

PRESS RELEASE

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wiiw FDI Report Central, East and Southeast Europe: Growth Engine Stutters

Strong growth in FDI inflows was observed in the New EU Member States (+35%) in 2012, despite sluggish economic growth or even contraction of GDP in several countries. In fact, the exceptionally high FDI inflows to the Czech Republic and Hungary were mainly the result of capital in transit and other financial flows not resulting in fixed investments. By contrast, a decline of 22% was reported in the Southeast European countries including Turkey, while inflows to the CIS remained flat (+1%) and strongly biased upwards by round-tripping Russian capital. For 2013 experts from the Vienna Institute for International Economic Studies (wiiw) expect a severe decline in FDI inflows. FDI, which used to be one of the driving forces of economic development and structural change in the CESEE economies, does no longer play the role of a growth engine. It is mainly demand driven and cannot escape being dragged down by the recession in Europe. These are the main results of the new *wiiw FDI Report* covering 22 countries in Central, East and Southeast Europe (CESEE). The *wiiw FDI Database* – a new service of wiiw – will go online in July.

The renewed decline of global FDI flows in 2012 impacted also on the CESEE countries. Due to diminishing outward FDI activities, economic contraction and declining imports of the euro area, the external conditions for FDI in the CESEE countries were unfavourable; export-oriented projects suffered from low external demand. This came on top of sluggish domestic demand that has put a brake on the development of host market-oriented FDI firms. FDI inflow to the NMS was reported to expand, nevertheless (Table 1).

The exceptionally high inflows to the Czech Republic and Hungary stand in contrast to the declining GDP in these countries. An explanation may lie with the method of statistical reporting. Financial flows reported as FDI are not necessarily related to fixed investments and may include round-tripping of domestic capital, capital in transit from one subsidiary to another and other tax-optimising flows.

A more realistic picture of the current stage of FDI in CESEE is obtained by the number of greenfield projects, which declined by 17% in 2012; the estimated investment value in these projects fell by 32% to an all-time low, with the Czech Republic and Hungary being no exceptions. Fewer new projects were registered in advanced services and in manufacturing, which have been the driving forces of relocations in recent years.

The financial sector and other business services including holding companies have the highest shares in the FDI stock next to manufacturing in most CESEE countries. On the side of the investors, holdings are most often based in the Netherlands, making this country the most important home country for the region. Austria is the third largest investor in the new EU members and second

in Southeast Europe by FDI stock. The country ranks only fifth in terms of the number of greenfield projects in the CESEE in 2012.

Profits of foreign direct investors in CESEE stagnated in 2012. The rate of profit once again climbed above 10% of FDI stocks in the Czech Republic, Estonia and Russia, but fell below 8% in Hungary, Lithuania, Poland and Slovakia. Meagre profits were recorded in Bulgaria, Romania, Slovenia and several SEE countries where a significant part of the investments made losses. About 60-80% of foreign investors' income was repatriated from the host country. Nevertheless, a positive contribution of FDI to the balance of payments could be maintained in some NMS due to the trade surplus achieved by foreign subsidiaries.

wiiw experts expect a decline of 22% in FDI inflows in 2013 as a result of the sluggish growth throughout Europe. This expectation is supported by plummeting first-quarter FDI flows and the falling number of greenfield projects compared with the previous year. Among others, Russian investments are bound to decline due to worsening economic conditions at home and possible losses related to Cyprus. Exceptions to the bleak FDI forecast may be countries with privatisation-related inflows such as Slovenia or those where greenfield investors see new chances such as Serbia.

FDI, which used to be one of the driving forces of economic development and structural change in the CESEE economies, does no longer play the role of a growth engine these days. It is mainly demand driven and cannot escape being dragged down by the recession in Europe.

wiiw FDI Report Central, East and Southeast Europe: Growth Engine Stutters
by Gábor Hunya (concept and analysis) and Monika Schwarzhappel (database and layout)
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Available in hard copy (EUR 70) or PDF (EUR 65) from wiiw's website, www.wiiw.ac.at.
Orders can also be sent by fax to +431 533 66 10-50 or by e-mail to koehrl@wiiw.ac.at.
New online FDI Database as of July 2013.

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Table 1

Foreign Direct Investment in 2012 and forecast 2013

	Inflow change		FDI net	Inflow	Inward stock	Forecast inflow 2013
	EUR mn	in %	EUR mn	per capita, EUR		EUR mn
Bulgaria	1478	12,5	1302	202	5191	1500
Czech Republic	8248	394,4	7204	785	9834	2800
Estonia	1144	518,6	455	887	11057	1000
Hungary	10462	179,8	2252	1055	7918	2000
Latvia	768	-26,5	621	378	4921	800
Lithuania	650	-37,6	337	217	3999	700
Poland	7267	-40,3	3308	188	4339	8000
Romania	1746	-3,8	1714	92	2963	1800
Slovakia	2199	42,7	2257	407	7762	1000
Slovenia	113	-84,3	186	55	5718	700
New Member States-10	34075	35,0	19635	344	5387	20300
Albania	745	-0,1	727	264	1313	800
Bosnia and Herzegovina	493	69,9	464	128	1561	500
Croatia	973	-9,9	1051	228	5615	800
Macedonia	105	-68,9	111	51	1819	200
Montenegro	474	18,2	454	764	6441	400
Serbia	274	-85,9	232	38	2517	700
Turkey	9668	-16,1	6488	132	1898	9000
Southeast Europe	12732	-22,0	9526	136	2113	12400
Belarus	1120	-59,8	1043	118	1152	1000
Kazakhstan	10909	9,2	9678	650	4763	11000
Moldova	124	-38,6	109	35	707	200
Russia	39997	1,1	278	279	2651	32000
Ukraine	6094	17,7	5156	134	1212	5000
Selected CIS	58244	0,9	16264	266	2418	49200
Total region	105051	5,8	45425	255	3064	81900

Remark: wiiw forecast excluding capital in transit.

Sources: wiiw Databases incorporating national and Eurostat statistics.