-2019 (absolute number)

Region/economy	Cross-border M&A			Greenfield		
	2017	2018	2019	2017	2018	2019
World	6,967	6,821	6,575	16,579	18,359	18,261
Developed economies	5,655	5,643	5,423	9,873	10,366	10,331
Europe	3,005	3,278	3,222	6,973	7,443	7,079
North America	2,190	1,823	1,719	2,117	2,090	2,410
Other developed economies	460	542	482	783	833	842
Developing economies	1,172	1,087	1,055	6,074	7,134	7,233
Africa	116	89	129	676	726	1,063
Asia	768	687	643	4,079	4,663	4,336
Latin America	288	312	276	1,309	1,739	1,832
Oceania	0	-1	7	10	6	2
Transition economies	140	91	97	632	859	697

Source: UNCTAD (2020a).

Looking forward, the currently estimated overall decline in FDI activity has affected all forms of FDI and all economies in 2020. As per UNCTAD's latest available data presented in Table 5, new greenfield investment project announcements were 35% lower in 2020 in comparison to 2019, cross-border M&As decreased by 10% and newly

announced cross-border project finance deals by 2%. In 2020 greenfield announcements in developing countries fell by 42% in number and international project finance deals by 14%, compared with 19% and 10% in developed countries (see Table 5). The trends in greenfield and project finance announcement pose a major concern for developing and transition countries, as the vast majority of this type of projects were historically concentrated in developed economies – many in renewable energy and other infrastructure projects (UNCTAD, 2020).

Table 5: Change in number of announced greenfield projects, cross-border M&As and international project finance deals, by group of economies 2020 (per cent change vs 2019)

	Cross-border M&As	Greenfield projects	International project finance
World	-10%	-35%	-2%
Developed economies	-10%	-19%	8%
Developing economies	-24%	-42%	-14%
Transition economies	-40%	-47%	-47%

Source: UNCTAD (2020a).

Data on an announcement basis provides a mixed picture on forward trends, confirming the weak outlook. A look at announced cross-border investment for 2020, suggests that rebound in global FDI flows is more likely to come from cross-border M&As than from new investments in productive assets, i.e. greenfield investment (UNCTAD, 2020). According to latest estimations for 2020, the announced cross-border M&A deals are highly driven by technology and healthcare deals, which were not as affected by the pandemic as the other industrial sectors (see Table 6). The highest decline in value of announced cross border M&A is concentrated in primary sector (52% decrease in comparison to 2020), which typically tends to represent a larger portion of the economy in developing countries than in developed (UNCTAD, 2020)

Table 6: Announced cross-border M&As, by sector and selected industries, 2020 (per cent change vs 2019)

Sector/industry	Value (USD billion)		Growth rate
	2019	2020	%
Total	505	456	-10
Primary	34	17	-52
Manufacturing	243	225	-8
Services	228	215	-6
<i>Top 10 industries in value terms:</i>			
Food, beverages and tobacco	20	85	320
Information and communication	25	79	216

(table continues)

Table 6: Announced cross-border M&As, by sector and selected industries, 2020 (per cent change vs 2019) (continued)

Pharmaceuticals	97	55	-43
Electronics	20	40	99
Utilities	12	33	172
Finance and insurance	49	28	-43
Real estate	35	21	-41
Trade	16	18	8
Automotive	6	17	167
Extractive industries	32	15	-53

Source: UNCTAD (2020a).

As presented in Table 7, the decrease in value of announced greenfield investments in 2020 in comparison to 2019 was significantly higher than the decrease in value of announced M&A investments. While the highest decrease is also observable in the primary sector, the decrease in value of greenfield investments in manufacturing sector follows closely. Namely manufacturing sector is vulnerable to supply and demand shock as they are very GVCs intensive and were thus impacted by supply chain disruptions. The highest value of announced greenfield investments is concentrated in utilities and information and communication industry sectors, which were less severely impacted by disruptions in value chains due to COVID-19 pandemic.

Table 7: Announced greenfield investment, by sector and selected industries, 2020 (per cent change vs 2019)

Sector/industry	Value (USD billion)		Growth rate
	2019	2020	%
Total	846	547	-35
Primary	21	12	-45
Manufacturing	42	224	-44
Services	422	311	-26
<i>Top 10 industries in value terms:</i>			
Utilities	113	97	-14
Information and communication	66	78	18
Electronics	53	46	-13
Chemicals	47	40	-14
Construction	66	36	-46
Coke and refined petroleum products	94	28	-70
Transportation and storage	43	26	-39
Automotive	62	25	-59
Trade	22	23	3
Finance and insurance	24	20	-14

Source: UNCTAD (2020a).

It is expected that the services industries will be more severely struck in the medium-term from the start of the COVID-19 pandemic, as they were directly affected by the lockdowns (for example travel and leisure sectors). Commodity-related industries will suffer from different effects, such as disruptions of supply chain and supply and demand shocks. Thus, a push to improve supply chains resilience especially in critical industries will be one of the major effects of future long-term trends (UNCTAD, 2020).

2.1.3 Future FDI prospects

The future of FDI flows is highly dependent on external factors such as geopolitical risks, trade tensions and concerns about countries shifting towards more protectionists policies. Recent shifts in global economic climate that were affected by trade tensions, have already contributed to a new rise in trade and investment uncertainty, which resulted in the estimated fall in global FDI by 40 percent in 2020. As evident from the decline in FDI that was mostly concentrated in the high-income countries in the recent years, the negative effects were mostly concentrated in the industrialized part of the world. However, a growing number of developing countries is also already structuring their policy agendas along similar lines.

Furthermore, structural changes in the nature of international production (such as adoption of digital technologies in global supply chains, which are shifting the international production toward intangibles and increasingly asset-light forms), are creating both opportunities and risks for foreign investment. The expected transformation of international production will bring new challenges, specially to developing countries, as for decades their development and industrialization strategies have been highly dependent on attracting FDI, increasing participation in GVCs, as well as gradually upgrading technology through international production networks (UNCTAD, 2020).

The global COVID-19 pandemic has added additional risk to the mix of rising protectionism and other uncertainties that were already causing the decrease in investor confidence. As a response to COVID-19 effects, MNEs are expected to adjust their production networks in order to improve their resilience. In order to sustain international cooperation, should the new investment patterns emerge, countries will need to evaluate their risk exposure, value propositions and competitiveness factors of individual sectors and value chains. Foremost, policymakers will need to identify emerging competitive sectors that may arise from the possible reorganization of GVC and FDI landscapes (UNCTAD, 2020).

2.2 FDI trends and prospects in Slovenia

General orientation of Slovenia is openness to FDI. As member state Slovenia acts in accordance with the principles of the European Union (EU) and the OECD, which promote non-discrimination between national and foreign investors. As per Treaty on the

Functioning of the EU from 2009, article 63 states that “all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.” (Treaty on the Functioning of the EU, 2009). However, as it will be presented in this chapter, Slovenia’s levels of inward FDI remain relatively small, especially in comparison to other comparable countries. As the goal of this master’s thesis is to study FDI effects on host economy and domestic companies, the focus will be mostly on inward FDI activity in Slovenia. The chapter will include data on FDI volume and origin in recent years and comparative advantages of Slovenia, to better understand why investors choose to invest in Slovenia.

2.2.1 Motives for investment in Slovenia

Until this time, the levels of inward FDI in Slovenia remain relatively low in comparison to other countries from similar geographical regions and with similar economic environments. This indicates that Slovenia was historically not as successful in attracting foreign investment to the same extent as other Central and Eastern Europe economies (i.e. Czech Republic, Slovakia, Hungary etc.), based on share of FDI in terms of GDP. However, from the historical trends it is also evident that no matter the relatively low historical levels of FDI inflows, Slovenian economy is strongly internationalized, especially within the EU economic sphere. Looking at FDI inflows by country of origin, the historical trends suggest enhanced intra-regional FDI inflows, as the main investors in Slovenia (i.e. Austria, Switzerland, Germany etc.) are all in geographical proximity of Slovenia. Thus, the future of FDI flows in Slovenia is highly dependent on economic conditions and dynamics in the EU.

Due to geopolitical issues and their economic implications, strategic development decisions agreed on the EU level and transformation of economic structure strongly marked also by the COVID-19 pandemic FDI flows in Slovenia currently face an uncertain future. As these events and their implications for the future cannot be fully understood at this time, it is also possible that potential investors might delay or change their investment plans as a result of this uncertain future. On the other hand, changes in the global economic structure might also result in positive outcome for Slovenia, due to Slovenia’s ability to attract new investments on the account of location advantages and its EU-membership (Kušar, 2020).

A survey on participation of foreign equity firms in the Slovenian economic environment, carried out CIR from Faculty of Social Sciences, University of Ljubljana and commissioned by SPIRIT from 2018 has identified the main motives of foreign investors for investment in Slovenia. Main identified enticement for foreign investors to invest in Slovenia is the pursuit of markets and strategic business development. In addition to its geographical location, Slovenia is also a member of international organizations (OECD, WTO) and in the euro area (EU). Given that Slovenia is part of EU’s single market, setting

up a company in Slovenia means also having access to one of the world's largest markets. Slovenia is also a good steppingstone for doing business with South-Eastern Europe, having good connections with economically important regions in neighboring countries such as Austria, Italy and Germany. Among the advantages of the Slovenian business environment, foreign investors also mention easy access to resources such as raw materials, business partners, customers and well educated and highly trained workforce at moderate expense (Jaklič, Koleša, & Knez, Tuji investitorji o slovenskem poslovnem okolju 2018, 2018).

Although economic factors are perceived as a key investment motive, the factors of investment climate cannot be neglected as these have proven to be decisive in investors' decision whether to realize the intended investment. Inadequate investment climate can deter a foreign investor who would otherwise invest based on the assessment of the economic factors. In this sense, Slovenia mainly faces the problem of high operational requirements such as administrative barriers, high taxes and rigid market (Živič, 2010). According to the survey conducted by SPIRT and CIR in 2018, the most common proposals of foreign investors regarding actions towards more FDI friendly environment are those relating to taxes and reduction of operating costs, regulation of labor market and payment discipline, as well as reduction of administrative burdens, simplification of administrative procedures and increase in efficiency and professionalism of the Slovenian public administration (Jaklič, Koleša, & Knez, Tuji investitorji o slovenskem poslovnem okolju 2018, 2018).

Additionally, regarding administrative and legal barriers, Slovenia has recently implemented regulatory measures regarding foreign investment, for the purpose of protection of strategic assets. Effective as per 31 May 2020, a new Act Determining the Intervention Measures to Mitigate and Remedy the Consequences of the COVID-19 Epidemic sets a new screening mechanism for FDI, which authorizes the Ministry of Economic Development and Technology to assesses if the intended FDI affects security or public order in Slovenia. The act refers to screening and approval of investment in the fields of critical infrastructure, critical technologies, supply of critical inputs, access to sensitive information, freedom and pluralism of the media and projects and programs of Union interest (Karanovic & Partners, 2020).

Going forward, given the level of its development, Slovenia can strengthen its position in attracting foreign investment. The question that remains is, however, what type of investment to attract in order to benefit from FDI's positive direct or indirect effects. Based on historical data, FDI in Slovenia is currently mostly concentrated in the Slovenian manufacturing sector, which is inherently more export oriented. Additionally, the majority of FDI inflows are made in a form of M&A, that target the most prosperous sectors in Slovenian economy. On the other hand, greenfield investments, that are theoretically more beneficial in terms of job creation and knowledge transfer, are to this time relatively scarce.

2.2.2 FDI flows and stock in Slovenia

The main indicators of the country's internationalization level or openness include, in particular, the share of imports and exports in GDP and the share of inward and outward FDI in GDP. As observed in Table 8 Slovenia is strongly export-oriented and well-integrated with GVCs as exports of goods and services continuously represent around 80% of Slovenia's GDP. However in terms of success in attracting FDI Slovenia is significantly lagging behind its potential, as Slovenia still remains a relatively closed economy in terms of FDI as it ranks as one of the countries with the scope of incoming FDI relative to its level of development and GDP (Schwab, 2019).

