

Evolution of the Economic Order in the Western Balkans: Foreign direct investment as the engine of (under)development

By
Jelena Šapić

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Supervisor: Professor Friedrich Kratochwil

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Abstract

This thesis aims to explore the evolution of the economic order in the Western Balkans in period from 2000 to 2013. It does so by looking closer at foreign direct investment (FDI) from a non-econometric and non-positivist perspective. Furthermore, this thesis examines the interplay between political, legal, and economic forces in shaping an economic order. In particular, I argue that actors' practices created the notion of FDI as an ultimate panacea for the economic underdevelopment promoting FDI as the only viable solution to the economic underdevelopment. During the time FDI spilled over from the economic to the political sphere turning into an obstacle to economic reforms. By assessing FDI rationalities in these ways, the thesis will disclose paradox of the regional approach to the FDI – by attempting to catch up, the Western Balkans found itself in a deadlock of (under)development. It aims to make a starting point in bringing the Western Balkans transformation in growing literature on outcomes of the economic transformation as well as to provide viable alternatives to FDI-led model of development.

Key words: economic transformation, the Western Balkans, FDI-led model of development

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Introduction

Ever since the onset of the global economic crisis in 2008, the economic transformation of the Western Balkans¹ has attracted attention of decision makers. The ongoing economic crisis has ushered in new-old concerns about the security and the stability of the region. This is reflected in high unemployment rates, mounting public debt, and sluggish economic growth.² Furthermore, the 2013 Enlargement Strategy, issued by the European Commission, warns that none of the Western Balkans economies is a functioning market economy yet.³ For the first time, the Enlargement Strategy underlined good economic governance as a basic accession requirement. Although it has been a part of the Copenhagen criteria, the novelty here is a shift from political towards economic set of requirements. Economic set of requirements presupposes developed functions to preserve market order which are yet not fully developed in the Western Balkans.⁴ The Western Balkans economies started introducing market-oriented reforms through a process of transformation.

But, the Western Balkans economic transformation has not been explored to the same extent as the transformation of the East Central European countries.⁵ When liberal democracy and market-based economies became the only games in town in the former socialist bloc twenty

¹ The Western Balkans initially consisted of the following countries: Albania, Bosnia and Herzegovina, Croatia, Macedonia, Kosovo*, Montenegro, and Serbia. Croatia joined the European Union on July 1, 2013. However, the thesis framework covers the period from 2000 to 2013, which means that Croatia will be included within observed group of the Western Balkans countries.

² Dušan Reljić, “Političko proširenje EU na Zapadni Balkan: Mučnava vremena za teške kandidate“ [EU’s Political Enlargement in the Western Balkans: Difficult Times for Complex Candidates], in Ronja Kempin and Marco Overhaus (eds.), *EU-Außenpolitik in Zeiten der Finanz- und Schlenkenkrise*, SWP S9 (April 2013).

³ European Commission, *Communication from the Commission to the European Parliament and the Council: Enlargement Strategy and Main Challenges 2013-2014* (Brussels: October 16, 2013), 2.

⁴ Those are capacities to create transparent and predictable policy environment, prevent rent-seeking behavior, and enforce symmetric market informational power. László Bruzst, “Market Making as State Making: Constitutions and Economic Development in Post-communist Eastern Europe”, *Constitutional Political Economy*, 13 (2002), 53-54.

⁵ For instance one of the most quoted article on so-called “transition” economies left the countries of the former Yugoslavia out of its analysis due to the wars. Jan Svejnar, “Transition Economies: Performance and Challenges”, *Journal of Economic Perspectives*, vol. 16, No. 1 (Winter 2002): 3-28.

five years ago,⁶ the countries of the Western Balkans were involved in the Yugoslav wars or faced an insurgency during the 1990s.⁷ This return to the state of nature led to the deferment of reforms; the postponement was consequently denominated as a “blocked transformation.”⁸ When the conflicts were finally settled the transformation was “unblocked” – regional governments, including an interim international civil administration in Kosovo, started intensively to introduce reforms oriented toward a democratic and free market system.

Being laggards in catching-up,⁹ regional governments tended to introduce reforms and policies which would provide fast recovery. One of the policies commonly applied across the region for this purpose has been the policy of attracting foreign direct investment (FDI). In a general context of transformation, FDI represents a way of economic internationalization providing a transfer of a newer technology and know-how requiring at the same time deeper structural changes of economies. In the context of the Western Balkans, FDI represented a patchy economic activity before the transformation. In Yugoslavia, a foreign investment in enterprises was authorized in 1967, while in Albania a foreign penetration of the economy was disallowed due to the country’s self-imposed isolationism.¹⁰

⁶ This is the reformulation of famous sentence by Guiseppe di Palma who originally stated that “democracy became the only game in town.” Guiseppe di Palma, *To craft democracies: an essay on democratic transitions*, (Berkeley: University of California Press, 1990). It is however often wrongly attributed to Juan J. Linz and Alfred Stepan who borrowed it in their book on the transition and consolidation of democracy. Juan J. Linz and Alfred Stepan, *Problems of democratic transition and consolidation: Southern Europe, South America, and Post-Communist Europe* (Baltimore: Johns Hopkins University Press, 1996).

⁷ During the 1990s, Albania faced a refugee crisis. Furthermore it had been at a conflict outbreak in 1997 when pyramid schemes collapsed making “half of all Albanian families lost some money and over a third lost most of their savings.” Robert Bideleux and Ian Jeffries, *The Balkans: A post-communist history* (New York: Routledge, 2007), 54.

⁸ The term “blocked transformation” is coined by Serbian sociologist Mladen Lazić as quoted in Filip Balunović, *Serbia on the European Periphery: A blurred reality of post socialism* (Nice: Lambert Academic Publishing, 2013), 16-17.

⁹ Catching up as a phrase frequently used in the literature on the transformation refers to a tacit competition in conducting democratic and market-based reforms.

¹⁰ Miodrag Sukijasovic, “Legal Aspects of Foreign Investment in Yugoslavia”, *Law and Contemporary Problems*, Vol. 37, No. 3 (Summer 1972), 474-484; Mamica Nene, “Foreign direct investment in Albania. A study on investors motivation”, *European Scientific Journal* (June, 2010), 40.

Despite the official efforts, the FDI inflows have been lower than expected. Political instability attributed to the former wars,¹¹ distance from major economies,¹² delayed and inefficient reforms¹³ are all stressed in empirical studies as the major reasons for lower FDI influx compared to Central and Eastern Europe. Another recent research disclosed the impact of the Balkans image upon foreign investors' restraints.¹⁴ Regardless of low inflows, FDI has continued to be discerned as an engine of economic development among the Western Balkans countries. This continuity and possible alternatives to the FDI-led model of development has not been investigated and comprehensively epitomized in previous work. Going beyond the econometrics studies concerned with the FDI influxes in the Western Balkans economies, this thesis explores the evolution of the economic (under)development in the period between 2000 and 2013 by looking at the interplay between political, legal, and economic forces.

In particular, I argue that actors' practices created the notion of FDI as an ultimate panacea for the economic underdevelopment. As illustrated in the case study of the Western Balkans, these cross-national practices were shaped by various political restraints such as cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY), anticorruption campaign, or the escalation of ethnic violence. These restraints created a perception of socially costly reforms in which FDI was promoted as the only viable solution to the economic underdevelopment. As a result, FDI spilled over from the economic to the political

¹¹Gábor Hunya, FDI in South-Eastern Europe in the early 2000s, a study commissioned by the Austrian Ministry of Economy and Labour, The Vienna Institute for international Economic Studies (July 2012); Gábor Hunya, *Recent FDI trends, policies and challenges in SEE countries in comparison with other regions in transition*, a study produced for the conference Foreign Direct Investment in South East Europe: Implementing Best Policy Practices, The Vienna Institute for International Economic Studies (November 2000); Laza Kekić, "Foreign direct investment in the Balkans: recent trends and prospects", *Journal of Southeast European and Black Sea Studies* Vol. 5, No. 2 (May, 2005), 171-190.

¹² Saul Estrin and Milica Uvalic, "Foreign Direct Investments into Transition Economies: Are the Balkans different?", *Economics of Transition*, Vol. 22, No. 2 (2014), 281-312.

¹³Josef Brada *et al.*, "The effects of transition and politics of instability on FDI flows in Central Europe and the Balkans". *Economics of Transition*, vol. 14, No. 4 (2006), 649-68; Gábor Hunya, *FDI in South-Eastern Europe in the early 2000s*, Demekas *et al.* "Foreign Direct Investment in Southeastern Europe:

¹⁴Estrin and Uvalic, "Foreign Direct Investments into Transition Economies", 300.

sphere turning into an obstacle to economic reforms. Specifically, the politicians crowned FDI as the key indicator of successful governance to mask their inability in tackling socio-economic issues (e.g. unemployment). In doing so, the politicians created shallow institutions to promote FDI and exports-oriented economy, and designed illusory policies with the same goal. Paradoxically these institutions and policies increased costs of accruing FDI while not significantly improving the level of economic development. The combination of actors' practices, institutions, and policies through creation of the FDI-led model of development shaped the economic order in the Western Balkans.

