

The Impact of the Efficiency of the Judicial System in Attracting Foreign Direct Investments in the Republic of North Macedonia

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Abstract: *Foreign direct investment is one of the major factors for the development of national economies with positive implications for the growth of their gross domestic product, technology transfer, as well as increased competitiveness and improved performance of local companies. They generate investment capital, provide new employment, transfer expertise and skills to employees, and increase exports. In the Republic of North Macedonia a number of reform activities have been undertaken relating the protection of property rights, improvement of the efficiency in the functioning of the legislative, judicial and executive branches of government, which result with reduced business risks and motivates companies to make investment decisions. Current paper aimed at outlining the connection between the effectiveness of the judicial system and increasing the number of foreign direct investments in the Republic of North Macedonia.*

Keywords: judicial system; foreign direct investment

JEL Classification: F21, D63, K49

Introduction

Countries compete with each other to become more attractive to foreign investors, reforming national legislation, introducing special benefits to meet the needs of investors, and ensuring legal certainty and efficiency.

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Foreign direct investment (hereafter: FDI) is one of the major factors for the development of national economies. The benefits of attracting FDI include generating investment capital, providing new employment, transferring professional knowledge and skills to employees, as well as increasing exports (Jones & Wren, 2006; Warrnock, 2016).

Despite certain shortcomings (source of external influence, control and competition of domestic companies, danger to domestic labor productivity, reduced autonomy of local companies, etc.), national economies are less skeptical towards foreign direct investment and are more oriented towards creating conditions for their attraction. This applies particularly to underdeveloped and transition countries, which need capital inflows to finance their development. (De Schutter, O., Swinnen, J. & Wouters, J., 2012).

Until 2007, foreign direct investment in the Republic of North Macedonia were noted as moderate, however, they were intensified later and experienced its expansion after 2015. To create a favourable business climate for foreign companies, various measures, from economic and legal aspects, have been constantly taken. In order to increase the interest of foreign companies for investment, a number of reform activities, related to the protection of property rights and the execution of contracts, have been undertaken; as well as the improvement of the efficiency in functioning of the legislative, judicial and executive branches.

Literature review

The long-standing practice so far has shown that the judicial system of Republic of North Macedonia does not have a unified methodology and reports, which will enable obtaining relevant comparable data and information. This particularly refers to the workload in the courts, the rest of the cases from the previous year, the number of newly received cases, the total number of cases pending, how many have been resolved and whether the backlog of court cases has decreased or increased, and the duration of court proceedings. Also, there is no monitoring mechanism that covers the entire duration of court proceedings, including all stages of legal proceedings and instances of courts (European Commission, 2012).

The methodology for measuring and analyzing the efficiency of the judiciary in the Republic of North Macedonia includes the use of secondary data sources (books, scientific papers, articles by relevant authors), and the use of instruments that measure the efficiency of the judicial system, indicated in the guidelines of the Council of Europe (European Commission for the Efficiency of Justice, 2018; European Commission, 2018).

Measurement indicator is the CR (Clearance Rate), which measures the ratio of the number of resolved cases in relation to the number of received cases, i.e how efficiently the courts within a country deal with the influx of cases and

Measurement indicator is the DT (Disposition Time), which estimates the time required in days to complete a court case.

Subject of analysis in this paper will be civil, i.e. commercial cases, from all three levels of courts: courts of first instance, courts of second instance and the Supreme Court (Law on Courts, 2006), due to a specific interest to foreign investors.

The comparative method has been used to analyze the efficiency of the judicial system of the Republic of North Macedonia in relation to with the countries from SEE and its impact on the effects of foreign direct investments.

Connection between foreign direct investment and the efficiency of the judicial system in the Republic of North Macedonia

Considering the importance of FDI, the Republic of North Macedonia, since its independence, pursue a consistent open door policy towards foreign investors and companies. The level of foreign direct investment for the period from 1997 to 2018 varied, but still with an increasing trend¹.

In the decade (1997-2007) FDI increased from 58.06 million dollars to 699.09 million dollars. From an institutional point of view have been established the following institutions: Invest North Macedonia, Agency for Foreign Investments, and Free Economic Zones Authority.

