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## Regional Effects of Foreign Direct Investments in Hungary

Literature has been searching the secret of the economic success of some regions. It can be better performance, higher productivity, the given region's specialisation in fast growing industries or other factors. Foreign investors can reduce the regional disparities of an economy. They may increase the competition in the certain industry and the less competitive companies are ousted from the market. On the other hand they introduce an activity that is characterised by a new modern and serious potential. (Markusen Vanables, 1999.) They may create a demand for related industrial sectors. Companies working in these industries can join even the international transporting networks.

Examining the progress of the regions it can be observed that 'growth poles' are developing. Growth pole means spectacular growth of a geographically determined region. Usually, in this region many plants belonging to joining industrial sectors can be found. In the growth pole the flow of information and knowledge become faster and faster since because of the concentration. The companies are much more flexible, efficient and innovative than their competitors that spread over the country. (Porte, 1998. Baptista, 1996. Garcia-Milá-McGuire, 1993.) Moreover, in the case of other new companies the risk is much lower since the infrastructure is better built and they work with skilled workers, the information is more easily accessible.

### Investment – stimulation in Hungary

The tendency can be more and more felt that the competition for investments is getting stronger between the countries, which encourages the states to establish more complex and target group oriented investment – stimulation systems.

Lately, Hungary has taken determined steps to attract the investors. A complex investment – stimulation system has been established, that includes the possibilities of investment into areas in more disadvantageous situation. The experience shows that these aims were realised to merely a small degree. The dominance of the central region has grown further. A lot of changes will occur after Hungary joins the EU. It will tighten the investment allowances without any discrimination, which is available for the whole country. They intend to reduce the administrative burdens of enterprises too. Some means of the investment- stimulation are determined in the scope of the Széchenyi Plain. This program considers the Central European regional company centres (logistical, informatical , service etc.) important. The settlement of these companies has positive effects on the economies. On the other hand, the research development investment belonging to the high technology should be supported, as they become initiators of the economic development.

In Hungary the tax allowances, the advantageous regulation of bonded warehouse, infrastructure development and the programs advancing the reinforcement of the transport networks are among the indirect means. Joining the EU will bring a significant change in this area. Hungary has to adopt the EU regulation referring to the tax benefits.

The new system has to be sector neutral transparent and easily understandable. [4] The tax benefits are less typical in the EU. The degree of the income tax that is advantageous in terms of capital investment probably should be changed in the period after the joining. The stimulation system may

be transferred to the level of regions. The cause of this may be that the level of self-governing is less regulated in the EU. The local possibilities and demands are better known by the self-governments.

## World market tendencies

The countries of Central–East–Europe are present to a modest degree in the field of FDI inflow. Although in value relatively significant capital inflow growth happened, but this growth pace did not reach the world market growth.

World became bipolar in terms of working capital export. The USA and the EU are the most significant capital importers; also in terms of working capital import the dominant role of the two powers can be observed.

**Table 1.** Distribution of Foreign Direct Investment in the World (in % of the world total)

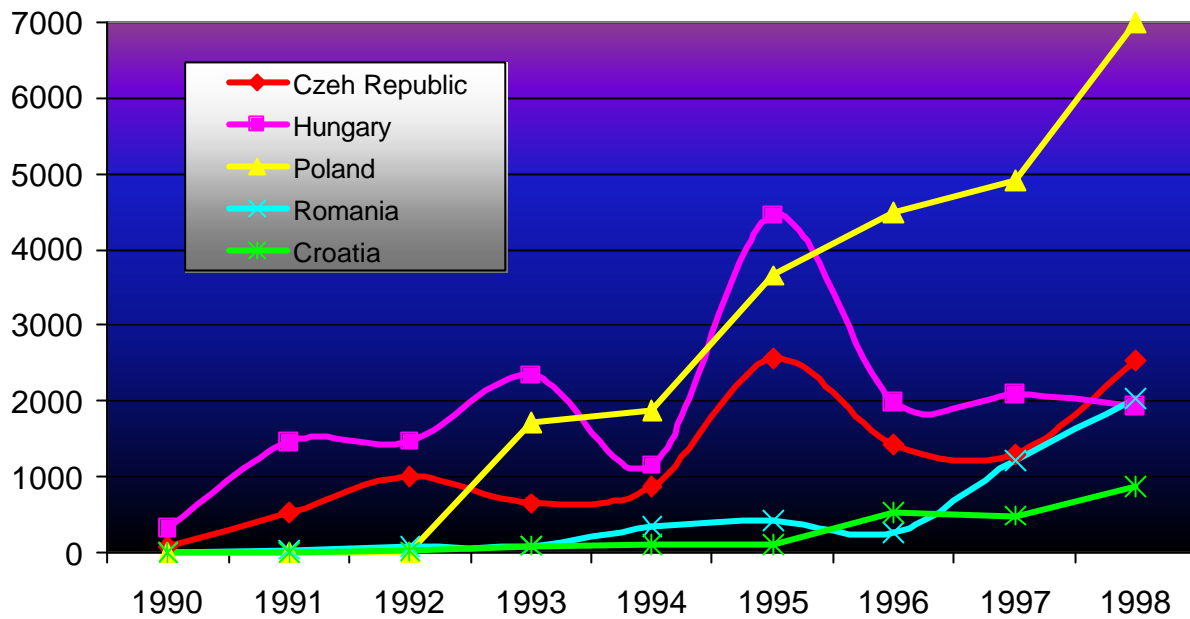
	Import				Export			
	1995	1996	1997	1998	1995	1996	1997	1998
<b>Developed countries</b>	63,4	58,8	58,9	71,5	85,3	84,2	85,6	91,6
<b>Western Europe</b>	37,0	32,1	29,1	36,9	48,9	56,7	50,6	62,6
<b>EU</b>	35,1	30,4	27,2	35,7	44,7	47,9	46,0	59,5
<b>Other Western Europe</b>	1,8	1,8	1,9	1,2	4,2	5,8	4,6	3,1
<b>USA</b>	17,9	21,3	23,5	30,0	25,7	19,7	23,1	20,5
<b>Japan</b>	-	0,1	0,7	0,5	6,3	6,2	5,5	3,7
<b>Other Developed</b>	8,5	5,3	5,6	4,1	4,4	4,6	6,4	4,9
<b>Developing</b>	32,3	37,7	37,2	25,8	14,5	15,5	13,7	8,1
<b>CEE</b>	4,3	3,5	4,0	2,7	0,1	0,3	0,7	0,3

