

THE IMPACT OF FDI ON ECONOMIC GROWTH AND DEVELOPMENT IN NORTH MACEDONIA SINCE 1991

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After World War II, foreign direct investments (FDI) gained significant importance in the international economy. Considering the increasing global population growth rate, economic growth is viewed as a key mechanism for maintaining the standard of living in society.

According to a group of authors, Borensztein et al. (1998), FDI impacts economic growth by serving as an engine of technological diffusion from the developed world directed toward the target country. However, there are also theorists and studies that prove the opposite, namely the negative impact of FDI on economic growth. According to other researchers, such as Elkomy et al. (2016), based on an empirical analysis conducted across 61 developing and transitioning countries from 1989 to 2013, domestic investments are a more significant driver of economic development in democratic states than FDI.

The Concept and Meaning of FDI

Foreign Direct Investment (FDI) is considered one of the fastest-growing economic activities globally. Many scholars view FDI and multinational enterprises (MNEs) as synonymous. For instance, interchangeably. Dunning and Pearce (1985) state that since multinational enterprises finance foreign subsidiaries

using their funds through the capital market or reinvested profits, these foreign subsidiaries are essentially equivalent to FDI. However, FDI cannot fully capture the activities of multinational enterprises in the best possible way (Hennart 2001, in Rugman and Brewer 2001). FDI represents just one of the many activities conducted by multinational enterprises. Specifically, “a multinational enterprise provides intra-company linkages... it is not merely a channel for single transactions but serves as a foundation for various types of internal and external organizational relationships” (Wilkins 2001, in Rugman and Brewer 2001).

The standard OECD definition (1996, :7) describes FDI as an enterprise in a particular country that has a degree of control over another enterprise in a different country, as opposed to merely providing financial capital. It is defined as “an investment that establishes, withdraws, or acquires a long-term interest in an enterprise operating in an economy” outside the investor’s country, with the aim of “having an effective voice in the management of the enterprise.” The IMF/OECD (1999) recommend a minimum ownership threshold of 10% for an investment to qualify as direct. However, this threshold varies between countries. For instance, in the United States, Australia, and Canada, the minimum is 10%, while in Germany and France, it is 20%, and in New Zealand, 25%. This variation indicates that any potential comparison of FDI statistics across these countries would be inconsistent (Dunning, 1993). Table 1 presents the procedure recommended by the OECD for calculating FDI:

Table 1. OECD Benchmark Definition of FDI

Foreign Direct Investments (FDI)	
equals	Retained earnings (i.e., the share of direct investors in the profits/losses)
plus	Direct investors purchase part of the company’s stock sale
plus	Net increase in long-term and short-term loans, credits, and other amounts provided by the direct investor to the foreign company
minus	The foreign company borrows money from the host country or from its own resources to give to the direct investor in the home country

Source: Walker, J. (1983). „OECD Benchmark Definition of Foreign Direct Investment.“ Statistical News, 61.1-61.4 and Office for National Statistics (1996).

In Table 1, FDI is calculated as the sum of four components: retained earnings, equity capital, intra-company loans, and intra-company liabilities. The above definition of FDI provides a benchmark calculation that offers a degree of transparency when comparing international flows of direct investment. However, in

practice, calculating FDI is very difficult. This is due to the varying laws and regulations in different countries regarding how to measure the components of FDI. Examples include measuring intra-company loans, the timing of investment project realization, the implementation of internationally agreed guidelines for measuring the balance of payments, and the lack of data for many developing countries (Stocker, 2000). As an alternative method for measuring the volume of FDI in a country, employment data or sales from foreign companies can be analyzed. FDI is increasingly concentrated in the hands of a large number of companies, known as multinational enterprises.

According to UNCTAD (2019), in 2016, multinational enterprises and their foreign subsidiaries generated one-third of global GDP and accounted for two-thirds of international trade. Due to their economic importance, many governments offer subsidies and tax breaks to attract multinational enterprises, and consequently, FDI. In 2014, total global FDI reached 1.23 trillion USD, a 16% decline compared to 2013, when it reached 1.47 trillion USD (UNCTAD, 2015).

According to UNCTAD (2017), there were approximately 100,000 multinational enterprises (MNEs) worldwide. The year 2013 is significant for FDI because it marked a record 52% of total FDI inflows going to developing countries, surpassing FDI inflows to developed countries for the first time in history. Additionally, for the first time in the global rankings of the largest FDI recipients, 9 out of the top 20 ranked countries were from developing nations.

Global FDI flows experienced a 13% decline in 2018, reaching 1.3 trillion USD, compared to 1.5 trillion USD in the previous year, 2017. The decline in FDI occurred despite the announced growth in the value of greenfield investments, which increased from 698 billion to 981 billion USD. Although FDI flows declined in developed countries and transition economies, they remained stable in developing countries, increasing by 2% (UNCTAD, 2019).

The COVID-19 pandemic is the largest crisis humanity has faced since World War II, with its impact on the global economy far surpassing that of the 2008 financial crisis (Duan, Zhu, and Lai, 2020). The COVID crisis has caused a dramatic decline in FDI. A global reduction in FDI is projected for 2020 compared to 2019. FDI is expected to return to pre-pandemic levels around 2022. However, despite this drastic decline in global FDI flows during the pandemic, the international production system will continue to play an important role in economic growth and development. Global FDI flows are expected to remain positive (UNCTAD, 2020).

FDI can generate new jobs, but not only that—they can also contribute to improving the skills of employees, as their criteria are typically higher than those of local

enterprises. Additionally, FDI enhances the trade flows of the host country and increases the competitiveness of exports (OECD, 2002). According to Colen, Maertens, and Swinnen (2009), it has been confirmed that FDI impacts growth more through its indirect effects on capital accumulation. Furthermore, FDI plays a crucial role in the transformation of former centrally planned economies into dynamic market systems (Chidlow et al., 2009). During times of economic disruption, it is essential for economic development organizations to focus on their existing investors and do everything possible to maintain their investment (UNCTAD, 2020).

Theories of FDI

Based on the extensive literature, FDI theories can be classified under the following headings:

- **Product Life Cycle Theory by Vernon:** Developed by Vernon in 1966, it was used to explain certain types of FDI carried out by American companies in Western European countries after World War II, specifically in the manufacturing industry. This FDI occurred in Western Europe by American firms between 1950 and 1970.
- **Monopolistic Advantage Theory:** Kindleberger (1969), by expanding on the work of Hymer, developed his theory of FDI based on monopolistic power. Kindleberger argued that the advantages enjoyed by multinational enterprises (MNEs) could only be useful in cases of market imperfections.

The most significant theory for FDI is the FDI Theory Linked to International Trade, where the expansion of FDI in recent decades and the continuous growth of multinational enterprises' production have greatly altered the structure of international trade. According to some measures, FDI has become even more crucial for international trade (Graham, 1996; and Helpman et al., 2003). Numerous attempts have been made to integrate the theory of FDI with the theory of international trade.

In the 1960s, significant technological changes were observed, which coincided with the rise of MNEs. Over time, it became evident that existing theories of international trade were inadequate to explain the changing trade patterns. This ultimately led to a call for alternative explanations of trade flows (Leontief, 1966). In response to this need, Vernon (1966), using multinational data from the United States, explained the cycle of their expansion in the post-World War II period. He argued that FDI is a reaction to the threat of losing markets as products mature, as well as to the need for lower factor costs compared to competition (Latorre, 2008).

Kojima (1973, 1975, and 1985) also integrated trade theories with theories of direct investment. He strongly argued that FDI is necessary to make factor markets more competitive and efficient at the international level, as well as to improve production processes in countries well-equipped with a given resource.

Research by Helpman (1984) and Helpman et al. (2003, 2004) was among others that linked international trade with vertical and horizontal FDI. Helpman (1984) developed a general equilibrium model of international trade in which MNEs play an important role. Helpman et al. (2004) developed a model of international trade where companies choose to serve the domestic market, export, or engage in FDI to address foreign markets. However, the way companies operate in foreign markets will differ depending on their level of productivity. As a result, the most productive companies will decide to serve foreign markets through FDI, while less productive companies will export to foreign markets.