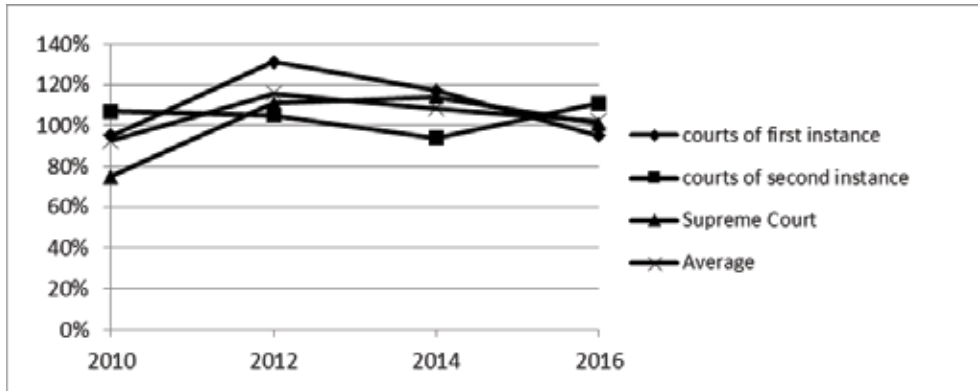
After 2007 began the period of greenfield investments - construction of new facilities in industrial zones, but due to the global crisis in 2008, there was an enormous decline in investment. Only in 2010 did foreign investments revive (\$ 211.61 million), but mostly due to reinvested profits by companies. This measure proved to be good for returning to the economy, because it led to a double increase in foreign direct investments, and according to data from the National Bank they came to amount of 385.68 million dollars in 2018.

An efficient and quality judicial system, built on the highest international standards is a good basis for the interests of all potential investors. Larger foreign companies pay particular attention to legal certainty and guarantees for the duration of court proceedings before their investment approach.

Therefore, the improvement of the judicial system, in terms of its efficient functioning, is an important prerequisite for the development of any democratic state governed by the rule of law, but also an important prerequisite for attracting foreign direct investment necessary for its economic development.

Within the Doing Business of the World Bank, a special segment is dedicated to several parameters that measure the efficiency of judicial systems. Legal certainty and efficient enforcement are among the key prerogatives for the business environment in each country, and thus for securing foreign investment.

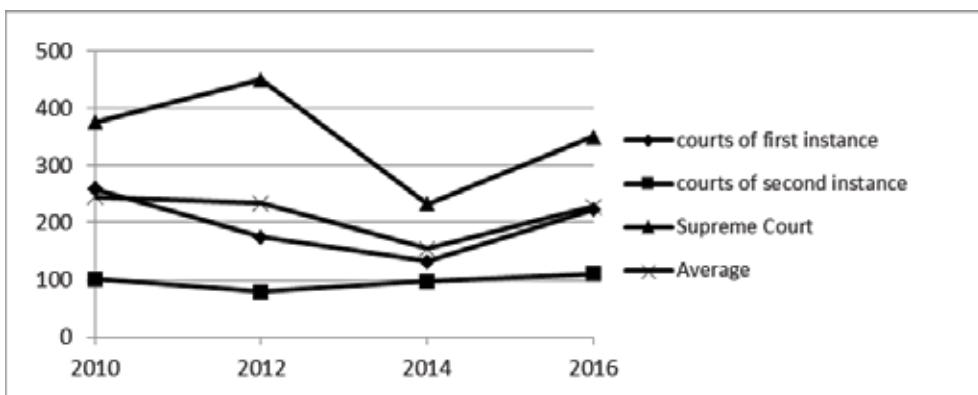
Figure 1: Update rate, i.e average rate of overflow of civil and commercial cases before the courts of the Republic of North Macedonia (2010 -2016)



Source: authors' design

According to the summarized data (European Commission for the Efficiency of Justice, 2018) shown in Figure 1, the average rate of total inflow of cases by the courts in 2010, for civil and commercial cases was 92% of the inflow of new cases, which means that not only failed to overcome the number of newly received cases, but also increased the total number of pending cases. In the following years, there was an increase of overflow inflow of 116% in 2012, with a slight decline of 108% in 2014 and 102% in 2016. This trend indicates increased efficiency in overcoming the influx of items and reducing the backlog of cases.

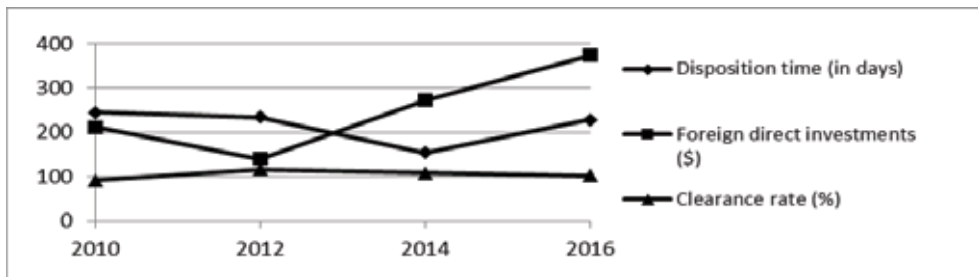
Figure 2: Average time required, expressed in days, to resolve the backlog of cases before the courts of the Republic of North Macedonia (2010 to 2016)



