

PRESS RELEASE NOT TO BE RELEASED BEFORE 30-06-2008, 12:00 a.m.**Foreign Direct Investment in Central, East and Southeast Europe 2007-2008:
decline to follow uneven growth**

The Vienna Institute for International Economic Studies (wiiw) presents an analysis of foreign direct investment (FDI) in 20 Central, Eastern and Southeastern European countries based on the latest update of its database. Raiffeisen Zentralbank Österreich AG (RZB) supported the analysis. RZB deputy CEO Herbert Stepic emphasized the great importance of FDI for the transformation in Eastern Europe, 'Not only are FDI the basis for hundreds of thousands new jobs, they also brought valuable know-how to the countries of the region.' The data rely on statistics of the balance of payments and international investment position as published by the respective central banks.

2007 was a year with *growing FDI* (+16%) to the CEECs (Table 1). Within the region, inflows shifted to the East: the share of the NMS-10 declined to 44% after 55% in 2006; the Western Balkans registered a share of 9% – similar to the previous year; and the European CIS expanded to 47% after 35% in 2006. This reflects the *dynamics of Russia* and other European CIS countries and indicates a *saturation with FDI in the NMS*.

The **NMS-10** received a *lower amount* (-7%) of FDI in 2007 than in the preceding year. In general, the countries that acceded to the EU in 2004 are losing steam. Here privatization is largely completed, foreign multinationals have finished the takeover of local markets, and also unit labour costs are rising. Additional investments take place primarily within the existing companies by reinvesting profits. Half of the NMS (Hungary, Lithuania, Poland, Romania and Slovakia) recorded a decline of FDI inflows. Except for Hungary, this setback took place despite high rates of economic growth and improving conditions of doing business. It was in part a cyclical setback following record inflows in Romania and Slovakia a year earlier. The NMS reporting increases were first of all the Czech Republic, Slovenia and Bulgaria. The Czech record was a result of expansion in all sectors. Due to the activity of foreign subsidiaries, this country and also Hungary and Slovakia achieved a *positive foreign trade balance*. In *Bulgaria* the upswing resulted mainly from projects in the 'real estate and business services' sector. A major problem with this type of FDI, however, is that it *will not generate exports* which would be necessary to correct the soaring foreign trade deficits.

Southeast Europe continued to receive *increasing* amounts of FDI in 2007 (+13%) but at a lower pace than previously. The privatization-related peaks of 2006 were corrected downwards in Macedonia and Serbia. By contrast, Bosnia and Herzegovina, Croatia and Montenegro benefited from remarkable increases continuing the trend of the past few years. These were often *privatization deals* causing one-time large inflows such as in the Bosnian (Republika Srpska) telecom or the Croatian pharmaceutical sector.

Russia plays an *increasing role both as a receiver of FDI and as an investor abroad*. In 2005 Russia's share in the FDI inflow to the region had been only 17%, in 2007 it was as much as 38%. Had it not been for the Russian boom, FDI in CEECs would have hardly increased last year. The country's dynamic consumer goods sector, rich natural resources and booming financial sector

attracted a growing number of investors despite relatively high perceived risks. Also Ukraine has established itself as an attractive FDI location, but the amount of inflow is still much below its potential. Belarus is new on the map of FDI, and so far one can only speak of single projects (telecom privatization) rather than a general trend of opening up to foreign investments.

Relative to population, larger countries receive lower amounts of FDI than smaller ones. *Estonia is ahead of the other countries* of the region while Croatia, the Czech Republic, Hungary and Slovakia form a group of countries with also relatively high stocks per capita. Low relative amounts of FDI can be found in the CIS countries and in a number of Southeast European countries that have a very short history of FDI.

The list of **investing countries** in the NMS has for many years been led by the Netherlands, Germany and Austria (Table 2). In 2006 the *share of Austria increased slightly*, to 11%, while those of the other two countries fell to about 17% each. The share of the EU-15 is overwhelming with 79%, but it is declining while the NMS investors invest more in each other's economies. In Southeast Europe, Austria is the largest investor with 18% of the 2006 stocks, with a decreasing share compared to the previous year, but much ahead compared to the early 2000s. Germany was overtaken by the Netherlands, which now ranks second. Austria is present first of all through its financial institutions and retail companies, Germany is primarily an investor in manufacturing, while the Netherlands is present in all activities, often as the European bridgehead of US investors. The opportunities for Austrian FDI are shifting to the East where mainly the more experienced and larger investors can expand.

