Outward foreign direct investment by enterprises from Slovenia

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The article evaluates the experience of a small new EU member state as an outward investor. Slovenia's early experience of foreign direct investment (FDI) was in "reverse order", in the sense that it first invested abroad and later allowed inward FDI. Its early start in internationalization and the advantage of knowing "how to do business" in the former republics of Yugoslavia, major destinations of Slovenian outward FDI, made it possible for Slovenia to become a net investor abroad at an early stage in its development. This article also assesses the motives and drivers of Slovenian outward FDI as well as the policies of the Government, which fluctuated from early tolerance of outward FDI ("system escape investment") to restriction and then finally to providing support. The timing and type of reforms were similar to those of some other emerging economies. Outward FDI proved to be instrumental in the development of firms. Outward investors performed better than non-outward investors. Outward FDI also seems to have strengthened the competitiveness of outward investors, large and small, as well as that of the Slovenian economy.

Key words: Slovenia, outward FDI, transnational corporations, competitiveness, development effects, policy

1. Introduction

Enterprise internationalization through outward foreign direct investment (FDI) is not new to Slovenian firms. Slovenian outward FDI dates back to the late 1950s when Slovenia was still part of the former Yugoslavia. This early development shaped contemporary Slovenian enterprise internationalization

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and it is therefore not surprising that some Slovenian companies have become global companies and others have become regional transnational corporations (TNCs). Slovenian enterprises, large and small, invest abroad for various reasons. They do so to improve competitiveness and to expand their market reach. The lion's share of Slovenian outward FDI is directed to neighbouring countries. Geographical proximity and cultural affinity influenced these outward FDI location decisions. The liberal policy environment and institutional support introduced in recent years have also encouraged outward FDI by Slovenian enterprises.

Despite the early start, Slovenia still lags behind many small developed countries in terms of participation in globalization,[1] specifically in enterprise internationalization, as reflected in UNCTAD's outward FDI performance index. Only in the period 2001-2003, did its position climb substantially to 42nd place as compared to 80th place in the period 1997-1999. Slovenia performed better than the average Central and Eastern European countries (CEECs) in terms of outward FDI stock as a percentage of GDP, but lags behind developed countries (UNCTAD, 2004). It also lags behind industrialized countries and the CEECs in terms of the share of services in outward FDI stock (Burger and Svetlicic, 2005, p. 8).

By 2004, 2,402 firms had invested abroad compared to 1,610 in 1995 (Bank of Slovenia, 2005b, p. 41). An average internationalized Slovenian enterprise has affiliates in four different host countries, but few have affiliates in more than ten countries (Jaklic and Svetlicic, 2003, p. 68). The internationalization index suggests that leading Slovenian firms are comparable to those of the world's most transnationalized enterprises (table 1). Slovenian firms lag behind in the transnationality index of the largest TNCs in the world but are more transnationalized compared to other firms in the region. In terms of assets and employees abroad, however, Slovenian

[1] Its position was a little better compared to new EU members in terms of foreign trade and innovation potential but not in terms of the FDI component of the globalization index (Korez, 2005, p. 130).

firms lag behind. In general, Slovenian firms are more globally oriented than those from developing countries. Compared to other transition economies, Slovenia has relatively more home-grown TNCs. This is because the country adopted an open economy policy before the transition period and had a strong export orientation, while its enterprises started investing abroad at an earlier stage. In fact, they started investing abroad before a significant amount of inward FDI began to flow in (Jaklic and Svetlicic, 2003).

This article examines the trends and development in Slovenian outward FDI, before analyzing its drivers and motivations. The article also looks at the impact of outward FDI on investing companies, especially with regard to firm competitiveness and performance. It concludes by assessing obstacles to outward FDI before making policy recommendations.

Table 1. Internationalization of Slovenian firms, 2003

	Transna-tionality Index[a]	Internatio-nalization index[b]	Assets abroad/ total assets	Foreign sales/local sales	Foreign employment/ total employment	Sales/ assets	Sales/ employed
Slovene TNCs[c]	36	60	22	59	23	n.a.	n.a.
The largest 100 TNC in the world	55.8[v]	66	49.8	54.1	49.5	69.3	$0.38 mil.
The largest 10 TNCs from South and Eastern Europe[d]	36.6	n.a.	24.6	56.5	8.5	n.a.	n.a.
The largest 50 TNCs from LDCs 2003	49	48	35	39.9	34.8	72	$0.16 mil.

Source: UNCTAD (2005, pp.17-19) and author's own calculations for Slovenia.

[a] Average of foreign/domestic assets, foreign/domestic sales and employed abroad/employed at home.

[b] Number of affiliates abroad/all affiliates.

[c] The following firms were included: Gorenje, Interevropa, Iskraemeco, Kolektor, Krka, Mercator, Merkur, Petrol and Prevent.

[d] Eight firms from Russia and two from Croatia were included. See UNCTAD (2005, p. 272).

[e] It is much higher in the case of small European states, for which the figure is 72.2.

2. Slovenian outward FDI: trends and development

Historical development

In the historical development of outward FDI from the former Yugoslavia, four stages can be distinguished:

(i) *Infant stage* (1950s-1964);
(ii) *Liberal stage* (1965-1972);
(iii) *Stringent regulation stage* (1973-1988);
(iv) *Political transition stage* (1989-1991).

In the 1950s, outward FDI was mainly a “by-product” of developments in the Yugoslav economic system and a reflection of foreign trade trends. Outward FDI was mostly regulated and reactive to the development of firms’ international activities - a characteristic of the system up until the late 1990s when a more active strategy was initiated. Outward FDI was initially regarded as a mechanism for enterprises to escape from the socialist system to overseas market economies and to operate more freely.

Up until the late 1990s, the motives for investing abroad stemmed from systemic factors, such as the sanctions imposed on Yugoslavia in 1948 and the market-oriented reforms in the 1960s. The establishment of representative offices, branches and affiliates abroad became a way of facilitating imports to Yugoslavia and, later, of promoting exports. Foreign trade was subsequently seen as a desirable activity to bolster the country’s foreign exchange position. These reasons became the primary motives for internationalization. By establishing companies abroad, Slovenian enterprises increased their competitive edge by gaining regular access to foreign exchange without losing the margin between the market and the official exchange rates (Svetlicic, Rojec and Lebar, 1994, p. 365).

The transition stage saw accelerated outward internationalization in spite of many attitudinal barriers. Macroeconomic considerations and the introduction of the market economy played a decisive role in influencing Slovenian attitudes towards outward FDI, particularly in the early 1990s.

