

# SIGNIFICANT CHARACTERISTICS OF FOREIGN DIRECT INVESTMENT

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Foreign investment represents a key issue for the Slovak Republic. In principle, we distinguish between foreign direct investment (FDI) through which foreign investors acquire ownership (control) of certain capital goods and foreign indirect investment in the form of the purchase of securities, mainly shares and bonds, which are not connected with control of the capital invested.

In 2000, foreign direct investments (FDIs) were made world-wide in the total amount of more than US\$ 1 billion. From 1999 to 2000, the structure of FDIs by region (Tab. 1) varied before returning to the initial level at the end of the decade (80% in 2000), while the share of advanced countries decreased steadily (from 81.9% in 1990 to 56.6% in 1994). These changes were also reflected in Central and Eastern Europe, except for the initial level which was much lower here (0.5% of the total volume of FDIs in 1990).

In future, foreign investors are expected to show interest mainly in China (in power industry, motorways, railway transport, and telecommunications) and in new areas in South America and Africa. The internal structure of investments will also change, i.e. from corporate investments to investments financed by banks and to portfolio

investments (acquisition and subsequent sale of shares issued by strategic companies).

Foreign investors seem to be interested in areas with duly qualified human resources, well-developed infrastructure, supplier background, and services.

A survey of FDIs since the coming into being of the Slovak Republic (SR) would be incomplete without comparison with other CEFTA countries (Tab. 2).

**The significant characteristics of FDI in the SR are the following:**

– permanent growth in the volume of FDI with marked increases in the years 1994/1993, 1996/1995, 1998/1997, but mainly in 2000/1999, when the index of growth in FDI reached 170.2 (Tab. 3). Comparison with other CEFTA countries shows that the problem of low per-capita FDI is the low initial level. In 1993, per-capita FDI in the SR was 2.25 times lower than in the CR; 6.8 times lower than in Hungary; 5.1 times lower than in Slovenia, but 1.2 times higher (1.5 times in 1998) than in Poland. Although the rates of growth in per-capita FDI in the years 1993 to 1998 were comparable with the figures for CEFTA countries, they failed to reach such a level that could offset the initial handicap;

**Tab. 1 Structure of FDIs by region**

Regions	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Advanced countries	81.9	71.3	65.6	61.5	56.6	61.8	58.2	58.4	71.0	78.5	80.0
Developing countries	17.6	26.9	32.0	35.8	41.0	34.0	38.4	37.6	26.1	19.4	17.3
Countries of Central and Eastern Europe	0.5	1.8	2.4	2.7	2.4	4.2	3.4	4.0	2.9	2.1	2.7
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: UN Conference for Trade and Development (UNCTAD), own estimates.

**Tab. 2 Per-capita FDI in the SR – comparison with CEFTA countries**

Countries	1993		1994		1995		1996		1997		1998	
	Position by FDI per capita	Index of growth against the previous year	Position by FDI per capita	Index of growth against the previous year	Position by FDI per capita	Index of growth against the previous year	Position by FDI per capita	Index of growth against the previous year	Position by FDI per capita	Index of growth against the previous year	Position by FDI per capita	Index of growth against the previous year
Slovakia	4		4	1.51	4	1.33	4	1.81	5	1.14	5	1.12
Czech Rep.	3		3	1.48	3	1.86	3	1.19	3	0.96	3	1.29
Hungary	1		1	1.25	1	1.60	1	1.21	1	1.09	1	1.11
Poland	5		5	1.53	5	1.58	5	1.76	4	1.47	4	1.73
Slovenia	2		2	1.40	2	1.32	2	1.10	2	1.24	2	1.08
Positon – SR*			2		4		1		4		3	

\* Based on the index of growth compared with the previous period.