Source: authors' design

Regarding the second instrument - the average time required to resolve civil and commercial disputes for all courts in the period from 2010-2016 (European Commission for the Efficiency of Justice, 2018), the summarized results in Figure 2 shows that in 2010, the average number of days required to resolve the backlog of cases before all courts in the Republic of North Macedonia was 245 days. In the following years, this trend decreased in the number of days required to resolve the backlog of cases, i.e in 2012 it took 234 days, while in 2014 there was a significant decrease to 154 days. In 2016, the number increased to 228 required days; however, compared to 2010, it decreased.

Figure 3: Ratio between the efficiency of the courts in resolving court cases with the inflow of foreign direct investments in the Republic of North Macedonia (2010 -2016)



Source: authors' design

From Figure 3 can be noted that with integrated use of data from the first and second indicators, the efficiency of the courts in the Republic of North Macedonia, despite the slight declines in the period from 2010 to 2016 was increasing.

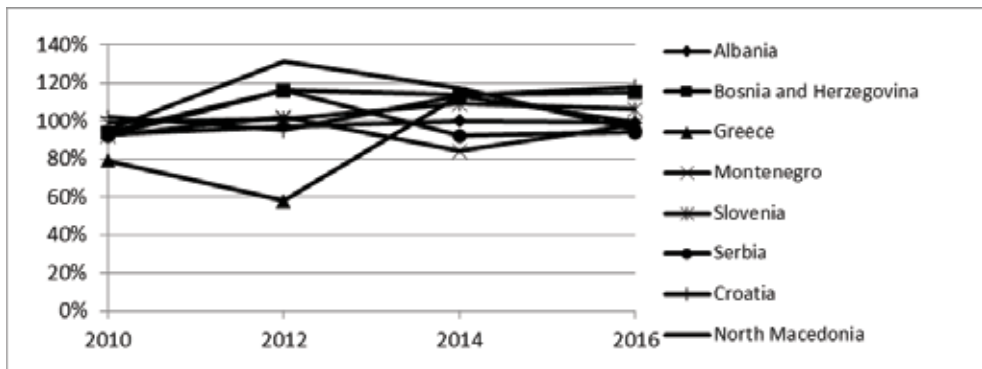
Comparing this trend of increased efficiency of the courts with the inflow of foreign direct investments, it can be noticed that, despite certain reductions in 2012, FDI in the Republic of North Macedonia increased. Following the movement curves, all parameters have a similar direct proportional trend, i.e the increase in FDI follows the increase in the efficiency of the judicial system in the Republic of North Macedonia.

Measuring the efficiency of the judicial system as a factor in attracting FDI in Southeastern Europe

When measuring the efficiency of the judicial system of Republic of North Macedonia, a comparison was made with the countries of Southeastern Europe, using the two indicators - *Clearance Rate* and *Disposition Time* in civil and commercial

cases for all instances of the courts, in the period from 2010 to 2016 (European Commission for the Efficiency of Justice, 2018). Regarding the efficiency of the courts in resolving first instance civil and commercial court cases, it should be emphasized that the measurement of efficiency in the analyzed countries of Southeastern Europe and the comparison to the Republic of North Macedonia is considered only for the first instance courts, considering the availability of data. Cannot be found complete, official data on the clearance rate and disposition time required to decide on second instance and higher courts. Also, cannot be found official, complete data regarding the efficiency of the judicial system for the period after 2016.

Figure 4: Average clearance rate of the courts in resolving first instance civil and commercial court cases by country (2010 -2016)