*Source: World Investment Report 1999. Page 20*

## General survey in Central-East-Europe

The most working capital flowed in Hungary in 1995, which was due to mainly the privatisation incomes (especially in the field of electric power-, gas-, heat-, water-supply). 1996 onwards the inflow has become stable on about two billion dollars. FDI stock per capita in Hungary is still the biggest, though its advantage is continuously decreasing.

**Figure 1.** Working Capital Import in Some Central-East European Countries – in million USD

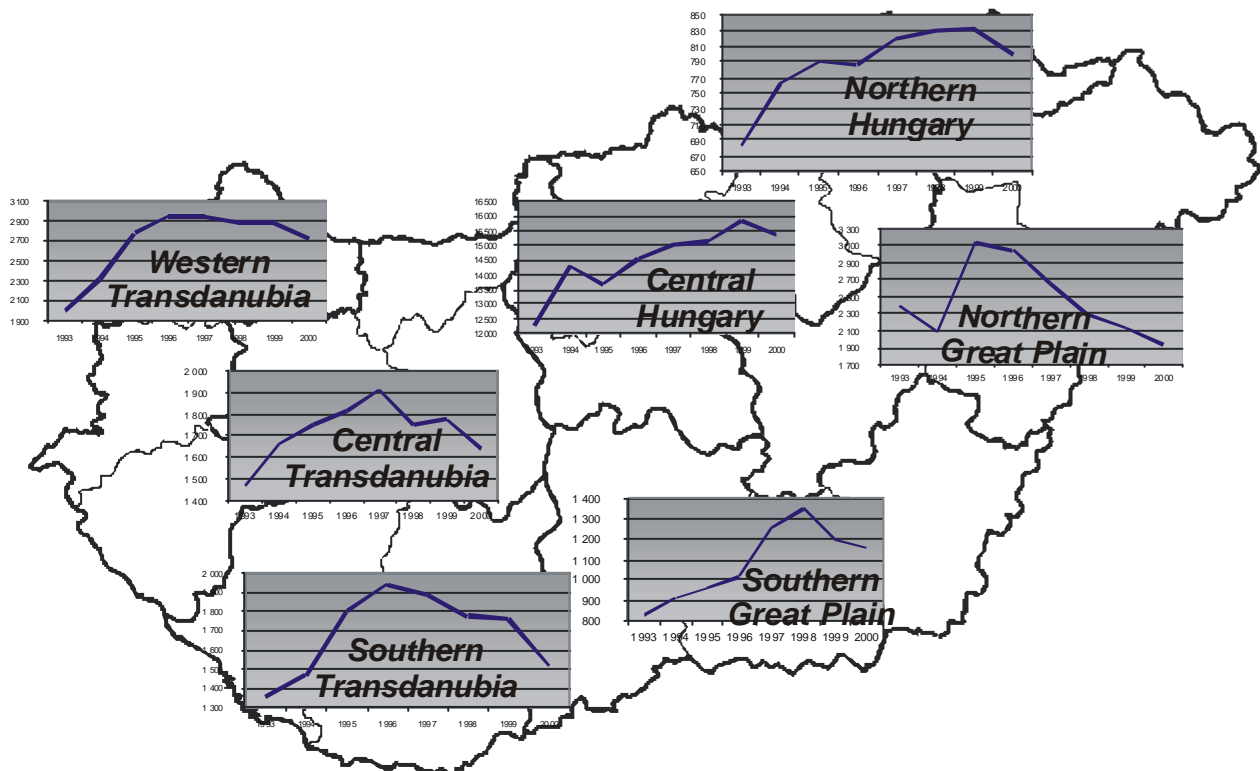


Source: World Investment Report, 1999 - personal editing

In terms of the volume of working capital import Poland, Hungary and the Czech Republic are the most successful states of the region. In the last few years positive tendencies can be observed in Croatia and Romania.

