POLITICAL RISK AND QUALITY OF GOVERNANCE AS DETERMINANTS OF FOREIGN DIRECT INVESTMENTS IN THE TRANSITION COUNTRIES

Miloš Dašić

Academy of Vocational Studies of Southern Serbia

✉ *dasicmil@yahoo.com*

Abstract: This paper uses dynamic panel data methods to examine the political indicators and governance quality indicators as determinants of foreign direct investment (FDI) into the Balkan and non-Balkan countries in transition. Our empirical model shows that the determinants, such as political terror scale and the control of corruption, have significant and plausible effects in the Balkan and non-Balkan countries in transition. In addition, analyzed factors such as government effectiveness and regulatory quality, which play important political roles in determining foreign direct investment flows into countries in transitions and help explain the differing attractiveness of individual countries to foreign investors in our empirical model, do not play a significant role in the inflow of foreign direct investment

Keywords: inflow FDI, governance quality, Balkan and non-Balkan countries

JEL classification: P27, E20, E27, F21

1. Introduction

This paper examines the political indicator and governance quality indicators as determinants of foreign direct investment into the Balkan and non-Balkan countries during their transition towards a market economy. In the last three decades, the Balkans and other Central and Eastern European countries have been in the process of transition from a socialist, centrally planned economic system to a capitalist market economy system. The speed and success of the transition of these countries is different due to a number of factors. In the observed Balkan and non-Balkan countries, the transition process did not start at the same time, nor is the time

period of its duration the same. Prior to joining the EU, the countries that became members of the EU underwent the transformations of their economic structures (Czech Republic, Hungary, Poland, Slovakia, Bulgaria, Croatia and Romania), while the other observed countries are still in the process of transition and the EU accession (Albania, Bosnia and Herzegovina, North Macedonia and Serbia). However, almost all of these countries have a significant share of FDI inflows as a factor in their development (see more: Di Mauro, 1999 and Buch, Kokta & Piazolo, 2001; Gorbunova, Infante & Smirnova, 2012). In this regard, Walkenforst (2004) emphasizes that in these countries FDI has played a major role in economic restructuring and has provided significant support for transition and the development of market-oriented economies.

Prior to the start of the transition, strict restrictions on FDI inflows were applied in the observed countries. By removing barriers to foreign capital entry and expanding trade relations with developed industrial countries, potential conditions have been created for rapid productivity growth, as well as opportunities to implement necessary reforms of market structures (UNCTAD, 1997). In the mentioned circumstances, the importance of FDI for the implementation of the process of transformation of the former centrally planned economies came to full expression, especially in the most successful countries, such as the Czech Republic, Hungary, Poland and Slovenia. These countries have been very successful in attracting FDI, largely due to a favorable institutional and political environment conducive to investment activity (Infante & Smirnova, 2009).

In the early years of transition, FDI mostly went to the manufacturing sector to take advantage of market-seeking FDI, or to establish more efficient production processes (Efficiency-seeking FDI). In the last decade, FDI has changed its direction and moved from the manufacturing to the service sector, first in the telecommunications sector and later in the financial sector (banking and insurance) (Gorbunova, Infante & Smirnova, 2012). Different FDI inflows have been driven by a variety of factors, such as uncertain or partial reforms in many countries, high social transition costs, and the presence of corruption and political instability. The influence of quality of governance as determinants of foreign direct investment and other determinants of FDI inflows in transition countries has been specifically addressed by Schneider & Frey (1985), Bevan & Estrin (2000), Kinoshita & Campos (2002), Carstensen & Toubal (2003), Globerman & Shapiro (2003), Azizov (2007), Benassy-Quere, Coupet & Mayer (2007), Mottaleb (2007), Khacho & Khan (2012), Liargovas & Skandalis (2012), Gorbunova, Infante & Smirnova (2012), Popovici & Calin (2012) , Soumia & Abderrezzak (2013) and Abbas & El Mosallamy (2016), etc.

The impacts of quality of governance variables are estimated within a dynamic panel data framework. By employing a dynamic panel data approach, we incorporate all available information in the cross section and time series dimensions (Carstensen & Toubal, 2003, p. 4). Accordingly, the structure of this paper is as follows. The second section presents the methods and data used in the

analysis, and the third presents a comparative analysis of independent variables in considered Balkan and non-Balkan countries. Section 4 gives modeling results separately for the non-Balkan countries and for Balkan countries. Finally, Section 5 concludes with a discussion and some suggestions for the considered countries.

2. Methods and data

In this research we analyze and compare 2 groups of countries in transition. The first group consists of 8 Balkan countries (Albania, Bosnia and Herzegovina, Bulgaria, Croatia, North Macedonia, Romania, Serbia and Slovenia), while the other group consists of 4 non-Balkan countries (Czech Republic, Hungary, Poland and Slovakia). Both groups of countries are analyzed within the same time range - from 2002 to 2019.

The following methods were used in the analysis: descriptive statistics, ANOVA and dynamic panel models. The statistical software "SPSS" conducted a descriptive statistical analysis of data, in order to clearly and reasonably display and describe the basic characteristics of the panel series of data, and determine the basic statistical indicators. For better clarity, the results of the research are presented in tables and graphs. To examine whether there is a difference between the two groups of selected countries in transition, variance analysis (ANOVA) is used to investigate the difference between the mean values, which allows describing the complex relationships between the variables. The testing results are presented with values of registered F statistics and p-value, and supported by values of mean and standard deviations.

The research uses panel data consisting of cross-sectional units observed in different time periods. The combination of cross-sectional data and time series within the panel data allows for richer econometric model specifications and more accurate conclusions. In addition, dynamic adjustment processes can be analyzed for a wide range of cross-sectional units. In order to investigate the influence of past observations of the variable on the current value and to explain the persistence of the dependent variable, the research analysis was conducted using a dynamic panel data model.

2.1. Methods

In literature, the analysis of determinants of foreign direct investment (FDI) is often based on gravitational models, and to explain the consistency of FDI, Kimura & Todo (2010), Olivero & Yotov (2012), and Kahouli & Maktouf (2014) set dynamic equations of gravity. Therefore, it is common practice in empirical work to apply the Generalized Method of Moments (GMM), the framework proposed by Arellano & Bond (1991), Arellano & Bover (1995), Blundell & Bond (1998), and further developed by Binder et al. (2005), Bun & Windmeijer (2010) and others.

In the analysis of panel data series, linear models are most often used, and here, comparative data and time series of data are combined.

$$y_{it} = \beta_{1it} + \sum_{k=2}^{k} \beta_{kit} x_{kit} + u_{it} \qquad (1)$$

i=1,......,N; t=1,......,T; k=1,......,K

The general form of the panel data regression model can be represented in the following way.

Here is:

y_{it} - value of the dependent variable for the i observation unit in the period t;

x_{kit} - value of the k independent variable for the i observation unit in the period t;

x_{1it} = 1, for each i and t;

β_{kit} - unknown regression parameters, which in the general form of the panel data model are variable by observation units and time periods, i.e. they are not as constant as in classical regression analysis.

u_{it} - random error with arithmetic mean equal to zero and constant common variance for each i and t.

In the general form of a linear regression panel data model, variations in the dependent variable Y are explained by variations of K independent variables (a system part) and random variations that include the effect of changes in other variables not explicitly included in the model (a stochastic part of the model). (Dragutinovic-Mitrovic, 2002).

The panel data model in this study is in the form of:

$FDI_{it-1} = \alpha + \beta_{it} (PTI_{it} + GE_{it} + GQ_{it} + CC_{it}) + u_{it}$

Where they are represented in the following way:

FDI – Foreign direct investment,

PTI – Political Terror Scale,

GE – Government Effectiveness

GQ – Regulatory Quality,
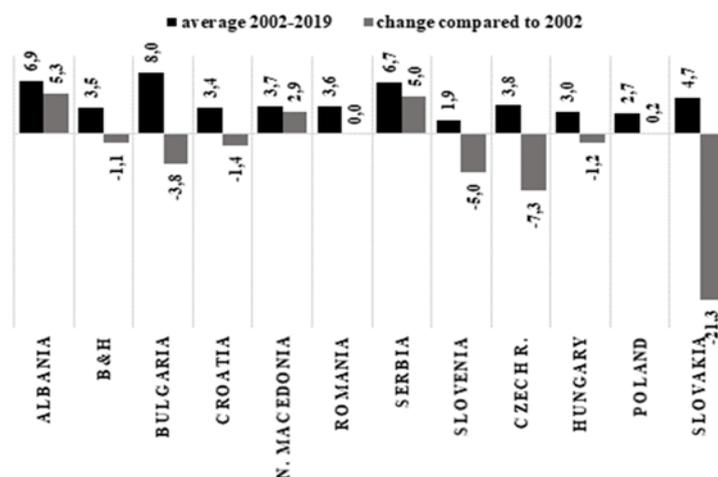
CC - Control of Corruption.

