THE IMPORTANCE OF GREENFIELD INVESTMENTS FOR THE ECONOMY OF MONTENEGRO

Značaj greenfield investicija za privreduprivredu CrneGore

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Abstract

Foreign direct investments are important component of economic development in the world. They are seen as important catalyst of economic transformations of significant number of countries. Even though this form of funding is the framework of growth model of Montenegrin economy, world economic crisis has shown that it has to be fundamentally to the advantage of greenfield investments and export-oriented foreign direct investments in order for more significant effect to be seen over a longer period.

Keywords: foreign direct investments, greenfield investments, global economic crisis

1. Introduction

The issue of foreign direct investments has been more intensively looked into by many economists during the Second World War, even though the origins of this form of funding date from before. It is a period that is characterized with growth of every forms of international capital, from classical debt to foreign direct investments, thanks to more intensive development of trade and international finances.

Particularly large growth of international financial debts occurred during 1980s and 1990s. For more intensive expansion during 90s there are stated following reasons such as appearance of large institutional investors on financial markets, increased network of world financial markets, globalization, as well as liberalization of financial markets, especially markets of European countries in the beginning of 80s [Babić, Pufnik, Stučka, p.1]. The domination of this form of funding can be seen even after 90s,
especially with the countries in transition, that were facing foreign investments with the goal of elimination of macroeconomic and structural disorders with which they were facing. The experience of the countries in transition has shown that foreign direct investments were essential for achieving their future goals, which has later served as an example for Montenegro.

2. Retrospective of previous influx of Foreign direct investments in the world

The analysis of movement of foreign direct investments in the world (Graph – 1) shows their constant growth until 2000. Then the amounts of income were reaching the amounts up to 1.414 billion dollars [www.unctadstat.unctad.org]. Namely, on the world market of foreign direct investments, in the year 2001 there was significant fall of 40.8% (from 1.4 billion dollars to 837.7 million dollars), which continued in 2002 from 24.9% (628.7 million dollars) and in 2003 from 3.9% (604.3 million dollars). In the literature, as main culprits for the global decrease of foreign direct investments in the period of 2001-03 are considered more cautious investments by foreign investors due to insufficient economic growth in most of the countries, as well as slow development of privatization process in many transitional countries.

Graph – 1: Review of movement of FDI by regions, 1990-2014.

(in millions of dollars)

Source: www.unctadstat.unctad.org, own research

In 2004 there was mild recovery in the movement of foreign direct investments, when there was growth of influx of foreign direct investments from 22% (737.6 billion dollars) compared to 2003. Global economic growth in 2004 was 4.1%, which allowed many countries to attract great number of foreign direct investments.

In 2005 and 2006, the increase in foreign direct investments in the world was significantly improved, but still remained far beyond the level reached in 2000. After four consecutive years of rapid growth, foreign direct investments increased influx during 2007 and surpassed the record from 2000 (from 1.4 billion dollars to 2 billion
dollars). The outbreak of global economic crisis influenced sharp drop of foreign direct investments in the world.

The incomes in developed countries were decreased, while in the countries in development and in transition the incomes were still in growth in 2008, even though with slower pace compared to 2007. After reaching historical peak in 2007, flows of foreign direct investments in developed countries had sharp decrease in 2008 and 2009. In 2008 the influx of foreign direct investments fell to 21.9% compared to 2007, while in 2009 the income fell for 40% compared to 2008.

Despite the crisis, countries in development and those in transition attracted record inflows of foreign direct investments in 2008. As a result, share of these economies in global inflow of foreign direct investments was 37%, which is the highest percentage ever recorded. Data on inflow of foreign investments in 2009 show different picture, because the investments in countries in development and those in transition, in almost all regions and subregions, dramatically decreased.

Namely, the inflows of foreign direct investments in countries in development in 2009 dropped for 20.4% compared to 2008, while the countries in transition had drop of income of 40%. Causes for such movements are, among others, decreased possibility for companies to invest due to difficult access to financial resources, slowing down economic activity as a whole in developed countries, decrease of mergers and acquisitions between companies of developed countries and countries in development, slowing down of privatization in countries in transition and other. [UNCTAD, 2009].

Dynamics of global FDI scene suggests, especially in the recent years, to certain changes on the relation developed countries - countries in development. It is evident that for countries in development (Graph 1) and countries in transition (together), first time share of FDI flows in 2009 and 2010 is half, while on the contrary, foreign direct investments in developed countries have fall tendency.