Slovenian enterprises acquired new markets abroad to compensate for the loss of the Yugoslav market after Slovenia became independent.

There were at least five reasons for the first (transition) internationalization wave. These reasons include:

(i) the emergence of a free pioneering entrepreneurial spirit;
(ii) the transformation of commercial entities in other parts of former Yugoslavia into companies ("inherited investment");
(iii) the need to continue business cooperation with Serbia, which introduced a formal ban on economic cooperation with Slovenia ("post-box companies");
(iv) political and market uncertainty (e.g. over the recognition of the new state), as a result of which companies abroad were seen as a mechanism to increase the stability of business operations;
(v) the need to transfer financial resources and certain profitable parts of business activities abroad before privatization ("by-pass companies").

Current outward FDI trends

Slovenian outward FDI in the early 1990s passed through three stages. They were:

(i) *the first wave of internationalization* (1990-1993), which saw an increase in outward FDI flows and divestments at the same time;
(ii) *the consolidation phase* (1994-1998);
(iii) *the new wave of internationalization* (from 1999 onwards) (Jaklic and Svetlicic, 2003, p. 46).

Outward FDI took off significantly after 1999 (table 2). The outward FDI stock increased from €0.3 billion in 1994 to €2.2 billion in 2004 (annex table 1).

The main reason for the substantial increase in outward FDI flows in 2003 and 2004 was the improved policy environment. The general climate for outward FDI was much friendlier than before. Slovenian enterprises realized that without internationalization, they would not be able to maintain their competitive positions. Investment opportunities from privatization in some major destination countries also encouraged Slovenian outward FDI to these countries. Globalization pressures intensified competition on cost, which forced firms in labour-intensive activities to relocate production to lower cost countries abroad. The accumulated experiences with outward FDI by Slovenian managers further encouraged enterprise internationalization, while new firms, including many small- and medium-sized enterprises (SMEs), joined the bandwagon to invest abroad.

Table 2. Slovenia: annual outward FDI flows, 1996-2004[a]
(Millions of Euro[b])

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Outward FDI	5.6	27.7	4.9	44.7	71.7	161.2	162.1	421.3	441.0	503.4
Inward FDI	138.2	294.9	194.3	99.2	149.1	412.4	1700.2	270.5	665.2	449.9

Source: Bank of Slovenia (2005a, p. 41) and Bank of Slovenia (2006, p.45).
[a] Annual outward FDI transactions registered in the balance of payments are not directly comparable to the change in book value of stock since this also includes exchange rates and other changes.
[b] In 2004 and 2005, the average €/$ exchange rate was 1.24. For other rates, see Bank of Slovenia (2006, p. 34).

The major destinations of Slovenian outward FDI are nearby lower-income countries, primarily newly independent constituents of the former Yugoslavia. These hosted as much as 56% of Slovenian outward FDI stock in 2004 (annex table 1). The fact that Slovenian firms are also investing elsewhere invalidates the frequently made assertion that they have competitive advantages only in investing in countries of the former Yugoslavia and not elsewhere in the world (Jaklic and Svetlicic, 2001). The EU-15 absorbed 22% [2] of Slovenian outward FDI stock, other CEECs received 13% and other

[2] The relatively low share of outward FDI in the EU is mainly explained by the fact that system-escape and "tariff factories" types of investment have ceased to be attractive. EU's share is expected to increase in the future due to the enlargement and outward FDI to the new member countries.

countries (such as the United States and Liberia) accounted for the remaining 9%.

The largest host country is Croatia, accounting for 30% of Slovenian outward FDI in 2004, followed by Serbia and Montenegro. The third-most important destination was the Netherlands. Despite the rising value of outward FDI to Croatia, the share is declining. Slovenian outward FDI to Serbia and Montenegro has increased substantially since the downfall of the Milosevic regime and because of the progress made in privatization. Exports usually serve as a forerunner to investment, although the two main export markets (Germany and Italy) have not been the main destinations for outward FDI.

Although Slovenian outward FDI in emerging economies is concentrated in the former Yugoslavia (table 3), Brazil and China have been rising as locations for Slovenian outward FDI, even by smaller firms.[3]

Table 3. Regional allocation of outward FDI, by number of affiliates, 2001-2004

Region/country	2001	2002	2003	2004
Former Yugoslavia total	3	12	30	25
Of which				
Croatia	1	-	14	7
Serbia and Montenegro	-	5	12	13
Bosnia and Herzegovina	1	6	4	4
TFYR Macedonia	1	1	-	1
EU-15	2	1	-	1
CEECs	1	3	4	4
Other countries	1	1	2	4
Total	7	17	36	34

Source: author's eassessment from media reports.[4]

[3] For instance, Le Tehnika, a family owned SME manufacturing electronic and mechanical components, has activities in five countries. It was the first Slovene company to establish a production affiliate in China in May 2002 (Sinoslo Technology Sip Co., Ltd. in Suzhou Industrial park near Shanghai). Esotech is another example of a firm that has established asn affiliate in China.

[4] Major newspapers reporting on business issues have been systematically reviewed for the respective period. This also applies to other media reports in this article. In case of conflicting data, additional data were collected for the relevant firms for clarification.

Slovenian companies that have invested abroad – whose number has almost doubled in the last seven years – represent a very modest share of the total business sector in terms of numbers but a significant influence on the total business sector (figure 1). At the end of 2004, there were 2,143 affiliates abroad, which belonged to 959 Slovenian companies (Bank of Slovenia, 2005b, p.26). There was a growing interest in Serbia and Montenegro in 2004 (27 new investors with 44 new affiliates) and the Netherlands (14 new investors with the same number of units). The main reason for investing in the Netherlands seems to be the tax advantages it offers. Some financial intermediary firms have moved their headquarters to the Netherlands.

Figure 1. The importance of Slovenian outward FDI

(Percentage)[a]

Source: Jaklic *et al.* (2005).

[a] Percentage share of total number of firms, exports and employment.