This regression model is based on a review of previous literature and defined dependent and independent variables. Their application in the continuation of the research will be used to determine the influence of politics and quality of governance on the trends of FDI inflows in selected Balkan and non-Balkan countries in transition.

The basic research hypothesis in the paper is that factors of quality of governance, as elements of a complex institutional system, affect FDI inflows and determine the quality of the investment environment in selected Balkan and non-Balkan countries in transition. In addition to the basic one, the paper investigates four auxiliary hypotheses that examine whether individually observed Government Effectiveness, Regulatory Quality, Control of Corruption and Political Terror Scale positively affect FDI inflows in selected Balkan and non-Balkan countries in transition. By applying the methodology in the field of analysis of regression panel models in the continuation of the work, the set hypotheses were checked.

2.2. Data

Annual data taken from UNCTADstat were used to analyze the dependent variable, FDI inflows. Of all the observed countries in transition (Balkan and non-Balkan countries), Albania and Serbia had the largest share of FDI inflows in GDP in 2019. They are followed by Hungary and the Czech Republic with a significantly lower share, followed by North Macedonia, Bosnia and Herzegovina and Romania. Slovenia and Bulgaria have the lowest share of FDI inflows in GDP, while Slovakia, Croatia and Poland have a slightly better situation. However, when looking at the average share of FDI inflows in GDP in the period 2002-2019, then the largest share was recorded by Bulgaria, followed by Albania and Serbia. Significant and fairly even participation was recorded by other observed countries in transition (Slovakia, Czech Republic, N. Macedonia, Romania, B&H, Croatia and Hungary), while the lowest participation was recorded by Poland and Slovenia.

**Graph 1: FDI inflows of Balkan and non-Balkan countries, on average
from 2002 to 2019, and changed from 2002 to 2019**

Source: Authors, according to data taken from UNCTADstat:
https://unctadstat.unctad.org/wds/ReportFolders/reportFolders.aspx

Compared to 2002, the growth of the share of FDI inflows in GDP was achieved only in Albania, Serbia, N. Macedonia, Poland, in Romania it is at the same level, and the decline in participation was recorded in B&H, Hungary, Croatia, Bulgaria, Slovenia, Czech Republic and Slovakia, which indicates that these countries are less and less basing their growth on FDI inflows.

Table 1: FDI inflows of Balkan and non-Balkan countries from 2002 to 2019, as % GDP

	Balkan countries								Non-Balkan countries			
	Albania	B&H	Bulgaria	Croatia	N. Macedonia	Romania	Serbia	Slovenia	Czech Republic	Hungary	Poland	Slovakia
2002	3.1	3.8	5.6	3.7		2.5	2.8	6.7	10.4	4.4	2.0	23.6
2003	3.2	4.4	9.9	5.2	2.3	3.7	5.8	0.9	2.1	2.5	1.8	8.8
2004	4.8	4.9	13.0	3.1	5.7	8.4	3.5	2.0	4.2	4.1	4.8	9.3
2005	3.3	3.1	13.1	4.0	1.5	6.2	6.9	1.6	8.6	6.8	2.7	6.3
2006	3.6	4.3	22.7	6.2	6.3	8.9	14.1	1.8	3.5	5.9	4.2	10.1
2007	6.2	11.5	27.9	7.8	8.3	5.6	12.2	1.6	5.5	2.8	4.6	5.2
2008	7.6	5.2	18.1	7.7	5.9	6.3	8.2	2.2	2.7	4.1	2.3	5.0
2009	8.3	1.4	6.5	4.7	2.1	2.7	6.8	-0.9	1.4	1.7	2.3	0.0
2010	8.8	2.4	3.1	2.0	2.3	1.8	4.8	0.2	3.0	1.8	2.7	2.0
2011	6.8	2.7	3.6	2.6	4.6	1.3	10.3	2.1	1.0	4.6	3.0	3.5
2012	6.9	2.3	3.1	2.3	1.5	1.9	3.4	0.7	3.9	11.4	2.5	3.2
2013	9.9	1.5	3.3	1.6	3.1	1.9	4.6	-0.3	1.7	2.6	0.5	-0.6
2014	8.4	3.0	0.8	5.0	2.4	1.6	4.3	2.1	2.6	5.7	2.6	-0.5
2015	8.3	2.2	4.4	0.2	2.4	2.2	6.2	3.9	0.2	-11.7	3.2	0.1
2016	9.3	2.1	1.9	0.5	3.5	2.7	5.5	2.8	5.0	-4.3	3.3	0.9
2017	8.8	2.5	3.1	1.0	1.8	2.6	6.2	1.8	4.4	2.5	1.7	4.2
2018	8.6	2.4	1.8	1.9	5.7	2.6	7.6	2.5	4.5	5.3	2.4	1.1
2019	8.4	2.7	1.8	2.3	2.9	2.5	7.8	1.7	3.1	3.3	2.3	2.3

Source: Authors, according to data taken from UNCTADstat:
https://unctadstat.unctad.org/wds/ReportFolders/reportFolders.aspx

The paper focuses on evaluation concerning the importance of three dimensions of the governance quality (Government Effectiveness, Regulatory Quality and Control of Corruption) and one political dimension (Political Terror Scale), whereas from the aspect of FDI inflows, good public governance accelerates, while bad slows down and limits FDI inflows.

In analyzing the quality of governance, the paper used secondary data taken from the World Bank: Worldwide Governance Indicators (WGI) which ranks 215 countries and territories based on six dimensions of quality of governance,

including government effectiveness, regulatory quality and control of corruption. These aggregate indicators combine the views of a large number of enterprise, citizen and expert survey respondents in industrial and developing countries. They are based on over 30 individual data sources produced by a variety of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms. (World Bank: Worldwide Governance Indicators)

Government effectiveness captures perceptions of the quality of public services, the quality of civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. (World Bank: Worldwide Governance Indicators)

Government Effectiveness reflects perceptions of the quality of public services, civil society and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of government within its commitment to such policies. Benassy-Quere et al. (2005, p. 28) came to the conclusion that the efficiency of public administration in a broader sense is the main determinant of FDI inflows. These include tax systems, ease of starting a business, absence of corruption, transparency, contract law, security of property rights, efficiency of the judiciary and prudential standards. In short, an efficient government removes the barrier to entrepreneurship and investment, that is, a government whose officials do not abuse power for private gain. On the contrary, slow, complicated and inflexible public administration that acts on discretionary rather than professional principles has a negative effect on FDI inflows (OECD, 2003, p. 22).

Of 8 Balkan countries observed, Slovenia has the highest government effectiveness in 2019 (which has a better result than 4 non Balkan countries), followed by Croatia, Bulgaria, Serbia and North Macedonia, while Bosnia and Herzegovina, Romania and Albania had the lowest Government effectiveness. Compared to 2002, all Balkan countries improved the values of this indicator (mostly Serbia by 0.53 pp, followed by North Macedonia by 0.52 pp, and Albania by 0.47 pp), except Romania, where the value of Government effectiveness decreased by -0, 08 pp. Non-Balkan countries have higher Government effectiveness than all observed Balkan countries (except Slovenia), with the Czech Republic having the highest Government effectiveness, followed by Slovakia and Poland, and Hungary having the lowest Government effectiveness among these countries.