Table 8: Selected indicators of Slovenia's level of internationalization (as % of GDP)

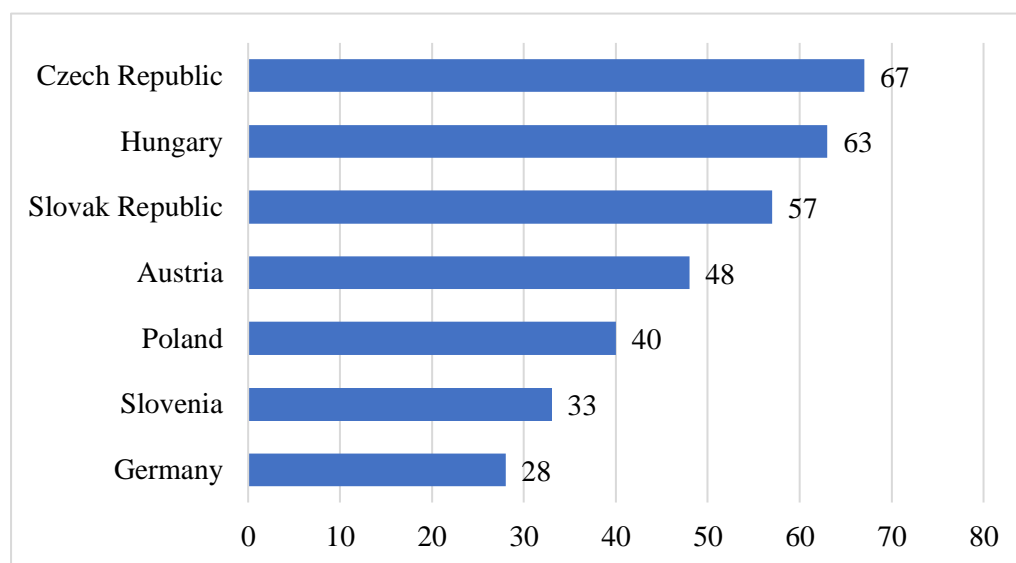
	2017	2018	2019	2020
Exports of goods and services	83.1	84.8	83.7	78.7
Imports of goods and services	74.2	76.3	75.3	68.8
Inward FDI	31.8	33.0	33.1	n/a
Outward FDI	13.7	13.2	13.7	n/a

Source: SURS (2020).

Representing less than one-third of Slovenia's economy (33.1% of Slovenia's GDP in 2019), the role of inward FDI is relatively small (Kušar, 2020). In absolute terms the stock of inward FDI in Slovenia amounted to EUR 16.0 bn at the end of 2019, which is also an increase by EUR 0.7 bn in comparison to the preceding year. Despite the growth in inward FDI in recent years, Slovenia is still behind the EU average and comparable countries in terms of geography and level of development, identified by the Bank of Slovenia (see Figure 3).

Directly comparing the relative values represented by FDI in individual economies, the figure below illustrates data from Bank of Slovenia's database of net FDI (outward less inward) stocks as percentages of GDP for selected countries for 2019. The selected countries comprise of Slovenia's main trading partners and/or comparable EU Member States in terms of GDP or region. In terms of inward FDI position as % of GDP Slovenia record significantly lower stock in comparison to other comparable countries, with the exception of Germany which is rather an investor country than recipient of FDI (Bank of Slovenia, 2019).

Figure 3: Inward FDI positions as % of GDP in selected countries in 2019 (% of GDP)



Source: Bank of Slovenia (2019).

As far as the mode of entry of foreign investors in Slovenia is concerned, the Bank of Slovenia's data distinguishes between greenfield FDI, acquisitions and other investments (in institutions, subsidiaries and foundations). The increase in inward FDI stock in 2019 was mainly attributable to inflows of equity and reinvested earnings (94% of end-year stock of FDI in Slovenia in 2019) (see Table 9). According to Bank of Slovenia's information, FDI in Slovenia are to this date mostly acquisitions or takeovers of existing companies, while larger greenfield investments are relatively scarce (Bank of Slovenia, 2019). In line with that, also the increase in equity in 2019 was mostly attributable to M&A activity (70% of total FDI inflows), while greenfield investments accounted solely for 10% of equity contributions.

Table 9: Mode of entry of foreign investors in Slovenia, 2019 (EUR t or %)

	End-year stock	Transactions	Other changes	End-year stock
	2018	2019	2019	2019
Total	15,254	1,096	-342	16,008
Equity and reinvested earnings	13,905	1,669	-541	15,033
% of total	91%	-	-	94%
Debt instruments	1,350	-574	199	975
% of total	9%	-	-	6%

Source: Bank of Slovenia (2019).

According to the cumulative data of the Bank of Slovenia, the majority of FDI inflows in Slovenia originate from other EU member states, which are also Slovenia's main trade partners. As presented in Table 10, dominance of FDI from EU-members is clearly seen in Slovenia, accounting for over 80% share in terms of total inward FDI in Slovenia.

Table 10: Top source countries investing in Slovenia, 2017 – 2019 (EUR million and % of total)

	2017		2018		2019	
	EUR m	% of total	EUR m	% of total	EUR m	% of total
EU 28	11,721	84.0	12,806	83.9	13,225	82.6
Austria	3,574	25.6	3,657	24.0	3,961	24.7
Luxembourg	1,565	11.2	2,099	13.8	2,085	13.0
Germany	1,197	8.6	1,365	8.9	1,355	8.5
Italy	1,146	8.2	1,189	7.8	1,263	7.9
Netherlands	1,064	7.6	1,134	7.4	1,243	7.8
Croatia	948	6.8	992	6.5	1,041	6.5
United Kingdom	300	2.1	407	2.7	438	2.7
Hungary	32	0.2	59	0.4	422	2.6
Cyprus	236	1.7	311	2.0	409	2.6
Czech Republic	296	2.1	305	2.0	303	1.9
Other	1,364	9.8	1,288	8.4	705	4.4
Non-EU	2,236	16.0	2,448	16.1	2,783	17.4
Switzerland	1,446	10.4	1,593	10.4	1,826	11.4
Serbia	1,058	0.8	171	1.1	226	1.4
US	146	0.1	81	0.5	172	1.1
Other	1,031	46.1	604	24.7	957	34.4
Total	13,957	100.0	15,254	100.0	16,008	100.0

Source: Bank of Slovenia (2019).

For a number of years, the most important foreign investors originate from Austria, Luxemburg, Switzerland, Italy and Germany (Kušar, 2020). The investments from these five countries together accounted for 65.5% of all inward FDI in value terms at the end of 2019 (Bank of Slovenia, 2020).

Inward FDI in Slovenia by activity is traditionally concentrated in manufacturing, financial and insurance activities and wholesale and retail trade and repair of motor vehicles and motorcycles, while important share FDI activity is also accounted for in real estate activities and in information and communication sector in the past years. The concentration of inward FDI by activity is presented in Table 11 below.

Table 11: Inward FDI in Slovenia by sector, 2017 – 2019 (EUR million)

	2017		2018		2019	
	EURm	% of total	EUR m	% of total	EUR m	% of total
Manufacturing	4,579	32.8	5,391	35.3	5,552	34.7
Financial and insurance activities	3,054	21.9	2,933	19.2	3,452	21.6
Wholesale and retail trade, repair of motor vehicles	2,438	17.5	2,660	17.4	2,721	17.0
Real estate activities	903	6.5	1,044	6.8	996	6.2
Information and communication	779	5.6	842	5.5	887	5.5
Professional, scientific and technical activities	545	3.9	567	3.7	553	3.5
Electricity, gas, steam and air conditioning supply	356	2.5	379	2.5	383	2.4
Transportation and storage	274	2.0	263	1.7	208	1.3
Construction	219	1.6	201	1.3	174	1.1
Accommodation and food service activities	102	0.7	121	0.8	138	0.9
Other	709	5.1	853	5.6	944	5.9
Total	13,957	100.0	15,254	100.0	16,008	100.0

Source: Bank of Slovenia (2019).

Interestingly, the majority of FDI activity is concentrated in sectors, for which Slovenia considers having comparative advantage. At the same time, FDI activity is more present in the export-oriented industries, which can be expected considering Slovenia's small local market. Looking at Slovenia's key export products, we find that predominantly Slovenian manufacturing sector is export oriented. Key export products are vehicles (15% of total exports), medicinal and pharmaceutical products (15%) and electrical machines and devices (10%) as reported by SURS for 2019.

3 EMPIRICAL ANALYSIS OF THE CHARACTERISTICS AND EFFECTS OF FOREIGN DIRECT INVESTMENT IN SLOVENIA

3.1 Definition of the research problem

3.1.1 Fundamental research question

Based on the review of the relevant literature and theoretical assumptions about the inward FDI trends, the advantages and disadvantages FDI can bring, the purpose of this master's thesis research is to present the scope and importance of FDI effects on host economy and domestic companies on the case of Slovenia.

As evident from the theoretical part of this master's thesis, the correlation between inward FDI and economic development has been studied extensively, however, the review of the relevant literature has also shown, that there is no simple equation that yields beneficial effects on the host economy in correlation with FDI. Seeing that inward FDI plays an important role in Slovenian economy, no matter the relatively low activity of foreign investors, the analysis is focused on characteristics and effects of FDI specifically on the case of Slovenia acting as a host country.

The review of the relevant theoretical literature on FDI trends combined with the analysis of the inward FDI on the case of Slovenia will serve as a basis to answer the fundamental question of this master's thesis:

“What type of investment and what type of companies foreign investors choose when deciding to invest in Slovenia and what are the effects arising from the FDI”

To summarize, the goal is to provide insight into inward FDI and its current state in the Slovenian economy, focusing on the potential benefits, while considering also possible drawbacks. Through my research of companies with foreign owned equity, I will try to determine the pattern of foreign investments in Slovenia, i.e. whether investors are attracted to Slovenia based on the country specific advantages as a predisposition for development of new business or do they choose to invest in sectors and companies that have historically shown the most advantage and success in the Slovenian economy.

The purpose of this research is to provide more in-depth findings and recommendations for Slovenia as a host country for FDI that will support faster productivity growth and economic development by exploiting the benefits of FDI, while considering possible drawbacks. The research part will be dedicated to analytical overview and statistical analysis, that will allow an overview of links between various factors relating to inward FDI trends in Slovenia.

To achieve my goal, the research will be focused on the following subcategories, related to effects of inward FDI in Slovenia:

- Impact on productivity
- Impact on export orientation
- Employment
- Technology transfers and innovation

3.1.2 Methodology

Empirical analysis will be conducted in a form of quantitative research. First part of the analysis is carried out based on the data gathered from SURS, which collects statistical data on all enterprises that are registered as legal or natural persons in market non-

financial activities (by the Standard Classification of Activities 2008 – SKD 2008) and which had turnover or personnel cost and were therefore active during at least a part of the reference period. The goal of analysis of performance of firms in foreign ownership in Slovenian corporate sector was to determine their performance and growth dynamics in comparison to fully domestic companies. The analysis provides an overview of participation of companies in foreign ownership in Slovenian economy, by number of enterprises and selected financial and other performance indicators. The analysis of performance and growth dynamics of companies with foreign capital is limited for the period of last five years from the latest available statistical data (from 2013 – 2018) and additionally to observation of changes between years 2017 and 2018. The analysis addresses the difference in growth dynamics and performance between companies in foreign ownership and domestic companies in the period from 2013 – 2018 and from 2017 – 2018, based on own calculations, using the data gathered from SURS. Specifically, achievements in terms of revenue, number of employees, export and value added at factor cost of comparable foreign owned and domestic companies performing in the Slovenian corporate sector are observed.

Furthermore, the analysis includes analysis of the survey results on perceptions of foreign investors about the Slovenian business environment, conducted by CIR, Faculty of Social Sciences and commissioned by SPIRIT Slovenia in the year 2020. SPIRIT Slovenia has given permission and agreed to the use of their survey results for the purpose of the research of this master's thesis. Permission from the SPIRIT Slovenia was given by e-mail on June 22nd, 2021, agreeing on the use of the survey results on perceptions of foreign investors about the Slovenian business environment for the purpose of the master's thesis. The sample of companies in the survey was formed on the basis of the database of companies with foreign capital of SPIRIT Slovenia. The sample included total population of 1,204 companies with foreign capital, out of which 993 companies were reached in the course of survey from September 3rd to October 2nd, 2020. The questionnaire was ultimately answered by 213 companies with foreign capital, which represents a 21.5% response rate, if all the companies with foreign capital that were reached are considered, and 17.7% share of total population of companies with foreign capital. The survey results belong to SPIRIT Slovenia and authorship rights to the CIR, Faculty of Social Sciences. The quantitative analysis includes descriptive analysis of the survey results. The analysis provides an overview of effects of FDI on productivity of companies with foreign capital, internationalization levels or export orientation, effect on development of human capital and lastly effect of foreign ownership on innovation and technology transfers, all as perceived by the responding companies with foreign capital in Slovenia.