To demonstrate this argument, I critically reassess FDI to provide better understanding of current economic affairs in the Western Balkans. My aim is to contribute to future formulations of more realistic and better-targeted policies of the economic development. Likewise my hope is to bring up the Western Balkans in the ongoing debate on the results of undertaken economic transformation through a non-econometric study. I identified two gaps in the existing literature on the economic transformation. According to the 2005 review of existing empirical studies on FDI in the former European socialist countries Demekas *et al.* discovered that only four studies out of forty were related to the experience of the Southeastern European countries.¹⁵ Additionally they demonstrated that those four studies looked “patchy and inconsistent”¹⁶ in comparison with the studies on East Central Europe. Moreover, Estrin and Uvalić assert that studies on FDI in the

¹⁵Demekas *et al.* identified following four studies: E. Christie, “Foreign Direct Investment in Southeast Europe”, Vienna Institute for International Economic Studies, Working Paper No. 24 (2003); P. Garibaldi, N. Mora, R. Sahay, and J. Zettelmeyer, “What Moves Capital to Transition Economies,” IMF Working Paper 02/64 (Washington: International Monetary Fund, 2002); J.I. Deichmann, “Distribution of Foreign Direct Investment Among Transition Economies in Central and Eastern Europe,” *Post-Soviet Geography and Economics* Vol. 42 (2001), pp. 142–52.; D. Holland, and N. Pain, “The Diffusion of Innovations in Central and Eastern Europe: A Study of the Determinants and Impact of Foreign Direct Investment,” NIESR Discussion Paper No. 137 (London: National Institute for Economic and Social Research, 1998). Dimitri G. Demekas *et al.* “Foreign Direct Investment in Southeastern Europe: How (and how much) can policies help?”, IMF Working Paper 05/110 (2005), 4.

¹⁶Demeka *set al.*, “Foreign Direct Investment in Southeastern Europe”, 4.

Western Balkans in the period after 2000 should be conducted due to dated researches and a strong upsurge of FDI in the 2000s (compared with the 1990s).¹⁷

The thesis is structured as follows: in the first chapter, I introduce the main concepts of the topic such as evolution of the economic order, the Western Balkans, and foreign direct investments. It is crucial to clarify the concepts of social sciences since they do not exist “out there.” Perplexing in their nature, concepts embody a wide array of meanings, and that is why their subtext should be clearly stated at the beginning of every inquiry.

In the second chapter, I shift my focus to tracing of the evolutionary path of the economic order. I conduct an inquiry into three constitutive elements of an order – actors, institutions, and policies – striving to identify different constraints and opportunities for the economic development. I examine statements by the regional prime ministers,¹⁸ and the opposition,¹⁹ then development strategies, work of specific agencies, and policies related to the FDI incentives all which are available on the Internet. As a native Serbian speaker, I could read original texts produced in other Yugoslav republics with an exemption of Macedonia.²⁰ Instead of the original texts produced in Albania and Macedonia, I examine available texts in English given by the Albanian and Macedonian stakeholders which represents a sort of a thesis shortcoming.

In the third chapter, I will reconsider emerged economic order and FDI-led model of development. I will employ contextual factors such as domestic (im)balances and timing of the

¹⁷Estrin and Uvalic, “Foreign Direct Investments into Transition Economies”, 285.

¹⁸According to constitutional provisions Albania, Croatia, Macedonia, Kosovo, and Serbia are set up as parliamentary democracies. Montenegro is a parliamentary system with a president, while the political system in Bosnia and Herzegovina can be portrayed as a hybrid system with presidential, semi-presidential, and parliamentary elements. Marija Sahadžić, “Priroda političkog sistema u Bosni i Hercegovini” [Type of the political system in Bosnia and Herzegovina] in Saša Gavrić et al. (eds), *Uvod u politički sistem Bosne i Hercegovine – odabrani aspekti* [Introduction in the political system of Bosnia and Herzegovina – selected aspects], (Sarajevo: Konrad Adenauer Stiftung, 2009), 28.

¹⁹In democracies, a political opposition has a right to challenge those in power and their ways of conducting policies. Therefore the opposition is included as a unit of analysis within the thesis as domestic players whose activities within a formal framework contribute to the political and economic order (re)shaping. Stephan Haggard and Robert R. Kaufman, *The political economy of democratic transition* (Princeton: Princeton University Press, 1995), 13.

²⁰Official texts in Kosovo are available in Albanian, English, and Serbian.

regional inclusion in the international economic arena. By assessing FDI rationalities in these ways, the thesis will disclose paradox of the regional approach to the FDI – by attempting to catch up, the Western Balkans found itself in a deadlock of (under)development.

1. Concepts Inquiry

In this chapter I firstly consider two concepts: transition, and the Western Balkans. These two concepts are frequently used in the academic and political forums as designations of natural phenomena in the social world. Namely transition is perceived as a natural phenomenon that facilitates embodiment of ideal models of organization within societies. These models are liberal democracy and market-based economy which are as ideal models inherited to the human nature.²¹ By their very nature they should not be questioned. On the other side, the Western Balkans term is broadly used to cover a natural region located in South East Europe. The term subsumes small former socialist states emerging from the 1990s bloodsheds and seeking the EU membership. Although characteristics of the countries' cluster are obviously politically driven, the term operates as a geographically driven designation.

My aim here is, however, to demonstrate that phrases like transition and the Western Balkans are ambiguous and as such incorporate a normative. Under a normative I understand a set of embodied meanings which have not been always clearly spelled out in the academic and political forums. In order to do investigate these neglected meanings, I draw on a context-oriented approach which does not recognize any natural phenomena or objectivity in the social world. The context-oriented approach provides a chance to question knowledge on a final result (e.g. democracy and market) as well as to challenges a notion of natural regions (e.g. the Western Balkans).

Secondly I am concerned with the concept of foreign direct investment. Foreign direct investment has been largely discerned as a useful tool to enact changes in economies of the former socialist countries. FDI renders transnationalization of national economies, leading at the

²¹ Francis Fukuyama, *The End of History and the Last Man* (London: Penguin Books, 1992).

same time to an opening of economies and bringing new business cultures.²² Nevertheless, FDI is not a mere economic tool; it embraces a normative (in the same sense as described above). In contrast to the neoclassical economic belief that economy is a “pure” science abstracted from any other spheres,²³ studies on FDI descry that related policies are primarily concerned with political features (political stability, rule of law, anti-corruption enforcements, non-captive state, effective and sustainable reforms).²⁴ With this in mind, I dwell upon the same approach striving to explain the attached subtext to FDI from the perspective of economic development. The purpose of the first chapter is to introduce and clarify concepts which will be then applied in the second and third chapter.

1.1 The Transition Concept

Exploring abundant literature on transition, Dejan Jović, a Croatian scholar analyzes the origins of *transition*, and the turning points of its understanding among political scientists.²⁵ He critically engages with works concerned with transition aspiring to identify its meanings. In doing so, he discovers certain fallacies which make usage of transition inadequate for the academic and practical purposes.

²² Thomas Anderson *et al*, *Multinational Restructuring, Internalization, and Small Economies: The Swedish case* (New York: Routledge, 2005), 1.

²³ Milja Kurki, “Locating the normative within economic science: towards the analysis of hidden discourses of democracy in international politics”, *Journal of International Relations and Development* 16 (2013), 65.

²⁴ Estrin and Uvalic, “Foreign Direct Investments into Transition Economies”; Milica Uvalić, “The economic development of the Western Balkans since Thessaloniki” in Eviola Prifti, ed. *The European Future of the Western Balkans: Thessaloniki@10 (2003-2013)*, (Paris: European Union Institute for Security Studies, 2013), 73-83; Gábor Hunya, *FDI in South-Eastern Europe in the early 2000s, Investing Across the Borders 2010*; Josef Brada *et al*, “The effects of transition and politics of instability on FDI flows in Central Europe and the Balkans”; Transition report 1999, 2006, European Bank for Reconstruction and Development; Gábor Hunya, *Recent FDI trends, policies and challenges in SEE countries in comparison with other regions in transition*.

²⁵ Dejan Jović, “Problems of Early Post-Communist Transition Theory: From *transition from* to *transition to*”, *Političkamisao* (2010), 44-68.

According to Jović, the term transition came into being in the late 1960s and early 1970s.²⁶ It originates in the theory of democracy, which initially focused on the regime changes in Latin America and Southern Europe.²⁷ Early works on transition examine “the interval between one political regime and another”²⁸ acknowledging nonlinearity and uncertainty of the undertaken political changes. It is only with the political changes generated by the fall of the Berlin Wall that transition gained the opposite connotation. In the post-1989 literature, transition is used to describe an inevitable progress toward liberal democracy and market-based economy.²⁹ The collapse of the socialist bloc was interpreted as a confirmation of a unique final outcome. Leaving no room for an alternative outcome, scholars focused their attention on identifying a set of “objective” factors as a key for a functional (consolidated) democracy and (competitive) economy. Another common argument of the post-1989 literature on transition is the perception of democracy and market as natural deeds inherited to the human nature. Both emerge from the understanding of human nature as a rational and individualistic one.³⁰

Peter Winch, a British philosopher, concisely comprehends the gist of transition inadequacy saying that:

[e]ven given a specific set of initial conditions, one will still not be able to predict any determinate outcome to a historical trend because the continuation or breaking off of that trend involves human decisions which are not determined by their antecedent conditions in the context of which the sense of calling them ‘decisions’ lies.³¹

His critique in a very clear way discloses how spotlight on transition can misguide analysis and policy. Taking into account Winch’s critique, I reject transition as defected primarily due to its

²⁶ Jović, “Problems of Early Post-Communist Transition Theory”, 46.

²⁷ Jović, “Problems of Early Post-Communist Transition Theory”, 46.

²⁸ Guillermo O’Donnell and Phillipe Schmitter, *Transitions from Authoritarian Rule. Tentative Conclusions about Uncertain Democracies* (Baltimore: The Johns Hopkins University Press, 1996), p. 6 in Jović, “Problems of Early Post-Communist Transition Theory”, 48.

²⁹ Jović, “Problems of Early Post-Communist Transition Theory”, 48-59.

³⁰ Jović, “Problems of Early Post-Communist Transition Theory”, 55.

³¹ Peter Winch, *The Idea of Social Science and Its Relation to Philosophy* (London: Routledge, 1958/1990) in Jović, “Problems of Early Post-Communist Transition Theory”, 60.

final projections. This way I refuse an existence of preexisting master plan or in advance determined trajectories which are “out there” waiting to be met.

