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HOST GOVERNMENT INCENTIVES FOR ATTRACTING FDIs: THE CASE OF REPUBLIC OF MACEDONIA

Ljubljana, September 2016 GORDANA SMILEVSKA

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AUTHORSHIP STATEMENT

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INTRODUCTION

Due to the faster development of communications and information technology, lower costs in all trade exchanges and the abolition of trade barriers as in finance, much of the international capital movement takes place in the form of foreign direct investments.

It is believed that the optimum access and opening of the domestic market at the capital international markets is a necessary condition for bringing positive impact on the inflow of foreign capital in a country. Hence, in order this integration to be achieved, the country needs to reduce the fiscal deficit to a sustainable level, and then to liberalize the foreign trade, taking into consideration also the strengthening of the financial institutions and finally to liberalize the balance payments' sub-accounts.

Regarding to this, the Foreign direct investment (hereinafter: FDI), compared to other forms of international movement of capital, provides a number of benefits: product placement, expanding the host countries' market, export of technology, managerial skills and experiences, usage of the resources (raw materials, labour, energy, etc.), as well as savings on the production and transport costs. They are specifically directed towards the countries in transition, market-based economies, since they largely completed the process of privatization and transformation. These countries are attractive for foreign investors as they have market with relatively high purchasing power, favourable infrastructure, cheap and skilled labour strength and significant natural resources.

Developing countries, emerging economies and countries in transition due to the advantages related to FDI have liberalized their FDI regime and follow best policies to attract investments. It has been recognized that the maximizing benefits of FDI for the host country can be significant, including the technology spill-over, the human capital formation support, enhancement of the competitive business environment, contribution to international trade integration and improvement of the enterprise development (Kurtishi-Kastrati, 2013, p.26)

Due to the fact that Macedonia faces a very low level of economic development and a very high level of unemployment the role of FDI is crucial for further economic, technological and social prosperity. For these reasons Republic of Macedonia, since its independence develops policies and incentives to attract FDI, offering special privileges for foreign investors which should reconcile national interests with business interests and foreign investors' strategies.

Since its independence, FDI in Macedonia has been taking place mainly in two phases throughout the acquisition of major domestic already privatized companies (banks, telecommunications, electricity distributors, petroleum companies), in the first phase (period from the independence up to 2006), and throughout opening factories in the free economic zones and the realization of Greenfield investments throughout the territory of Macedonia in the second phase (period from 2006 and on-going).

In the first phase of FDI inflow period, almost all of the major acquisitions of Macedonian private and publicly owned companies took place, and according to the reports of the National Bank of the Republic of Macedonia (hereinafter: NBRM), FDI amounted to almost two billion dollars. In comparison to other countries in the region, Macedonia is among those with low level FDI (Kapital, 2013, p.10).

The second phase of FDI inflow in Macedonia is characterized with significant Greenfield investments, i.e. construction of new industrial zones as well as investments throughout the territory of the country. In order to improve the investment climate, the current Government of Republic of Macedonia in 2006 undertook a series of initiatives and activities with the purpose to become an attractive place for foreign investments including the implementation of strategy for acceleration of the economic development by promoting the Technological Industrial Development Zones (hereinafter: TIDZ), and also municipal industrial zones are opened within the country.

The overall purpose of the master thesis is to assess how successful the policy of the Macedonian government to attract FDI has been.

At a more operational level, the thesis has got three objectives. The first one is to analyze the major determinants for FDI inflows, both from the point of view of host and home countries. Here, the general theoretical overview will focus on types and motives as well as the assessment of host country policies for attracting FDIs.

The second objective is to present the recent trends of FDI flows into Macedonia with respect to the volume and its structural characteristics. In this area, through statistical data, the sector and regional structure of FDI in RM in the recent years will be determined.

And finally the third objective is to assess how successfully the explicit government policy has aimed at attracting FDI inflows i.e. major initiatives taken by the current government since 2006 been.

According to Saunders, Lewis and Thornhill (2009), new (primary) data is information that the researcher gathers on his own, throughout observations, by using interviews and questionnaires. On the other hand, secondary data refers to the data such as literature sources, books, reports, documents and articles that are collected by other researchers and institutions. In order to meet the above mentioned objectives and to fulfil the purpose of this research, both, primary and secondary data is collected. The secondary data used in chapter 1 and 2 has been critically evaluated and collected from books, scientific articles, internet sources, governmental institutions and company reports.

In order to obtain some better insight of the evaluation and main sector and regional characteristics in Macedonia, chapter 3 is based on information and primary data sources provided by Macedonian authorities and other sources like The National Bank of the Republic of Macedonia, State statistical office as well as the Agency for foreign investments and export promotion of the Republic of Macedonia and the Directorate for technological industrial development zones.

And finally, chapter 4, the Government policy for attracting FDI as assessed by the business sector is analysed in details on the basis of replies, collected data on a structured questionnaire carried out with a certain number of a representatives from foreign companies that have invested in Macedonia.

1 CONCEPT OF FDIS AND OVERVIEW OF THEIR DETERMINANTS

1.1 Definition and Classifications of FDI

There are three forms of international capital movements that are recognized within the economic flows. These forms include an international lending or movement loan capital, international portfolio-investment and direct investment abroad. The role and importance of each of these categories of international capital movements have changed over time. In the first half of the twentieth century, the dominant share mainly included loans, while today the importance of foreign direct investment is inviolable.

FDIs are defined as investments that include long-term relationship and reflect a lasting interest and control of the company - resident of one country (foreign direct investor's investment or parent company) in the company which is a resident of another country. FDI is an investor's acquisition with "long-term influence" on the management of a firm in another country (Contessi & Weinberger, 2009, p.61). Hence, the transnational companies are mostly focused in placing the capital abroad in the form of direct investments with the intention to win easily the international market by allowing access to certain resources and/or accelerating the business efficiency.

In the literature, there could be different ways of defining foreign direct investment. Foreign direct investment as defined by the Organization for Economic Co-operation and Development (hereinafter: OECD)fourth edition from the Detailed Benchmark Definition of FDI from 2008 and International Monetary Fund (hereinafter: IMF) fifth edition - Balance of Payment Manual from 1993, is a category of cross-border investment made by a resident in one economy (the direct investor or parent) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise or affiliate) that is resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long-term relationship with the direct investment enterprise to ensure a significant degree of influence by the direct investor in the management of the direct investment enterprise. The “lasting interest” is evidenced when the direct investor owns at least 10% of the voting power of the direct investment enterprise.

Most important FDI characteristic which sets them apart from foreign portfolio investments is that it is undertaken with the intention of exercising control of certain company. The IMF’s Balance of Payment Manual recommends usage of these 10% as a basic dividing line between direct investment and portfolio investment in the form of shareholdings. Consequently, the way that the direct investments are defined, highly influences the amount of foreign direct investments that is accounted in Balance of payments. The guideline of 10% share is not optimal; however this is the most common way to distinct direct investments from the portfolio investments (Duce, 2003, p. 3).

The FDI classification may differ in the literature. According to IMF sixth edition Balance of Payment Manual (2009, pp. 80-81), the classification of direct investment is based primarily on a directional basis-resident direct investment abroad and non-resident investment in the reporting economy which is subdivided into equity capital, reinvested earnings and other capital. Equity capital and other capital, in turn, are subdivided into asset and liability transactions.

Duce, (2003, p.5) also classifies the direct investment firstly according to the direction of investment both for assets or liabilities; and secondly to the investment instrument used (shares, loans, etc.); and thirdly to the sector breakdown.

As for the direction, it can be looked at it from the home and the host perspectives and as for the instruments, direct investment capital comprises the capital provided and capital received in which transactions are made up for the three basic components: equity capital, reinvested earnings and other direct investment capital.

OECD (2008, p. 117) fourth edition of the Detailed Benchmark Definition of FDI presents the classification of more detailed analyses of foreign direct investments, by economy and by industry. The OECD Benchmark recommends methodology for presenting detailed ”industrial“ breakdowns of direct investment which includes economic sectors shown in the table 1:

Table 1. Industrial Breakdowns

Economic or industry sector (OECD)	
1. Agriculture, forestry and fishing 2. Mining and quarrying 3. Manufacturing 4. Electricity, gas and water 5. Construction	6. Wholesale and retail trade and restaurants and hotels 7. Transport, storage and communications 8. Financing, real state and business services 9. Community, social and personal services

Source: OECD, *Fourth edition of the detailed benchmark definition,* 2008, p.117.

1.2 Types and Forms of FDI

The division and classification of types and forms of FDI can be implemented according to several criteria including the methods of entry (Cohen, 2007, p. 38):

- establishment of the enterprise - building production capacity by developer, a new entity,
- merger with or acquisition of a stake in ownership of already existing company - purchasing of the company through privatization or purchasing of shares and
- form of a joint venture with another company

The foreign investments on the basis of motivational factors (as one of the main factor of classification of investments) are divided into four categories: investments that tend to new resources, investments focused on new markets, investments focused on increasing of the production and productivity investments that tend to retention and promotion of long-term goals of one’s company.

The other form of FDIs classification is vertical, horizontal and conglomerate classification of the foreign direct investment. This kind of classification is implemented regarding the role and activities of the investment in business, i.e. entrepreneurship of company investors:

- horizontal FDI – the same product is produced in both countries included in the investment project,
- vertical FDI – the production and marketing of a same product is implemented in various countries,
- conglomerate FDI – the investment in a new country is not in a correlation with the production line of the investor’s host country

Horizontal FDI refers to firm's desire for investing in the same type of production in different countries. With horizontal FDI, the transnational corporations (hereinafter: TNCs) increase the number of factories that already exist in the host country, i.e. TNC duplicate roughly the same activities in multiple countries. The advantages resulting from this type of investments are lower transport costs, better products' adaptation to local standards, awareness of the customer requirements, etc.

Horizontal FDI occurs when a firm sets up a plant abroad in order to supply the foreign market. Vertical FDI, on the other hand, occurs when a firm exploits international differences in factor prices by moving part of its production process abroad (Akpansung, 2013, p. 1479). The main focus of vertical FDI is the internationalization of the production chain within the transnational corporations where companies locate different stages of production in different countries. Locating the different phases of vertical chain production in different countries aims at making use of comparative advantages of countries for each production stage (based on the labour costs, available sustainability of resources, etc.). The main objective of production in this case is not the local market, but the export of the products at the market of the country of FDI origin or at the world market.

While the conglomerate FDI includes the most unusual form of investments that attempts to overcome two barriers simultaneously - entering in a new industry and a new foreign country. Conglomerate FDI are the least common type of investment, and their formation is explained by the desire to provide diversification to minimize risk. Conglomerate TNCs is typically caused by buying a controlling stake in a foreign company, or a merger with a foreign company with a different type of production. They occasionally take place in the form of Greenfield investments, as the parent company usually does not possess the necessary knowledge and expertise to win and produce a new and different product.

Emerging markets attract relatively more vertical FDI than mature markets which are more horizontally FDI involved. According to Aizenman and Marion (2001, p.1) greater uncertainty reduces the expected income from vertical FDI but increases the expected income from horizontal FDI. In addition, predatory actions by the host country are costlier to the multinational as it has structured its production vertically rather than horizontally. Consequently, increased uncertainty should encourage the horizontal FDI but discourage the vertical one. If vertical FDI is more likely to flow into emerging markets and horizontal FDI into mature markets, then the empirical finding that most of FDIs are horizontal rather than vertical might be partly due to the greater uncertainty associated with emerging markets.

According to the above implemented research, it can be concluded that the definition and categorization (types and forms) of foreign direct investments are different from author to author, regarding to the fact that the distribution of foreign direct investment is carried out by different criteria.

1.3 Classification of Motives of FDI

There are several studies that are based on empirical research and information that refer to the motives and factors that a company is driven to undertake direct investment abroad. Those factors include avoidance of various import barriers, direct entry to foreign markets, strengthening the position in relation to local competitors, lowering production costs, utilization of resources, use of production factors, organization, financing, etc.

Concerning the foreign investors, they have clear motives which are primarily confined to the maximization of profits, considering the creation of conditions in order to achieve their business venture in many stable and long-term yields. In order the FDI to be achieved, there must be motives among the actors in the investment, including the recipient of FDI and the countries where they locate these investment projects. Foreign investors undertake investment activity driven by different motives, but in the end, the main goal is to achieve higher profits. The main motives driven by foreign investment and that on the basis of their characteristics enable profitable business abroad in relation to their own country. These motives mostly include:

- market-seeking FDI- expansion into new markets,
- resource-seeking FDI – access to resources,
- efficiency-seeking FDI- improving operational efficiency and
- strategic-asset seeking FDI- strategic investments (Dunning & Lundan, 2008, pp. 67, 68).

An additional motive set by Akpansung (2013) is the political safety FDI seekers, acquirement or establishment of a new operation in countries that are considered unlikely to expropriate or interfere with private sector firms.

Hence, it should be noted that the motives for the investors, as well as for the country where the investment is implemented, are primarily different. Market-seeking FDI is driven by the motives that include gaining access to new markets and/or increasing existing market shares that are also called horizontal FDI as replication of production facilities in the host country is involved. Tariff-jumping or export-substituting FDI is a variant of this type of FDI. As the reason for horizontal FDI is better serving of the local market by local production, market size and market growth, the host economy plays important roles (Demirhan & Masca, 2008, p.357). Franco, Rentocchin and Marzetti (2008, p.7) stating that various reasons (besides that of searching and exploiting new markets) lead to this choice by MNEs: to follow suppliers or customers that have built foreign production facilities, to adapt goods to local needs or tastes and to save the costs of

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serving a market from distance. Market seekers produce in foreign markets either to satisfy local demand or to export to markets other than their home market. Raw material seekers extract raw materials whenever they can be found, either for export or for further processing and sale in the host country. Firms in the oil, mining, plantation and forest industries fall in this category (Akpansung, 2013, p.1479).

The resource-seeking FDI is usually driven by the motives to invest in countries in order to obtain particular or specific natural resources, raw materials or low-costs labour that are not available in the home country. According to Dunning and Lundan (2008) there are three groups of resources seekers: the motive for the first group is driven by pursuing physical resources that include primary producers and manufacturing enterprises that seek minerals, fossil fuel and agricultural products; the motive for the second group is comprised of seeking cheap and well-motivated workforce of unskilled or semi-skilled labour; the third type of resource-seeking FDI is driven by the need of the firms to acquire technological capability, management or marketing expertise and organizational skills. Vertical or export-oriented FDI that involves relocating parts of the production chain to the host country is FDI driven resource.

Efficiency-seeking FDI-foreign investors who have got such motives aim for rationalization of production, distribution and marketing activities or achieving synergy among geographically dispersed activities. As it is said by Kinoshita and Campos (2003, p.4), the foreign investment is efficiency-seeking when the firm can gain from the common governance of geographically dispersed activities in the presence of economies of scale and scope.

The intention of the efficiency seeking MNCs is to take advantage of different factors, endowments, cultures, institutional arrangements, economic systems and policies and market structures by concentrating the production in a limited number of locations to supply multiple markets (Dunning & Lundan, 2008, p.72). In order to efficiency seeking foreign production to take place, cross-border markets must be both well developed and open, therefore it often flourishes in regionally integrated markets (Dunning, 1993, p.59).
Strategic-asset seeking FDI motives imply to foreign investors that promote their strategic objectives in order to maintain and improve their competitiveness usually by acquiring the assets of foreign corporations. The involved investing firms include both established MNCs pursuing an integrated global or regional strategy, and firstly foreign direct investors seek to access or to buy some kind of competitive strength at an unfamiliar market (Dunning & Lundan, 2008, 72).

UNCTAD (2006, p.159) pointed that all of these above stated that the motives in many cases might be mixed, complementary and evolutionary FDI motives. **Mixed motives** are when companies invest for more than one reason simultaneously; **complementary motives** are when companies combine more than one motive or strategy to secure a particular goal; and **evolutionary motives** mean that motives can evolve over time.

Dunning and Lundan (2008) in their book argue that there are other motives for MNCs activities that do not fit into four above mentioned motives: **escape investments** - FDI that is made to escape restrictive legislation or macro-organizational policies by home governments, **support investments** - that is to support the activities of the rest of the enterprise and they are apart from and **passive investments -** that concerns the degree of active management pursued by their owners ranging from complete to non-existent.

2 OVERVIEW AND ASSESMENT OF DETERMINANTS AND HOST COUNTRY POLICIES FOR ATTRACTING FDIS

A large portion of the literature has examined the various assessments of a country policies and determinants for attracting FDIs. Some determinants such as market size and market distance are beyond the influence of policymakers in host countries and some institutional determinants such as costs factors, investment promotion and incentive structures are more malleable (Parcon, 2008, p.1).

Authorities engaged in incentive-based strategies by assessment of a determinant and policies for attracting FDI, face a two-fold challenge to attract FDI and to secure benefits from these flows. If a host country operates in an already attractive environment, then some incentives may serve as a supplement for investment. On the other hand, in some circumstances, incentives may serve as a compensation for proven market imperfections.

Core FDI policies are consisted of rules and regulations that govern the entry and operations of foreign investors, the standards of treatment according to them and the function of the markets within which they operate (UNCTAD, 1998, p.92). They might satisfy various objectives such as reducing or increasing FDI by restrictions or openness of the country, encouraging the development of specific sectors to the economy in the given country, and so on. However, to achieve these objectives, national FDI policies are usually accompanied by supplementary policies that might influence investors' decisions like privatization policies (acquiring of state owned firms) and policies determined by the international agreements that a country has signed.

UNCTAD (1998, p. 90), a host country's FDI determinants are described through a graphic overview. Determinants begin with the role of **national policies framework** for FDI, followed by **economic determinants** and **business facilitation** (see table 2).

Table 2. Host Country Determinants of FDI Table

Host country determinants	
1. Policy framework for FDI - Economic, political and social stability - Rules regarding entry and operations - Standards of treatment of foreign affiliates - Policies on functioning and structure of markets (especially competition and M&A policies) international agreements on FDI privatization policy - Trade policy (tariffs and NTBs) and coherence of FDI and trade policies tax policy **2. Economic determinants** - Type of FDI classified by motives of TNCs - Principal economic determinants in host countries **Market-seeking** - Market size and per capita income - Market growth - Access to regional and global markets - Country-specific consumer preferences - Structure of markets **Resource/asset-seeking** - Raw materials - Low-cost unskilled labour - Skilled labour - Technological, innovatory and othercreated assets (e.g. brand names), including as embodied in individuals, firms and clusters - Physical infrastructure (ports, roads, power, telecommunication)	- Skilled labour - Technological, innovatory and other created assets (e.g. brand names), including as embodied in individuals, firms and clusters - Physical infrastructure (ports, roads, power, telecommunication) **Efficiency-seeking** - Cost of resources and assets listed under B, adjusted for productivity for labour resources - Other input costs, e.g. transport and communication costs to/from and within host economy and costs of other intermediate products - Membership of a regional integration agreement conducive to the establishment of regional corporate networks **3. Business facilitation** - Investment promotion (including imagebuilding and investment-generating activities and investment-facilitation services) - Investment incentives - Hassle costs (related to corruption, administrative efficiency, etc.) - Social amenities (bilingual schools, quality of life, etc.) - After-investment service

Source: UNCTAD. *World Investment Report 1998, Trends and Determinants.*1998, p. 91, Table IV

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Consistent with the table 2, national policies, broadly speaking, are related to the economy and include those that affect the taxes (corporate and personal), exchange rates related to stability of the country, interest rate and thus costs of capital and rate of inflation, as well as political and social stability. In this framework there are also policies which determine the function and structure of the markets, such as labour market policies, trade policy, international agreement on FDI, etc.