The recovery of inflows of total foreign direct investments comes in 2010, when the inflows were slightly increased to 1.328 billions of dollars [UNCTAD, 2015], but they were still under their average from the time before crisis. The increase in inflows continued in 2011, reaching the amounts of 1.563 billion dollars, which is about 17.7% more compared to 2010, which made foreign direct investments a significant form of funding world economy. In 2010 total income of FDI was decreased for 10.3% compared to 2011 and totals 1.4 billion dollars. As reasons for drop in inflows there are stated macroeconomic instability and unstable politics for investors. In 2013 it is experiencing moderate growth of foreign direct investments for 4.4% compared to previous year with the amounts of 1.467 billion of dollars, while in 2014 fall was recorded for 16.3% to 1.228 billion from 1.47 billion in 2013 [UNCTAD, 2015].

3. Analysis of the inflow of foreign direct investments in Montenegro

Foreign direct investments became the backbone of growth model of Montenegrin economy. Aware of the fact that key development problems under which Montenegrin economy was at the end of '90s couldn't be solved overnight, the government, led by previous experience of countries in transition, found solution in foreign direct investments. What kind of experience had Montenegro when it comes to inflows of foreign direct investments we can see in Graph – 2.
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Graph – 2: Inflow of FDI in Montenegro in period 2004-2014.

Source: CBCG 2014.g. preliminary data

Graph covers periods from 2004-2014, even though the inflows of foreign direct investments came in from 2001, after significant reforms and liberalization of market, but named inflows to 2004 were minor so for that reason they are not taken into consideration.

The values of incomes of foreign direct investments in 2004 were about 52.6 million Euros, and yet those inflows were lower than expected. However, the situation changes in 2005, when foreign direct investments reached the amount of 410.8 million Euros, which is 7.8 times more than in 2004. The largest inflow was made from privatization of two biggest companies, Montenegro Telekom (114 mil €) and Kombinataluminijuma (70.7 mil. €).

Trend of foreign direct investments growth continues in 2006, when total inflow was 647.3 million Euros, while in 2007 the income of foreign direct investments was 1.057.2 million Euros, which is 63.3% more than 2006. In 2008, the inflow of foreign direct investments fell on 847,315.6 million Euros, which is 19.8% less than in 2007.

Despite crisis, in 2009 it was recorded growth of inflow of foreign direct investments of 44.5% compared to 2008, reaching the amounts of 1,223.9 million Euros. To mentioned growth influenced performed partial privatization and recapitalization of Elektroprivreda CG from Italian company “A2A”. The sale of shares to the Italian company is confirmation that for good companies and projects, even with crisis, it is not hard to find investors, and good signal for foreign investments to participate in investment projects is important for development of Montenegro.

In 2010 it is recorded inflow of foreign direct investments of 652.8 million Euros, which is evident drop compared to 2009. Even though there was a drop compared to previous year, relatively high income was recorded, because in 2010 there weren’t larger privatizations.

Also, in 2011 inflows significantly dropped and were 494.7 million Euros, which 24.2% less than in 2010. However, even though the inflow is smaller compared to previous year, we can say that the inflows were significantly involved in current account deficit funding and that those inflows cannot be ignored, considering the period
of crisis. In 2012 it is recorded growth of inflows for 28.1% compared to 2011 (633.7 million Euros), while in 2013 there was drop of 24.4% compared to 2012 (479.2 million Euros). During 2014, foreign direct investments recorded slight growth of 3.8% (498.1 million Euros).

When it comes to the structure of investments, it is evident that equity investments dominated in the period prior to crisis, while their share was later decreasing. In 2009 their share was 72% of total inflows, thanks to privatization of Elektroprivreda. Investments in real estate constantly have significant share in investments structure, where the share prior to crisis was most evident, with share of 48% in 2007. Foreign direct investments in the form of intercompany debt had the most significant share in overall structure in 2013 and 2014 with 39% and 46%.

**Graph – 3: The structure of total incomes of FDI in Montenegro in 000 Euros**

![Graph](image)

*Source: CBCG
*preliminary data

If we analyze sector structure of investment, Montenegro is characterized with extremely high percentage of investment to tourism sector, which is compatible with world trends of foreign direct investments, in accordance with strategic orientation of Montenegro. Apart from tourism sector, it is visible investment in industrial and financial sector, while somewhat less is represented sectors of agriculture, construction and services [Strategija, p.22].