Results of the empirical analysis are interpreted, and the obtained findings summarized in relation to the fundamental research question of the thesis.

3.1.3 Limitations

The limitations of the research are connected to the availability of data, especially in terms of availability of up-to-date data. As the data on selected indicators determining performance of firms in foreign ownership is only available until year 2018, the analysis is limited in terms of more recent years. According to information from SURS's administrative office, the data for 2019 will become available only in September 2021.

Furthermore, there are quite significant discrepancies between data gathered by different sources regarding the number of companies with foreign capital in Slovenia. This section will be dedicated to analysis of the data on companies in foreign ownership collected by SURS. SURS statistics include all enterprises that are registered legal or natural persons in market non-financial activities (by the Standard Classification of Activities 2008 – SKD 2008) which had turnover or personnel cost and were therefore active during at least a part of the reference period. The data analyzed does not distinguish enterprises in foreign ownership based on size of equity share or form of foreign investment, which poses limitations of direct interpretation of the results.

Lastly, as the microeconomic data regarding foreign enterprises in Slovenia is not publicly available, the regression analysis of productivity cannot be performed. This means the observations from the analysis need to be carefully interpreted and not generalized.

Due to limitations related to the accessibility of the data, for the purpose of the quantitative research on the effects of FDI on domestic companies, further research is based on results from a survey conducted by another organization (i.e. SPIRIT Slovenia in cooperation with CIR, Faculty of Social Sciences). Limitations were also identified in the analyzed survey, relating to incompleteness of gathered questionnaires. As only the valid ones were considered in the analyzed answers, the size of the sample varies from question to question. It is also noted that the response rate for some of the questions was very small, thus special attention is needed when interpreting those answers and generalizing the results to the entire population.

The survey sample of companies with foreign capital predominantly includes smaller businesses, which are more present in the service sector, according to the sample description. On the other hand, only 11.6% of the sample companies are large enterprises, which are more commonly found in the manufacturing sector, which is thus less represented in the survey.

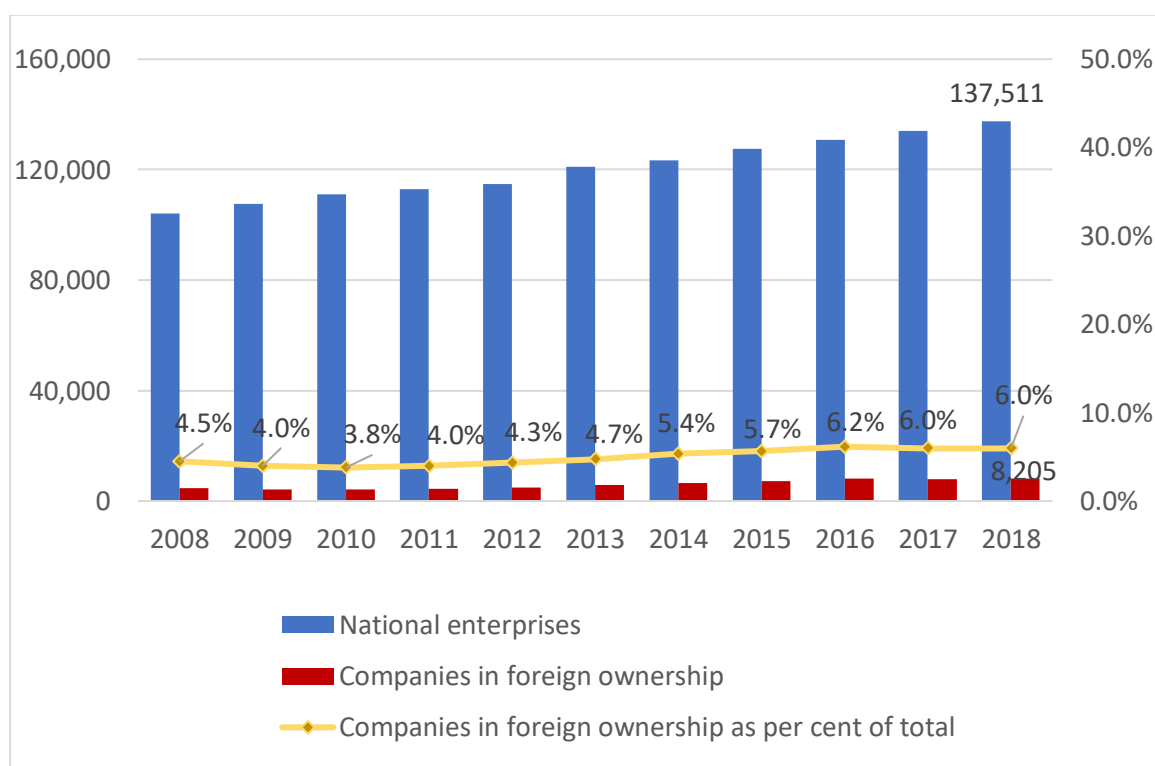
The survey results pertain only to observed effects in selected business categories for companies in foreign ownership that were included in the sample. There is no comparison with domestic companies, that would also address the question whether the identified positive effects are truly related to the type of ownership.

3.2 Performance of firms with foreign ownership in the Slovenian corporate sector

Despite the still relatively small share of inward FDI in the Slovenian corporate sector, it is perceived that until now FDI has played an important role in Slovenian economy. Besides increasing share of inward FDI in Slovenian economy, it is also perceived that firms in foreign ownership grow faster than domestic Slovenian enterprises in the Slovenian corporate sector.

While, according to the statistical data collected by SURS, the share of foreign owned companies remains relatively low in terms of total population of companies in the Slovenian corporate sector, in absolute terms the number of companies with foreign investment is nonetheless increasing (see Figure 4).

Figure 4: Foreign-owned and domestic companies by number of enterprises 2008 - 2018 (absolute number or %)



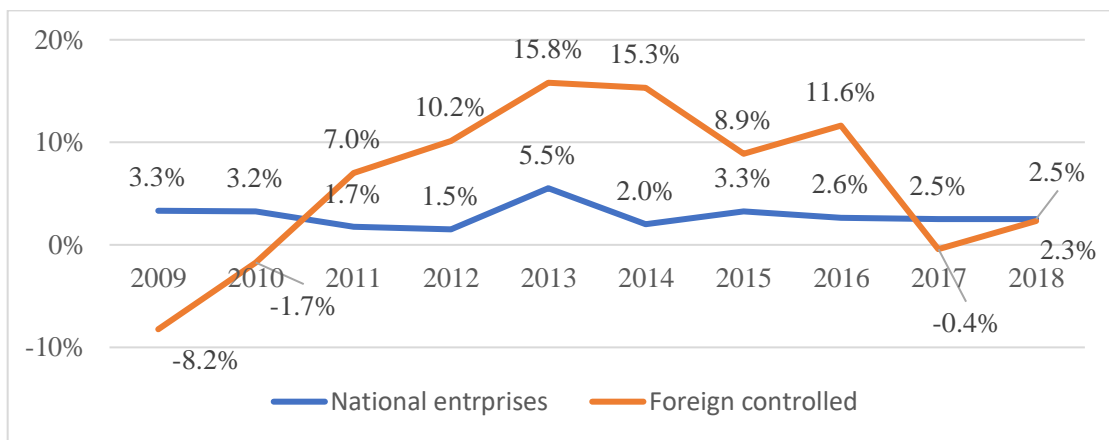
Source: Own work.

It is important to note, that SURS's statistical data considers all enterprises that are registered legal or natural persons in market non-financial activities, which means that presented number of foreign companies, their growth rate and their share in terms of all companies in Slovenian corporate sector does not relate strictly to companies receiving FDI, but also other types of foreign investment. According to SURS the share of foreign-owned companies in the Slovenian corporate sector stood at 6.0% in 2018, while

according to Bank of Slovenia’s data, the share of companies with FDI accounted for 1.6% of the total population of Slovenian companies at the end of 2018 (*Bank of Slovenia, 2018*).

In line with trends of foreign investments on global level identified in the theoretical part of the thesis, also in Slovenia, the peak in increase of foreign investments was observed in year 2016. After 2016 the volume of new foreign investments decreased significantly, which can also be observed in Figure 5, presenting the yearly growth rate of newly established foreign-owned and domestic companies.

Figure 5: Number of foreign-owned and domestic companies growth rate 2008 - 2018 (%)



Source: Own work.

While the growth rate of number of enterprises in foreign ownership is significantly higher than the growth rate in number of national enterprises, the establishment of foreign controlled enterprises is also significantly more volatile. While the number of national enterprises showed a steady growth rate in the observed historical period, foreign controlled companies show higher dependency on turbulences occurring in the global economy.

Again, it is important to note, that the presented data from SURS includes enterprises with all forms of foreign ownership in the Slovenian corporate sector, which needs to be taken into account also in the continuation of the analysis on performance and growth rates of foreign controlled enterprises in comparison to national enterprises. The observed trend was, however, also recorded by Bank of Slovenia, which noted that in 2016 the share of companies with FDI represented 4.7% of the entire population of Slovenian firms, followed by significant decrease to 1.5% in 2017 (*Bank of Slovenia, 2016; Bank of Slovenia, 2017*).

Following tables present the results based on the statistical data gathered from SURS regarding cumulative growth of the studied categories in the period from 2013 to 2018,

separated by group of companies under domestic control and group of companies under foreign control. Additionally, results on growth rates of studied indicators are presented for the latest available year in terms of available data (from 2017 to 2018). Selected indicators relate to total sales revenue of observed groups of companies (i.e. turnover), value of revenue generated through exports, number of persons employed, and value added at factor cost (calculated by SURS as gross income from operating activities after adjusting for operating subsidies and indirect taxes). The results indicate higher growth rates for companies under foreign control for all the categories studied.

Table 12: Growth rate in cumulative value of turnover, exports, number of employees and value added at factor cost by ownership type from 2013 – 2018 and from 2017 - 2018 (% growth rate)

	2013 - 2018	2017 - 2018
Turnover		
National enterprises	16.3%	5.6%
Foreign controlled	66.0%	11.4%
Exports		
National enterprises	19.0%	5.5%
Foreign controlled	34.7%	15.7%
Number of employees		
National enterprises	4.2%	2.8%
Foreign controlled	65.8%	9.3%
Value added at factor cost		
National enterprises	28.2%	5.9%
Foreign controlled	77.2%	10.0%

Source: Own work.

In terms of growth rates of cumulative values of selected performance indicators, foreign controlled companies exhibit significantly higher growth rates in the observed period, in comparison to national enterprises. In the period from 2013 to 2018, companies under foreign control increased their cumulative turnover (i.e. total turnover of all foreign controlled enterprises) by staggering 66.0%, while national companies increased their turnover by 16.3%. Similarly, in the last year from the observed historical period, total value of turnover of companies under foreign control increased by more than 11%, while the total value of cumulative turnover of national enterprises increased by 5.6%.

In terms of exports, in the period from 2013 to 2018, companies in foreign control increased the cumulative value of their export revenue by 34.7%, while national enterprises recorded increase in the total cumulative value of their export revenue of 19.0%. In the latest observed year 2018, the total value of export revenue increased by almost 16%, while export revenue of national enterprises grew only at 5.5% annual growth rate.

In terms of number of employees, foreign controlled companies cumulatively increased the total number of employees by 65.8% in the period from 2013 to 2018 and national enterprises by 4.2%. From 2017 to 2018 foreign controlled companies increased their number of employees by 9.3% in cumulative terms, while increase in cumulative number of employees for all national enterprises stood at 2.8%.