Economic determinants are driven by the motives of TNCs to invest market-seeking, resource/asset-seeking and efficiency seeking.

Business facilitation determinants include investment promotion and investment incentives efforts, reduction of the "hassle costs" of doing business in a host country and provision of amenities that contribute to the quality of life of non-resident personnel.

Over the last decade, the value of cross-border investment has raised significantly, especially the foreign direct investment, and governments continue to adopt investment policy measures both on national and international level. Investment policies are shaped to a constant change for many of reasons, economic and financial crisis, as well as global challenges such as climate change and food security, where developing country's engagement is a crucial precondition for any viable solution.

As it is stated by UNCTAD (2012, p. 99) statistics, developing countries and economies in transition are now primary FDI destinations and their importance as FDI recipients continues to increase. In 2010, for the first time, developing countries received more than half of the global FDI flows – they are now at 55 per cent. This increases the opportunities for strategic investment targeting, promotion and protection policies in the developing countries. Kornecki (2010, p.10) in his study that refers to the post-communist era in the Central and Eastern Europe (hereinafter: CEE) concluded that the inward FDI in the CEE has increased in the past twenty years becoming the most common type of capital flow during the transition period and that foreign capital plays a vital role in CEE economies as well as an important indicator of the advancing globalization processes in CEE. There are also new types of investors at the scene like state-owned enterprises and sovereign wealth funds, funds that come from central bank reserves that are accumulated as a result of budget and trade surpluses becoming important FDI players (Investopedia, n.d.).

In order to fulfil the economic growth in the country, national governments have to deploy an investment policy that would support the country's overall development strategy. UNCTAD in the paper from 2015, Investment policy framework for sustainable development suggests a general framework that consist policy actions on three levels:

- on strategic level, policymakers should ground investment policy in a broad road map for economic growth and sustainable development such as those set out in formal economic or industrial development strategies in many countries,
- on normative level, through the setting of rules and regulations, on investment and in a range of other policy areas, policymakers can promote and regulate investment that is geared towards sustainable development goals and
- on administrative level, through appropriate implementation and institutional mechanisms policymakers can ensure continued relevance and effectiveness of investment policies (UNCTAD, 2015, pg. 111).

2.1 Size of Markets

One of the most important factors for TNCs which affect the desirability of locating the plant on a certain site is the market potential with its size and purchasing power. Market size is very important for a decision on the investment location because it may primarily affect the growing demand for all manufactured goods. Market size is guaranteed in most cases regarding to the existence of a larger number of companies - larger host countries are associated with greater FDI owing to greater market opportunities for investors (Bevan & Estrin, 2000, p. 16). The higher the concentration of firms in a particular region, it is easier for foreign investors to find a supplier (if not importing raw materials), decreased transport costs and therefore the lower the final price of the implemented product.

Various authors (Markusen & Venables, 1998; Markusen, 2002) have concentrated on the issue of the market size as one of FDI determinant, and put forward various theories to explain them. Thus, the new theory of trade combines the advantages of ownership (knowledge) and location (market size and low transaction costs) with technology and the intrinsic characteristics of a country (factor endowments) (Assuncao, Forte & Teixeira, 2011, pp. 5, 6).

This new theory is an addition to Dunning's eclectic paradigm in which he aims to correlate the three variables OLI (ownership, location, internalization) with technology and the country's characteristics in a coherent manner (Markusen, 2002). Developed by Dunning (1993), known as OLI paradigm Dunning theory, which argues those three sets of determining factors, must be satisfied for FDI to occur: the firm must have both an ownership--specific advantages (O) (a new patented or licensed technology, technical know-how, firm's production process and management skills) that should be combined with the location (L) advantages of host countries (e.g. large markets or lower costs of resources or superior infrastructure) and the possibility of production internalization (I) advantage.

However, in the process of globalization, Porter's theory goes even deeper whilst analyzing country-specific sources of advantage that improve the international competitive advantage of firms. While the above mention theories propose that a company may choose to be present on international markets, whether as a form of exporting company or a form of foreign investment, according to Porter, successful firms that expand on international markets are not in a position to choose, they must participate in order to be successful in exchange of commodities and capital flows (Kikerkova, 2003, p.159).

Market size is one of the important drivers for attracting FDI flows, particularly horizontal FDIs. Theoretically, the larger the market size of the host country is, the more attractive is to FDI. Mateev (2008, p.7) states that the market size of the host country that is usually measured by GDP, is considered an important determinant of horizontal FDI as the returns from such investment depend on the economic scale on the firm level.

As it is mentioned in the first chapter, among the motives for FDI is the market-seeking investment which may be undertaken to sustain or protect existing markets, or to exploit or promote new markets (Dunning & Lundan, 2008, p.70). Accordingly, Phil (2014, p.1) states that the market size of host countries is very important location factor for market oriented FDI. There is a positive effect of FDI and market size. If market size is large, it attracts more capital inflow and vice-versa or spill-over effect is bigger in case of large market size and it attracts large capital inflow.

On the other hand, the small size of the market in the developing countries is associated with non-market seeking FDI activities. According to economic concept, FDI towards developing countries flows for low-technology and labour-intensive production, i.e. FDI inflows to less-developed countries are associated with vertical investments. The vertical FDI occurs when a firm relocates only a part of its production process. In such case, foreign investors are encouraged and attracted more from the low labour force and specific skills, from the natural resources they find, from the infrastructure, etc. (Botrić & Škuflić, 2005).

Overseas Development Institute (hereinafter: ODI), (1997, p.8) in their brief paper concludes that the structural weaknesses of low-income economies, the inefficiencies of their small markets, their skill shortages and weak technological capabilities are all characteristics that depress the prospective profitability of investment thus FDI is minimal.
In addition, based on the previous statement, the South East European countries (hereinafter: SEECs) have developed various strategies to attract (promote) FDI actively to their countries rather than relying solely on market size and low wage costs as location factors. The FDI attraction especially the changes in corporate taxes, the endowment with production-related material infrastructure and institutional improvement, have become an

important policy goal for regional development of SEECs (Bellak & Leibrecht, 2010, p. 38.).

2.2 Labour Costs and Productivity

As a result of globalization, the internationalization of the foreign direct investment within the progressive flows of the world economy, along with the international trade of goods and services, promotes the economic growth, increases the employment and raises the living standard worldwide. In other words, inward foreign direct investment is welcomed as for an employment opportunity and the promise about superior technology for a given country.

One of the key driving forces of globalization today and thus carriers of FDI is the increased international production carried by TNCs. As part of the major economic organizers and a source of capital, technology, managerial and organization know-how, TNCs are main drivers of the employment worldwide, both direct (with direct contribution employment in manufacturing and services) and indirect (through linkages of suppliers and subcontractors).

The influence of international production on employment is determined upon several factors:

- mode of entry of FDI, Greenfield and thus creation of new employment, or M&A wherever the current employment may reduce or remain constant,
- depending on the sector and industry, some production processes are more labour intensive than others and
- international production substitutes for domestic production (drive domestic firms out of the market) or complements domestic investment by releasing financial and technological activities.

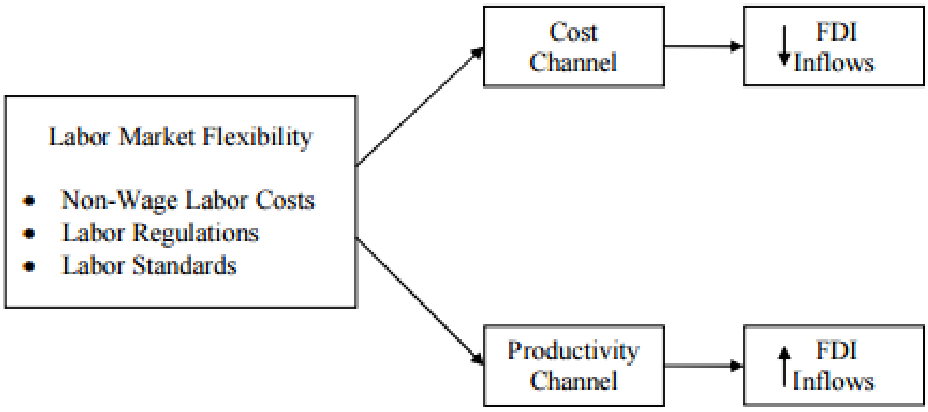
One of the main factors linked to international production that influences the quantity, quality and location of the employment are the strategies of transnational corporations. MNCs strategies involve choices about the location for different activities and the degree of integration among the various entities falling under the governance of the firm. In its annual monograph, the World Investment Report, the authors of the report (UNCTAD, 1998, p.109,) identify that firms, in order to integrate cross-border production, can pursue a variety of strategies, simple and complex.

Simple integration strategies involve the establishment of affiliates to perform specific activities abroad, while the most important operations remain based in the home country. Usually, foreign affiliates established within the framework of this strategy are located in developing countries and in economies in transition driven by costs considerations relating to specific inputs, such as low-costs unskilled labour in labour-intensive industries (textiles and clothing, shoes, toys,) and labour-intensive aspects/components of capital-intensive industries (electronics and automobile industry).

Complex integration strategies refer to the establishment of affiliates on locations best suited to the particular firm activity, in order to perform a variety of different functions such as finance, R&D, accounting, training, parts production, distribution or segments of these functions. Unlike the simple integration strategy that is limited to one type of resource (unskilled low-costs labour), this type of strategies assigned to specialized foreign affiliates in the production process, involves a broad range of resources in the host countries: low-costs labour and engineering skills, workforce with technological sophistication and adaptability, functions like accountancy, legal services, purchasing and marketing, and finance and R&D capabilities. Therefore, a variety of employment effects will result from the major tendencies associated with complex integration strategies such as high- quality skilled workforce.

Rigidity of labour market imposes costs on firms and therefore profit-maximizing firm would most likely want to locate in countries with more flexible labour markets. According to some authors, a regulated labour market imposes additional costs on firms, which may deter FDI inflows (Parcon, 2008; Verma, 2015). Alternatively, there is an argument that a highly regulated labour market may help to enhance the labour relations and increase the labour productivity. Labour market standards and regulations can add to the social stability and these attract FDI inflows (Praveen & Sakti, 2008).

Figure 1. The Impact of Labour Market Flexibility on FDI Inflows



Source: H. Parcon, *Labour market flexibility as a determinant of FDI inflows*, 2007, p. 10, Figure 3.

Parcon, (2008, p.9) has noted that the relationship between the labour market flexibility and FDI inflows will be sensitive to the choice of the used labour market flexibility indicator. Thus, depending on the chosen indicator, labour market flexibility can have two opposing effects on FDI inflows, as illustrated in Figure 1. On one hand, labour market standards and regulations increase the costs and decrease the ability of a firm to respond to the market changes which deters FDI. On the other hand, labour market standards and regulations enhance labour productivity which attracts FDI.

Rigid regulation of the labour market is generally perceived to be a disadvantage for a nation seeking for attracting FDI, and particularly for those industries subject to a greater than average risk of failure, whereby exiting costs from a particular market become increasingly important. Thus, any study indicates that flexible labour markets characterized by low closure costs are significant attractors for FDI (Whyman & Baimbridge, 2006).

2.3 Infrastructure

There is no commonly agreed usage of the term infrastructure, but the concept in its broadest sense comprises the physical facilities, institutions and organizational structures, or the social and economic foundations for the operation of a society (UNCTAD, 2008, p. 87). While the definition covers a comprehensive concept, both social and economic infrastructure, covered by FDI literature, infrastructure is related to economic concept and is comprise of a group of industries including electricity, gas, telecommunications, water supply, sanitation, and waste management, and a transport infrastructure - airports, roads, railways and seaports.

Worldwide, there are differences in infrastructure development between developed and developing countries, because most of low-income countries have got the need for infrastructure investment funds, but have got a domestic lack of necessary capacity to meet them. Infrastructure development is also directly linked to poverty reduction. In particular, market imperfections that result from the lack of adequate infrastructure lead to monopolistic pricing, particularly in rural areas that hurt the poor. Inadequate infrastructure also hinders the market participation of the poor, thereby, perpetuating their poverty (Diwesh, Bindu, Masahiro & Rajat, 2007 p.3).

Consequently, in last two decades, governments have opened up the infrastructure industries for the private sector as well as the TNCs. Major privatization programs of State-owned infrastructure assets contribute the increase of FDI and other forms of TNCs involvement to many developing and transition economy’s infrastructure participation, especially in telecommunication facilities and services and electricity industry.

According to ODI (1997, p. 7), poor infrastructure can be seen, however, as both, an obstacle and an opportunity for foreign investment. For the majority of low-income countries, it is often cited as one of the major constraints. But foreign investors also point to the potential for attracting significant FDI, if host governments permit more substantial foreign participation in the infrastructure sector.

Each infrastructure industry has got its own separate features and each infrastructure industry includes potentially competitive and non-competitive segments. Private and foreign investors can enter former publicly provided infrastructure services if a given segment is separated from the rest of the industry such as transmission lines in electricity, cable lines in telecommunications, etc. Such networks are very capital-intensive and involve large sunk costs and assets and once built, they are location bound and cannot be moved to other sites.

Thus, electricity industry is a technology and innovation-intensive industry that is consisted of three segments: generation, transmission and distribution and each segment have got its own economic features. Some segments, like electricity generation, are separated from transmission and distribution, allow possibility for competition, transmission and distribution networks, in contrast, they are classic natural monopoly.
The most important segments within telecommunications infrastructure are the fixed-line telephony, mobile telephony and transmission of digital data. They differ from each other in terms of their technology and services and they can improve economic growth directly through their demand of inputs, or indirectly, as better telecommunication network helps other industries to improve and expand their production capacities (OECD, 2014).

Transport infrastructure includes roads, railways, airports and seaports. For manufacturing and trading activities, the quality and coverage of the transport networks significantly influences the costs of production and distribution. According to Aoki and Roberts(2006, p.1) the transport contributes to national key activities such as production, employment, domestic and international trade and the quality, and the transport coverage network significantly affects the costs of inputs, production and distribution. In order for client countries to improve their investment climate, quality transport indicators need to have clear policy implications and help policy makers to identify the priority areas of reform.

With the rising population, water supply has got continuous shortages in several regions of the world. Water industry supply chain – extraction, transmission, distribution and supply – involve economies of scale and the provision of water services normally involves high sunk and fixed costs (UNCTAD, 2008, p. 91). Water distribution remains a natural monopoly and the possibility for governments to introduce competition in the water industry is limited.

Infrastructure industry has got general characteristics. They act as monopoly or natural monopoly due to an economic scale, and the public sector is usually the leading provider of the infrastructure services. Yet, technological changes and changes in management practices have led to alternative models of private sector participation in infrastructure.

In infrastructure the assembling of the necessary financial resources from domestic public and private sector is difficult for many countries, especially developing countries. Therefore, they have opened up for TNCs and FDI. However, TNCs are willing to invest in projects in which they can expect sufficient returns, and the higher the perceived risks associated with a project, the greater will have to be the expected returns.

Practice has shown that infrastructure investors are very sensitive to country risk. In this sense, governments have to manage such risks throughout enabling effective regulation and policy. Therefore, the governmental role has expanded to a renew investment policies by providing development and support to new legal and regulatory frameworks, including protection of property and contractual rights, regulation to protect the poor and the environment as well assess the suitability forms of infrastructure provision.

2.4 Openness to International Trade and Access to International Markets

One of the important factors for the internationalization of production and encouraging FDI in the world represents a liberalization trade policy of separate national economies, especially the less developed countries in the FDI treatment. Efforts like economic reforms, trade open polices, lower tariff and non-tariff barriers, etc., in order to promote trade through bilateral trade agreements and unilateral actions attract the export oriented FDI.

There are a number of empirical studies that include trade openness and access to the international markets as one of the FDI determinants. Jordan (2004, p.46) claims that trade liberalization allows goods to move more freely and hence, it is expected to reduce the amount of international investment as a trade-off between trade and foreign production (FDI).

Along with Bishnu, (2011), the degree of trade openness is likely to influence the flows of international capital in terms of risk-return relationship, meaning that no one feels interested in committing long-term investment in a country that imposes tariff and non-tariff barriers on investment and creates problem in repatriating capitals as well as profits.
Managing the relations between international trades has to do with a number of agreements on bilateral, regional and multilateral levels on FDI.

As stated by UNCTAD (1996, p.134), on bilateral level, key investment concepts, principles and standards have been developed throughout the conclusion of treaties for the protection and promotion of FDI and these treaties have remained virtually unchanged in their format, and the issues they address continue to be among the most important for FDI.
Regional integration, also known as preferential trade agreements, take account of **free trade area** where tariff and non-tariff barriers for the trade of goods between member states are eliminated, **custom union** with the common customs legislation between member states, **single market** where not only international trade is liberalized, but also includes elimination of barriers to the free circulation of capital and labour within the territory and **economic and monetary union**.

Since 1995, OECD member-countries and the European Commission have been engaged in negotiations to develop a multilateral agreement on investment (hereinafter: MAI). Their task is to elaborate the first comprehensive framework for investment with high standards of liberalization and investment protection with effective dispute settlement and open to non-members. (OECD, 1998, p.2)

On 1 January 1995, the World Trade Organization (hereinafter: WTO) officially commenced and it is the only global international organization dealing with the rules of trade among nations. At its heart there are the WTO agreements, negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments. The goal is to help producers of goods and services, exporters and importers to conduct their businesses (WTO).

Buthe & Milner (2008, p. 741) argue that the flow of foreign direct investment into developing countries varies greatly across countries and over time and that international trade agreements and preferential trade agreements (hereinafter: PTAs) provide mechanisms for making commitments to foreign investors about the treatment of their assets, thus reassuring investors and increasing the investment.

All countries in accession to the WTO are obliged to sign and accept the terms of the following three multilateral agreements:

- General Agreement on Tariffs and Trade (GATT)
- The General Agreement on Trade in Services (GATS)
- Trade-related aspects of intellectual property rights (TRIPS), (Kikerkova, 2003, p.83)
- Other specific issues that cover most pertinent agreements signed on multilateral level are
- Insurance coverage for political risks in developing countries is available for foreign investors under the Multilateral Investment Guarantee Agency (MIGA), an organization belonging to The World Bank Group.

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- Settlement of disputes. The issue of the settlement of investment disputes between private investors and host countries is specifically addressed in the Convention on the Settlement of Investment Disputes between States and Nationals of other States.
- Employment and labour relations. This issue is covered by the Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy (UNCTAD, 1996, p.154)

FDI is also treated with the Guidelines on the Treatment of Foreign Direct Investment, developed by The World Bank, informal guidelines for serious effort to reconcile the concerns of developing countries with the need to meet investors (The World Bank, n.d.).

