

DIASPORA AS A GENERATOR OF FOREIGN DIRECT INVESTMENT

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Abstract

Focusing on Bosnia and Herzegovina, this study examines how diasporas contribute to the creation of foreign direct investment (FDI) in developing countries. It defines FDI as the acquirement over assets in a foreign nation and highlights how diaspora populations support investment flows. It also examines diaspora investment strategies, such as diaspora portfolio investment (DPI) and diaspora direct investment (DDI), and offers a historical overview of diaspora FDI patterns and how Bosnia and Herzegovina's policies are changing to engage its diaspora more.

One case study illustrates the impact of diaspora-led FDI by highlighting the success of Senad Šantić, a Bosnian entrepreneur who returned to his home country to start a tech company. While these investments support development and economic growth, there are still issues, like the possibility of putting one's own interests ahead of the interests of the economy as a whole. Particularly in Bosnia and Herzegovina, where diaspora participation has historically been low, the implementation of effective policies and procedures is crucial, especially from a regulation perspective.

The study also looks at the future of FDI, emphasizing the part that digital technology and new investment patterns will play. Opportunities for developing nations can be found in digital FDI, especially in industries like fintech and e-commerce, yet obstacles still exist in luring these investments. According to all the findings, developing nations can improve their chances for economic success by creating an atmosphere that encourages diaspora investment which will shift those nations into the global investment scene. Ultimately, FDI regulations and government programs are needed in order to fully utilize diaspora-led FDI for sustained growth.

Keywords: Foreign Direct Investment (FDI), Diaspora Investment, Bosnia and Herzegovina, Economic Development, Diaspora Engagement.

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1. INTRODUCTION

To begin, it is important to define Foreign Direct Investment (FDI) and discuss how diaspora can influence it. FDI is the process whereby residents of one country (the source country), acquire ownership of assets to control the production, distribution, and other activities of a firm in another country (the host country) (Moosa, 2004).

The distinguishing feature of FDI, compared to other forms of international investment, is the element of control over management policies and decisions (Moosa, 2004, p.2). Control implies that the investor has some degree of discretionary decision-making power in management policies and strategies. For example, this control can occur through the ability to elect or select one or more members of the board of directors of the foreign company or subsidiary. These features are crucial for successful and profitable FDI. In regards to FDI and diaspora, researchers have found a positive association between migration and international flows of goods and capital (Fossati, 2019). The size of ethnic diasporas is certainly associated with the volume of trade between their home and their host countries as migrants capitalize on unique cultural skills to take advantage of international business opportunities (Fossati, 2019, p.5). This is crucial because a lot of the time the cultural differences between trading partners created the need for mediation, a role that was typically assumed by trusted countrymen of exporting countries serving as commercial agents in order to help a business deal go through. From this perspective, diasporas can be conceptualized as an example of a broader class of groups who leverage on their distinctive sociocultural status and occupational skills to facilitate domestic and international economic exchanges.

While globalization and technology have reduced the need of mediation in cross-border economic exchanges, informational irregularities continue to impede transnational economic engagement as investors in source countries often lack knowledge about key factors that shape the investment climate in investment destinations, such as prevailing business culture and regulatory framework, diasporas can still leverage on their knowledge of host and home countries. In the context of international investment, in particular, diasporas can decrease uncertainty through two channels. First, investors in a source country may assume about cultural and social conditions in destination countries by observing and interacting with ethnic diasporas. Second, diasporas can provide information about specific business opportunities and help alleviate credible commitment issues, thereby decreasing the informational irregularities that hinder cross-border economic exchanges. This will be discussed in more detail below.

2. HISTORICAL OVERVIEW OF DIASPORA AND FDI

Throughout history, especially the 20th century, we saw many advancements in transportation, communication, technology etc., which all led to globalization. Markets were opening and trade laws were put in place for a safer way of conducting business, and therefore, encouraging foreign direct investment.

A major change over the past three decades has also been that governments have become more favorable towards FDI, and have liberalized their FDI regime accordingly, though at different times, speeds and depths in different countries and regions. Over the past fifteen years, countries have regarded FDI increasingly as contributing to their development strategies for the technology and capital it provides. They have even have started to compete for FDI. Investment policies have become more liberal at the national and regional level, but there is no comprehensive framework at the multilateral level. Some home countries are also increasingly facilitating FDI into developing countries using guarantee funds, matchmaking and other measures (Willem te Velde & Nair, 2006). In a globalized and interdependent world, every country needs cooperation and partnership. In the framework of this mission, every state undertakes policies and reforms that impose radical internal changes. Supporting these changes requires financial and human resources that states are trying to secure through various sources. Diaspora is in fact the first catalyst that provides incentives to the economy to meet national needs with financial and human resources and that helps overcome relative isolation from global trade flows. Through the engagement of the diaspora, states are extending their political and administrative functions beyond national borders and through agreements are improving relationships with other countries.

