ASSESSMENT OF FDI ATTRACTIVENESS OF V4 COUNTRIES

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Abstract: *Countries applying for foreign capital in the form of foreign direct investments (further referred to as "FDI") are trying to create favourable economic, legal and business conditions for potential investors. It is not easy to identify and quantify the key factors of country's attractiveness for FDI inflow because some determinants may be perceived differently, depending on the type and nature of FDI, and motives and preferences of investors. The goal of this paper is to evaluate and compare the FDI attractiveness of V4 countries, applying various approaches in the form of international composite indices.*

Keywords: Factor of attractiveness; FDI; international indices; Visegrad Group.

1 INTRODUCTION

If the company has already decided to invest abroad in the form of direct investment, then the potential investor will carefully consider the choice of the country, which would provide investor with the best result in respect to his/her objective that is usually defined as maximum profit achieved by penetration into new markets. At this point the important role is played by the proper information on host countries. This is where the opportunity for application of various indices (usually composite) is created, which measure the attractiveness of country for inflow of FDI. There are various approaches to the most important determinants of FDI with respect to index itself. On one side there are indices that are attempting to cover a wide base of attractiveness factors, on the other side are indices focused on a specific area, such as regulatory restrictions or barriers to business.

2 FDI FLOWS AND FACTORS OF HOST COUNTRY ATTRACTIVENESS

According to OECD [11], the FDI are an integral part of an open and effective international economic system and they represent a major catalyzer for development. However, the contribution of FDI does not grow in all countries, sectors and local communities automatically and in the same manner. At the same time, it is important to note that some countries are more attractive to investors than other. The location and control decisions of multinational enterprises are at the core of managerial decision-making and academic theorising in international business [1].

FDI mean to the country or region not only additional external financing, but also the inflow of know-how, experience, knowledge and also the arrival of new technologies supporting R&D activities, which can contribute to increasing the competitiveness of domestic firms [15]. The attractiveness of the host country is determined by all factors, which affect the enlargement of appreciation of invested capital. The expected profit may explain the movement of FDI, but management may emphasize all the range of another determinants. A clear attraction for the maximizing corporate profits is the market size and sustainable growth of markets [16]. Also, the state aid impact is apparent [14]. The existence of local business networks, which can be used in supplier – customer relationships, can also be one of the factors important for investment localization. The indicator of economic openness can indirectly inform on this factor [4], [18].

3 THE ATTRACTIVENESS OF V4 COUNTRIES THROUGH INTERNATIONAL INDICES.

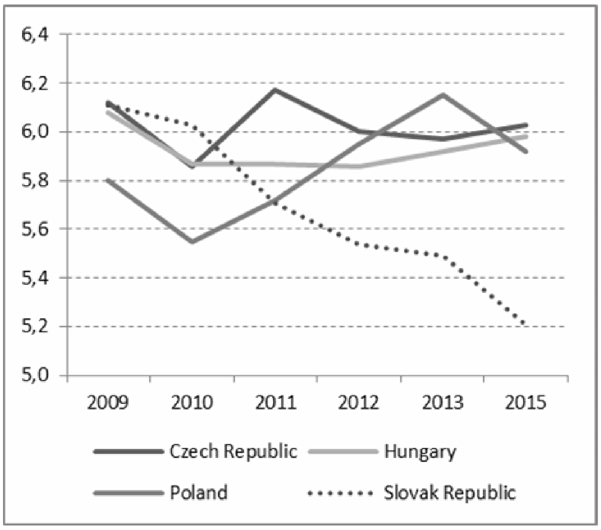
The countries of the Visegrad Group (V4) have the similar economic level and comparative and structural advantages. And this is the reason why these countries are competing with each other for attracting the foreign investments. The attractiveness of these countries for FDI was influenced also by their accession to the European Union in 2004, which brought them new opportunities for their economic development, however also certain restrictions, which caused the end of some advantages, e.g. stricter EU rules on granting tax relief for potential investors [13]. The Visegrad Group creates the space for strengthening coordination and consultation mechanism to find common positions and opinions on topical issues of foreign and European policy, regional development, economic and cultural cooperation [6]. The European Attractiveness Survey 2015 shows that the region of Central and Eastern Europe (CEE), where the V4 countries belong, is the fourth most attractive region in the world for investors. However, it should be noted that compared to 2008, there has been a significant decline. Currently the region of CEE is considered to be attractive for 28% of investors, while in 2008 it was 42%. CEE has established a role as a workshop and back-office for the European market and become an integral part of many European value chains [2].