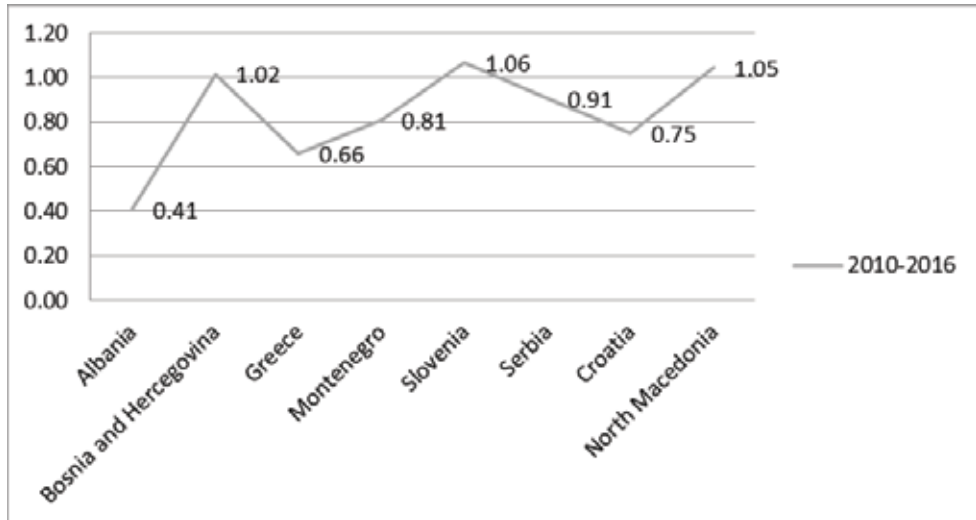


Source: authors' design

From Figure: 4 can be notice that the data collected in the last four evaluations show a positive trend of improving the clearance rate over a long period (2010 - 2016). The highest clearance rate, i.e overcoming inflow of court cases, was achieved by the first instance courts in the Republic of North Macedonia in 2012. The average clearance rate from 2010 to 2016 was 105%. The good results in 2012 were due to the implemented reforms for reducing the large number of pending cases in the courts in the Republic of North Macedonia, with a significant number of enforcement cases and non-litigation cases (around 330,000 cases) which were removed from the court system in the second half of 2011, as a result of the transfer of competencies to professional enforcement agents and notaries. However, the main reason for the decrease in the number of unresolved cases is the high rate of resolved cases in the trial courts, as a result of the increased procedural discipline and work monitoring of individual judges.

The trend in clearance rate of countries for the specified period is shown in Figure: 5.

Figure 5: Average clearance rate disputes by countries

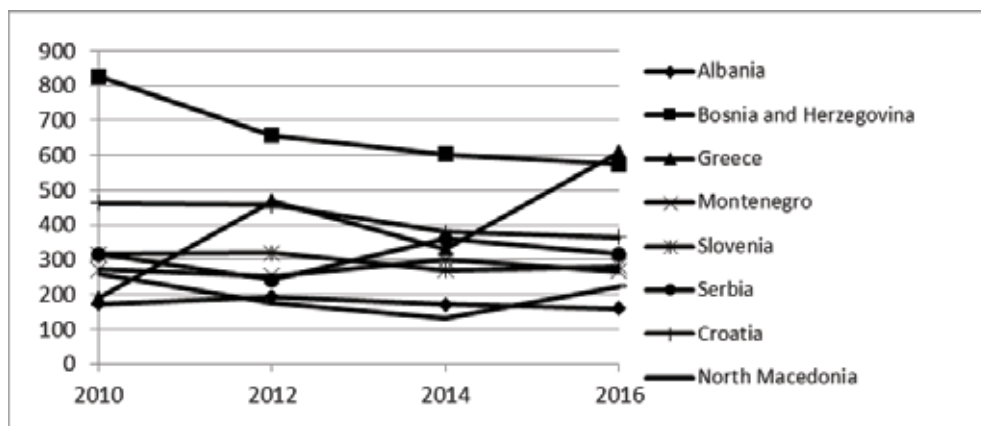


Source: authors' design

However, according to the European Commission Report on the Republic of North Macedonia (European Commission, 2016) the country's judicial system raises concerns, as reforms have been hampered by political interference in the work and appointments in the judiciary. Selective justice reports continue in certain high-profile or politically sensitive court cases. Corruption remains prevalent in many areas and continues to be a serious problem.

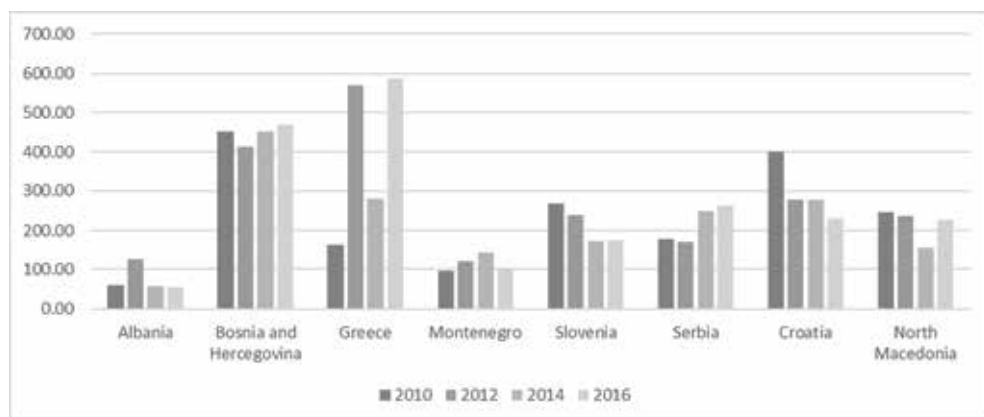
Figure: 6 shows a positive trend of reducing the disposition time, expressed in days, for resolving backlogs in all analyzed countries, for the period from 2010 to 2016 (European Commission for the Efficiency of Justice, 2018). Disposition time required for resolving civil and commercial cases in the first instance courts was the shortest in the Republic of Montenegro from 96 days in 2010, in the Republic of North Macedonia the shortest time was 154 days in 2014, and the longest is in Bosnia and Herzegovina with 586 days in 2016, to resolve the backlog of court cases.