**Table 2: Government effectiveness of 8 Balkan and 4 non-Balkan countries
from 2002 to 2019, range from -2.5 to 2.5**

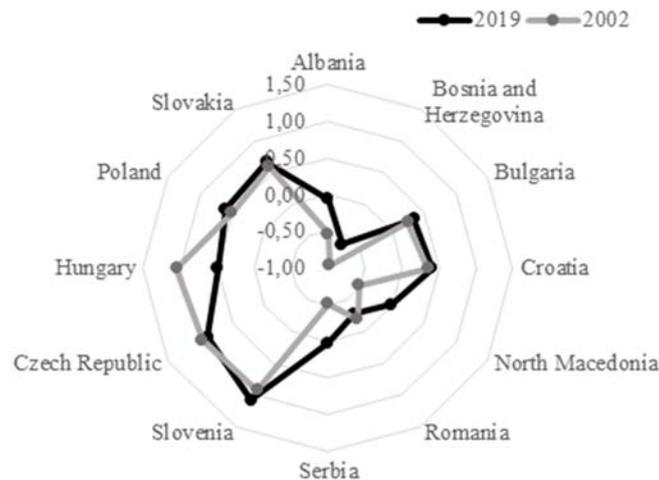|	Balkan countries								Non-Balkan countries			
	Albania	B&H	Bulgaria	Croatia	N. Macedonia	Romania	Serbia	Slovenia	Czech Republic	Hungary	Poland	Slovakia
2002	-0.5	-1.0	0.3	0.4	-0.5	-0.2	-0.5	0.9	1.0	1.1	0.5	0.6
2003	-0.5	-0.8	0.1	0.4	-0.4	-0.3	-0.6	1.1	0.9	1.0	0.6	0.7
2004	-0.4	-0.6	0.2	0.4	-0.2	-0.2	-0.2	0.9	0.9	0.9	0.5	0.9
2005	-0.7	-0.8	0.2	0.5	-0.3	-0.3	-0.3	0.9	0.9	0.8	0.5	0.9
2006	-0.5	-0.6	-0.1	0.6	-0.1	-0.2	-0.2	1.0	1.1	0.9	0.4	0.9
2007	-0.4	-0.8	0.0	0.5	-0.2	-0.3	-0.2	0.9	0.9	0.7	0.4	0.7
2008	-0.4	-0.6	-0.1	0.6	0.0	-0.3	-0.2	1.2	1.0	0.7	0.5	0.9
2009	-0.3	-0.7	0.2	0.6	-0.1	-0.4	0.0	1.2	0.9	0.7	0.5	0.9
2010	-0.3	-0.7	0.1	0.6	-0.1	-0.3	-0.1	1.0	0.9	0.7	0.6	0.8
2011	-0.2	-0.7	0.1	0.6	-0.1	-0.3	-0.1	1.0	0.9	0.7	0.6	0.8
2012	-0.3	-0.5	0.1	0.7	-0.1	-0.3	-0.1	1.0	0.9	0.6	0.7	0.8
2013	-0.3	-0.4	0.2	0.7	-0.1	-0.1	-0.1	1.0	0.9	0.7	0.7	0.8
2014	-0.1	-0.5	0.1	0.7	0.1	0.0	0.1	1.0	1.0	0.5	0.8	0.9
2015	0.0	-0.5	0.2	0.5	0.1	-0.1	0.1	1.0	1.0	0.5	0.8	0.8
2016	0.0	-0.4	0.3	0.5	0.1	-0.2	0.1	1.1	1.0	0.5	0.7	0.9
2017	0.1	-0.5	0.3	0.6	0.1	-0.2	0.2	1.2	1.0	0.5	0.6	0.8
2018	0.1	-0.6	0.3	0.5	0.1	-0.3	0.1	1.1	0.9	0.5	0.7	0.7
2019	-0.1	-0.6	0.3	0.4	0.0	-0.3	0.0	1.1	0.9	0.5	0.6	0.7

Source: Authors, according to data taken from World Bank: Worldwide Governance
Indicators (WGI): http://info.worldbank.org/governance/wgi/

Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. (World Bank: Worldwide Governance Indicators)

Regulatory Quality (application of regulations that promote private sector development). Experience has shown that states play a key role in creating an effective legislative and regulatory framework in which the private sector operates. The private sector cannot be fully developed if the state does not provide an institutional framework that guarantees and protects property rights, monitors the legality of business relations and ensures the implementation of contracts. The rule of law is a system in which all citizens are equal before the law and in which every violation of the law is credibly sanctioned. Complicated and lengthy administrative

procedures are in the group of very important disincentives for FDI inflows. A high degree of bureaucratization can drive away foreign investors regardless of the existence of generous incentives and solid legal certainty.

Graph 2: Government effectiveness of Balkan and non-Balkan countries in 2002 and 2019

Source: Authors, according to data taken from World Bank: Worldwide Governance
Indicators (WGI): http://info.worldbank.org/governance/wgi/

Slovenia has the best regulatory quality of the 8 observed Balkan countries in transition in 2019, and according to this indicator it is at the same level as Slovakia, better than Hungary, and worse than the Czech Republic and Poland, which recorded the best results in terms of regulatory quality of all observed countries, and Balkan and non-Balkan countries. Among the Balkan countries, better results, although weaker than Slovenia and non-Balkan countries, are achieved by Croatia, Bulgaria, North Macedonia and Romania, and the weakest results were recorded by Bosnia and Herzegovina, Serbia and Albania.

Serbia and North Macedonia achieved the greatest progress in terms of regulatory quality in the period 2002-2019. Albania, Romania, Bosnia and Herzegovina, Croatia, Poland and Slovenia also made progress. Countries such as Slovakia, the Czech Republic and Bulgaria are at about the same level, and a decline in regulatory quality has been observed only in Hungary.

Table 3: Regulatory quality of 8 Balkan and 4 non-Balkan countries from 2002 to 2019, range from -2.5 to 2.5

	Balkan countries								Non-Balkan countries			
	Albania	B&H	Bulgaria	Croatia	N. Macedonia	Romania	Serbia	Slovenia	Czech Republic	Hungary	Poland	Slovakia
2002	-0.2	-0.6	0.6	0.3	-0.2	0.0	-0.6	0.9	1.2	1.3	0.8	1.0
2003	-0.5	-0.5	0.7	0.5	-0.2	0.0	-0.6	0.9	1.2	1.1	0.7	1.0
2004	-0.2	-0.2	0.7	0.5	-0.1	0.2	-0.5	0.9	1.0	1.2	0.8	1.1
2005	-0.4	-0.6	0.6	0.5	-0.2	0.2	-0.6	0.9	1.1	1.1	0.8	1.2
2006	-0.1	-0.5	0.6	0.4	-0.1	0.5	-0.4	0.8	1.1	1.2	0.7	1.1
2007	0.1	-0.3	0.6	0.5	0.1	0.5	-0.3	0.8	1.0	1.2	0.8	1.0
2008	0.2	-0.2	0.7	0.5	0.2	0.6	-0.3	0.8	1.2	1.2	0.8	1.1
2009	0.2	-0.1	0.7	0.6	0.3	0.6	-0.1	0.9	1.3	1.1	1.0	1.1
2010	0.2	-0.1	0.7	0.6	0.3	0.6	0.0	0.8	1.3	1.0	1.0	1.0
2011	0.2	0.0	0.5	0.5	0.3	0.7	0.0	0.7	1.2	1.0	0.9	1.0
2012	0.2	-0.1	0.6	0.5	0.4	0.6	-0.1	0.6	1.1	1.0	1.0	1.1
2013	0.2	-0.1	0.5	0.5	0.3	0.6	-0.1	0.6	1.1	0.9	1.0	0.9
2014	0.2	-0.1	0.6	0.4	0.5	0.6	0.1	0.7	1.0	0.8	1.1	0.9
2015	0.2	-0.2	0.6	0.4	0.4	0.6	0.2	0.6	1.1	0.8	1.0	0.8
2016	0.2	-0.2	0.7	0.4	0.4	0.6	0.1	0.6	0.1	0.6	1.0	0.9
2017	0.2	-0.1	0.6	0.4	0.5	0.5	0.0	0.6	1.2	0.6	0.9	0.8
2018	0.3	-0.2	0.6	0.5	0.5	0.4	0.1	0.7	1.3	0.6	0.9	0.8
2019	0.3	-0.2	0.5	0.6	0.5	0.5	0.1	1.0	1.3	0.6	1.0	1.0

Source: Authors, according to data taken from World Bank: Worldwide Governance Indicators (WGI): http://info.worldbank.org/governance/wgi/

Control of corruption is the third indicator whose impact on FDI we analyze in this paper. This indicator captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capturing" the state by elites and private interests. (World Bank: Worldwide Governance Indicators)