FDI as a Factor Influencing Economic Sustainability

When analyzing the concept of sustainable development, it can be defined as “a type of development that meets the needs of the present without compromising the ability of future generations to meet their own needs” (WCED, 1987). Since the challenges posed in this definition include economic, social, and environmental criteria, with an underlying subjective temporal, cultural, and spatial integration, it does not lead to a better understanding of sustainable innovations. These innovations are seen as “a process in which economic, social, and environmental considerations of sustainability are integrated into the structure of a company, from idea generation to research and development activities and marketing. This applies to products, services, and technologies, as well as new business and organizational models,” evident in the long-term perspective (Charter et al., 2008).

It is worth emphasizing that companies aiming to contribute to sustainable development are predisposed to integrate sustainability into their activities (Labuschagne et al., 2005). Consequently, it can be concluded that innovations are fundamental because this strategy directly contributes to sustainable development, while at the same time allowing companies to reap the benefits of creating new markets and segments (Fichter and Clausen, 2016). This factor is easily observable in the current international sphere, where competitiveness is growing, forcing companies to differentiate and compete on an international level through innovations, with a particular focus on high-tech sectors (Mcgaughey, 2002). This results in a trend that establishes the use of sustainable innovations to achieve win-win situations, where economic and sustainable development are mutually interconnected (Boons et al., 2013).

Companies with greater business support and a stronger economic infrastructure will have more chances for success, which aligns with the claims of stakeholder theory regarding the challenges of corporate sustainability (Porter and Kramer, 2011; Matos and Silvestre, 2013). Although large companies have become aware that their activities can impact sustainable development (Bos-Brouwers, 2010), it should be noted that the innovative process of SMEs differs from that of large companies, mainly due to the lack of economic resources and human capital (Nieto and Santamaría, 2010; Narula, 2004). These shortcomings can be addressed through FDI, which provides knowledge, external capital, and management capacity, generates new employment opportunities, and facilitates technology transfer (Haskel et al., 2007; De Gregorio, 2005; Iamsiraroj and Doucouliagos, 2015).

In support of addressing the shortage of economic resources and human capital, sustainable development has recently become the focus, where through their positioning, FDI can positively influence the well-being of society. Therefore, the scientific community's interest in the impact of this type of investment is shifting, but it can be observed that there is a lack of knowledge regarding the relationship between FDI and sustainability (UNCTAD, 2014; Kardos, 2014).

FDI leads to technological improvements and increases income levels (Lemoine and Ünal-Kesenci, 2004), which can, in turn, affect sustainability issues by increasing human capital and competition, stimulating innovation in companies from the same sector (Vahter, 2010; Kneller and Pisus, 2007). In short, it can be concluded that FDI has a positive effect on economic growth (Tvaronavicius and Tvaronaviciene, 2008).

FDI, through cooperation with SMEs, contributes to making them more suitable for developing sustainability-oriented innovations by meeting technological capacity requirements, thanks to skilled personnel, technological information, and financial capacity, whether through public or private external funds, or through internal funds (Melane-Lavado et al., 2018).

The role of FDI is gaining significance in developing countries, as they are the largest source of external financing for these nations (UNCTAD, 2017). The significant partnership between low- and high-income countries is fundamentally important for effectively addressing sustainability challenges (Caiado et al., 2018). Developing countries are characterized by weak corporate governance mechanisms, high political and economic instability, and a high degree of corruption, which limits their ability to profit from their natural resources (Iamsiraroj and Ulubaşoğlu, 2015).

Attracting FDI is one of the main priorities for countries in the Western Balkans. But not only that, countries like Serbia, Albania, and Bosnia and Herzegovina are taking it a step further, focusing on the sustainability of their economies.

The Role of FDI in Uneven Regional Economic Growth

The relevance of FDI in the global economy has rapidly increased over the past three decades. FDI as a percentage of global GDP grew from 10% in 1990 to approximately 35% in 2016 (UNCTAD, 2017). Estimates suggest that in 2012, the number of multinational corporations (MNCs) worldwide was around 100,000, while the number of their subsidiaries was close to 1 million (Javidan & Bowen, 2013). This exponential growth is increasingly driven by small and medium-sized enterprises (SMEs), which either emerge as global companies or evolve into MNCs. The geography of global FDI recipients and investors has also expanded, with developing economies steadily increasing their share of global FDI flows. For example, in 2014, developing countries accounted for about 55% of total global FDI inflows, meaning more than half. Some metropolitan regions, or “global cities,” exhibiting specific combinations of economic and social openness, coupled with key hard and soft infrastructures and the monopolization of financial and political powers, have acted as key hubs in the global spread of production, technology, and trade networks (Sassen, 2001, 2009; Taylor, 2004). These regions are the primary hosts for knowledge-based MNCs and the true beneficiaries of globalization, serving as centers of political influence, corporate decision-making, control, and the generation and exchange of knowledge, skills, and jobs (Yeung, 2009; McCann & Acs, 2010).

FDI is generally considered an effective form of international economic relations, capable of directly contributing to a significant increase in investment resources in each individual economy. The issue for individual economies is the lack of internal resources, which is why FDI represents an irreplaceable complement, increasing economic growth, affecting employment, improving technological and managerial know-how, and positively influencing other areas of the economy. It is evident that FDI leads to more efficient operations of companies and regions, and indirectly, through spillover effects, generates positive externalities. The competition for attracting FDI is high, and therefore, local economies must create appropriate economic, political, and legislative conditions to increase their inflows.

When highlighting the role of FDI in the economy, it is essential to consider its impact on regional development and the reduction of regional disparities. It can be said that the entry of a large foreign investor into a country automatically

increases the regional GDP, boosts employment, and improves the overall business environment in terms of enhancing managerial skills, organizational structure, workforce education, etc. (Stachová and Stacho, 2016, 2017; Gozora and Hudáková, 2014).

The results of a study by Mbekeani (1997), which investigates the role of foreign capital in the growth process of developing countries, imply that FDI is more likely to be directed towards high-growth regions and regions characterized by high-income levels. The market size, represented by the GDP level, is very important when determining FDI inflows into all regions and countries.

In North Macedonia, the Law on Balanced Regional Development defines balanced regional development as a process of identifying, encouraging, managing, and utilizing the developmental potentials of planning regions and areas with specific development needs to reduce disparities in the level of development within and between planning regions. Over a decade, the policy for promoting balanced regional development has been implemented through the Strategy for Regional Development of North Macedonia, a long-term planning document that establishes the principles, goals, and priorities of regional development in the country and defines the measures, instruments, financial, and other resources for their realization.

The creation of a productive, innovative, competitive, and dynamic SME sector in each planning region directly contributes to increasing the region's attractiveness and retaining the population, especially young people and women, in the planning regions. At the same time, it enhances the regions' attractiveness for domestic and foreign private investments. Over 99% of all active business entities are SMEs, contributing 77% to the total gross added value of North Macedonia's economy, with an almost identical percentage of employed individuals.

Regarding the institutional framework for attracting FDI, it is centralized. The Directorate for Technological-Industrial Development Zones (TIDZ) plays a leading role in attracting foreign investors. TIDZs are distributed across the country, except in the Vardar Planning Region. However, regional disparities can be observed in the number of zones, the size of investments, the number of companies operating within the zones, and other factors.

Table 2. Total Number of TIDZs by Regions

Planning Region	No. Of Zones	City
Vardar	0	
East	4	Zone Štip/Berovo/Vinica/Delčevo
Southwest	2	Zone Kičevo/Struga
Southeast	3	Zone Strumica/Gevgelija/Radoviš
Pelagonija	1	Zone Prilep
Polog	1	Zone Tetovo
Northeast	1	Zone Rankovce
Skopje	3	Zones Skopje 1/2/3

Source: Calculations based on input data from www.fez.gov.mk/

In the section of priorities within the Regional Development Strategy 2020-2030, a significant focus is placed on attracting FDI to TIDZs, a process that has resulted in solid economic effects. In the context of smart specialization, the interest of foreign investors highlights the need for targeted development of knowledge and skills related to the production of automotive parts— a non-traditional economic sector for the country, which has nonetheless attracted the largest and most significant greenfield investments. This leads to the realization that the package of incentives in TIDZs was crucial in the decision-making process for investing, despite the current state of the quality and relevance of skills and knowledge, or the contribution of the existing human capital in the planning regions.

On the other hand, these very greenfield investments in TIDZs are characterized by high productivity and the use of advanced technologies. As a result, they contribute not only to increasing exports, foreign exchange reserves, and reducing unemployment but also to improving human capital and modernization. This, in turn, enhances the competitiveness of the domestic private sector, SMEs, and the service sector in the planning regions while aligning them with the real needs of foreign investors.