Chemicals, the retail trade and other business activities dominated Slovenian manufacturing outward FDI over the period 2001-2004 (43% of total outward FDI stock in 2004).[5] In 1994, these three industries accounted for just 10% of outward FDI stock. Up until 1999, financial intermediation, excluding insurance, dominated Slovenian outward FDI. Retail firms started to invest abroad substantially only in 2000, while firms in other business activities did so from 2002. Textile firms were among those very late in grasping global changes in this industry

[5] Manufacturing outward FDI contributed 53% to the total outward FDI flows in 2004.

and started to invest abroad substantially from 2001, primarily in lower cost locations. Rising investment in other business activities, such as advertising, marketing and accounting demonstrates the increased competitiveness of Slovenian firms in the main destination countries. Outward FDI in banking is dominated by Nova Ljubljanska banka (NLB)[6] and in insurance by Triglav.[7]

A survey-based study by Ruzier (2005) showed that among the top 25 non-financial TNCs from the CEECs, seven were Slovenian TNCs (UNCTAD 2004, p. 317). Medium- and large-sized Slovenian firms account for a large part of outward FDI in terms of volume, while SMEs dominate in terms of the number of outward investors. Only 16 out of 257 small-sized Slovenian firms (10-250 employees) interviewed invested abroad (Ruzier, 2005).

The internationalization of SMEs in Slovenia is at an early stage, although there are SMEs that are well established as international firms.[8] Some SMEs have used FDI as their first entry to the international market instead of entering through exporting.[9] Most SMEs in the study by Ruzzier (2005) started internationalizing at an early stage of their existence. It took,

[6] NLB has 14 banks abroad (i.e. Bosnia and Herzegovina, TFYR Macedonia, Serbia and Montenegro, and outside former Yugoslavia, Austria, Bulgaria, Germany and Italy). Together they employ 2,835 employees, most of them in the former Yugoslavia. Market shares range from 1% in markets outside the former Yugoslavia to 17.2% in Montenegro, 11.8% in TFYR Macedonia and over 25% in Bosnia and Herzegovina (NLB Annual Report 2004, p. 42-45).

[7] Triglav presently operates in four countries (the Czech Republic, Croatia, Bosnia and Herzegovina and Montenegro).

[8] Two examples are Ultra and Akrapovic. Once an R&D start-up, Ultra is today the leading technology and service provider in Slovenia. Its operations cover the globe with a network of affiliates and partnerships. Akrapovic was founded in 1990 with just six employees, based on the experience gained by the owner in the field of motorcycle tuning. Today, the company employs over 300 highly qualified staff and is now one of the world’s leading makers of high-end exhaust systems.

[9] Out of 919 Slovene firms having outward FDI in 2002, 76% engaged in exporting before they undertook their first outward FDI (Jaklic et al., 2005, p. 33).

on average, 3.3 years for their share of international sales to reach 20%; 57% of them had affiliates in more than three countries; and on average they had about 40% of their sales abroad. They also employed as many as 46% of their workers abroad. Their outward FDI motives included gaining new customers overseas, e.g. through a focus on key foreign market niches, and cost reduction. Good management was considered a very important source of competitive advantages together with the quality of products and services provided by these firms.[10] A number of managers also had previous international experience and possessed good knowledge of foreign languages (Ruzzier, 2005).

Large firms dominate outward FDI in most industries, including the financial and chemical industries.[11] The largest projects in 2003 and 2004 were in the pharmaceutical industry (in Poland, Croatia and Russia); in hotels (in Bosnia and Herzegovina and Montenegro); in trading (in Croatia, Bosnia and Herzegovina and TFYR Macedonia); in banking (in Bosnia and Herzegovina and Serbia and Montenegro); and in transport (in Croatia). Large firms received most of the state aid for outward FDI (36% allocated to 20 projects) in 2003.[12] It is encouraging that 18 SMEs applied for and received 18% of the funds for supporting internationalization.

A study by Jaklic (2004) showed that the difference in the average value of outward FDI between larger (medium and big) and smaller (micro and small) Slovenian companies was not statistically significant. They did not differ significantly in their choice of entry mode. Therefore, the propensity for outward FDI does not seem to be completely tied to the company size, nor does it significantly influence the pattern of internationalization in terms of market choice or product selection. According to the same study, only a minor proportion of sample enterprises were likely to become international,

[10] Human capital seems to have the strongest impact on internationalization (defined broadly to include exports). See Ruzzier (2005, pp. 155 and 163).

[11] Major exceptions are other business activities where there are many medium and even small firms investing abroad.

[12] See Institute for Civilization and Culture (2004).

suggesting the need for steps to enhance relevant firm capabilities (Jaklic, 2004, p. 23).

The average age of companies investing abroad was 35 years (Svetlicic and Rojec, 2006), meaning that companies established in the pre-transition period dominate. This is in line with theoretical predictions that older (i.e. more experienced) firms have a greater propensity to internationalize through outward FDI.

Unlike other transition states where outward internationalization tends to be driven by foreign-owned companies, in Slovenia it is mostly driven by indigenous, locally-owned companies without the participation of foreign capital (Svetlicic and Rojec, 2003). One explanation is the kind of autonomous status that firms received in socialist times. Only 11% of companies that invested abroad were foreign-owned (Jaklic and Svetlicic, 2003, p. 59).[13] Consequently, the idea of Slovenia as a springboard for investing in other countries has not taken root.

The type of market entry has changed rapidly. Of the total number of outward FDI deals in 2003, 45.6% were investments in newly established companies (greenfield investments). They accounted for 33.5% of equity invested abroad. Investments in existing companies accounted for 21.6% of the total number of investments, but for 53.7% by equity value. Of the other investments, 80.5% were made in real estate, mostly in Croatia (Bank of Slovenia 2004, p. 26).[14] According to media reports, acquisitions, which used to be rare, are at least as important today as greenfield investment (table 4). The number of acquisitions has been growing, from four to at least

[13] The only substantial exceptions were Kolektor (but it became Slovenian-owned in 2003) and Lek, which after its acquisition by Novartis in November 2002 became foreign-owned.

[14] New investments refer to cases where a resident is the founder or co-founder of a company. Existing investments are those made by residents in existing companies that they did not establish. Other investments refer to investments made in institutions, branches, foundations, real estate etc.

15 annually in the past two years.[15] This partly reflects the enhanced consolidation process (domestic mergers and acquisitions) in the Slovenian economy since it became an EU member since larger firms tend to use acquisition more than smaller ones (Burger and Svetlicic, 2004, p. 7).

Table 4. Types of market entry, 2001-2004[a]
(Number of investments)

	2001	2002	2003	2004
Greenfield outward FDI	2 (2)[b]	2	13	15 (3)
Acquisitions[c]	3 (6)	6	17	12 (7)
Joint ventures	-	2	1	1 (2)

Source: author's assessment based on companies and media reports.
a The numbers do not correspond to those in table 3 since the type of market entry was not known for all projects.
b Planned ventures are in brackets.
c Defined as more than 50% equity ownership.