After continuous expansion in 2004 through 2007, FDI inflows to the CEECs will face a setback in 2008 in all parts of the region. The global financial turbulence had negative effects first of all on countries which are indebted or run a high current account deficit – Estonia, Latvia, Hungary and Bulgaria. A further challenge to FDI growth is the growing scarcity of available capital for investors. The lending policy of banks being more cautious now than before, investors are facing more expensive financing through bank credits. Particularly real estate investments are vulnerable. Countries where this type of FDI predominates, such as the Baltic countries and Bulgaria, may be especially affected. The European economic slowdown currently under way has contagion effects on CEECs, markets and investments expand less than earlier. Effects are not necessarily negative on export-oriented FDI. True, if demand declines and company profits shrink, less can be spent on new investments abroad. But we can also expect that a euro appreciating against the dollar challenges the external competitiveness of European producers unless these are able to cut costs. One of the ways to reduce costs is to outsource to low-cost locations. The NMS will remain favourable locations for export-oriented activities.

Table 1

Overview of FDI in Central, East and Southeast Europe

FDI inflow, EUR million

	2001	2002	2003	2004	2005	2006	2007	forecast 2008	Per capita inflow EUR 2007	Per capita stock EUR 2007
Czech Republic	6296	9012	1863	4007	9374	4797	6674	6000	646	6612
Hungary	4391	3185	1888	3633	6172	5428	4049	3500	403	6600
Poland	6372	4371	4067	10453	8317	15198	12834	13000	337	2900
Slovakia	1768	4397	1914	2441	1952	3324	2093	2000	388	5900
Slovenia	412	1722	271	665	473	512	1073	500	531	4000
New Member States-5	19240	22687	10002	21200	26287	29258	26722	25000	405	4300
Bulgaria	903	980	1851	2736	3152	5961	6109	4500	798	3252
Romania	1294	1212	1946	5183	5213	9060	7141	8000	332	1914
Estonia	603	307	822	775	2255	1341	1815	1200	1353	8416
Latvia	147	269	270	512	568	1326	1589	1100	698	3183
Lithuania	499	772	160	623	826	1448	1412	1200	418	2977
New Member States-10	22685	26226	15051	31029	38301	48394	44789	41000	439	3716
Albania	232	143	158	278	224	259	463	600	147	722
Bosnia and Herzegovina	133	282	338	567	478	564	1478	800	384	1200
Croatia	1468	1138	1762	950	1468	2738	3626	2800	817	6841
Macedonia	499	112	100	261	77	345	239	500	117	1200
Montenegro	5	76	44	53	393	644	1008	800	1612	3556
Serbia	184	504	1204	777	1265	3504	2258	2000	304	1341
Southeast Europe	2520	2255	3606	2885	3906	8054	9072	7500	421	2400
Belarus	107	262	152	132	245	282	1293	300	133	319
Moldova	116	89	65	121	159	193	335	200	94	344
Russia	3069	3660	7041	12422	10354	25979	38344	35000	270	2000
Ukraine	884	734	1260	1380	6263	4467	7220	7000	155	565
European CIS	4175	4744	8518	14055	17021	30921	47192	42500	234	1500
Central and Eastern Europe	29380	33226	27175	47970	59227	87369	101052	91000	310	2300

Source: wiiw Database on Foreign Direct Investment in Central, East and Southeast Europe, 2008.

Table 2

Inward FDI stock by major home countries

as of December 2006, share in per cent

	CZ	HU	PL	SK	SI	BG	RO	EE	LV	LT	NMS-10
	2005										
Austria	11.3	11.4	3.7	14.8	32.3	25.4	23.0	1.2	1.5	0.5	11.0
Germany	20.8	27.0	16.4	19.3	7.9	5.7	10.1	2.0	11.1	9.7	17.1
Netherlands	27.1	13.2	19.9	19.7	9.1	10.7	17.1	3.4	5.6	2.5	17.8
EU-15	84.4	74.7	83.1	79.0	75.4	72.3	78.0	82.9	52.3	51	78.9
	AL	BA		HR	MK		ME	RS	SEE-6	RU	UA
	2004										
Austria	2.3	39.5		20.4	10.5		9.0	6.2	18.1	.	7.6
Germany	1.0	8.4		8.5	3.1		5.6	16.6	9.6	4.9	25.8
Italy	30.0	2.5		13.4	2.1		1.0	1.4	9.2	.	0.6
Netherlands	.	3.2		17.1	10.1		0.5	7.9	12.9	28.4	7.1
EU-15	82.4	.		83.9	45.7		34.6	58.3	67.4	.	55.1

Source: wiiw Database on Foreign Direct Investment in Central, East and Southeast Europe, 2008.

wiiw Database on Foreign Direct Investment in Central, East and Southeast Europe, 2008:**Decline to Follow Uneven FDI Inflow Growth**

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