As an alternative to the term of transition, I will use *evolution of the economic order*. Assuming that we cannot know or predict the final upshot, I use the phrase in order to designate various forces engaged in changing an old system at the same time creating a new configuration. Furthermore I understand *evolution* in its original storage, *an unrolling (a book)*,³² or *an opening of what was rolled up*.³³ Using these words I will strive to unroll what was rolled up in the economic field among countries of the Western Balkans in the last thirteen years. Additionally, I do not use evolution as an indication of a necessary progress, since the idea of progress was attributed to the evolution during the Victorian era.³⁴ In contrast an evolution in the thesis is employed as a process whose path depends on a specific context, past experiences, actors, and their practices. Therefore evolution can mean either a progress or stagnation since both can be molded by these strains. Finally, under *economic order* I understand a configuration which is an outcome of the interplay of legacies, actors and their practices.

Moreover, usage of the term evolution of the economic order in the thesis should be distinguished from an evolutionary-institutionalist approach to the transition. Some authors examine the economic transformation making a difference between two reformist strategies: a shock therapy and evolutionary-institutionalist approach. Unlike the shock therapy prescription of radical break-up with a previous system, the evolutionary-institutionalist approach stands for a step-by-step process of altering old practices and institutions.³⁵ In the interpretation of the

³² From Latin *evolutio, onis*, f. Charlton T. Lewis and Charles Short, *A Latin Dictionary*, accessed May 10, 2014, <http://www.perseus.tufts.edu/hopper/text?doc=Perseus%3Atext%3A1999.04.0059%3Aentry%3Devolutio>.

³³ Evolution, *Online Etymology Dictionary*, accessed May 10, 2014, http://www.etymonline.com/index.php?term=evolution&allowed_in_frame=0.

³⁴ Evolution, *Online Etymology Dictionary*.

³⁵ Hubert Gabrisch and Jens Hölscher, *The Successes and Failed of Economic Transition: The European Experience* (New York: Palgrave, MacMillan, 2006), 20-42.

evolution term utilized in the thesis, it does not imply any type of strategy. Conversely it denotes a process in which strategies are made by actors.

Eventually, in this way understood evolution of the economic order affords an opportunity to include Agnes Heller's notion on antagonisms within liberal-democratic modernization and Karl Polanyi's notion of capitalism. In contrast to the transition scholars, Heller claims that liberal-democratic promotion includes promotion of civil society, capitalism, and industrialism, whose interaction produces tensions against themselves. Namely, foundation of the civil society (democracy and equality) is opposed to the basis of capitalism (inequalities) and industrialism (hierarchy).³⁶ Tensions between the strands are not the only ones. According to Polanyi, capitalism represents fundamental conflicts between market efficiency, social cohesion, and political legitimacy which set "capitalism's political life in motion".³⁷ The adoption of Heller's and Polanyi's insights reveals that a process of reforms is composed of constant tensions between democracy and capitalism, between movements and countermovements, between social cohesion and disintegration, between external and domestic aspects of macroeconomic (in)stability. Thus, evolution of the economic order will be used to encompass all of these tensions in the context of the Western Balkans.

1.2 The Western Balkans Concept

The Western Balkans phrase has become extensively accepted among the academia and practitioners reproducing an idea of a natural region, which includes following seven countries: Albania, Bosnia and Herzegovina,³⁸ Croatia, Macedonia, Kosovo*, Montenegro, and Serbia. The

³⁶ Quoted in Balunovć, *Serbia on the European Periphery*, 10.

³⁷ Dotothee Bohle and Béla Greskovits, *Capitalist Diversity on Europe's Periphery* (Ithaca: Cornell University Press 2012), 13.

³⁸ Hereafter: Bosnia. The name of Bosnia will be used to denote both entities (the Federation of Bosnia and Herzegovina and Republic Srpska).

dominant understanding of the Western Balkans as a natural region will be called in the question below. A new term for listed countries will not be proposed, but since the Western Balkans will be used as a reference in the thesis, I feel obliged to point out its normative.

The Western Balkans is a relatively new denomination. It appeared for the first time during the 1998 European Union Summit in Vienna.³⁹ A suggestion of introducing it in the public discourse provoked negative reactions of the Summit participants. They were primarily concerned with a possibility of creating new divisions in the already fragmented region.⁴⁰ But these negative reactions were overcome in 2000 during the meeting of the Club of Three which consists of the British, German, and French stakeholders. Their main argument indicated that the “use of the term ‘Southeast Europe’ rather than ‘Western Balkans’ would imply recognition of the fact that the region is already part of Europe, that its problems are European problems and that any viable solution has to be a European solution, involving both the deepening and the widening of the Union.”⁴¹ In addition, “the structural problems like *economic underdevelopment*

*This designation is without prejudice to positions on status, and is in line with UNSCR 1244 and the ICJ Opinion on the Kosovo Declaration of Independence.

³⁹ Although used as synonyms in the excerpt, it is noteworthy that the Balkans and the Western Balkans distinguish in at least two regards. Firstly the Balkans is defined as an in-between the East and the West having unclear border lines. The Western Balkans on the other hand represents a definite territory surrounded by the European member states. Secondly the Balkans is perceived as a cultural identity, while the Western Balkans gains its identity through political criteria. In this regard, Croatian example is eminent. Vague borders of the Balkans would occasionally include Croatia as its part. For instance, Maria Todorova counts Croatia as a part of the Balkans, but Croatian politicians would deny any connection with the Balkans region. Simultaneously, Croatian intellectuals of the 1990s produced articles proving cultural differences between Croatia and the Balkans nations. Yet Croatia was subsumed under the Western Balkans notion due its lack of functional institutional design. Irina Bokova, “Integrating Southeastern Europe into the European Mainstream,” *Southeast Europe and Black Sea Studies* vol. 2, issue 1, (2002), 24; Tihomir Topuzovski, *Post-Communist Territorialisation of the Western Balkans*, (2010) Accessed March 14, 2014, <http://www.lse.ac.uk/europeanInstitute/research/LSEE/PDFs/PhD%20Symposium/Papers%202010/Topuzovski.pdf>, 4; Maria Nikolaeva Todorova, *Imagining the Balkans* (New York: Oxford University Press, 1997; Milica Bakić-Hayden and Robert Hayden, “Orientalist variations on the theme ‘Balkans’: Symbolic geography in recent Yugoslav cultural politics”, *Slavic Review* Vol. 51, No. 1 (Spring 1992), 9.

⁴⁰ Bokova, “Integrating Southeastern Europe into the European Mainstream”, 32.

⁴¹ Club of Three, “The Balkans and New European Responsibilities,” *Special meeting of the Three*, Brussels, (29-30 June, 2000), 15 in Bokova, “Integrating Southeastern Europe into the European Mainstream”, 32.

and *ethnic nationalism* are now reduced to *this shrinking periphery*.⁴² A meeting summary underlined that the fall of the Berlin Wall abolished the old⁴³ and created a new division in Europe – *Europe and the Balkans*.⁴⁴

In addition to emphasized economic underdevelopment and ethnic nationalism by the Club of Three, this shrinking periphery displayed the lack of institutions, rule of law, and competitive economies all which existed in the European Union countries.⁴⁵ These weaknesses of the Western Balkans have been attributed to wars exhaustion and economic organization. The former have destroyed industry, the human resources, and the infrastructure of involved countries.⁴⁶ Moreover, the Western Balkans economies have been dependent on the primary sector which has stood for a retarded level of development from the Western point of the view.⁴⁷

This set of distinctions between the Western Balkans and the European Union (EU) led to the setting up the relationship between the center and its periphery. The EU acted as an advanced, civilized model in which bloodsheds are not possible anymore. Furthermore the EU imposed a set of political requirements to be met by the periphery. This way, the Western Balkans became an instrumentalized territory in which the European periphery should be reconfigured.⁴⁸ Externally set distinctions between the two were soon internalized. Internalized relation is best depicted in statements made by Zoran Đinđić, former Serbian Prime Minister. He pronounced that Europe

⁴² Bokova, “Integrating Southeastern Europe into the European Mainstream”, 32 (emphasis added).

⁴³ It refers to the division of Europe as capitalist and communist factions. This interpretation of the fall of the Berlin Wall is opposite to the one of early 1990s when it was interpreted as a unification of two (capitalist and former communist) Europe.

⁴⁴ Bokova, “Integrating Southeastern Europe into the European Mainstream”, 24 (emphasis added).

⁴⁵ Bokova, “Integrating Southeastern Europe into the European Mainstream”, 27; George Petrakos, “The Balkans in the New European Economic Space: Problem of adjustment and policies of development”, *Eastern European Economics*, Vol. 40, No. 4 (July-August 2002), 9-11.

⁴⁶ Petrakos, “The Balkans in the New European Economic Space”, 15.

⁴⁷ Petrakos, “The Balkans in the New European Economic Space”, 14.

⁴⁸ Tihomir Topuzovski, “Enjoying the instrumental space” *Political Thought*, Year 8, No. 31 (September 2010), 99-103; Topuzovski, *Post-Communist Territorialisation of the Western Balkans*, 4.

should accept the Balkans as its part⁴⁹ but that the Western Balkans countries should accept Europe as a teacher.⁵⁰ The inquiry suggests that the Western Balkans represents an artifice rather than a natural region; in other words it is a construct made by external actors interested in regional affairs and their impact on the rest of Europe.

1.3 The Foreign Direct Investment Concept

Foreign direct investment has become an important economic instrument in the second half of the twentieth century.⁵¹ The FDI importance is reflected into “more rapidly [increase of its flows] than world income or the total trade in goods. While income and trade almost doubled in value, the stock of FDI quadrupled to an amount corresponding to some 8 per cent of world income.”⁵² Although an expanding activity, FDI has preserved common features which can be abstracted in the form of the following definition, “a long-term interest and control (usually above 10%) in an enterprise resident abroad.”⁵³ These common features can be further sorted out as the FDI types,⁵⁴ determinants,⁵⁵ and spillovers.⁵⁶ Their interplay triggered a debate about a developmental potential of FDI in receiving (or host) country.