Macedonia as a small country has strived to achieve a high level of foreign trade liberalization in recent years. From its independence and ongoing, the country stands for developing a policy aimed to openness to international trade and liberalization and as a result it has been achieved the following:

- Membership of the World Trade Organization since 2003,
- Stabilization and Association Agreement with EU since April 2001, giving Macedonia duty-free access to European markets for the majority of the goods,
- Member of CEFTA – Central European Free Trade Agreements with Albania, Bosnia and Herzegovina, Serbia, Montenegro, Kosovo and Moldova,
- European Free Trade Association (EFTA)- with Switzerland, Norway, Lichtenstein and Iceland, signed 2000 and became into force 2002,
- The Energy Charter Treaty, entry into force 1998
- Bilateral Free Trade Agreement with 40 partner countries.

2.5 Incentives and Operating Conditions

Incentives are any measurable economic advantages afforded to specific enterprises or categories of enterprises by (or by the direction of) a government, in order to encourage them to behave in a certain manner. They include measures either to increase the rate of return of a particular FDI undertaking, or to reduce (or redistribute) its costs or risks (UNCTAD, 1998, p.102). It simply represents a non-negative per unit subsidy paid to foreign investors in addition to the regular market-determined rate of return on capital (Blanchard, 2013, p. 18).

Host governments worldwide have lowered entry barriers, opened up new sectors, and also provided various forms of investment incentives programs and good business operating conditions to encourage foreign investment and MNCs to enter with a goal to raise employment, exports, increase tax revenue or the prospect that some of the knowledge brought by foreign companies may spill over to the domestic ones. The host governments provide investment incentives which are typically arranged in three extensive categories:

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fiscal incentives such as tax holidays and reduced tax rates, financial incentives related to such as grants and loans at concessionary rates and other incentives including subsidized infrastructure or services, preferential government contracts, special treatment to foreign exchange etc., broadly listed in the table 3 (UNCTAD, 1996, p.180).

Despite the macroeconomic problems such as unemployment and low growth rates, FDI promotion efforts and initiatives by governments are motivated also by the globalization and trade liberalization of the international economy through multilateral agreements, GATT and WTO, or regionally through EU, NAFTA, AFTA and other regional agreements. As a result, the importance of the market size of one country has diminished, and now even a small country may compete in attracting foreign investment by providing a reasonably attractive incentive package. Blomstrom and Kokko (2003, p. 6) emphasize that market integration has reached further at the regional rather than global level and in that point the effects of incentives are likely to be particularly strong in the competition for FDI within regions (or even countries) when the initial investment decision has been taken and the investor is chosen among alternative locations in a given region.

Nevertheless, to influence the location decisions of foreign investors in an increasingly open and highly competitive global environment, incentives programmes are offered to encourage FDI. Some programs are directed specifically to foreign investors, others are addressed to local as well as foreign investment (e.g., regional development incentives), while, for particular investments considered of special importance to the country, incentives are often negotiated on an ad hoc basis (UNCTAD, 1996, pp.131,132).

In accordance of what measures and incentives programs governments would use, UNCTAD (2000) global survey in over 45 countries from all regions of the world finds that the most widely used are the fiscal incentives; reductions in the standard rates of corporate income tax and tax holidays. According to the research, incentives are targeted for:

- regional investment where countries often employ a mix of incentives to channel investment for development of a particular area or region, like rural development, building industrial centres away from major cities and reducing environmental hazards,
- sector Investment where countries employ tax incentives in order to promote sectors of industry or activities considered crucial for development like mining and industrial parks, promotion of export, film industry and businesses with new technologies, tourism and leisure sectors,
- performance enhancement where incentives are targeted for activities, such as export promotion, Free Trade Zones (hereinafter: FTZs), employment/skills training and domestic value added and headquarters location and
- transfer of technology, a specific set of incentives directed towards research and development (hereinafter: R&D) activities and technology projects (pioneer industries)

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Authors and global survey, (Blomstrom, 1991; Blomstrom & Kokko, 2003; UNCTAD, 2000), mark the importance of production technology diffusion and flow of labour skills and managerial expertise from multinational corporations, as positive externalities "spill-over" which is spread in the host country. However, since international investment incentives for FDI is potential (are needed) for beneficial externalities or spill-over there is a question whether investment incentives can be justified in terms to yield benefits that are at least as large as the costs (Blomstrom, 2002). Yet, Cohen, (2007) suggests that estimating in advance the costs/benefit ratio of any given incentives package could be a very imprecise art.

The economic rationale for offering investment incentives to attract FDI is with an aim to facilitate faster economic growth, produce positive externalities in the form of larger employment, technology transfers and skills to the local industry. Though, I must emphasize that many authors look upon the justification of incentives with a critic and there is an adverse economic and political effects on the host country. Measures aimed for attracting FDI are not always sufficient to ensure the greatest possible benefits that countries expect from FDI, such as technology transfer to foreign affiliates and domestic firms, more and deeper links with local enterprises, higher exports, higher employment and upgraded skills (United Nations, 2003, p.104).

Also, in the wider economic debate there is an understanding of the issue of inequality of MNCs contrary to the consumers of public goods. In this sense, the negative aspects relating to the allowances given to FDI are in correlation with the fiscal burden on the host country as well as the income from tax revenue for providing public goods. For a tax incentive to be beneficial to the host country, the decrease in government revenues resulting from the incentive would have to be more than offset by the increase in tax revenues resulting from increased foreign investment flows (UNCTAD, 2000, p. 14).

The arguments also relate to the unequal treatment of domestic entities by the government regarding investment incentives (Žilinske, 2010; Kurtishi-Kastrati, 2013). FDI can generate negative externalities when foreign firms with superior technology force domestic firms to exit. These negative externalities are often called also competition effect, crowding-out effect or business-stealing effect (Damijan, Knell, Majcen & Rojec, 2003, p. 4). When measuring spill-over effects of foreign investment on domestic firms, Aitkenand and Harrison (1999) conclude that increased foreign equity participation lead to an increase in productivity for domestic small plants with less than 50 employees. However, the increase in foreign ownership negatively affects the productivity wholly of domestic owned firms in the same industry.

Table 3. Main Types of Incentive Measures Offered to Foreign Investors

Fiscal incentives including:

- Reduction of the standard corporate income-tax rate
- Tax holidays
- Allowing losses incurred during the holiday period to be written off against future profits
- Accelerated depreciation allowances on capital taxes
- Investment and reinvestment allowances
- Reductions in social security contributions
- Deductions from taxable earnings based on the number of employees or on other labour-related expenditures
- Corporate income-tax deductions based on, for example, expenditures relating to marketing and promotional activities
- Value-added based incentives, including:
- Corporate income-tax reductions or credits based on the net local content of outputs
- Granting of income-tax credits based on net value earned
- Import-based incentives, including:
- Exemption from import duties on capital goods, equipment or raw materials, parts and inputs related to the production process
- Tax credits for duties paid on imported materials or supplies
- Export-based incentives, including:
- Exemptions from export duties
- Preferential tax treatment of income from exports
- Income-tax reduction for special foreign-exchange-earning activities or for manufactured exports
- Tax credits on domestic sales in return for export performance
- Duty drawbacks
- Income-tax credits on net local content of exports
- Deduction of overseas expenditures and capital allowance for export industries

Financial incentives including:

- "Direct subsidies" to cover (part of) capital, production or marketing costs in relation to an investment project
- Subsidized loans
- Loan guarantees
- Guaranteed export credits
- Publicly funded venture capital participating in investments involving high commercial risks

(table continues)

(continued) - Government insurance at preferential rates, usually available to cover certain types of risks such as: - Exchange-rate volatility, currency devaluation, or non-commercial risks such as expropriation and political turmoil (often provided through an international agency)
Other incentives including: - Subsidized dedicated infrastructure - Subsidized services, including assistance in identifying sources of finance, implementing and managing projects, carrying out pre-investment studies, information on markets, availability of raw materials and supply of infrastructure, advice on production processes and marketing techniques, assistance with training and retraining, technical facilities for developing know-how or improving quality control - Preferential government contracts - Closing the market to further entry or the granting of monopoly rights - Protection from import competition - Special treatment with respect to foreign exchange, including special exchange rates, special foreign debt-to-equity conversion rates, elimination of exchange risks on foreign loans, concessions of foreign exchange credits for export earnings, and special concessions on the repatriation of earnings and capital

Source: UNCTAD, *World investment report –Investment, trade and international policy agreements,* 1996, p.180, Table VI.4

When measuring the outcome of the given incentives a controversy arises. If the investment truly is the outcome of the incentives provided, difficulties arise in the evaluation of the positive (creation of new jobs, technology transfer etc.) as well as the evaluation of above mentioned negative effects. The challenge for policy makers is to deepen their understanding of what policies and policy tools are most important from a development perspective in order to maximize the positive effects of FDI and minimize its negative effects. The economic benefits of FDI are real, but they do not accrue automatically. The magnitude of the benefits from FDI depends on the efforts of host countries to put in place the appropriate frameworks but even less-well performing countries may benefit, inter alia by using FDI as a supplement to scarce financial resources (OECD, 2002, pp. 21, 22).

3 FDIS IN MACEDONIA: EVOLUTION AND MAIN CHARACTERISTIC

3.1 Evolution of FDI Volume in Macedonia

Maintaining macroeconomic stability and gradually increasing economic growth, is the main priority of Republic of Macedonia. Stable macroeconomic situation is achieved through healthy macroeconomic policies, prudent and cautious fiscal policy through a high level of public investment, implementing and introducing anti-crisis measures by structural reforms so it can improve the business environment in this country.

The Republic of Macedonia, like the other transitional countries, constantly makes efforts to attract most of the foreign capital through foreign direct investment. Drastic reforms are undertaken concerning the business climate after 2006, from economic and legal aspects of creating a favourable international investment environment – reduction of taxation, introduction of the 10% flat tax as well as reforms regarding all segments of administration and bureaucratic issues, with the goal of achieving a favourable international investment position and the intention of targeting companies which establish Greenfield or new industrial capacities.

Since its independence until today, FDI in Macedonia has been taking place mainly in two phases, through the acquisition of major domestic or already privatized companies (banks, telecommunications, electricity distributors, petroleum companies), in the first phase (period from the independence up to 2006), and through the opening of factories in the free economic zones and the realization of Greenfield investments throughout the territory of Macedonia in the second phase (period from 2006 and ongoing).

Accordingly, by the end of 2006, government completed the privatization of AD ESM (a distribution segment) by selling 90% of shares to the Austrian EVN Group. AD MEPSO (Electricity Transmission System Operator of Macedonia) an electricity transmission asset, and AD ELEM, which is consisted of all electricity generation assets established in 2005, and are fully state-owned companies.

Through the years, technological change has led to increased competition and the sector continues to innovate rapidly. In Macedonia, the former state monopoly – Makedonski Telekomunikacii was privatized in 2001: Magyar Telekom (Deutsche Telekom Group) now holds a majority stake in the company, 51%, while the State remains a minority shareholder. In addition, two mobile operators are active on the market: T-Mobile Macedonia (a subsidiary of Makedonski Telekomunikacii), ONE (owned by Telekom Slovenia Group) and VIP (a subsidiary of Mobilkom Austria) that joint together in the past year. The mobile networks cover up to 99% of the population and the country has one of the highest rates of internet usage in the region, with nearly one third of the population connecting regularly to the Internet.

By the end of the 1990s up until 2006, almost all of the major acquisitions of Macedonian private and publicly owned companies took place, and according to the reports of NBRM, FDI amounted to 1.8 billion USD (Kapital, 2013, p. 10). In comparison to other countries from South-eastern Europe, Macedonia, in this period, is among those with low level of FDI.

The second phase is the period of realization of Greenfield investments throughout the territory of Macedonia and opening of factories in the free economic zones (period from 2006 and ongoing). After the government's campaign, called Invest in Macedonia, some large foreign companies started implementing their investment projects in Macedonia. Thus, the larger Greenfield investments in Macedonia began with the construction of Johnson Controls, the British Johnson Matthey (2010), American Kemet Electronics, Kromberg & Schubert, Italian Techno Hose, Russian oil company Lukoil, Turkish TAV, Sutas and others.

Although, with new government politics in the period when a large influx of FDI was expected (2008), the global economic crisis occurred which resulted with reduction of foreign investments in the following two years. Therefore, in the following two years (2009, 2010) a slowdown regarding investment from multinational companies occurs. Still, the next year 2011, there was greater interest in building new industrial production capacities.

Hence, year 2011 is characterized with several significant foreign investments that resulted with a doubled amount of direct investments in the country, and is the largest by far FDIs in recent years with almost 344.41 EUR or 4.5 % of GDP. One of the investments mentioned above is the arrival of Turkish TAV with the reconstruction of the two airports. The same year, in Skopje1 zone, construction of a factory under the company Prodis and a part of Russian pharmaceutical holding Protek Group that produces organic products began.

Furthermore, after initial investment in 2007, Johnson Controls launched the second investment project for a new cut and trim factory for car seats in the TIDZ Stip. The Croatian company Agrokor opened a purchasing and distribution centre for fruits and vegetables Agrofruktus, a Greenfield investment. Additionally, in the municipality of Petrovec, a cornerstone for a multifunctional trade centre was set in place, an investment of the Italian group Eurositalia. This same year a new trade centre began construction in Skopje, Skopje City Mall. As well, two joint ventures occurred, the coffee production factory Nelina Kafe, cooperation between a Macedonian company and Kord, a company from Hamburg, as well as between Macedonian company StilKon in cooperation with Dutch partner Gerliko Group, dealing with the processing of reinforced iron.

In year 2012 the promotion of the initiatives and politics of investing in Macedonia intensifies, targeting multinational companies and investors from different countries and cities, with the goal of significantly increasing foreign investments. In this year, many significant Greenfield investments entered Macedonia; firstly, with construction of the manufacturing plant by German company Kromberg & Schubert in the industrial zone Zhabeni, Bitola, DMM Drexler Mayer Kavadarci founded the namesake group for manufacturing cable sets from the automobile industry; furthermore, the American company Kemet Electronics entered Skopje1 free zone and started up a factory for producing electronic products intended for the aviation, defending and automobile industry, as well as the Italian company Techno Hose-Vitillo group in industrial zone Skopje1, which is intended for the manufacturing of armoured hoses for usage in construction, automobile and other industries. This same year British company Johnson Matthey" started the construction of a second plant intended for manufacturing catalysts, located in Skopje 1 free zone. Besides all the Greenfield investments, FDI this year decreased compared to the previous year in total of 111.22 million Euros.

In year 2013 major FDI include: The Macedonian-Croatian company, Dalmah Frigo that operates its business in the field of industrial refrigeration, refrigeration equipment, placed in Marino, Vptex Macedonia under the Dutch Van Pujienbroek Texitel, manufacturing Labour and Protective clothing, located in Kadino industrial zone, municipality of Ilinden. Furthermore, the acquisition of Swedmilk by Turkish Sutas, the Turkish company Cevahir commenced the construction of a complex that will include a combination of residential, business and retail areas as well as a large shopping mall in the base of the towers. The Italian construction company Condote began with the construction of four small hydropower plants in Macedonia. This year FDI in Macedonia marks an increase compared to the previous and amount to 252.20 million Euros or a growth of 2.8% of GDP.

In 2014 the Italian firm Itek, for the production of composite materials intended for the construction and automobile industry, began with the construction of a factory in Tetovo, the American company Amfenol in the building of Atom-Kocani, opened a plant for production of automobile parts. Furthermore, Dubai based company Apple Land opened an apple repurchasing and distribution centre in the industrial zone Makazi near Resen. Construction of the German ODW Electrik factory in the Ohrid-Struga free economic zone began. The facility will produce components for the automotive industry and construction will take place in two phases. At the technological and industrial development Zone-Skopje 2, a new plant of the Belgian bus manufacturing factory Van Hool is being officially opened. The German producer of mechatronic and electronic automotive parts

Kostal signed a contract to invest in a new plant in Macedonia as well as Technical Textiles, one more German company that produces fibreglass used in the automotive and aviation industries, wind turbines and ships, and insulating materials for the construction industry. Key Safety Systems (KSS), an American company and global supplier of advanced automotive safety - critical components and systems launched a Brownfield operation in the city of Kicevo, followed by a Greenfield operation in the Kicevo free zone. One of the most major Greenfield investments significant for the north-east region of Macedonia is the Turkish textile company Weibo Group that is expected to launch the construction of several textile factories in K. Palanka. Initially, the group started to use an existing textile factory in the same city. This 2014 year, FDI amount to 205.14 million Euros and a growth of 2.3% of GDP.

In year 2015 as well there is a decrease in FDI which amounts to 157.02 million Euros, despite the entry of several major investors in the TIRZ throughout the territory of Macedonia, regardless the benefits are expected in the following years. This year a contract with the Austrian company Teksport was signed for the construction of a factory intended for the manufacturing of protective clothing for labour. Following the success of the Government’s favourable investment incentives and availability of skilled workforce, the American Gentherm plant commenced its production in Prilep. Despite this, other American companies entered such as Delphi Automotive through a Greenfield investment in the industrial development zone Skopje 1, then Lear corporation, supplier of automotive seating and electrical distribution systems, Cap-Con Automotive Technologies that produces a full complement of automotive airbag inflators, Visteon Corporation signed a contract with the American company Johnson Controls to buy their automotive electronics segment, including the plant in Macedonia.

That same year, several Italian companies entered the industrial development zones including Montane group which began with the construction of a factory which will produce absorbers for rail vehicles, Diatec producing coated media for the graphic, textile and packaging markets, Condevo based in TIDZ Stip for production of wall-hung boiler components, also Italian Vitillo Group opened a second manufacturing plant in Macedonia. Although the political situation is getting worse, intensive campaigning and promotion of Macedonia as a favourable destination for foreign investments, is still the basis for the continuation of targeted events, road-shows, advertisements videos and the continued presence in all of the worlds more relevant mediums. According to Mizo, (2016), CEO of DTIDZ, the current political situation does reconsider foreign investors to come into the country but only prolong the process of investing in some companies.

Furthermore, in 2016, contracts with several investors are announced as well as signed, including German automotive company Akomplast for the manufacturing of car parts for automobiles by the latest technologies and German Electro-Mechatronic Systems GES for production of solar panels and LED fixtures. Furthermore, Indian group BRG in Veles signed a contract for the realization of an investment which the old factory Porcelanka will be reconstructed and restarted.

3.2 Structural Characteristics of FDI to Macedonia

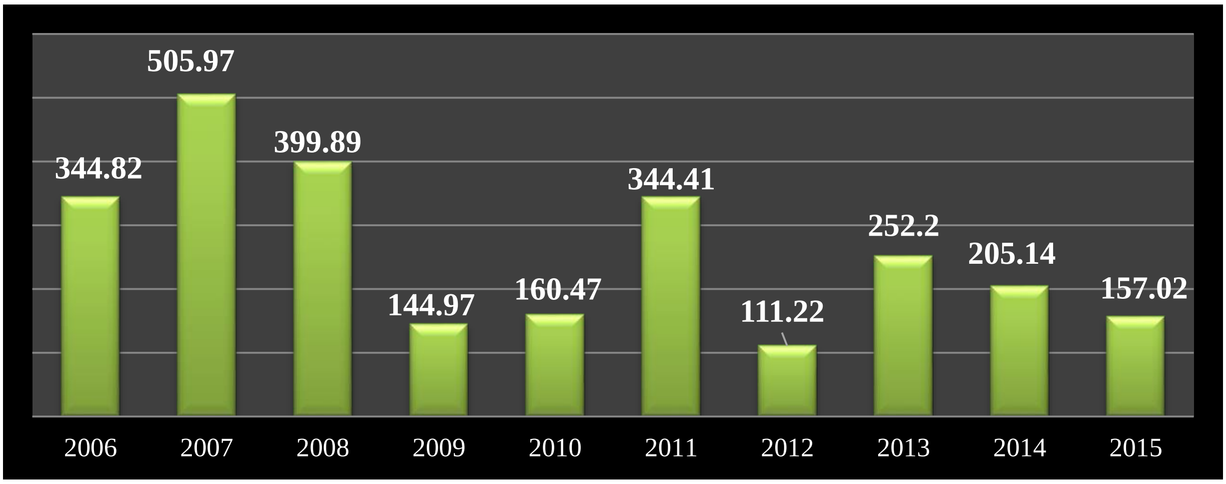
According to methodological calculations of NBRM which fully correspond to the methodological calculations of IMF and OECD, in the structure of foreign direct investments the following components are involved: **equity capital** and **retained (reinvested) earnings** and **remaining capital**. The first two components are related to invested equity capital and profits earned in Macedonia by companies that are already present here, but that profit is not to be transferred abroad rather reinvested in the businesses in the subsidiaries in Macedonia. In the structure of FDI in Macedonia the most significant share belongs to the equity capital and retained earnings.