The following table outlines some of the most important foreign direct investments in Montenegro.
Table 1: Review of important foreign direct investments in Montenegro

<table>
<thead>
<tr>
<th>Company</th>
<th>Activity</th>
<th>Customer</th>
<th>Country of origin</th>
<th>Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telekom Crne Gore</td>
<td>Telecommunications</td>
<td>Matav RT</td>
<td>Hungary</td>
<td>Privatization</td>
</tr>
<tr>
<td>Jugopetrol AD</td>
<td>Oil industry</td>
<td>Hellenic petroleum</td>
<td>Greece</td>
<td>Privatization</td>
</tr>
<tr>
<td>KAP</td>
<td>Aluminum industry</td>
<td>Rusal</td>
<td>Russian Federation</td>
<td>Privatization</td>
</tr>
<tr>
<td>Pro Monte</td>
<td>Telecommunications</td>
<td>Telenor ASA</td>
<td>Norway</td>
<td>Greenfield</td>
</tr>
<tr>
<td>Hotel Maestral, Milocer</td>
<td>Tourism</td>
<td>HIT Nova Gorica</td>
<td>Slovenia</td>
<td>Privatization</td>
</tr>
<tr>
<td>HTP Budvanska rivijera, Hotel Avala</td>
<td>Tourism</td>
<td>Bepler &amp; Jacobson</td>
<td>United Kingdom</td>
<td>Privatization</td>
</tr>
<tr>
<td>Podgoricka banka AD</td>
<td>Banking</td>
<td>Societe generale Bank</td>
<td>France</td>
<td>Privatization</td>
</tr>
<tr>
<td>LB leasing Podgorica</td>
<td>Financial Services</td>
<td>LB leasing Ljubljana</td>
<td>Slovenia</td>
<td>Greenfield</td>
</tr>
<tr>
<td>Hotel&quot;Panorama”</td>
<td>Tourism</td>
<td>Springer&amp;Sons</td>
<td>Austria</td>
<td>Privatization</td>
</tr>
<tr>
<td>Hypo Alpe Adria Montenegro</td>
<td>Banking</td>
<td>Hypo Group</td>
<td>Austria</td>
<td>Greenfield</td>
</tr>
<tr>
<td>Rudnici Boksita AD Podgorica</td>
<td>Mining</td>
<td>Salamon</td>
<td>Russian Federation</td>
<td>Privatization</td>
</tr>
<tr>
<td>Elektroprivreda CG</td>
<td>Energetics</td>
<td>A2A</td>
<td>Italy</td>
<td>Privatization</td>
</tr>
</tbody>
</table>

**Source:** MIPA

It can be seen that privatization is the basic method of entry of foreign direct investments in Montenegro. It is indisputable that foreign direct investments had positive influence on Montenegrin economy, but it must be stressed that so far it was mostly about taking over companies, and less about import of new technologies and greenfield investments. In the years to come, the inflow of greenfield and brownfield investments should become main channel of foreign capital inflow. Greater presence of mentioned investments is clear indicator that country successfully implements economic reforms.

4. The importance of Greenfield investments for Montenegro economy

Greenfield investments are new investments that are made by opening new branches or facilities abroad. These investments are particularly important for countries in transition, whose experience show that after performed privatizations of big national and social companies, in which mergers and acquisitions had dominant role, greenfield investments became very important significant form of entry of foreign direct investments. Considering that so far over 90% of companies in Montenegro have been
privatized, incomes based on that will gradually decrease, so it is inevitable that the level of greenfield investments will increase, i.e. we should focus on attracting them in the following period. UNCTAD’s Report on investments in the world shows that greenfield investments have bigger value for the host country compared to other kinds of foreign direct investments (M&A), especially in the initial period. Those advantages can be seen in the following [WIR, 2000, according to Begović, p.15]:

- Both ways of entry of foreign direct investments bring foreign capital to the host country, but financial means secured through M&A do not always lead to increase in the value of capital, while in the case of greenfield investments it is regular practice. But, in cases where some local firm is in great difficulties, and closing is the only real alternative, cross-border merger or acquisition can indeed play the role of “savior”;
- There is less probability that foreign direct investments through mergers and acquisitions (M&A) provide transfer of more modern or better technology/knowledge compared to greenfield investments. M&A can directly lead to reducing or extinguishing local production or functional activities (e.g. research and development) or to their relocation in accordance with corporate strategy of acquiring company;
- FDI through M&A lead to opening new jobs when entering the country. They can lead to layoffs, although in the case of company that would have gone bankrupt if it wasn’t bought, they can lead to preserving jobs. Greenfield foreign direct investments, on the contrary, necessarily lead to opening new jobs;
- FDI through M&A can increase concentration and lead to monopoly. However, it is possible that these investments increase competition, if the takeover manages to preserve local company that would otherwise go bankrupt. Greenfield investments, according to definition, increase the number of companies and do not increase market concentration upon entering.

