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FOREIGN DIRECT INVESTMENT IN SLOVENIA¹

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1. Introduction

Slovenia is one of few countries in the region that has been undergoing a process of double transition, i.e. from socialist into market economy and from a regional (Slovenia as a part of former Yugoslavia) into a national economy. Becoming independent in 1991, Slovenia joined the family of UN organizations in 1992, became the member of IMF and IBRD in 1993, joined GATT in 1994 and, thus, became the member of WTO and its main agreements in 1995, in 1996 European Agreement was signed and Slovenia become member of CEFTA. Slovenia also concluded free trade agreement with EFTA, with Croatia, Macedonia, Estonia, Latvia, Lithuania, Israel and Turkey. Slovenia opened accession negotiations with the EU in 1998; it belongs to the first round candidates for EU membership. Until now Slovenia preliminary closed 21 of the 31 chapters of the *acquis communautaire*, and proved itself as one of the most qualified candidates for EU accession.

Slovenia is a small economy with population of approximately 2.0 million. With GDP per capita of USD 9,105 in 2000, or 72% of EU average in PPP terms, it is the most developed among transition countries of Central and Eastern Europe. After initial transitional recession, reflected in decreasing GDP growth rates, Slovenia succeeded quickly to considerably reduce inflation rate and already in 1993 to regain economic growth. GDP growth rates are expected to remain between 3.5%-4.5% in the near future, and inflation rate is expected to be reduced from 8.9% (annual average) in 2000 to 5.1% in 2003. In the whole transition period, Slovenia has kept more or less sustained fiscal and external balance. After reaching the peak of 9.1% in 1993, the rate of unemployment by ILO has been reduced to 7.0% in 2000 and is expected to be further reduced. 59.0% share of exports of goods and services in GDP (in 2000) demonstrates that the country has a distinctive export oriented economy. This goes primarily for its manufacturing sector. Most of exports are destined for EU. In 2000, 63.9% of Slovenia's exports went to EU (in Germany 27.2%, in

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Italy 13.6% and in France 7.1%), 15.6% to the successor states of the former Yugoslavia (7.9% in Croatia and 4.3% in Bosnia and Hercegovina), 11.2% to transition countries of Central and Eastern Europe (2.6% in Poland, 2.2% in Russia etc.), 4.6% to non-European OECD member countries (3.1% in the USA) etc. (IMAD 2001).

Over the past few years, Slovenia has fully or partially completed a number of structural reforms, such as trade liberalization, privatization of manufacturing, trade and service sectors (with the exception of financial sector and public utilities), bank rehabilitation, introduction of VAT, reform of the pension system etc. Though significant advancement in institutional and structural reforms has been made, Slovenia's economy still has to finish some of them. From the point of view of FDI, the most relevant are the restructuring and privatization of financial sector and public utilities, as well as the ongoing transition restructuring of the enterprise sector encompassing post-privatization consolidation of ownership and establishment of corporate governance in the privatized enterprises, and privatization of companies involved in the government enterprise rehabilitation programs. All these activities will offer ample opportunities for foreign investors to engage in Slovenia.

2. FDI trends and country/sectoral breakdown

Flows and stocks of FDI. FDI stock in Slovenia at the end of 2000 amounted to USD 2,808.5 million. Taking into account USD 199.8 million of FDI inflows in January-August 2001 the present stock of inward FDI in Slovenia stands at about USD 3 billion. Stock of inward FDI in Slovenia in the period 1993-2000 increased from USD 954.3 million to USD 2,808.5 million², that is by 2.9 times. FDI inflows and stock were increasing rather fast all until the end of 1997. Afterwards, Slovenia experienced a slowdown in FDI inflows, which recovered only in 2001. First half of 2001 brought about an important positive change in FDI inflows in Slovenia; in January-August 2001 FDI inflows amounted to USD 199.8 million, compared to only USD 44.0 million in the same period of 2000. Higher inflows are predominantly the consequence of several foreign acquisitions. Until the end of 2001 one can expect continuation of higher inflows of FDI in Slovenia. FDI projects already realized or announced for 2001 indicate FDI inflows in the approximate amount of USD 500 million what would be far the highest annual FDI inflow in Slovenia recorded so far. In the years to come, one can expect the same or even higher inflows of FDI. The major reason for that is the forthcoming privatization of the state property, mostly in financial sector and public utilities. Motivation of the government to involve foreign investors in the forthcoming privatization is strong and is related to strategic development as well as fiscal considerations. Expected participation of foreign investors in the privatization, accompanied by the support of investment incentives policy, embodied in the government Program for the Promotion of FDI in 2001-2004 (TIPO 2001), would eventually have a positive influence on the perception of Slovenia as investment location and, consequently, also on the increase of FDI inflows in general.