Source: Own estimates

**Tab. 3 Volume of FDI in Slovakia (in millions of Sk)**

Year	Volume as at 31 December	Index compared with the previous year
1994 ( <i>volume as at 1. Jan</i> )	15 276	
1994	24 266	153.9
1995	32 125	132.3
1996	44 239	137.7
1997	55 337	125.0
1998	73 121	132.1
1999	86 385	118.2
2000	165 686	170.2

Source: Dept. of Foreign Investments at the Ministry of Economy

**Tab. 4 Structure of FDI by sector**

Sector	1993	1994	1995	1996	1997	1998	1999	2000
Agriculture, hunting, and forestry	0,3	0,2	0,2	0,1	0,0	0,0	0,2	0,1
Extraction of raw materials	0,0	0,1	0,1	1,7	1,5	1,2	1,2	1,2
Industrial production	50,9	46,9	43,34	49,5	43,6	48,9	48,4	53,5
Production and distribution of electricity and gas	0,0	0,0	0,0	0,5	0,7	0,6	0,5	0,3
Construction	2,0	1,4	1,1	2,3	2,5	2,1	2,1	1,0
Wholesale and retail trade	22,7	31,2	32,4	20,0	18,8	16,9	18,9	12,4
Hotels and restaurants	4,9	3,2	2,4	1,4	1,2	0,9	1,2	0,7
Transport, storage, and communications	0,5	0,5	0,4	3,7	4,0	3,3	3,2	15,1
Banking and insurance	12,2	11,0	15,7	17,9	24,8	22,9	20,4	13,0
Real estate, leasing, and business services	5,7	5,0	3,4	2,4	2,4	2,8	3,6	2,4
Health care and social services	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Other public, social, and personal services	0,8	0,5	0,9	0,5	0,5	0,4	0,3	0,3
	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0

**Tab. 5 Structure of FDI by country of origin**

	1993	1994	1995	1996	1997	1998	1999	2000
Germany	21,0	22,4	17,5	20,9	25,7	20,6	22,0	27,7
Austria	24,5	20,6	21,4	21,7	21,4	18,5	16,9	15,1
Great Britain	0,3	2,6	7,2	13,4	11,4	11,6	9,1	3,4
USA	12,9	14,4	11,4	2,3	7,8	10,6	13,0	8,9
The Netherlands	4,1	4,9	6,4	7,4	7,3	12,9	15,0	22,7
Czech Republic	11,2	15,2	16,2	15,9	7,5	9,5	8,6	5,9
France	10,5	7,0	5,9	5,9	7,5	6,9	4,2	2,8
<b>Total</b>	<b>84,5</b>	<b>87,1</b>	<b>86,0</b>	<b>87,5</b>	<b>88,6</b>	<b>80,6</b>	<b>88,8</b>	<b>86,5</b>

Source: Dept. of Foreign Investments at the Ministry of Economy

– the high share of the corporate sector in FDI (up to 90.6% of total FDI in 2000), which will be modified by the entry of foreign investors into banks or the corporate sector;

– the concentration of FDI in three sectors in 1999 (Tab. 4) – i.e. industrial production, banking and finance,

wholesale and retail trade – whose share reached 88.1% of the total volume of FDI in 1999; in 2000, a fourth sector appeared on the scene – transport, storage, and communications. These four sectors accounted for as much as 94% of total FDI in 2000;

– continued concentration of FDI in terms of the country of origin (Tab. 5): seven major foreign investors (from the EU – 5, USA – 1, and CR – 1) have had a share of more than 84% of total FDI since 1993. If we include Hungary (with a share of 5.47%), the share of 8 countries reached almost 90% of total FDI in 2000. Within the internal structure of FDI, the share of Germany is still high, while that of Austria, France, and the Czech Republic has fallen significantly, whilst, at the same time, the share of the

Netherlands has recorded a steep increase;

– the concentration of FDI in the Bratislava Region: more than 55% of total FDI takes place in this region, i.e. since 1993; changes in the level of FDI in other regions: investment in the Košice and Prešov regions fell to the initial level in 2000 (Tab. 6);

– the structure of FDI in industry shows a change in the preferences of strategic investors. While FDI in 1999 took place mostly in the manufacture of vehicles, trailers, and semi-trailers (i.e. production with a higher added value, which was a positive development), FDI in 2000 was directed to metal production (VSŽ, a.s.), the production of refined oil products and nuclear fuels (Slovnaft, a.s.), and that of pulp, paper, and paper goods (SCP, a.s.). We can only hope that foreign investors will give preference to investment in production with a higher added value in future;