In the following period, Montenegro should be oriented to increased promotion of investment potentials and creating preconditions for faster inflow of greenfield investments, considering the advantages that those investments have for host country. The best example for positive effects of greenfield investments is Ireland [Barry, Bradley, p.1798-1811, according to Babić, p.9] which applies as an example in Europe, with fast and sustainable attraction of big investments, especially the ones that encourage production for export. Ireland has, in the late 1950s started attracting foreign direct investments, introducing special incentive measures like for example: it has set low tax rates for gain on production intended for export (0%, after that 10%) and attractive investment incentives, and it predicted complete repeal of customs barriers in within span of 10 years. As a result of above incentive measures, Ireland recorded high growth rates of GDP and export from the middle of 1980s and onward, which decreased its trade dependence on Great Britain (from 90% to 30% decreased the share of Great Britain in foreign trade of Ireland). Greenfield investments in Ireland were aimed (in production and manufacturing industry) according to those sectors where there are great possibilities to apply economies of scale on the enterprise level and according to sectors with high technology. Greenfield investments lead to increase in salaries, significantly bigger productivity and profitability. The great success that Ireland achieved can be attributed to greenfield investments, as well as investments to sectors that in Ireland were not developed before, and that related to tradable goods, export expansion and fast growth of overall productivity.

The structure of foreign direct investments in Montenegro must improve, because the big inflow of investments was related non-tradable goods sector (according
to data of CBCG, in the structure of inflows the biggest share goes to investments to real estate, especially in 2007 or 2013, 48% and 42%). In short term, certainly this structure of investments is favorable, because balance of payment deficit is financed without another borrowing, but in the long term it can be counterproductive. The example of Portugal best confirms above attitudes. Namely, the great inflows of capital that entered Portugal related to non-tradable goods sector, mostly real estate. Current account recorded increasing deficits and at some point it became unsustainably high, therefore its reduction had to be followed with recession [Čalina, Čizmić, p.614].

Montenegro should extract the lessons, from positive, as well as from negative experiences of countries whose development models are based on the foreign direct investments as well. In the following period it is necessary to focus on greenfield investments and import-oriented foreign direct investments, which is long term interest for every country.

The following tables gives a view of greenfield projects in the period 2008-2014 with selected countries of Central and East Europe, as well as countries from South-East Europe.

**Table – 2: Overview of greenfield projects, according to source, for the period 2008-2014 with selected countries**

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Czech Republic</td>
<td>3771</td>
<td>1137</td>
<td>2640</td>
<td>2002</td>
<td>2174</td>
<td>2131</td>
<td>378</td>
</tr>
<tr>
<td>Hungary</td>
<td>2817</td>
<td>940</td>
<td>372</td>
<td>1107</td>
<td>921</td>
<td>666</td>
<td>738</td>
</tr>
<tr>
<td>Poland</td>
<td>1754</td>
<td>1045</td>
<td>1851</td>
<td>833</td>
<td>1353</td>
<td>854</td>
<td>1400</td>
</tr>
<tr>
<td>Slovakia</td>
<td>98</td>
<td>388</td>
<td>1311</td>
<td>32</td>
<td>285</td>
<td>262</td>
<td>5</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>325</td>
<td>25</td>
<td>120</td>
<td>119</td>
<td>83</td>
<td>216</td>
<td>277</td>
</tr>
<tr>
<td>Romania</td>
<td>339</td>
<td>115</td>
<td>758</td>
<td>104</td>
<td>139</td>
<td>287</td>
<td>467</td>
</tr>
<tr>
<td>Croatia</td>
<td>1830</td>
<td>148</td>
<td>810</td>
<td>83</td>
<td>172</td>
<td>241</td>
<td>113</td>
</tr>
<tr>
<td>BIH</td>
<td>7</td>
<td>-</td>
<td>19</td>
<td>3</td>
<td>4</td>
<td>38</td>
<td>4</td>
</tr>
<tr>
<td>Macedonia</td>
<td>-</td>
<td>9</td>
<td>1</td>
<td>33</td>
<td>-</td>
<td>99</td>
<td>-</td>
</tr>
<tr>
<td>Montenegro</td>
<td>-</td>
<td>-</td>
<td>7</td>
<td>-</td>
<td>-</td>
<td>9</td>
<td>-</td>
</tr>
<tr>
<td>Serbia</td>
<td>653</td>
<td>316</td>
<td>365</td>
<td>146</td>
<td>71</td>
<td>78</td>
<td>142</td>
</tr>
</tbody>
</table>