2 The decrease of stock by USD 109.3 million in 1999 is predominantly due to high appreciation of USD in that year; in fact, the stock measured in EUR increased by EUR 317.8 million.

TABLE 1: Flows & stocks of inward FDI¹ in Slovenia in 1993-2000²

	1993	1994	1995	1996	1997	1998	1999	2000
VALUES, in millions of USD								
Year-end stock – total	954.3	1,325.9	1,763.4	1,998.1	2,207.3	2,765.8	2,656.5	2,808.5
Equity&reinvested earnings	709.7	966.5	1,203.5	1,274.9	1,559.4	2,011.6	1,893.9	1,883.2
Net liabilities to foreign investors	244.4	359.4	559.8	723.1	647.9	754.2	762.6	925.3
Changes of stock – total ³	n.a.	371.6	437.5	234.7	209.2	558.5	-109.3	152.0
Annual inflow – total ³	112.6	128.1	177.4	194.0	375.2	247.9	181.2	175.5
Inflows from abroad	112.6	128.1	176.0	185.5	320.8	165.4	83.4	83.4
Reinvested earnings	n.a.	n.a.	1.4	8.5	54.4	82.5	97.8	92.1
GROWTH RATES, in %								
Year-end stock – total	n.a.	38.9	33.0	13.3	10.5	25.3	-4.0	5.7
Annual inflow – total	1.4	13.7	38.5	9.4	93.4	-33.9	-26.9	-3.1

Source: Bank of Slovenia.

Notes: 1/ FDI whereby a foreign investor holds a 10% or higher share in a company; 2/ From 1996 onwards direct investments with indirectly affiliated enterprises are also included; 3/ Inflows are in principle smaller than changes in stocks since international payments transactions comprise only part of the changes in stock; most notably, inflows data do not include changes in net liabilities to foreign investors. Furthermore, inflows do not include data on directly affiliated companies. From 1995 onwards data on reinvested earnings are also included in inflows and, thus, in the balance of payments; n.a. = not available.

Investing countries. Investors from EU countries dominate FDI in Slovenia. At year end 2000 no less than 84.0% of total inward FDI stock was accounted by EU countries, the major investors among them being Austria (45.6% of total foreign equity stock at year-end 2000), Germany and France, followed by Italy, United Kingdom and Netherlands. FDI from other EU countries lags behind. Of non-EU countries, only USA, Czech Republic, Switzerland and Croatia are relevant investors. Proximity of Slovenia to the EU and traditionally strong economic co-operation of Slovenia with Austria, Germany, Italy and France are the major reasons for the domination of investors from these countries.

Distribution by economic activity. Manufacturing with 43.1% of total 2000 end year FDI stock is by far the most important recipient of FDI in Slovenia. Inside manufacturing, FDI is heavily concentrated in paper and paper products, chemicals and chemical products, machinery and equipment, rubber and plastic products, and motor vehicles and trailers. Outside manufacturing, FDI is concentrated in trade, financial intermediation and other business services. Industrial distribution of FDI is to a major extent determined by a handful of large (for Slovenian circumstances) FDI projects, which as a rule emerged out of previous co-operation between foreign investor and invested-in Slovenian company.

3. Legal and institutional framework for FDI

1999 was a key year for developments in FDI policy. The government adopted a new programme for the promotion of foreign direct investment, and reinforced this commitment with a number of important legislative reforms. In particular, amendments were made to the *Commercial Companies Act* and the *Foreign Exchange Act*, the only law to deal directly with FDI, was adopted. Together with the *Take Overs Act* of 1997, these three pieces of legislation provide for an open and non-discriminatory legal regime that extends the national treatment secured under the Europe Agreement, which also entered into force in 1999, to all foreign investors. Only a few restrictions similar to those maintained in many OECD countries

remain, such as on investment in the production of armaments, gambling, obligatory public health insurance, essentially based on public order and national security considerations.