### General survey in Hungary

**Figure 2.** Trend of the Number of Foreign Enterprises 1993 - 2000



Source: Hungarian Central Statistical Office, personal editing

In 1990, 81,4% of the companies with foreign interest were in domestic majority property. By 1998, 84,3% of the enterprises with foreign interest got at least in 50% to foreign property. It seems that the foreign capital strives for mainly a full-scale possession.

**Table 2.** Trend of the Number and Proportion of Employees (1998)

Sectors of the economy	Proportion of employees in the sectors compared to all the employees (%)	The employees' proportion in certain sector in companies with foreign interest (%)	The employees' proportion in all FDI related companies (%)
<b>Agriculture, animal management, fishing</b>	7,6	3,9	1,1
<b>Mining</b>	0,5	30,0	0,5
<b>Processing industry</b>	37,0	44,87	61,4
<i>Foods, beverage, tobacco</i>	6,5	41,3	9,8
<i>Textile goods, clothes, leather products</i>	6,5	36,9	8,9
<i>Wood-, paper- and printing industry</i>	2,9	27,5	3,0
<i>The chemical industry</i>	4,1	65,6	10,0
<i>Non-metal mineral products</i>	1,6	50,5	3,0
<i>Metallurgy, metal-processing</i>	3,8	32,3	4,6
<i>Engineering industry</i>	10,3	55,0	21,0
<i>Other processing industry</i>	1,3	26,0	1,3
<b>Electric power-, gas-, heat- and water-supply</b>	3,9	37,6	5,8
<b>The building Construction industry</b>	6,6	10,3	2,5
<b>Trade, repairing of vehicles and consumer goods</b>	17,7	21,8	14,1
<b>Hotel, hospitality</b>	2,9	23,7	2,6
<b>Transport, post, telecommunications</b>	10,8	12,8	5,1
<b>Real estate</b>	9,5	15,6	5,6
<b>Education</b>	0,3	5,8	0,1
<b>Public health, social supply</b>	0,9	7,4	0,3
<b>Other services</b>	2,3	10,4	0,9
<b>Altogether</b>	100		100

*Source: Hungarian Central Statistical Office 2000, personal editing*

The presence of foreign companies are significant, especially in the field of processing industry, trade, electric power-, gas-, heat-, and water supply. 61,4% of the employees of all the foreign related companies are employed by the processing industry. It can be explained on the one hand by inflows capital into the processing industry, on the other hand by the fact that the processing industry needs more workers. Inside the sector those workers' proportion, who are employed by foreigners, is the highest in the field of food-, chemical-, non-metal-, mineral product-, engineering industry.

In agriculture the proportion of the workers employed by companies with foreign interest is relatively low, due to the fact that foreigners are restricted to come by land. The potential large investment possibilities are diminishing that's why the proportion of workers employed by companies with foreign interest may not grow significantly any more.