Lastly, value added at factor cost, which considers gross income from operating activities after adjusting for operating subsidies and indirect taxes, increased by 77.2% for foreign owned companies and for 28.2% for national enterprises in the period from 2013 to 2018. From 2017 to 2018 value added at factor cost grew by 10% for foreign owned companies and by 5.9% for national enterprises.

As identified in the theoretical part of this master's thesis, some of industries in Slovenian corporate sector have stronger presence of FDI than others. For the purpose of identifying performance and growth dynamics of companies in foreign ownership in comparison to national enterprises in the same industry, the following Table 13 presents an analysis of the latest available statistical data (i.e. from 2017 to 2018) on number of enterprises according to ownership and selected industries, that are more FDI intensive, for the period from 2017 to 2018.

Table 13: Number of enterprises by ownership and activity 2017 – 2018 (absolute number)

Activity	National enterprises			Foreign owned enterprises		
	2017	2018	% of total within industry in 2018	2017	2018	% of total within industry in 2018
Wholesale and retail trade, repair of motor vehicles and motorcycles	24,026	23,751	91%	2,365	2,397	9%
Professional, scientific and technical activities	32,929	34,164	97%	1,151	1,158	3%
Construction	17,465	17,912	94%	1,203	1,127	6%
Transportation and storage	7,778	7,801	90%	800	884	10%
Manufacturing	18,518	18,824	96%	858	847	4%
<i>% of total</i>	<i>75%</i>	<i>75%</i>	-	<i>80%</i>	<i>78%</i>	-
Other	33,419	35,059	-	1,641	1,792	-
Total	134,135	137,511	-	8,018	8,205	-

Source: Own work.

The selected industries that are more FDI intensive are wholesale and retail trade, repair of motor vehicles and motorcycles; professional, scientific and technical activities; construction; transportation and storage and manufacturing. Foreign owned enterprises in

selected industries represent 78% of total number of foreign owned enterprises in the Slovenian corporate sector in 2018 (80% in 2017).

While the number of foreign owned enterprises in absolute terms is the highest in the selected industries, they still represent a relatively low share of total companies in the selected sectors in comparison to national enterprises. The more FDI intensive industries appear to be also the industries with the highest number of national owned enterprises in the Slovenian corporate sector, as also the domestic companies from the selected industries represented 75% of all domestic companies in Slovenian corporate sector in 2017 and 2018.

The following Table 14 provides a further breakdown of the total value of selected performance indicators (i.e. turnover, export revenue, number of employees and value added at factor cost) for the latest available year 2018 and the share of foreign enterprises from the total that includes combined results for national and foreign enterprises.

Table 14: Total value of selected performance indicators by activity in 2018 (EUR m) and share of foreign enterprises (% of total)

Activity	Turnover	Share of foreign enterprises (%)	Export revenue	Share of foreign enterprises (%)	Number of employees	Share of foreign enterprises (%)	Value added at factor cost	Share of foreign enterprises (%)
Wholesale and retail trade, repair of motor vehicles and motorcycles	36,669	40%	5,737	40%	106,268	37%	4,500	40%
Professional, scientific and technical activities	5,017	12%	500	5%	37,412	10%	2,062	11%
Construction	5,953	9%	167	9%	54,869	10%	1,692	9%
Transportation and storage	6,367	22%	192	14%	47,204	17%	2,245	13%
Manufacturing	31,279	43%	19,401	54%	201,722	35%	8,811	37%
<i>% of total</i>	83%	-	95%	-	80%	-	80%	-
Other activities	17,098	21%	1,294	17%	113,410	21%	4,805	21%
Total	102,384	33%	27,291	48%	560,885	27%	24,114	28%

Source: Own work.

Regardless of relatively low absolute number of foreign owned companies in comparison to national enterprises and their representation in terms of total share of companies in

selected industries, based on the selected performance indicators, they nonetheless represent an important part of the Slovenian corporate sector. While the share of foreign owned enterprises in the selected industries in the Slovenian corporate sector does not exceed 10% of total number of enterprises in selected industries (see Table 13 on page 38), the analysis of selected performance indicators shows a different picture.

For example, in terms of turnover in selected industries in 2018, foreign owned enterprises generated 43% of turnover in manufacturing and 40% of total turnover in wholesale and retail trade, repair of motor vehicles and motorcycles, whilst foreign owned enterprises in these two industries are represented only by 4% and 9% share of total companies in the selected industries. In terms of export revenues, foreign owned enterprises generated 54% of export revenue in manufacturing and 40% of export revenue in wholesale and retail trade, repair of motor vehicles and motorcycles in 2018. Similarly, the analysis of number of employees distinguished by ownership and activity showed that foreign owned companies employed 35% of all employees in the manufacturing industry and 37% of total employees in wholesale and retail trade, repair of motor vehicles and motorcycles in 2018. Finally, looking also at value added at factor cost, foreign owned companies in manufacturing and wholesale and retail trade, repair of motor vehicles and motorcycles generated 37% and 40% of total value added at factor cost in 2018.

Summarizing the presented data, it can be observed that the share of foreign owned companies in the Slovenian corporate sector is increasing and also their importance in the Slovenian economy. The presented aggregated statistical data on performance of firms in foreign ownership in comparison to domestic enterprises, cannot be directly interpreted and compared, especially over the longer time period from 2013 - 2018. One of the main reasons is the fact that the share of foreign companies as a share of total companies in the Slovenian corporate sector was significantly increasing throughout the observed period, especially until year 2016. For example, according to statistical data collected by SURS, in 2008 the share of foreign companies accounted for 4.5% of all non-financial enterprises in the Slovenian corporate sector, in 2014 5.4% and in 2018 6.0%.

However, the overview of selected indicators of firms by industry provides a clearer picture of performance of firms in foreign ownership in comparison to national enterprises. From the overview, it is apparent that while firms in foreign ownership still represent a relatively low share in terms of all firms in the Slovenian corporate sector, they generate a fair share of total results of the selected performance indicators. This is especially evident in manufacturing and wholesale and retail trade, repair of motor vehicles and motorcycles, in which foreign owned firms contribute a large share of revenues and also employ a large share of total personnel, despite the low representation of foreign-owned firms in terms of total population of enterprises in the observed industries. At the same time, it appears that the reason for higher growth of foreign owned companies in absolute terms and in practically all observed indicators can also be attributed to the selection process of foreign investors, as they appear more invested into

industries and companies where above average profitability and high potential for penetration into new market or larger economies of scale can be expected. For detailed overview on performance of companies distinguished by ownership type and activity, please refer to Appendix 2.

3.3 Results of the survey among companies with foreign capital in Slovenia in 2020

The results of the survey among companies with foreign capital in Slovenia will serve as a basis for descriptive analysis of impact of foreign investments on the receiving companies. The presented data was gathered by CIR, Faculty of Social Sciences in their survey on perceptions of foreign investors about Slovenian environment, commissioned by SPIRIT Slovenia. The sample included total population of 1,204 companies with foreign capital, out of which 993 companies were reached in the course of survey from September 3rd to October 2nd, 2020. The questionnaire was ultimately answered by 213 companies with foreign capital, which represents a 21.5% response rate, if all the companies with foreign capital that were reached are considered, and 17.7% share of total population of companies with foreign capital. The sample companies and their perceptions related to the Slovenian business environment in the survey are analyzed and studied according to the size of the company, their activity and markets of the predominant realization of sales revenues (Jaklič & Koleša, 2020).

Out of foreign investors (owning 10% or more of equity in a Slovenian company) included in the sample of the 2020 survey the origin of investing country of 23.7% is Austria, 15.6% Germany, 9.0% Italy, 8.5% Croatia, 5.7% from Netherlands and 4.3% from Switzerland. The foreign ownership of the remaining share of sample companies (33.2%) relates to 25 different countries. The structure of the sample according to the origin country of foreign capital is similar to the structure of inward FDI, according to the macroeconomic data presented in the theoretical part of this master's thesis.

The majority of sample companies categorize as small businesses. Specifically, 4.0% of surveyed companies are micro companies (with up to 10 employees), 62.3% small companies (with 11-50 employees), 22.1% medium-sized companies (with 51 – 250 employees) and 11.6% large companies with more than 250 employees. The predominant part of the sample companies has 10 years or more experience in the Slovenian business environment (58%).

Relating to the industry, the predominant share of sample companies are service companies (65.8%), while only 34.2% of them operate in manufacturing. Among service companies, most (more than 50%) categorize as small companies (with less than 51 employees). On the other hand, larger companies are more common in manufacturing (8.0% of manufacturing companies versus 3.5% of service companies). In terms of revenue generation, the majority (55.3%) of sampled companies generate most of their

revenue on foreign markets (primarily large and medium-sized enterprises) and 44.7% mainly on the domestic markets (mostly micro-enterprises) (see Table 15).

Table 15: Sample companies by sector and target market (%)

Market	Manufacturing companies	Service companies	Total
Mostly export oriented	27.6%	27.6%	55.3%
Mostly oriented towards domestic market	6.5%	38.2%	44.7%
Total	34.2%	65.8%	100.0%

Source: Jaklič & Koleša (2020).

As it will be observable from the presented survey results in the continuation of this part of master's thesis, many sample companies did not observe any effects on their businesses in the areas that were analyzed in the survey. On the other hand, among the companies that did acknowledge a certain impact of foreign investment on their operations, the majority noticed positive impacts in all of the studied areas. According to analysis of sample companies' financial reports included in the survey, companies with foreign investment grew on the cumulative level in the observed year, according to several selected indicators. The research in the survey relied on the latest available financial data and thus compared financial results from 2019 to financial results from 2018. As it can be observed from Table 16, on average, sample companies have increased sales revenue, export activity, labor productivity, as well as the number of employees in the observed historical period.

Table 16: Selected indicators from the annual financial reports of companies with foreign investment, 2018 – 2019

Average values for sample companies (in EUR t if denoted with (*), otherwise absolute number)	2019	Average growth rate 2019/2018 (in %)	Average values for companies with FDI in Slovenia (according to data collected by BS)
Added value*	6,504,000	n.a.	6,659,000
Added value per employee	53,650	7.6	53,775
Number of employees	139	14.6	103
Sales revenue*	24,533,810	13.5	30,966,000
Export	11,157,743	14.1	16,199,000
Export intensity (in terms of sales revenue)	53.7%	n.a.	52.3%
Net profit*	1,035,780	n.a.	1,619,000

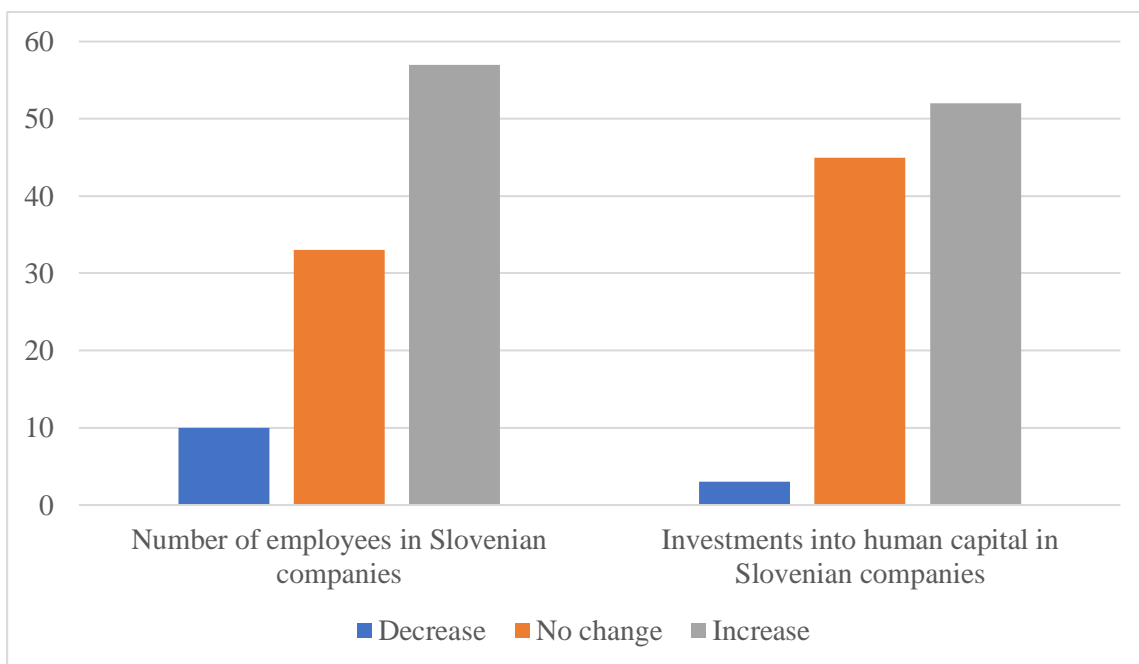
Source: Jaklič & Koleša (2020).