The Foreign Exchange Act introduced a general freedom for inward and outward FDI. All residents irrespectively of whether controlled by Slovenian nationals or nationals of a foreign country are in the same position vis à vis performing foreign exchange operations. The Act defines FDI as “all investments made by a foreign investors with a purpose of establishing lasting economic links and acquiring possibility of effective influence on management of a company or other legal entity”. 10% foreign equity share is the one, which formally distinguishes direct from portfolio investment. There are no restrictions regarding the legal status of foreign investors. Both foreign legal persons and foreign natural persons are permitted to invest in Slovenia. In addition, branches are considered as residents and are in respect of investments in the same position as other residents established and operating in accordance with Slovenian regulations.

The Foreign Exchange Act abolished, without prejudice to other laws dealing with establishment, all restrictions regarding FDI, except investments in companies or other undertakings whose activity is production and trading in armaments or the provision of obligatory pension and health insurance financed from the budget. Remaining restrictions, which essentially concern right of establishment in specific sectors (investment funds’ management companies, investigation and security services, gambling, audit, air and maritime transport), will be abolished according to the timetable set out in the Europe Agreement and in The Slovenian negotiation position vis a vis EU.

Registration and business activity permits. No specific registration is necessary. According to the Foreign Exchange Act, FDIs are all investments effected with purpose of establishing permanent economic relations and of gaining possibility of an effective control of a management over a particular company or other legal entity: (i) establishment or capital increase of a wholly foreign-owned company, (ii) establishment of a branch, (iii) acquisitions of existing companies that represent exclusive foreign ownership, (iv) investments intended for performing activities of sole entrepreneurs (natural persons), (v) more than 10% capital participation or more than 10% voting rights in new or existing companies effected with the purpose of establishing permanent economic relations and effective control of management, or (vi) loans with 5 or more years repayment periods with the purpose of establishing permanent economic relations if the credits are considered as subordinate claims and if such loan was given to related companies.

The registration of FDI or the establishment of wholly or partially foreign-owned companies is subject to the same conditions as apply to domestic legal entities. In order to acquire legal status, all kind of investment – establishment of a company, joint venture, (share) acquisition must be registered at the local Court of Justice. In order to begin operations, all businesses in Slovenia must obtain a permit to do business (operating licenses).

Acquisitions. The major piece of legislation in case of foreign acquisitions is the Takeovers Act. This Act requires a potential acquirer in any acquisition of shares with voting rights of 25 per cent or more to publicly announce its acquisition intention and to offer to buy shares of all the existing shareholders at the same price. The Act regulates foreign acquisitions according to the national treatment principle. In the transitional period of five years envisaged by the Act, the government has a special right to intervene in the takeovers of large privatized companies. The Article 83 of the Takeovers Act says “when the value of the share capital of a company/issuer of shares which had undergone the process of ownership transformation exceeds SIT 800 million at the time of taking down the legal effects of ownership transformation in the court register, a special permission issued by the government of the Republic of Slovenia on the proposal of the Ministry of Economic Relations and Development is required to acquire more than 25 per cent of the shares of individual issuer, issued pursuant to the Ownership Transformation Act”. This right of the government expires within 5 years from the day of entry into the court register of the legal consequences of

the ownership transformation of a company, which is a target of a takeover. Since the process of ownership transformation has been completed, also this right of the state has been progressively expiring, and will no longer apply after 2003.

The Companies Act. The framework for doing business is essentially determined by the Companies Act which does not contain any specific stipulations as far as foreign investors is concerned meaning that no distinctions are made on the basis of foreign ownership. The Companies Act provides for three types of companies, i.e. joint stock company, limited liability company and limited partnership by shares, and for three types of partnerships, i.e. limited partnership, general partnership and silent partnership. The Act also provides for the establishment of interest groupings and foreign company's branches.