This stimulates the interest of foreign investors who are always looking for new markets, less expensive, rich in natural sources. FDI through financial capital and foreign currency it brings, technological innovation, human capital development, trade opening contributes to the economic growth of the country (Milova & Vokshi, 2022). Migration is also an increasingly important facet of the global political economy. Like flows of commodities and capital, flows of labor have increased dramatically in recent years. The United Nations' Population Division put the share of the world's population residing outside their nation of birth at almost 200 million people- or approximately 3% of the world's population- in 2007. That number continues to grow: The Organization for Economic Cooperation and Development (OECD) estimates that the number of legal immigrants entering OECD countries stands at about 3 million annually (Leblang, 2010, p. 584). Just as with flows of commodities and capital, scholars have devoted enormous energies to the exploration of the consequences of immigration. Some academics argue that migration causes "brain drain", in which highly qualified and educated citizens of a nation depart in quest of higher salaries. Some argue that the possibility of leaving encourages those who remain to invest in their own human capital, therefore offsetting the brain drain. There are many different viewpoints regarding FDI and diaspora, all the pros and cons, highlighting different aspects and effects.

On one hand, diaspora investment can be a very positive thing where knowledge and financial skills are brought to the home country, and the familiar contacts, market condition, legal framework and other networks can lead to an increased economic growth. On the other hand, some say that diaspora investments might not be as good as they seem, because investors might have their own motives, like increasing their wealth without much thought about building up the home country's economy and creating jobs. Lastly, the varying

viewpoints on the relationship between FDI and diaspora highlight the complexity of both phenomena.

Diaspora communities' potential for attracting foreign direct investment (FDI) can have varying effects based on a range of factors, such as financial resources, cultural affinities, and the extent to which investment decisions align with the country's development goals. To effectively use the positive aspects and remove any possible disadvantages, policymakers and stakeholders need to have a comprehensive understanding of these complexities.

3. UNDERSTANDING DIASPORA INVESTMENT (DPI AND DDI)

The diaspora plays a variety of roles in the economy, and in particular, its potential for development has been recognized. Diaspora investment has been utilized to describe cross-border business-directed investment flows transacted by a "diasporan" (an individual living in diaspora) in their country of origin. (Elo & Riddle, 2016).

Concerning diasporans, their place of investment is often connected to homeland or home region, particularly due to their market-specific knowledge and social network advantage as mentioned before. Their home-country investments may not be limited to payments or entrepreneurship, instead, they may take the form of diaspora portfolio investment (DPI), such as diaspora bonds, home-country equity or debt-structured investments, etc. or diaspora direct investment (DDI) through which business operations are brought to and started in the diasporan's home country (Elo & Riddle, 2016, p.16). Regarding diaspora portfolio investment (DPI), a mentioned above, diaspora bonds are one such mechanism that can enable developing countries to borrow from their expatriate (diaspora) communities (Ketkar & Ratha, 2010). A diaspora bond is a debt instrument issued by a country or potentially, a sub- sovereign entity or even a private corporation, to raise financing from its overseas diaspora. In the example of India, on three occasions since 1991 it has raised over US\$35 billion using these bonds- the rationale behind the Indian authorities, is that they have used this instrument for balance of payments support, to raise financing during times when they had difficulty in accessing international capital markets (Ketkar & Ratha, 2010, p. 252). It's also crucial to remember that by acquiring these bonds, diaspora members can contribute to the advancement and economic growth of their home countries while potentially earning financial rewards in the future. On the other hand, with diaspora direct investment (DDI), this is, as the name suggests, a way to directly invest in businesses in the form of purchasing equity or ownerships stocks. In this way, the use of diaspora bonds or other governmental instruments is avoided.

All in all, both types of investment have their advantages and disadvantages, but one thing is for sure; the reason diaspora choose to invest in their home country is much deeper than one would initially think. It mostly has to do with their strong emotional and cultural ties to their homeland. It is a sense of familiarity like nowhere else, which can be a useful thing

when wanting to invest, or do business in their country of origin. Accordingly, in this case, investing would be one way for them to get closer or reconnect with their roots.

