FDI and industrial upgrade of Albania

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Abstract

Foreign direct investment (FDI) in developing countries brings economic development and enhances the international competitiveness of domestic enterprises. The entrance of FDI would normally be considered as a prerequisite for the success of the introduction of foreign capital. FDI accounts for the largest and most important proportion of foreign capital in Albania, which undoubtedly plays an important role in the Albania's economic development growth and country. However, as the country continues to taking various preferential policies to promote foreign investment and the good momentum of Albania's economic development, FDI increases, and in this paper we want to evaluate how the FDI has influenced the technological progress of the country. In general, multinational companies have advantages of capital, technology or management-intensive elements, if there is no foreign direct investment, for the host country producing new industries or upgrading of the structure of traditional industries shall be more difficult. The promoted technological progress and management level can lead labor force, labor tools to have productivity growth and can lead directly to changes in the structure of industrial technology. FDI inflows give the "package" of resources, technology and management skills needed not only to help the host country to establish new industries, but also to help host country to promote inter-industry structure within a structural optimization and industrial upgrading. Based on the theory of FDI, this paper through a theoretical analysis and an analysis on data on country's data reaches conclusion that FDI has positive effects on industrial upgrade in Albania.

Keywords: FDI, Albania, industrial upgrade.

Introduction

FDI (Foreign Direct Investment) is an important way of international capital flow. International Monetary Fund (1985) refers to international direct investment as obtaining a lasting interest in the investment carried out in a foreign enterprises with the aim to gain practical business management control; OECD (1996) thinks that international direct investment is when residents of a country (direct investor) in another country or countries residents (direct investment enterprises) conducts activities for the purpose of obtaining a lasting interest. Thus, the international direct investment and enterprise "effective control" or "lasting benefits" are closely related and, therefore, we believe that FDI means that international investors to participate in the production and business activities of enterprises, having actual management, controlling investments in right way and investing purpose is to obtain durable profits. We believe that a country's or region's FDI utilization ability is not only ability to attract foreign investment but also from the larger, broader perspective to think that the host country is considering FDI in promoting industrial restructuring, promotion of enterprise technology progress, and increase local employment and tax revenue,

promoting the role of foreign trade and other aspects of the series. Based on this, we define FDI utilization ability as follows: The so-called FDI utilization ability shows how the host country's legal and regulatory framework attracts foreign investment, how FDI effects the local economic growth, industrial restructuring and technological progress, residents' employment, how positive is the contribution to foreign trade development. The multinational companies with advanced technology with regard to keep the technological leadership, get competitive advantage by maintaining its technological dominance, they always take actions to prevent the spillover of core technology. From the foreign policies of FDI utilization in these states, they all paid high attention to the effect of technology progress, especially the developing countries, they took various measures to induce foreign investors to play the role of technological promoting effect. Take Brazil as the example, the government required that all the technology and equipment which can offered domestically are not allowed to use FDI, at the same time, took measures on loans, tax, ordering, supply of raw materials, etc., try to promote the foreign companies to expand the production of capital goods, transfer the technology, shorten the duration of the technology confidentiality. Korea also put great emphasis on the technological progress effect of FDI, actively introduced advanced foreign technology, strengthen the digestion and absorption of imported technologies, for those industries that foreign companies are unwilling to transfer their technology by technical trade, such as chemical industry, electronics and automotive industries, the government will encourage them to invest in Korea. Another example, Singapore put emphasis on the transplantation of science and technology during the FDI utilization process, actively absorbed the FDI of the technology-intensive industries, capital-intensive industries and knowledge-intensive industries, advocated the domestic capital and foreign capital set up joint venture associates in order to play the effects of the FDI technological progress. Albania's FDI is increasing day by day since the opening of country's economy after 90's, and a lot has entered since than in the country's technology.

Literature based on FDI effects to industrial structure adjustment and upgrade

Vernon (1966) research pointed out that multinational companies based at product stages take different strategies at different stages, through direct investment in developing countries will transfer to the host country certain products technical level, and thus will influence a certain impact on the structure of host country's industry; at the same time, developing host countries can through attraction of FDI build a number of not yet formed industries, but still yet the host country shall find it difficult to cross and level the gap between its industry and investor country's industry. After that, some theories came up such as: labor-intensive industrial structure, marginal industrial theory, flying geese model theory, growth stage theory etc., which all predict international transfer of industry where the host country uses FDI inflows to upgrade the industrial structure adjustment. These theories suggest that FDI can effectively enhance the comparative advantages of host countries, thus promoting industrial structure adjustment and upgrade host country industries. Frank Barry (1999)