Various reasons explain the growth of M&As by Slovenian firms. Recent privatizations in major destination countries, such as Serbia and Montenegro, is an explanatory factor. Another is the accumulated knowledge of Slovenian firms in mastering this form of entering overseas markets.[16] A third reason is the strategic choice to exploit first-mover advantages and take advantage of low prices of firms in less advanced transition economies.

3. Drivers and motivations

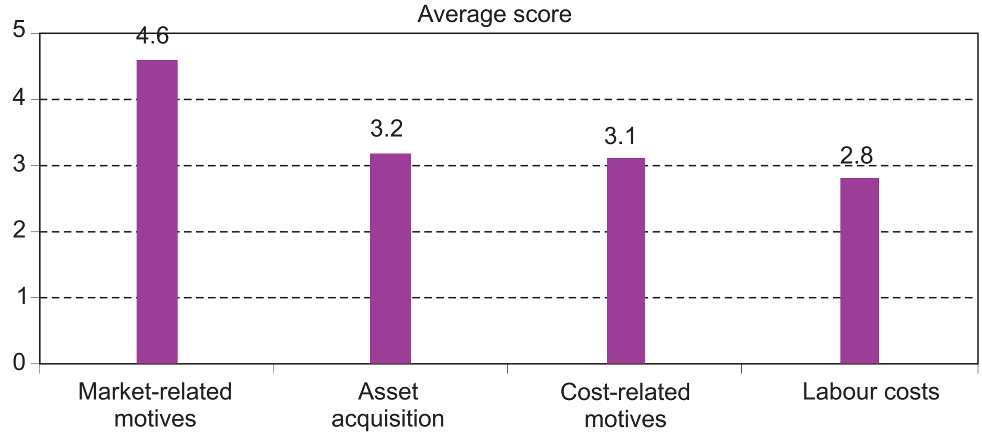
During the early stages of enterprise internationalization, Slovenian firms invested abroad to facilitate trade (strengthening imports or exports) and to escape from the socialist system. The main motives were market-seeking, followed by strategic asset-seeking, efficiency-seeking and resource-seeking (Jaklic and Svetlicic, 2003, p. 114). While cost considerations were not an

[15] Larger acquisitions were notable in the financial, pharmaceuticals, retail trade, electrical appliances and food industries.

[16] Mercator, for instance, has made 23 acquisitions, and all of them have been successful.

overwhelming reason for outward FDI, it is now gaining in importance (table 5).

Figure 2. Motives of Slovenian firms for investing abroad



Source: Jaklic (2003, p. 214).
Note: Average score, 1 = not important, 5 = very important. Valid number of answers: 36.

Table 5. Selected outward FDI by activities and motives, 2002-2004
(Numbers; Millions of Euro)

	2002		2003		2004	
	No.	Value	No.	Value	No.	Value
Other services	3	14	14	93	7	72
Production:	8	43	16	46	35	316
Market-seeking [b]	4	36	6	23	7	147
Third-market-seeking	n.a.	n.a.	1	n.a.	5	34
Efficiency-seeking	4	7	7	14	19	126
Strategic investment [c]	n.a.	n.a.	2	9	4	9
Trade and retail	1	34	8	54	5	23[a]
Total	12	91	38	193	47	411

Source: author's evaluation of media reports.
Note: This table is constructed based on information collected from media and company reports.

a These firms revealed that they plan to invest approximately €124 millions in the trade industry, mostly in shopping centres.

b Motives overlap; therefore, when one motive was not clearly dominant, these investments were included in both activity groups.

c Strategic investments are defined as those aiming to acquire local capabilities, complementary to those of the investor.

The small domestic market and relatively high labour costs in Slovenia are key drivers of outward FDI. Maintaining and expanding foreign market shares have been priorities for Slovenian enterprises. Excess production capacity, which was previously utilized to service the large Yugoslav market, has been another factor. The need to operate close to customers has also encouraged outward FDI. However, internationalization still has a relatively low priority in firms' general strategies (Cater and Pucko 2005, p. 11).

A significant proportion of Slovenian outward FDI in the trading industry relates to the establishment of shopping centres in the region. Large Slovenian trading houses (e.g. Mercator) and smaller ones (e.g. Era) are involved. Slovenian outward FDI in services (e.g. banking, insurance, tourism, trade-related services) has been increasing in order to access local customers. Although labour costs are high and the cost competitiveness of Slovenia is low compared to other transition economies, until recently the relocation of production was rare (Jaklic and Svetlicic, 2003, p. 122). This is surprising given that Slovenia has large textile and footwear industries, which are typically labour-intensive. However, efficiency-seeking (reduction of labour costs) and market-seeking motives are gradually becoming important for the textile, footwear and food industries. Many firms have already started moving their production to South-East Europe, while others are planning to do so. Resource-seeking motives were less important until 2003. Strategic investment in the wider sense (assets-augmenting or the desire to become major players in local markets) is also picking up.[17] There has been an increase in the number of M&A purchases, particularly in service industries, such as banking, trading, tourism, telecommunications and energy.

Foreign affiliates at this stage of internationalization primarily serve to promote exports rather than to engage in international production. As competition in host markets

[17] Many firms declared their outward FDI as "strategic", e.g. seeking third-country markets and even reducing labour costs, but not many would qualify as strategic according to standard definitions.

increases, Slovenian companies have started to follow their competitors and customers abroad. By doing so, they try and exploit the first-mover advantage in those markets where their trademarks are well established. The move overseas is all the more important because of the country's small domestic market. With liberalization and global competition, Slovenian firms will face increasing pressure to internationalize through outward FDI to improve their competitiveness.

The key determinants of outward FDI performance relate to ownership-specific advantages, e.g. the quality of products, knowledge about foreign markets, personal contacts, international experience, skilled personnel and management. Skills and knowledge were the most important preconditions for the success of outward FDI, and the lack of them was the reason for failures (Jaklic and Svetlicic, 2003, pp. 94 and 163). The second most important factor for successful outward FDI was the acquisition of strategic assets leading to an improved international image, higher quality, increased product variety and efficiency.

4. Outward FDI and competitiveness

Analysis of available information shows that investing abroad, in general, has contributed to increasing the competitiveness of Slovenian firms. Outward investing firms performed better than non-outward investing firms. For instance, profit as a percentage of sales is higher compared with non-outward investing firms (table 6). Although the average size of outward investors is significantly bigger than non-investors, only 15% of them were large firms. Firms with direct investment abroad were also more capital-intensive than non-outward investing firms (Jaklic and Svetlicic, 2003, pp.100-103). The major outward investors were among the 100 largest and most efficient Slovenian firms according to sales in 2004 (Finance, 2005). Improved exports, sales and efficiency were the main reasons accounting for the better performance of outward investing firms compared to non-outward investing ones.