– foreign investors have mostly market-based incentives (low wage costs may turn Slovakia into a export base);

– FDI in the SR contributes significantly to ‘shaping’ the structure of sectors, especially in industrial production. It would be much better if the key sectors were not the material, energy, and import-intensive ones;

The benefits of FDI may be evaluated according to the form of FDI, i.e. whether it is a green-field investment or

Tab. 6. Structure of FDI by region

Region as at 31/12/92	1993	1994	1995	1996	1997	1998	1999	2000
Bratislava	56.1	62.1	62.5	61.1	61.3	37.2	55.2	55.4
Trnava							11.2	
Trenčín	9.5	14.5	14.2	15.2	17.0	16.4	7.8	12.0
Nitra							4.2	
Žilina							3.3	
Banská Bystrica	10.2	7.3	10.2	9.5	9.0	7.4	5.5	7.6
Prešov							3.7	
Košice	24.2	16.1	13.1	14.2	12.7	19.0	9.1	25.0
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: Dept. of Foreign Investments at the Ministry of Economy

Tab. 7

<b>Name of company</b>	NYLSTAR, a. s.	Siemens. s. r. o.
<b>Size of company</b>	Over 300 employees	Up to 300 employees
<b>Organisational form</b>	Joint stock company	Limited liability comp.
<b>Country of origin</b>	France, Italy	Germany
<b>Form of investment</b>	Acquisition	Green-field investment
<b>Motives for foreign investment (FI)</b>	<ul style="list-style-type: none"> <li>• lower wage costs</li> <li>• export base</li> </ul>	<ul style="list-style-type: none"> <li>• acquisition of new markets</li> </ul>
<b>Benefits of FI to the company</b>	<ul style="list-style-type: none"> <li>• management (know-how)</li> <li>• technology (in part)</li> </ul>	<ul style="list-style-type: none"> <li>• technology</li> <li>• management (know-how)</li> <li>• marketing (know-how)</li> <li>• increase in the qualification of the workforce</li> </ul>
<b>Benefits of FI to the region</b>	<ul style="list-style-type: none"> <li>• new business culture</li> <li>• new approach to the working environment</li> </ul>	<ul style="list-style-type: none"> <li>• job opportunities</li> <li>• new business culture</li> </ul>
<b>Export</b>	Export: EU, North America, CEFTA, Eastern Europe, and other countries	Share of exports in turnover: 80% Export: EU
<b>Certificates achieved</b>	ISO 9001	ISO 9001
<b>Future objectives</b>	<ul style="list-style-type: none"> <li>• technological innovations</li> </ul>	<ul style="list-style-type: none"> <li>• extension of the production capacity</li> <li>• construction of new premises</li> <li>• diversification of production</li> </ul>

Source: Own research

an investment in an existing company, through purchase (acquisition) or privatisation in the form of direct sale (Tab. 7). The critical point of acquisition is the fact that, in most cases, acquisition results in a change in ownership and the shift of control abroad. It is obvious that this form of FDI is rarely connected with the inflow of new technologies or technological know-how. In the initial phase, this type of investment does not usually create new jobs. Green-field investment appears to be more useful to the economy. In the long term, however, the two forms are roughly equal in terms of benefits. The benefits of FDI in the SR to companies are seen mainly in the area of management, marketing, and to some extent technology. The benefits to regions are: the introduction of a new business culture, new approach to the working environment, and the creation of new jobs (many jobs would be lost without acquisition);

– a positive aspect of FDI in the SR is that foreign investors show interest mostly in companies exporting their products to the EU or CEFTA countries (future EU members), which results in the establishment of links between the Slovak corporate sector and the common market of the EU;

– the basic requirement of foreign investors wishing to invest in Slovakia is the existence of long-term stability in the business environment;

– another positive feature of FDI is that most investors consider investment in Slovakia a wise decision and plan to extend or diversify the range of production in future;

The above facts show that there are reserves as well as other possibilities for FDI in Slovakia. Each FDI is a unique act and its effects should be evaluated accordingly.