4. FDI IN DEVELOPING COUNTRIES

It is widely believed that the trend towards globalized production and marketing has major implications for developing countries' attractiveness to foreign direct investment (FDI). The boom of FDI flows to developing countries since the early 1990s indicates that multinational enterprises (MNEs) have increasingly considered these host countries to be profitable investment locations. At the same time, various experts argue that the determinants of and motivations for FDI in developing countries have changed in the process of globalization (Nunnenkamp, 2002). Regarding the factors that determine foreign direct investment, this is anticipated to have two connected effects:

- Host countries are evaluated by MNEs on the basis of a broader set of policies than before. The number of policies constituting a favorable investment climate increases, in particular with regard to the creation of location-specific assets sought by MNEs.
- The relative importance of FDI determinants changes. Even though traditional determinants and the types of FDI associated with them have not disappeared with globalization, their importance is said to be on the decline. More specifically, "one of the most important traditional FDI determinants, the size of national markets, has decreased in importance. At the same time, cost differences between locations, the quality of infrastructure, the ease of doing business and the availability of skills have become more important" (Nunnenkamp, 2002, p.4).

This is the reason why today, MNEs are expected to move some of their production facilities to developing countries which characteristically have a large work force that is willing to work for low wages and long hours. All of this can be described as a result of the pressure that globalization has placed on prices as a way to keep up with the global competitiveness. In this regard, human resource development (HRD) and foreign direct investment (FDI) are generally considered among the key drivers of economic growth in developed and developing countries. While HRD and FDI individually affect growth, they also reinforce each other through complementary effects. In general, enhanced HRD increases incoming FDI by making the investment climate attractive for foreign investors. This is done through a direct effect of upgraded skill level of the workforce, as well as via indirect effects such as improved sociopolitical stability and health. On the other hand, FDI contributes to HRD since MNEs themselves can be active providers of education and training, bringing new skills, information and technology to host developing countries. Ultimately, this complementary effect leads to a virtuous circle of HRD and FDI where host countries experience continuous inflow of FDI over time by increasingly attracting higher value-added MNEs, while at the same time upgrading the skill contents of preexisting MNEs and domestic enterprises (Majeed & Ahmad, 2008).

5. POLICY IN BOSNIA AND HERZEGOVINA FOR DIASPORA DRIVEN FDI

The main objective of Bosnia and Herzegovina would be to achieve long-term growth based on increased investments and on adoption new technologies with increased competitiveness of the products on the world market. Investments for the renewal and increase of domestic capital, for keeping up with new technologies, are necessary prerequisite for making a long-term growth.

Foreign direct investments are considered to be the best source of capital, and have an advantage over other sources of capital, such as debt, portfolio investment and foreign aid. The advantages of foreign direct investment, compared to credits are, that they do not represent a significant capital outflows in the future, which can disrupt the current balance and economic growth in the future. Foreign direct investment is related to investments in fixed assets and represent a long-term investment. Analysis of financial effects show that foreign investments represent the inflow of foreign resources which are contributing to increase of total investment in the host country. Their share in total domestic investment increasing, especially in countries in transition. In addition to the basic (initial) capital inflows, foreign direct investment is presenting also all reinvested profits of branches of foreign companies in a host country (Sušić, Stojanović-Trivanović, & Sušić, 2017). Furthermore, there are Business zones (BZ) that represent a space for wide variety of business activities. They operate and are managed by specialized team of professionals or a specific organization, and are formed as a result of organized development concept of the state, region or municipality. To the entities that operate within the business zone, are typically offered certain benefits, such as cheaper rent or allowance, various tax benefits, deferred payment options, assistance with exports of goods and services, faster and easier access to capital and so on. Business zone can be organized and managed by the local government or regional organization, which is proved to be the most effective approach to managing and developing the business areas. Efficiency of the business area depends on the characteristics and imposed operating policies in the zone. So, business zones are a tool for the development of entrepreneurship and attracting investment, both domestic and foreign.

The free zone is part of the customs territory of a particular country, which is specially separated by fence and marked, in which the economic activities are performed under special conditions. Usually, these conditions are defined in detail by national laws on free zones. The users of these zones do not pay import duties and value added tax- VAT. Customs duties and tariffs are not charged on imports, and import of equipment that will be used for production and operations within a free zone, is exempted from customs and other duties. It is important to point out that investments in the free zone, transfer of profit and transfer of investment are not charged at all. Free Zone, first of all, implies more liberal regime of business. The need for regulatory standardization requirements for the formation, function and defining benefits for work in free zones is stated in the regulation, which was initially defined by the entities' Laws on Free Zones, and finally established by the Law on

Free Zones BH. The relevant legislation that touches the issues of operations in free zones, refers to the Law on Customs Policy of BH, the Law on Free Zones in BH and the Law on foreign direct investment in BH (Sušić, Stojanović-Trivanović, & Sušić, 2017, p. 8). More importantly, up until April of 2017, BiH had no official policies adopted or implemented towards its diaspora population.