Table 6. Selected performance indicators of Slovenian outward investors abroad and non-outward investors, 1994-1998

	Outward investors		No-outward investors	
	1994	1998	1994	1998
Operating profit as a share of net sales (%)	3.3	3.9	3.2	3.1
Net profits per equity (%)	1.5	2.4	1.3	1.1
Value added per employee (Sit billions)	2.22	3.85	3.46	3.21
Return on equity (%)	3.1	4.1	5.9	5.8

Source: Jaklic and Svetlicic (2003, p. 103).

There are risks involved in outward FDI, and not all overseas ventures have been successful (table 7). Outward FDI by chemical firms recorded the largest profits in 2004, followed by those in wholesale, financial intermediation and retail. With the exception of two loss-making activities, all major industries improved their performance in the last four years. Dividends have been constantly rising since 2000. The largest net profits were recorded in Liberia (€13.9 million) and Poland (€9.2 million), while Croatia, which has the largest stock of Slovenian outward FDI, recorded the largest loss amounting to €9.4 million (Bank of Slovenia, 2005b, pp. 29, 74, 75).

Table 7. Earnings/losses of selected Slovenia direct investors abroad, by activity, 2001-2004
(Millions of Euro)

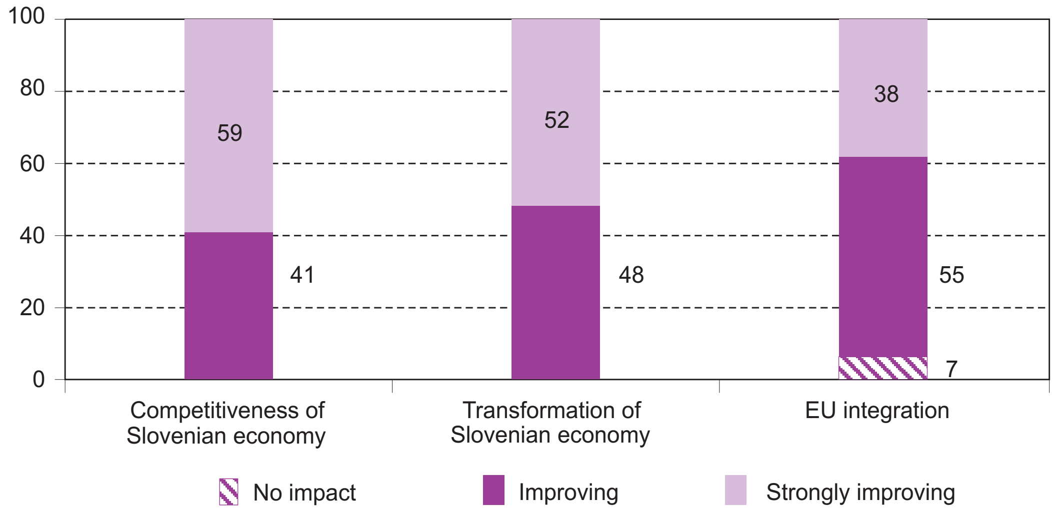
Activity	2001	2002	2003	2004
24. Mfr. Chemicals &chemical products	3.1	2.4	8.5	17.1
51. Wholesale commission, not motors	-1.4	3.8	7.0	11.4
65. Financial intermediation, not insurance	3.8	1.7	5.5	6.7
52. Retail trade, not motor repair	-4.8	-9.9	-1.1	6.0
63.Support; transport; travel agencies	2.6	3.1	4.1	4.3
50. Sale repair etc.	5.5	4.9	5.5	4.3
17. Mfr. of textiles	-0.7	2.1	3.7	4.2
34. Mfr. of motor vehicles, trailers etc	-5.1	-0.6	-0.2	-12.6
15. Mfr. of food products & beverages	0.4	-1.6	-6.9	-15.4
Total	6.3	- 6.1	15.3	46.9

Source: Bank of Slovenia (2005, p.73).

Slovenian managers believe that internationalization through outward FDI strongly influences the domestic economy, improving national competitiveness, supporting transformation and restructuring the economy (figure 3). The effects of outward FDI on enterprise competitiveness were far more important than other effects. Market-seeking investments resulted in increased market shares, growth of exports and domestic production. Outward FDI helped to enhance efficiency and corporate restructuring, although they were not necessarily the initial motives. Some Slovenian enterprises had introduced new and more differentiated products. Having a presence in a foreign market has helped Slovenian enterprises respond to customers' needs more rapidly.

In an econometric study (Jaklic *et al.*, 2005), investing abroad is also shown to have enhanced enterprise competitiveness. Investing firms' "premiums", defined as the average difference (in percentage) in various variables between outward investing firms and the control group in the same industry, are much higher compared to non-outward investors. Such premiums go up to over 100% in terms of employment and sales but not in terms of productivity. Premiums differ in terms of firms' size and other aspects. The largest are in employment in the case of micro and large firms, and sales in the case of small and large firms.

Figure 3. Impact of outward FDI on the Slovenian economy (managers' opinions)
(Percentage)



Source: Jaklic and Svetlicic (2003, p. 174).

In the period 1994-2002, premiums (in sales, profits, productivity) were the highest in the case of outward investors that started to establish affiliates abroad between 1998 and 2000, indicating that at least a two-year time lag is needed for assessing the results of such investment. An analysis of 634 new outward investors revealed that firms had significantly increased their sales in the second year (all firms including SMEs) after investing abroad.[18] They also increased profits (only small firms in the second year) and employment for medium size firms (negative for large firms) (Jaklic *et al.*, 2005, pp. 38 and 67).[19]

An evaluation of all state aid programmes promoting competitiveness and internationalization for the period 2001-2003 provides an even more positive picture of outward FDI performance (Deloitte and the Ljubliana Faculty of Economics, 2004). Most applicants assessed outward FDI projects as very successful. For instance, 76% of the 560 firms that responded to the survey undertaken for this evaluation[20] claimed that their competitiveness had increased; 60% had developed key technologies, 79% indicated that the value-added of their products had increased, and investment in knowledge and the development of human capital had been enhanced. According to the results of the evaluation, the levels of R&D expenditure and skilled labour intensity of Slovenian firms abroad were above the Slovenian domestic average and, their growth rate was above the average rate of Slovenian firms at home during the period 1997-2000 (Jaklic, 2004, p.13).