The objective of this paper is to evaluate and compare the attractiveness of V4 countries for FDI and to identify the strengths and weaknesses of individual countries. Taking into consideration the stated objective, the selection of indices was influenced primarily by the presence of V4 countries in the file of evaluated countries. We base our assessment on results of multi-criterial evaluation of countries through the international composite indicators, which are specifically oriented on analysis of factors of attractiveness of host country for FDI in the form of quality of business environment, barriers for FDI to enter a country, quality of regulatory framework and other.

When evaluating the level of attractiveness of a host country, it is necessary to monitor a variety of indicators and conduct analysis in terms of macroeconomic performance, stability of political and legal environment, quality of business environment and human capital and other [3]. This creates a wide base of data, which may be in some cases difficult to fulfil numerically. Evaluating through simple tools of descriptive statistics may be a starting point, but not fully sufficient. International institutions quantify the indices in their journals, which monitor and assess the attractiveness of countries and these indices can be used as starting element when evaluating the suitability of the country for investments [10]. The univariate methods, in which every indicator is assessed individually, provide the information on the status and development of given indicators, which are valuable in terms of country's attractiveness for FDI inflows, but those are only partial information. Therefore it is necessary to use such indicators, which allow a complex evaluation of a given issue. And this is where the opportunity for composite indicators opens up, as they are able to describe simultaneously several aspects of the problem. They can be easily interpreted as a set of sub-indicators, allowing a quick comparison from a certain point of view.

3.1 Global opportunity index

The Milken Institute is a nonprofit, nonpartisan think tank determined to increase global prosperity by advancing collaborative solutions that widen access to capital, create jobs and improve health. It does this through independent, data-driven research, action-oriented meetings and meaningful policy initiatives. The Milken Institute assembles the Global Opportunity Index (GOI), which is designed to assist companies and countries as they explore FDI opportunities. It fills gaps in information that frequently discourage mutually beneficial transactions that spur development and job growth. Moreover, the index provides a baseline assessment for countries seeking to improve their business environments and attract foreign investors, the kind that commit capital to strategic projects rather than move it around as a fleeting portfolio tactic. For 2015, the index ranks 136 countries on six continents for which data is available. Sixty-one variables are assessed across four categories related to national economies and supporting infrastructure [19]. Score is between 0 and 10. 10 indicating the most favourable conditions for investment, and 0, signalling the least favourable.



Note: Data for 2014 not available.

Fig.1 Development of GOI in V4 countries
Source: Self-elaboration based on [8]

As shown in Fig. 1, a leader of country's attractiveness changed during the reporting period. While in 2010 the most attractive country was the Slovak Republic with overall evaluation of 6.03, in the following two years was replaced by the Czech Republic. In 2013 the best score was reached by Poland with 6.15. Currently the leader among V4 countries is again the Czech Republic. In case of the Czech Republic, Poland and Hungary, we see the alternating phases of growth and decline, however the Slovak Republic reports the downward trend throughout the entire period. Slovakia even belongs to top 5 countries with the greatest decline, where the total decrease (2009/2015) went from 6.11 to 5.21 (-0.9). Decrease of Slovakia's attractiveness, two years in advance, follows the trend of FDI inflows, which has been declining since 2011.

The GOI benchmarks and tracks countries' progress in four categories: Economic Fundamentals (EF), Ease of Doing Business (EoDB), Regulatory Quality (RQ), and Rule of Law (RoL). Each category measures an aspect of the power of economic and institutional factors to attract FDI [19].