Graph 3: Changes in the regulatory quality of Balkan and non-Balkan countries in the period from 2002 to 2019
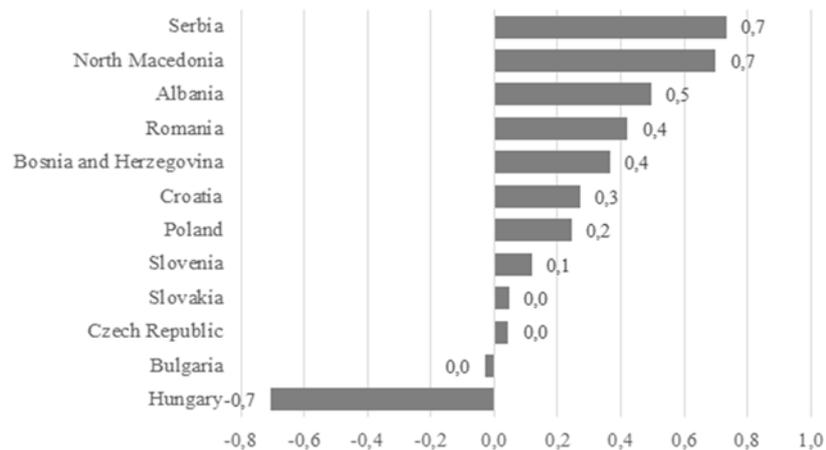
Source: Authors, according to data taken from World Bank: Worldwide Governance Indicators (WGI): http://info.worldbank.org/governance/wgi/

Corruption control (reflects perceptions of the extent to which public power is used for private gain, including petty and significant forms of corruption, as well as "usurpation" of the state by elites and private interests) (Kaufmann, Kraay, Mastruzzi, 2010). Wei (1997) also came to the results that corruption has a negative impact on FDI inflows. In addition, he mentions weak enforcement mechanisms and political instability, which means uncertainty for FDI and it negatively affects the investment decision. A high corruption index negatively affects FDI inflows or, in the worst case, it is replaced by the wrong type of FDI (Costa, 2010). For economic development policy makers, the fight against corruption is an important tool to help stimulate FDI.

Mauro (1995) was among the first authors to conduct the first systematic empirical research showing that corruption has a negative impact on the ratio of total and private domestic and foreign investment to GDP, and, consequently, harms economic growth. Over time, empirical evidence of the negative effects of corruption on economic growth and FDI flows has steadily increased. For example, Mauro (1997) uses Business International indices to determine that corruption actually harms growth and investment. In his study of a sample of 67 countries, Mauro argued that corruption can directly affect FDI by undermining the perception of stability and quality of investment potential, so investors lose interest in investing due to additional costs. Mauro found that if the country could increase the efficiency of its administration and reduce the level of corruption from 4/10 (four out of 10) to 6/10 (sixth out of ten), the investment rate would increase by 3% and the rate growth of 0.5%.

Later conducted research also confirms the previously given assumptions. Besides, Wei (1997) came to a conclusion that corruption has a negative impact on FDI inflows. In addition, he mentions weak enforcement mechanisms and political instability, which means uncertainty for FDI, and it negatively affects the investment decision. Smarynzka and Wei (2000) argue that corruption in the host country leads foreign investors to favor joint ventures over wholly foreign-owned enterprises. Wei (2000) using data on bilateral FDI inflows from the Organization for Economic Co-operation and Development (OECD), finds that corruption has an economically significant and negative impact on FDI. Its results suggest that increasing the level of corruption is equivalent to increasing the tax rate for multinational companies by more than 20 percentage points. The main conclusion of the research conducted by Wei (1997 and 2000) is that the corruption is a significant obstacle to FDI inflows. Similarly, Gastanga, Nugent and Pashamova (1998) examined the relationship between policy variables and found that efficient governance (bureaucracy) and low levels of corruption positively affect FDI inflows. However, these results have been challenged by Daude and Stein (2001) who pointed out the existence of high collinearity between their corruption rate and GDP per capita, which can lead to false results when GDP per capita is not included in the equation. Using a wider range of institutional variables, however, they showed that FDI inflows are significantly influenced by the quality of institutions. Specifically, five of the six management indicators developed by Kaufman et al. (1999) proved to be important: political instability and violence, government efficiency, regulatory burden, the rule of law and corruption, only the voice and accountability indicator is not a significant determinant of FDI.

The impact of corruption on FDI was also examined by Habib and Zurawicki (2002). The results of their research show that foreign investors generally avoid corruption because they consider it wrong and can create operational inefficiencies. Focusing on corruption, these authors found that the absolute difference in the values of the corruption index between the investors and the host country has a negative impact on FDI inflows. On the other hand, Larrain and Tavares (2004) analyzed the impact of openness to foreign direct investment on corruption. They found that foreign direct investment is a strong determinant of corruption, meaning that higher FDI inflows reduce corruption within the country. Also, although the results of previous research clearly show the existence of a direct link between corruption and FDI inflows, in the sense that low levels of corruption encourage FDI inflows, there are other views. For example, some authors suggest that bribery may have a positive effect on FDI inflows by helping to avoid bureaucratic inefficiencies, and corruption is claimed to have a beneficial effect known as "lubricating the wheel" (Leff, 1964). Corruption can have detrimental long-term effects, but can "lubricate the wheels" of the economy and increase investment in the short term. Egger and Winner (2005) also found that in a sample of 73 countries between 1995 and 1999, there was a positive link between corruption and FDI and concluded that in the presence of

excessive regulations and other administrative controls, corruption can act as a "hand help "to stimulate FDI inflows.

In 2019, of the 12 observed countries in transition, Slovenia, Poland, the Czech Republic had the greatest success in the fight against corruption, and Slovakia, Croatia and Hungary were relatively successful. Less success in the fight against corruption was recorded in Romania, Bulgaria, North Macedonia and Serbia, and the most unfavorable situation is in Albania and Bosnia and Herzegovina.

Table 4: Control of corruption of 8 Balkan and 4 non-Balkan countries from 2002 to 2019, range from -2.5 to 2.5

	Balkan countries								Non-Balkan countries			
	Albania	B&H	Bulgaria	Croatia	N. Macedonia	Romania	Serbia	Slovenia	Czech Republic	Hungary	Poland	Slovakia
2002	-0.9	-0.4	-0.2	0.2	-0.8	-0.4	-0.9	0.8	0.4	0.6	0.4	0.0
2003	-0.8	-0.3	0.0	0.3	-0.6	-0.4	-0.5	0.9	0.5	0.7	0.4	0.3
2004	-0.7	-0.3	0.1	0.3	-0.5	-0.3	-0.5	1.0	0.4	0.7	0.1	0.4
2005	-0.8	-0.2	0.1	0.2	-0.5	-0.2	-0.4	0.9	0.5	0.7	0.3	0.5
2006	-0.8	-0.3	-0.1	0.1	-0.4	-0.2	-0.3	1.0	0.4	0.7	0.3	0.4
2007	-0.7	-0.4	-0.2	0.1	-0.4	-0.2	-0.4	1.0	0.3	0.6	0.3	0.4
2008	-0.6	-0.4	-0.3	0.0	-0.2	-0.1	-0.3	1.0	0.4	0.5	0.5	0.4
2009	-0.5	-0.4	-0.2	-0.1	-0.1	-0.3	-0.3	1.1	0.4	0.4	0.5	0.3
2010	-0.5	-0.3	-0.2	0.1	-0.1	-0.2	-0.3	0.9	0.3	0.4	0.5	0.3
2011	-0.7	-0.3	-0.2	0.1	-0.1	-0.2	-0.3	1.0	0.3	0.4	0.6	0.3
2012	-0.7	-0.3	-0.2	0.0	0.0	-0.3	-0.3	0.8	0.3	0.4	0.7	0.1
2013	-0.7	-0.2	-0.3	0.1	0.0	-0.2	-0.3	0.7	0.2	0.3	0.6	0.1
2014	-0.5	-0.3	-0.2	0.2	0.0	-0.1	-0.2	0.7	0.4	0.2	0.6	0.2
2015	-0.5	-0.4	-0.3	0.2	-0.3	0.0	-0.3	0.8	0.4	0.1	0.7	0.2
2016	-0.4	-0.5	-0.2	0.2	-0.3	0.0	-0.3	0.8	0.5	0.1	0.7	0.2
2017	-0.4	-0.5	-0.2	0.2	-0.3	0.0	-0.4	0.8	0.6	0.1	0.7	0.2
2018	-0.5	-0.6	-0.2	0.1	-0.4	-0.1	-0.4	0.9	0.5	0.1	0.6	0.4
2019	-0.5	-0.6	-0.2	0.1	-0.4	-0.1	-0.4	0.9	0.5	0.0	0.6	0.3

Source: Authors, according to data taken from World Bank: Worldwide Governance Indicators (WGI): http://info.worldbank.org/governance/wgi/

Compared to 2002, the greatest progress in the control of corruption has been made in Serbia and North Macedonia, and positive progress has been made in Albania, Slovakia, Romania, Poland, the Czech Republic and Slovenia. In Bulgaria, in 2019, compared to 2002, the situation remained unchanged, and the

control of corruption was reduced in Croatia, Bosnia and Herzegovina and Hungary, which indicates that the control of corruption is a great challenge not only for the Balkan countries, which have not yet met the strict conditions for EU accession, but also for the countries that have been members of the EU for many years and.