To implement this critical priority, i.e., attracting FDI to TIDZs, the following measures have been determined:

- Introducing specific measures (tax exemptions and similar incentives) to direct private investments toward less developed planning regions;
- Improving the conditions for starting a business:
 - Lowering the initial capital for company formation: According to the current legal regulations, the initial capital required for establishing a

company is the same across the entire country. The initial capital in economically underdeveloped planning regions should be lower to encourage individuals with business ideas to establish companies;

- Providing enterprises with access to: 1) **Informal sources of funding**, especially informal venture capital, i.e., business angels (through the adoption of a law on business angels); and 2) **Formal sources of funding**, focusing not only on mobilizing money through banks and the stock market but also paying greater attention to formal venture capital and developing the operations of investment funds;
- Establishing an information system to provide individuals who want to start a business with all the necessary information to realize their ideas;
- Tax exemptions for all newly established private enterprises formed by youth under 30 years old or women, up to a certain revenue threshold;
- Direct support for youth and women's entrepreneurship through grants for starting a new and independent business;
- Creating statistics to monitor women's entrepreneurial (business) activity.

According to the Regional Development Strategy 2020-2030, considering the need to place greater emphasis on attracting private investments in the next decade, particularly in planning regions lagging in development, special attention should be given to business centers established within the development centers of planning regions. These centers should be entrusted with a more substantive role in mobilizing and attracting domestic and foreign investments and playing a more concrete role in distributing public funds to support entrepreneurship. Additionally, they should ensure more efficient access, particularly for women and young people, to the labor market at the planning region level.

To implement this priority, the following measures have been established:

- Organizing regional forums as a regular practice to involve all stakeholders in the planning regions, particularly representatives of socially vulnerable groups, youth, and women (with 50% of participants being women), in the prioritization and selection of regional projects.
- **Implementing capacity-building activities** for the development centers of planning regions and supporting the business centers established within them.
- Enhancing the capacities of employees in the development centers of planning regions regarding the collection, analysis, and monitoring of

gender-disaggregated data and indicators, as well as their application in shaping policies for balanced regional development.

The Role of FDI in Local Economies: Direct and Indirect Impacts

Foreign Direct Investment (FDI) is one of the fastest-growing economic activities. In 2014, global FDI flows reached \$1.23 trillion, representing a 16% decline compared to 2013, when they peaked at \$1.47 trillion. Notably, 2013 marked a significant year for FDI, as, for the first time, 9 out of the top 20 recipients of FDI were developing countries. Global FDI flows experienced a 13% decline in 2018. This drop occurred despite an announced increase in the value of greenfield investments, which rose from \$698 billion to \$981 billion.

While FDI flows declined in developed and transitioning economies, they remained stable or even increased by 2% in developing countries. Despite the dramatic reduction in global FDI flows during the COVID-19 pandemic, the international production system continues to play a critical role in economic growth and development. Global FDI flows are expected to remain positive.

Apart from these trends, FDI represents a force that directly contributes to economic growth, fosters development, facilitates the free transfer of technology to less-developed countries, and promotes the adoption of best practices in corporate governance (UNCTAD, 2015; 2019; 2020).

The concept of FDI has been analyzed by numerous theorists. Many view FDI as a driver of growth (Simionescu, 2016; Alzaidy et al., 2017; Begum et al., 2018; Caesar et al., 2018). According to Almfraji and Almsafir (2014), FDI is generally perceived as a composite package of capital and technology that can enhance economic growth through spillover effects, both direct and indirect. Furthermore, Colen et al. (2009) confirmed that FDI impacts growth more significantly through indirect effects than through a direct increase in capital.

The Internationalization of Markets and the Role of FDI

The globalization of markets has encouraged enterprises to develop various approaches to international business, resulting in extensive activities such as Foreign Direct Investment (FDI). The International Monetary Fund (IMF) defines FDI as an investment involving a long-term relationship that reflects a lasting interest of an entity resident in one economy in an entity resident in a different economy. According to the World Bank, FDI refers to net inflows of investments aimed at acquiring a lasting managerial interest—defined as 10% or more of voting shares—in a company operating in an economy different from that of the

investor. These investments can further be categorized into equity capital, reinvestment of earnings, and other long-term and short-term capital, as reflected in the balance of payments of the respective economy.

FDI is generally regarded as a composite package of capital and technology that can enhance the existing knowledge reserves of the local economy through labor training, skill acquisition, diffusion, and the introduction of new managerial practices and organizational arrangements. It can be concluded that FDI has the potential to influence economic growth both directly and indirectly (De Mello, 1999).

Theoretically, FDI impacts growth directly by contributing to capital accumulation and integrating new inputs and foreign technologies into the production function of the local economy. Empirically, neoclassical and endogenous growth models are widely used to test these theoretical benefits of FDI. However, the results are varied (Almfraji and Almsafir, 2014).

The literature treats economic growth as one of the key mechanisms for at least maintaining the standard of living in society. Therefore, significant effort is invested in analyzing FDI as a factor directly influencing growth. However, there are also theorists and studies that prove the opposite, namely the negative impact of FDI on economic growth. Li and Liu (2005) analyzed panel data from 84 countries worldwide during the period from 1970 to 1999, presenting a significant endogenous relationship between FDI and economic growth starting in the mid-1980s.

In the study by Borensztein, De Gregorio, and Lee (1998), it was found that in the regression framework among 69 less-developed countries during the period 1970–1989, FDI influenced growth not only directly but also indirectly through its interaction with human capital. Additionally, FDI contributed more to growth than domestic investments, and this had a positive effect on increasing those domestic investments.

From panel data coming from 18 Latin American countries, it can be concluded that to achieve a positive effect from FDI, a country must have an appropriate level of economic stability, a liberalized capital market, and human capital (Ben-go and Sanchez-Robles, 2003). Considering the fact that the global economy is driven by large enterprises, the benefits for SMEs from cooperation with MNCs are often indirect, such as through the relationships created with larger companies or through the transfer of knowledge that facilitates the adoption of best work practices (Lembcke and Wildnerova, 2020).

FDI can be an important stimulus for economic development and the creation of new jobs, both locally and nationally. FDI can create new jobs in a region as

foreign enterprises relocate their production to a certain area and can increase aggregate productivity through various channels. In addition to direct impacts, there is hope and expectation that FDI generates additional positive spillovers. The demand for goods and services from other local enterprises can create benefits in the direction of realizing more employment and increased productivity. Local enterprises can acquire knowledge about various technologies and production processes brought by FDI, which can, in turn, stimulate productivity growth in local sectors.

FDI can create direct positive effects on an acquired local enterprise and thereby raise the prosperity in the region by increasing the productivity of the local workforce as well as potentially generating additional employment.

Attracting FDI is on the agendas of practically all governments worldwide (OECD, 2018). There are many reasons why foreign investments are attractive to national and local policymakers. These investments tend to be relatively large and create a significant number of new jobs in a country.

Spillovers from MNCs into the local economy represent an additional and indirect channel and are often a significant justification for policies aimed at attracting FDI. The transfer of technology or knowledge and its impact on innovation, along with job creation, are among the main priorities of investment promotion agencies used by countries and regions to promote FDI (OECD, 2018; UNCTAD, 2014). Connections with MNCs can also facilitate access to international markets. MNCs and their foreign affiliates account for half of global exports (Cadestin et al., 2018), while only a small number of local SMEs export directly. The contribution of SMEs to exports is indirect, i.e., as suppliers of goods or services to exporting enterprises (Miao and Fortanier, 2018). Therefore, having local access to foreign affiliates can create opportunities for enterprises to enter international markets.

Connections with MNCs also create the potential for local enterprises to upgrade their technological capacity, as MNCs are incentivized to invest in upgrading the capacities of enterprises within their supply chain.

Given the potential benefits of FDI, it is not surprising that policymakers have developed an extensive list of options to support the process of attracting FDI. Investment incentives typically include regulatory, financial, and fiscal measures. Regulatory exemptions often relate to easing environmental, labor market, and social requirements for investors. Financial incentives can include direct subsidies, such as for capital investments or wages, as well as support measures, such as investments in infrastructure or training, or implicit support, such

as administrative assistance. Fiscal incentives may involve direct corporate tax exemptions but also include various allowances, tax credits, or other reliefs (OECD, 2003).