⁴⁹ Quoted in Balunović, *Serbia on the European Periphery*, 30.

⁵⁰ Balunović, *Serbia on the European Periphery*, 35.

⁵¹ At least three changes can be identified: (1) a shift from natural resources extraction to the service sector, (2) greenfield activities were substituted by acquisition of already established firms, (3) FDI flows started penetrating new regions such as East Asia, Latin America, Africa, and South East Europe. Thomas Anderson *et al*, *Multinational Restructuring, Internalization, and Small Economies*, 2-3.

⁵² Quoted in Thomas Anderson *et al*, *Multinational Restructuring, Internalization, and Small Economies*, 13.

⁵³ Quoted in “The Western Balkans in Transition”, Directorate-General for Economic and Financial Affairs, European Commission, occasional paper, No. 5 (January 2004), 11.

⁵⁴ FDI can take a form of greenfield, acquisition and merger, brownfield, and joint venture investment; horizontal or vertical; market- or resource- seeking investment. Goran Pejaković, “Direktne Strane Investicije i Bosna i Hercegovina” [Foreign Direct Investment and Bosnia and Herzegovina], *Sarajevo Business and Economics Review* 30 (2010), 724-725.

⁵⁵ There could be distinguished political and economic determinants. Among political determinants are usually stressed political stability and a possibility of conflict outbreak. On the other side, among economic determinants are underlined a market size, labor costs, and inflation rates. Fridriech Schneider and Bruno S. Frey, “Economic and Political Determinants of Foreign Direct Investments”, *World Development*, Vol. 13, No. 2 (1985), 161-175.

⁵⁶ Whereas literature under positive spillovers denotes transfer of technology, managerial skills, and reinvestments; negative ones include the greater degree of integration within international economy, exposure to the external

A developmental potential can be assessed by two questions: whether FDI spurs the economic development, and how it does. Theory and practice are divided on this issue.⁵⁷ Regarding the theoretical debates, even they do not provide a uniform set of conclusions, but rather pros and cons on developmental potential of the FDI. A strand in theoretical debates which argues that FDI enhances development relies on pointing out either a transfer of technology and know-how or strengthening domestic capabilities and institutions.⁵⁸ In more negative vein other scholars argue that actual FDI impact on the development is negligible or none. They point to an increased domestic dependence on mobile foreign companies.⁵⁹

In fact the relationship between the economic development and FDI is far more complex in its nature than these two strands suggest. That is why theoretical predictions and practice diverge. It is necessary to take into account context in order to grasp developmental potential of FDI. For instance, a project conducted by Barbara Stallings demonstrated that regional context highly matters in assessing the FDI impacts on the development.⁶⁰ The project showed that regional dynamics are influenced by context-specific forces (e.g. regional development of Southeastern Asia is influenced by the Japanese model of development and trade links with other Asian countries) which drive developmental paths in various ways.⁶¹

shocks, and so called a race-to-the-bottom. Josef Brada *et al*, "The effects of transition and political instability on foreign direct investment inflows", 677.

⁵⁷ Nauro F. Campos and Yuko Kinoshita, "Foreign Direct Investment as Technology Transfer: Some Panel Evidence from Transition Economies", *The Manchester School*, Vol. 70, No. 3 (June 2002), 399.

⁵⁸ Eduardo Borensztein *et al*, "How Does Foreign Direct Investment Affect Economic Growth?", *Journal of International Economics*, Vol. 45, (1998), 115-135.

⁵⁹ Rajneesh Narula and John H. Dunning, "Multinational Enterprises, Development and Globalization: Some clarifications and a research agenda", *Oxford Development Studies*, Vol. 38, No. 3 (September 2010), 263-287; Rajneesh Narula and John H. Dunning, "Industrial Development, Globalization, and Multinational Enterprises: Reality for Developing Countries", *Oxford Development Studies*, Vol. 28, No. 2 (2000), 141-167.

⁶⁰ Barbara Stallings, "The new international context of development", 349-387 in Barbara Stallings (ed), *Global Change, Regional Response: The new international context of development* (Cambridge: Cambridge University Press, 1995). For a review of debates on the globalization impact on regionalization of FDI flows, and a review of the FDI amounts in regions, see: Aristidis Bitzenis, *The Balkans: Foreign Direct Investment and EU Accession Process* (Farnham, England; Burlington, VT : Ashgate, 2009), 127-154.

⁶¹ Barbara Stallings, "The new international context of development, 384-385.

Similarly it is important to depart from the dominant econometric approach in accessing a developmental potential of the FDI. The econometric approach leaves aside dynamics of the political, social, economic forces. The interplay of these forces explains how a context was created. In other words, it contributes to shaping an environment for FDI to take place and produce effects. Hence, in assessing developmental potential in the Western Balkans, I will conduct an inquiry on the interplay of political, economic, and legal forces.

1.4 Conclusion

This chapter aimed to discuss concepts that will be applied in the thesis below. It sought to demonstrate that words are not empty nomenclatures. In contrast they comprise a wide range of meanings. In order to investigate meanings of the concepts that will be applied in the thesis, the first chapter was structured into three subsections dealing with transition, the Western Balkans, and foreign direct investment, respectively. Echoing earlier debates on the transition concept, several drawbacks were pointed out. Underlined drawbacks delude academic and policy discussions. As a consequence, I have suggested a substitute in a form of evolution of the economic order. In my opinion it allows us to take into account various forces, which are actively involved in shaping outcomes of undertaken reforms in the former socialist countries. The second subsection has explored hidden meanings which the Western Balkans phrase carries out. In opposition to the dominant take, the inquiry denoted a connotation of the Europe's periphery missing the Western type of institutional set-up. Finally the third subsection looked at the concept of foreign direct investment. The FDI concept was considered in terms of spurring economic development. It stressed out the importance of the context in grasping a developmental potential of FDI. The focus of next chapter is how FDI as such influenced evolution of the economic order in the Western Balkans.

2. The Impacts of FDI-related Catalysts on the Economic Order in the Western Balkans

At the beginning of the 2000s violent conflicts had been mostly settled in the Western Balkans. In 1999, the Kosovo conflict was brought to the end by placing the province under the international protectorate in accordance with the UNSC Resolution 1244. In 2001, the Ohrid Framework Agreement put an end to the armed conflict in Macedonia. Negative peace being restored⁶² across the region endowed countries to (re)start reforms of political and economic systems. Decision-makers were inclined to carry out a process of integration into the international economic system and the European economic order.⁶³ They all shared a common assurance that it is prime time to break off with historical backwardness and to join the rest of Europe. Following that way, market oriented policies and policies of institutional changes should have been pursued.⁶⁴ Evolving from the low starting base, the Western Balkans economic reforms were additionally burdened by the conflict inheritance of the 1990s. Many reformist-oriented governments failed to deliver promised changes due to the political and social constraints.

In this chapter I look closer at the economic transformation and related domestic constraints against changes in the Western Balkans. In order to do so, I examine the role of actors, institutions, and policies related to the accruing of FDI influxes. I argue that these three elements have shaped the economic order in the Western Balkans. Unlike previous studies on foreign direct investment in the Western Balkans, I apply a bottom-up approach. The bottom-up

⁶² Hereby, I refer to the distinction introduced by Johan Galtung. He distinguishes between negative and positive peace; whereas negative peace is associated with the absence of direct violence, the positive peace includes the absence of structural and cultural violence. Johan Galtung, *Peace by peaceful means: peace and conflict, development and civilization* (London: Sage Publications, 1998).

⁶³ Bohle and Greskovits, *Capitalist Diversity on Europe's Periphery*, 5; Bokova, "Integrating Southeastern Europe into the European Mainstream", 29; Mamica Nene, "Foreign direct investment in Albania", 40.

⁶⁴ Petrakos, "The Balkans in the New European Economic Space", 7.

approach gets into an inquiry of reasons and motives which have driven actors' practices. The aim is to steer away from academic endeavors particularly interested in the FDI determinants and their impact on the economic development.

2.1 Actors

In a project undertaken to grasp changes of the international politics after the Soviet Union collapse, Rey Koslowski and Friedrich Kratochwil underline the importance of actors' role in both creating and changing an international system.⁶⁵ According to them a change of actors' beliefs and identities generates a change of rules and norms which are basic components of a political interaction. The change of rules and norms takes place through actors' practice. Their notion on the role of actors in changing a system is noticeable in the case of the Western Balkans transformation. Namely elections that took place in 2000 brought new political actors across the region.⁶⁶ They were "new" in comparison with their predecessors exactly in terms of the values and the identities. Unlike political leaders of the 1990s, these new ones highly insisted on breaking with the past and looking into the future. While the past was used to label the economic and political backwardness, the notion of future was employed to mark prosperity and the Euro-Atlantic integration.⁶⁷ Furthermore new politicians were identified as pro-European or pro-

⁶⁵ Rey Koslowski and Friedrich Kratochwil, "Understanding Change in International Politics: The Soviet Empire's Demise and the International System", *International Organization*, Vol. 48, No. 2 (Spring 1994), p. 216

⁶⁶ In Albania, Ilir Meta came into power after several years of continuous political instability. In Bosnia, multi-ethnic party won the elections for the first time after enforcement of the Dayton Accords, and Alija Izetbegović, a Bosniak leader from the time of the Bosnian war, stepped out of his office. In Croatia, a coalition of the social-democrats and liberals led by Ivica Račan won the elections against the party of the Croatian war leader, Franjo Tudjman. Similarly, a large coalition called the Democratic Opposition of Serbia led by Zoran Đinđić won elections in Serbia and made Slobodan Milošević to withdraw from power. In Serbian province of Kosovo, international protectorate was established, preparing local elections and forming an administrative council. Robert Bideleux and Ian Jeffries, *The Balkans: A post communist history* (New York: Routledge, 2007): 54, 375-376, 562-563; Charlemagne: Ilir Meta, *The Economist*, accessed May 20, 2014, <http://www.economist.com/node/627408>; Inagural speech delivered by Zoran Đinđić, January 24, 2001, accessed on May 10, 2014, <http://www.zorandjindjic.org/govori/ekspoze-dr-zorana-%C4%91in%C4%91i%C4%87-u-skup%C5%A1tini-srbije?format=simple>.