No ratio of domestic to foreign investment is prescribed and all combinations are possible. The Companies Act specifies only the minimum founding capital for a company in absolute figures, which is applicable to all companies. It also specifies the proportion of the founding capital, which should be paid in at registration. The capital contributions may be in cash, rights, or in kind. At least one third of the founding capital must be contributed in cash. The importation of goods as a foreign contribution to equity capital is unrestricted. Cash contributions may be in foreign currency or in Slovenian Tolars. A foreigner may also invest Tolars deriving from his share of the profits and of the assets of a company which has been liquidated. There are no special conditions, other than those applicable to domestic investors, on the investment of rights by foreign investors. The Companies Act is fully harmonized with the *acquis communautaire* in the respective field.

There are no restrictions imposed either on the management, proxies or composition of company boards. Managers and board members in foreign investment enterprises can be foreign nationals. There are also no requirements relating to the choice of language employed by management in a company.

Branches. Foreign investors may establish a branch in Slovenia if they have been registered in their own country of origin for at least two years. Branch offices cannot be legal entities. The branch performs its business activities in the name and on behalf of the parent company. The name and address of the parent company must be used in business transactions. Appointment of a proxy with a permanent residence in Slovenia is compulsory. The parent company is liable for all obligations of the branch. The branch must be registered with the court register in Slovenia. Branches of EU countries' companies have full national treatment, except in respect of acquisition of real estate in Slovenia (Foreign Exchange Act).

Guarantees to foreign investors. Under the Foreign Exchange Act, transfer of profits and repatriation of capital is free provided non-residents have met all their tax liabilities in Slovenia. The Act also guarantees compensation for nationalization or losses caused by other measures of the state. These guarantees are secured by the provisions of twenty-two bilateral investment treaties, twenty-five bilateral taxation treaties and adherence to important international conventions.

4. Government policies affecting FDI environment

Slovenia's comprehensive regulatory reforms, particularly those designed in more recent years to bring the country in line with the EU *acquis* in preparation for EU membership have resulted in a generally liberal trade regime, and a largely open and non-discriminatory framework for FDI. Slovenia has undertaken comprehensive reforms in practically all areas that affect economic activity. The legal regimes for establishment, foreign exchange transactions, competition, labour relations, and securities trade have been revised and modified according to international standards and notably the EU *acquis*. However, like all economies in transition, Slovenia faces somewhat of an "implementation gap" in some areas. Administrative barriers, complicated procedural requirements and an overloaded court system create

implementation challenges for the country. Another problem is that of land use and development, due to inconsistencies in the legal regime inherited from the Yugoslav era and the country's restitution process. The Slovenian government is taking action to combat these problems. It has already adopted a number of new laws aimed at procedural fairness and simplicity, as well as education programmes for court personnel, to enable quicker processing of disputes. In terms of real estate, the government is modernising its property registration system, with the assistance of the World Bank and the EU. A new law for the employment of foreigners came into force early 2001 and another, which concerns the recognition of foreign qualifications, is under preparation. Acceleration of the privatisation process has been identified as an FDI policy priority, with positive results. In 2001 FDI inflows increased sharply, in large part due to the privatisation of a mobile telecommunications operator and the foreign acquisition of one of the recently privatised banks. The government's target is to raise annual net FDI inflows to 3 per cent of GDP by 2003. Privatisation procedures are underway for the country's two largest banks, with the completion date for the first planned before the end of 2001 and the second early 2002. Authorities are ready to embark on important transactions in the telecommunications sector as soon as market conditions permit.

The actual Slovenian policy stance towards FDI is based on the recognition that considerable increase of FDI in Slovenia can not occur without: (i) widely opening the door of privatization of state property to foreign investors and accelerating the privatization process at the same time; (ii) an attractive investment incentives program (iii) immediately making ready for use new industrial land with all the necessary (infrastructural) facilities and (iv) ambitious program for the elimination of administrative barriers to investment.

The Program of the Government of the Republic of Slovenia for the Promotion of Foreign Direct Investment in 2001-2004 tackles some of the above issues. Measures, which aimed at improving Slovenia's competitiveness as a destination for FDI, are (i) maintaining an internationally comparable system of non-refundable incentives; (ii) improving the supply of construction sites for industry; and (iii) lifting of administrative barriers to investment in general. The Program also pledges for privatization being more open to foreign investors (strategic and institutional), especially concerning the public utilities and companies owned by the Slovenian Development Corporation and other state-owned industrial enterprises (Slovenian Ironworks - Slovenske železarne). Program also provided for active role of foreign investors in the privatization of the financial and other services sectors.

