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THE HOST COUTRY ATTRACTIVENESS FROM PERSPECTIVE OF SELECTED FDI INDICES

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Abstract: *The expansion of business to foreign markets can provide countless opportunities for growth. The attractiveness of a country for foreign investors depends on a whole set of factors. The information about the macroeconomic performance of the country, the stability of the political environment and the quality of the legal framework, favourable business environment and available human capital are very important when making a decision about the location of foreign direct investment. This aim of the paper is to describe the external determinants of the host country as factors of the country attractiveness for foreign direct investment and on the base of selected FDI indices identify the most attractive European countries for foreign investors.*

Keywords: Attractiveness; foreign direct investment;, determinant; host country; indices.

1 INTRODUCTION

The actual business activities have more international character than ever. With the penetration of globalization in field of business and entrepreneurship, enterprises respond to saturation of domestic markets and seek success in new foreign markets.

The process of foreign market entry to the international market is not a single-shot act, but a set of related and interlinked activities and activities of firms. Ultimately, these decisions have crucial for the further development of the company. Companies choose the form appropriate to their level of resources, market potential, and experience operating in the international sphere. The various categories of foreign market entry include export/import of goods and services, licensing and franchising agreements and capital investment in a foreign market through FDI. If the company has already decided that for its next activity will be profitable to invest abroad through direct investment, the potential investor has to carefully consider the choice of country. The result of this phase of the decision-making process should be the selection of such a country that will bring to the investor the best results with respect to the target which is usually the maximum profit achieved through penetration into the new markets.

2 FACTORS OF THE HOST COUNTRY ATTRACTIVENESS

The most cited taxonomy of FDI motives is the Ownership, Location, and Internalization (OLI) paradigm was developed by J.H. Dunnning. This framework describes the behaviour of firms investing abroad for three reasons.

The specific ownership advantages (O) of companies that the firm has in comparison to other are for example ownership of the tangible assets, patents and designs, or organizational efficiencies. The Location advantages (L) making the country attractive for the firm can be low cost labour, low cost raw material or government incentives to FDI. As for the advantages of internationalization (I), these are representing the internal factors motivating firms to invest abroad, such as reducing of transaction cost, control over operations and avoidance of tariff`s and other barriers [6]. The objects of our focus are location advantages.

Economic theory and empirical studies agree that the movement of FDI is controlled by anticipation of future profits. Determinants influencing investors' decisions can be divided into two basic groups - internal and external determinants [3], [8].

Internal determinants are based on internal conditions and resources of the enterprise, such as a manager's decision, the utilization of workers who have experience in the international environment, significant events that may lead to investment abroad (decrease in sales in the domestic market).External determinants appear from the environment in which company operates and presenting determinants in the home country (high cost of labour, shortage of raw materials) and determinants in the host country (growing market and demand, an attractive investment climate). Just determinants in the host country as factors of host country attractiveness for FDI inflows are the object of our paper.

In terms of substantive content of external determinants we distinguish cost and demand factors and investment environment. Cost factors increase profit by reducing costs of production and distribution, demand factors affect the amount of profitably by increasing/decreasing in sales, and investment environment is formed by the legal norms, restrictions and political relations in the host country, affecting decisions about the allocation.

In analysing of location factors, is needed to observe the host country determinants from a more comprehensive perspective. It is important to appreciate the political and economic risk on entry to the host country, to explore the competitive environment, the possibility of risk diversification, the effectiveness of new markets and the possibilities of penetration on the regional market through the national market of the host country.

For American studies addressing theme of investment determinants is typical emphases on motive of higher profit and the associated searching of countries with comparative advantages, while European studies highlight the market factors, political stability or avoidance of trade barriers [16]. Several studies [21], [13], [5] support the importance of economic growth and income of certain country for attracting FDI. According Hošoff and Hvozdíková [11] the attractiveness of the host country for FDI inflow depends on several factors, which include economic development of the country, respectively development of overall macroeconomic stability, stable legal and political environment, favourable business environment, quality of institutional framework and quality human capital, which the host country disposes. Walsh and Yu [21] and also Addison and Heshmati [2] found that openness has significant positive impact on attracting FDI. Torrisi et al. [20] qualified that market size is an essential factor for attracting the FDI, especially for transition countries of Central Europe such as Hungary, Poland, Czech Republic and Slovakia. Also, the business cycle has impact on the host country attractiveness, whereas the expansion is associated with an increase in FDI and the recession with a decrease [9]. Bénassy-Quéré, Coupet and Mayer [4] found that the complexity of bureaucratic procedures is an important factor in the attractiveness of the host country for FDI inflows, as well as the tendency to corruption reduce the inflow of FDI. This conclusion is confirmed by Wei [22], who emphasized that corruption affects the volume and composition of capital inflows, thereby is greatly reducing the inflow of FDI. Several studies [19], [15], [10] qualified the wages (labour cost) as significant determinants.

There are several studies and surveys that more closely address to the issue of the country attractiveness for FDI. A.T. Kearney is one of the largest and most important strategic consulting firms in the world. In its survey looked for the answer to the question *"What are the most important factors to your company when choosing where to make foreign investments?"*. The result can see in Table 1.