⁶⁷ The Euro-Atlantic phrase was launched to denote processes of the integration in the EU and the North Atlantic Treaty Organization (NATO).

Western bearing opposite characteristics to the nationalistic oriented politicians of the 1990s. In that sense, they proclaimed a dedication to the regional cooperation. The regional cooperation was reflected in launching initiatives for reconciliation and projects for the return of refugees and internally displaced persons.

The brand-new political actors were primarily concerned with introducing a set of reforms in the field of politics and economy, which were necessary for a modern liberal state. Regarding politics, their stated goal was building reliable, indiscriminate institutions and transparent mechanism of the institutions activities. Political actors pleaded for a greater democratization of their respective political systems aiming to eradicate inherited crony-nepotistic relations.⁶⁸ Additionally, democratization was highly set goal in the post-conflict regional environment. For instance, in Macedonia the Ohrid Framework Agreement engendered constitutional changes, delivering quotas for the equal ethnical representation in government's institutions, enhancing decentralized government, introducing Albanian as an official language, and granting an identity expression.⁶⁹

Concerning the economy, an increase of a living standard, modernization of industrial systems, and a necessity for trade liberalization and privatization were emphasized.⁷⁰ Initial economic changes and institutions building were supported throughout various donations and aid programs designed for a reconstruction and stabilization. In some cases like Croatia, these changes were proscribed by bilateral agreements signed with the International Monetary Fund

⁶⁸ Charlemagne: Ilir Meta, *The Economist*,

⁶⁹ Ohrid Framework Agreement, 13.08.2001, art. 3, 4, 6, and 7.

⁷⁰ Inagural speech delivered by Zoran Đinđić, January 24, 2001; "Račan: Gospodarski rast od najmanje 5 posto godišnje" [Račan: Economic growth of at least 5 percents per year], *Index*, accessed May 15, 2014, <http://www.index.hr/vijesti/clanak/racan-gospodarski-rast-od-najmanje-pet-posto-godisnje/169875.aspx>; Aristidis Bitzenis, *The Balkans: Foreign Direct Investment and EU Accession Process* (Farnham, England; Burlington, VT : Ashgate, 2009), 18; *Ekonomski izveštaj o Saveznoj republici Jugoslaviji*, [Economic Report about Federal Republic of Yugoslavia], OECD Rezime, (November 2002).

(IMF).⁷¹ In addition, the restoration of political stability and regional cooperation, including as well as altering the old institutions were followed by FDI influxes. They were primarily carried out through the privatization of the larger state-owned firms and a privatization of the bank sector. However the issue, which aroused here is that financial assets achieved through FDI flows were largely used to stimulate the public consumption. This policy contributed to the economic growth in a short run. In a long run, it has not contributed to the economic development since no innovation for the future comparative competitiveness was intensified.

Moreover political restraints such as the cooperation with the ICTY (Bosnia, Croatia, and Serbia), addressing ethnic violence escalation (Kosovo, Macedonia), minority inclusion (Bosnia, Macedonia, Kosovo), and anticorruption (among all Montenegro) slowed down the market-based reforms. Most of these political restraints set by the external actors had to be addressed and resolved by domestic actors. Addressing these restraints contributed to a country's progress in the EU integration and international (external) reputation to domestic actors. However, coping with these restraints weakened internal actors' capacity to conduct reforms, especially market-based ones since they presented painful steps like public cuts and layoffs. Any attempt of introducing of the reforms was interpreted as an attempt of the national betrayal. Therefore domestic actors aiming to preserve political legitimacy and social cohesion put painful reforms aside.

Regarding painful reforms, in an interview Nikola Gruevski as a Macedonian Minister of Finance (1999-2002)⁷² acknowledged that:

[p]oliticians, dependent on voter satisfaction often need prodding to implement painful reforms. Some of the measures included in our arrangement have increased unemployment. We had to sell or shut down 12 large loss makers. Another 30 are to be sold or closed. We have pared more than 3000 workers off the state administration payroll. But this is a drop in the unemployment bucket.⁷³

⁷¹ "Pismo sporazuma sa MMF-om: Inflacija najviše četiri posto" [Agreement with the IMF: Inflation rates up to four percent], *Slobodna Dalmacija*, accessed May 20, 2014, <http://arhiv.slobodnadalmacija.hr/20010202/novosti1.htm>.

⁷² Gruevski currently runs the office of the Prime Minister (since 2006) in Macedonia.

⁷³ "An Interview with Nikola Gruevski", accessed May 15, 2014, <http://samvak.tripod.com/nm095.html>.

The case in point provides several important implications for understanding the economic order in the Western Balkans. One, politicians concerned with short-run results and re-elections did not want to engage in painstaking changes, and be the one who would pay a price for decades-long aggregated problems. Consequently, economic analysts and technocrats became those who addressed necessity of painful reforms to spur the development. Two, although costs of potential reforms increased due to political restraints, a demand for fresh capital has still been there. High unemployment rates and poor production should have been worked out. Discrepancy between political will and demand for fresh capital flow shaped a perception of FDI as the engine of the economic development.

Furthermore this discrepancy was deepened with the outbreak of the 2008 economic crisis. Many domestic actors in the Western Balkans saw a chance for the economic taking off exactly in circumstances of the crisis. They claimed that foreign companies would have relocated their production from crisis affected areas to the Western Balkans. Thus, domestic actors have extensively embraced foreign direct investment as a part of their agendas. Additionally a capability to attract new amounts of the investment became a yardstick in accessing politicians' efforts to provide public goods.⁷⁴ A striking example comes from Serbia, where after changes in the government composition the former president under whose presidency the economy has got even more deprived accused new officeholders for a dramatic drop in FDI amounts.⁷⁵

⁷⁴ "Medojević: Osvojićemo vlast na Cetinju, i dovešćemo investitore koji će obnoviti Obod" [Medjević: We will win the elections in Cetinje, and bring investors to restore Obod], *Vijesti*, accessed May 15, 2014, <http://www.vijesti.me/vijesti/medojevic-osvojicemo-vlast-cetinju-dovesemo-investitore-koji-ce-obnoviti-obod-clanak-157536>;

⁷⁵ Legally Serbia is a parliamentary system, but the practice in the period from 2008 to 2012 brought an exception. Namely a president as a head of state gained more powers than at that time prime minister. "Tadić: Dramatičan pad stranih investicija" [Tadić: Dramatic decline in foreign investments], *Vesti Online*, accessed May 15, 2014, <http://www.vesti-online.com/Vesti/Srbija/348577/Tadic-Dramatican-pad-stranih-investicija>; "Italijanske kompanije odustale od ulaganja u Srbiju" [Italian companies gave up from investments in Serbia], *Vesti Online*, accessed May 15, 2014, <http://www.vesti-online.com/Vesti/Ekonomija/230344/Italijanske-kompanije-odustale-od-investiranja-u-Srbiju>.

Likewise, dominant features in actors' public speeches are personalization of any newly accrued investment. Personalization refers to a public representation of new FDI influx as politicians' individual success. In this vein the elections that took place from 2012 to 2013 in the Western Balkans countries are illustrative.⁷⁶ During the electoral campaign politicians underlined their ongoing talks with foreign investors about creation of new jobs. Similarly their interlocutors would have always insisted to stay anonymous. The best depiction of this trend is found in the following journalist excerpt reporting Gruevski's speech in the elections outset, "he cannot disclose the names of companies until they decide to announce their intentions to that effect. He however listed French, US, German and regional companies, which have plans to invest in Macedonia."⁷⁷

By unrolling actors' practices in last thirteen years, the construction of FDI as an ultimate panacea to socio-economic problem was displayed. Unlike recent studies on the Western Balkans and its individual countries, which find explanations for current economic underperformance in the structures of the world system,⁷⁸ the inquiry into actors' practices showed that the economic underperformance can be more accurately grasped by actors' activities, odds, and restraints. This inquiry can take a step further and interpret the role of domestic actors in perpetuating relations like the center and the periphery, not the other way.

2.2 Institutions

Koslowski and Kratochwil in the earlier mentioned article define institutions as "settled or routinized practices established and regulated by norms."⁷⁹ Institutions moreover represent a

⁷⁶ CG: Izbori pokrenuli investicije [Montenegro: Elections launched investments], *Večernje novosti*, accessed May 15, 2014, <http://www.novosti.rs/vesti/planeta.300.html:391563-CG-Izbori-pokrenuli-investicije>;

⁷⁷ "Gruevski: Macedonia must be economically powerful", Macedonia Intl News Agency, accessed May 15, 2014, <http://macedoniaonline.eu/content/view/23588/2/>

⁷⁸ Balunović, *Serbia on the European Periphery*.

⁷⁹ Koslowski and Kratochwil, "Understanding Change in International Politics", 222.

framework within which actors interact with each other in order to engender reforms and achieve goals. Relying on these utterances the focus below will be on an institution launched to support the economic development and foreign direct investment. This institution is the agency for investment promotion constituted after two large decreased FDI flows, after 2004 and 2008.⁸⁰ Its task has been to attract fresh capital influxes as well as to promote domestic exports; through these channels the institution should spur the economic development of the respective countries.