## Regional distribution of investment

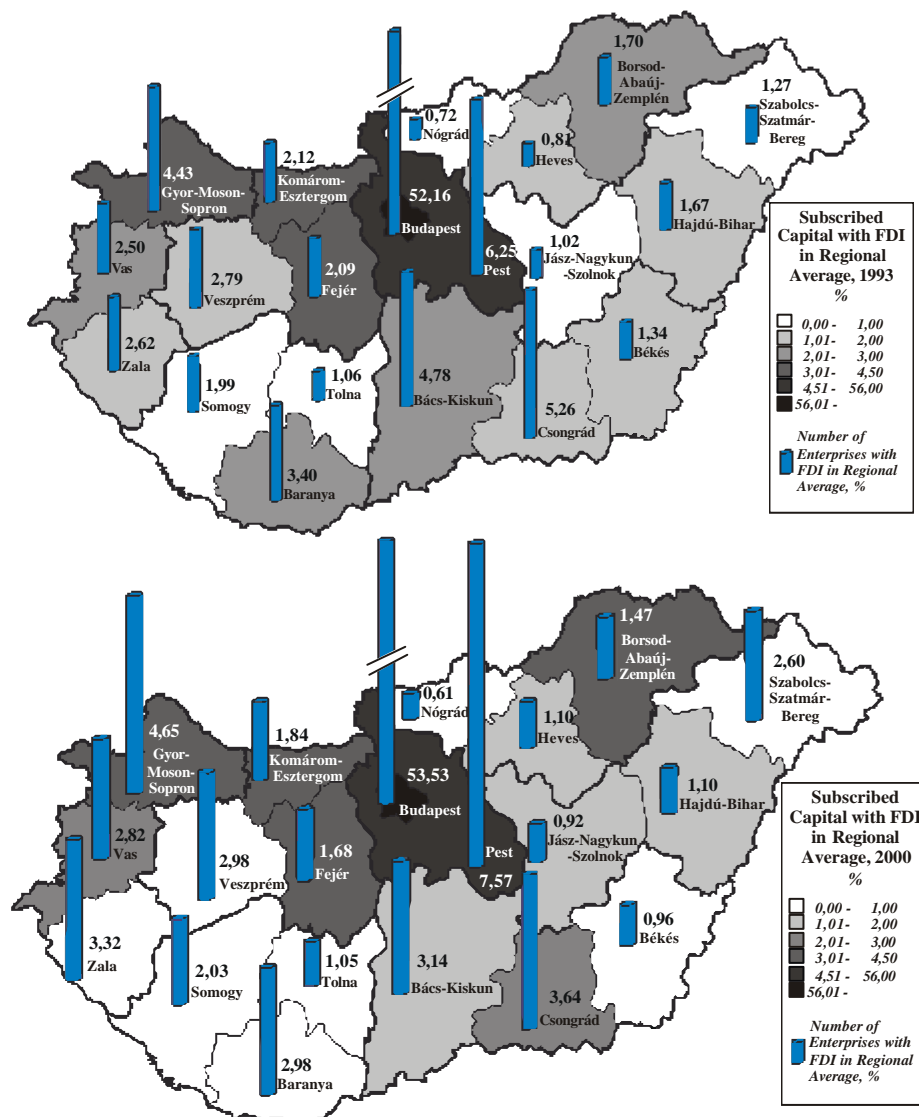
The Hungarian economy is capital centred, which appears also in the field of FDI. After the change of regime, foreign capital of a significant quantity flowed in Hungary. FDI is unevenly distributed.

According to some researchers, all these may lead to a further growth of the regional disparities. The FDI may have an intensive spill over effect on the economy of the disadvantaged areas. It is also true in the case of the sectors that need an extensive supplier network. [5]

In this case the huge settling companies may bring higher-level corporate, production, business, etc. culture and they expect these from their business partners. All this may increase economic efficiency.

The measure of capital flowing in the given regions and the regional distribution of the population do not keep in close touch. The value of investments can be connected much rather with the rate of the corporate financial strength of the certain region and with the FDI in the whole corporate capital.

**Figure 3.** Regional Distribution of the Number and Subscribed Capital of Enterprises with Foreign Interest in 1993 and 2000



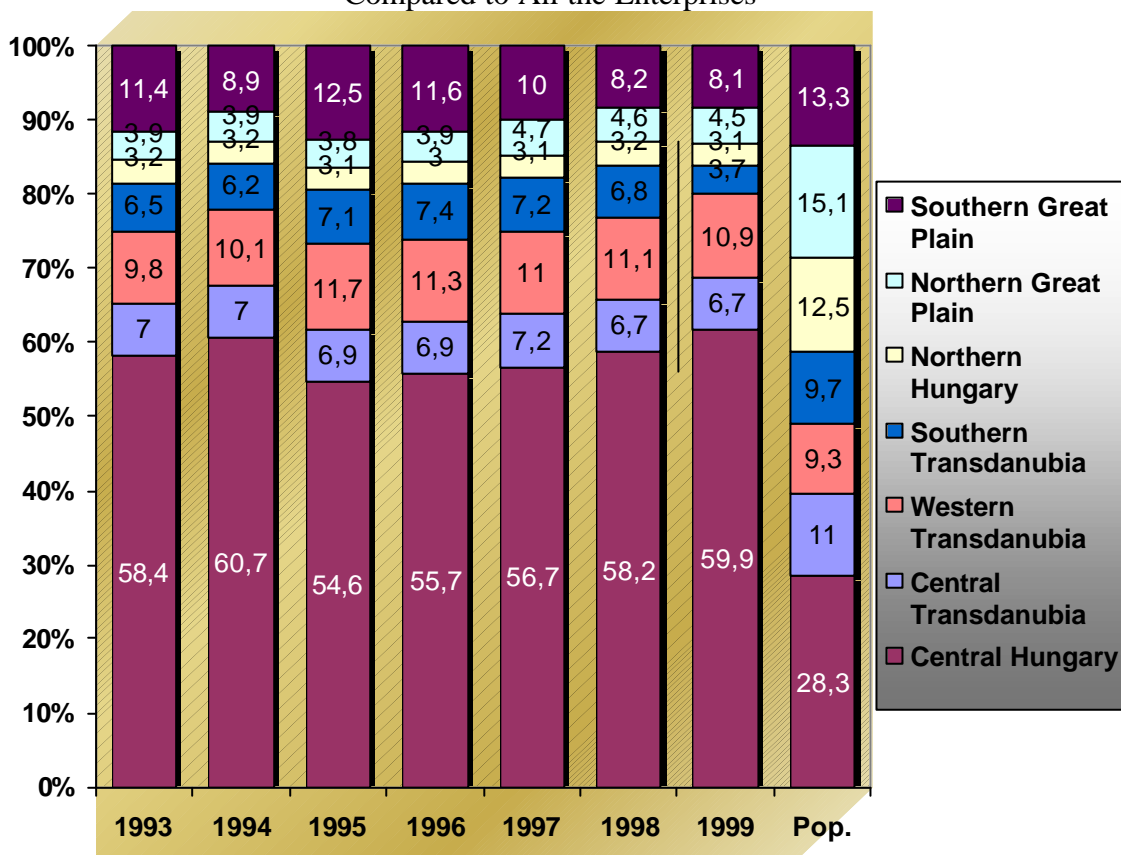
Source: Regional Statistical Yearbook - Hungarian Central Statistical Office 2001, personal editing