Financial incentives. According to the Program, in the 2001-2004 period the government will implement the scheme of allocating non-refundable financial incentives for investments with the aim of improving the competitiveness of Slovenia as FDI location. The scheme contains incentives to help investors in introducing technologically advanced businesses in the field of industry and services and in creating jobs.

Domestic and foreign companies undertaking an investment project are equally eligible for non-refundable financial incentives. Incentives are given for new investment projects as well as for considerable expansions of existing activities. To be eligible for incentives the investment project should provide for the establishment of a new business activity in the field of manufacturing or services, which results in internationally marketable products. Another criteria for being eligible for incentives is that investment project should create at least 100 new jobs in a period of two years and the investment should total over EUR 2 million. In less developed regions, the threshold is 50 new jobs in a period of one year, but this does not include the expansion of the existing production in the same location. The program also stimulates the establishment or expansion of research and development departments where investment totals over EUR 5 million and creates at least 10 jobs in the period of one year.

Incentives are earmarked for: (i) infrastructure and other facilities necessary for industrial land (up to 40% of costs), (ii) construction or purchase of buildings (up to 40% of costs), (iii) purchase of new machinery and equipment (up to 40%), and (iv) training (up to 40% of costs). In 2001, the total amount of incentives

will be SIT 500 million³, in 2002-2004, between SIT 500 million and SIT 1,000 million will be allocated annually (TIPO 2001). In 2000 and 2001, EUR 1,000 to EUR 6,000 per job created (depending on region and technology) have been awarded.

Companies registered in Slovenia are also eligible to various facilities for export promotion and protection provided by the Slovenian Export Corporation. Facilities include a broad range of financial services related to export insurance, financing and guarantee issuing. Slovenian Export Corporation insures export credits against commercial as well as non-commercial risks. It also provides insurance against non-commercial risks in the case of Slovenian outward FDI (Slovenska izvozna družba 2000).

Tax incentives. Apart from low 25% tax rate, the *corporate income tax* in Slovenia contains the following favorable elements: (i) losses may be carried forward for a maximum 5 years; (ii) depreciation of tangibles and intangibles is calculated by the straight-line method and may be included in the expenses of a company. The depreciation rate for fixed tangibles and long-term intangibles varies between 5% and 50%; (iii) taxpayers are entitled to a deductible allowance amounting to 40% of the financial resources invested in tangible assets (except for passenger cars) and long-term intangible assets, but this may not exceed the amount of the taxable base. If such tangibles and intangibles are sold before the expiration of three years after the year in which such allowance was granted, the taxable base must be increased by the amount of the allowance in the year of sale; (iv) investment reserves for investments in tangible and intangible assets and long-term portfolio investments in Slovenia may be deducted up to the amount of 10% of the taxable base. Such allowances may be granted for a four-year term.

Social security contributions (pensions, health care, employment and maternity leave) are partly paid by the employees (22.1% of gross wages) and partly by employers (15.9% of gross wages). The Employment Service of Slovenia carries out a series of measures for encouraging employment, through which it advises and financially supports employers, which employ new workers. A provision for repayment of contribution when employing certain groups of unemployed persons provides reimbursement for employers of between 25% and 100% of the compulsory contributions for pension, disability and health insurance, and also the contributions for maternity leave and unemployment insurance. Similar reimbursements of contributions are provided to employers with up to 50 employees who employ an unemployed person or a permanently redundant worker⁴.

3 1 USD = 246.0116 SIT (Slovenian Tolars); as of November 6, 2001.

4 More detailed, employment incentives related to the social security contributions are the following:

- Taxpayers employing first job holders, who were previously registered with the employment agency for at least 6 months, are entitled to 50% refunds of social security contributions for the first 2 years, and 25% for the third year.
- Taxpayers employing workers previously unemployed and registered with the employment agency for at least 12 months are entitled to 50% refunds of social security contributions for 2 years.
- Taxpayers employing persons older than 50 years, who are beneficiaries of the employment agency, are entitled to 50% refunds of social security contributions for the first 3 years, and 25% for each following year.
- Taxpayers employing beneficiaries of the employment agency are entitled to social security refunds for a period twice as long as the rest of the term in which the beneficiaries would have been entitled to employment agency benefits.