In comparison to total population of companies with foreign capital, sample companies recorded slightly lower sales revenue and net profit in 2019, while other performance indicators showed higher or similar results than those of total population. It is important also to note that in comparison to 2018 sample companies recorded increase in sales

revenue (13.5%), export revenue (14.1%), number of employees (14.6%) and added value per employee (7.6%).

Looking more into details of individual selected indicators of effects of FDI on companies with foreign capital, the largest share of companies noting positive effects coming from foreign investment was observed in the area of employment and investments into human capital development in Slovenian companies. Out of 183 sample companies, 57% observed increase in employment on the account of foreign investment and only 10% of sample companies, under the same circumstances, observed decrease in employment. The positive effects of FDI on growth in number of employees in comparison to number of employees before the entrance of foreign investor, was noted in companies of all sizes. Specifically, among sample companies 58% small companies, 55% medium-sized companies and 59% large companies recorded an increase in employment, irrelevant of their primary activity (59% manufacturing and 56% service companies answered positively regarding increasing number of employees).

Figure 6: Impact of FDI on employment and human capital development 2020 (% of total sample companies)



N = 183 (number of employees), 184 (investments into human capital)

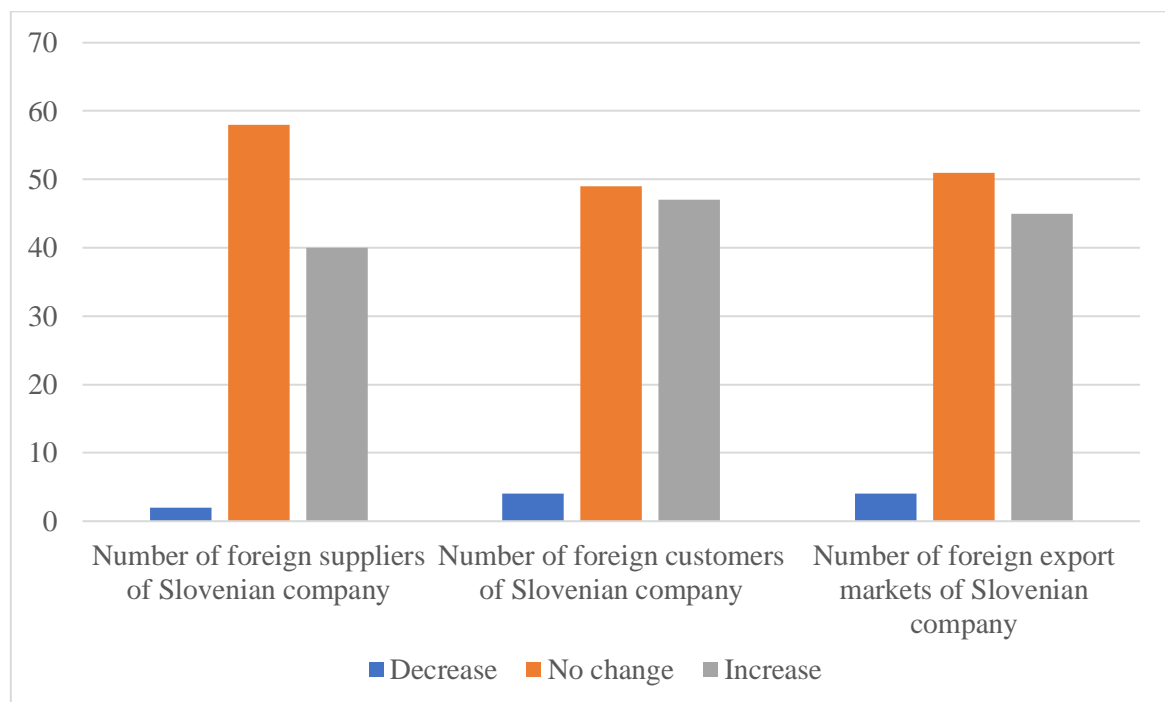
Source: Jaklič & Koleša (2020).

As it can be observed in Figure 6, similarly as with number of employees in Slovenian companies with foreign capital, the majority of sampled companies (52%) noted that FDI has positively influenced the increase in investments into human capital development and only 3% out of sample companies observed a decrease in such investments in comparison to investments into human capital before the entrance of foreign investor.

The results by the size of the company are similar as with results for number of employees. The increase was observed in 48% small sample companies, 63% medium-sized sample companies and 59% large sample companies, which shows that rate of employment goes hand in hand with investments into human capital development. However, by contrast to number of employees which showed small differences in results comparing service and manufacturing companies, the survey reports that a larger share of companies investing in human resources is among manufacturing companies (44%) than service companies (28%).

Further results of the survey also found positive effects of FDI in the field of internationalization of the companies with foreign ownership and their export orientation. With regards to internationalization before and after the entrance of foreign investor the survey tracked the effect of FDI on increase or decrease of supplier networks, foreign customers networks and geographical dispersion of exports (see Figure 7).

Figure 7: Impact of FDI on internationalization of Slovenian companies 2020 (% of total sample companies)



N = 180 (number of foreign suppliers), 181 (number of foreign customers and export markets)

Source: Jaklič & Koleša (2020).

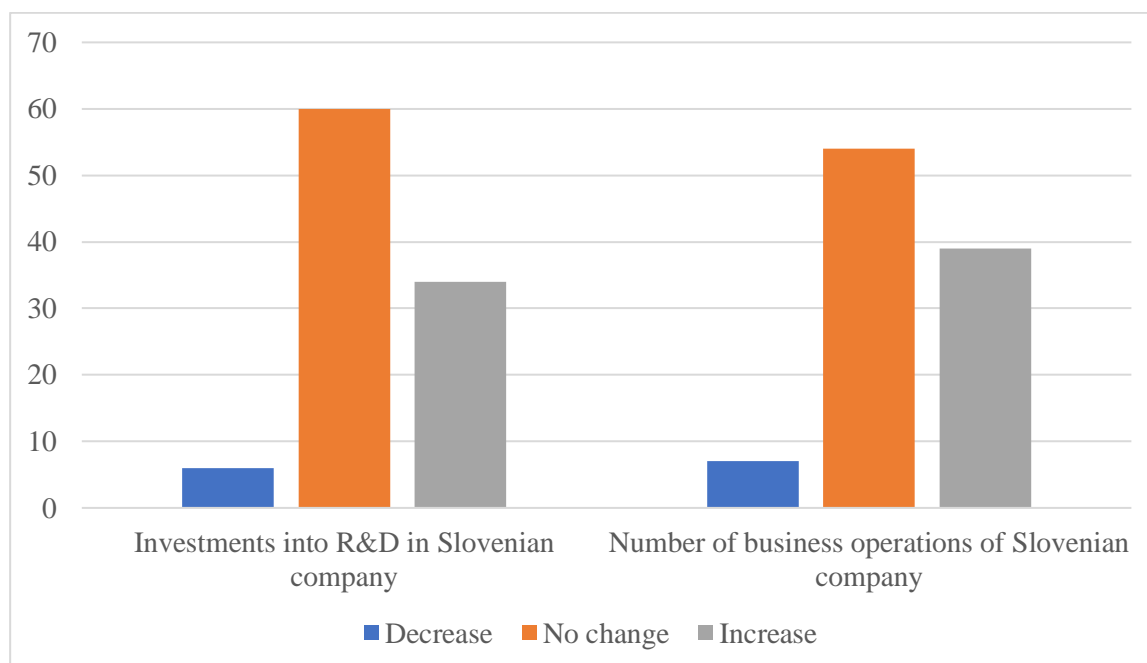
The results show that foreign investments indeed strengthened the presence of Slovenian companies with foreign investment in foreign markets. The surveyed companies observed the highest positive effects in increasing the number of foreign customers (47% of sampled companies), followed by increase in export markets (45%) and also increase in number of foreign suppliers (40%). According to the survey, the positive benefits of

internationalization relate mostly to large companies (72% of them increased the number of foreign customers, 64% increased the number of foreign suppliers and 59% increased the number of export markets). Furthermore, positive effects are mostly recorded by companies from manufacturing sector, which are de facto more export oriented.

The survey also examined the impact of FDI on business functions, measuring the level of diversification of business operations before and after FDI. The impact of FDI for this category appears less relevant as the majority of sample companies did not observe any changes in business operations due to foreign investments. However, 39% of sample companies with foreign capital still increased the number of business operations and 34% increased investments into R&D after entrance of foreign investor (see Figure 8).

The diversification of business operations thus appears not to be connected to the type of ownership. However, for this interpretation, also development in Slovenian-owned companies would need to be compared with the presented results on companies in foreign ownership.

Figure 8: Impact of FDI on business functions of Slovenian companies 2020 (% of total sample companies)



N = 178 (investments into R&D), 181 (number of business operations)

Source: Jaklič & Koleša (2020).

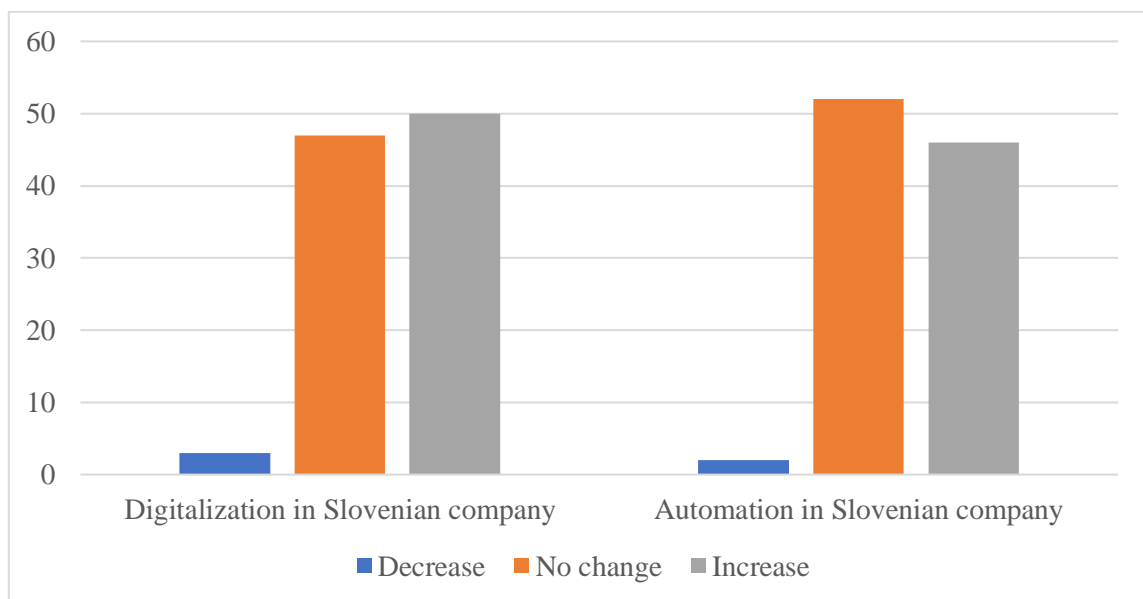
Again, most of the sample companies that observed the increase in business operations were large companies (46% of large companies), closely followed by medium-sized companies (40%) and small companies (37%). Regarding industry classification, the

increased complexity of business operations was higher among service companies (42%), than manufacturing (33%).

On the other hand, increase in investments into R&D showed higher discrepancies among the different structured companies. The effect of FDI related to R&D is most observable in large sample companies, out of which 50% increased such investments after entrance of foreign investor. Also, in contrast to number of business operations, R&D investments are more intensive among manufacturing companies (46%) than service companies (37%).