Graph 4: Control of corruption of Balkan and non-Balkan countries in 2002 and 2019
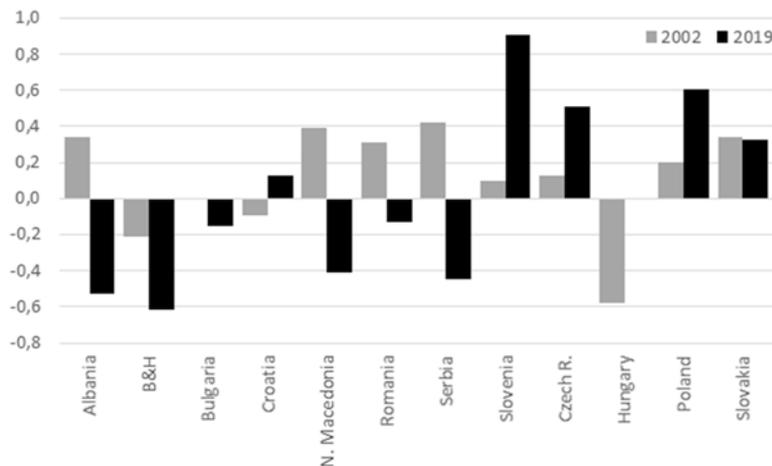
Source: Authors, according to data taken from World Bank: Worldwide Governance Indicators (WGI): http://info.worldbank.org/governance/wgi/

In addition to the three previously presented governance quality indicators, the paper also analyzes the impact of political risk on FDI inflows, based on indicators called political terror scale. The PTS measures levels of political violence and terror that a country experiences in a particular year based on a 5-level "terror scale" originally developed by Freedom House. The data used in compiling this index comes from three different sources: the annual country reports of Amnesty International, the U.S. State Department Country Reports on Human Rights Practices, and Human Rights Watch's World Reports." (The Political Terror Scale)

Political stability speaks of the possibility of destabilizing the government by unconstitutional or violent means. The success of democratic political systems in generating positive economic results should be sought primarily in involving all relevant actors in key decision-making, thus achieving a broader social consensus and ensuring accountability of governing structures (Ahrens, & Meurers 2001). Growth in a democratic environment is much more stable than in countries with a less democratic tradition (Ikbal, & Dali, 2014). This is confirmed by data of higher ten-year growth rates achieved after democratic transformations and political changes in the past forty years in Latin America, Europe, Africa and Asia (Shen, 2002). Also, examining the determinants of FDI inflows per capita in 80

developing countries, Schneider and Frey (1985) concluded that market size (measured as GDP), balance of payments deficit, bilateral aid (from Western and socialist countries) and political instability are significant determinants of FDI. According to these authors, political instability reduces FDI inflows. The survey results of the Busse and Hefeker (2005) confirmed that government stability, the absence of internal conflicts and ethnic tensions, basic democratic rights, and the maintenance of order and peace largely determine FDI inflows. Similar results were obtained in the research by Busse and Hefeker (2005) by taking into consideration the links between political risk, institutions and FDI inflows using different econometric techniques in a sample of 83 developing countries from 1984 to 2003. They used 12 different indicators for political risk and institutions in the empirical analysis. They, also, found that the investment profile, internal and external conflict, ethnic tensions and democratic accountability are important determinants of FDI flows. Also, Busse and Hefeker (2007) in their research showed that government stability, the absence of internal conflict, and basic democratic rights are important determinants of FDI inflows.

In 2019, the lowest level of political terror scale among the selected Balkan and non-Balkan countries was recorded in Bulgaria, Romania, Serbia, Slovenia, the Czech Republic and Hungary. A slightly worse situation was recorded in other observed countries, Albania, Bosnia and Herzegovina, Croatia, North Macedonia, Poland, Slovakia, where the basic assessment was that the level of political terror scale in all observed countries was relatively low.

Graph 5: Political terror scale in Balkan and non-Balkan countries in 2019

Source: Authors, according to data taken from
https://www.politicalterrorscale.org/Data/Download.html
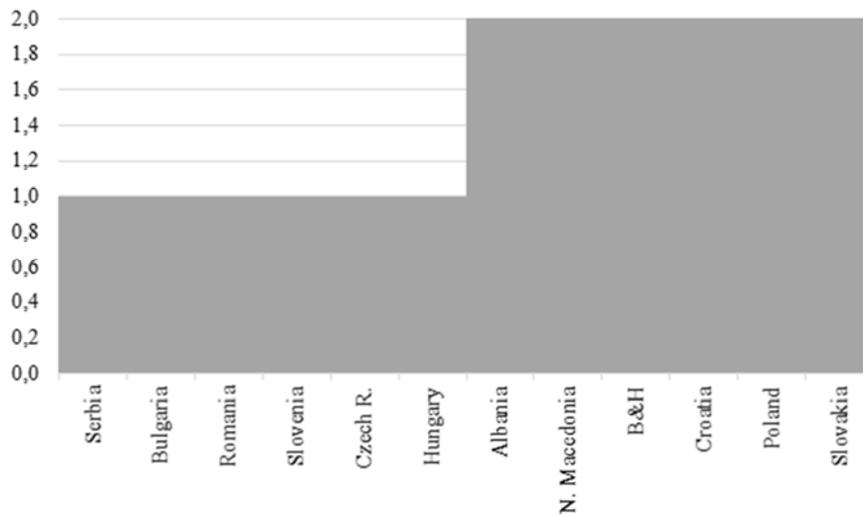
Table 5: Political terror scale in 8 Balkan and 4 non-Balkan countries from 2002 to 2019, range from 1 to 5