In practice, incentives, especially tax reliefs, can represent a significant cost for countries, regions, and local governments while failing to deliver the desired benefits for the local economy. Instead, a targeted approach granting tax incentives based on supplier engagement appears to be an effective policy choice when accompanied by indirect measures supporting the skill and capacity development of workers in local enterprises (OECD and UNIDO, 2019).

The returns from stimulating technological adoption or productivity growth in local enterprises are not confined to the investing enterprise. This has two important implications. First, investments may fall below the socially optimal level. Second, FDI policies should not focus solely on attracting FDI but should consider additional measures supporting domestic enterprises to leverage the opportunities brought by FDI (Lembcke and Wildnerova, 2020).

The impact of FDI on the economic growth of local economies can have both direct and indirect effects. FDI can contribute to economic growth through the expansion of capital accumulation and technological progress. Following the traditional neoclassical growth approach, this capital accumulation can influence growth only in the short term (Solow, 1956 and 1957). Long-term growth is achievable only through sustained increases in technology levels. However, newer growth models view technology as endogenous and consider capital to play a role in driving technological progress (Romer, 1990).

Capital enables investment in developing new ideas and skills, and since knowledge, at least to some extent, is a public good, it elevates the technological level not only within the enterprise but also at the economy-wide level. According to new growth theories, capital—including FDI—can permanently impact production growth by increasing investments in technology and know-how, enhancing the overall level of knowledge and technology within the economy.

The indirect effects of FDI on economic growth can be classified into two main categories. Blomström and Kokko (1998) identify two types of spillover effects from FDI to local economies: productivity spillovers and market access spillovers. Productivity spillovers occur when the entry of MNCs into the host country leads to productivity or efficiency gains in local enterprises. Market access spillovers happen when the entry of MNCs improves export market access for local enterprises.

Economic theory suggests that FDI can generate positive spillovers to local enterprises in the host country. In recent decades, FDI has been regarded as a force

that directly and indirectly impacts economic growth. FDI is highly beneficial for market development, primarily because foreign entrepreneurs bring significant innovations. Additionally, they introduce or promote new technologies, products, management practices, and skills in the host country.

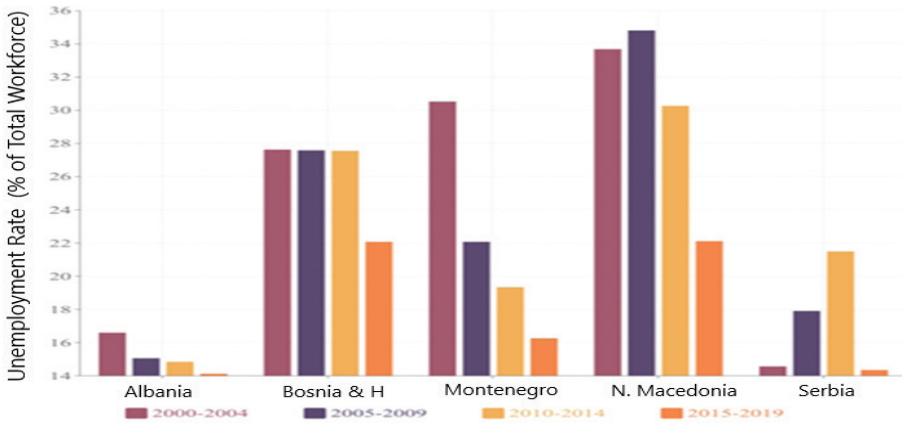
Developmental Effects of Policies and Collaboration Models in Western Balkan Countries

Trends in FDI Movements in Western Balkan Countries

Positive trends in the form of macroeconomic improvements, economic reforms, and rapid growth in the Western Balkans began with the new millennium. The region also experienced significant improvements in international trade within the region and with the EU following trade liberalization and privatization processes. Consequently, this led to an increase in FDI inflows into the region, which was not the case before 2000. In addition to FDI inflows originating from EU countries, significant investments were made by countries such as Norway, Turkey, and Canada. It can be noted that most of these FDI inflows were concentrated in services such as banking, telecommunications, retail trade, and real estate investments rather than in manufacturing sectors. This resulted in a limited contribution to the economic growth of the region. Positive trends came to a halt in 2008 due to the global financial crisis, exposing the vulnerabilities and structural issues of the countries. The region experienced economic stagnation, and recovery began only in 2011. Despite this situation, the prior privatization process facilitated the integration of the Western Balkans into the EU. However, the region faced another recession triggered by the Eurozone debt crisis (Uvalić, 2010, 2013).

These challenges further exacerbated the difficult conditions in the region. Several structural problems persisted, such as rising current account and trade deficits stemming from inefficient policies, weak infrastructure, and uncompetitive local enterprises struggling in global markets (Estrin & Uvalić, 2016). Moreover, analyzing the period from 2000 to 2019, the region faced high unemployment rates, significantly higher than EU member states. For instance, North Macedonia recorded the highest unemployment rate, which stood at 33.7% during 2000–2004, decreasing to 22.13% during 2015–2019. Similarly, unemployment in Albania dropped from 16.62% to 14.14%, in Bosnia and Herzegovina from 27.65% to 22.09%, and in Montenegro from 30.54% to 16.28% during the same period. In Serbia, the unemployment rate was 14.58% during 2000–2004, with an upward trend until 2013, after which it improved, reaching around 14.36% during 2015–2019.

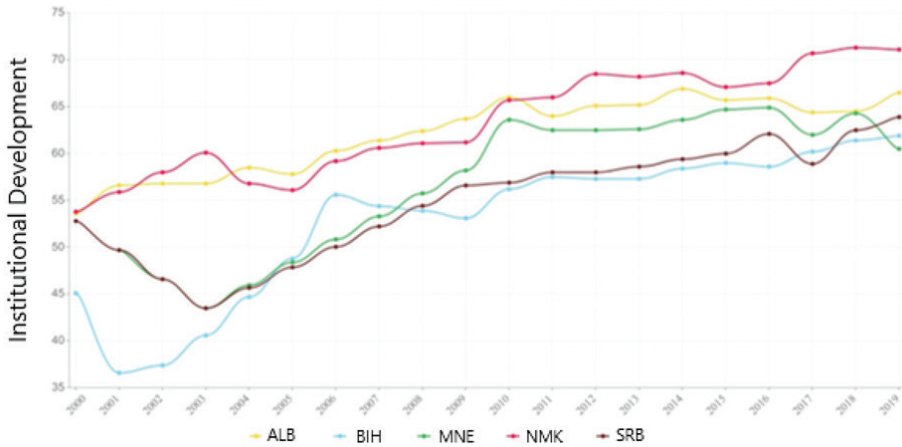
Figure 1. Unemployment Rate in Western Balkan Countries (% of Total Workforce)



Source: International Labour Organization (2020), ILOSTAT database.

As Western Balkan countries undergo significant institutional changes over the years, the processes and conditions in these countries differ considerably. Despite the implementation of numerous changes and reforms, many of which were sponsored and supervised by EU representatives and institutions, numerous institutional issues still hinder FDI inflows and economic growth (Popovic et al., 2020). Chart 2 illustrates a steady improvement in the institutional development of Western Balkan countries, with North Macedonia emerging as the leading country. According to the overall institutional development scores by the Heritage Foundation, the lowest point was recorded in Bosnia and Herzegovina in 2001 (36.60), while the highest point was in North Macedonia in 2018 (71.30), with the regional average being 58.07. During the same period, the lowest score among EU member states was recorded in Bulgaria in 2000 (47.30), while the highest was in Ireland in 2007 (82.60). However, it is worth noting that the gap between EU member states and Western Balkan countries has been narrowing over the past decade, indicating significant convergence in institutional development between the two regions.