Similar trends were identified among the positive effects of FDI on Slovenian companies in terms of digitalization and automation of their business. As presented in Figure 9, 50% of sample companies increased their level of digitalization with foreign investment and 46% increased their level of automation. Only 2.1% of sample companies experienced a decrease in level of digitalization and automation in connection to foreign investment. Based on the survey results, it can be assumed that foreign ownership has positive impact of increased levels of digitalization and automation of Slovenian companies.

Figure 9: Impact of FDI on digitalization and automation of Slovenian companies 2020 (% of total sample companies)



N = 181 (digitalisation), 180 (automation)

Source: Jaklič & Koleša (2020).

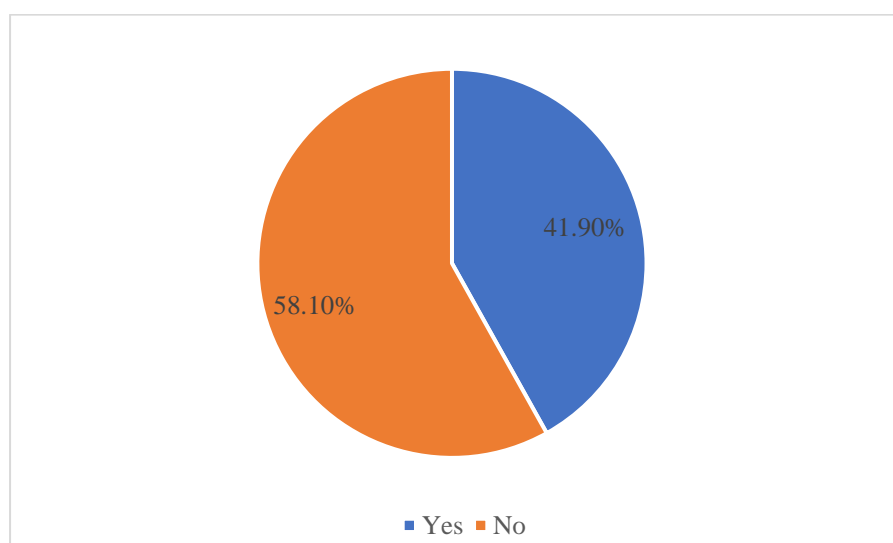
The most intensive processes of automation were noticeable among large companies, as 73% of sample companies increased their levels of automation and among manufacturing companies, out of which 56% increased their level of automation due to foreign investment. Digitalization levels were also correlated with the size of the company with

foreign capital, as increase was reported by 68% of large sample companies, 56% of medium-size sample companies, 46% of small companies and 33% of micro companies included in the survey. Technological modernization is to a greater extent present in manufacturing companies than service companies.

Additionally, the survey also addressed the planning of future investment projects of firms with foreign capital in general, their investment plans in Slovenia and their plans to expand outside Slovenia. It is important to note, that in light of the COVID-19 pandemic that had a significant impact on business operations of all companies, the sample companies also highlighted the fact that their future business expansions depend on the general epidemiological situation and economic situation in Slovenia and in the region.

The majority of sample companies do not plan new investment projects for 2021 (58.1%). Only 41.9% of sample companies stated they have plans for new investment projects in 2021, which include strategic and operational projects (for example investments into plant and equipment, business premises, digitalization and automatization, R&D, business expansions, human capital etc.).

Figure 10: Investment planning for 2021 (% of total sample companies)

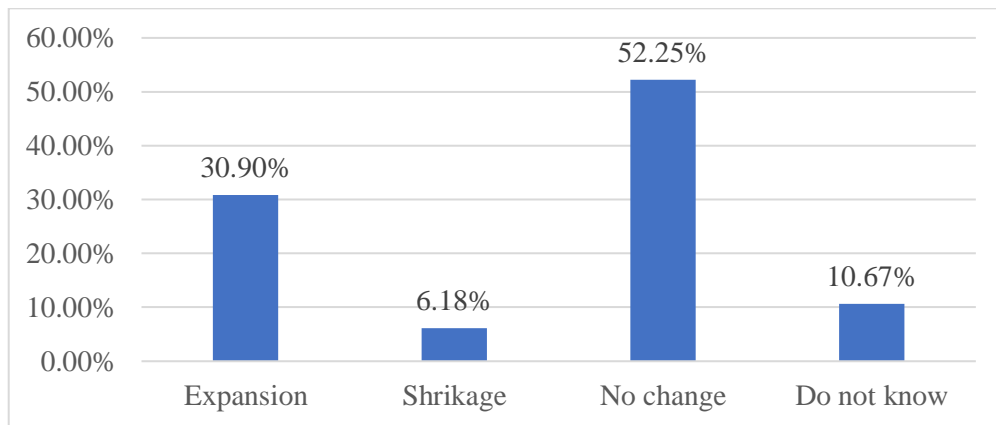


N = 179

Source: Jaklič & Koleša (2020).

With focus specifically on Slovenia, the majority of survey companies (52.2%) does not plan any changes in investment, while part of sample companies is not informed about the investment plans of foreign investor. 30.9% of sample companies plan to expand in Slovenia and 6.2% plan shrinkage of their business activity.

Figure 11: Investment planning for 2021 in Slovenia (% of total sample companies)

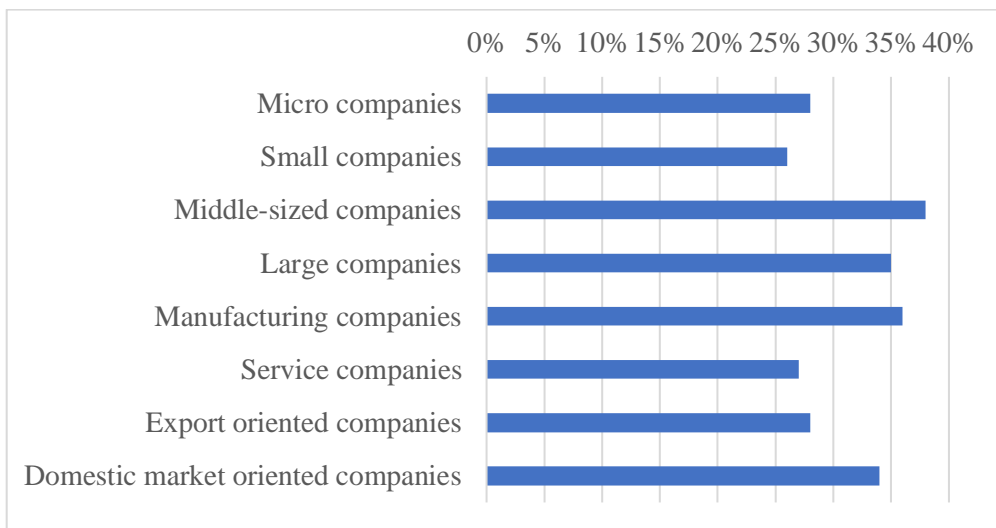


N = 178

Source: Jaklič & Koleša (2020).

The majority of companies planning further investments in Slovenia are middle-sized or large companies predominantly from manufacturing sector.

Figure 12: Investment planning for 2021 by share of sample companies from each category (% of total sample companies from each listed category)

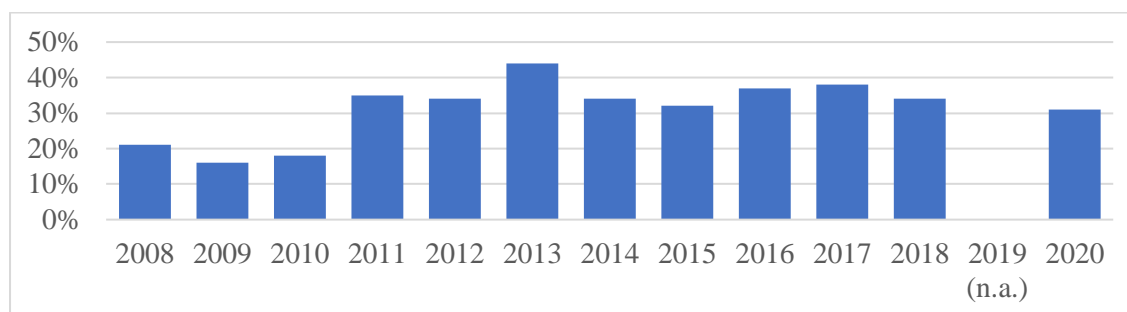


N = 172

Source: Jaklič & Koleša (2020).

Interestingly, the expansion plans of companies with foreign capital in Slovenia are similar to those reported by companies in researches from previous years (N differentiates over the years and the survey was not conducted in year 2019), despite COVID-19 pandemic. However, as mentioned above, also the intended expansion plans will depend on future developments of the epidemiological situation.

Figure 13: Investment planning in the period 2008 – 2020 (% of total sample companies that planned investment from each year's sample)

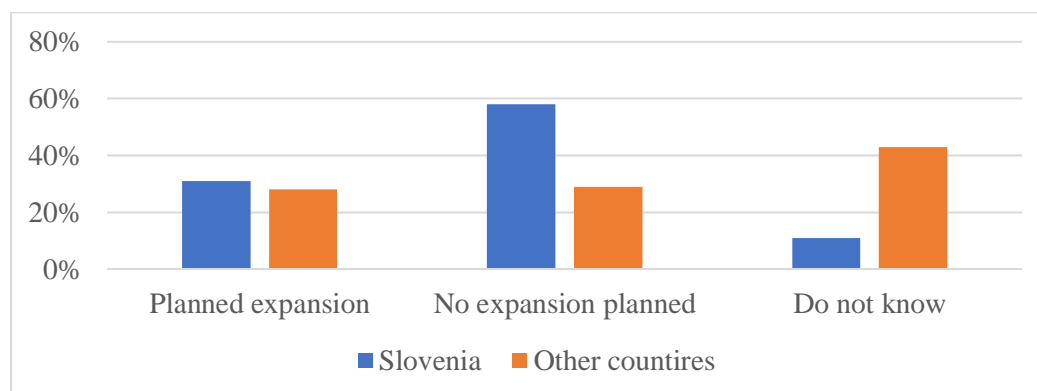


Source: Jaklič & Koleša (2020).

While the according to the growth in investment plans of companies with foreign capital in Slovenia over the observed historical period, it can be concluded that Slovenia has the potential for attracting new FDI, it can also be expected that new investments by existing investors can be expected to limited extent, as the majority (more than 58%) of sample companies with foreign capital do not plan to expand in Slovenia.

Looking also at share of sample companies that plan investments in 2021 outside of Slovenia, we notice that similar share of companies that plan new investments in Slovenia also plans investments outside of Slovenia.

Figure 14: Investment planning in 2021 in Slovenia and outside of Slovenia (% of total sample companies)



N = 178 (Slovenia), N= 177 (Other countries)

Source: Jaklič & Koleša (2020).

According to the results, sample companies evaluate investment locations in a comparative manner, and foreign investors in Slovenia also have investment plans in many other locations. In terms of investments into other countries, the surveyed companies most commonly listed planned investments and expansions to Germany, Austria and Poland and also to USA, Serbia and the Czech Republic. Some of the sample

companies only listed the regions where they plan to expand instead of specific locations, and most often they listed EU or Europe. As these are investments plans of foreign investors that are already present on the Slovenian market, their plans also confirm the theoretical suggestion about foreign investors choosing Slovenia for investment due to its locational advantages and with its access to other foreign markets, especially in the EU.

To summarize, the effects of FDI on Slovenian companies are noticeable in changes in the number of employees and business functions, investments into human resources development, R&D, automation and the number of foreign suppliers, customers and export markets of Slovenian companies with foreign ownership. In all these areas, based on the collected responses of the sample companies, the positive effects of FDI on domestic companies receiving foreign investment are much more common than negative effects. The presented results are relevant for companies that received foreign investment, while companies in Slovenian ownership were not included in the sample for comparison of results.

The most pronounced positive effects of FDI are reflected in increased number of employees and greater investments of companies in human resources development. While more than half of sample companies did not notice positive benefits in the organization and implementation of business functions, investments into R&D and the number of foreign suppliers due to foreign investments, the share of companies receiving foreign investments and noticing positive effects in these business segments is not negligible. 39% of sample companies have increased the number of business functions they perform in the company, more than a third increased investment in R&D and 40% the number of foreign suppliers.