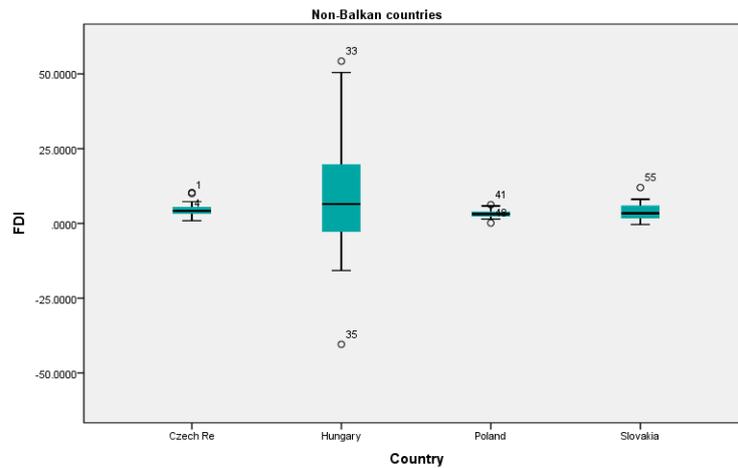|	Balkan countries								Non-Balkan countries			
	Albania	B&H	Bulgaria	Croatia	N. Macedonia	Romania	Serbia	Slovenia	Czech Republic	Hungary	Poland	Slovakia
2002	3.0	2.0	2.0	2.0	3.0	2.0	3.0	2.0	2.0	2.0	2.0	2.0
2003	2.0	2.0	2.0	2.0	2.0	2.0	3.0	2.0	2.0	2.0	1.0	1.0
2004	3.0	2.0	2.0	2.0	2.0	3.0	3.0	1.0	2.0	2.0	2.0	2.0
2005	2.0	2.0	2.0	2.0	2.0	2.0	3.0	1.0	2.0	2.0	1.0	1.0
2006	3.0	2.0	2.0	2.0	2.0	2.0	3.0	1.0	2.0	2.0	2.0	2.0
2007	2.0	2.0	2.0	1.0	3.0	2.0	2.0	1.0	2.0	2.0	2.0	2.0
2008	2.0	2.0	2.0	1.0	2.0	3.0	2.0	1.0	1.0	1.0	1.0	1.0
2009	2.0	2.0	2.0	1.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
2010	2.0	2.0	2.0	1.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
2011	2.0	1.0	2.0	1.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
2012	1.0	1.0	1.0	1.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
2013	2.0	2.0	2.0	1.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
2014	2.0	2.0	2.0	1.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0	1.0
2015	3.0	2.0	2.0	1.0	3.0	2.0	1.0	1.0	1.0	1.0	1.0	2.0
2016	2.0	2.0	2.0	1.0	2.0	2.0	1.0	1.0	1.0	2.0	2.0	1.0
2017	2.0	1.0	2.0	2.0	2.0	2.0	1.0	1.0	1.0	2.0	2.0	1.0
2018	2.0	2.0	2.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	2.0	1.0
2019	2.0	2.0	1.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0	2.0	2.0

Source: Authors, according to data taken from
https://www.politicalterrorscale.org/Data/Download.html

Compared to 2002, progress in the field of political terror scale was recorded the most in Serbia (by 2 pp), and progress was made by Bulgaria, Romania, Slovenia, Czech Republic, Hungary, Albania and North Macedonia, while in Bosnia and Herzegovina, Croatia, Poland and Slovakia, the situation has not changed compared to 2002 according to the political terror scale.
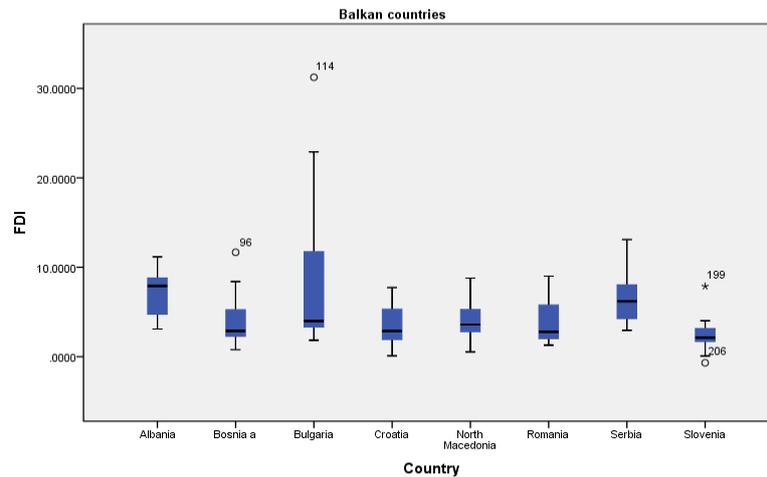
3. Results of descriptive statistics

3.1. Comparative analysis of dependent variable in considered countries

There is no statistically significant difference in FDI among considered non-Balkan countries (F = 1.136, p = 0.341). The highest average of FDI is recorded in Hungary, while the lowest one is recorded in Poland.

Source: Author's calculation

There is a statistically significant difference in FDI among considered Balkan countries (F = 5.903, p = 0.000). The highest average of FDI is recorded in Bulgaria and Albania, while the lowest one is recorded in Slovenia.

Source: Author's calculation

3.2. Comparative analysis of independent variables in considered Balkan and non-Balkan countries

In Table 6 we present the mean and standard deviation of all independent variables across all considered Balkan and non-Balkan countries. Using ANOVA we examined whether there is difference between countries in examined variables. There is no statistically significant difference in the Political Terror Scale among considered non-Balkan countries (F = 0.213, p = 0.887), while the difference exists in Balkan countries (F = 8.989, p = 0.000). However, governance quality indicators show homogeneous results in these two groups. Government effectiveness statistically significantly differ in both groups of countries (non-Balkan: F = 29,941, p = 0,000; Balkan: F = 193,473, p = 0,000). The same results are obtained for Regulatory Quality (non-Balkan: F = 9.014, p = 0.000; Balkan: F = 62.550, p = 0.000) and for Control of Corruption (non-Balkan: F = 5.930, p = 0.000; Balkan: F = 217,670, p = 0,000). The obtained results of comparative analysis of independent variables in the considered countries are completely in line with the previously obtained results of the analysis of input data for each indicator of quality of governance.

Table 6: Comparative analysis of independent variables in considered Balkan and non-Balkan countries Modeling results

Country in transition		Political Terror Scale		Government Effectiveness		Regulatory Quality		Control of Corruption	
		mean	std	mean	std	mean	std	mean	std
Non-Balkan	Czech Republic	1.41	.481	.951435	.0686123	1.148366	.1018444	.406379	.0971762
	Hungary	1.52	.489	.679154	.1705796	.957563	.2400098	.376870	.2383788
	Poland	1.45	.474	.592920	.1309608	.896885	.1055787	.502168	.1748292
	Slovakia	1.41	.481	.807732	.0885804	.985607	.1142258	.267603	.1282758
	Total	1.45	.473	.757811	.1807686	.997105	.1756305	.388255	.1849906
Balkan	Albania	2.13	.535	-.261205	.2325680	.076292	.2316636	-.629450	.1407188
	Bosnia and Herzegovina	1.80	.381	-.632178	.1537361	-.225168	.1760846	-.375414	.1048118
	Bulgaria	1.85	.326	.150652	.1133635	.607596	.0523977	-.154172	.1074749
	Croatia	1.47	.488	.531138	.1092563	.475663	.0800269	.134207	.0976294
	North Macedonia	2.13	.411	-.085384	.1836064	.229756	.2614292	-.296687	.2166545
	Romania	2.02	.432	-.229578	.0989328	.452435	.2114278	-.189351	.1146462
	Serbia	1.97	.773	-.115075	.2163142	-.164569	.2739513	-.373799	.1452082
	Slovenia	1.17	.336	1.033105	.0926779	.764972	.1283817	.895119	.1036430
	Total	1.82	.566	.048934	.5122068	.277122	.3868893	-.123693	.4567198

Source: Author's calculation

4 Modeling results

4.1 Results for non-Balkan countries

The analysis of the impact of governance quality indicators (government effectiveness, regulatory quality and control of corruption) and political indicator (political terror scale), on the level of FDI inflows in 4 non-Balkan countries (Czech Republic, Hungary, Poland, Slovakia) in the period from 2002 to 2019 via regression model:

$$FDI_{it-1} = \alpha + \beta_{it}(PTI_{it} + GE_{it} + GQ_{it} + CC_{it}) + u_{it.}$$

It shows a significant statistical impact of political factors represented by the Political Terror Scale indicator. Although less pronounced, the Control of Corruption indicator has an impact on the level of FDI inflows in the observed 4 non-Balkan countries in transition, which indicates that FDI inflows are influenced by both factors (Political Terror Scale and Control of Corruption). The increase of both of these factors by one unit will lead to the increase of FDI inflows given with the values of respected estimated coefficients (see Table 7). The obtained results are in line with the expectations and results of numerous empirical studies in this field, such as Schneider & Frey (1985), Azizov (2007), Benassy-Quere, Coupet & Mayer (2007), Bevan & Estrin (2000), Mottaleb 2007), Liargovas & Skandalis (2012), Soumia & Abderrezzak (2013), Abbas & El Mosallamy (2016), etc, when it comes to the movement of the Control of Corruption indicator, but it differs in the movement of the Political Terror Scale indicator, because economic theory and the results of previous research suggest a negative link between FDI inflows and the Political Terror Scale, i.e. political risk growth should be negatively affected on FDI inflows.