If we examine the distribution of enterprises with foreign interest in Hungary, the dominance of Central-Hungary appears unambiguously that is always about 60 per cent. Less investment characterise the South-Great Plain and the South-Transdanubia. [5]

The rest of the county has similar values year by year. The largest investments/units are made not necessarily in Budapest. In terms of the FDI stock a very rapid growth can be observed in Csongrád, Hajdú-Bihar and Borsod- Abaúj- Zemplén counties. It is important to consider that these counties had an extremely small FDI stock at he beginning of the 90's.

Examining Figure 3., the column shows the number of enterprises with foreign interest. The coloured territory shows the percentage of all subscribed capital of enterprises with foreign interest. There are six levels of the percentage (colour). If one county's colour becomes darker , that means in that region the percentage of subscribed capital is increased. If one county's colour becomes lighter, that means in that region the percentage of subscribed capital is decreased. For example Borsod-Abaúj County became darker, so the foreigners invest more in that region.

**Figure 4.** The Proportion of the Enterprises with Foreign Interest Compared to All the Enterprises



Source: Statistical Yearbook - Hungarian Central Statistical Office 1993-2000, personal editing

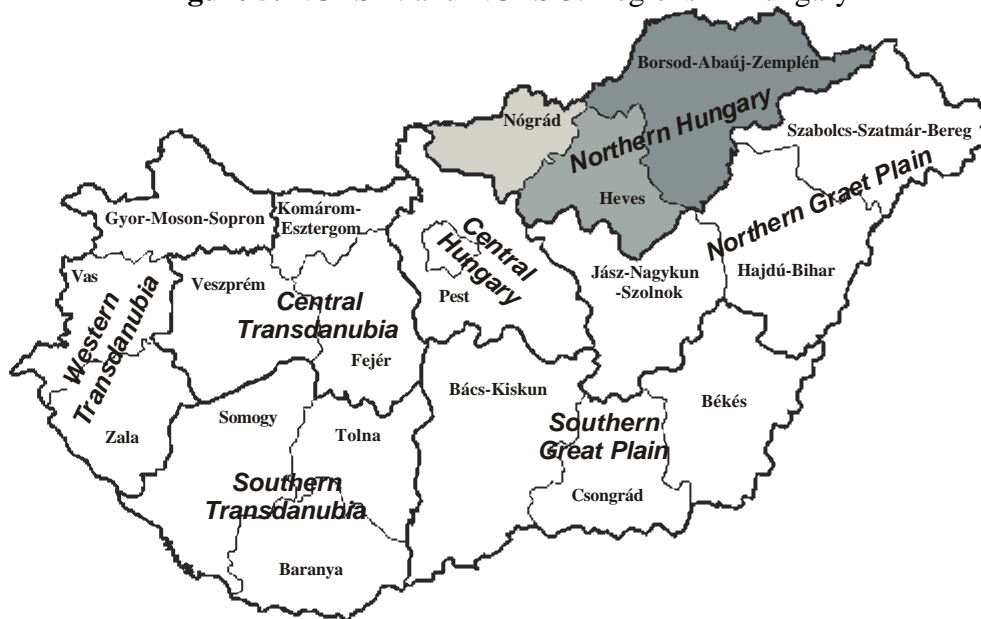
### Foreign capital inflow in Borsod- Abaúj- Zemplén county.

B.-A.-Z. county is known as an underdeveloped region when compared to the rest of the country. Its reasons arise from the history of the count(r)y.

After the change of regime this basically industrial county became a declining region. Factories were closed, which caused a huge unemployment rate.

Migration from the region is continuing. Infrastructure began to decline rapidly. An urgent restructuring was needed.