Agencies for the investment promotion are government-run agencies with an aim to attract new investors, keep existing (providing reinvestment), and to support exports, primarily of domestic-owned firms. A suggestion of setting up this type of institutional framework came from the European Commission. In its assessment prospective of the economic development in the Western Balkans, the European Commission underlined a necessity to set up investment promotion agencies.⁸¹ As an answer to external incentives and domestic demands (e.i. unemployment), the agencies have been launched since 2004. The first one was established in Bosnia, while the latest agency is opened in Croatia.⁸²

⁸⁰ An agency for investment promotion is not the only one institution created for this particular purpose, but rather the only one which could be found in all of seven countries in the Western Balkans. Other specific institutions established with the same purpose are economic diplomats, or Ministry without portfolio responsible for attracting foreign investment (in Macedonia, established in 2006). Regarding the economic diplomats, there are indications of introducing these new special envoys in diplomatic representations of the regional countries; but by far the economic diplomats have been introduced as a part of the Croatian and Serbian *corps diplomatique*. Their achievements are differently evaluated. While in Croatia, they are praised for contributing to the exports growth, in Serbia their position was revoked due to the poor results. However the common ground is that economic diplomats represent a rise in costs, and an increase in the stuff (there are already public servants in diplomatic representations in charge for the economic activities and promotion). “Gospodarska diplomacija: Naši rezultati prvih šest meseci” [Economic Diplomacy: Our results after the first six months]; “Velika laž o ekonomskoj diplomaciji” [Big lie about the economic diplomacy], *Globus*, accessed May 14, 2014, <http://globus.jutarnji.hr/hrvatska/velika-laz-o-gospodarskoj-diplomaciji>; “Ekonomске diplomate se vraćaju kući” [Economic diplomats go back home], *Vesti*, accessed on May 14, 2014, <http://www.vesti-online.com/Vesti/Srbija/247865/Ekonomske-diplomate-se-vracaju-kuci>; Republic of Macedonia, Minister without portfolio responsible for attracting foreign investment, accessed on May 20, 2014, <http://www.msi.gov.mk/?q=frontpage>; Mile Sadžak and Mirza Pašić, *Ekonomska diplomatija-izazov visokog prioriteta za Bosnu i Hercegovinu* [Economic Diplomacy: A challenge of high priority for Bosnia and Herzegovina], (Sarajevo: Friedrich Ebert Stiftung, Vanjskopolitička inicijativa BiH, 2012).

⁸¹ “The Western Balkans in Transition”, 11, 31.

⁸² Foreign Investment Promotion Agency (FIPA, Bosnia, 2004), Agency for Foreign Investments and Exports Promotion of the Republic of Macedonia (2004), Montenegrin Investment Promotion Agency (MIPA, Montenegro,

The agencies commonly endeavor to underline the strategic position of the countries' economies using the notion of a crossroad between the West and the East, and the idea of a gateway to major markets of Europe.⁸³ In addition, the agencies point out the significance of their location, either by describing as the very heart of Europe or the Balkans,⁸⁴ or by outlining the closeness of the European markets (e.g. from Croatia all of Europe is reachable in three hours, or it takes up to five hours to the sea-ports from Kosovo).⁸⁵ These characteristics reveal a self-perception of a transit area in gravity of the European markets.

Closely related to the notion of the transit area is the agencies' emphasis on bilateral free trade agreements with other countries (including Stabilization and Association Agreements with the EU which entails liberalization of the trade)⁸⁶ or a membership in the World Trade Organization⁸⁷ and the 2006 CEFTA (Central Economic Free Trade Agreement). In the light of being the transition zone, emphasis on free agreements can be interpreted as an open call to non-European companies to invest in the region and from there export to the larger European markets without enormous costs (cheap labour force, no customs tariffs). Among non-European

2005), Albanian Investment Development Agency (AIDA, Albania, 2006), Serbian Investment and Exports Promotion Agency (SIEPA, Serbia, 2010; during the 2000s it was the office of the government), Agency for Investment and Competitiveness (AIK, Croatia, 2012; although it has its predecessors throughout the 2000s), Investment Promotion Agency of Kosovo (IPAK, Kosovo, it is a part of the Ministry of Trade and Industry of the Kosovo government).

⁸³ "Top ten reasons to invest in Albania", Albanian Investment Development Agency, accessed May 20, 2014, http://aida.gov.al/?page_id=299; "Why invest in Croatia", Agency for Investment and Competitiveness, accessed May 20, 2014, <http://www.aik-invest.hr/en/why-croatia/>; Alexander Petritz, "Serbia's Economic Situation at the Crossroads", 193 in Wolfgang Petritsch *et al.* (eds), *Serbia Matters: Domestic Reforms and European Integration* (Baden-Baden: Nomos, 2009); "Excellent Infrastructure", Agency for Foreign Investments and Exports Promotion of the Republic of Macedonia, accessed May 20, 2014, <http://www.investinmacedonia.com/node/35>; "Land of nature", Agency for Foreign Investments and Exports Promotion of the Republic of Macedonia, accessed May 20, 2014, <http://www.investinmacedonia.com/node/31>.

⁸⁴ "A Strategic Location", IPAK, accessed May 20, 2014, <http://www.invest-ks.org/en/A-Strategic-Location>.

⁸⁵ "Why invest in Croatia", *Agency for Investment and Competitiveness*; "How to get to Kosovo", Investment Promotion Agency of Kosovo, accessed May 20, 2014, <http://www.invest-ks.org/en/How-to-get--to-Kosovo>.

⁸⁶ The EU is the first trade partner to the countries of the Western Balkans. Particularly, 67.4% of total regional exports were directed toward the EU member states. "European Union Trade in Goods with Western Balkans", Directorate Directorate-General for Trade, European Commission, accessed December 19, 2013, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113477.pdf, 9.

⁸⁷ The WTO membership holds Albania, Croatia, Macedonia, and Montenegro.

companies, those from China, India, and lately from the Arab countries are a targeted audience. Even more some of the European companies are interested in investing in the region because of the bilateral free trade agreements with Russia.⁸⁸ Therefore, these particular bilateral free trade agreements could be a chance for the countries to attract exports-oriented investments.

The latter (CEFTA) is a multilateral framework established to convert poor economic performance of the Western Balkans into the bright one and restore trade ties among them. CEFTA was initially devised among the Visegrád countries in 1992. The Visegrád four encouraged by the EU set it up as an economic framework of cooperation aiming to accelerate economic reforms, to liberalize trade, and to strengthen economic competitiveness of the Visegrád countries. In addition the CEFTA presented a preparatory stage for the EU economic affairs. With the same goals the CEFTA framework was applied among the countries of the Western Balkans and Moldova in 2006.⁸⁹ Trade liberalization achieved through the CEFTA matters for FDI upsurge because individual Western Balkans countries do not represent large markets.

To return to the subject, the role of the investment promotion agencies has warped during the time. Initial purpose of the agencies was set up to increase countries “attractiveness” in the regard to FDI; by far results are rather of the low intensity. Promotion of the investment environment has been reduced to the presentation of promotional materials at various fairs, organizing business forums, and trainings about the exports culture for the local companies. The main critiques of these institutions are based on emphasizing disparity between the costs and their accomplishments. Closely related to these critiques is their activity in the regions which have

⁸⁸ “Vlada Srbije i FIAT potpisali Ugovor o zajedničkom ulaganju u “Zastavu” - potpisan i Memorandum o razumevanju sa “Iveco” i “Magnetit Marelli”, *Ekapija*, accessed May 20, 2014, <http://www.ekapija.com/website/sr/page/195453/Vlada-Srbije-i-FIAT-potpisali-Ugovor-o-zajedni%C4%8Dkom-ulaganju-u-Zastavu-potpisan-i-Memorandum-o-razumevanju-sa-Iveco-i-Magnetit-Marelli>.

⁸⁹ *CEFTA Secretariat*, accessed May 15, 2014, <http://www.cefta.int/>.

already been covered by other institutions, for example by chambers of commerce. Furthermore, a recent case of the Serbian promotion agency brought to the fore misuses of the public finance. It has prompted up discussions on the role, results, and the purpose of investment promotion agencies in regional states.

Eventually the inquiry on the investment promotion agencies in the Western Balkans divulges the following paradox: while the agencies are established as bodies of technocrats to attract more investors, their role is reduced to the marketing or a public relations (PR) promotion of their countries. Consequently arrivals of the investors have become more of a political deal than actual work of technocrats. It additionally enabled domestic political actors to materialize investments as their personal achievements. Thus, a purpose of the inquiry into the institutions, e.i. the investment promotion agencies, was to demonstrate that a shift from insistence on reforms to FDI attraction has been accompanied by hollow institutional set-ups to resolve a question of the economic underdevelopment.

2.3 Policies

The discussion in the previous subsections affords to introduce another constitutive element of the economic order; that is a policy component. Policies are transparently defined means for achieving a targeted goal, and as such they are a product of actors' pursuits. Policies in the field of the economic transformation spell out a wide range of mechanisms, instruments, and procedures to enhance reforms and to induce desired developments on the ground. Therefore investigation of the policies as actors' endeavors to influence change and reduce adverse state of affairs appears to be an important step in tracing evolution of the economic order.