Table 1 presents causes of GOI development based on partial evaluation of categories. As we see, V4 countries reached an overall good rating in categories Economic Fundamentals and Ease of Doing Business. The first category is dominated mainly by Czech Republic. On the contrary, the worst results were reported in category Quality of Regulations in 2009-2012 and in category Rule of Law in 2013 a 2015. A major strength of Hungary is Ease of Doing Business, which reaches values above 7, with exception of year 2010. However, since 2012

Hungary has reported a decline in category Rule of Law, which decreased its attractiveness for foreign investors. Poland currently loses in Economic Fundamentals, but the worst results has been achieving throughout the entire period in Quality of Regulation. The results of the Slovak Republic are very specific, where according to the latest evaluation three out of four monitored areas reported a drop. The most obvious drop is in category Rule of Law, with rating of only 4.1, which is the lowest recorded value among all countries for the entire period.

Table 1 Results of V4 countries in four categories according through GOI

Country	Category	2009	2010	2011	2012	2013	2015
Czech Republic	EF	**7.41**	**6.82**	**7.40**	**6.86**	6.73	**7.00**
	EoDB	6.58	6.63	6.63	6.52	**6.94**	6.52
	RQ	4.60	4.30	5.30	5.20	5.20	5.60
	RoL	5.90	5.70	5.70	5.40	5.00	5.00
Hungary	EF	6.50	6.54	6.64	6.45	6.54	6.77
	EoDB	**7.21**	**6.94**	**7.50**	**7.00**	**7.15**	**7.15**
	RQ	5.50	5.20	5.30	5.40	5.60	5.70
	RoL	5.10	4.80	4.50	4.50	4.40	4.30
Poland	EF	**6.23**	**6.90**	**6.90**	6.18	6.23	5.95
	EoDB	5.79	5.52	5.79	**6.31**	**6.58**	**6.94**
	RQ	5.50	5.00	5.40	5.30	5.60	5.00
	RoL	5.70	5.60	5.60	6.00	6.20	5.80
Slovak Republic	EF	6.82	6.73	5.45	5.59	5.50	5.59
	EoDB	**6.84**	**6.79**	**7.00**	**6.79**	**6.58**	**6.50**
	RQ	5.90	5.80	5.80	5.50	5.60	5.10
	RoL	4.90	4.80	4.60	4.30	4.30	4.10

Note: Data for 2014 not available.
Source: Self-elaboration based on [8]

In summary, according to the GOI the most attractive country for foreign investors is the Czech Republic, whose strength is the macroeconomic environment. On the contrary, the least attractive country is the Slovak Republic, where the main cause is in the area of applicable legal framework in the country.

3.2 Global competitiveness index

The World Economic Forum prepares the Global competitiveness report annually. Ranking of the countries according to the final score (1-7), is prepared based on country's position within 12 pillars. The general competitiveness of country is closely connected with the country's competitiveness in attracting FDI, at which the competitiveness is defined as the set of institutions, policies, and factors that determine the level of productivity of an economy, which in turn sets the level of prosperity that the country can earn [21].

The Fig. 2 proves that overall the most competitive country is the Czech Republic, despite the decline in value of GCI in 2009-2013 and better rating of Poland in 2013. Similar to the evaluation of GOI, the sharpest decline was reported in the Slovak Republic; however we have noticed a slight improvement in competitiveness since 2013.

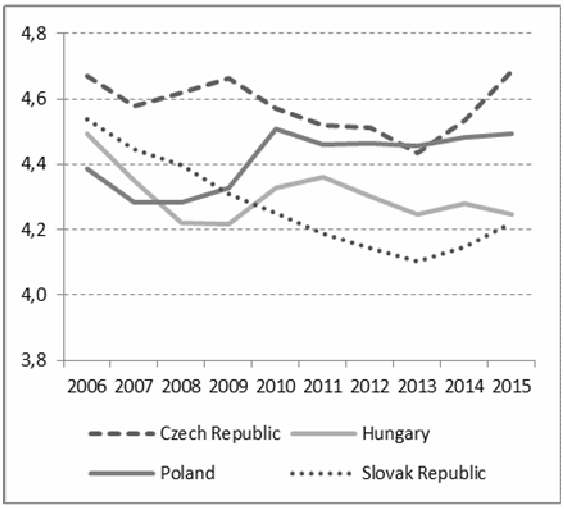


Fig.2 Development of GCI in V4 countries
Source: Self-elaboration based on [22]

As indicated above, the GCI is composed of 12 pillars. V4 countries reported very comparable results in individual pillars and therefore there is no need to analyse the partial evaluation. However in general, there are no significant variations in development of competitiveness of V4 countries, as confirmed by the values of the GCI, which are for all four countries in a range of 4.10 – 4.69 throughout the entire monitored period.