**Figure 5.** NUTS 2. and NUTS 3. Regions in Hungary



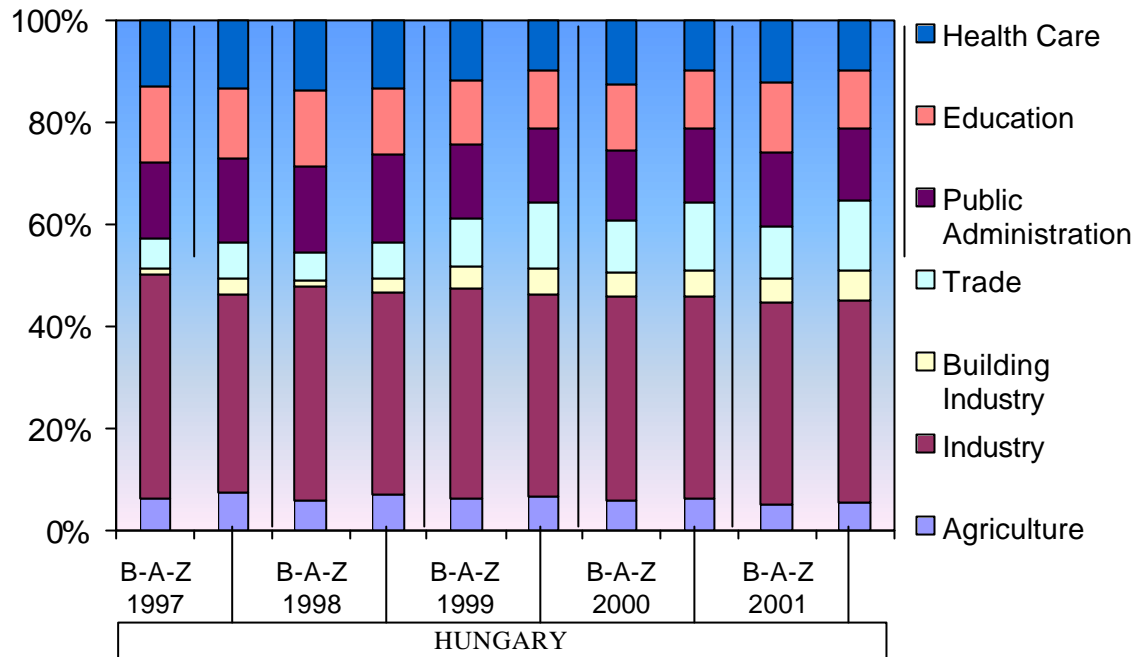
*Source: University of Miskolc, Department of Regional Economics*

Between 1995 and 1998 in the scope of Integrated Restructuring Programme 75 million dollars were spent on economic development aims. The county programme mixed the elements of the supply- and demand-oriented strategy. Besides the infrastructure investment and industrial parks (7 industrial parks, 2 enterprise parks, 3 incubators were established) the supported priorities included the development of different sectors of processing industry, the support of small and medium-sized enterprises, product promotion, the development of institutional system and also development of the labour and enterprises.

### **B.-A.-Z. county in index numbers**

Unemployment is an important problem in BAZ county. The gross average monthly wage does not reach the national average. Many people in this county work in the secondary sector. The proportion of employees in the secondary sector is significant. However, trade and construction industry is gradually gaining ground.

**Figure 6.** The Distribution of Employees According to Sectors in B-A-Z County and Hungary



Source: Regional Statistical Yearbook - Hungarian Central Statistical Office 1993-2000, personal editing

The competitiveness of some regions and their economic participants is basically influenced by the social and relational capital (Dallago, 2000, Granovetter, 1985). The mobility of multinational companies is not so powerful as it is known. It can occur that because of the increase of the productivity and the reduce of the labour input in case of output companies will not find an own plant, although they increase the local labour input very much. (Lee, 1999). Since a multinational company may give preference to the density and state of development of the institutional system over the advantages of spatial mobility.

With the help of 'soft' index numbers from the less measurable side the achievements are very significant. In the last few years a serious knowledge developed about the regional development, strategy construction, application and monitoring methods of the EU. The programme mobilised the local powers, the participants of the local and national institutional system and those of the economy. Stagnation and lethargy in the declining regions gave their places to the initiatives and self-organisations coming from below.