Improving the supply of construction sites for industry. Changes in the administrative framework regulating the acquisition of land and building permits and the introduction of real estate tax will result in greater availability of land in the long term. Before this is achieved, the state intervenes more actively in order to increase the supply of land in the market by: (i) setting up an agency for providing services in the area of acquiring land for industry within Trade and Investment Promotion Office; (ii) devising a divestment program for state-owned companies in order to dispose of non-essential assets; (iii) enabling local communities to become more actively involved in the development of industrial parks; and (iv) by stimulating FDI in the area of industrial estate management. In order to lift the existing barriers in the field of land supply and to stimulate the construction of industrial parks, the Government will implement a program of granting financial incentives to local communities and other investors for the construction of all infrastructure and facilities necessary for an industrial land in the period 2001-2004.

The lifting of administrative barriers to investment in general. Activities related to the lifting of administrative barriers entail the areas of purchasing land for the purposes of investment, acquiring permits for site development, acquiring work permits for foreigners and hiring and firing procedures for employees, facilitating procedures for setting up companies (registration at court and business activity permit), and reporting on companies' international operations.

5. Problem areas highlighted by foreign investors and opportunities available to foreign investors

In existing analysis of foreign investors' motivation in Slovenia (see, for instance, Rojec 1998, Dedek & Novak 1998), access to the local and other (adjacent, neighboring) markets have been quoted as the two most important single motives, however, altogether relevance of other motives - like technology and know-how, quality of labor, recognized trade marks and financial support of the Slovenian target company/joint venture partner and securing material and parts - denoting factor cost advantages-seeking FDI seem to prevail. The interviews of foreign investors indicate that, apart from FDI in the service sector, most of FDI in Slovenia is of the factor cost advantages-seeking type. As far as the role of labor in that is concerned, it is not the low price but rather the quality of labor, which motivates foreign investors in the case of Slovenia. The value added to labor costs ratio in the manufacturing foreign investment enterprises in Slovenia is 1.97, as compared to 1.57 in overall Slovenian manufacturing sector, 1.46 in the manufacturing sector of EU-15, 1.67 in Austrian, 1.44 in German, 1.39 in Italian and 1.63 in French manufacturing sectors (1998 data; see Rojec and Stanojević 2001).

Existing analysis of foreign investors' motivation and of competitive advantages of Slovenia as investment location (see for instance FIAS 1998, TIPO 1999) suggest that it is reasonable to distinguish between (i) investment opportunities opened to foreign investors which represent a direct motive, that is a factor because of which foreign investor would begin to consider investment in Slovenia, and (ii) natural and created factors/environment and investment climate in Slovenia in the framework of which the potential investment is realized. The latter represents a framework, which determines to a considerable degree whether an investor will decide to attempt to realize an investment opportunity.

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- Small companies (less than 50 employees) employing unemployed persons or persons formerly dismissed for technological surplus reasons are entitled to a 100% refund of social security contributions for the first year, 50% for the second year and 25% for the third.
 - Taxpayers employing persons for at least 2 years who increase the total amount of employees (except persons over 50 years of age) are entitled to refunds of social security contributions.

According to FIAS (1998), investment opportunities for foreign investors in Slovenia could be classified into five groups:

- a) Acquisitions of and joint ventures with Slovenian enterprises where investment opportunities arise from: (i) relatively high domestic purchasing power; (ii) high export propensity of Slovenian companies with relevant market shares in EU countries; (iii) strong trade and business links of Slovenian companies with other parts of the former Yugoslavia and with Central and Eastern European countries in transition; (iv) high level of managerial and technical skills in companies; (v) local industrial environment assures technological capabilities which enable speedy mastering of the technology transferred by foreign investor; (vi) transport costs are low; main investing countries are near, transport connections are good; (vii) good acquisition opportunities (of not yet privatized) Slovenian companies.
- b) Subsidiaries in Slovenia as part of integrated international production of multinational enterprises. Investment opportunities arise from: (i) quality of workforce: well educated and trained, dedication to work, industrial tradition, language skills, high level of computer literacy; (ii) low labor costs if compared to productivity level (high value added to labor costs ratio); (iii) relatively high level of managerial and technical skills in companies; (iv) central geographical position (proximity) making transport costs low (good international transport and communication linkages); (v) trade links with other countries; liberal foreign trade regime and integration in the EU and CEFTA; (vi) industrial tradition and especially experiences in manufacturing of middle technology level products; (vii) opportunities for location of parts of integrated international production in Slovenia are especially in production asking for higher level of workforce quality, industrial experiences, middle technology level and low transport costs.
- c) Investment in infrastructural sectors – public utilities. Investment opportunities arise from: (i) Slovenia is just about to start privatization of public utilities; (ii) gap between Slovenian investment needs in infrastructural facilities and available financial sources requests more intensive engagement of private capital in infrastructural investment.
- d) Slovenia as a location for regional headquarters, as regional and not as a local market. Investment opportunities arise from: (i) location between EU countries, CEFTA countries and successor countries of former Yugoslavia with well developed business links with all three groups of countries; (ii) high level of managerial and technical skills in companies; (iii) high quality of life for representatives and executives of foreign investors, including high level of security; (iv) good international transport and communication links; (v) political stability.
- e) FDI in services, especially in business infrastructure. Investment opportunities arise from: (i) fast growing economy and market with very high demand for business services; (ii) forthcoming privatization of financial sector; (iii) full liberalization of capital flows, introduction of funded pension schemes, changing of savings habits of population and modes of investment financing in enterprises strongly increase the need for financial intermediation, especially via capital market.

Factors, which create attractive and friendly environment for investing in Slovenia, are:

- a) Market factors consisting of: (i) growing and open economy; (ii) economic and political stability with the highest international ratings among Central and Eastern European countries in transition; (iii) good access to markets on the West, East and SouthEast Europe.
- b) Production factors consisting of: (i) location in the heart of Europe with a maritime cargo port; (ii) excellent infrastructure with extensive transport grid and telecommunications network; (iii)

long industrial tradition coupled with ability to implement new technologies; (iii) well educated, flexible and motivated work force with good command of foreign languages – model industrial relations; (iv) experienced managers; (v) high quality of life.

- c) Regulatory framework consisting of: (i) intensive adoption of EU legal and system framework; (ii) liberal regime of international economic relations, characterized by WTO membership and European Agreement with the EU; (iii) liberal FDI regime, based on national treatment principle and unlimited profit and equity repatriation; (iv) low, 25% corporate profit tax and other incentives for FDI.

Two major determinants of future FDI inflows in Slovenia will be process of privatization of financial sector and public utilities and process of integration in the EU. In this framework, of course, a number of other factors will be relevant; above all the finalization of the transition process.

The major opportunity for increased foreign acquisitions (privatisations) in Slovenia is the forthcoming privatization of state ownership, mostly in the financial sector and public utilities. Slovenia still waits for the privatization of the energy sector, telecommunications, railways and some other public utilities, insurance companies and two largest banks, companies in the ownership of the Slovenian Development Corporation and steel industry. The second opportunity is foreign acquisitions of already privatized companies. Intensified foreign acquisitions of already privatized Slovenian companies is expected due to the need for intensified restructuring process which is going on in the Slovenian enterprise sector. Companies are increasingly aware of the possibilities of FDI for speeding up their restructuring.

Slovenia's integration in the EU. EU integration processes are strong incentive for FDI among member countries, but also for FDI from non-member to member countries. Accession of a new country in the EU is even stronger incentive for increasing FDI flows in the accessing country. With accession in the EU, the accessing country becomes an integral part of the internal market and adopts internal market's common rules of the game (*acquis communautaire*) what stimulates FDI inflows from EU member countries as well as from other countries. With accession in the EU, the problem of small local market as the most important constraint for more FDI inflows in Slovenia will also cease to exist.

