Panel 6 - Investment opportunities in the new EU member countries

<u>Summary report:</u>
Written and presented by Gabriel SIPOS, Analyst, INEKO

The panel 6 participants came mostly from the significant group on the receiving end of the reforms discussed at this conference – foreign investors. The panelists looked at the factors determining an attractiveness of a given country to foreign direct investment (FDI). FDI to central and eastern Europe boomed during the last few years. What caused these inflows?

The panel speakers highlighted two sets of factors – inherited endowment and fiscal policies. The advantageous endowment consisted of well-educated, skilled and abundant labour force that proved to be relatively productive yet inexpensive in comparison with the western European workers. Location is also seen as a positive factor, especially to firms looking at expanding further east, to Russia.

But none of these positive endowments would be enough to attract FDI, should the governments keep its fiscal policies in disorder. Fiscal stabilization came in many forms. Ms Ovesny-Straka of Slovenska Sporitelna, the largest bank in Slovakia, mentioned the pioneering role of the bank privatization in the overall fiscal stabilization efforts of the accession countries' governments. Within a decade of reforms, most of the local banks were taken over by foreign owners, which led to the introduction of sound banking policies and limited the scope for fiscal deterioration. Slovakia's new flat income tax system, including zero tax on dividends, has added to both fiscal stability as well as FDI attractiveness of the country, added Mr Ovesny-Straka.

Professor Steinherr of the European Investment Bank stressed the committment of accession country governments to join EU as an important factor in their attraction to FDI. While the European Union is often seen as lacking in reforms in comparison to the U.S., for instance, it has improved its business environment in the past few years, said Prof. Steinherr. The prospects of standards and stability of the early EU memberships has increased the attraction of the accession countries to investors.

FDI-friendly policies themselves have worked for the benefit of the former communist countries, said Mr Bauder of Volkswagen, recounting VW's successful experience in Slovakia. Due to its openness and flexibility, Slovakia has now attracted two other world-class automakers, Peugeot Citroen and Hyundai/Kia.

While the focus on automotive sector could serve Slovakia well, Professor Kennedy of Michigan Business School warned the local governments not to forget the contribution of service sector FDI. Services make the growing part of the world economy and their transfer to emerging countries is supported by technology and continuing liberalization of the world trade.

To improve the accession countries' competitivness, panelists recommended to focus on improving and reforming its education system with the focus on foreign languages and technology literacy. Small-business regulations should be simplified further. Overall, while gaps remain, the accession countries, not least Slovakia, have made their economies a rather attractive place to invest, proving that the reforms efforts are bearing fruit.