But we will take a closer look on the factors that are decreasing the attractiveness of V4 countries for foreign investors in the form of barriers to business. The barriers to the business are monitored through a questionnaire survey and they are part of the Global competitiveness report. The results are based on respondents' answers to the Executive Opinion Survey. Respondents to the Executive Opinion Survey were asked to select the five most problematic factors for doing business in their country and to rank them between 1 (most problematic) and 5. The presented numbers show the responses weighted according to their rankings [21].

However, comparing the barriers to business in the V4 countries, the diversity is visible. The three biggest barriers are in Table 2 shown in bold. The highest value among all stated (21.8) was reached by the Czech Republic in the area of Inefficient government bureaucracy. The second problem of the Czech Republic is corruption and then political instability. The same three dominant barriers are observed also in in case of Hungary. The problem of the Slovak Republic is also a high level corruption and bureaucracy. Besides these, the attractiveness of the Slovak Republic is also reduced by tax rates. Interesting results can be seen in case of Poland. The biggest barrier is represented by the complexity of tax laws and restrictive labour laws.

Table 2 Top 10 the most problematic factors for doing business in V4 countries

Factor	Czech Republic	Hungary	Poland	Slovak Republic
Access to financing	3.5	6.3	7.8	3.5
Complexity of tax regulations	10.4	9.5	**21.3**	9.5
Corruption	**13.2**	**14.6**	2.3	**18.1**
Inadequate supply of infrastructure	5.2	3.6	5.8	4.6
Inadequately educated workforce	7.1	7.6	5.1	6.6
Inefficient government bureaucracy	**21.8**	**12.2**	11.1	**16.6**
Policy instability	**12.7**	**15.7**	5.1	8.8
Poor work ethic in labor force	5.0	7.3	3.7	3.0
Restrictive labor regulations	7.6	1.9	**14.7**	11.3
Tax rates	5.7	9.8	**12.8**	**11.4**

Source: Self elaboration according to [21]

3.3 Factors decreasing the attractiveness of country for fdi

The attractiveness of the country for foreign investors is determined not only by its macroeconomic stability and economic performance, but also by the stability of political environment and the quality of legal framework [5]. The decision of foreign investors whether to invest in a new market may depend on the access to ownership of lands and buildings at transparent prices. In addition, in many countries, there are certain conditions relating to the composition of the board of directors or the appointment of executives [20]. Taking into consideration the results that we mentioned in the identification of barriers to business in the form of high level of corruption and bureaucracy, or restrictive regulations, we will take a closer look to assessment of V4 countries through indices that apply to these areas. Specifically, it is the FDI Regulatory Restrictiveness Index (FDI RRI) and the Corruption Perceptions Index (CPI).

3.3.1 Fdi regulatory restrictiveness index

FDI RRI was developed by OECD to measure the obstacles that could hamper the inflows of investments between the states or that could obstruct setting up a business abroad. Regulatory restrictions on foreign ownership are the most obvious obstacles to FDI inflows. These restrictions may take the form of company's equity share in the targeted sector, when nonresidents may hold e.g. less than 50% or the foreign ownership might be even prohibited. The FDI RRI consists of four indicators: the limitations of foreign capital, screening and approval mechanisms, restrictions related to employment of foreigners as key personnel and operational restrictions, e.g. limits on the purchase of land, restriction on profits or capital repatriation [7]. The index can take value from 0 to 1. If the country has no impediments to the movement, the index value is 0; on the other side, if the country is closed and prevents the movement of investments, then the index value is 1.