The **remaining capital** component depicts the net amount of loans that subsidiary (daughter) companies (meaning present in Macedonia) and their parent (holding) companies give to each other. Trade loans as well as short-term and long-term loans between related entities fall under remaining capital. This component in the period from 2006 until 2009 marked positive value, i.e. the difference between **liabilities** to foreign investors (lending made by them to their daughter companies in Macedonia) and **assets** by them (the lending of their daughter companies in Macedonia to companies abroad, reverse investment in the table 4), so in the country there was an inflow of total 545.36 million Euros, and an outflow of total 92.22 million Euros in the form of lending done by daughter-companies. If the difference between the liabilities (Direct investor in direct investment enterprises) and the assets (Reverse investment) demands are added upon the equity and reinvestment of earnings from these four years, it amounts to total 1,395.66 million Euros of FDI for the above mention period. As a consequence of the world economic crisis, in 2009 the reinvestment of earnings is minus 113.17 million Euros, which represents the amount of profit by the companies transferred out of Macedonia. Consequently, in 2010 we have a drop of FDI in the country and it amounts to 160.47 million Euros (see figure 2).

As a result of the world economic crisis faced with decreased income, FDI in that period compensated with the earnings from emerging market economies. According to the table 4, there is a higher reverse investment to the parent companies from abroad of 68.35 million.
The following 2011, FDI marked an increase and amount to 344.41 million Euros, and in 2012, again, as a result of uncertainty regarding the sovereign debt crises and present risks globally, retroactive reverse investment towards holding companies abroad reappears, and there is a decrease of FDI in Macedonia which amounts111,22 million Euros (figure 2).

Although 2013 is characterized with an increase of FDI in relation to 2012 (252, 2 million Euros see figure 2), it's not long before in 2014 we have an outflow of the foreign companies earnings, i.e. a deficit balance of reinvestment of earnings of -169.4 million Euros according to table 4. The same year FDI amounts 205.14 million Euros (figure 2).
In 2015 the equity capital results negative rates -69.28 mainly because the equity component is recorded as – 81.69 million Euros (table4). This, as well as the previous (2014) year, the FDI flows in Macedonia investments between horizontally connected enterprises that appear for the first time (fellow enterprises are enterprises that are under the control or influence of the same immediate or indirect investor, and the capital relation between them does not exceed 10%.), NBRM (2014, p.6), and FDI amounts to total 157, 2.

Figure 2. FDI Inflows to Macedonia in Million Euros (2006-2015)



As a percentage of the gross domestic product of Macedonia, the foreign direct investments inflow in the period between 2006 and 2015 is displayed in the following Figure 3.

Figure 3. FDI in Macedonia as a Percent of GDP (2006-2015)

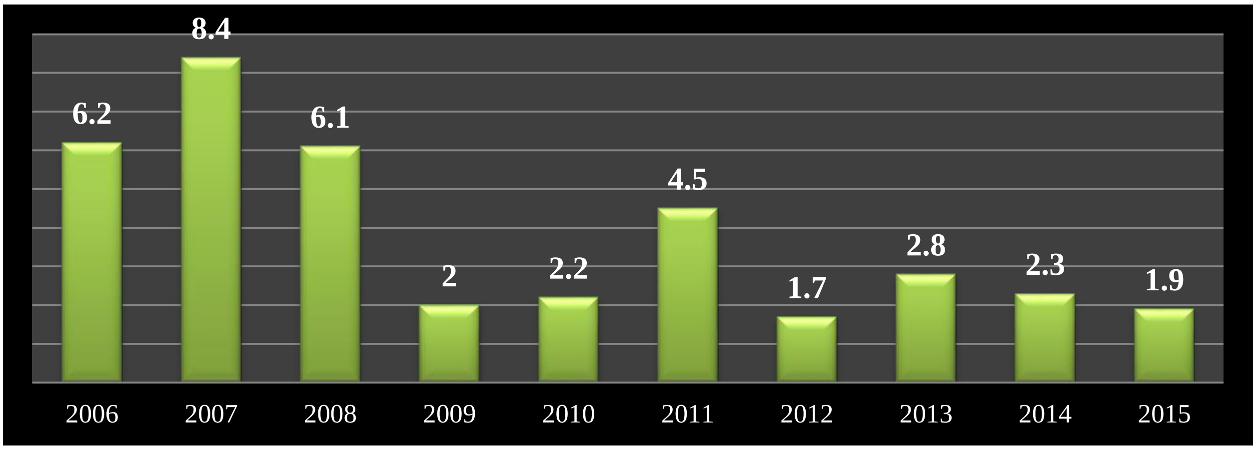


Table 4. Structural characteristics of direct investment in Macedonia (2006-2015)

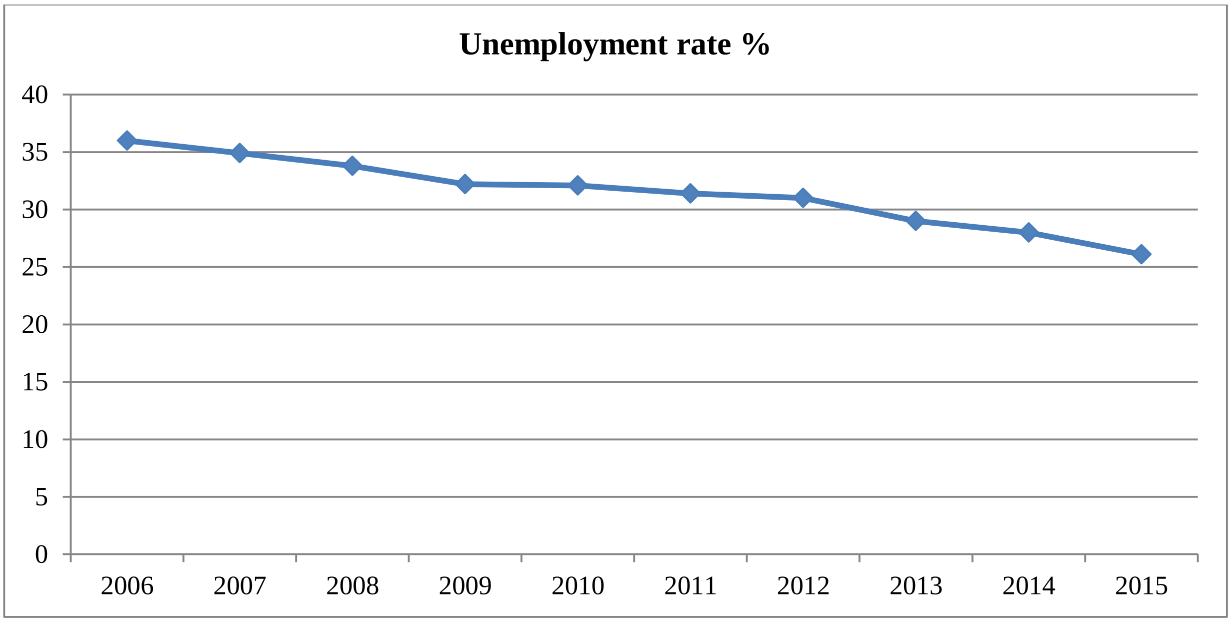
SDI in RM (in million Euros)	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
1. Net equity capital (Equity and reinvestment of earnings) (total a-b)	304.4	369.15	223.34	45.67	151.95	414.73	110.77	147.71	-107.55	-69.28
a. Equity	/	185.7	206.7	159.3	125.1	373	68.8	46.4	61.8	-81.69
b. Reinvestment of earnings	/	183.5	16.7	-113.7	26.9	41.7	42	101.3	-169.4	12.41
2. Direct investor in direct investment enterprises (liabilities)	43.09	162.56	193.94	145.77	76.87	-44.43	150.22	146.05	124.45	211.25
3. Reverse investment (assets)	2.62	25.74	17.39	46.47	68.35	25.90	149.76	41.56	-175.31	-6.69
4. Between fellow enterprises (net liabilities)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	12.94	8.37
5. Total remaining capital (5=2-3+4)	40.4	136.82	176.55	99.30	8.51	-70.32	0.46	104.49	312.69	226.30
6. Total FDI (6==1=5)	**344.8**	**505.97**	**399.89**	**144.97**	**160.47**	**344.41**	**111.22**	**252.2**	**205.14**	**157.02**

Since its independence up to now the Republic of Macedonia notes high rates of unemployment and as one of the measures that the government undertakes is the activities related to the increased volume of investments all with a goal for opening new employment opportunities and reduction of the unemployment rate. According to Mizo, (2016), at the moment 23 foreign companies are operating in the Technological Industrial Development Zones throughout the territory of Macedonia, employing 6100 employees. (Here I must note that this number is not negligible in relation to the current amount of unemployed citizens that is 248.933 persons, State statistical office, 2016). This sum would be even higher if we were to add the jobs that were opened because of the foreign investors out of the zones, for example Drexler Mayer and Kromberg and Schubert etc., and a figure of over 13 thousand employments is reached, (Kapital, 2015 p.25).

Moreover, there is a constant decline in the rate of unemployment in Macedonia in recent years (2006-2015; see figure 4). Positive movements on the labour market correspond to an accelerated economic activity in the same period, as well as the measures and policies that are continuously implemented by the government with an aim of reducing unemployment and the FDI inflow and the creation of new capacities in the technological industrial development zones which absorbed a new labour force, (Ministry of finance of the Republic of Macedonia, 2014).

A record rate of 26, 1 % unemployment was reached in 2015 (lowest since independence). Below in the figure 4 there is graphical presentation of the unemployment rate from year 2006 to 2015 from where it can be seen the continuous decline in the unemployment rate.

Figure 4. Unemployment Rate in Macedonia (2006-2015)



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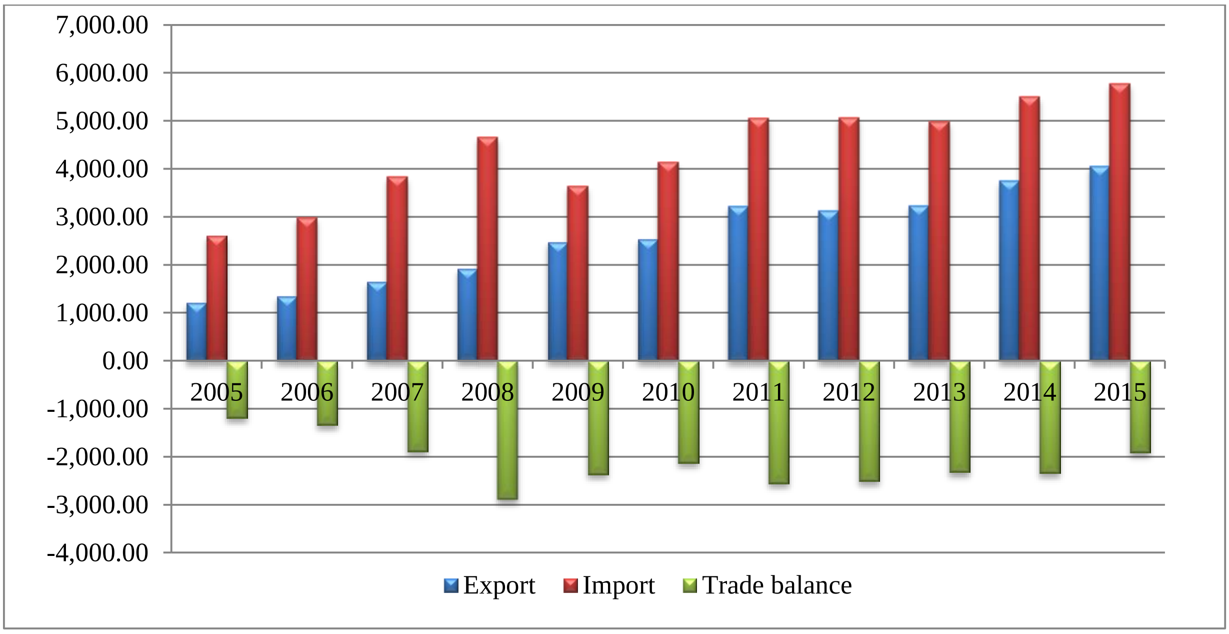
What is also evident is that the foreign investors' entry increases the net-exports and at the same time change the structure of Macedonian current account (the current account in Macedonia is in constant deficit and private transfer flows-remittances are major source of financing for the large trade deficit). Only in the Industrial zones in 2015 the net-export reached 229, 39 billion Euros, i.e. export in the Industrial zones is 1475, 22 million Euros and the import in these areas amounts to 1245, 83 million in absolute value (ZMAI, 2016). Several years in succession, one of the major exporters is the foreign company Johnson Matthey which manufactures catalysers, and its export equals to 20% of the entire country net-export (Kapital, 2015, p.26).

In figure 5, giving the period of 2005 to 2015 there is a continuous increase of an overall country export, however, at the same time the foreign companies are importers as well, so it can be concluded that up until foreign companies in Macedonia started to provide raw materials and goods from the domestic sector, the real net export effect from FDI in Macedonia would be far from the expected. According to Mizo (2016), foreign companies from the Industrial Zones employ the domestic companies only for servicing and maintenance of the equipment and machinery, transport and logistics, catering; construction companies are hired for the building of the plants. The investment strategy of the government focuses on industries without any previous presence in the sector structure of the country (automotive industry) and that is exactly why the linking of foreign companies with the domestic economy is a challenge; because of the technological gap foreign investors on the domestic market have a difficult time finding suppliers needed for their inputs.

Figure 5. Export, Import and Trade Balance in Macedonia in Million Euros (2006-2015)



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3.2.1 Sector Structure of FDI in Macedonia

The most available data for sector structure of FDI in Macedonia is according to the database compiled from NBRM (n.d.) and table 5 below shows a breakdown of the main export products of Macedonia by their sector composition of FDI contribution in the year 2006 up to 2015 (here I must highlight that there is not available data of separate foreign companies' participation in accordance to industrial sectors by none of any institutions in Macedonia). The heavy reliance on primary products is noticeable (several separated rates -3 in manufacturing and 3 in services compositions); it doesn't show more advanced level of export diversity and overall economic complexity (higher value added products).

Investments have gradually branched out of traditional sectors such as food and metal processing into technology-intensive industries, in particular automotive components for which major global players have become Macedonian main exporters (IMF, 2015 p. 11).
If data on the proportion of FDI in sectors in particular is analyzed, a fluctuating movement can be seen, i.e. manufacturing marks a negative rate in 2008 of -15.50 million Euros and an increase in 2011 of 208.77 million Euros. In 2015 it is on a relatively low level of 11.28 million Euros. While the service activities decrease after 2008, and in 2015 they are at an in elevation level of 219.49 million Euros.

Analyzed rate by rate, among the highest FDI structure contribution in Macedonia is the overall **service activities** participation, of which mostly in the **wholesale trade and retail trade** sector. In principle, possibilities for FDI to take place at other points on the food value chain, especially in downstream activities such as warehousing, wholesale and retail trade (UNCTAD, 2012 p.16), and what is unique for this rate (wholesale and retail trade in the service sector) is that in 2015 it notes the highest FDI inflow of 214.64 million Euros, a year in which all of the listed rates in table 5 note small, insignificant and even negative FDI inflows.

Among other services with the high participation of FDI are **information and communication** (here in the year 2006, 2007 and 2008 the calculations from the National Bank are not submitted) and **financial and insurance** activities which are also presented in table 5. In the last two components there is a fluctuation and the amount of FDI inflows varies differently in different years, due to the economic crises fluctuation. So, sector financial and insurance activities according to table 5, in 2007 reach the amount of 119.00 million Euros of the FDI inflow. In 2009 and 2010 they note a negative rate (mainly because of the reverse investment-assets of subsidiary to holding parental financial companies), but in the following years the FDI inflow slightly increases.

As mentioned above, the result of the newly established capacities in the economy, a notable improvement in the sector structure is registered as well as in the **manufacturing**

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sector. The highest participation of foreign investments in manufacturing is in 2011 (208.77 million Euros), and the lowest in 2015 (11.28 million Euros), (see table 5). That is based on the increased share of a higher value-added product, vehicles and other transport equipment, in the previous years and from 2009 according to table 5 there is a continuous growth of FDI in this sector, (Ministry of Finance of the Republic of Macedonia n.d.). The country also collaborates closely with international firms through contract manufacturing; textile production companies in Macedonia work mostly for European and United States companies such as Jean Biani, Kigili, Insight, C&A, Boss, Mexx, Liz Clairborne, etc. and composition textiles and wearing apparel and a composition **textiles and wearing apparel** with participation of FDI shown in table 5.

Climate conditions, a longstanding accumulation of skills and traditions make agriculture the particularly important sector for the economy of Macedonia. This does not mean, however, that it would be automatically a major target for inward FDI, UNCTAD (2012 p.16). **Agriculture, forestry and fishing** display oscillating movements of FDI inflow presented in the table 5 and a slight significance indicates in year 2007 amount of 10.46 million Euros, 2013 an amount of 8.28 and amount of 10.67 million Euros in 2014.

Macedonia possesses both metal ores and water resources, making it an attractive destination for steel production (UNCTAD, 2012 p.17). Here I would remark that in Macedonia the water is an important element for electric power production, agriculture, industrial and urban sectors and the sector is State owned and is controlled on national and municipal level. However, over the past 20 years, governments of some developing countries have opened up some elements of water infrastructure for private investment and the reason behind this is better management and more funding of water infrastructure.
In addition, sector **Mining and Quarrying** displayed in table 5 for the given period, also shows volatile movements (in some years negative rates of an investment appear see table 5 below) of FDI inflow, due to the fact that all major mines acquisitions happened before 2006. Thus, I will single out the significant FDI inflow in the years: in 2008 there is an amount of 70.24 million of FDI manly because of a subsequent investment for modernization programme and investment for the projects related to environmental protection of Duferco (Switzerland) in year 2007 and a purchase of lead and zinc mines Zletovo and Toranica, UNCTAD (2012). Although in 2009 as a consequence of the world economic crisis there is a negative balance, in the next two (2010 and 2011) years there is still an inflow of 3.62 million Euros in total. Successively, in the following year a decreasing level of FDI in this area reappears.