analyzed Ireland, Britain, Spain, Portugal, four countries data and by comparing the industrial structure upgrading in these countries, concluded that FDI inflow during the upgrade played a very important role in promoting host country's industrial structure upgrading. Nigel Driffield (2001) analyzed the concentration of FDI on the impact of British industry, and thinks that FDI inflows increased competitive pressure within the enterprises and reduced the excessive concentration of industry so it made possible UK's industrial upgrading. Many scholars have made studies on China FDI inflows effect to industrial structure, most empirical analysis shows that FDI in China has promoted industrial upgrading. Representative literature of which are: Wang Luolin, Jiang Xiaoyuan, Lusheng Liang et al (2000) which pointed out 500 worlds biggest enterprises investment projects in China and the effect of these large-scale investments will help enhance China's industrial structure. Fu Qiang, Zhou Kehong (2005) pointed out that China's domestic industrial restructuring and foreign investments in China have a strong correlation. Since open up reforms from 1978, FDI inflows to China greatly promoted industrial upgrading and improved competitiveness of various industries. In summary, we see that evaluation of a country's or region's FDI utilization ability involves many indicators, these indicators require not only theoretical support, but also must be based on empirical basis on data analysis testing. Therefore, exploration and research of this topic has some difficulties. Because of this, in order to successfully make a research on countries of South East Europe FDI utilization ability we have to grasp its main aspect and give up some minor factors. After review of literature, we create an idea that a country's or region's FDI utilization ability is mainly reflected on economic growth, industrial restructuring, technological progress, trade and other major impacts.

Host countries ability to use FDI in industrial structure upgrading

In 30's of 20th century , British economist Fisher first proposed the concept of the three economic stages of mankind; he thinks that in history of the world economy, development of human activities has gone through three phases: In the first phase, the primary production stage, production activities was based largely on agriculture and animal husbandry; the second phase began in the British Industrial Revolution, which brought rapid development of large-scale industrial production with the symbol industries such as textile, steel and other manufacturing having rapid rise and development; third phase began in the early 20th century, a lot of labor and capital flows entered travel, entertainment, culture, arts, health, education, government and other activities. These phases respectively phase of primary production industries, second phase of industry and the third phase of industry are called primary industry, secondary industry and tertiary industry, this classification began from the late 50's 20th century. In many countries, is widely used in economic statistics. Generally it is believed that FDI has played a positive role in evolution to the host country's industrial structure. Most of the existing research results from the point of view in demand structure changes, changes in factor supply, structural changes in international trade and international industry transfer try to explain the effects of

FDI to industrial structure on the mechanism of the host country. First, we look at FDI enterprises demand to lead to upgrade industrial structure, of the host country. Cao Junwei (2002) pointed out that the inflow of FDI may cause changes in the structure of the host country needs and demand; above all, changes usually are caused in the intermediary demand. FDI enterprises usually use the local advantages of resources for production, for example many of FDI inflows into China take advantage of cheap labor and other related raw materials. In this case, FDI enterprises have an enormous demand-pull effect on the upper reaches of industry, promote quality improvement and production of technological progress of raw materials and intermediate products, thus it promotes development of these industries and stimulate the upgrading of industrial structure. Based on this, we can see that emergence of demand prompted direct promotion of the industrial structure changes, while FDI inflows which brought changing to the demand structure of the host country, at the same time leaded to changes in industrial structure. Secondly, FDI inflows enhanced host country's level of technological progress and management, which to some extent, changed the trend of production factors diminishing marginal returns, thus changing the input-output structure of the host country and promoting the development of related industries. The promoted technological progress and management level can lead labor force, labor tools to have productivity growth and can lead directly to changes in the structure of industrial technology. FDI inflows give the "package" of resources, technology and management skills needed not only to help the host country to establish new industries, but also to help host country to promote inter-industry structure within a structural optimization and industrial upgrading. In general, multinational companies have advantages of capital, technology or management-intensive elements, if there is no foreign direct investment, for the host country producing new industries or upgrading of the structure of traditional industries shall be more difficult.

Foreign direct investment (FDI) in Albanian economy and analysis of country's industrial upgrade

The competitive advantages of a country are particularly important in the field of direct investment. Albania has significant opportunities to attract foreign direct investment, among them its geographic position (ports in the Adriatic and the Ionian Seas); natural resources; an educated labor force; and competitive salaries. All of these are attractive elements to foreign investors. Consequently, our country will gain great economic benefit from FDI. Experience has shown that foreign direct investment has had a major impact on the economic growth of a country. Some of these benefits are:(1) An increase in competitive potential between domestic production enterprises. FDI increases the pressure, enabling stronger competition between domestic producers;(2) The entrance of advanced technology;(3) Experience of the skills of management;(4) Progress in knowledge of various fields of production resulting from contacts with foreign customers;5) Possibilities for the optimal utilization of human resources, which represents a major source for development in Albania and also it helps to increase their professional skills.