Based on the results of the survey, it can be concluded that if FDI has effects on the domestic company, they tend to be positive. Furthermore, based on the survey results, it can be concluded that foreign investors perceive the Slovenian economy as attractive for investments, both in terms of expansion on the Slovenian market, as well as Slovenia being a starting point for accessing foreign markets, mostly based in the EU or Europe.

3.4 Recommendations based on results of the research

As observed in the empirical part of this master's thesis, Slovenia leads an open and competitive economy, that is strongly export oriented and well-integrated in GVCs. Nevertheless, the role of FDI in Slovenian economy is still relatively small (representing less than one-third of Slovenia's GDP), which signals that Slovenia has not yet reached its full potential in attracting inward FDI. (Kušar, 2020).

Looking at the structure of inward stock of FDI in 2019, the most important foreign investors in Slovenia originate in Austria, Luxembourg, Switzerland, Italy and Germany, which means that the future of FDI in Slovenia depends greatly on economic conditions

in the EU (Kušar, 2020). COVID-19 health crisis, geopolitical and financial risks and continuing trade tensions all together have an effect on falling of investors' confidence and add to the uncertainty of the future. Changes due to uncertain future are already demonstrating in changes in the nature of FDI in all the regions in the world. While UNCTAD expects the global economy to recover already in 2022, it also predicted that the pandemic could have lasting effects on investment policymaking, especially in terms of the degree of fragmentation and the length of GVCs, geographical spread of value added and governance choices of MNEs that would rather change long value chains for arm's-length trade. As per UNCTAD's predictions, despite the drastic decline in global FDI flows during the crisis, the international production system is expected to continue to play an important role in economic growth and development (UNCTAD, 2020). In these unprecedented times, it is thus important also for Slovenia to rethink its policymaking decisions regarding FDI and position in global economy as a host country for FDI.

According to World Bank's document by Wells, Jr & Wint (2000) marketing a country, with regards to attracting foreign investments, includes a three steps approach including marketing of:

- The product (in terms of a country this relates to advantages and disadvantages of an investment location)
- the price (in terms of tax incentives, tariff protection and grants, which effect the const of entrance for an investor) and
- promotion (creating an incentivizing image of host country and provision of investment services for the perspective investor) (Wells, Jr. & Wint, 2000).

The policies and marketing activities to make the most of inward FDI in terms of economic development of a host country, however, need to be context specific to attract and retain the right type of FDI, while at the same time focusing on promoting upgrade of the activities and investments of existing FDI. Through promotional techniques, the relevant sources (i.e. municipalities, ministries, public agencies), can advertise specific advantages and sector-specific opportunities and through that greatly impact the overall image and of a host-country in the global economy and investment generation. According to Wells, Jr. & Wint (2000) the idea of targeting the right type of FDI can mean either targeting a particular type of investor or a particular type of project for investment. In a sense of targeting a particular type of investor, agencies can identify a group of prospective investors by sector, geography, size etc., that can be matched with competitive advantages a particular country has to offer. On the other hand, targeting a particular type of project for investment relates also to host country's image, that can be built through engagement in targeted image-building programs (Wells, Jr. & Wint, 2000).

In case of Slovenia, it is important to highlight key geographical features of Slovenia, as one of the key enticements for MNEs to enter in Slovenia is the pursuit of markets and

strategic business development. The geographical advantages of Slovenia as a host country for FDI can be seen in a context of position at the crossroads of several major European regions as well as in a context of foreign trade relationship developed between Slovenia and neighboring countries and other EU members (Kušar, 2020). However, while Slovenia can build its image on its advantage of favorable investment location, it still faces the problem of high operational requirements and administrative barriers for foreign investors. In this sense, according to the survey conducted by SPIRT and CIR in 2018, the most common proposals of foreign investors regarding actions towards more FDI friendly environment are those relating to taxes and reduction of operating costs, regulation of labor market and payment discipline, as well as reduction of administrative burdens, simplification of administrative procedures and increase in efficiency and professionalism of the Slovenian public administration (Jaklič, Koleša, & Knez, 2018). As observed by Kušar (2020), MNEs often expect additional support coming from local governments – in case of Slovenia municipalities, in terms of more active support in finding solutions to the problems they face (Kušar, 2020). Adequate local support is especially important in a context of greenfield investments, which depend highly on planned industrial zones (in terms of necessary infrastructure, at locations near highway exits etc.). In this sense, Slovenia faces an obstacle, as the second-tier government is highly fragmented and regional development over the country highly uneven. The administrative barriers, lack of local support and decentralization across Slovenia thus appear to be the major challenges to tackle for Slovenia as host country. One of main attractions of Slovenia as a host country in terms of easy access to necessary resources is also the relatively well educated and highly trained workforce. However, the prospects for the future show that there is already a mismatch existing between the type of labor that is sought after and the type of labor that is available and companies operating in Slovenia often need to hire workers from other countries (Kušar, 2020). This trend is especially already noticeable in the manufacturing sector (Jaklič, Koleša, & Knez, 2018). In this context, in the future it will be important for Slovenia to address this mismatch between available educated workforce and attracted FDI.

Summing up, until now Slovenia in terms of FDI has been mostly integrated in the international markets through commodity markets and less in services. The majority of attracted inward FDI in Slovenia is concentrated in the labor-oriented manufacturing sector, where Slovenia lacks the appropriately educated workforce. Furthermore, it is important for Slovenia to work on policymaking on local levels as especially greenfield investments rely highly on appropriate industrial zones. Going forward, it is important to reconsider Slovenia's advantages in comparison to similar competing investment locations in terms of making the most for economic development of the country on the account of attracting the right type of FDI.

CONCLUSION

The present thesis addressed the importance of FDI as a vehicle of global economic development, the characteristics and effects of FDI, current global trends and future prediction on FDI flows and the role FDI plays in the Slovenian economy. The theoretical overview provided a framework, based on which the most common theoretical suggestions on benefits and negative effects FDI can spur was challenged and verified in the empirical part of the thesis.

Based on the review of the relevant literature, it is evident that the benefits arising from FDI do not occur automatically with foreign investment. Different types of FDI are likely to have different impact on the host economies and the impact is also highly dependent on the host country's predispositions that allow it to absorb the potential beneficial effects from FDI, as well as the general country's policy framework regarding FDI that manages the attraction of the right type of FDI to spur the domestic economic development.

In line with global FDI trends, also Slovenia has started to increase its participation in FDI flows. However, based on the reviewed trends of inward FDI, Slovenia has not yet harnessed its full potential in attracting FDI. In comparison to comparable countries by levels of development, Slovenia's level of inward FDI to this day remains relatively low. No matter the low activity of foreign investors in Slovenia, the companies receiving foreign capital, play an important role in the Slovenian economy.

The purpose of this master's thesis research was to determine what type of investment and what type of companies foreign investors choose when deciding to invest in Slovenia and what are the effects arising from the FDI. The overview of economic trends and indicators on performance of companies with foreign capital in comparison to national enterprises has shown that firms in foreign ownership grow faster. The higher growth was determined based on the growth rates of cumulative turnover, export revenue, number of employees and added value based on factor cost. While the results on the cumulative basis over a longer time period cannot be directly interpreted, as the share of firms with foreign capital in terms of total population of enterprises in the Slovenian corporate sector has been increasing significantly over the observed period of time, the in-depth analysis of participation of companies in foreign ownership in the selected industries has shown more accurate results. The analysis has shown that while the share of foreign companies in the selected individual industries does not exceed 10% of total enterprises operating in the selected industries, their contribution in terms of the selected indicators points towards better performance. This trend is especially apparent in the manufacturing industry and wholesale and retail trade, repair of motor vehicles and motorcycles. It is important to note that Slovenia is strongly export-oriented and well-integrated with GVCs, predominantly in manufacturing and wholesale and retail trade, repair of motor vehicles and motorcycles. Based on this, it appears that foreign investors in Slovenia are predominantly interested in the export-oriented industries that have high potential for

penetration of new markets. This trend is in line with defined motives for investment in Slovenia, as besides its geographical location, Slovenia has strong connections with economically important regions especially in neighboring countries and wider EU and European markets.

Based on additional analysis that was done on the basis of survey on perceptions about the Slovenian business environment among foreign investors conducted by CIR, Faculty of Social Sciences and commissioned by SPIRIT Slovenia, the effects on Slovenian domestic companies receiving foreign investment are predominantly positive. The survey focused on the analysis of business areas, that are also most commonly cited in theoretical literature focused on positive effect arising from FDI – impact on productivity, impact on export orientation, impact on employment and technology transfers and innovation. While the survey firstly confirms that the effects from FDI are not automatic, as many sample companies did not identify any effects on their business in the studied areas, the positive effects from FDI cannot be neglected, as among the companies that did acknowledge a certain impact of foreign investment on their operations, the majority noticed positive impact in all of the studied areas.

The most noticeable positive effect of foreign investment on Slovenian companies was identified in the area of employment, that was reported by more than 50% of sample companies, regardless of their size. However, the larger share of companies that noticed also increase in investments into human capital, was predominantly reported by manufacturing companies. Similar trend is noticeable when observing the level of internationalization after foreign investments, where the positive effects were also concentrated in the companies from the manufacturing sector, that are de facto more export oriented. While R&D investments after the entrance of foreign investor were identified by a smaller share of sample companies the positive effect again concentrated among the companies from the manufacturing sector. On the other hand, sampled service companies recorded a higher increase in diversification of their business operations. Lastly, also increase in levels of digitalization and automation is predominant in the manufacturing sector.

The common trend evident from the theoretical overview and empirical research is that foreign investors investing in Slovenia are mostly interested in the manufacturing, export-oriented industries, which are also Slovenia's main advantage. It is also evident, that the companies from manufacturing sector receiving foreign investment tend to capture most of the positive effects that can be triggered by FDI. The positive effects are also noticeable in the performance of companies in foreign ownership, which show higher growth rates than comparable national enterprises. The question, however, remains on whether the investments targeting mostly the manufacturing, export-oriented industries are the preferred type of FDI for future economic development of the country. As identified by Kušar (2020), Slovenia should also focus on attracting investments in services and high-

technology industries, that would also incentives construction of new high-quality work facilities.

Based on identified future plans of expansion of existing foreign investors in Slovenia, it is evident that Slovenia has high potential to attract also new foreign investors. However, as Slovenia is strongly internationalized, especially within the EU space, recent developments in the global economy and its implications cannot be neglected when considering the future of FDI dynamics in Slovenia. In light of recent unprecedented COVID-19 pandemic and other geo-political developments that initiated more restrictive trade policies, future positioning and identification of Slovenia as a destination for FDI is very important. As the global economic structure is shifting, the new structure might have positive implications for Slovenia in terms of attracting new investments. While foreign investors might be more conservative due to the uncertain future, in the light of Slovenia's proximity to the economic core of the EU, they be incentivized to disperse their GVC vulnerability while retaining strategic/specialized suppliers (Kušar, 2020).

Answers to the research question set in the thesis provided a better understanding of the importance and scope of inward FDI in Slovenia, as well as its current state in the Slovenian economy. Based on the results of the research, going forward, it is very important for Slovenia to strategically communicate the advantages of Slovenia as a destination for FDI.

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APPENDICES

Appendix 1: Povzetek (Summary in Slovene language)

Predstavljeno magistrsko delo obravnava pomen tujih neposrednih investicij (TNI) kot nosilca svetovnega gospodarskega razvoja, značilnosti in učinke TNI, trenutne svetovne trende in prihodnje napovedi glede tokov TNI, ter vlogo TNI v slovenskem gospodarstvu. Teoretični pregled magistrskega dela služi kot okvir, na podlagi katerega empirični del naloge obravnava rezultate glede najpogostejših teoretičnih predpostavk glede pozitivnih in negativnih učinkov spodbujenih s strani TNI, na primeru Slovenije kot države gostiteljice.