Outward FDI appears to be complementary to exports. As shown in table 8, the impacts of outward FDI were substantial increases in market shares, exports and production. Internationalization has boosted the development of outward investors, but less so in terms of employment. Our analysis indicates, however, that even in terms of jobs, either the situation

[18] The average effect of investment abroad was assessed by comparing investing firms with control firms.

[19] This may indicate that large firms are increasingly locating labour-intensive production abroad and consequently reducing the number of employees at home.

[20] The details of the sample are available in Deloitte and Faculty of Economics (2004).

has not changed or the outward FDI has created more new jobs overall than displaced existing ones. Furthermore, it does not appear to have reduced domestic investment (Jaklic and Svetlicic, 2003, p. 175).[21] Similarly, the survey of state aid programmes indicated that out of 442 new jobs created by outward FDI projects, only 32 would not have been created if no state aid had been provided. In addition, applicants' assessments indicated that some other jobs, which would otherwise have been lost had outward FDI not occurred, were retained (Deloitte and Faculty of Economics, 2004).

Table 8. Effects of foreign affiliates on the parent company
(Percentage of outward investors)

Effects on:	Strong increase	Increase	Unchanged	Decrease	Strong decrease
Market share	26	53	18	3	0
No. of employees	0	24	59	12	6
Exports	9	74	18	0	0
Imports	0	29	53	6	12
Production volume	9	68	24	0	0

Source: Jaklic and Svetlicic (2003, p. 165).

Slovenian transnational companies' competitive advantages lie in their superior marketing, technology and management skills (table 9). Technological superiority is a result of the much larger R&D expenditure of firms investing abroad compared to the average Slovenian company. Slovenian outward investors increased their R&D expenditures from 3.6% to 4% as well as the percentage of university-educated employees' in the period 1997-2000 (Jaklic and Svetlicic, 2003). The major managerial advantage is their experience of business in the familiar environment of the Western Balkans. Although managers claim that their competitive advantages are long-term and sustainable, a close analysis reveals that some of these advantages are temporary.[22] Therefore, they have to be exploited rapidly before other competitors enter the market. If their only

[21] The correlation coefficient of 0.2 between domestic and overseas investments was statistically significant and positive.

[22] For instance, many products are known to the older generation living in the former Yugoslavia, but not to the younger generation.

competitive advantages were business and marketing knowledge, these advantages would evaporate as soon as other foreign firms become familiar with the host country market. To sustain their advantageous positions, Slovenian firms need to upgrade their capability through technology advancement and new products/brands, among other measures.

Table 9. Competitive advantages of Slovenian investors abroad

Types of competitive advantages	No.	Min.	Max.	Mean	Std. Dev.	Skewness	Kurtosis
Technological know-how	38	1	5	3.9	0.96	-0.79	1.16
Organizational know-how	38	1	5	3.8	1.05	-0.78	0.36
Marketing know-how	39	1	5	4.2	0.97	-1.28	2.10

Source: Jaklic and Svetlicic (2003 p. 125).
Note: 1 = not important, 5 = very important

A number of case studies have shown that the management of companies played a crucial role in outward FDI decisions (Jaklic and Svetlicic, 2003, pp. 181-276).[23] Without the clear and ambitious visions of managers, successful internationalization would have been impossible. A realistic internationalization strategy, management with excellent training, adapted technology and their own R&D efforts[24] have proved to be the key success factors in most cases. Some managers have developed a very specific management style based on personal contacts and are highly assimilated in the cultures of the host countries.

5. Obstacles to outward FDI

Slovenian enterprises face many barriers in their internationalization. In terms of *home country barriers*, the available evidence suggests that enterprises consider the lack of government support as the most challenging factor.

[23] Seven in-depth case studies were prepared and others were evaluated in less detail.

[24] The largest Slovene investors invested from 2.5% to 10% of net sales in R&D. The average for all investors in the sample was 4.1% in 2001. (Jaklic and Svetlicic, 2003, p. 136).

Legislation and the general climate at home and in the host country are considered to play a role in deterring outward FDI. The slow privatization process that held back the internationalization of companies, especially during the early years of transition, was another impediment. Among *host-country barriers,* political instability, high economic risk, the lack of legal frameworks and slow administrative procedures are regarded as major obstacles.

During the transition, many large Slovenian outward investors underwent a disintegration process or found themselves in crisis, which forced them to close down their foreign operations. For affiliates abroad that had been established as ‘system-escape’ operations, the reasons for their existence simply disappeared. Unfriendly political and public opinion regarding outward FDI also discouraged managers from embarking on developing long-term international investment plans. The legislation itself prevented firms from investing abroad before their privatization was completed.

Following this, after the general business climate changed, firms’ internal barriers were seen as being more important than external barriers. The biggest internal barrier to internationalization was the lack of experience, the capacity to manage risks and knowledge, including information on how to invest and operate abroad (table 10). The lack of financial resources was not considered a major barrier, partly because major outward investors are large firms. Therefore, it is not surprising that outward investors financed most of their investments from their own funds and reinvested earnings.[25] However, recently, this has become a more pronounced barrier, especially as SMEs seek to enter the outward FDI arena. They have much more limited access to financing at home.

Slovenian firms also face additional barriers compared with some other international investors. Public opinion initially considered investing abroad as unpatriotic. The relatively high

[25] Reinvested earnings constituted only about 1% of total flows in 2003, although almost all earnings abroad were reinvested.

quality of life in Slovenia makes it difficult to find experienced experts/managers who would be willing to go abroad. The high rate of employment among women, as a consequence of which many of them would be unwilling to discontinue their professional careers to accompany their husbands abroad (or vice versa), adds to this limitation. In short, in the long run, lack of human capital seems to be one of the biggest barrier to internationalization. Another one is the lack of cross-cultural management knowledge required for expanding business outside Europe.

Table 10. Selected micro barriers to outward FDI
(Percentage)

	Very important	Important	Not important
Lack of personnel	51.6	45.2	3.2
High risk	48.4	41.9	9.7
Lack of knowledge	32.3	41.9	25.8
Lack of own funds	30.0	36.7	33.3
Lack of government help	25.0	46.9	28.1

Source: Jaklic and Svetlicic (2003, p.153).

6. Outward FDI policy

Slovenia's policy framework for outward FDI has evolved over time, from the initial restrictive policy to the current generally encouraging regime. The country's legal framework for outward FDI has been adjusted in line with the European Union's regulations, and is regulated by the Foreign Exchange Act of 2 October 2003. The Act on Attracting FDI and Internationalization of Companies, which entered into force in August 2004, further demonstrated the shift of policy towards promoting such a form of international cooperation.