*Izvor: UNCTAD, WIR 2015., own research*

Data show that some countries of Central and East Europe record constant growth of greenfield investments, which implies attractiveness of this region for investors and estimations that the region has good development prospects. Montenegro cannot commend with significant amounts of mentioned investments. However, the experiences of the countries that have gone through the process of transition show that participation of greenfield investments show significant growth only after the
completion of privatization process and approximation to EU, which for Montenegro comes in the following period.

Direct effects that Montenegro can have from greenfield investments are:
- higher economic growth (Econometric research that was performed for the period 2004-2011 showed that current structure of foreign direct investments in Montenegro has very little influence on economic growth, but the influence is statistically significant [Gardašević, A., 227-232]. However, with attraction of increasing number of greenfield projects, economic growth would increase, because greenfield inflows influence growth stronger than investments in general [Sandrine Levasseur, 2004., according to Begović p.40];
- stimulating domestic investments (The results of World Bank research [Begović, p.41] confirm that greenfield and M&A investments encourage domestic investments, and they are encouraged by growth of GDP. This means that economic growth as the most important indicator of domestic yields, serves as effective factor “that pulls” foreign direct investments, and they help in growth of domestic investments in the future);
- export growth (Experiences of countries in transition show that greenfield investments contribute to export growth before any other forms of foreign direct investments. Without fast export growth there will not be fast economic growth in Montenegro. Therefore we need greenfield investments);
- opening of new work positions and investment in human capital (It is about new investments that contribute to opening new work positions. The experience showed that foreign investors give great amount of attention to continuous training and development of employees, which would directly contribute to development of labor force in Montenegro);
- increase in competition (In the long term, competition would be useful, because it would contribute to increase in economic efficiency. The arrival of greenfield investments in Montenegro would encourage every company in any branch to increase economic efficiency through development of new, better products, services, lower prices, lower costs etc.
- technological progress (Greenfield investments give great attention to research and development and generally have more contemporary technology from that available in Montenegro. Through transfer of technology there would be increase of productivity);

In addition to stated positive effects, of course, there are negative effects of greenfield investments (environment pollution, degradation of natural resources, repatriation of profit, creating instability through increased financial risks on market etc.), but most studies that were conducted on this subject confirmed the positive effect on economic well-being of the host country, so further arguments on the importance of greenfield investments in Montenegro are redundant. The more Montenegro advances in the reform process, the more greenfield investments there will be.

5. Conclusion

Foreign direct investments are the necessity of modern economic life of Montenegro, but they must be seen as a package of development factors (equipment, technology, knowledge, market channels, managerial and organizational skills) that
could help Montenegrin economy in the period if institutional reforms that are ahead. The inflows of foreign direct investments so far in Montenegro showed that Montenegrin economy has been recognized as attractive location for foreign investments, but that bigger inflows can be expected in the period of advance in reforms and success in pre-accession negotiations with EU. Certainly, Montenegro should not be dependent on foreign direct investments and see them as only source of financial means. In the following period, it is necessary to focus on greenfield investments and export-oriented direct investments, which is long-term interest for every country considering the advantages that those investments have for host country.

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Apstrakt

Strane direktné investici predstavujú važnu komponentu ekonomického rozvoja v svijetu. Nanajšíh se gleda k o znácníj katalizor ekonomických transformácií velikog broja zemalja. Iako je ovaj oblik finanširanja okosnica modela rasta crnogorske privrede, svjetska ekonomska kriza pokazala je da se on mora temeljno mijenjati u korist greenfield investicija i izvozno orijentisanih stranih direktnih investicija kako bi se znacajniji efekti mogli vidjeti u nekom dužem periodu.

Ključne reči: strane direktné investicié, grinfild investicié, globalna ekonomska kriza