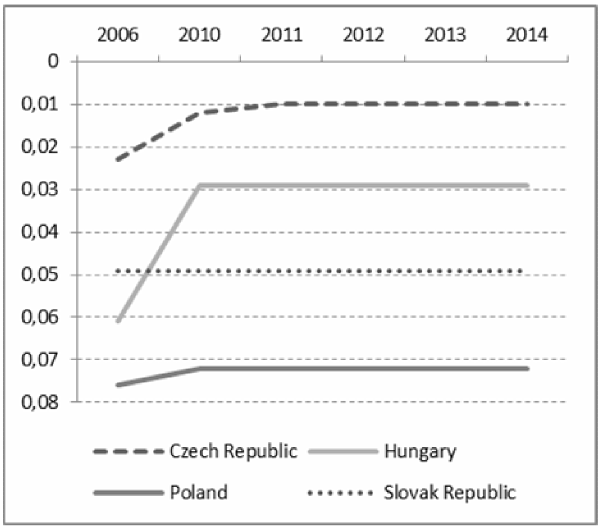


Fig.3 Development of FDI RRI in V4 countries
Source: Self-elaboration according to [12]

The FDI RR Index defines the V4 countries as open economies with minimal obstacles preventing the movement of capital. However, when comparing these countries, the best score was reached again by the Czech Republic, where the index is stable at the value of 0.01 from 2011. The most "regulating" country is Poland. It is mostly the regulation in limiting the foreign capital (0.056 in 2014). Slovakia, as the only V4 country, recorded zero values in three out of four indicators. The "only" barrier is then the limitation of foreign capital in the country (0.049).

3.3.2 Corruption perceptions index

FDI are long term investments and one of the essential aspects that decide on the allocation of these investments is the existence of corruption in a future host country. The corruption sending confusing signals to the investors and affects the volume and structure of capital inflows and may cause a redirecting of FDI somewhere else. The CPI was created to monitor corruption of selected countries. The CPI was established in 1995 as an indicator used to measure perceptions of corruption in the public sector in different countries around the world. It is a composite index, a combination of surveys and assessments of corruption, collected by a variety of reputable institutions. The CPI is the most widely used indicator of corruption worldwide [17].

The index varies from 0 to 100, with 100 being the best and state of the art.

As the results show, the corruption is a problem of all four countries. The most interesting development is in case of Poland, which moved within the monitored period from the worst position (37 in 2006) to the best position (62 in 2015). The least dynamic development was in Hungary. The biggest decline in evaluation is in case of the Slovak Republic. In 2011 Slovakia reported a problem with the high level of corruption and CPI reached a value of 40.

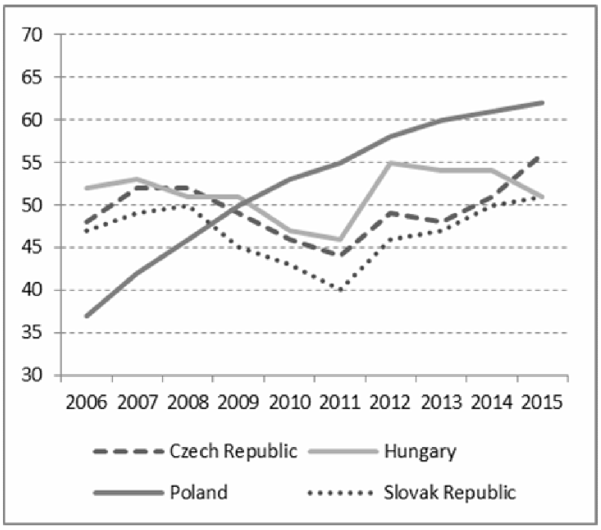


Fig.4 Development of CPI in V4 countries
Source: Self-elaboration based on [17]

4 COMPARISON

We evaluated the attractiveness of the Visegrad Group countries, as host countries for FDI, using four indices – Global Opportunity Index, Global Competiveness Index, FDI Regulatory Restrictiveness Index and Corruption Perception Index. These indices use different scales for evaluation and therefore, to be able to compare achieved results, we normalised the values of individual composite indicators through a method of ranking, which is the simplest normalisation technique. This method is not affected by outliers and allows the performance of countries to be followed over time in terms of relative positions (rankings) [8]. The normalised values of indices are presented through the quadrangle. The largest area of the quadrilateral represents the best rating. Figure 5 presents the comparison of indices' results for the V4 countries in 2010, 2012 a 2015.