Figure 6: Average length of court proceedings in resolving first instance civil and commercial court cases by country 2010-2016



Source: authors' design

Figure 7: Average rate of resolving disputes by countries



Source: authors' design

In the 2014 Progress Report on Republic of North Macedonia (European Commission, 2014) was noted that the legislative framework, governing the judiciary, as well as its physical and technical infrastructure, has been significantly developed because of the comprehensive reforms implemented over the past decade. Many of the general issues, facing all candidate countries, have been resolved, including the elimination of backlogs in the courts, the formal independence of the judiciary (Judicial Council), the introduction of a system of administrative justice and improvement of

legislation on civil and criminal proceedings. Regarding the fight against corruption, a legal and institutional framework has been established, and have been registered investigations, indictments, and verdicts.

Discussion about the analysis

The efficiency of the judicial system is an important factor for attracting FDI in the Republic of North Macedonia. The results of the above measurement of the efficiency of the judicial system in the Republic of North Macedonia through both instruments, show increased efficiency of the courts in dealing with the inflow of cases and the required time, in days. That works in direct proportion to the movement of the inflow of foreign direct investments which (2010 - 2016) shows upward growth.

Clearance Rate was increased from 92% in 2010 to 102% in 2016, even though in 2012 and 2014 there was a higher growth, which slightly decreased in 2016.

Regarding the necessary days to complete the remaining cases, the required 245 days in 2010 were reduced to 228 in 2016.

These two positive trends, for the same period (2010-2016), have been followed by the inflow of foreign direct investments in the Republic of North Macedonia, i.e they show an increase.

FDI inflow in 2010 increased from 211.61 (US million dollars) to 372.99 (US million dollars) in 2016, which means, from 2014 to 2016, foreign direct investment grew in direct proportion to only one of the indicators “Time needed to resolve”, but also in accordance to the overall analysis (Figure: 1) for the measurement period (2010 - 2016).

However, this increase has been slowed in the recent period, which indicates the need for greater commitment in taking measures to improve and increase the efficiency of the judicial system in the Republic of North Macedonia. The Government needs to take action to harmonize the legislation of the Republic of North Macedonia with the legislation of the European Union, to strive for an independent judiciary, transparency and efficiency of the judiciary, as well as to reaffirm its commitment to an uncompromising fight against corruption.

Conclusions and recommendations

In order to attract foreign direct investment, Republic of North Macedonia needs to ensure a positive climate, macroeconomic stability and transparency in the conduct of public spending.

Overall, sound policies (macroeconomic and structural) are needed, crucial for further foreign direct investment, which would increase the long-term potential of the economy without increasing its weaknesses.

In providing the conditions for more dynamic attracting foreign direct investment the following recommendations can be given:

- Establishing secure and non-discriminatory legal framework, which will enable simplification of administrative procedures for the entry of foreign investors, i.e. providing institutional legal frameworks for foreign companies, under the same conditions that apply to domestic companies as an important prerequisite for legal certainty of investors. That certainly implies changing the legislation with provisions that will enable the fight against the grey economy, crime, and corruption.
- Adoption of a Judicial Statistical Methodology, as a methodological tool for collecting, processing and analyzing statistical data, to be developed on the basis of the Judicial Statistics Instruments of the European Commission for the Efficiency of Justice (CEPEJ) and the Judicial Progress Review of the European Union (EU Justice Scoreboard). In this way, a compatible measurement of the work of the courts and judicial achievements will be enabled, which of course, is one of the basic conditions in creating a positive climate for attracting foreign investment.
- In the Republic of North Macedonia numerous reform activities have been undertaken in relation to FDI, which refer to greater attractiveness of investors, protection of property rights, execution of contracts. Therefore, the recommendations go in the direction of further alignment with national legislation that provides legal certainty, efficiency and special benefits to meet the needs of investors.

NOTES

¹ more information http://www.nbrm.mk/diriektni_inviestitsii_dvizhienja.nsp

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