A higher share of FDI in the sector **Electricity, Gas, Steam and Air Conditioning supply** surfaces in 2006 as a result of the privatization of AD ESM (a distribution segment) by selling 90% of the shares to Austrian EVN Group. During the remaining period no significant FDI are noted in this sector.

Table 5. Sector Structure of FDI in Macedonia in Million Euros (2006-2015)

Year	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Agriculture, forestry and fishing	2.13	10.46	4.06	0.08	0.98	2.64	2.92	8.28	10.67	4.46
Mining and Quarrying	0.60	8.92	70.24	-5.77	42.09	43.55	-17.22	4.02	27.85	-103.65
Manufacturing	99.40	126.80	-15.50	48.44	84.59	208.77	49.35	85.17	57.87	11.28
-Food products, beverages and tobacco products	5.50	21.83	0.00	34.01	13.81	49.27	-17.43	-5.87	-2.11	34.42
-Textiles and wearing apparel	3.66	7.26	0.00	4.71	6.22	26.22	23.60	17.18	8.32	-13.11
-Vehicles & other transport equipment	1.08	0.27	0.00	54.67	69.03	88.34	24.04	99.44	90.10	-24.53
Electricity, Gas, Steam and Air Conditioning supply	119.20	-3.57	26.23	24.42	1.28	5.09	21.90	14.92	27.60	-6.63
Construction	3.27	14.80	20.52	10.04	18.98	21.51	16.59	42.55	6.34	4.88
Total services	118.87	339.01	295.23	69.35	12.94	63.72	38.53	96.57	74.77	219.49
-Wholesale and retail trade	42.96	45.57	0.00	37.68	23.06	23.55	8.95	38.07	19.57	214.64
-Information and communication	/	/	/	17.88	10.27	-79.39	-2.27	6.77	-4.06	17.06
-Financial and insurance activities	40.99	119.00	0.00	-8.90	-25.75	75.48	36.42	29.11	52.06	-33.02

3.2.2 Regional Structure of FDI in Macedonia

The analysis of the geographic distribution of Macedonian regional structure confirms the dominance of the EU countries as major foreign investors (see figure 6). According to the NBRM taken into account the total period of 2006 to 2015, the largest share of FDI among countries shown in the figure 6 below, the major regional participants are: Austria with total investments of 427, 6 million Euros or 21% of the total country participation. In Macedonia over 60 Austrian companies are present in the service sector of which: banking, insurance, power distribution, telecommunication, construction and other.
The second place is taken by Slovenia and Slovenian investors and it is up to 17% of FDI participation and they are active in various areas including: banking telecommunications, real estate and others with 362.8 million Euros in total for the given period (see figure 6).
In addition, the Netherlands, the third largest investor with amount of total 343.4 million and also 17% of FDI participation, with a continuous growth in the given period from figure 6. Dutch investors mainly allocate the manufacturing (metal industry) and service activities (transport and communications).

Turkey, Germany and Switzerland are also important trading partners of Macedonia with a participation of 9% and 8% in total FDI in Macedonia (figure 6). Turkish investments already developed in the banking sector, metal, food and textile industries. Because of the intensified economic and trade collaboration, Germany is becoming an ever more significant investor through several major investments of German companies such as Krombert and Shubert, ODW Elektrik, Drekselmaer, Technical Textiles.
Bulgaria although by value has got permanent growth; percentile participation in relation with total foreign direct investments in Macedonia, is relatively low and up to 2015 is 119.8 million Euros or 6% (figure 6).

Greece is present in services (banking sector and food processing), manufacturing (oil refining, food industry and textile industry), in construction and in mining (marble industry), the most significant investments took place before 2007, and in the following years they are in a constant fall as a consequence of the economic crisis in Greece.

Among the ones with the smallest share of total 3% regional participation are Croatia, Italy, England and USA mainly present in recent years in the Technological Industrial Development Zones (Tekno Hose, Johnson Matthey, Johnson Controls, Kemet Electronics Corporation, Lear Corporation, Key Safety Systems etc.

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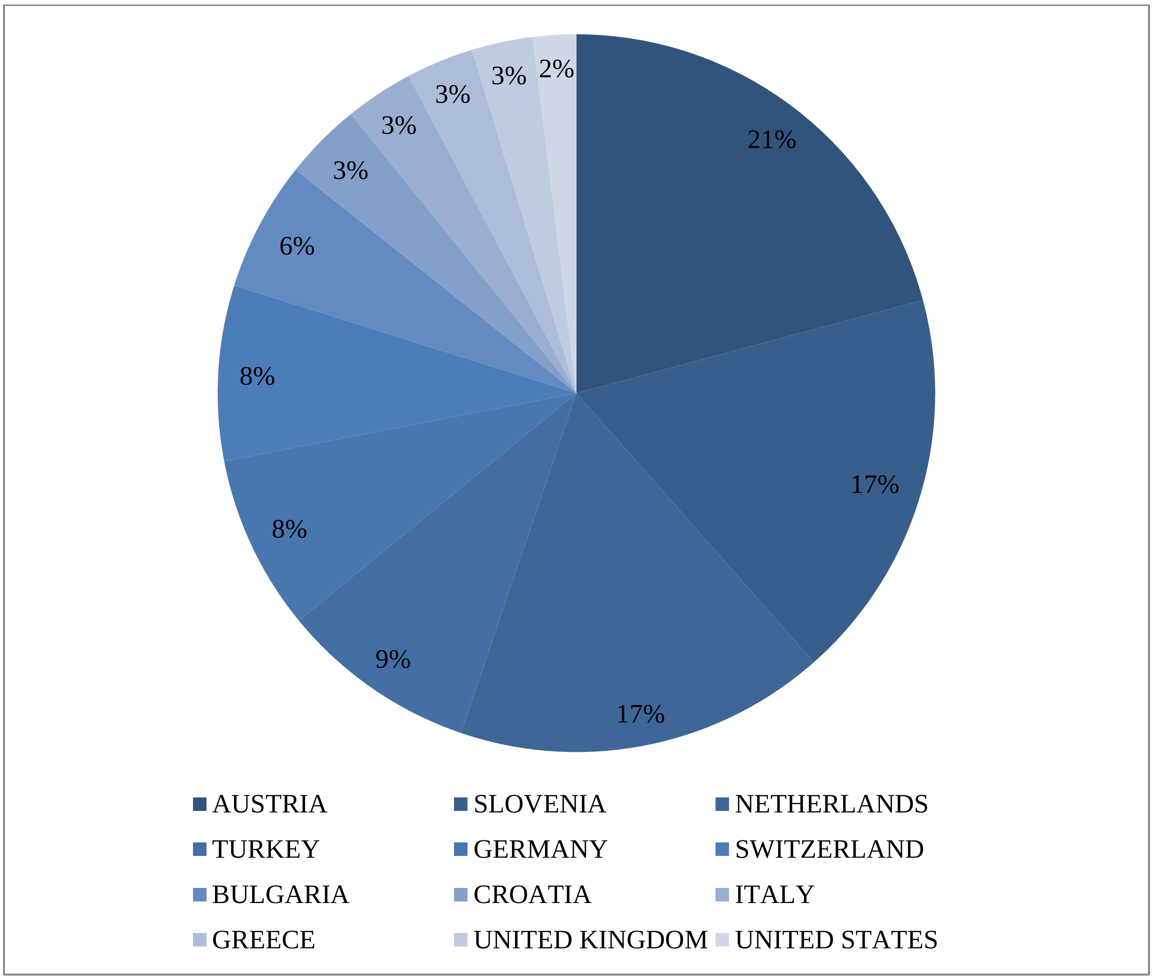
Figure 6. Largest Shares of FDI in Macedonia by Country



4 ECONOMIC POLICY IN MACEDONIA AIEMED AT ATTRACTING FDIS

4.1 Key Features of the Government Policy for Attracting FDI

The policy of the Republic of Macedonia focused to increase FDIs inhabits an important place in the Government program in order to encourage the foreign investment in Macedonia. Since the internal market of the country (population of 2.1 million inhabitants and a GDP of 11.3 USD billions in 2014) is not sufficient to maintain long term high growing rates, Macedonia should rely on exports as the engine of growth.

Over the past years, the country developed and implemented key reforms to improve various attractive features to foreign investors including investor protection, a favourable and simple tax system and improving the process of registration and licensing. In 2016 Macedonia based on the reforms it ranks as one of the most successful countries in the world, springing from the 92nd position within the report “Doing Business” of the World Bank Group (2016) in 2006 to 12th place in 2016.

Regarding this, policies and measures to increase FDI usually are divided into broad and tight measures. Broad measures cover the global stability of the country in the economic, legal and political sense by improvement of the business environment with an aim of promoting investment, both domestic and foreign.

4.1.1 Overall business environment

The business environment in Macedonia has consistently improved. Stable macroeconomic position is achieved through healthy macroeconomic policies, prudent and cautious fiscal policy, high level of public investment, introduction of anti-crisis measures and structural reforms.

The Global Competitiveness Report has been one of the main tools for benchmarking competitiveness, and is a set of institutions, policies and factors that determine the level of productivity of an economy which in turn sets the level of prosperity that the country can earn (The Global Competitiveness Report, 2015, p.4).

To come to its conclusions, the Global Competitiveness Index combines 114 indicators that capture the concepts that matter for productivity, grouped into 12 pillars and the results for Macedonia from the recent Global Competitiveness Report for 2015 – 2016 (2015, pp.10-14) are shown below in table 6, 7 and 8.

Table 6. The Global Competitiveness Index 2015-2016: Basic requirements

Basic Requirements							
Pillars							
Institutions		**Infrastructure**		**Macro-economic Environment**		**Health and Primary Education**	
Rank	Score	Rank	Score	Rank	Score	Rank	Score
52	4.14	78	3.77	47	5.09	76	5.61

Source: World Economic Forum, *The global competitiveness report 2015–2016*, 2015, Table 3, pp. 10, 11.

Table 7. The Global Competitiveness Index 2015-2016: Efficiency Enhancers

Efficiency Enhancers											
Pillars											
Higher Education and Training		**Goods Market Efficiency**		**Labour Market Efficiency**		**Financial Market Development**		**Technological Readiness**		**Market Size**	
Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score
46	4.79	33	4.65	84	4.07	52	4.09	63	4.15	108	2.94

Source: World Economic Forum, *The global competitiveness report 2015–2016,* 2015, Table 4, pp. 12, 13.

Table 8. The Global Competitiveness Index 2015-2016: Innovation and Sophistication Factors

Innovation and Sophistication Factors			
Pillars			
Business Sophistication		**Innovation**	
Rank	Score	Rank	Score
72	3.87	58	3.38

Source: World Economic Forum, *The global competitiveness report 2015–2016,* 2015, Table 5, p.14.

Macedonian overall ranking is 60^{th} out of 140 countries, and it is considered to be on Stage 2 of Development so called “Efficiency Driven”, along with 31 similar economies.

4.1.2 Institutions aim to support foreign direct investment in Macedonia

The conditions that encourage investment with wider social, economic and institutional context are largely determined by the state. In that context, it is necessary to build a solid institutional basis for policies for domestic and foreign investment in order to support a sustainable investment promotion in Macedonia. Institutions that aim to support foreign investments in Macedonia are institutions that apply to national (Government) and regional as well as local level.

Since 2006, policy of the Republic of Macedonia for increasing foreign investment, occupies an important place in the Working Program of the Government and in the Program for promotion of investments in the Republic of Macedonia.

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The aim of the Government is to develop policies and implement reforms that would lead to a more dynamic economic development. Thus, the economic part of the Program to encourage investments in Macedonia contains reform policies and measures in five main groups: stable macroeconomic and fiscal policies, tax and customs policy, improvement of the business climate and competitiveness, encouragement of the investment and support for small and medium enterprises (Програма за поттикнување и инвестиции во Република Македонија 2011-2014) [Program for encouraging investments in Macedonia 2011-2014].

In year 2006 the Government started the regulatory reform that has been introduced as Regulatory Guillotine which led to improved regulatory quality, the abolition of bureaucratic procedures and formalities and reduction of the possibility of bureaucracy and corruption.

The Republic of Macedonia has got a developed infrastructure for dialogue between the public and private business sector on the topics related to investments to improve investment climate to different levels of efficiency, including:

- **Foreign Investors Council** (established in 2006, counts 127 members and tasked to help to attract foreign investors to promote the country and help to create a more favourable legal and regulatory climate, and it is closely associated with the Economic Chamber of the Republic Macedonia);
- **International Investors Council** (established in 2002, comprises 22 investors, most of Greece and seeks to cooperate with private sector, municipalities and international organizations in order to promote the private sector and by promoting the cooperation among participants to improve the investment climate of the country);
- **National Council for Entrepreneurship and Competitiveness** (established 2004 year in order to improve the dialogue between the private civil and public sector. Government realizing the importance of this Council has decided to revive and strengthen the organization in order to use his great potential as a tool to achieve a successful public-private dialogue between foreign and domestic investors)

Activities associated with the promotion of domestic and foreign investments and as well as the activities in the area of tax reform, regulatory reform, cadastre reform, investment in infrastructure, policies on agriculture and energy sectors are within the competence of *the Deputy Prime Minister for Economic Affairs* and coordination of economic sectors.

Under the Government Working Program for attracting FDI is *Minister without portfolio* for FDI, whose task is to establish contacts with potential investors and to put focus on the priority sectors, especially in manufacturing and Greenfield investments which are related to the specific technological industrial development zones.

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Investment Committee audits the process of investment and care of the removal of any obstacles to investment in the country. Members of the Investment Committee are the Prime Minister, Deputy Chairman of the Government for Economic Affairs and coordination of economic sectors, the Minister without Portfolio for FDI, the Minister of Economy, Minister of Finance, Minister of Transport and Communications, Director of ASIPIRM, Director of the Directorate for technological industrial development zones and the Director of the State Geodetic Institute.

Team Macedonia, that in turn is consisted of the Prime Minister, Deputy Chairman of the Government for Economic Affairs and coordination of economic sectors and Director of ASIPIRM and marketing initiative on a high level that deals with the preparation and implementation of a series planned visits for marketing purposes i.e. international visits and an offer of land to potential investors from selected companies.

Agency for Foreign Investments and Export Promotion of the Republic of Macedonia – Invest Macedonia, is the primary government institution which is in charge of attracting new foreign investments in the country and supporting the expansion of the foreign companies with already established operations (Invest in Macedonia).

The responsibility of Invest Macedonia includes the following activities:

- encouraging Greenfield investments,
- subcontracting for providing state aid for TIDZ and provide information on the total amount of state aid,
- information services for exporters about international trade, export procedures, customs tariffs, legal procedures for taxes, obtaining licenses and permits, business partners etc.,
- actions to promote exports to connect the Macedonian exporters with foreign buyers; information services for foreign companies about export potential of Macedonia,
- organizing participation and support of Macedonian exporters at international fairs, seminars and business events,
- researching the access to foreign markets and study the key sectors in the countries and regions (Програма за поттикнување инвестиции во Република Македонија 2011-2014) [Program for encouraging investments in Macedonia 2011-2014]

The Directorate for free economic zones which was founded by the Law on free economic zones by adopting the law on technological industrial development zones continued working as Directorate for Technological Industrial development zones (hereinafter: DTIDZ) in order to create, develop and care industrial development zones for related activities, including monitoring and regulating the activities for the users of the zones and issuance permits for starting, developing and completing users' activities. Technological industrial development zones provide favourable conditions for developing business activities by offering regulated industrial sites and pre-built factories with fully ready legal and physical infrastructure investment, services and tax, customs and other benefits.

4.1.3 Specific FDI incentive

In order to revive the economy, foster economy growth and reduce poverty, Macedonian government has taken many measures specifically about attracting foreign investors. Since 2006, with the intention of creating a favourable international investment position, country's actions have been in direction of an expansive campaign to attract foreign investors that include the promotion of Macedonia in many of the world's leading newspapers and magazines and frequent government-led road shows. In addition, the country also has taken legal actions by changing the regulatory framework and regulating business activity in Macedonia. All foreign investors are granted the same rights and privileges as Macedonian nationals; they are entitled to establish and operate all types of self-owned private companies or joint-stock companies. Macedonia has introduced a one-stop-shop system that enables investors to register their business after 2 hours of submitting an application (DTIDZ, n.d.).

After 2006, the Government introduced their FDI attraction policies, tax policies and active labour market measures. In the period from 2007 up to 2009, the Government began to implement policies operational plans by introducing one of the lowest flat taxes on profit and income in the region (10%), and reducing the rates of social security contributions.
Having in mind that Macedonia is a small country in terms of potential, due to lack of natural resources and market attractiveness due to its small size, the government investment measures, also mainly focused on developing high value-added manufacturing and strengthen export promotion efforts, and on establishing enabling conditions for labour market flexibility and skills development (The World Bank, n.d.).By offering tax breaks incentives, competitive wages and improvements in business environment, the Government has successfully attracted FDI in recent years and contributed to Macedonian overall export diversification. An improved export performance is needed to strengthen the trade balance and reduce the country's dependence on remittances from migrant workers to raise the national income. Attracting FDI and building up export capacities has been the linchpin of the authorities' economic policy over the last decade (IMF, 2015, p.3).

One of the reasons behind the governmental incentives and the establishment of the Technological Industrial Development Zones is the effort to attract foreign companies with an export of value-added commodities, i.e. diversified away from traditional product lines to more capital intensive goods. Reflecting developments in the TIDZ, Macedonia has recently built up revealed comparative advantage in new products. While remaining highly competitive in the production of textiles, beverages, tobacco and food products, the country managed to push dramatically its advantage in chemical products as well as technology-intensive industries, in particular automotive components (IMF, 2015, pp. 3-11).

Another reason behind the governmental incentives is the establishment of TIDZ throughout the entire territory of the country in order to create employment opportunities in accordance with the strategic concept recall of a country equal economic development (Kapital, 2013). The Free Zones Authority currently manages three fully operational zones: Skopje 1 and 2 in the capital, and one in Stip, the largest town in Eastern Macedonia. The zone in Tetovo is currently operating as a public private partnership, and is in the process of implementing its first investment projects. Simultaneously, eleven zones intended for equal economic advancement of all regions in Macedonia are in various stages of development (DTIDZ, n.d.).
Incentives offered to foreign investors in TIDZ include:

- 10-year profit tax exemption and to 100% reduction of personal income tax for a period of 10 years,
- investors are exempt from payment of value added tax and customs duties for goods, raw materials, equipment and machines,
- the land in the TIDZs in Macedonia is available under long-term lease for a period of up to 99 years at concessionary prices,
- investors are exempt from paying utility taxes to the local municipality and fees for land building permits,
- free connection to natural gas, water and sewage network,
- the Government of Republic of Macedonia may participate in the construction costs of the investor in the TIDZ up to EUR 500.000 depending on the number of new employees and the user's investment amount (Directorate for Technological industrial development zones).

Thanks to the impact of the government's TIDZ program which offers industrial parks and incentives to attract FDI and sustained quality of TIDZ services, FDI inflows in the zones has continued to grow, in fact they more than doubled since 2011 with increasing exports and creating jobs (The World Bank, 2015, pp. 18-19). Owing to the government's targeted investment promotion investment efforts, Macedonia emerged as an attractive destination for the FDI mostly in the automotive industry: 18 foreign companies have established manufacturing facilities since 2007 (with a significant acceleration over the past three years). Foreign investment also provided new employment opportunities; more than 6000 new jobs have been created in the zones since 2011.