As an illustration let us take Sali Berisha, the former Albanian Prime Minister who explained that Albanian miracle (economic growth, significant FDI inflows, i.e. *desired*

developments) has been based on reduced public expenditure, i.e. *policy*. In an interview for the Forbes Magazine in 2010, Berisha underlined that he as a cardiologist did not know much about the economics, but the political engagement made him to obtain an economic knowledge.⁹⁰ He found an inspiration in Ronald Reagan's policies:

He [Ronald Reagan] was an ideal to me as a leader who fought so successfully against companies. And that's why I have a deep belief for him. He was a low-tax president. And he wrote that low taxes, money, more or less, money in the accounts of the investors, of private people, are much more efficient than in public cases. And that was absolutely true for Albania, because the mandrel capacity of the public sector was almost inexistent. That's why I started the career as a low-tax man. I put, at that time, the lowest fiscal burden country on Europe. But it worked.⁹¹

Further on Berisha acknowledged that this policy has cost him voters' support in the late 1990s. However, he has not given up his ideas about low taxes policy. When he returned to the office in 2005 one of his first takes was reduction of high taxes which have been introduced by previous governments and diminishing the Social Security contribution. Even in the crisis period he strongly aspired to pursue low taxes policy claiming that the "best immunity from this crisis is to help business. [Therefore it is necessary] to enlarge the spaces and freedoms for it."⁹²

Taking in consideration Berisha's agenda as an example of the legal framework stimulating the development, policies concerned with tax incentives and other state subsidies are to be explored. Out of the focus stays a privatization policy, while trade liberalization and its significance are briefly discussed in the previous section on institutions. Although the former is remarkably important, its investigation would introduce additional (new) element of the transformation (e.i. transformation of the ownership) which is out of the thesis scope.⁹³ The focus

⁹⁰ "Transcript: Sali Berisha", *Forbes Magazine*, accessed May 15, 2014, <http://www.forbes.com/2010/10/08/flat-tax-albania-intelligent-investing-berisha.html>

⁹¹ "Transcript: Sali Berisha", *Forbes Magazine*.

⁹² "Transcript: Sali Berisha", *The Forbes Magazine*.

⁹³ For the studies on the privatization in the Western Balkans, see: Milica Uvalic, "Privatization in the Yugoslav Successor States: Converting Self-management into Property Rights", 267-302 in Milica Uvalic and *et al.* (eds) *Privatization Surprises in Central and Eastern Europe* (1997); Bideleux and Jeffries, *The Balkans*, 67-68, 214-216, 252, 322-323, 397, 460, 463-464, 503-504; Timothy Donais, "The Politics of Privatization in Post-Dayton Bosnia",

here is on policies that are designed in the process of economic transformation to attract FDI and improve the economic state of affairs. The pro-active FDI policies are not endemic;⁹⁴ they are common in countries that lack advantages in technology and innovation.⁹⁵ Nevertheless policies effects on the economic development are specific for a country or region.⁹⁶

Regarding tax incentives, it is suggested that lower tax would appeal to a greater FDI upsurge. Tax incentives are provided for investments which are supposed to contribute to the exports shares, production, and research and development activities. Even more these are granted for activities which a host country sees as its strategic advantage like in the case of Montenegro; targeting tourism its authorities who agreed to exempt from payment of utilities investors who decide to build hotels on its coastline.⁹⁷

Using a business forum in the United States as a chance to accrue FDI influxes, Gruevski promoted a tax regime in Macedonia which in comparison with the American system appears to be more advanced and liberal:

Sounding more like an economic developer than a head of state, the prime minister beamed while highlighting a tax regime many Americans would envy: a flat 10 percent on income and 10 percent on distributed profits from corporations.⁹⁸

In other words an emerging fragile economy provides more favorable conditions for doing business than a mature market economy. Here emerges a contradiction of the catching up – states in a process of the economic transformation strive to catch up with developed countries following norms and rules tailored by developed countries. Norms and rules are adjusted to their mature

Southeast European Politics 3(1) (2002), 3-19; Olle Andréasson, "The Good, The Bad and The Ugly: Post-war privatization in Bosnia and Herzegovina" (MA Thesis submitted to the Department of Economic History, Uppsala University, 2007).

⁹⁴ Barbara Stallings, "The new international context of development", 364-372.

⁹⁵ Vera Šćepanović, *FDI as a Solution to the Challenges of Late Development: Catch up without Governance?* (PhD Dissertation, Central European University, 2013), 15.

⁹⁶ The influences of policies are discussed more in detail in the third chapter.

⁹⁷ "Radenović: Do kraja godine olakšice za investitore" [Radenović: Incentives for Investors till the End of Year], *CDM*, accessed May 15, 2014, <http://www.cdm.me/turizam/radenovic-do-kraja-godine-olaksice-za-investitore>.

⁹⁸ "Macedonian Prime Minister Touts Investment Climate", *Global Atlanta*, accessed May, 15, 2014, <http://www.globalatlanta.com/article/25771/macedonian-prime-minister-touts-investment-climate/#largeBanner>.

level of developments.⁹⁹ Unlike developed countries which built their welfare on often protective practices, states seeking to catch up are expected to do so by not protecting their growing economies. Moreover developed countries maintain their advanced position through innovation,¹⁰⁰ while others are supposed to rely on outdated technology and lax policy provisions. The case of Macedonian tax regimes shows that transnational character of economy brings unequal starting positions between developed and developing.¹⁰¹

Governments' subsidies on the other hand go from incentives for newly created jobs up to the improvements of infrastructure capacities. Financial incentives depends on the areas in which investments come in (developed, or undeveloped regions), as well as depends on categories (disabled persons, minorities, women, etc.) and numbers of newly employed. In two of the poorest countries in Europe, Bosnia and Macedonia, incentives for every newly employed vary between 1 300 and 1 5000 Euros or go up to 70% of the total wages, respectively. Governments also finance retraining of the labour force at the request of an employer. In the regard to the infrastructure, governments and local authorities often agree to improve existing facilities, primarily transportation networks.

Finally, inauguration of these policies is not only inspired by a belief that incentives would bring new investors, but also by the regional rivalry. The regional rivalry pertains pointing out to neighboring countries' practices and legal provisions as a justification to adopt novel policies.¹⁰² Since the regional rivalry is often understood as a race-to-the-bottom meaning that more lax provisions regulate economic affairs, an impetus to introduce policies can be interpreted as an

⁹⁹ Ha-Joon Chang, *Kicking Away the Ladder: Development Strategy in Historical Perspective*, (Anthem Press, 2002), 125-142.

¹⁰⁰ Šćepanović, *FDI as a Solution to the Challenges of Late Development*, 9.

¹⁰¹ Joseph Stieglitz, *Making Globalization Work* (New York: Norton & Company, 2006), 61-101.

¹⁰² "Šehović: Strane investicije kao preduslov razvoja" [Šehović: Foreign investments as precondition to the development], *SDP*, accessed May 15, 2014, <http://sdp.co.me/aktuelnosti/2756>;

effort not to lose a comparative advantage in attracting external mobile capital.¹⁰³ If we recall earlier scrutiny on actors, then a supplement to the argument of that discussion can be made as it follows: not only domestic actors (politicians, and other stakeholders), but also states as international actors and states' practices (embodied in policies) influence transformation process.

2.4 Conclusion

This chapter was concerned with the evolution of the economic order in the Western Balkans from 2000 to 2013 by scrutinizing foreign direct investments. Steering away from the dominant research patterns of investigating the impact either of the FDI determinants or macroeconomic and political stability on developmental potential of the FDI, the bottom-up inquiry examined three main elements of a political environment (domestic actors, institutions, and policies). In a first step I explored actors and their practices in construing the economic order. I identified a shift from insistence on reforms toward FDI and its consequences. In a second step I examined agencies for the investment promotion and their role in attracting FDI upsurge. In a final step I investigated domestic policies formulated to provide FDI incentives. This examination not only showed characteristics of investigated policies, but also the aftermath of regional rivalry. Next chapter is a discussion of above analyzed practices, seeking for a theoretical explanation and policy alternatives.

¹⁰³ Unlike this trend, impetus to unify regional FDI-related policies came from the Stability Pact for Southeastern Europe. In particular, its component, the Investment Compact proscribed “unifying FDI registration and approval procedures with those for domestic firms; allowing acquisition of real estate by foreign investors for FDI purposes; minimizing FDI-related requirements on statistical reporting, work and residence permits; eliminating discrimination in access to government procurement contracts; and removing obstacles to FDI in financial and professional services.” Demekas *et al.* “Foreign Direct Investment in Southeastern Europe”, 13.

3. Reflections on the Economic Order in the Western Balkans

The most recent review of FDI in the Western Balkans reports that more than a half of attracted FDI were intended in the services sector by 2010.¹⁰⁴ Investments in the services sector do not generate indispensable development in the region. Firstly, these investments do not decrease unemployment, since a large-scale labour force is not required for their realization. Secondly, services-oriented investments are market-seeking in their character, and as such do not contribute to countries' exports and long-term economic growth. Specifically in the Western Balkans, only two firms significantly contributed to the exports rates: the US Steel branch located in Serbia¹⁰⁵ and the Aluminum Plant in Montenegro.¹⁰⁶ Thirdly, the highest shares of FDI went into the banking sector. Foreign (European) banks penetration in the Western Balkans countries is astonishing; their ownership is between 75-90% of total regional banking sector.¹⁰⁷ Albeit empirical studies identified different crisis impacts on the foreign banks behavior,¹⁰⁸ there is a concern of possible banks withdrawal and consequences it may have upon fragile economies in the Western Balkans.

¹⁰⁴ "The services sector represented just over 60 percent of total inward FDI stock in Bosnia and Herzegovina, Macedonia and Romania, but more than 75 percent in Croatia and Serbia." Estrin and Uvalic, "Foreign Direct Investments into Transition Economies", 293.

¹⁰⁵ It produced around 12% of the Serbian exports. However in 2012 the US Steel withdrew from Serbia due to negative crisis impacts on the markets. Consequently the Serbian government purchased the US Steel factory for one dollar in order to preserve five thousand jobs. Micheal Ehrke, "The Global Crisis at the European Periphery", 189, in Wolfgang Petritsch *et al.* (eds), *Serbia Matters*; "Vlada otkupila US Steel za jedan dolar" [Government redeemed the US Steel branch for a dollar], *Vreme*, accessed May 20, 2014, <http://www.vreme.com/cms/view.php?id=1032167>.

¹⁰⁶ It is owned by the Russian company; it has produced around 40% of the Montenegrin GDP. Ehrke, "The Global Crisis at the European Periphery", 189.

¹⁰⁷ *Western Balkans: Bumps on the road to EU accession*, Deutsche Bank, DB Research (August 24, 2012), 9.