Table 7: Model for non-Balkan countries: 1-step dynamic panel, using 64 observations including 4 cross-sectional units

Dependent variable: FDI

	Coefficient	*Std. Error*	*z*	*p-value*
FDI(-1)	−0.0120133	0.0275880	−0.4355	0.6632
const	−0.199983	0.0978339	−2.044	0.0409**
Political Terror Scale (PTI)	2.38015	1.08702	2.190	0.0286**
Government Effectiveness (GE)	−16.3321	20.3225	−0.8036	0.4216
Regulatory Quality (GQ)	14.4792	12.9072	1.122	0.2620
Control of Corruption (CC)	12.2640	7.00954	1.750	0.0802*

Sum squared resid	17567.35	S.E. of regression	17.40360

Number of instruments = 63

Test for AR(1) errors: z = -1.08416 [0.2783]

Test for AR(2) errors: z = -0.979913 [0.3271]

Sargan over-identification test: Chi-square(57) = 58.153 [0.4326]

Source: Author's calculation

4.2 Results for Balkan countries

Analysis of the impact of governance quality indicators (government effectiveness, regulatory quality and control of corruption) and political indicator (political terror scale) on the level of FDI inflows in 8 Balkan countries (Albania, Bosnia and Herzegovina, Bulgaria, Croatia, North Macedonia, Romania, Serbia, Slovenia) in the period from 2002 to 2019 was also implemented through a regression model:

$$FDI_{it-1} = \alpha + \beta_{it}(PTI_{it} + GE_{it} + GQ_{it} + CC_{it}) + u_{it}.$$

The obtained results show that the only statistically significant influence on the level of FDI inflows in these countries is the political factor, which is represented by the Political Terror Scale indicator. The increase of this indicator value for one unit will lead to the increase of FDI by 0.86, which deviates from the assumed expectation. As this indicator is also important in non-Balkan countries, it means that foreign investors significantly value the levels of political violence and terror that a country experiences when deciding whether to invest in countries in transition, in the sense that the estimates of this index affect the inflow of foreign direct investment. One of the reasons is the transition process (political, economic, social and security) in which these countries are still (although most of them are at the end of that process). The fact is that the observed countries in transition still do not have a strong enough democratic institution that would greatly reduce the possibility of political risk, which in turn means that the level of political risk in these countries is still a significant determinant of FDI inflows.

Table 8: Model for Balkan countries: 1-step dynamic panel, using 126 observations

Included 8 cross-sectional units
Time-series length: minimum 14, maximum 16
Dependent variable: FDI

	Coefficient	Std. Error	z	p-value
FDI(-1)	0.625731	0.0975361	6.415	<0.0001***
const	−0.0302572	0.0815711	−0.3709	0.7107
Political Terror Scale-Amnesty International	0.861121	0.306782	2.807	0.0050***
Government Effectiveness	−3.42929	2.29754	−1.493	0.1355
Regulatory Quality	−0.752422	2.25686	−0.3334	0.7388
Control of Corruption	1.97389	3.74254	0.5274	0.5979

| Sum squared resid | 1453.796 | S.E. of regression | 3.480655 |

Number of instruments = 103

Test for AR(1) errors: z = -2.36645 [0.0180]

Test for AR(2) errors: z = -0.815884 [0.4146]

Sargan over-identification test: Chi-square(97) = 108.553 [0.1988]

Wald (joint) test: Chi-square(5) = 165.364 [0.0000]

Source: Author's calculation

However, the fact that in Balkan countries the indicator of control of corruption does not have the same statistical significance as in non-Balkan countries may indicate that there is a significant difference in the level of institutional and political development in the observed Balkan and non-Balkan countries.

5 Discussion and conclusion

In a dynamic panel model, we analyzed and compared 2 groups of countries in transition - 8 Balkan countries (Albania, Bosnia and Herzegovina, Bulgaria, Croatia, North Macedonia, Romania, Serbia, Slovenia), and 4 non-Balkan countries (Czech Republic, Hungary, Poland, Slovakia) within the same time range - from 2002 to 2019.

A comparative analysis of the dependent variable in the considered countries showed that there is no statistically significant difference in FDI among considered non Balkan countries, and that there is a statistically significant difference in FDI among the considered Balkan countries.

A comparative analysis of the independent variables showed that there is no statistically significant difference in the scale of political terror among the observed non-Balkan countries, while the difference exists in the Balkan countries. However, governance quality indicators show homogeneous results in these two groups of countries. Government efficiency significantly differs statistically in both groups of countries. The same results were obtained for the quality of regulations and for the control of corruption. The obtained results are completely in accordance with the previously obtained results of the analysis of input data for each individual indicator.

Modeling results for non-Balkan countries show a significant statistical impact of the Political Terror Scale. Although less pronounced, the impact of FDI inflows in the observed 4 non-Balkan countries in transition has an indicator of control of corruption, which indicates that FDI inflows are influenced by both factors (Political Terror Scale and Control of Corruption). The obtained results are in line with the expectations and results of numerous other empirical studies in this field,

as previously indicated in the paper regarding the impact of corruption levels, but it differs from the expected impact of indicators measuring the Political Terror Scale.

Modeling results for Balkan countries show that the level of FDI inflows in these countries is only statistically significantly influenced by the political terror scale. As the political terror scale factor is important in both the Balkans and non-Balkan countries, it means that the levels of political violence and terror that a country experiences significantly influence the decision on FDI inflows. This impact is expected because the transition process carries quality of governance that is a consequence of still undeveloped sufficiently strong democratic institutions that significantly reduce this type of risk in developed EU countries, but also the USA, Japan and others, but the direction of influence is contrary to expectations.

As the obtained results show that in Balkan countries the indicator of control of corruption does not have the same statistical significance as in non-Balkan countries, it can be concluded that there is a significant difference in the level of institutional and political development between the observed Balkan and non-Balkan countries. Although at first glance the result deviates from the results of most works in this field, which concluded that extreme corruption together with inefficient state apparatus is a very strong barrier to attracting foreign investors and increasing FDI inflows, there are works that also did not find a significant link between corruption and FDI inflows. For example, Azizov (2007) used a regression model with stochastic effects to examine the impact of potential determinants of FDI inflows in 12 Commonwealth countries between 1992 and 2005 and concluded that corruption, as a variable of the institutional sector, is not statistically significant and does not represent the determinant of FDI inflows in these countries. The results of research are also known in the literature, which even views corruption as a phenomenon that can positively affect the inflow of FDI. For example, Leff (1964) found that corruption helps avoid bureaucratic inefficiency, so it has a positive role to play in FDI inflows. According to this view, corruption has long-term detrimental effects because it increases costs and uncertainty, but it can "lubricate the wheels" in the short term and accelerate FDI inflows in countries with inefficient institutional systems and cumbersome bureaucracies. In these countries, corruption may be the only effective way to encourage investment by offering alternative ways of doing business.

Based on all previously obtained results, it can be concluded that FDI inflows have a significant role in the development of both Balkan and non-Balkan countries, but also that there is a significant difference between the countries themselves, in terms of institutional and political development. Although political terror scale factor are still present in both groups of countries, indicating that the transition process is not yet fully completed, the fact that factor of corruption control has a significant impact on FDI inflows to non-Balkan countries. This indicates that the political and institutional development of Balkan countries lags significantly behind the development of non-Balkan countries and that in Balkan countries, due to excessive

bureaucratic burdens and inefficiencies, corruption may even play a positive role in attracting FDI in the short term because it reduces bureaucratic inefficiency. Although the results do not directly show that corruption encourages higher FDI inflows to the Balkan countries, the fact that the existence of relatively high levels of corruption in these countries is not one of the most important factors in deciding to join the FDI, which indicates the existence of institutional and bureaucratic inefficiencies from which a recommendation can be drawn on the need for accelerated development and strengthening of institutional infrastructure, i.e. political and bureaucratic capacities in the analyzed Balkan countries.

References

Abbas, S. & El Mosallamy, D. (2016). Determinants of FDI Flows to Developing Countries: An Empirical Study on the MENA Region. *Journal of Finance and Economics*, 4(1), 30-38.

Ahrens, J., Meurers, M. (2001), *How Governance Affects the Quality of Policy Reform and Economic Performance: New Evidence for Economies in Transition*, Department of Economics, University of Goettingen, Germany.

Arellano, M. & Bond, S. R. (1991). Some Tests of Specification for Panel Data: Monte Carlo Evidence and an Application to Employment Equations. *Review of Economic Studies,* 58 (2), 277–297

Arellano, M. & Bover, O. (1995). Another look at the instrumental variable estimation of errorcomponents models. *Journal of Econometrics,* 68 (1), 29–51.