Ultimately, though very important institution which plays an important decision attracting foreign and domestic investors is *the local government.* Municipalities in the Republic of Macedonia with the decentralization process gained new responsibilities related to strategic government measure regarding country equal economic development and because many municipalities have established offices for local economic development which should help in determining the potential locations for investment and facilitate the process of buying land and obtaining construction permits. Also, the municipalities building and develop industrial zones for investments of domestic and foreign investors.

4.2 Government Policy for Attracting FDIS as Assessed Through the Questionnaire

In order to determine the possibilities of the government policies to attract foreign direct investment in the country, it has been taken a survey research in companies with foreign capital in Macedonia.
The results of the survey implemented on the theoretical postulates of thesis contributes to the appropriate conclusions aimed to identify opportunities and provide appropriate recommendations for attracting foreign direct investment in the country.

4.2.1 Introduction into the survey and its questionnaire

The following questionnaire is based on the survey for master thesis regarding the FDI in Macedonia, with title: "Host governmental incentives for attracting FDIs: the case of Macedonia", for which questions are prepared in order to assess.

The survey relies on the structured questionnaire that has got five chapters, including, in the first part questions which identify the general information about the responding company which, as it is indicated in the questionnaire, are strictly confidential. The second part of the questionnaire provides questions in order to access the factors that influence the organizational motives for investment decision. The third set of questions refers to location selection; the forth part is related to the challenge factors that may cause a problem in the investment process. Finally, the fifth part is a set of questions about the economic parameters in Macedonia and the future plans for investment decisions.

The data for the survey has been acquired partly through the internet and partly through direct contacts with relevant representatives of the companies. Although, participation in this study is voluntary and confidential, it must be emphasized that companies are not as responsive (it has been sent to more than 40 companies with foreign participation in Macedonia). Also, the research is narrowed mainly due to the targeted group of FDI entered RM after 2006.

The survey was conducted during the years 2015 and 2016 and the processing of the responses on the questionnaire was performed by using Microsoft Office Professional Plus 2010 (Microsoft Word and Excel Professional Plus 2010).

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The following sections contain the number and positioning of the questions and responses on the questionnaire analysis received which are presented in tables and appropriate graphs (figures).

Equity share of the investor in the company of the recipient are mostly in form of Greenfield investments or joint venture foreign investments. 15 responding companies come from altogether 8 countries, 4 from UK, per 3 from Turkey and Austria, and per 1 from Belgium, Bulgaria, Croatia, Germany and Switzerland.

Table 9 signifies the main activities of the responding companies included in the survey.

Table 9. Main Activities of the Responding Companies

Main activities of the researched companies	**Number of responses**
Wholesale	1
Industrial supplies	1
Manufacturing of wiring harnesses and electromechanical assemblies	1
Informational technology services	1
Civil engineering	1
Call services	1
Warehousing	1
Catalyst manufacturing	1
Electronic parts for sailing vehicles	1
Manufacturing of buses and coaches	1
Airport management	1
Garment manufacturing	1
Renting and selling equipment for gambling	1
Transport and logistics	2

4.2.2 Analysis of responses on the questionnaire

Section 1. Motives for investment

In this section, 15 optional motives for investment are offered to the responding companies, wherein, consistent with the implemented Likerd scale, there is a grading possibility of 1 to 6 important ranking points (not at all up to highly relevant motive for investment). Therefore, the closer the degree of importance is to unity, the more important is the corresponding motive.

The below shown figure 7 in average terms lists all the possible motivational factors that stand out in the questionnaire. Hence, factors graded as the most influential concerns the foreign motives for the investment decision in Macedonia are the **low labour costs,** where the average importance ranking value is 5 out of maximum 6 points. Besides the **low labour costs,** for the responding companies among the high-graded motives for investment are also the motives of **quality labour force and the access to knowledge, skilled labour and technology in Macedonia.**

Understandably, cheap, quality and knowledge skilled labour is the most attractive motivational factor to labour intensive MNEs, like the producers of auto catalysts, manufacturing of buses and coaches, textile whose production is price sensitive and labour costs, is the major element of the total production costs. Cheap and quality labour was also found to be an important factor to wholesale and retail trade, services like transportation and storage which emphasize that Macedonia has got a lot of inexpensive, but skilled and promising young professionals. In addition, while FDI inflows in the country investment zones are mainly targeted on the automotive industry and labour qualification, Mizo (2016) in his interview stressed out that in Macedonia an educated staff could be found with some basic qualifications which can then later be additionally improved.

Low labour costs motivational factor is followed by **Good geographic location and infrastructural connection,** with the ranking of average value 4, 8; another important motive and a location factor for foreign investors to invest in Macedonia. This high average ranking could be described by two factors, reflecting the two aspects of the geographical location motive: proximity to the investor's countries and proximity to the markets. Macedonia also is a gateway to Southeast Europe (hereinafter: SEE), most of the responding companies export to SEE countries. Besides its geographical proximity, Macedonia has a lot of knowledge about SEE countries' culture, business style, customs and language.

But then again, regarding the other motives, there is also a tendency of foreign investors, by accessing the Macedonian market, **to access to SE European markets as well as access to EU markets** which consecutively means **development of products and services** for global markets.

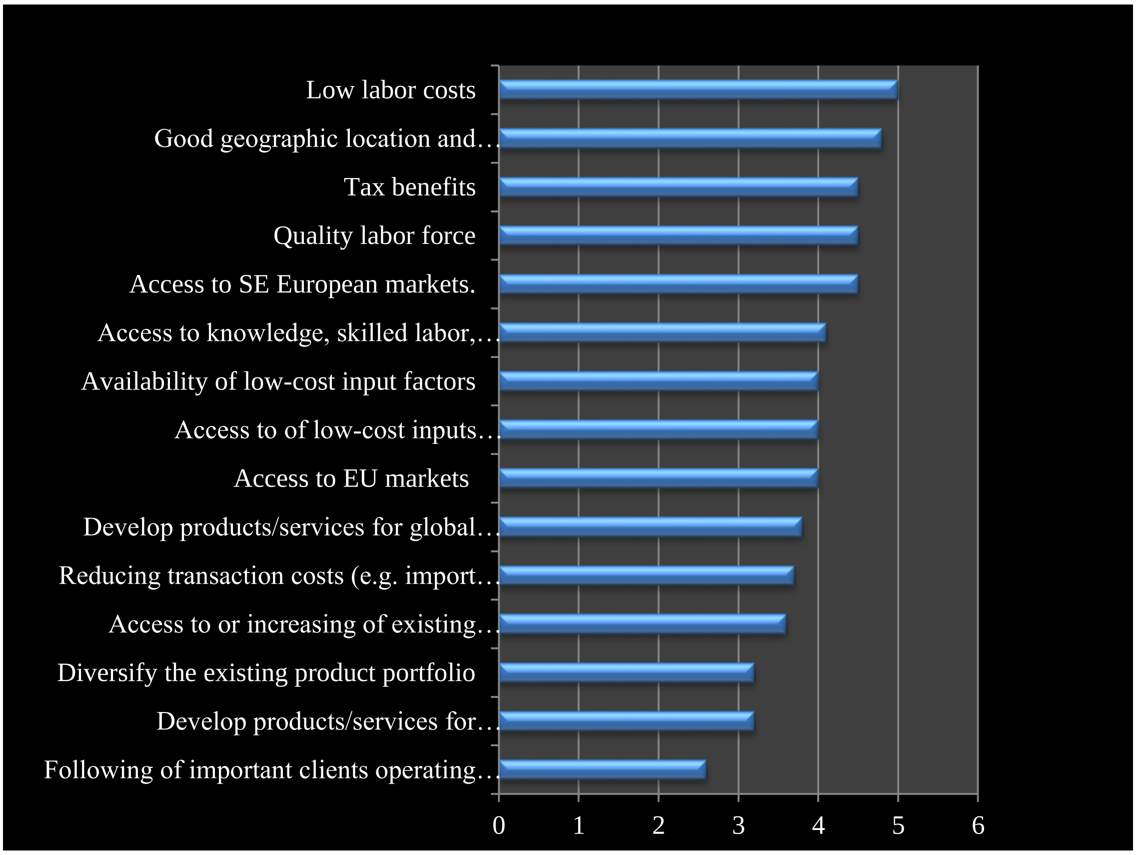
In addition, economic stability, monetary and fiscal regulations and a pleasing **tax system and benefits** offered by the government have favourable effects in FDI attracting power in recent years. By creation of an attractive tax package in recent economic reforms like introduction of flat tax rate of 10% for corporate and personal income and simplifying the tax system, it stimulates the successful companies to further improvement of operations and increase of the profitability (Invest in Macedonia).

With the average grade of 4 concerning **availability and access of low costs input factors (material, components, and parts)** are behind the responding companies' motive for investment in Macedonia. Foreign investors are a kind of a new market for domestic firms and for many countries that bases their economic development on FDI and this aspect represents a key effect and priority that countries recipients have set up as their goal (Kapital, 2014). It is remarkable that responding companies in investment zones rated cheap inputs of no importance at all. Virtually all of the raw materials that foreign investors consume are imported from abroad since the majority of companies have no connection with the capacities and potentials of the Macedonian economy.

Among the lower rated investment motives from the figure 7 are **reduction transaction costs (e.g. import tariffs)** with the average grade of 3,7 and **access to or increasing of existing market share in Macedonia** with the average grade of 3,6.

The unfavourable motives for the investors are **following of important clients operating in Macedonia, developing products/services for Macedonian market and diversification of the existing product portfolio** (figure 7) which leads to the conclusion that MNEs that entered these previous years are still oriented towards the manufacturing of the current products.

Figure 7. Average Ranking of the Motives for Investment



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And finally, as a completion point for the analysis of motives regarding foreign investment in Macedonia is to distinguish two types of investment projects by their main strategic motivation for locating in the country. According the respondent companies in the questionnaire, among dominant motives are the efficiency-seeking foreign investments made with the purpose of taking advantage of tax benefits, low labour costs and availability of low-costs input factors. The second category represents market-seeking foreign investments whose main objective is to supply the Macedonian and other SEE and EU markets.

Section 2. Reasons for selecting Macedonia as FDI location

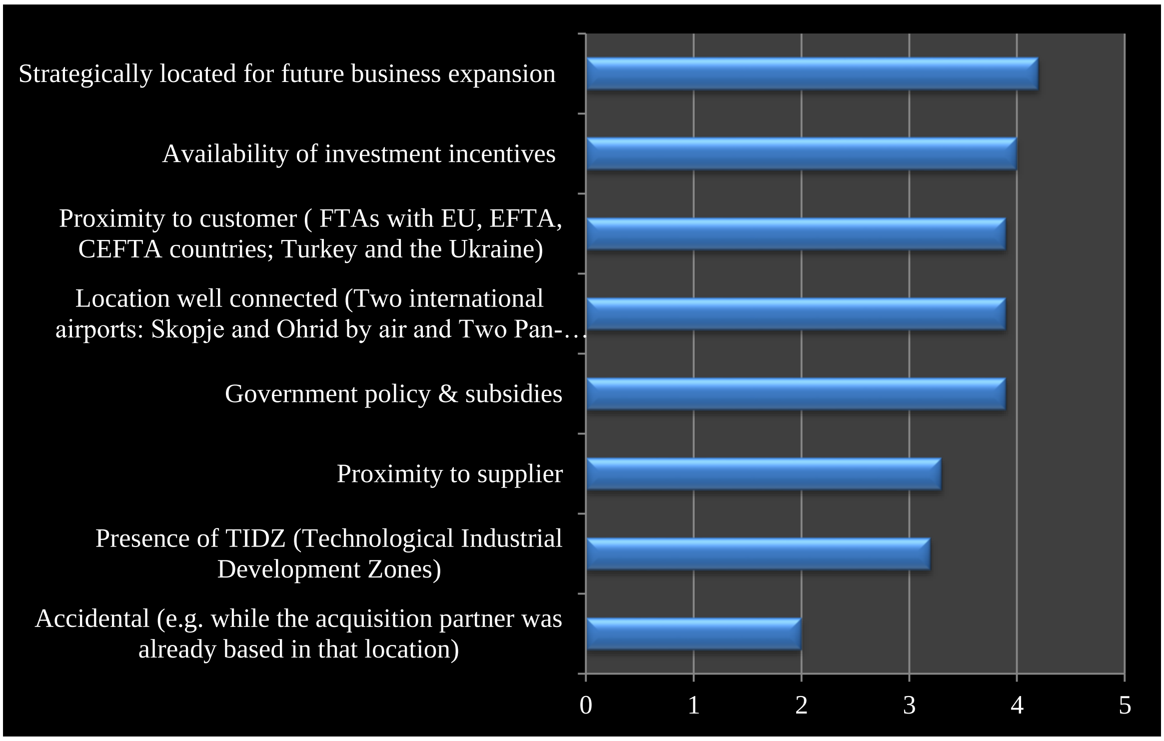
Considering the reasons for selecting Macedonia as FDI location within the Likert scale ranking, a degree of influence of 1-no influences up to 6-high influence, the average results collected from the responding companies are represented in figure 8.

Here two most influential factors for the selection of Macedonia as FDI location are: **strategically located for future business expansion and availability of investment incentives**. Thus, according to the expectations of the surveyed, several points should be highlighted: Macedonia is a major transport hub in the Southern Balkans with the features that include its strategic location as the gateway for Central and Eastern European countries. Furthermore, as a country with its strategic geographical position is at the crossroads of Two Pan-European corridors (East-West Corridor 8 and North-South Corridor 10 by land) and two international airports: Skopje and Ohrid which make it an ideal transit and distribution centre for products for European markets. Also, through three multilateral agreements (FTAs with EU, EFTA and CEFTA) and two bilateral Free Trade agreements with Turkey and Ukraine, Macedonia enjoys duty free access to a market of over 650 million customers. With continuous investment in road and railway infrastructure in combination with the small area of the country enables access to every inhabited place in Macedonia in less than 3 hours (Invest in Macedonia n.d.).

In addition, not surprisingly, availability of **investment incentives and government policy and subsidies** are rated with the average high grade (figure 8) for choosing Macedonia as a foreign investment location. Macedonian legal and regulatory framework is generally favourable to foreign investors and provides numerous incentives to attract them. Investors benefit from a ten-year tax exemption and free access to public services. The country has made significant efforts to harmonize its legal framework with the criteria, standards and practices of the European Union (Santander Trade portal, n.d.).

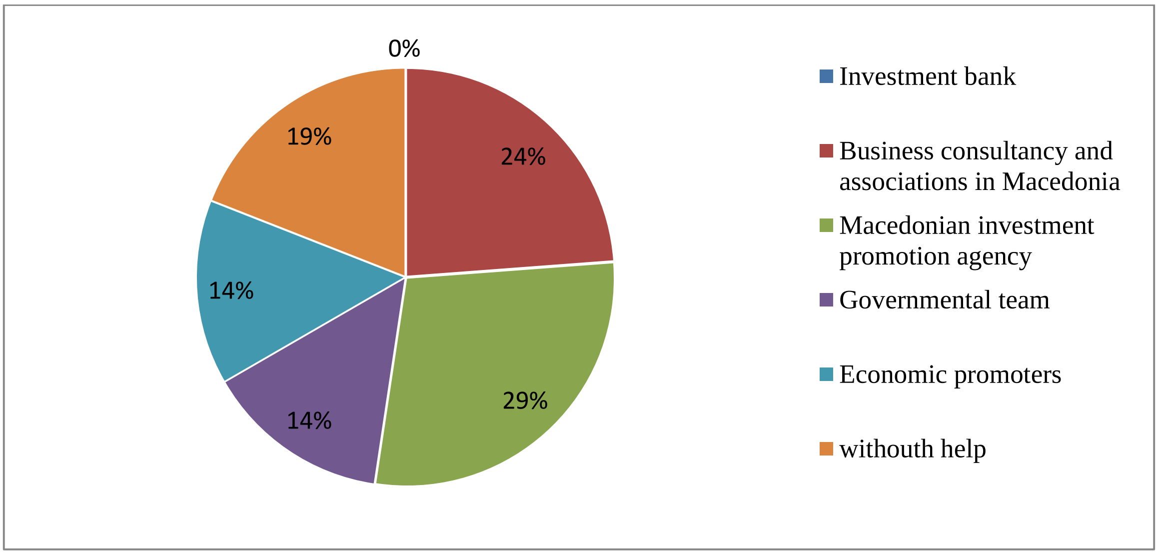
Not all of the responding companies are present in the Technological-industrial zones, so they don't regard the **presence of TIDZ** as an influential factor. Also, the factor with the lowest influence is the **accidental location selection** (e.g. while the acquisition partner has already been based on that location).

Figure 8. Average Ranking for Selecting Macedonia as FDI Location



The question from the questionnaire regarding to the help of any institutions or bodies in selecting partner and location in Macedonia is answered by the responding companies as figure 9 below represents.

Figure 9. Helpful Institutions/Bodies in Selecting Partner and Location in Macedonia



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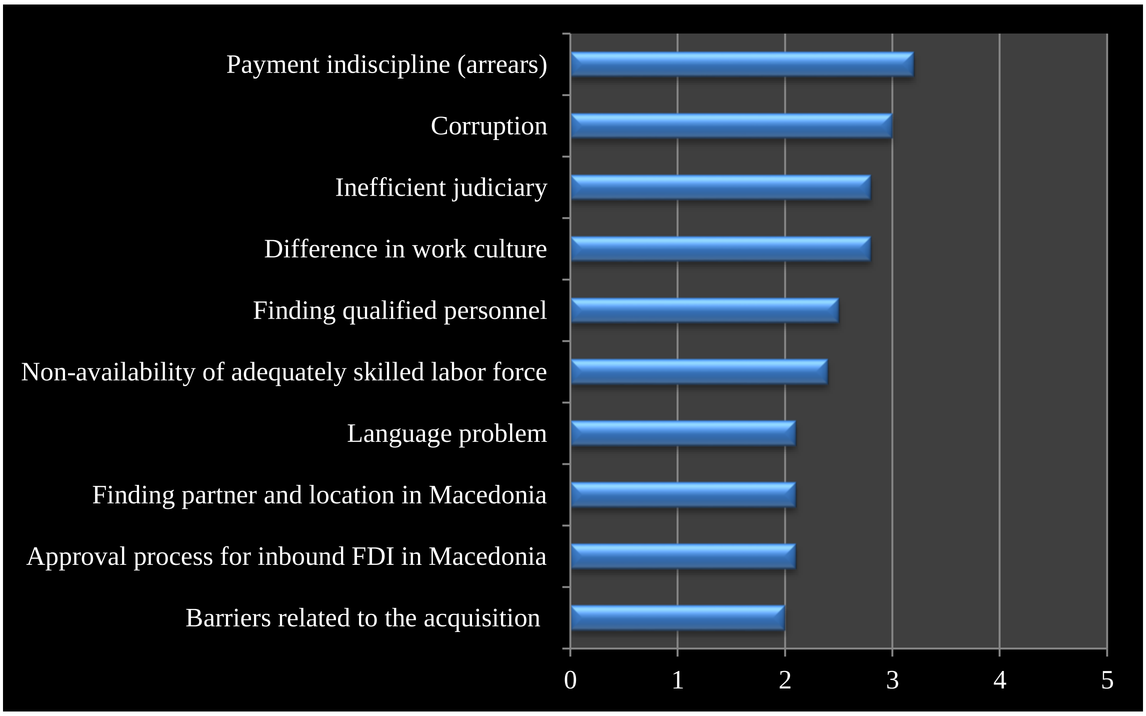
According the response of questionnaire respondent companies, Macedonian investment promotion agency and business consultancy and associations in Macedonia are the most helpful institutions for selecting partner and location in Macedonia as it is shown in the chapter above. The companies also receive help from the governmental team and economic promoters. This is a conclusive remark regarding the position of the governmental bodies and their work in gaining trust from the investor in order to implement a FDI in the country.