Engagement of BiH institutions towards its diaspora communities has been quite limited and underdeveloped, and with viable initiatives to move forward. This is unfortunate as the Bosnian–Herzegovinian diaspora population is estimated at anywhere between 1.6 million to 2.4 million people, yet has a limited involvement in democratic processes at home, disproportionate to their overall size and diversity (Hasić & Telalović, 2021). Our country needs to actively promote diaspora investment opportunities through marketing initiatives, and bureaucratic barriers need to be removed in order to have more investment and therefore, more long-standing economic growth.

6. SUCCESSFUL DIASPORA DRIVEN FDI PROJECTS

One of the most interesting success stories in regards to diaspora driven FDI belongs to Senad Šantić, a Bosnian diaspora member, who returned to Mostar, Bosnia and Herzegovina, and co-founded an IT consulting company called ZenDev.

The company quickly grew to 15 employees and is expected to hire even more people as time goes by. Šantić recognized the availability of support in BiH to expand his company, including co-financing and training provided by USAID through the Diaspora Invest project. The main goal of the project is to encourage diaspora investment in BiH and provide grants and technical support to startups and early-stage companies. The software development industry in BiH has seen considerable expansion, with exports rising by nearly 30 percent in 2017 and job opportunities increasing by 17 percent. He thinks that the present is the right moment to invest in BiH because of its growth potential. The Diaspora Invest initiative took place from April 2017 until March 2022 (Sarajevo Times, 2019).

ZenDev is the example of a successful FDI project, driven by the diaspora. It is through these initiative projects like Diaspora Invest, that an opportunity is created for FDI ventures that are essential for success. By recognizing and fostering the opportunities of diaspora investment, governments can establish a stable framework for diaspora-led FDI and motivate additional diaspora individuals to assist in the development of their home nations.

7. FUTURE OF FDI

The landscape of FDI is changing very quickly, fueled by digital innovations and a more interconnected global marketplace. As economies all over the world adjust to digital transformation and new business models, the methods of conducting FDI are shifting.

FDI is currently moving towards digital FDI, and as businesses grow more dependent on digital platforms and technologies, investments are progressively directed towards areas like e-commerce, fintech, and digital infrastructure. These new sectors of FDI

are thriving because they are easy to scale, and there are lower entry barriers. An example could be the rise in digital start-ups and platforms, all driven by the global expansion of internet and mobile technology.

The diaspora can be very helpful in turning these investments into promising digital enterprises, leveraging their networks to overcome the barriers that many emerging economies face. However, despite many advancements, developing countries still face the before-mentioned barriers of attracting FDI, especially in digital areas. One challenge is the lack of digital infrastructure, which prevents entry or participation in the first place. Digital FDI cannot be realized without fast and reliable internet connection and secure payment systems. Knowledge and resources are going to be needed in order to support this digital infrastructure expansion. The role of diaspora will also entail the provision of advocacy for the improvement of digital laws and policies in their home countries. Many countries are shackled with outdated regulations that do not provide little to no clarity in regards to digital economy, creating uncertainty for potential investors which prevents them from investing.

According to the World Economic Forum, “countries that provide a stable political and economic environment are more likely to see increased digital FDI” (World Economic Forum, 2023). In this context, the diaspora can also act as a stabilizing force, encouraging better governance and promoting trust in the political and economic systems of their home countries. The most pressing issues continue revolving around data privacy and cybersecurity, therefore, the quality and quantity of FDI will likely depend on how governments and businesses choose to adapt to this changing landscape of global investment. Forward-thinking policies will be needed in order to unlock the full potential of FDI.

Ultimately, the potential that FDI holds is undeniable, however, only with the collaboration among governments, investors, and entrepreneurs can a setting that promotes digital FDI be established. Diaspora communities have widespread networks and strong connections to both their homeland and host countries, and are uniquely fit to significantly influence this future, aiding in the assurance that digital FDI flows are sustainable, inclusive, and advantageous for all stakeholders.

8. CONCLUSION

In summary, this study emphasized how diaspora-led FDI plays one of the most important roles in promoting economic growth in developing countries. Through the analysis of the historical context of FDI and diaspora, we have gained insight into the vast potential it has. I also highlighted the importance of policies and initiatives that promote and support diaspora-led FDI. For example, the legal framework of Bosnia and Herzegovina requires a reform of the FDI laws and new laws need to be implemented in this regard. Support mechanisms are needed to create an investable environment in which diaspora people can invest in their home countries and contribute to economic development. Successful projects like ZenDev in Bosnia and Herzegovina highlight the positive outcomes of diaspora-led FDI. As the world's diaspora communities become increasingly connected and technology advances, future trends suggest that diaspora-led FDI will continue to grow in importance, which is why governments need to proactively continue their work on establishing a framework suitable for FDI.

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