Three key outward FDI policy stages can be discerned in the 1990s:

(i) The inherited Yugoslav liberal regime – the absence of almost any specific regulations related to capital exports (1991-1993).

(ii) The “monitoring” stage – mostly as a response to certain negative aspects of outward FDI in the privatization process (end 1993-1994).

(iii) The gradual application of international standards in the field of outward FDI with full liberalization (Foreign Exchange Law, 1999).

Initially, only legal entities were allowed to establish companies abroad, and a permit to do so was required. In 1993, the Slovenian Parliament passed a more liberal Foreign Trade Law (subsequently amended in 1994 and 1995). After initiating negotiations with the EU by signing the Association Agreement (1996), the process of harmonizing financial and foreign trade legislation started. Liberalization was then driven by the Association Agreement, rather than any specific industrial policy.

In April 1999, Slovenia adopted a new Foreign Exchange Law which was a major step towards the full liberalization of capital flows – adopting a domicile approach and phasing out all restrictions on outward FDI. Outward FDI became to be seen as a restructuring instrument and was to be promoted. In 1999, the then Ministry of Economic Affairs introduced a new concept of industrial policy – enterprise and competitiveness development. The newly created Ministry of the Economy (ME) sought to expand exports and to enhance the internationalization of SMEs’ businesses through attracting strategic foreign investment and promoting outward FDI by Slovenian companies. In 2002, a special promotional programme for outward FDI was launched[26] as part of the promotion of entrepreneurship development and competitiveness.[27] The programme attracted

[26] Firms could receive support for (i) the preparation of projects up to the registration of an affiliate abroad (feasibility studies, training); and (ii) starting-up operations abroad and the strengthening of development work in the parent company (financing of mentors, production start-up costs, material investments etc.).

[27] Altogether 17 programmes were included; of which two were for stimulating exports by SMEs and one was for stimulating inward FDI.

a large number of projects and all the designated funds were allocated.

Table 11. Evaluation of the outward FDI programme

	2003	2004
Number of applications	100	79
Number of projects approved	48	63
Number of SMEs receiving state aid (share in value)	28 (36%)	38 (42%)
Approved state aid (millions of Euro)	1.7	2.1
Total value of projects (millions of Euro)	19.79	10.33
Share of state aid in total project costs (%)	0.68	2.03
Share of this programme in all state aid programmes (value; %)	6.3	11.4

Source: Andric (2003, pp. 8-9; 2004, pp. 7-8).

The Act on Attracting FDI and the Internationalization of Companies (August 2004) can be considered as a first sign of a new policy of actively promoting outward FDI. This received further momentum when the government acknowledged the deteriorating competitive position of Slovenia[28] and increasingly recognized the important role of outward FDI in improving competitiveness. The policy of the government since December 2004 has been to provide specific support for outward FDI, which includes (i) a programme for the internationalization of firms 2005-2009 and (ii) a programme on the establishment of new business representative offices abroad.

The Government has also signed bilateral investment treaties so far with 47 countries, covering all major destination countries for outward FDI, including India and China.[29] Conventions on the elimination of double taxation with 35 countries are also in force.

7. Conclusion

The systemic factors explaining the early internationalization of Slovenian firms also explain the reverse

[28] Of these, 12 are in countries where economic counsellors are already located while four will be those of the PAEFI.

[29] There is no such treaty with Brazil, however.

sequence of Slovenian internationalization (outward FDI started before inward FDI). Slovenian firms are investing abroad through greenfield investment as well as through acquisition, particularly that of privatized assets. The major Slovenian outward investors are large and medium-sized firms, although smaller ones, following a niche strategy, are catching up in terms of number. At first glance, some of these firms, including SMEs, appear to be "born global" although their level of internationalization is still very limited. Such companies may be "born multinational", but that does not apply to their management, which comes mostly from large (previously socialist) companies where they acquired their basic knowledge of internationalization. Most of the firms investing abroad are "leapfrogging globals", i.e. they become global in a very short time by jumping over some stages predicted by evolutionary models.

The strongest advantages of Slovenian firms, particularly in countries of the former Yugoslavia, are partly inherited from earlier periods and partly developed later by faster transition. Their "leapfrogging" internationalization is strongly motivated by the desire to attain a first-mover advantage, since the firms' competitive advantages in these markets are in knowing how to do business and having networks in neighbouring countries. Some advantages are temporary in nature and must be enhanced with firm-specific marketing, organizational and technological advantages.

The search for markets has been a major motive for outward FDI. Efficiency-seeking FDI has only begun to pick up over the past few years, indicating that firms are perhaps slow in responding to rapid changes in the global economy. After harmonizing the outward FDI regime with the EU's regulations, firms' internal factors are becoming the main barriers to outward FDI. Even for larger firms, the lack of experienced managers who are willing to go abroad has become a major impediment. However, for SMEs, particularly newcomers, the lack of capital is an additional problem.

Most of the accumulated stock of FDI has been in countries of the former Yugoslavia. Although it is still too early to evaluate many of the relatively young outward FDI projects, the high satisfaction of outward investors suggests that they are on their way to achieving their objectives. There have been very few outright failures. Outward FDI has enhanced firms' competitiveness, helped develop new products and services, increased exports and generated employment at home and abroad. The most successful Slovenian outward investors (e.g. Gorenje, Kolektor, Krka and NLB) are now competing in the world market with TNCs from developed economies. Outward FDI is therefore instrumental for the growth of Slovenian firms and for the growth of the country's economy. ■

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Annex

Annex table 1. Slovenia: outward FDI stock, by destination, 1994-2004 (Millions of Euro)

	1994	1997	1998	1999	2000	2001	2002	2003	2004
Total stock year-end	289.0	416.0	543.0	625.0	825.0	1,139.0	1,470.0	1,889.0	2,231.0
Former Yugoslavia	205.0	282.0	366.0	408.0	530.0	664.0	855.0	1101.0	1,269.2
Croatia	157.3	219.8	292.9	307.7	380.2	452.2	530	617.3	679.1
Bosnia and Herzegovina	12.0	17.7	21.6	32.4	67.9	109.5	170.0	208.6	217.0
Serbia and Montenegro	22.7	26.7	29.9	28.2	31.9	49.0	95.0	205.7	291.6
TFYR Macedonia	13.0	17.5	21.4	39.2	50.1	53.3	60.0	75.7	81.5
CEECs	25.1	55.9	61.1	87.2	120.1	179.4	227.0	272.2	300.1
Poland	10.8	29.4	33.3	48.3	60.7	89.0	101.0	117.0	132.8
Russian Federation	3.9	8.4	7.9	10.3	19.6	39.2	56.0	67.0	76.3
Romania	0.3	2.2	3.8	4.6	5.9	14.2	22.0	21.6	25.2
Bulgaria	0.1	0.4	0.5	0.7	1.2	2.1	9.0	20.3	4.5
Czech Republic	2.0	8.1	3.8	4.5	13.0	13.9	14.4	19.3	25.5
EU	33.2	43.2	77.9	96.0	117.5	210.6	303.7	359.6	484.0
Netherlands	3.0	-0.2	0.8	0.4	-0.6	19.3	103.5	146.3	252.8
Germany	24.9	31.1	37.1	43.6	44.1	99.6	108.8	105.9	104.4
Austria	7.8	14.6	28.5	26.2	41,0	57.6	62.5	65.9	81.5
Others	25.3	35.6	38.1	34.0	57.6	85.2	76.7	115.7	156.0
United States	11.3	20.5	15.6	21.4	27,9	41.0	23.2	80.3	54.9
Liberia	13.5	26.0	15.5	22.6	25.9	27.0	20.0	19.7	32.6