Figure 2. Institutional Development in the Western Balkans (Overall Score)

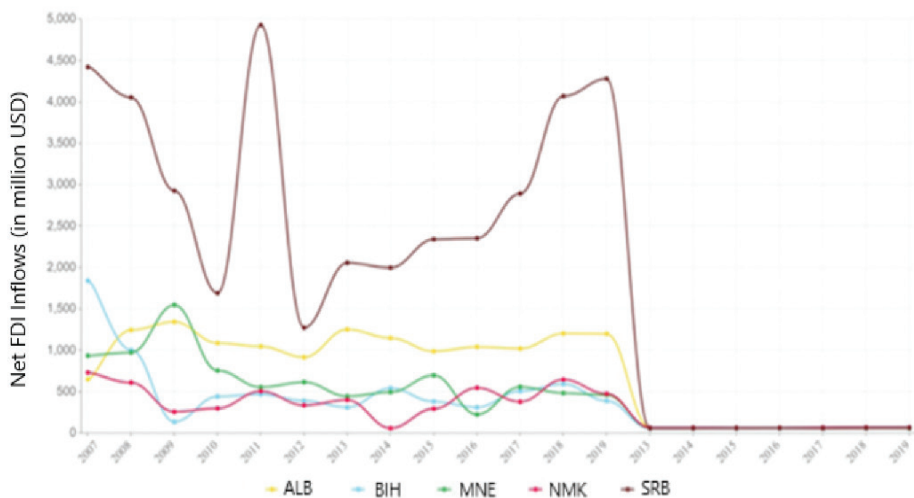


Source: The Heritage Foundation. (2022). Index of Economic Freedom 2022

Although the region has witnessed relative improvements in overall institutional development, this progress has not significantly aided the process of attracting FDI for further development. The low growth rate and competitiveness of the region, combined with high unemployment rates, the lack of effective institutions, and inadequate infrastructure, are some of the primary reasons for the lack of investment inflows in the region (Popovic et al., 2020). According to the 2020 Doing Business Index published by the World Bank, North Macedonia ranked the highest at 17th place, followed by Serbia at 44th, Montenegro at 50th, Albania at 82nd, and Bosnia and Herzegovina at 90th.

Chart 3 illustrates the trend of FDI in the Western Balkans. Since 2007, Serbia has attracted more FDI than all other countries in the region combined. However, a sharp decline in FDI inflows has been observed in the region since 2013. From that point onward, FDI inflows in the Western Balkans remained low, accounting for less than 9% of GDP.

Figure 3. Net FDI Inflows (in million USD)



Source: International Monetary Fund (2020), Balance of Payments database

As seen in Table 2, which presents FDI inflow values for the period from 2019 to 2021, the Western Balkans region experienced a decline in inflows in 2020 compared to the previous year, followed by a return to a positive trend in 2021. Additionally, the significant FDI inflows realized by Serbia are also noteworthy.

Table 3. FDI Inflows in the Western Balkans (in million euros)

	2019	2020	2021	Total
Albania	1.072	937	1.032	3.041
Bosnia and Herzegovina	388	364	445	1.197
Montenegro	255	346	415	1.016
Kosovo	372	466	590	1.428
North Macedonia	488	28	615	1.131
Serbia	3.815	3.039	3.863	10.717
Western Balkans	6.390	5.180	6.960	18.530

Source: The Vienna Institute for International Economic Studies (2022)

For the countries of the Western Balkans, the 1990s can be considered a lost decade because the region remained deeply entrenched in political and economic crisis as a result of the prolonged conflict that accompanied the breakup of Yugoslavia, along with the external embargo and sanctions, double-digit negative growth rates, uncontrolled inflation, unstable exchange rates, and

non-market-oriented policies. As a result of all this, the 1990s in the Western Balkans region were marked by a deep recession. Real GDP dropped by as much as 50% in Bosnia and Herzegovina and in the Federal Republic of Yugoslavia, which today represents Serbia, Montenegro, and Kosovo, while in North Macedonia, real GDP decreased by 25%. At the same time, it can be noted that the region made slow progress in terms of structural reforms and very limited domestic and foreign investments (EBRD, 2003).

From 1989 to 2002, the first wave of large privatizations in the Western Balkans region was carried out through FDI, most of which were in the service sector. Despite this, real revenues from FDI were small, not only because only a few foreign companies entered the region at that time, but also due to the fact that these privatizations were carried out at very low prices as a result of high-risk premiums associated with investments in these economies during that specific period (EBRD, 2003; OECD, 2003a).

FDI in manufacturing remained quite limited throughout most of the first decade of the 21st century because the region's competitive position remained weak. Although it can be noted that FDI significantly increased in the run-up to the global financial crisis, only 10-15% of them were concentrated in manufacturing, mainly related to the privatization of commodity-based industries such as mining, metals, oil, etc. (EBRD, 2010).

The entry of banks from Western countries into the markets of the Western Balkans region, along with the abundance of cheap credit, sparked a consumption boom, which constituted the majority of GDP growth in the pre-crisis period, but this generally had a negative effect on the competitive position of these economies. Capital inflows spurred an increase in wages, which, however, were not aligned with productivity growth, resulting in a weakening of the external competitive position of these economies in terms of labor costs. Furthermore, the growth driven by credit-fueled consumption likely acted as a disincentive for more aggressive pursuit of economic reforms (IMF, 2016).

The global financial crisis, which hit the Western Balkans in 2009, exposed the flaws of the pre-crisis growth model of the region. Over time, the cheap credits from Western banks dried up, while the economies of the Western Balkans faced serious difficulties in trying to find alternative sources of growth. Attracting investments, particularly in the productive sectors of the economy, became an even greater challenge due to the unfavorable external environment, i.e., the global economic and financial crisis, as well as the weakened external competitive position of the region. After the 2009-2012 crisis, the regional GDP of the Western Balkans grew by only 0.5% of GDP (IMF, 2016).

The liberalization of foreign trade regimes since 2001 led to a much faster increase in imports, mainly from the EU, than in exports, due to the limited competitiveness of Western Balkan products in external markets. The external imbalance peaked in 2009, when the Western Balkan countries had nearly the highest current account trade deficits among all countries in Central and Southeastern Europe. However, since 2011, the external imbalance has improved. In some countries, export-led growth policies, linked to increased FDI inflows into the manufacturing sector, led to a significant reduction in the trade deficit for goods and services. Other countries, particularly Kosovo and Montenegro, were less successful and continued to run large trade deficits for goods and services.

ANALYSIS OF THE IMPACT OF FDI ON THE LOCAL ECONOMY IN NORTH MACEDONIA

Historical Overview of FDI Models and Effects in North Macedonia

FDI in North Macedonia has not always been given the importance it holds today, nor was it a priority in the past. Up until 1998, FDI figures in North Macedonia were relatively insignificant. This is evident from the fact that, in 1995, FDI in the country amounted to less than 10 million euros. Since then, FDI has gradually increased, becoming increasingly significant and influential in the economy of North Macedonia. By 2001, FDI had reached a value of 400 million euros. This rapid increase was largely driven by the acquisition of major domestic companies and banks by foreign investors during the privatization process. A record-breaking acquisition was made by Magyar Telekom, part of the Deutsche Telekom Group, which took over the national telecommunications operator.

This upward FDI trend in North Macedonia experienced a sharp decline due to the 2001 conflict. As a result, total FDI in 2002 and 2003 barely reached 100 million euros. However, due to strong efforts and determination to achieve economic and political stability in North Macedonia, supported by significant international assistance, FDI began to show an upward trend starting in 2004.

Between 2006 and 2008, a new significant wave of FDI was recorded in the country, primarily as a result of several privatizations in the energy sector and greenfield investments in the free economic zones. Following this positive FDI trend, the global economic crisis led to a decline in investment inflows in 2009. In 2010, only slight signs of recovery and renewed investor interest were observed, with FDI levels showing a minimal increase compared to the previous year.