In identifying markets for FDI, investors prioritize market size (25%), followed by a variety of regulatory factors (B, C, G, K, N) affecting the ease of doing business and the overall security environment (D). Also, question of labour in the form of cost (E) and quality of human resources (H) belongs to the most significant determinants. Consequently, investors mark financial and legal environment of host country (F, I, J). In addition to referred motives, survey confirmed the importance of quality of infrastructure (L, O, P) and availability of inputs (M, R).

Table 1. Factors of host country`s attractiveness I. (% of respondents)

A - Domestic market size	25%
B - Transparency of government regulations and lack of corruption	22%
C - Tax rates and ease of tax payment	22´%
D - General security environment	21%
E - Cost of labour	20%
F - Efficiency of legal and regulatory processes	20%
G - Government incentives for investors	18%
H - Talent and skill level of labour pool	17%
I - Ease of moving capital into and out of country	17%
J - Availability of financial capital in domestic market	15%
K - Strength of investor and property rights	15%
L - Quality of transportation infrastructure	11%
M - Availability of raw materials and other inputs	11%
N - Country's participation in regional and bilateral trade agreements	11%
O - Quality of telecommunications infrastructure	10%
P - Quality of electricity infrastructure	8%
R - Availability of land and real estate	8%

Source: Own processing according to [1]

Table 2 presents the answers of similar question (*"What do investors want?"*) asked within EY's 2015 European attractiveness survey. Company Ernst & Young, global leader in assurance, tax, transaction and advisory services, realizes this survey every year since 2002.

Table 2. Factors of host country`s attractiveness II. (% of respondents)

Stability and transparency of political, legal and regulatory environment	46%
The country's or region's domestic market	37%
Transport and logistics infrastructure	30%
Potential productivity increase for their company	29%
Labour costs	24%
Local labour skill level	22%

Source: Own processing according to [7].

In a sample of 808 respondents (international decision-makers), almost half (46%) consider political, legal and regulatory environment as most important factor of host country`s attractiveness. Consequently, among the six significant determinants qualify domestic market, infrastructure and labour market conditions.

3 FDI INDICES

FDI Indices are also based on above factors attractiveness. Most of them are composite indices. The attractiveness of the selected European countries (included in the evaluated sample of countries) is evaluated by three different indices - FDI Regulatory Restrictiveness Index (FDI RR Index), FDI Confidence

Index and FDI Value Indicator. The aim is to identify the most attractive European countries and compare the results of these indices.

3.1 FDI REGULATORY RESTRICTIVENESS INDEX

FDI Regulatory Restrictiveness Index was developed by OECD to measure the obstacles that could restrict the investment flows between countries, respectively setting up businesses abroad. Regulatory restrictions on foreign ownership are the most obvious obstacles to FDI inflows. They may take the form of limits on the company share equity in the target sector, where non-residents may dispose, for example, of less than 50% or it may even be prohibited foreign ownership.

The FDI RR Index retains its focus on four types of measures: equity restrictions, screening and approval requirements, restrictions on foreign key personnel, and other operational restrictions, such as limits on purchase of land or on repatriation of profits and capital [14].

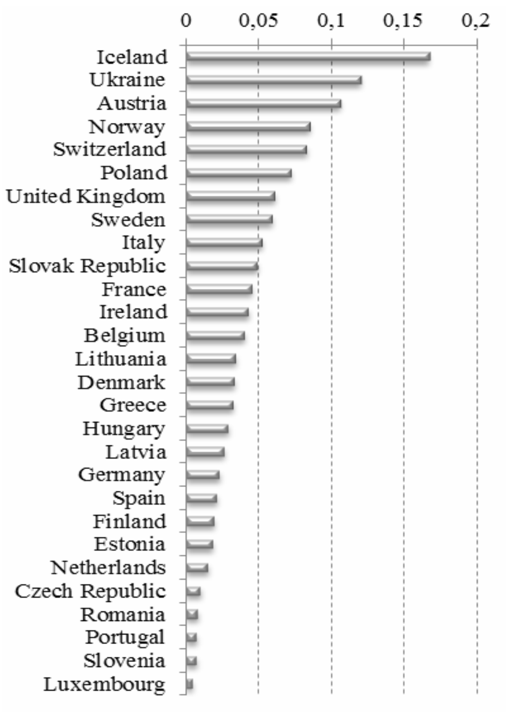

Fig. 1 FDI RR Index 2014
Source: Own processing according to [17]

The index can take a value from 0 to 1. In case that in the country is no obstacles to the movement of investment, it gets the value 0; conversely, if the country is closed and prevents the movement of investment, so the index is 1.

As we see, European countries are according to FDI RR Index open economies. The best rating reached Luxembourg, Slovenia and Portugal. Conversely, Iceland with the value of FDI RR Index 0,167 is the closest European country.