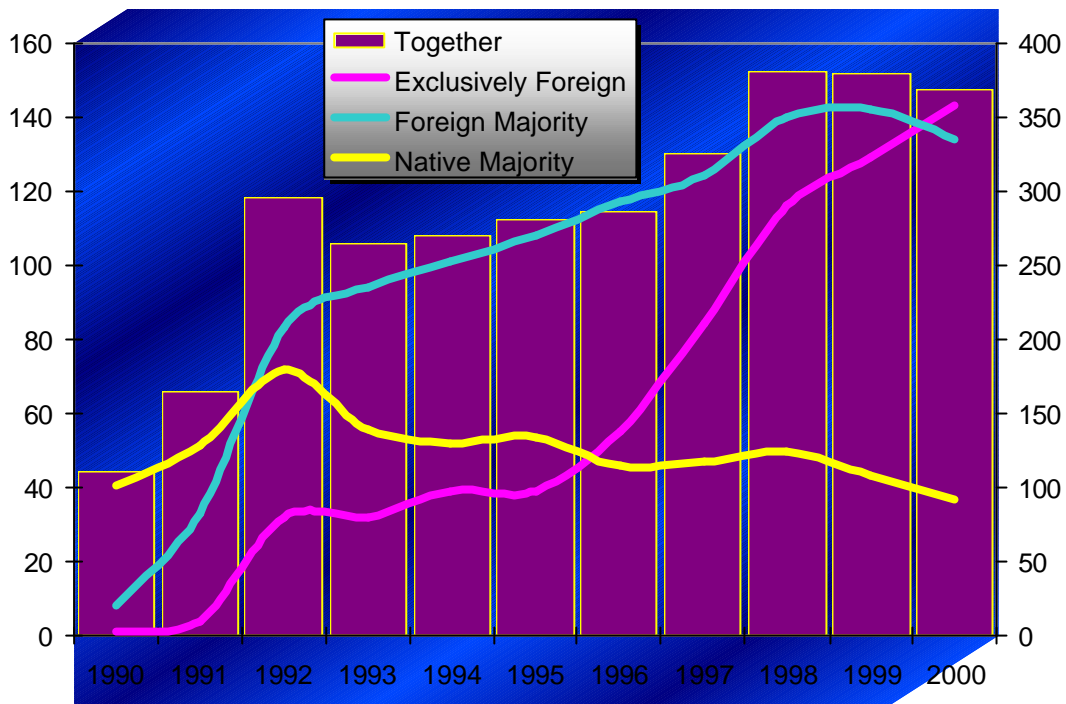
Close connections developed between the participants of the local economy and between the institutions and information began to flow. In the North of Hungary a slow, but relatively balanced growth could be examined. Foreign direct investments in Borsod-Abaúj-Zemplén county became a bit more significant.

Considering the ten-year period in B-A-Z County it can be said on the basis of the Figure 7. that the number of the enterprises with foreign interest grew from 1993 to 1998. From 1998 a slow decrease can be observed. In our opinion, this can be explained by the disappearance of smaller enterprises with foreign interest.

1995 onwards more and more exclusively foreign enterprises have been settled in this region. This can be explained on the one hand by appearance of new companies and on the other by that the foreign investors prefer to be majority owners. That's why they buy out systematically Hungarian partners from the enterprises. This tendency is justified by the formation of the number of enterprises with a decreasing domestic majority.



**Figure 7.** Formation of the Number of Enterprises with Foreign Interest in B.-A.-Z. County



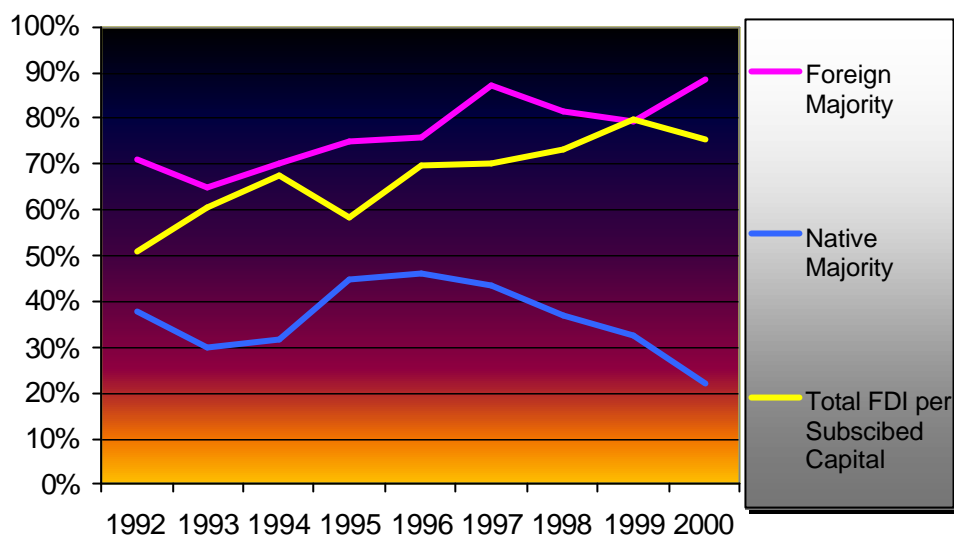
*Source: Statistical Yearbook of Borsod-Abaúj-Zemplén County – Hungarian Central Statistical Office 1990-2000, personal editing*

In the case of foreign enterprises it is not enough to examine the number, but it is also important to analyse the formation of the subscribed capital. In 1991 in the case of the subscribed capital of the foreign related enterprises the majority domestic proprietary form was higher. From 1993 the enterprises in exclusively foreign property represent a significant degree in terms of subscribed capital. Comparing the subscribed capital of the enterprises in exclusively foreign property with the number of these enterprises, it can be observed that their number grew strongly in the last few years, while their subscribed capital did not grow to the same degree. It means that many enterprises with smaller capital and exclusively foreign interest were founded. (The research is not completed since the Hungarian Central Statistical Office classifies the enterprises according to only the registered residences. Survey according to promises is going to be made in the near future.)