Completion of transition process. Another important factor of future FDI inflows in the country will be the dynamics of transition reforms and reforms related to the integration in the EU. The fact that Slovenia is among the forefront candidate countries for EU membership considerably reduces the perception of risk of doing business with Slovenia by potential foreign investors. This is mostly because potential foreign investors are sure of what the future economic and legal system will look like (*acquis communautaire*) and the timing of the adoption of this system is also known (National Program for the Adoption of the *Acquis*). Adoption of appropriate normative framework is, however, not enough; the catchword is implementation of this framework. The completion of transition, thus, much depends on the enforcing and implementing of changes, establishing of enterprise sector, which will be able to viably compete on the internal market of the EU, establishing of efficient corporate governance, of competition and competitiveness of public utilities, of competitive banking sector. In short, the completion of transition means establishment of (fully) functioning market economy institutions. For Slovenia, the process of EU accession is nothing else but an acceleration of the transition process, a guarantee that transition process will be faster and more thorough.

Slovenia as a springboard for SouthEast Europe. Stability Pact for SouthEast Europe and, after changes that happened in Federal Republic of Yugoslavia, gradual long-term integration of the area in European integration processes has definitely demonstrated the possibilities, which Slovenia has in the region. Therefore, affirmation of Slovenia as a springboard for doing business in the successor countries of the former Yugoslavia is definitely one of the possibilities for increasing future FDI inflows in Slovenia. Slovenia should try to persuade foreign investors to handle the markets of other parts of former Yugoslavia

from Slovenia (establishing of regional headquarters for successor countries of former Yugoslavia in Slovenia). Slovenia has undeniable advantages in this regard, i.e. much lower country risk, knowledge of circumstances, language, culture, people, high reputation of Slovenian products in these countries, geographical location.

Opposite to the above mentioned investment opportunities and positive aspects of investment climate in Slovenia foreign investors tend to mention the following problems of Slovenia as an investment location:

- a) Small local market. The small size of Slovenian domestic market is the major constraint preventing more FDI inflows.
- b) Privatization and enterprise restructuring. There are several aspects because of which privatization have not contributed enough to FDI inflows. (i) The first is the (mass) privatization concept in industry and trade, which implicitly favored internal (employee and management) buy-outs. Foreign acquisitions were only exceptional in the privatization dominated by distribution through the use of ownership certificates and internal buy-out at considerable discounts. (ii) The second aspect is not fast enough (transition) restructuring process in the privatized enterprises, which do not encourage them to search for strategic foreign partners. (iii) The third aspect is hesitant privatization of state ownership in the financial and public utilities sector, where only recently more decisive moves have been initiated.
- c) Unfinished transition process. Incomplete transition increases the costs of establishing and operating a company. This is especially reflected in the so-called implementation gap, i.e. the gap between formally adopted regulation and inability to (fully) implement it. Economic and legal systems are now approaching fast to the one consistent with EU and one can expect accomplishment of this process along with the integration in the EU.
- d) Administrative barriers to investment and operating of companies are a relevant constraint to more active engagement of domestic and foreign investors since they increase the costs of company establishing and operating. Although in a number of areas (like tax administration, customs procedures, industrial property rights and standardization procedures, and to a certain extent also procedures for establishing businesses and foreign exchange transaction reporting requirement) definite or important breakthroughs have already been made, in certain areas administrative procedures remain to long and complicated. FIAS (2000) gives specific recommendations to the Slovenian government on how to ease and improve administrative procedures in the field of company registration, business activity permit, acquiring land, site development, expatriate work permit and employment regulation.
- e) Problems in acquiring industrial locations. Access to business premises and land to do business, especially for industry, getting clear title to it, and getting the necessary permits to build and operate a factory, are often complex and time consuming. Problem is also high price and low availability of land and industrial and business premises in general (FIAS 2000).
- f) Relatively rigid and protective labor legislation which does not take into account enough the interests of employers, i.e. in general, the rules governing the relationship of employers and employees is biased towards employees (FIAS 2000).
- g) Relatively rigid labor market. Slovenia has relatively well educated and productive labor force, but labor costs are relatively high compared to competitive investment locations, and mobility of labor force in Slovenia is relatively low (in certain regions there is a lack of certain professions which are in surplus in other regions) (FIAS 2000).

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