3.2 FDI CONFIDENCE INDEX

Since 1998, company A.T. Kearney it prepares FDI Confidence Index, which assesses the impact of political, economic and regulatory changes on the FDI intentions and the preferences of top managers of leading companies worldwide.

The 2015 A.T. Kearney FDI Confidence Index is constructed using primary data from a proprietary survey administered to senior executives of the world's leading corporations. The participating companies represent 27 countries and span all sectors. The Index is calculated as a weighted average of the number of high, medium, and low responses to questions of direct investment in a market over the next three years.

Higher Index values indicate more attractive investment targets. The sample of countries included in the survey accounts for approximately 90% of FDI inflows [1].Values are calculated on a 0 to 3 scale. Higher value means higher confidence.

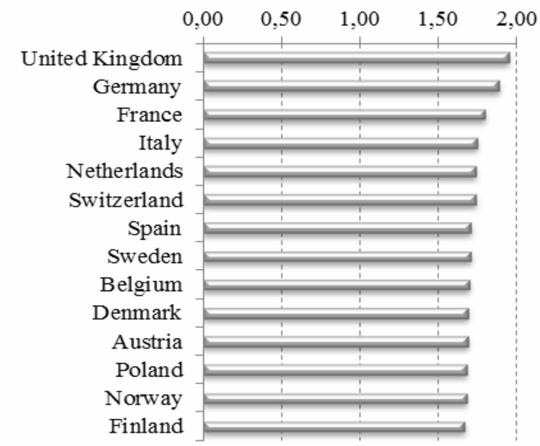

Fig. 2 European Countries in top 25 according to FDI Confidence Index 2014.
Source: Own processing according to [1].

According to the FDI Confidence Index United Kingdom, Germany and France belong to the most attractive countries in Europe. Conversely, the evaluation of Finland, Norway and Poland is low.

3.3 FDI VALUE INDICATOR

IBM-Plant Location International (IBM-PLI) is a division of IBM Global Business Services that specializes in corporate location and economic development strategies. It provides location strategy and site selection services to corporate clients, analysing international business locations for expanding or consolidating companies to help them select the optimal location. In study Global Location Trends is evaluated the success of countries in attracting FDI with regard to the type of investment projects.

IBM-PLI has developed FDI Value Indicator that assesses the added value and knowledge intensity of the jobs created by an investment project [12].

Fig. 3 FDI Value Indicator 2014

Source: Own processing according to [12]

Many countries are primarily interested in attracting higher-value investment projects which create high-paying and knowledge-intensive jobs. For the fourth year in a row, Ireland is the top ranking country in the world on this measure. It continues to attract investment projects in industries characterized by high knowledge intensity and economic value added, such as life sciences and information and communication technology. Most attractive countries are primarily mature economies with a mix of investments similar to Ireland's. The ranking confirms that mature economies attract investment with high added value.

3.4 COMPARISON OF FDI INDICES RESULTS

Above mentioned indices bring diverse views on the host country attractiveness for FDI inflows and use various methods. In view of these two facts can be expected differences in results.

Table 3 shows the considerable differences in evaluation of host country attractiveness. Actually, different approaches of used indices to the question of location factors for FDI have meant that among the top 5 countries was no consensus. This creates an area for the investors themselves and their own preferences. Important role plays the type of FDI which the company wants to realize.

Table 3. Top 5attractive countries according to FDI Indices

FDI RR Index	*FDI Confidence Index*	*FDI Value Indicator*
Luxembourg	United Kingdom	Ireland
Slovenia	Germany	Switzerland
Portugal	France	Sweden
Romania	Italy	Denmark
Czech Republic	Netherlands	Lithuania

Source: Own processing.

In case of Greenfield investment, the investor may use FDI RR Index, which informs him inter alia about equity restrictions or limits on purchase of land. If investor has risk aversion, FDI Confidence Index, which assesses the impact of political, economic and regulatory changes, may be helpful in decision-making process. FDI Value Indicator inform about countries attracting sophisticated investments, thus investments with higher added value. In conclusion, despite of significant differences among results of FDI Indices, each one offers relevant information about potential host countries for the investors.

4 CONCLUSION

Foreign direct investments are globally considered one of the most important catalysts of economic development. The countries seeking after this kind of capital are trying to create favourable economic, legal and business conditions for potential investors. This fact results in the issue of which factors increase the attractiveness of host countries and leading the investors to locating long-term investment in the host country. Foreign investors mean to the 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 in the region [18]. The question of determinants of the host country attractiveness is the object of various studies and surveys of domestic and foreign authors. Among the most important location factors can include market size, political, legal and regulatory environment, labour market conditions and cost factors.

On the basis of the three FDI indices, we analysed the attractiveness of European countries. The results were completely different. While according to FDI Regulatory Restrictiveness Index the most attractive countries are Luxembourg, Slovenia and Portugal, FDI Confidence Index identified United Kingdom, Germany and France. Ireland, Switzerland and Sweden are the most attractive European countries based on FDI Value Indicator. Therefore, investor's expectations and preferences in ultimately play key role. The factors like risk aversion, the FDI intensity on inputs, FDI type and economic sector where investment leading, are crucial.

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