Figure 8. illustrates the distribution of the FDI in the relation of the subscribed capital. In the case of the companies with foreign majority interest the foreign share is continuously growing. In the case of companies with domestic interest it is continuously decreasing. In BAZ County, a tendency is felt that in the companies with foreign interest the majority shareowner strives for a total control of the company. It means that the enterprises are already prosperous that's why the partners' support is less needed.

The proportion of total FDI per subscribed capital shows a growth. It means that the foreign capital wants to achieve a dominance in the companies with foreign interest in the county.

**Figure 8.** Foreign Capital in the Subscribed Capital  
According to the Possession in B-A-Z County

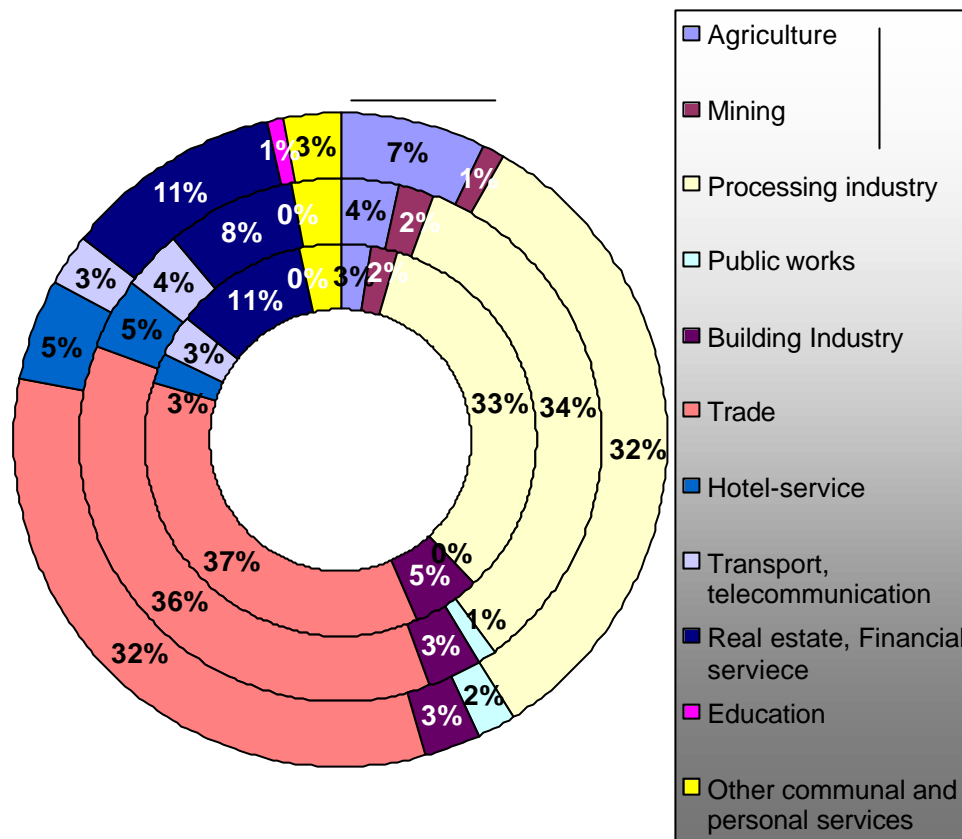


*Source: Statistical Yearbook of Borsod-Abaúj-Zemplén County – Hungarian Central Statistical Office 1990-2000, personal editing*

In the followings we examine that employees of the companies with FDI. The Table 10 illustrates employees' distribution according to the sectors in B-A-Z County. In the middle it illustrates the distribution in 1995 and going outwards 1997 then 1999.

In the county most employees of the companies with foreign interest work basically in two sectors: in the processing industry and in trade. The number of employees in the agriculture and in the hospitality is growing. Figure 9. shows the most popular sectors in BAZ county. The processing industry and trade the agriculture, hospitality, the building industry, the financial and real estate spheres are preferred.

**Figure 9.** Employees' Distribution According to the Sectors in B-A-Z County  
 Inside: 1995, 1997, 1999



Source: Statistical Yearbook of Borsod-Abaúj-Zemplén County –  
 Hungarian Central Statistical Office 1995-2000, personal editing

According to our analysis, the foreign capital interest in this region started. It is helped by the regional investment-system or by continuously developing infrastructure. It can be observed that the most enterprises works well and the majority owners endeavour to buy out large parts.

To sum up it can be stated that the neglected BAZ County in terms of foreign capital starts its career.

## Summary

In the last few years we came to the conclusion that Hungarian economy is regionally very centralised. In the course of our analyses we concluded that Central-Hungary is actually preferred very much in terms of FDI inflow. However, we stated that other regions also shared in foreign direct investments. On the other hand, disadvantageous regions received significant grants in order to develop the infrastructure. All these factors may advance the rise of underdeveloped regions.

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