Azizov, A. (2007). *Determinants of FDI in CIS countries with transition economy*. Aarhus, Denmark: Aarhus School of Business.

Benassy-Quere, A., Gobalraja, N. & Trannoy, A. (2007). Tax and public input competition. *Economic Policy*, 22(50), 386-430.

Bevan, A. & Estrin, S. (2000). The determinants of foreign direct investment in transition economies. *CEPR discussion paper*, No. 2638

Binder, M., Hsiao, C. & Pesaran, M. H. (2005). Estimation and Inference in Short Panel Vector Autoregressions With Unit Roots and Cointegration. *Econometric Theory,* 21 (4), 795–837.

Blundell, R. &. Bond, S. R (1998). Initial conditions and moment restrictions in dynamic panel data models. *Journal of Econometrics,* 87 (1), 115–143.

Bun, M. J. G. & Windmeijer F. (2010). The weak instrument problem of the system GMM estimator in dynamic panel data models. *Econometrics Journal,* 13 (1), 95–126

Busse, M., & Hefeker, C. (2007). Political risk, institutions and foreign direct investment, *European journal of political economy, 23(2*), 397-415

Costa, A. M. (2010). The economics of crime: A discipline to be invented and a Nobel Prize to be awarded. *Journal of Policy Modeling*, 32(5), 648-661.

Dragutinović-Mitrović, R. (2002). Analiza panel serija. Beograd: Zadužbina Andrejević

Egger, P., & Winner, H. (2005). Evidence on corruption as an incentive for foreign direct investment. *European journal of political economy*, *21*(4), 932-952.

Globerman, S. and Shapiro, D. (2003). Governance infrastructure and U.S. foreign direct investment. *Journal of International Business Studies*, 34, 19-39.

Gorbunova, Y., Infante, D. & Smirnova, J. (2012). New evidence on FDI determinants: an appraisal over the transition period. *Prague Economic Papers*, 2, 129-149.

Habib, M., & Zurawicki, L. (2002). Corruption and foreign direct investment. *Journal of international business studies*, *33*(2), 291-307.

Hefeker, C., & Busse, M. (2005). *Political risk, institutions and foreign direct investment* (No. 315). HWWA Discussion Paper.

Infante, D., & Smirnova, J. (2009). Entrepreneurship, rent-seeking spillovers and decreasing returns: A microeconomic approach. *Acta Oeconomica*, 59(1), 79-89.

Kahouli, B. & Maktouf, S. (2014). The determinants of FDI and the impact of the economic crisis on the implementation of RTAs: A static and dynamic gravity model. *International Business Review.*

Kaufmann, D., Kraay, A., & Mastruzzi, M. (2010). The Worldwide Governance Indicators: Methodology and Analytical Issues, *Hague Journal on the Rule of Law*, 3(2).

Kaufmann, D., Kraay, A., & Zoido-Lobatón, P. (1999). *Aggregating governance indicators* (Vol. 2195). World Bank publications.

Kimura, H. & Todo, Y. (2010). Is Foreign Aid a Vanguard of Foreign Direct Investment? A Gravity-Equation Approach. *World Development 38 (4),* 482–497.

Larraín B, F., & Tavares, J. (2004). Does foreign direct investment decrease corruption?. *Cuadernos de economía*, *41*(123), 199-215.

Leff, N. (1964) "Economic Development through Bureaucratic Corruption" American Behavioral Scientist

Leff, N.H. (1964). Economic development through bureaucratic corruption. *American behavioral scientist*, *8*(3), 8-14.

Liargovas, P. G. & Skandalis, K. S. (2012). Foreign direct investment and trade openness: The case of developing economies. *Social Indicators Research*, 106(2), 323-331.

Mauro, P. (1995). Corruption and growth. *The quarterly journal of economics*, *110*(3), 681-712.

Mauro, P. (1997). The Effects of Corruption on Growth, Investment, and Government Expenditure: A Cross-Country Analysis, *Elliott*.

Mottaleb, K. A. (2007). *Determinants of foreign direct investment and its impact on economic growth in developing countries. MPRA* - Munich Personal RePEc Archive.

OECD, (2003). Enterprise Policy Performance – Croatia, The South East Europe Compact for Reform, *Investment, Integrity and Growth*, OECD and EBRD.

Olivero, M. P. & Yotov, Y. V. (2012). Dynamic gravity: endogenous country size and asset accumulation. *Canadian Journal of Economics* 45 (1), 64–92.

Schneider, F. & Frey, B. (1985). Economic and political determinants of foreign direct investment. *World Development*, 13(2), 161-175.

Schneider, F., & Frey, B. S. (1985). Economic and political determinants of foreign direct investment. *World development*, *13*(2), 161-175.

Shen, J.G. (2002), Democracy and growth: An alternative empirical approach, *BOFIT Discussion Papers 13/2002*, Bank of Finland, Institute for Economies in Transition.

Smarzynska, B. and Wei, S.J. (2000). Corruption and the Composition of Foreign Direct Investment: Firm-level Evidence, *National Bureau of Economic Research Working Paper 7969*, Cambridge MA.

Soumia, Z. & Abderrezak, B. (2013). The determinants of foreign direct investment and their impact on growth: Panel data analysis for AMU countries. I*nternational Journal of Innovation and Applied Studies*, 2(3), 300-313.

The Political Terror Scale: https://www.politicalterrorscale.org/Data/Documentation.html, accessed: January 05, 2022

UNCTAD, (1997). *World Investment Report 1997, Transnational Corporations, Market Structure and Competition Policy*, United Nations Conference on Trade and Development, United Nations, New York and Geneva, https://unctad.org/system/files/official-document/wir1997_en.pdf

UNCTADstat: https://unctadstat.unctad.org/wds/ReportFolders/reportFolders.aspx, accessed: January 03, 2022

Wei, S. J. (1997). Why is corruption so much more taxing than tax? Arbitrariness kills.

Wei, S.J. (2000). How Taxing is Corruption on International Investors, *Review of Economics and Statistics*, LXXXII (1), 1-11.

Wei, Shang-Jin, (1997), *"Why is Corruption So Much More Taxing Than Tax? Arbitrariness Kills.*" The National Bureau of Economic Research Working Paper 6255, November.

World Bank: Worldwide Governance Indicators (WGI): http://info.worldbank.org/governance/wgi/, accessed: January 04, 2022

POLITIČKI RIZIK I KVALITET UPRAVLJANJA KAO DETERMINANTE DIREKTNIH STRANIH INVESTICIJA U ZEMLJAMA U TRANZICIJI

Apstrakt: Ovaj rad metodom dinamičkih panel podataka ispituje indikatore političkog rizika i kvaliteta upravljanja kao determinante stranih direktnih investicija (SDI) u balkanskim i nebalkanskim zemljama u tranziciji. Empirijski model pokazuje da determinante, kao što su politički rizik (skala političkog terora) i indikatori upravljanja (kontrola korupcije), imaju značajne i verodostojne efekte u balkanskim i nebalkanskim zemljama u tranziciji. Pored toga, analizirani faktori, kao što su efektivnost vlade i regulatorni kvalitet koji igraju važnu političku ulogu u određivanju priliva SDI u zemljama u tranziciji i pomažu da se objasni različita privlačnost pojedinih zemalja stranim investitorima, u našem empirijskom modelu nemaju značajnu ulogu u prilivu SDI.

Ključne reči: priliv SDI, kvalitet upravljanja, balkanske i nebalkanske zemlje

Author's biography

Miloš Dašić was born in Priština, where he gained primary and secondary education with outstanding results. In 2003, he enrolled and successfully finished Military Academy – Department of Economics in Belgrade with a GPA of 8.98 (Master of Economics). Along with Military Academy, Miloš finished Business School, Department of Business IT, and shortly after that Faculty of Management – IT in Management Department. Currently, he is working on his doctoral dissertation after passing all the exams at the Faculty of Economics in Niš. So far, he has published more than 30 scientific articles in prestigious domestic and international journals and one book used as a textbook at Business School. He is the founder and director of two companies, president of Vozdovac Business Club, and a member of several local and state-wide organizations with an economic development portfolio.