Table 4. Foreign Direct Investment Inflows by Country on an Annual Basis

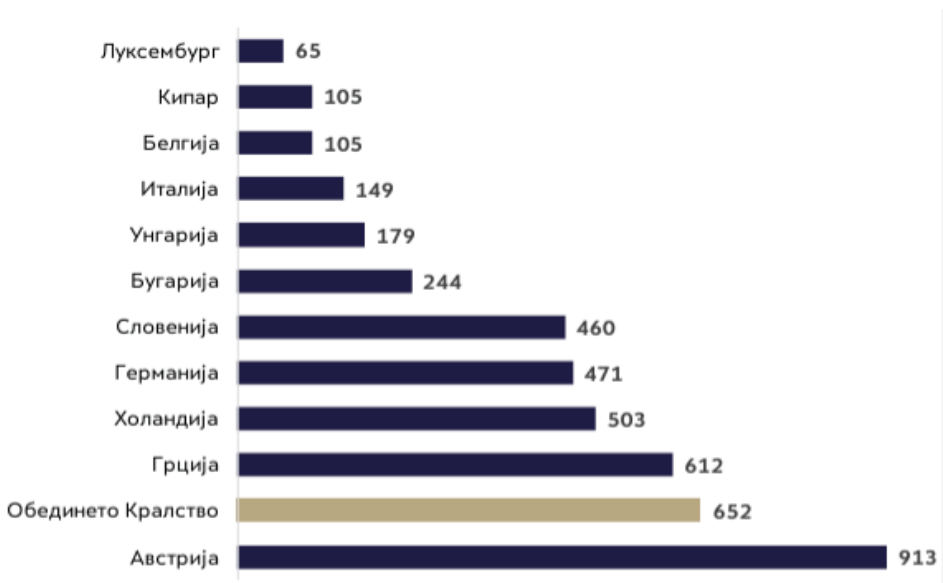
	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €
Total	512.0	201.42	398.76	614.08	181.73	338.43	216.72	205.14	252.2	111.22	344.41	160.47	144.97	399.89	505.97	344.82
Largest Countries – Investors																
United Kingdom	-79.68	120.65	-78.73	204.78	22.74	50.26	-37.63	39.19	45.13	0.46	-59.25	31.62	-45.84	38.02	40.49	12.1
Austria	101.48	34.17	31.37	49.27	29.47	35.21	18.01	26.19	56.26	47.71	48.12	-10.64	30.07	95.69	10.79	130.9
Germany	74.64	20.65	48.59	46.62	47.59	48.47	39.28	45.83	31.97	12.05	10.71	11.93	2.91	4.01	9.32	0.57
Greece	66.51	28.88	29.68	23.58	27.14	-15.69	43.75	-3.25	-0.91	2.10	14.78	15.18	-57.15	6.72	44.58	40.68
Netherlands	26.72	-46.20	-1.80	48.92	-37.58	10.96	94.45	40.15	37.10	8.11	136.56	0.47	65.15	2.33	26.54	14.67
Türkiye	54.22	32.32	55.46	33.86	6.62	32.95	27.05	17.05	22.81	23.53	77.12	15.53	4.43	-1.50	2.01	3.90
USA	23.84	8.70	21.12	3.72	-7.04	17.66	13.37	-0.42	3.65	11.35	2.74	-2.22	2.12	9.64	1.61	6.17
Belgium	18.74	-10.02	14.22	6.91	14.55	4.40	16.56	5.46	13.36	14.49	0.77	0.07	0.07	0.13	0.27	0.09
Hungary	-12.20	-13.46	-7.02	-1.86	-0.28	-3.17	-0.59	-1.36	-22.04	-0.10	-0.28	-38.97	-23.59	-8.70	73.04	0.80
Slovenia	60.48	6.79	37.52	37.51	19.36	4.57	-7.68	-6.56	37.98	8.80	19.10	19.70	134.13	79.23	59.97	10.5
Switzerland	-2.90	4.50	-13.50	-12.30	25.06	18.19	3.46	131.68	-8.50	-15.05	-5.76	-41.25	4.64	24.78	30.86	21.27
Bulgaria	31.30	21.45	23.47	11.54	-11.76	17.85	-0.44	-8.07	-2.86	7.10	4.66	31.09	10.52	38.94	25.35	11.70
Croatia	1.32	-6.41	3.11	-12.91	-12.99	2.47	-2.99	0.54	4.61	5.43	8.08	0.09	5.04	17.92	23.50	6.02
Russia	2.13	-5.70	2.68	-7.20	-0.65	11.35	18.10	-0.87	2.31	0.16	6.65	3.54	-0.26	-0.13	0.19	0.01

Source: National Bank of North Macedonia.

Thus, in 2010, FDI reached a value of 160.4 million euros, and by 2011, this figure had risen to 344.4 million euros. This increase in total FDI value was driven by several agreements for new greenfield investments, primarily in free economic zones, with projects commencing implementation in 2012. However, in the same year, FDI levels in North Macedonia declined to 111.2 million euros. In 2013, there was a positive trend in FDI inflows, and according to the 2013 report of the National Bank of North Macedonia, net FDI inflows rose to 252.2 million euros—almost three times higher than in 2012. As seen in Table 4, FDI inflows in 2016 increased to 338.4 million euros, dropped by nearly half in 2017 to 181.73

million euros, and reached an all-time high in 2018 at 614.1 million euros. In 2019, this value fell to less than 400 million euros. In 2020, FDI inflows again decreased, reaching 201.4 million euros, but rose to 512.0 million euros in 2021. Data from 2020 and 2021 highlight that the United Kingdom, with 120.6 million euros, and Austria, with 101.5 million euros, were significant foreign investors. Other notable investors in North Macedonia include countries such as Germany, Slovenia, Greece, Turkey, Belgium, the United States, and Bulgaria. For the period from 1997 to 2021, the total cumulative FDI inflows in the country amounted to 6.298 billion euros. The state of foreign direct investments in North Macedonia by the end of 2021, categorized by country (annual data in millions of euros), is illustrated in Graph.

Figure 18. Foreign Direct Investments in North Macedonia by Country at the end of 2021



Source: National Bank of North Macedonia.

In 2021, investments from the United Kingdom in North Macedonia amounted to a net value of 191.88 million euros. Other countries with the highest amounts of FDI in 2021 were from the EU-27. Thus, 108.54 million euros were invested from Germany, 87.40 million euros from Austria, and 69.14 million euros from Greece. In 2022, 378.99 million euros of FDI originated from EU-27 countries, while 385.71 million euros came from countries outside the EU-27. In 2023, total direct investments in North Macedonia amounted to 616.7 million euros, based

on data from the National Bank. The structure of investments showed net inflows in equity of 274.8 million euros, reinvested earnings of 172.9 million euros, and intercompany debt of 169.1 million euros, which represents a decrease from 745 million euros compared to 2022. In the first half of 2024, FDI inflows into the Macedonian economy reached 535.29 million euros, a 73.5% increase compared to the same period in 2023, when they amounted to 308.51 million euros.

Table 5. Share of FDI in GDP (2009–2021) in North Macedonia

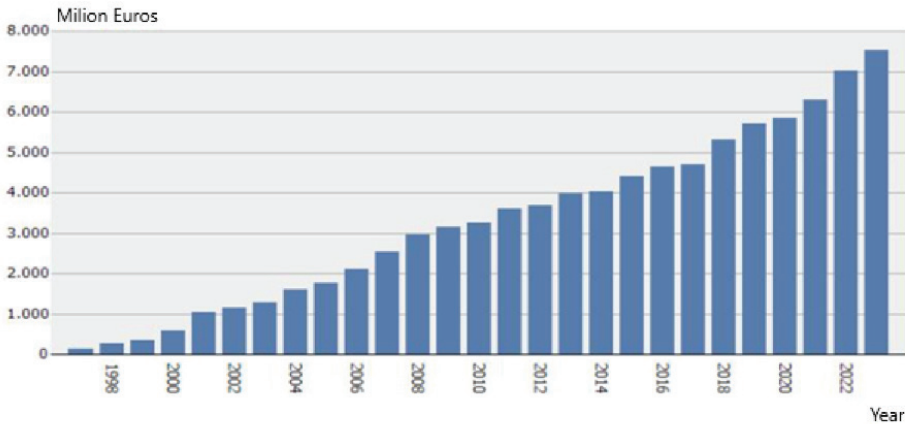
	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009
	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €	Mil. €
Total	512.0	201.4	398.76	614.08	181.73	338.43	216.72	205.14	252.2	111.22	344.41	160.47	144.97
% of GDP	4.37%	1.85%	4.4%	5.1%	3.4%	5.1%	2.9%	0.5%	3.7%	3.5%	4.8%	3.2%	2.8%

Source: National Bank of North Macedonia.

As shown in Graph, FDI in 2009 was estimated at 2.8% of GDP, reached 4.8% of GDP in 2011, dropped to only 0.5% in 2014, then recovered to 5.1% in 2018. However, their share fell to 1.85% of GDP in 2020, followed by an increase to 4.37% of GDP in 2021.

As of December 31, 2023, the total stock of direct investments in North Macedonia amounted to 7,532 million euros (55.2% of the estimated GDP), of which 5,256 million euros were in equity and 2,276 million euros in debt instruments. The highest direct investments were registered from Austria (1,199 million euros), Greece (751 million euros), Turkey (715 million euros), Germany (652 million euros), and the Netherlands (597 million euros), accounting for 51.9% of total investments. By sector, 33% (2,470 million euros) of investments were in “manufacturing,” and 22.9% (1,724 million euros) were in “financial and insurance activities.”

Figure 19. Stock of Direct Investments in North Macedonia



Source: National Bank of North Macedonia

Source: National Bank North Macedonia.