The attractiveness of the V4 countries has changed. The highest attractiveness for FDI over the monitored period has been reached by the Czech Republic, whose assessment is still improving. The only weakness remains the question of corruption. Interesting developments can be observed in case of Poland, which achieved the best rating in 2012. According to the Global Opportunity Index, Poland has currently reported a decline, resulting from decreased quality of regulatory framework. However, during the reporting period this country shows the least corrupt environment. The main factors of Hungary's attractiveness are ease of doing business and low regulatory restrictions on foreign capital. On the other side, the growth of corruption, political instability and complexity of bureaucratic procedures are its weakness.

The biggest drop in attractiveness was reported in Slovakia. While in 2010 was Slovakia according to the GOI a leader among the V4 countries, today it reaches the weakest rating. The cause can be found in the low legal protection of investors and property rights, limitation of foreign capital and in corruption.

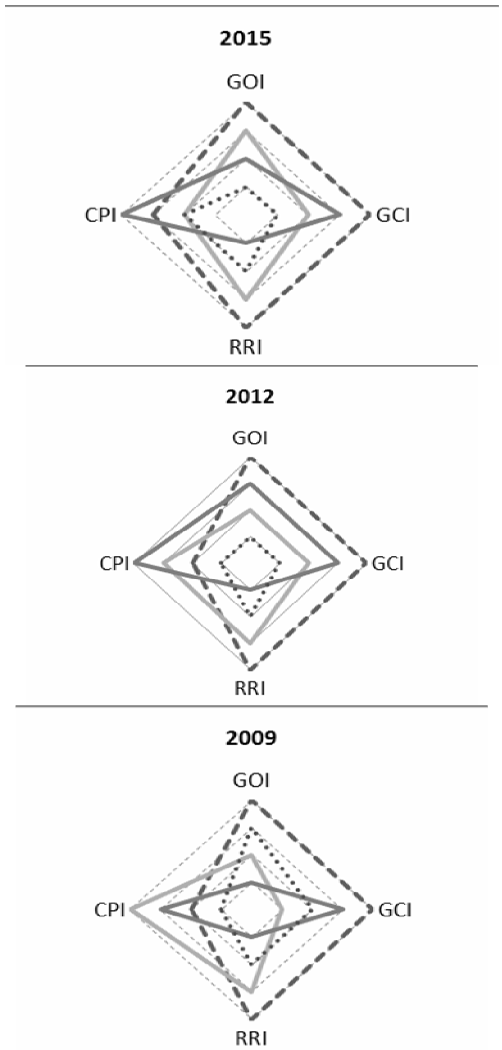


Fig.5 Comparison of results 2015, 2012, 2010
Source: Self-elaboration

CONCLUSION

The attractiveness of country represents a potential of effective use of capital, depending on conditions provided by a host country for investors. A file concerning the information on potential host countries must contain a relatively large number of different data and characteristics from various areas, but the importance of each of them is ultimately decided on by investors themselves. The same applies to suitability and usability of index, which could affect the location of investment.

Among the countries of the Visegrad Group, the highest attractiveness for foreign investors is reported by the Czech Republic, whose strength is the macroeconomic environment and weakness is represented mainly by bureaucratic delays. In contrary, the least attractive country seems to be the Slovak Republic and the cause can be found in the area of applicable legal framework in the country and the high level of corruption, which is a problem also in other V4 countries. This issue has been handled the best way by Poland, however a problem for foreign capital entry can be in Poland explained through the complexity of tax laws, restricting labour laws and limitation of foreign capital.

To conclude this topic we can summarize that in global the V4 countries represent open economies that are attractive to potential foreign investors.

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