However, regarding the process of investment ventures in Republic of Macedonia, it is a great concern considering the challenge factors where many companies and investors are challenged in their work and the process of realizing the foreign direct investments (presented in next section).

Section 3. Problems / challenges that you face with respect to your investment in Macedonia

In this section of the questionnaire, respondent companies were answering about the challenge factors that cause or continue to cause problems within the foreign investment process and operation in Macedonia. Their answers are summarized (from 1-not at all problem up to 6-major problem) in the next figure 10:

Figure 10. Problems/Challenges of FDI Companies with Respect to the Investment in Macedonia



By looking at the average score, the problems that foreign investors are facing are not as significant for concerning, but still several remain. Thus, as larger problems the responding companies highlight and which can be categorized as policy and regulation related are: **payment indiscipline (arrears), corruption and inefficient judiciary.** These problems that have been existing since the country's independence and although a strong reforms have been done in order to improve the business environment, Macedonia still has got limitations and weaknesses that do not allow the economical entities to carry out smoothly their activities.

"And they do not pay to me. When they'll pay me – I will pay you! "
This is the motto that realistically demonstrates the mutual payments situation between the companies in Republic of Macedonia. This situation of late obligations payment causes a chain reaction and disruption liquidity of companies and in the economy in general. It is estimated that domestic debt as a result of the financial indiscipline over the years, measured by billions of Euros (Dimitrova, 2016, p.1).

In addition, corruption is also a large concern in the business sector and unfortunately according to Transparency international (2015), as very worrying is the marked deterioration in countries like Hungary, FYR of Macedonia, Spain and Turkey. These are places where there was once a hope for positive change. Now we're facing corruption growth, while civil society space and democracy shrink.

Also, the lack of efficient judicial system hinders the development of the country. According to Tasevski (2009), foreign investors avoid the country, the property protection blurs, and the citizens lose their faith in the system and thus are reluctant to take active role in the democratic debate.

Another group of challenging factors that cause minor problem in Macedonia are labour related: **difference in work culture** and some responses of the questionnaire are based on problems regarding **finding qualified personnel and non-availability of adequately skilled labour force.**

As it is shown in section 1, the motive for investment in Macedonia is still attractive because of the cheap labour pool and in order to avoid problems such as finding qualified and an adequately skilled labour force, the government has undertook several measures. Hence, according to Mizo (2016) in Macedonia, when MNEs are taken into consideration, finding appropriate skilled employees together with the most appropriate investment location pursues along with the governmental cooperation, (taking into consideration whether previously existed the same or similar labour-intensive industry for textile, leather or footwear industry etc.). Also, to overcome the problem of finding qualified workforce and to avoid major labour overlap in the same investment zones, dispersed industrial areas for investment are settled in Macedonia, in different cities with different sizes.

In addition, as more labour-intensive industries enter the country, the government policies regarding high education ought to focus on quality rather than quantity. Although, the Government made reforms with a goal of making the STEM (Science, technology, engineering, math) study fields more desirable, which are mostly needed in the companies from TIRZ, there is still a deficit of an adequately skilled labour force.

Section 4. Your future FDI plans in Macedonia

Questions from a questionnaire:
Is there an improvement of the general business climate in Macedonia after the period of your initial investment?
What would be the extent of your investment activity in Macedonia in the future compared to the plans which you had when you entered Macedonia?

Concerning economic parameters and future plans, half of the responding companies demonstrate that there is an improvement of the general business climate in Macedonia after the period of their initial investment, another half of the responding companies is with a negative answer (table 10). Also, what worries is the figure that 27 percent of the responding companies display lower expectations for future investment (table 11).

To sum up, solving the above mentioned problems would result in substantial improvements in Macedonia which would make the Macedonian business environment more stable, increase the inflow of FDI and ensure sustainable country development. Most important is that it would allow the foreign companies, which have already entered the Macedonian market, to upgrade their functions by extending their investment activity and to consider about diversification of the existent production portfolio. Also, by overcoming these problems, foreign companies that have entered Macedonia would be even more engaged in backward and forward linkages with domestic market players which is another worrisome issue related to governmental incentives.

Table 10. Responses to the Improvements to the General Business Climate

Improvements to the general business climate	**Number of responses**
Yes	7
No	7
Without answer	1

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Table 11. Extend of Investment Activity

Extent of investment activity	Number of responses
Higher	5
In line with the expectations at entry	6
Lower	4

Section 5. Importance of individual governmental incentives for your investment in Macedonia

In this part of the questionnaire the emphasize is placed on the package of incentives that our country provides for realization of foreign investments presented through the low and flat taxes and benefits in the technological – industrial development zones (figure 11). Not surprisingly, all the incentives offered by the government have positive consequences and high importance for MNEs considering the country as an investment destination.

Conforming to the responses in the questionnaire, the initiative that most of the participants point out with major importance is the **100 % reduction of personal income tax for 10 years.** Personal income tax on employees' salaries in Macedonia since 2008 is 10%; however, from the day of starting the business activities in the industrial zone, foreign investors are exempt from it. With the same importance is also **a 10-year corporate income tax exemption,** with the average score of 5.1 shown in figure 11. Foreign investors are entitled for reduction in the profit tax base by the amount of prior profit reinvested in tangible assets (such as real estate, facilities and equipment) and intangible assets (such as computer software and patterns) for period of 10 years used for expanding the business activities of the entity.
Slightly, but almost insignificantly less important incentives for the responding companies are the **reducing of labour market barriers** (easer dismissal from employment, faster procedures), **fast procedures for business activity registration and reduction of the costs for setting up and reduction of value added tax and customs duties for goods, raw materials, equipment and machines** (figure 11).

Here I would like to highlight that as a very important governmental incentive is the so called ready and built infrastructure, meaning that is the thing for one foreign company to decide to enter the country, DTIDZ as an institution deals with all the necessary construction and occupancy permits for the entire investment process. Also, the Directorate issues work permits for non-residents who come to work in the management team, brings about further contacts with the Customs Administration and the Public Revenue Office, i.e. for all the MNEs requirements there is one institution that is involved in the whole bureaucratic procedure.

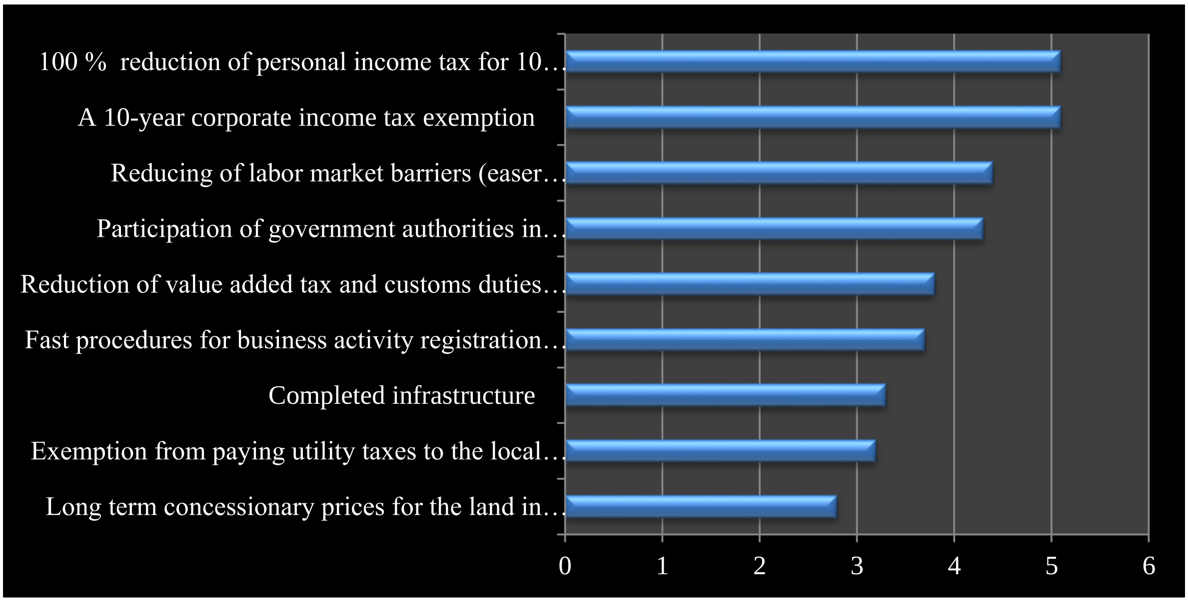
The Government pays special attention to production activities, activities from the IT area (software development, hardware assembling, digital recording, computer chips and the like), scientific research activity and new technologies with high environmental standards, for which additional benefits are envisaged in the TIDZs. Investors in TIDZs who operate in these areas are exempt from the liability for submission of a guarantee as collateral for any customs arrears (Invest in Macedonia, n.d.).

Another initiative that is outlines as important for the respondents in the questionnaire is the **participation of government authorities in construction costs in TIDZ up to 500000 *EUR*.** This initiative is also favourable incentive and denotes potential grant administered by the state based on the value of the investment or the number of jobs created by foreign investor. Also, TIDZ users have significantly lower rent areas of the parcels (3, 1, MKD/m2).

Less but not insignificant is the initiative **Completed infrastructure,** that enables free connection to electrical energy, natural gas, water supply, sewage and accesses to the main international road network. Investors are also exempt from paying a fee for preparation of the construction site (invest in Macedonia, n.d.).

Next initiatives with less importance in relation with the responding companies are the **exemption from paying utility taxes to the local municipality and fees for land building permits in TIDZ** and **long term concessionary prices for the land in TIDZs up to 99 years.**

Figure 11. Average Importance of Individual Governmental Incentives for Investment in Macedonia



Here are some recommendations from the participants; improvement of some initiatives, improvement of infrastructure, uncertain political environment, improving work culture…

The corruption has to be solved to establish equal positions for all companies on the market not only the companies close to the government...

Finish the started construction of the roads between all main cities in Macedonia as soon as possible for better and faster transportation of the goods...

Changing the import laws for the companies which do not sell on the Macedonian market. Those companies that are recognized as companies which have no influence on the Macedonian market and such as that, non-usual importing laws should be implemented for them. Some exclusion must be made…

Fair competition, luck on long terms, political and economic stability…

Improving the legal and regulatory environment…

CONCLUSION

This study is aimed to identify the main host governmental incentives for attracting FDIs in Macedonia. The main idea for this study has come out as a result of a large effort of the current government, in order to intensify the employment and economic growth of the country and to make a sophisticated way of presenting and promoting Republic of Macedonia to foreign investors. Consequently, in the last decade, in Macedonia an unavoidable topic of many debates on all levels of society is the subject of foreign investment. In addition, in the light of the academic literature reviewed above, the main motives driven by foreign investment and that on the basis of their characteristics enable profitable business abroad in relation to their own country are: market-seeking - FDI expansion into new markets, resource-seeking - FDI access to resources, efficiency-seeking - FDI improving operational efficiency and strategic asset seeking FDI- strategic investment.

On the other hand, the key FDIs determinants are consisted of market size variables, labour market conditions such as costs and productivity, infrastructure, openness to international trade and access to international markets, as well as institutional measures and incentives provided by the host government in order of realization of attracting FDI inflow. With the goal to raise employment, export, increased tax revenue or the prospect that some of the knowledge brought by foreign companies may spill over to the domestic ones, the host governments provide investment incentives which are typically arranged in three extensive categories: fiscal incentives such as tax holidays and reduced tax rates, financial incentives

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related to such as grants and loans at concessionary rates, and other incentives including subsidized infrastructure or services, preferential government contracts, special treatment to foreign exchange etc.

The main priority of Republic of Macedonia is the maintenance of the macroeconomic stability and gradually increasing economic growth and like the other European transitional economies it constantly makes efforts to attract most of the foreign capital through foreign direct investment. Drastic reforms have been undertaken concerning the business climate after 2006, tax system has undergone significant reforms to be more consumption oriented by introduction of the 10% flat tax as well as key reforms to improve various attractive features to foreign investors, protection of the property rights improving the performance and functioning of the legislative and more efficient administration.

As a consequence, some large foreign companies started implementing their investment projects throughout the territory of Macedonia by opening factories in the free industrial economic zones, TIRZ. Hence, the larger Greenfield investments in Macedonia has begun with the construction of Johnson Controls, the British Johnson Matthey (2010), American Kemet Electronics, Kromberg& Schubert, Italian Techno Hose, Russian oil company Lukoil, Turkish TAV, Sutas and others. At the moment 23 foreign companies operate in the Technological Industrial Development Zones throughout the territory of Macedonia, employing 6100 employees. As a result, investments have gradually branched out of the traditional sectors such as food and metal processing into technology-intensive industries, in particular automotive components for which major global players have become Macedonian main exporters. The overall picture of Macedonian regional structure confirms the dominance of the EU countries as major foreign investors.

The goal of this master thesis is to identify whether a series incentives in various forms, tax and customs exemptions and incentives, direct state aid for the construction of facilities, support in the area of salaries and other benefits, make Macedonia competitive investment destination in the region. This research imposes separate positive and negative conclusions.

In order to increase the volume of foreign direct investment and foster technological development of Macedonia, 14 Technological Industrial Development Zones (until the end of 2016, the government plans to build 3 more technological development zones) as well as municipal industrial zones are opened within the country. In the future, the Government plans to open and develop health zones, IT zones and tourist areas. The overall policy of creating a greater number of zones has got an aim for greater opportunity of dispersion and diversification of the investments for greater regional development and economic dynamics of the smaller and underdeveloped areas in Macedonia. According to the valuation of ZMAI (2015), that in 2015 organized a telephone survey with a representative sample of 1,118 respondents, 56% of respondents believe that the effect of the foreign investment in the Macedonian economy is positive.

Among the most prominent motive for investing in Macedonia in the above questionnaire survey is the cheap skilled and labour pool, as it is the continued increase of employing people by foreign companies. According Mizo (2016), the implementation of recent projects of foreign companies is expected to reach 16,000 employees, which is a significant figure consistent with country population. Additional positive benefit that I would like to highlight is the transfer of knowledge, skills and expertise (knowhow), acquiring practices and applications of advanced western standards of production and management, thus helping to create mobile labour force that would overcome what the participants pointed out as a challenging factor that caused problem in the investment process - finding qualified personnel. The largest number of Greenfield or Brownfield investors, currently in the country, is the automotive industry, the established labour-intensive companies with production of various segments. Macedonia represents a potential opportunity in this industry and with the good geographic location and infrastructural connection, the country meets the requirements in the major markets in Europe and the manufactured goods can be reached in less than 3 days. However, most of the respondents highlight some business barriers in the investment and operation process like payment indiscipline (arrears), corruption and inefficient judiciary. Thus, although the government through the so-called ready and built infrastructure makes efforts to overcome the inefficient bureaucracy, curt regulatory and efficiency here is crucial.

In addition, a negative finding of this research is a small number of cooperation with the domestic companies. Foreign companies in Macedonia exploit local assets / local market, and thus improve their own static positions without engaging in too many backward and forward linkages with the domestic companies. Here, the government should encourage links between the foreign and the local companies, a larger number of domestic companies should meet some of the needs and demands of foreign investors by certification of additional quality certificates, lowering the product prices, meeting default delivery times etc.

Whether a government in the field of attracting investments would succeed, it is fair to have estimation based on the long-term results as the process of improving the business environment and then promoting the country and bringing decision by the investors is extensive. Macedonia, at the beginning of last decade devoted considerable time for state branding in order to create an image of openness for the foreign investment. Nowadays, the perception about doing business in the country is different; doing business and some related business activities in Macedonia are similar or on the same level of competitiveness as in Western Europe or North America, Mizo (2016).

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APPENDICES

LIST OF APPENDICES

Appendix A: List of Abbreviations

CEE - Central and Eastern Europe
DTIDZ-Directorate for technological industrial development zone
FDI- Foreign direct investment
FTZ – Free trade zones
IMF - International Monetary Fund
MAI - Multilateral agreement on investment
MNC-Multinational Company
NBRM-National Bank of the Republic of Macedonia
ODI -Outward Direct Investment
OECD - Organization for Economic Co-operation and Development
PTA - Preferential trade agreements
R&D – Research and development
SEE- Southeast Europe
SEEC - South East European countries
TIDZ-Technological industrial development zone
TNC-Transnational Company
WTO – World trade organization

Appendix B: Questionnaire for the Survey

Questionnaire

The following questionnaire is prepared by the candidate Gordana Smilevska, as a student of the accredited Consortium Master Studies of the Faculty of Economics at the University of Ljubljana in the Republic of Macedonia.
In this questionnaire, based survey for master thesis regarding the FDI in Macedonia, with title: Host governmental incentives for attracting FDIs: the case of Macedonia, I have prepared questions for your assessment.
Therefore, I kindly request you to participate in this survey by answering these questions. It will take about 20 minutes to complete the questionnaire. All answers will be held strictly confidential and anonymous and your contact information will not be traceable to the answers.
There will be no reference by any means to the person who is answering the questionnaire. Upon your request, you will be provided a summary of the key findings for the case study.

Methodology and Goals of the Survey

The survey has got five chapters, including the first part of questions which identify the general information about the company.
In the second part it provides questions to access the factors that influence the organizational motives for investment decision.
The third set of questions refers to location selection; the forth part is related to the challenging factors that may cause a problem in the investment process.
Finally, the fifth part is set of questions for the economic parameters in Macedonia and the future plans for investment decisions.

Please return the completed questionnaire within two months period and for some further information my address is:
GordanaSmilevska,
PodravkasKomerc
Ul.Voindraskovic 5b
smilevska.g@gmail.com
tel: +38970225356
Skopje

QUESTIONNAIRE FOR FOREIGN OWNED ENTERPRISES IN MACEDONIA year 2015

This questionnaire is prepared for foreign owned companies doing business in Macedonia. All data required will be treated confidentially.