Analysis of the Effects of Existing Models and Practices of Cooperation Between FDI and SMEs in North Macedonia

In North Macedonia, the cooperation between SMEs and MNEs is very limited. This is confirmed by numerous available data and research, including *The Global Competitiveness Report (2016-2017)*. According to the FDI and Technology Transfer parameter, which indicates the level of technology transfer from FDI to the local economy—more specifically, from MNEs to SMEs—North Macedonia ranks 89th out of 135 countries. Additionally, regarding the parameter for technology absorption at the local firm level from FDI, North Macedonia ranks 67th out of 135 countries. These rankings highlight North Macedonia's lack of progress in an area that should represent one of the main benefits of FDI—namely, technology transfer. This is largely due to weak collaboration between local SMEs and foreign MNEs. Furthermore, in the aforementioned FDI and Technology Transfer parameter, North Macedonia showed no progress between 2011 and 2017. Meanwhile, for the firm-level technology absorption parameter, only an 18% improvement was recorded over the same period, which underscores a poor trend.

According to research by Finance Think (2018), it can be observed that local suppliers have minimal collaboration with MNEs operating in North Macedonia. In 2015, the cooperation between SMEs and MNEs in North Macedonia amounted to approximately 46 million euros, while the number of local enterprises collaborating with MNEs was around 500. Compared to the total exports from MNEs in the same year, which amounted to approximately 1.5 billion euros, this value

is significantly negligible. Finance Think (2018) found that only 10% of MNEs' total obligations were directed toward domestic enterprises.

Table 6. provides an analysis of the total export sums from all TIDZs (Technological Industrial Development Zones) across North Macedonia for the period from 2011 to 2021, with data presented for each year separately. An interesting observation from analyzing these figures is the percentage growth of these sums year over year. For instance, the sum of 815.7 million euros in 2013 grew by an impressive 66.7% in 2014, reaching 1,360.2 million euros. This growth rate consistently increased in all analyzed years, except for 2020, due to the COVID-19 pandemic, eventually reaching 3,717.6 million euros in 2021.

Moreover, the participation percentage of exports from TIDZs across North Macedonia in the country's total exports showed a rapid upward trend over the period from 2011 to 2021. Specifically, it grew from 16.3% of total exports in 2011 to surpass half of the total export value for the first time in 2017, reaching 50.04%. This trend continued, reaching 61.7% in 2021.

Table 6. Exports from Operational TIDZs in North Macedonia

Year	Mil. EUR	% growth	% of total exports
2011	523.6	/	16.3%
2012	600.1	14.6%	19.2%
2013	815.7	35.9%	25.2%
2014	1360.2	66.7%	36.3%
2015	1724.9	26.8%	42.2%
2016	2086.9	20.9%	47.5%
2017	2511.8	20.4%	50.04%
2018	3129.6	24.6%	53.3%
2019	3523.2	12.6%	54.85%
2020	3110.7	-11.7%	59.4%
2021	3717.6	19.5%	61.7%

Source: Author's analysis

Note: * total export data for 2020-2021 are projections of the Ministry of Finance.

In Table 7, the total import sums in all TIDZs (Technological Industrial Development Zones) across North Macedonia for the period from 2011 to 2021 can be analyzed year by year. The growth percentage of these sums increased in all years within the mentioned time interval, except for 2020, also due to the COVID-19 pandemic. Over ten years, the value of imports in the TIDZs across North Macedonia grew from 487.1 million euros to 3,346.1 million euros. Between 2013 and 2014 alone, the value

of imports rose from 774.1 million euros to 1,181.6 million euros, representing an increase of 52.6%. The reasons for the increase in imports are often attributed to the shortage or inadequacy of supply options for the raw materials required for the economic activities of MNEs in North Macedonia. The participation of imports from the TIDZs in North Macedonia in the country's total imports also grew rapidly, starting from 9.6% of total imports in 2011 and reaching as much as 41.8% in 2021.

Table 7. Imports in Operational TIDZs in North Macedonia

Year	Mil. EUR	% Growth	% of Total Imports
2011	487.1	/	9.6%
2012	559.8	14.9%	11.04%
2013	774.1	38.3%	15.5%
2014	1181.6	52.6%	21.5%
2015	1460.4	23.6%	25.2%
2016	1724.1	18.1%	27.9%
2017	2122.9	23.1%	31.1%
2018	2551.7	20.2%	33.2%
2019	2998.7	17.5%	35.5%
2020	2647.7	-11.7%	37.8%
2021	3346.1	26.4%	41.8%

Source: Author's analysis.

Note: *The data on total exports for 2020–2021 are projections by the Ministry of Finance.

Table 8. Net Export from Operational TIDZs in North Macedonia

	Export from TIDZ (in mil. EUR)	Import in TIDZ (in mil. EUR)	Net Export (in mil. EUR)	% Growth
2011	523.6	487.1	36.5	/
2012	600.1	559.8	40.3	10.4%
2013	815.7	774.1	41.6	3.2%
2014	1360.2	1181.6	178.6	329.3%
2015	1724.9	1460.4	264.5	48.1%
2016	2086.9	1724.1	362.8	37.2%
2017	2511.8	2122.9	388.9	7.2%
2018	3129.6	2551.7	577.9	48.6%
2019	3523.2	2998.7	524.5	-9.2%
2020	3110.7	2647.7	463.0	-11.7%
2021	3717.6	3346.1	371.5	-19.8%

Source: Author's analysis.

Taking into account the data from the aforementioned Table 8, where the value of imports into the TIDZs is subtracted from the exports from the TIDZs—representing funds that flow into other foreign economies—the net export value is obtained. This value stood at €36.5 million in 2011, increased to €178.6 million in 2014, reached €362.8 million in 2016, and maintained a positive trend until 2018 when it peaked at €577.9 million. Considering that the net export value includes added value, which may comprise cooperation with SMEs as well as the profits of multinational enterprises (MNEs), it can be concluded that the cooperation between local SMEs and foreign MNEs, along with their effect on the domestic economy, is very limited. A crucial data point from the above analysis that requires careful attention is the negative trend in the growth rate of net exports since 2019, which has been worsening annually. While the net export value was €577.9 million in 2018, it dropped to €524.5 million in 2019, representing a decrease of 22.7%. It further declined to €463 million in 2020, an 11.7% drop from the previous year, and reached €371.5 million in 2021, down by 19.8% from the previous year. This continuous negative trend confirms that even the existing cooperation between local SMEs and MNEs is diminishing. Nonetheless, it can be concluded that there remains significant potential to strengthen ties between MNEs and local suppliers (SMEs), thereby increasing the secondary effects of FDI on the economy. According to the National Bank of North Macedonia, the export structure has significantly improved over recent years due to new capacities in the economy. This improvement is based on a gradual increase in the share of products with higher added value in exports, primarily chemical products and machinery and transport equipment, which reached nearly 57% by the end of 2020. These changes in the export structure correspond to foreign direct investments, which in recent years have been primarily concentrated in these industries. On the other hand, a reduction has been noted in the share of traditional export products—iron and steel, and textile products—whose combined share declined from a dominant 40% in 2010 to approximately 16% by the end of 2020. This trend reflects greater production diversification and modernization of the export structure. Regarding the export of iron and steel, despite a decline during the global crisis, its share in total exports stabilized in 2017 due to favorable price trends in the global market and global recovery. It saw modest growth in 2018 and experienced acceleration in 2020 and the first three quarters of 2021.

SMEs in North Macedonia contribute only 36% of the country's total exports, whereas, on the other hand, they account for more than 90% of GDP. An analysis of the geographic orientation of North Macedonia's exports confirms the dominance of the EU as the main export destination, with around 78% of exports

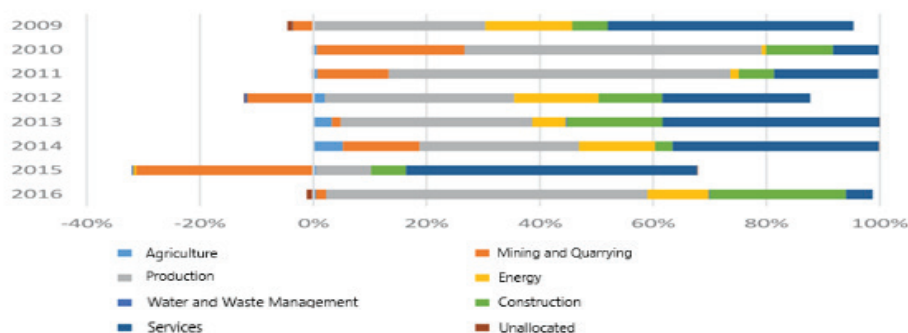
directed to the EU during the January–September 2021 period. This represents a significant increase compared to 2008 when nearly 60% of exports were EU-bound. Within the EU, recent years have seen a notable increase in the share of exports to Germany, with positive developments in exports to Hungary, Romania, and Belgium, albeit from lower initial shares. Conversely, the share of exports to Greece, Italy, and Bulgaria has decreased (Ministry of Finance of North Macedonia; Economic Reform Programme 2022–2024).