Analysis: The ability of using FDI to promote industrial structure upgrading

The industrial structure upgrading means the industrial structure shift from low technology level to high technology level, from dominant industries with low productivity to dominant industries with high productivity. One purpose of the introduction of FDI is to lead the local industrial structure upgrading by FDI enterprises, with the expectation of the host country which is to occupy a part of higher value added section in the international industrial chain. All researches made on Albania, every scholar who has made an article on FDI for this country absolutely agrees that the FDI inflows have brought rapid development in the country's industrial upgrade. Since 1990 when Albania's FDI was practically 0 and now that it has very open policies, the structure of Albanian economy has totally changed, and the output of each sector of economy is bigger than the entire GDP of Albania at 1990. Many scholars have said that FDI has some certain influence on industrial structure upgrading, but there has no indicators to measure the extent of the effect. In accordance with the research on the Quality of China's use of FDI by Han Gang (2005), he considered that the influence of FDI on industrial structure upgrading mainly reflected in the inter-industrial structure upgrading and the structure optimization within the industry. Here we use the research methods of Han Gang (2005) as reference and try to introduce the relative strength of FDI in service industry and the relative strength of FDI in manufacturing industry as the measure indicator to measure the influences of FDI utilization in Albania on the inter-industrial structure upgrading and the structure optimization within the industry. The formula is as follows:

$$OSFS = \frac{FDI_3 / FDI}{GDZC_3 / GDZC} \quad (4.1) \qquad OSFM = \frac{FDI_M / FDI_2}{GDZC_M / GDZC_2} \quad (4.2)$$

OSFS and OSFM indicate the FDI investment strength in service and manufacturing, FDI_2, FDI_3, FDI_M, FDI express the FDI in the second, third, manufacturing industry and the total FDI in different industries, $GDZC_2$; $GDZC_3$; $GDZC_M$;GDZC represent the fixed asset investment of the second, third, manufacturing industry and the total fixed asset investment in different industries. On the above formula, the greater the value of OSFS and OSFM that suggests the FDI has a larger effect on the inter-industrial structure upgrading and the structure optimization within the industry in Albania. Based on the statistic data offered by Bank of Albania from 1998 to 2008 (tab 4.1), the results are shown in tab.4.2. From the table we can see that the effect of FDI utilization on domestic industrial structure upgrading is growing in recent years.

Table 1. Data on primary, secondary and tertiary sectors of economy of Albania

	FDI	% of Primary industry to GDP	% of Secondary industry to GDP	% of Tertiary industry to GDP	Fixed assets total investments (mn USD)	Manufacturing fixed assets total investments (mn USD)	Secondary industry fixed assets total investments	Tertiary industry fixed assets total investments	FDI Manufacturing sector investments	FDI secondary sector investments	FDI Tertiary sector investments
	Mn USD	%	%	%	Mn USD	Mn USD	Mn USD	Mn USD	Mn USD	Mn USD	Mn USD
1998	138.0	26.58	40.79	32.63	274169.91	154906.00	170677.97	89105.25	74.60	92.70	31.70
1999	185.0	24.16	42.81	33.03	318315.47	189397.70	203403.58	97086.72	100.70	114.30	58.60
2000	152.5	22.92	43.01	34.07	355669.49	216958.39	227628.47	112747.23	82.90	89.60	49.30
2001	207.3	21.66	43.49	34.85	408358.02	232764.07	256857.19	121282.36	116.40	134.20	66.20
2002	135.0	18.85	44.82	36.33	410989.10	226044.00	274951.71	122885.74	80.60	95.00	32.80
2003	178.0	19.37	45.08	35.55	460927.27	270593.91	315613.07	157988.55	83.10	94.80	51.70
2004	341.8	17.85	41.56	40.59	521795.67	312555.61	336036.41	164365.63	192.10	211.10	94.50
2005	264.5	16.72	43.24	40.04	559765.33	321865.06	363791.49	177725.49	155.50	179.50	75.90
2006	306.7	16.30	44.60	39.10	632543.70	366875.34	404195.42	192925.83	167.90	197.40	89.80
2007	389.4	15.98	46.63	37.39	635089.57	353744.89	419730.70	189574.24	216.80	234.30	134.60
2008	343.9	14.88	46.77	38.35	706025.68	377608.09	458210.66	225575.21	199.80	208.70	132.90

Data Source: CES DATABASE

Table 2. FDI Relative intensity of the third and manufacturing industry

Year	OSFM	OSFS
1998	0.89	0.71
1999	0.95	1.04
2000	0.97	1.02
2001	0.96	1.08
2002	1.03	0.81
2003	1.02	0.85
2004	0.98	0.88
2005	0.98	0.90
2006	0.94	0.96
2007	1.10	1.16
2008	1.16	1.21

Conclusions

Albania, a formerly closed, centrally-planned state, is making the difficult transition to a more modern open-market economy but in the last few years has achieved more success than its neighbors, this because it has better geographic position, younger population and much more natural resources than all other neighbor countries

together. Services (tertiary industry) FDI relative intensity already reflects the impact of FDI on the inter-industry structure upgrade, it is represented as the ratio of FDI refers to the proportion of tertiary industry and the fixed assets investment's proportion to the tertiary industry, measuring the relativity of foreign investment strength in tertiary industry and the intensity of total fixed asset investment.

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