Na podlagi pregleda ustrezne literature je razvidno, da pozitivni učinki, ki lahko izhajajo iz TNI, niso samodejni ob pojavu TNI. Različne vrste TNI imajo lahko različne vplive na države gostiteljice, prav tako pa so pozitivni učinki večinoma tudi močno odvisni od predispozicij države gostiteljice, ki ji omogočajo, da absorbira potencialne pozitivne učinke TNI. Prav tako pa so pozitivni učinki, izhajajoči iz TNI, odvisni tudi od splošnega političnega okvira posamezne države glede TNI, ki služi kot temelj za pridobivanje prave vrste TNI za spodbujanje razvoja domačega gospodarskega okolja.

Skladno s svetovnimi trendi TNI je tudi Slovenija začela povečevati svojo udeležbo v tokovih TNI. Vendar pa je na podlagi pregledanih trendov vstopnih TNI v Sloveniji razvidno, da Slovenija še ni izkoristila svojega celotnega potenciala za privabljanje TNI. V primerjavi s primerljivimi državami po stopnjah razvoja je namreč razvidno, da raven TNI v Sloveniji do danes ostaja razmeroma nizka. Ne glede na nizko udeležbo tujih vlagateljev v Sloveniji pa podjetja s tujim kapitalom igrajo pomembno vlogo v slovenskem gospodarstvu.

Namen raziskave predstavljene magistrske naloge je bila obravnava ključnega vprašanja: »kakšne vrste naložb in katere vrste podjetji tuji vlagatelji izberejo, ko se odločajo za naložbo v Slovenijo, ter kakšni so učinki izhajajoči iz neposrednih tujih naložb«. Pregled trenutnega stanja podjetji s tujim kapitalom v slovenskem gospodarstvu v primerjavi z domačimi podjetji, je pokazal, da podjetja v tuji rasti v povprečju rastejo hitreje. Višja rast je bila ugotovljena na podlagi pregleda stopenj rasti kumulativnega prihodka, rasti prihodkov iz izvoza, števila zaposlenih in dodatne vrednosti na podlagi stroškovnega faktorja. Medtem ko neposredna razlaga in splošna aplikacija rezultatov na celotno populacijo podjetji s tujim kapitalom ni mogoča predvsem v pregledu daljšega časovnega obdobja, saj se je delež podjetji s tujim kapitalom glede na celotno populacijo podjetji v slovenskem podjetniškem sektorju v opazovanem obdobju znatno povečeval, je poglobljena analiza udeležbe podjetji v tuji lasti v izbranih panogah pokazala natančnejše rezultate. Analiza je pokazala, da kljub nizkemu deležu tujih podjetji, ki v izbranih panogah ne presega 10% celotnega števila podjetji, njihov prispevek glede na izbrane kazalnike uspešnosti kaže na boljše poslovanje v primerjavi z domačimi podjetji. Opažen trend je predvsem očiten v predelovalni industriji v trgovini na debelo in drobno, popravilu motornih vozil in motociklov. Na tej točki je pomembno omeniti tudi, da je

Slovenija na splošno močno izvozno naravnana in dobro integrirana v globalnih vrednostnih verigah in to predvsem v predelovalnih dejavnostih ter v trgovini na drobno, popravih motornih vozil in motornih koles. Na podlagi tega lahko sklepamo, da se tuji vlagatelji v Sloveniji zanimajo predvsem za izvozno usmerjene panoge, ki imajo velik potencial za širitev na nove tuje trge. Opazovan trend je prav tako v skladu z opredeljenimi motivi tujih investitorjev za naložbe v Sloveniji, saj ima Slovenija poleg svoje geografsko močne lege prav tako močne povezave z gospodarsko pomembnimi državami v regiji, zlasti v sosednjih državah ter na trgih EU in Evrope.

Dodatna analiza, ki je temeljila na raziskavi o percepcijah tujih investitorjev o slovenskem poslovnem okolju, ki jo je v letu 2020 po naročilu SPIRIT Slovenija izvedel Center za mednarodne odnose, Fakultete za družbene vede, je pokazala, da so učinki na slovenska domača podjetja, ki prejemajo tuje naložbe, v veliki večini pozitivni. Raziskava, ki je temeljila na anketi podjetji s tujim kapitalom, je bila osredotočena na analizo poslovnih področji, ki so glede učinkov TNI prav tako najpogosteje navedena v teoretični literaturi – vpliv na produktivnost, vpliv na izvozno usmerjenost, vpliv na zaposlovanje ter na prenos tehnoloških znanj in inovacij. Medtem ko raziskava najprej potrjuje dejstvo, da učinki TNI niso samodejni, saj številna vzorčna podjetja niso zaznala nobenega vpliva na svoje poslovanje na preučevanih področjih, raziskava prav tako potrjuje, da pozitivnih učinkov TNI ni mogoče popolnoma zanemariti, saj med podjetji, ki so zaznala določen vpliv tujih investicij na poslovanje, prevladuje opažanje pozitivnih vplivov na vseh preučevanih področjih.

Najbolj opazen pozitiven učinek izhajajoč iz TNI je bil med anketiranimi podjetji zaznan na področju višje stopnje zaposlovanja, o čemer je poročalo več kot 50% vzorčnih podjetji, ne glede na velikost podjetja. Prav tako je večina podjetji zaznala povečanje naložb v človeški kapital, vendar pa so na tem področju glede pozitivnih učinkov prevladala podjetja iz predelovalne dejavnosti. Podoben trend je bil opažen tudi pri povečani stopnji internacionalizacije po vstopu tujega investitorja, saj so bili pozitivni učinki prav tako koncentrirani med podjetji s tujim kapitalom iz predelovalnih dejavnosti, ki so že v osnovi bolj izvozno usmerjena. Medtem ko povečanje naložb v raziskave in razvoj po vstopu tujega vlagatelja opaža zgolj manjši delež vzorčnih podjetji, je pozitiven učinek iz tega naslova ponovno najbolj pogost med podjetji iz predelovalnega sektorja. Po drugi strani pa so storitvena podjetja iz vzorca opazila porast v diverzifikaciji svojega poslovanja. Nazadnje pa v proizvodnih dejavnostih prav tako prevladuje pozitiven učinek povečanja ravni digitalizacije in avtomatizacije.

Skupna točka v trendih, ki so razvidni iz teoretičnega okvirja in empirične raziskave, je, da tuje vlagatelje, ki investirajo v Slovenijo, zanimajo predvsem predelovalne, primarno izvozno usmerjene industrije, ki pa so hkrati tudi glavna prednost slovenskega gospodarstva. Prav tako je razvidno, da podjetja iz predelovanih dejavnosti, ki so prejemniki tujih naložb, po navadi zaznavajo večino pozitivnih učinkov, ki lahko izhajajo iz tujih neposrednih naložb. Pozitivni učinki so opazni tudi pri poslovanju podjetji v tuji

lasti, ki kažejo višje stopnje rasti kot primerljiva nacionalna podjetja. Ne glede na trende opazovane v empirični raziskavi, pa ostaja vprašanje, ali so tuje naložbe, ki so usmerjene predvsem v predelovalne, izvozno naravnane panoge, preferenčna vrsta TNI za nadaljnji razvoj slovenskega gospodarstva. Kot ugotavlja Kušar (2020), bi se morala Slovenija osredotočiti tudi na privabljanje naložb v storitvenih in visokotehnoloških industrijah, kar bi spodbudilo nadaljnji razvoj tudi z gradnjo visokokakovostnih delovnih proizvodnih objektov.

Na podlagi opredeljenih načrtov obstoječih tujih vlagateljev glede nadaljnjih širitev, je razvidno, da ima Slovenija še velik potencial tudi za privabljanje novih tujih vlagateljev. Ker pa je Slovenija močno internacionalizirana, zlasti v sklopu EU, pri opredelitvi prihodnosti v dinamiki TNI v Sloveniji, ni mogoče zanemariti nedavnih trendov v svetovnem gospodarstvu in njihovih posledic. V luči nedavne pandemije korona virusa in drugih geopolitičnih trendov, ki so vplivali na vzpostavitev restriktivnejših trgovinskih politik posameznih držav, je prihodnja umestitev in identifikacija Slovenija kot destinacije za TNI zelo pomembna. Spremembe v strukturi svetovnega gospodarstva imajo namreč lahko v smislu privabljanja novih TNI za Slovenijo tudi pozitivne posledice. Medtem ko bi bili tuji investitorji zaradi negotove prihodnosti morda lahko bolj konservativni pri novih investicijah, jih lahko bližina Slovenije gospodarskemu jedru EU spodbudi k investiciji v Slovenijo, s katero bi razpršili tveganja v svojih globalnih vrednostih verigah, hkrati pa obdržali svoje strateške/specializirane poslovne partnerje (Kušar, 2020).

Odgovori na raziskovalno vprašanje, zastavljeno v magistrski nalogi, omogočajo boljše razumevanje pomena in obsega TNI v Sloveniji, ter njihovega trenutnega stanja v slovenskem gospodarstvu. Na podlagi rezultatov raziskave, bo v prihodnosti strateško komuniciranje prednosti Slovenije kot destinacije za TNI ključnega pomena za Slovenijo.

Appendix 2: Breakdown of selected performance indicators for the latest available year 2017 – 2018, by ownership groups and industries

a) Turnover by ownership and activity 2017 – 2018 (EUR m)

Activity	National enterprises			Foreign owned enterprises		
	2017	2018	% of total within industry in 2018	2017	2018	% of total within industry in 2018
Wholesale and retail trade, repair of motor vehicles and motorcycles	20,553	22,093	60%	13,252	14,576	40%
Professional, scientific and technical activities	4,019	4,391	88%	558	627	12%
Construction	4,438	5,422	91%	405	531	9%
Transportation and storage	4,625	4,952	78%	1,203	1,415	22%
Manufacturing	17,539	17,818	57%	11,814	13,461	43%
% of total	79%	80%	-	50%	50%	-
Other	13,407	13,512	-	3,462	3,587	-
Total	64,580	68,188	-	30,695	34,196	-

Source: Own work.

b) Export revenue by ownership and activity 2017 – 2018 (EUR m)

Activity	National enterprises			Foreign owned enterprises		
	2017	2018	% of total within industry in 2018	2017	2018	% of total within industry in 2018
Wholesale and retail trade, repair of motor vehicles and motorcycles	2,960	3,468	60%	2,121	2,269	40%
Professional, scientific and technical activities	432	473	95%	30	26	5%
Construction	124	152	91%	16	15	9%
Transportation and storage	135	165	86%	28	27	14%
Manufacturing	8,814	8,858	46%	9,065	10,543	54%
% of total	93%	92%	-	98%	98%	-
Other	975	1,070	-	215	224	-
Total	13,440	14,186	-	11,475	13,105	-

Source: Own work.

Number of employees by ownership and activity 2017 – 2018 (absolute number)

Activity	National enterprises			Foreign owned enterprises		
	2017	2018	% of total within industry in 2018	2017	2018	% of total within industry in 2018
Wholesale and retail trade, repair of motor vehicles and motorcycles	65,953	67,263	63%	37,060	39,005	37%
Professional, scientific and technical activities	33,075	33,730	90%	3,490	3,682	10%
Construction	45,113	49,416	90%	5,205	5,453	10%
Transportation and storage	37,241	39,158	83%	7,031	8,046	17%
Manufacturing	129,446	130,196	65%	63,651	71,526	35%
<i>% of total</i>	<i>93%</i>	<i>92%</i>	-	<i>98%</i>	<i>98%</i>	-
Other	88,143	89,612	-	22,110	23,798	-
Total	398,971	409,375	-	138,547	151,510	-

Source: Own work.

c) Value added at factor cost by ownership and activity 2017 – 2018 (EUR m)

Activity	National enterprises			Foreign owned enterprises		
	2017	2018	% of total within industry in 2018	2017	2018	% of total within industry in 2018
Wholesale and retail trade, repair of motor vehicles and motorcycles	2,590	2,722	60%	1,645	1,778	40%
Professional, scientific and technical activities	1,686	1,845	89%	183	217	11%
Construction	1,308	1,536	91%	124	156	9%
Transportation and storage	1,849	1,950	87%	269	294	13%
Manufacturing	5,350	5,514	63%	3,015	3,297	37%
<i>% of total</i>	<i>78%</i>	<i>78%</i>	-	<i>85%</i>	<i>85%</i>	-
Other	3,619	3,798	-	902	1,007	-
Total	16,403	17,365	-	6,138	6,749	-

Source: Own work.