According to *The Global Competitiveness Report (2019)*, SMEs in North Macedonia face low investments and poor rankings in several parameters, such as: innovation capacity at the 97th place out of 141 countries, SME financing at the 115th place out of 141 countries, R&D expenditure at the 75th place out of 141 countries, and roads and connectivity at the 91st place out of 141 countries. Hence, it can be concluded that there is a significant gap between the domestic economy and MNEs that focus on higher productivity, technology, and standards.

Industrial and Sectoral Cooperation between MNEs and SMEs in North Macedonia

Despite the fact that cooperation between domestic SMEs and foreign MNEs in North Macedonia is at a very low level, it is evident that some cooperation has already been established. According to the research by Finance Think (2018), conducted during April–May 2018, 81.5% of MNEs operating in our country responded that they cooperate or have cooperated with some local SMEs, compared to 18.5% of them who have not established any cooperation so far. On the other hand, according to the same research, 37.8% of local SMEs have successfully established cooperation with MNEs, compared to 27.0% that have not established any form of cooperation or connection with MNEs. Additionally, 18.9% of local SMEs are in the process of negotiating cooperation, while 16.2% stated that they have had unsuccessful cooperation with MNEs due to various reasons, such as failed or unsuccessful negotiations, terminated cooperation due to non-compliance with agreed terms, etc.

Figure 4. FDI Participation by Industrial Sector



Source: Finance Think (2018). Bridging gaps and seizing potential: Domestic SMEs in the supply chain of multinational companies in the country <http://www.financethink.mk/wp-content/uploads/2018/11/Policy-study-19.pdf>

On Figure 4, the distribution of FDI in North Macedonia by sectors is presented. It can be concluded that from 2009 to 2016, the most attractive sector for foreign investors was the manufacturing sector, with an average concentration of 42.3% of total FDI inflows. The main driver of these investments is the automotive industry and other transport equipment, with an average share of 74.5% in total foreign investments in the manufacturing sector. Other significant drivers of FDI include the service sector, with 41.5%, and the construction sector, with 12.7% of total FDI in North Macedonia.

As shown in the table (Appendix 1), although the cooperation between local SMEs and foreign MNEs is far from a satisfactory level, this cooperation does exist, primarily in the sector that attracts the largest percentage of total FDI in North Macedonia—the manufacturing sector, particularly the automotive industry. Eighteen SMEs from various cities across the country, as a result of FDI and established connections with several renowned foreign companies operating in North Macedonia, such as Johnson Matthey (United Kingdom), Johnson Controls (USA), Kemet (USA), Van Hool (Belgium), Kromberg & Schubert (Germany), Draexlmaier (Germany), EVN (Austria), etc., in various TIDZs (Technological Industrial Development Zones) as well as outside them, collaborate daily and progress through expanding their production and business operations, becoming technologically advanced and certified manufacturers. Local SMEs that are gradually entering the global supply chain firmly adhere to principles of good product quality, competitive pricing, and timely delivery.



APPENDICES

Appendix 1. SMEs from the manufacturing sector – automotive industry collaborating with foreign MNEs

NAME OF SME	CITY	MAIN PRODUCTS	MAIN PARTNERS
1. AKTIVA SHTIP	SHTIP	Production and installation of all types of steel structures, roofs, cladding, and sheet metal.	Johnson Control, Van Hool, Trimo Macedonia, Inter Ingeneering, VIP, Maksima, Tus, Ford, Lukoil.
2. ALATNICA LIVA	SKOPJE	Tools for impact, injection, and vacuum casting of plastic. Tools for cutting, punching, bending, extraction, and extrusion of sheet metal. Tools for extrusion, injection, and cutting of aluminum. Various mechanical components made of steel, aluminum, and brass.	Johnson Matthey, Johnson Controls, Teal Tetovo, Toraks, Praktika MS, Plambeks, Hemiks, SegalPlast Albania.
3. ALATNICA LONOSKI	SKOPJE	Tools. Injection and blow-molded plastic components - custom plastic parts for the automotive and medical industries.	
4. ALGRETA (ALUMINUM FOUNDRY)	RESEN	1. High-precision casting of aluminum and zinc parts for: - the electronics industry - the automotive industry - hydraulics and pneumatics - household items - heating radiators 2. Production of electricity from photovoltaics - installation of photovoltaic stations.	Alukon Germany, Basic GmbH Germany.
5. ARILMETAL	SKOPJE	Production and trade of metal coatings.	Kemet Elektroniks, Johnson Matthey, Sasa, Feni Industry, Makstil, Indo Minerals and Metals, Bucim, Aktor.

6. BRAKO	VELES	- Wire products (mesh, nails, Zn-coated mesh) – MIG-MAG welding wires – Medical aids – Virus equipment – Vehicle frames and metal vehicle parts – Turbine housings – Telecom poles and containers – Bulldozer buckets.	Handicare group –Sweden, Biostrada – Italy, Gugler –Austria, GHE – Austria, LST –Germany, Telecom Austria – Austria, EVN –Austria, PTK Vala-Kosovo, Feroinvest – Macedonia, Nino De Martis – Austria, Ato form – Germany, Weighpack – Netherland, Orlandi – Italy, Dael – Netherland.
7. FABER RDV	SKOPJE	Parts for injection molding. Ventilated parts.	OOO “Impex Ll-c”-Ukraine, Elektron-abava-Slovenia, Tmt Elkom, Kimtech, Mega El-Bulgaria, Enpi, Dule sh.p.k.-Albania, Elektrometal Plus DOO, CableTrade-Serbia.
8. HI-TECH Corporation	SKOPJE	Multilayer printed circuit boards for automobiles, communication, and electronics.	
9. LTH FOUNDRY	OHRID	Production of components for photocopiers and products for vibration protection for OEM.	
10. MZT Engineering	BITOLA	- Processing of parts from metals and lightweight metals, cast from various steel, aluminum alloys, brass, etc. - Servicing machines for machining - Production and installation of special machines (e.g., limousines, impact and bending machines).	Feroimpex Zagreb, LTH Learnica, MZT Learnica, MZT Hepos, Wabtec, Algreta Resen.
11. MZT FOUNDRY	SKOPJE	Production of casting parts for water distribution systems.	GF Waga, Kolk Holland, Hawle, Avk Group.
12. NOVA REFRACTORIES	PEHČEVO	Production of waterproof materials.	
13. ORION ENGINEERING	PRILEP	Design and production of metal molds and tools for manufacturing steel, aluminum, and polymer products, making spare parts for various machines.	Kromberg & Schubert, Draxelmeier, Wabtech, Mikrosam, Vitamin-ka AD Prilep, Komfi Angel, Krin K.G.

14. RADE KONČAR	SKOPJE	Electrical and electronic sector: production of low-voltage energy equipment.	Elem, Tinex, SP Markets, Eling, ATB Beograd, ATS Slovenia, Konvar BiH, Varkon Croatia, Dial Russia, GSMU Turkey, AEP Poland.
15 RUEN INOX AUTOMOBILE	KOČANI	Production of couplings for three types of vehicles: heavy (trucks and buses), tractors, and passen- ger cars.	
16. STD	DOJARAN	Products: Shock absorbers for trucks, buses, trailers, wagons. Machine parts for the automotive industry.	
17. TE-TE PLAST	SKOPJE	Tools and plastic components.	Hella, Webasto, Johnson Matthey, Kromberg & Schu- bert, Draexlmeier, Kemet Electronics, Amphenol.
18. WABTEC MZT	SKOPJE	Production of: - Complete equi- pment for braking systems for rail vehicles (UIC standard) - IBS, reservoirs, valves - Pneumatic control systems.	DB Bahn, GATX, Greenaber, Tulomsas, Alstom, Tudemasas, Bombardier, Zeleznice Srbije, EKK Poland, New York City Subway, GE Transportation, MZ etc.

Source: Author's analysis.

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