¹⁰⁸ Ursula Vorgel and Adalbert Winkler, "Do foreign banks stabilize cross-border bank flows and domestic lending in emerging markets? Evidence from the global financial crisis", *Comparative Economic Studies*, Vol. 54, No.3 (September 2012), 507-530; Rachel A. Epstein, "Central and Eastern European banks response to the Financial 'Crisis': Do domestic banks perform better in crisis than their foreign-owned counterparts?", *Europe-Asia Studies*, Vol.65, No.3 (May 2013), 528- 547; Zdenek Kudrna and Daniela Gabor, "The return of political risk: foreign-owned banks in emerging Europe", *Europe-Asia Studies*, Vol.65, No.3 (April 2013), 548- 566.

This brief discussion on attracted FDI does not coincide with actors' take on the economic development. In contrast to actors' claim about FDI being an ultimate panacea for economic underperformance, attracted FDI appears not to be sufficient to solve the key socio-economic problems. Therefore my objective in this final chapter is to try to explain this divergence. In order to do so, I address two questions: why actors have kept presenting FDI as the engine of the economic development in spite of poor FDI-induced results, and what policy alternatives to FDI-led model of the development could be. I address the contention between actors' practices and materialized FDI in order to make an assessment to the economic order in the Western Balkans, with a particular emphasis on broader contextual factors. Then, I identify feasible substitutes to FDI in the context of the Western Balkans.

3.1 The economic order in the Western Balkans: reconsidered

Answer on the divergence between actors' practices and attracted FDI is partly embodied in the inquiry in the second chapter. The inquiry proposed that actors have crowned FDI as the only viable solution to the regional economic underdevelopment due to political restraints. These restraints caused a shift among actors' priorities in the field of economy. They shifted actors' priorities from market-based reforms to preservation of political legitimacy and social cohesion. Second part of the answer can be found in contextual factors, or more precisely in domestic (im)balances and timing of the regional inclusion in the international arena.

Domestic imbalances in the Western Balkans were additional forces that made actors to promote FDI as an economic panacea. At the beginning of the 2000s, the lack of domestic savings was the main imbalances of concerned. The lack of domestic savings meant the lack of available financial assets which could have launched the production and induced altering of an outdated technology. Furthermore a slow economic recovery reflected in low levels of GDP rates

and trade and account deficits in 2004 reassured the idea that any development strategy for the Western Balkans should have included its capacity to attract FDI.¹⁰⁹

In the time when the Western Balkans started the transformation, the Visegrád countries recorded the highest FDI amounts among all former socialist countries. Specifically Hungary was the only emerging economy which received significant levels of investments until 1997, when other Visegrád countries caught up.¹¹⁰ The records on the FDI amounts in the Visegrád region indicate that “their share of total world’s FDI was nearly three times larger than their share of the world markets.”¹¹¹ Consequently transformational paths of the Visegrád group converged toward a common foreign-led capitalist model.¹¹²

The Visegrád example is taken as representative of FDI-led model of development.¹¹³ In looking for the solution to the crisis, a Croatian economic analyst singled out Slovakia as an example to be followed.¹¹⁴ Similarly the Visegrád politicians from the time of reforms are active within the Western Balkans region giving their wisdom to local politicians. One of these politicians is Mikulas Dzurinda, former Slovak Prime Minister.¹¹⁵ Making comparison between Slovakia as a laggard of the Visegrád group and the Western Balkans as a laggard of transformation and the EU integration Dzurinda advises about necessary reforms which should the region turn in a successful story like Slovakian one.

¹⁰⁹ “The Western Balkans in Transition”, Directorate for Economic and Financial Affairs, European Commission, occasional paper, No. 5 (January 2004), 11.

¹¹⁰ Svejnar, “Transition Economies”, 16.

¹¹¹ Šćepanović, *FDI as a Solution to the Challenges of Late Development*, 1.

¹¹² Bohle and Greskovits, *Capitalist Diversity on Europe’s Periphery*, 151.

¹¹³ Demekas *et al.* “Foreign Direct Investment in Southeastern Europe”, 12.

¹¹⁴ “Jurčić: Trebamo investicije koje će brzo donijeti profit! Od najavljenog profit će biti za deset godina”, *Politika Plus*, accessed May 20, 2014, <http://www.politikaplus.com/novost/52016/jurcic-trebamo-investicije-koje-ce-brzo-donijeti-profit-od-najavljenog-profit-ce-bit-za-10-godina>.

¹¹⁵ “Taxpayers’ Festival Held in Serbia”, *Libek*, <http://libek.org.rs/en/news/2013/06/17/taxpayers-festival-held-in-serbia>, accessed May 10, 2014.

Hence, fully-employed answer on the question why actors have kept presenting FDI as the engine of the economic development in spite of poor FDI-induced results covers not only actors' practices, but also contextual factors such as internal imbalances and a broader policy environment.

3.2 The FDI-led model of development in the Western Balkans: reconsidered

Above discussed considerations provide a possibility to engage with policy alternatives to the FDI-led model of development. This subsection seeks to identify viable alternatives that could resolve the regional underdevelopment in a long-run. The examination below employs analysis of the remittances, regulation of the grey economy, the Euro-Balkans bonds, and creation of regional joint ventures. These four are chosen to fit earlier discussion on FDI depicted as fresh financial assets and market-seeking investments.

Besides foreign direct investments, remittances have kept representing a constant fresh capital inflow in the Western Balkans economies.¹¹⁶ They stand for high shares of regional economies contributing to the economic growth respectively. But the remittances as accrued foreign investments have been utilized in public consumption. Here again the problem of the economic growth in a long-run emerges; as we earlier discussed stimulation of the public consumption does not lead to sustainable economic development. In addition to the question of growth ongoing economic crisis hit “source” countries inducing insecurity of the employment. Therefore even reliability of the remittances for boosting economic growth in a short-run is questioned during the crisis.

¹¹⁶ Estimations show that remittances account for around 9% of GDP in all Western countries, with an exception of Macedonia where remittances level is 3% of GDP. The main countries from which remittances flow are Germany, Austria, Greece, and Italy. *Western Balkans*, Deutsche Bank, 9.

Furthermore grey economy that is widespread among the regional countries is a serious problem that has not been yet on the official agendas. A large percent of the working population is employed in grey economy (mostly retails) receiving minimal wages without any health and pension insurance.¹¹⁷ In the times when governments borrow money from international financial institutions to cover budget spending and support foreign investors' arrivals, a policy that would effectively deal with grey economy would ensure new budget surpluses. Moreover this policy would provide increased inflow of taxation which would further cover deficits of the public funds, and put in order business ethics of new entrepreneurs.

Regarding dependency on foreign bank activity in the region, Fikret Čaušević, a Bosnian economist puts forward an idea of establishing Euro-Balkan bonds which would act as a sort of substitute to this dependency.¹¹⁸ The Euro-Balkan bonds would be issued by new set up Guarantee Fund for the Western Balkans. The main goal of the bonds would be investments in the field of infrastructure.¹¹⁹ Finally instead of strengthening regional rivalry, authorities should consider regional cooperation in terms of establishing joint ventures. Initial steps have been made already made in this direction. Further incitement of joint investments will be necessary in order to overcome low FDI influx, but also to preserve certain level of regional wages, and obtain technology.

3.3 Conclusion

My task in this chapter was to address two questions: why actors have kept presenting FDI as the engine of the economic development in spite of poor FDI-induced results, and what policy alternatives to FDI-led model of the development could be. Regarding the first question, I

¹¹⁷ It is even more concerning since the demographic structure of the regional countries is characterized by older population, with an exception of Kosovo.

¹¹⁸ Fikret Čaušević, "Small open economies in the Western Balkans: Controlled fiscal expansion for a new deal for the Western Balkans", *South East Europe Studies*, St. Antony's College, University of Oxford (March, 2012), 5.

¹¹⁹ Čaušević, "Small open economies in the Western Balkans", 7.

considered contextual factors like internal imbalances and timing of the regional inclusion in the international arena. The inquiry into contextual factors showed actors' practices were reinforced by the lack of domestic savings, deficits in the accounts, and successful examples of FDI-led model of development in high policy environment. Concerning the second question, I reviewed possible alternatives to the regional model of development. I started with a consideration of the remittances and grey economy as two sources of additional financial assets, which could be used to spur the economic development. Since the overarching regional FDI characteristic is an overwhelming foreign penetration of the banking system I looked up for an alternative which could reduce a level of dependency on the foreign banks. Finally, I suggested regional investments in joint ventures which would operate in within the regional market.

Conclusion

This thesis aimed to demonstrate changes of the economic order advanced by actors in the Western Balkans. I have argued herein that the economic order has been evolving through the practices of altering socialist economies, and concurrently spelling out foreign direct investments as the key mechanism of spurring the development. Actors' practices in shaping the economic order were driven by political restraints, efforts to keep political legitimacy and social cohesion. Additionally, actors' practices were underpinned by contextual factors. Among contextual factors, I have identified internal imbalances and a broader policy environment. Thus, the interplay of these forces has shaped the economic order in the Western Balkans, which primary feature turned to be FDI-led model of the economic development.

Likewise, I have argued that in the case of the Western Balkans the notion of FDI as an ultimate panacea for the economic underdevelopment has been created. Furthermore, FDI has been perceived and represented as the only viable solution to the economic underdevelopment. Dealing with investment, either actual or potential, has blurred side effect of FDI discourse – promoted as the main engine of the regional development, it turned out to be one of the obstacles to stimulating it. My focus in the thesis was primarily the role of domestic actors and their practices in shaping the economic order. An inquiry into different constraints and opportunities set up by different investors for domestic governments and how the domestic actors have responded to them is warranted. In the end, I do not claim that insights into foreign direct investment dynamics exhaust all explanation how the economic order in the Western Balkans has evolved. A deeper inquiry into the labor regulations, financial markets, and production systems are also important in assessing dynamism of the regional economic order, and therefore further research should be undertaken in these directions.

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