1. General information about your firm in Macedonia

1.1. Name of the company:

____

1.2. Address and registered office of the company:

____

1.3 Investor's (foreign parent company's) home country:

1.4 Equity share of foreign investor in the company: _______%

1.5 Main activity:

____

1.6 What are the most important products / services in your company?

____

1.7 Entry mode of foreign investor:

- Acquisition of existing company
- Joint Ventures / M & A
- Greenfield investment
- Privatization process in Macedonia
- Representative Office / Branch
- Other, please define: ____

1.8 Year of first entry in Macedonia: I__I__I__I__I year

2. **Motives for investment**
   2.1. To what degree did the following factors influence your **decision to invest in Macedonia**

	MOTIVES	1 = not at all……..….6 = highly relevant
1	Access to or increasing of existing market share in Macedonia	□1 □2 □3 □4 □5□6
2	Access to SE European markets.	□1 □2 □3 □4 □5□6
3	Access to EU markets	□1 □2 □3 □4 □5□6
4	Access to low-costs inputs factors(material, components, parts)	□1 □2 □3 □4 □5□6
5	Availability of low-costs input factors	□1 □2 □3 □4 □5□6
6	Develop products/services for Macedonian market	□1 □2 □3 □4 □5□6
7	Develop products/services for global market	□1 □2 □3 □4 □5□6
8	Diversify the existing product portfolio	□1 □2 □3 □4 □5□6
9	Access to knowledge, skilled labour, technology in Macedonia	□1 □2 □3 □4 □5□6
10	Quality labour force	□1 □2 □3 □4 □5□6
11	Low labour costs	□1 □2 □3 □4 □5□6
12	Reducing transaction costs (e.g. import tariffs)	□1 □2 □3 □4 □5□6
13	Tax benefits	□1 □2 □3 □4 □5□6
14	Following of important clients operating in Macedonia	□1 □2 □3 □4 □5□6
15	Good geographic location and infrastructural connection	□1 □2 □3 □4 □5□6
17	Other, please describe: ______________________________	

3. **Selection of the location within Macedonia**

3.1. To what extent did the following factors influence **your decision about the location of the investment within Macedonia**?

	Location selection	1 =no influence……….6 =high influence
1	Accidental*(e.g. while the acquisition partner has already been based in that location)*	□1 □2 □3 □4 □5 □6
2	Availability of investment incentives	□1 □2 □3 □4 □5 □6
3	Government policy & subsidies	□1 □2 □3 □4 □5 □6
4	Presence of TIDZ (Technological Industrial Development Zones)	□1 □2 □3 □4 □5 □6
5	Location well connected (Two international airports: Skopje and Ohrid **by air** and Two Pan-European corridors: East-West Corridor 8 and North-South Corridor 10 **by land**)	□1 □2 □3 □4 □5 □6
6	Proximity to supplier	□1 □2 □3 □4 □5 □6
7	Proximity to customer (FTAs with EU, EFTA, CEFTA countries; Turkey and the Ukraine)	□1 □2 □3 □4 □5 □6
8	Strategically located for future business	□1 □2 □3 □4 □5 □6
9	Other*(please specify)*	
10	Do you have any specific comments about your location decision? ………………………………………………………………………………… ………………………………………………………………………………… …………………………………………………………………………………	

3.2. Did you take help of any the following institutions/bodies in selecting partner and location in Macedonia?*(Multiple answers possible)*

- Investment bank
- Business consultancy and associations in Macedonia
- Macedonian investment promotion agency
- Governmental team
- Economic promoters
- Others *(please specify)* ……………………………………………………………………………………
…

4. Challenges

4.1 To what extend did the **following challenging factors** cause (or continue to cause)a problem for you in the investment process and operation **in Macedonia**

	Challenge factors	**1=not at all……6=major problem**
a.	Approval process for in bound FD in Macedonia	□1 □2 □3 □4 □5□6
b.	Finding partner and location in Macedonia	□1 □2 □3 □4 □5□6
d.	Language problem	□1 □2 □3 □4 □5□6
e.	Finding qualified personnel	□1 □2 □3 □4 □5□6
f.	Barriers related to the acquisition of land and	□1 □2 □3 □4 □5□6
g.	Non-availability of adequately skilled labour force	□1 □2 □3 □4 □5□6
h.	Difference in working culture	□1 □2 □3 □4 □5□6
i.	Payment indiscipline (arrears)	□1 □2 □3 □4 □5□6
j.	Inefficient judiciary	□1 □2 □3 □4 □5□6
k.	Corruption	□1 □2 □3 □4 □5□6
m.	Other(please specify)	
Do you like to specify any other challenges that you face or faced in Macedonia?		

5. Economic parameters and future plans

5.1. Is there **<u>an improvement</u>** to the general business climate in Macedonia after the period of your initial investment?

Yes No

5.2. What would be the <u>**extent of your investment activity** in Macedonia in the future</u> compared to the plans which you had at the entry in Macedonia?

- In line with the expectations at entry
- Higher
- Lower

5.3. Please, assess **<u>the importance</u>** of the following Governmental incentives <u>for investment in Macedonia</u>. (only for companies that invest in TIDZ)

	Incentives for foreign investment	**1=not at all…… 6=major importance**
1	A 10-year corporate income tax exemption	☐1 ☐2 ☐3 ☐4 ☐5☐6
2	100 % reduction of personal income tax for 10 years	☐1 ☐2 ☐3 ☐4 ☐5☐6
3	Reduction of value added tax and customs duties for goods, raw materials, equipment and machines	☐1 ☐2 ☐3 ☐4 ☐5☐6
4	Reducing of labour market barriers (easer dismissal from employment, faster procedures.)	☐1 ☐2 ☐3 ☐4 ☐5☐6
5	Fast procedures for business activity registration and reduction of the costs for setting up	☐1 ☐2 ☐3 ☐4 ☐5☐6
6	Long term concessionary prices for the land in the TIDZs up to 99 years	☐1 ☐2 ☐3 ☐4 ☐5☐6
7	Exemption from paying utility taxes to the local municipality and fees for land building permits in TIDZ	☐1 ☐2 ☐3 ☐4 ☐5☐6
8	Completed infrastructure that enables free connection to natural gas, water, electricity and access to a main international road network.	☐1 ☐2 ☐3 ☐4 ☐5☐6
9	Participation of government authorities in construction costs in TIDZ up to 500000 EUR	☐1 ☐2 ☐3 ☐4 ☐5☐6
10	Other, please describe: ______________________________	☐1 ☐2 ☐3 ☐4 ☐5☐6

5.4. Please, indicate your recommendations for improvement of the business climate in Macedonia and removing barriers which you encounter.

1. ____
____
______

2. ____
____
______

3. ____
____
____

4. ____
____
____

5. ____
____
____

THANK YOU FOR YOUR COOPERATION!

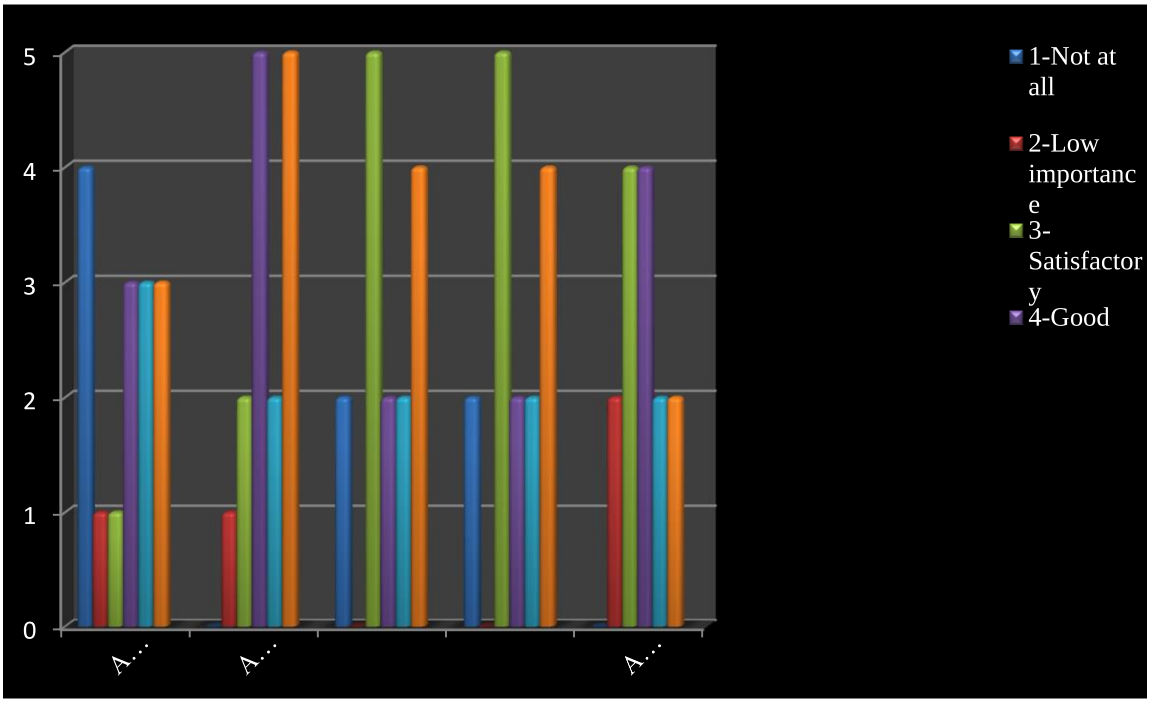
Company name: ____

E-mail address: ____

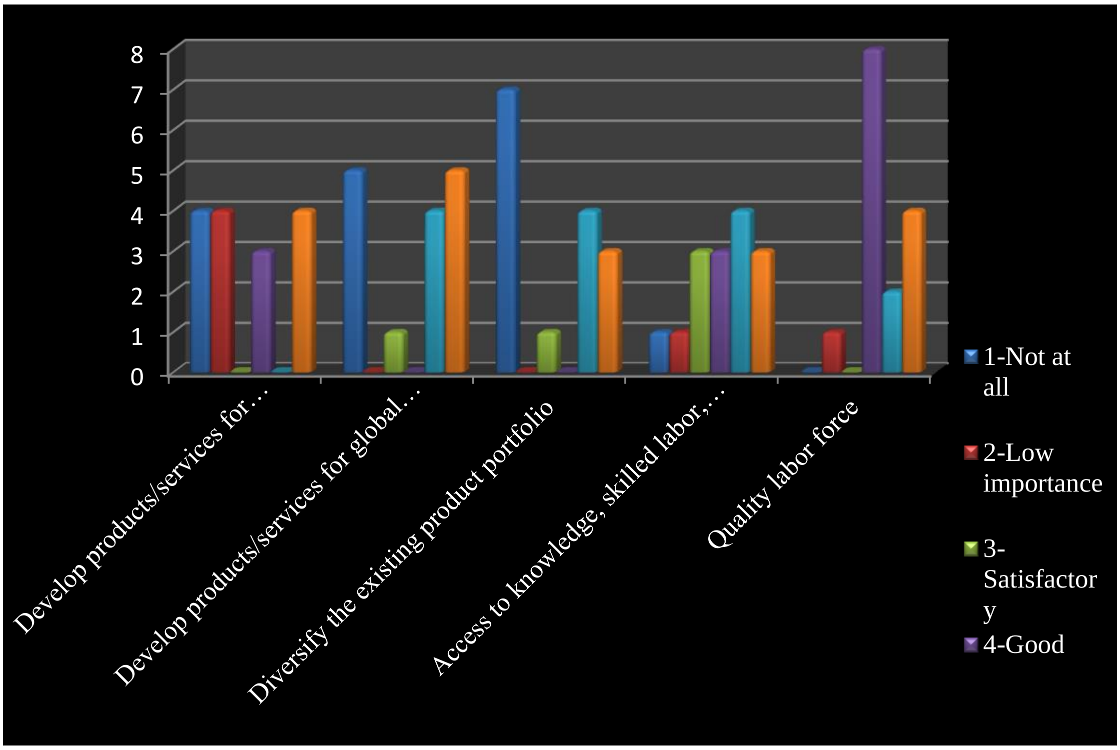
Date: ___________________

Appendix C: Results from the Survey

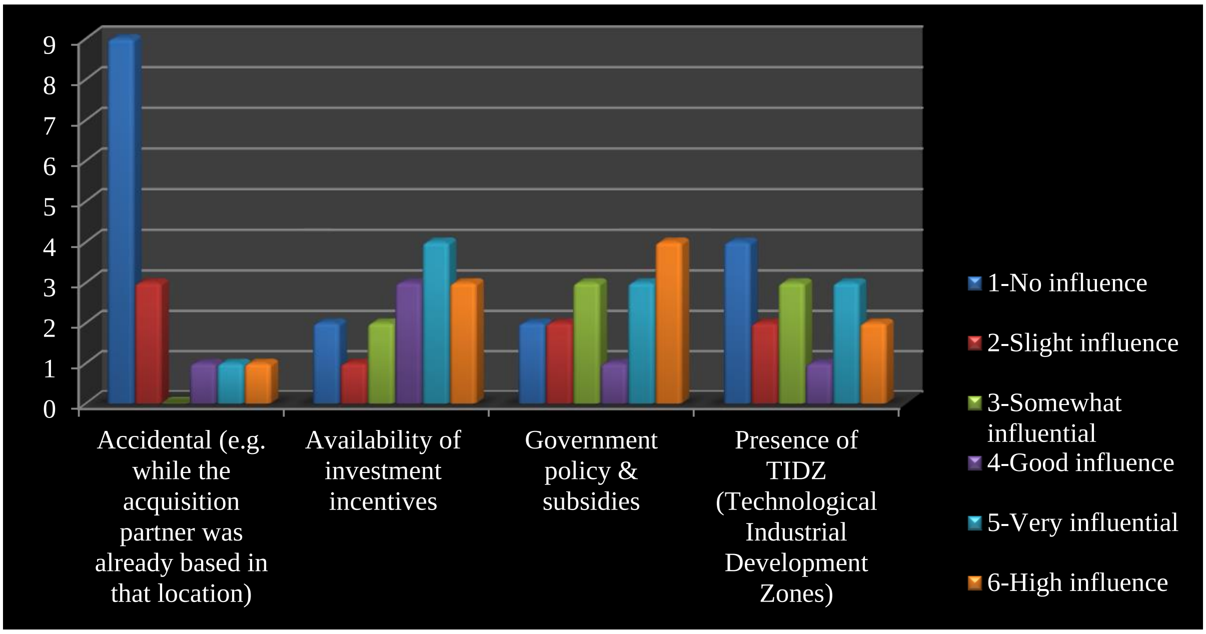
Motives for investment



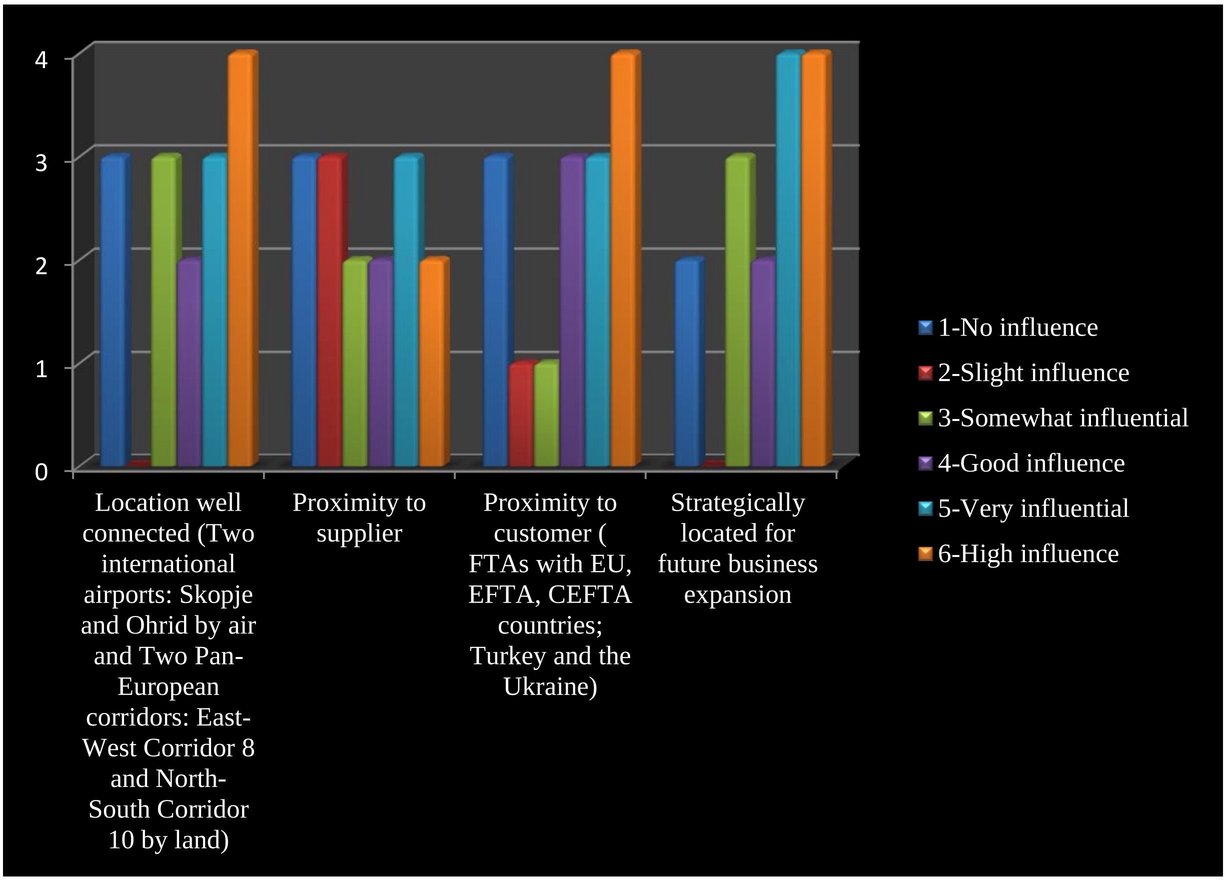
Motives for investment



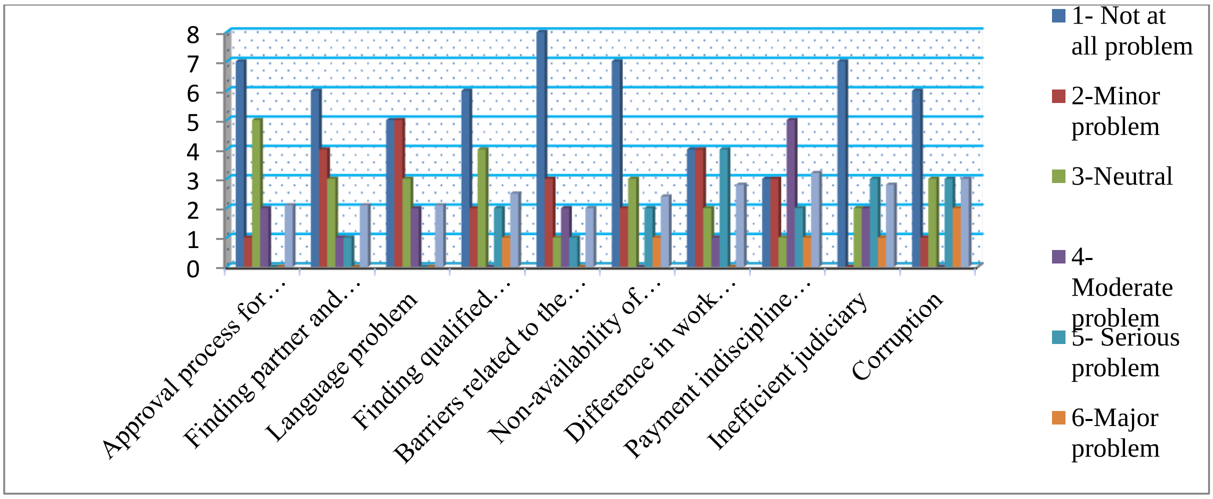
Motives for investment



Selection of the location within Macedonia



Challenging factors cause (or continue to cause) a problem in the investment process and operation in Macedonia



Governmental incentives for investment in Macedonia