Source: Bank of Slovenia (2004, p. 57) and Bank of Slovenia (2005b, p.57) for 2004.

Note: These figures do not include real estate owned by Slovenian households abroad (mainly real estate in Croatia); claims on other countries within the territory of former SFRY that are the subject of negotiations on succession; expropriated assets within these territories; and other assets transferred to the Government of Slovenia during the privatization process.

Annex table 2. Slovenia companies with direct investment abroad, by main destinations, 1996-2004
(Cumulative number)

	1996	1997	1998	1999	2000	2001	2002	2003	2004
Total	503	508	553	567	627	779	929	943	959
Former Yugoslavia									
Croatia	323	344	386	397	428	519	615	626	621
Serbia and Montenegro	72	76	77	73	80	128	207	244	287
Bosnia and Herzegovina	65	78	89	109	139	176	201	204	203
TFYR Macedonia	66	68	63	61	63	69	80	83	81
EU-15									
Germany	85	77	73	65	70	65	78	74	78
Austria	92	62	59	52	59	54	55	53	60
Italy	49	48	43	39	43	49	47	40	44
United Kingdom	8	8	7	8	11	12	15	18	19
Netherlands	5	5	6	4	5	7	8	23	35
CEECs									
Hungary	34	26	24	23	27	31	32	28	30
Czech Republic	28	28	30	26	28	34	33	31	32
Russian Federation	21	20	23	24	27	30	33	34	45
Poland	11	13	15	15	20	27	27	28	27
Others									
United States	25	24	22	27	31	39	40	34	30

Source: Bank of Slovenia (2005b, p. 65).

Annex table 3. Slovenia: outward FDI stock, by industry, 1994-2004

(Millions of Euro)

	1994	1997	1998	1999	2000	2001	2002	2003	2004
Mfr. chemicals and chemical products	35.2	51.9	74.2	104.9	143.2	195.5	244.9	337.8	349.4
Other business activities	16.1	23.7	43.2	59.7	60.6	99.3	243.8	291.8	362.0
Retail trade, excl. motors; repairs	8.2	-12.7	7.6	13.0	68.4	125.1	152.1	212.5	238.7
Mfr. of machinery and equipment nec.	11.6	45.2	57.6	65.5	87.3	105.4	115.0	125.8	141.2
Mfr. of food products and beverages	24.8	29.1	31.6	39.4	68.7	86.9	101.7	113.5	108.2
Financial intermediation, excl. insurance	33.5	72.2	68.7	73.9	83.0	106.0	91.5	99.9	166.1
Manufacture of textiles	-2.5	6.2	-2.9	0.5	6.7	54.5	63.2	84.3	69.6
Wholesale, commission, excl. motors	47.4	43.2	35.0	33.3	25.5	37.6	52.9	61.4	113.6
Mfr. of motor vehicles, trailers etc.	-10.9	5.8	28.2	17.1	17.7	36.9	39.3	52.3	52.4
Support transport; travel agencies	4.6	7.5	8.3	16.6	21.5	34.0	42.7	46.3	50.3
Sale, repair etc. motors; fuel	-22.6	-35.3	-6.8	-15.6	-19.1	-3.1	-4.2	44.0	90.3
Total above activities	145.4	236.8	344.7	408.3	563.5	878.1	1142.9	1469.6	1,211.2
Total outward FDI	288,6	416,2	542,8	624,7	825,3	1.139,2	1,461,5	1.848,9	2,200.3

Source: Bank of Slovenia (2004, p. 68).

Annex table 4. Level of internationalization of Slovenian firms included in the list of the top 25 non-financial TNCs from Central and Eastern Europe, plus Kolektor and Prevent, 2004

	Internationalization index*	Network spread index**	Transnationality index***
Interevropa	75 (with branch off. 117)	5.1	40
Iskraemeco	90 (with ass.comp. 100)	8.2	38
Kolektor	42	4.1	48
Krka	93	6.2	55 (without assets)
Gorenje	67	11.2	50 (53 after acquisitions in 2005)
Mercator	24	1.5	16
Merkur	80	4.1	15
Prevent	30 (with branch off. 117)	4.1	54
Petrol	42 (45 without parent comp.)	2.6	11
Average	60	5.2	36
Memorandum: average for 100 largest non-financial TNCs	65.46	17.93	n.a.

* Internationalization index; number of foreign affiliates/number of all affiliates x 100

** Network spread index = number of host economies/number of potential host economies (those having inward FDI stock; for 2003 this is 195); see UNCTAD 2004, p. 280

*** Transnationality index = is average of 3 ratios: foreign assets to total assets; foreign sales to total sales; and foreign employment to total employment*100; see UNCTAD 2004, p. 317

Annex table 5. Level of internationalization of Slovenian firms included in the list of the top 25 non-financial TNCs from Central and Eastern Europe, plus Kolektor and Prevent. 2004

	Foreign employment/ total employment	Foreign assets/ total assets	Foreign sales/ total sales
Interevropa	0.40	0.20	0.59
Iskraemeco	0.15	0.08	0.91
Kolektor	0.28	0.32	0.85
Krka	0.30	n.a. for assets	0.79
Gorenje	0.09 (0.18 after acq. in 2005)	0.48	0.94
Mercator	0.15	0.21	0.13
Merkur	0.11	0.06	0.15
Prevent	0.49	0.31	0.82
Petrol	0.11	0.12	0.09
Average	0.23	0.22	0.59

Note: Data for 2004 based on annual reports, data available on the Internet and direct communications with firms. Data for groups refer to consolidated balances.