Galileu
Revista de Economia e Direito
Special edition 2001, pp. 81-89

Consequences of foreign direct investment inflow from EU countries to Poland

Danuta Babinska [1]

SUMMARY

In recent years Poland has become the leader among the countries of Central and Eastern Europe in terms of foreign direct investment (FDI) inflow, of which approx. 60 % is of the EU origin. As the country moves towards the integration with the single European market the incentives for EU countries to invest in Poland are still growing bigger.

However, besides the inflow of financial capital, FDI also encompasses the transfer of technologies, know-how, managerial skills, new techniques in marketing and production organization. This paper discusses the consequences, both positive and negative, of these transfers for Polish economy and the competitiveness of Polish enterprises.

The importance of foreign direct investment (FDI) for the countries of Central and Eastern Europe undergoing economic transformation is unquestionable in the face of their huge capital needs, connected with opening and restructuring of their economies and insufficient internal financial resources. The processes of economic transition, that have been taking place in Poland since the beginning of the nineties, developing a mechanism of a competitive market economy, have created a favourable climate for foreign entities to conduct economic activity in Poland. Together with capital inflow the investment also meant introducing new technologies, management techniques, educating workforce, enriching the domestic market and export structure with new products and generally contributed to giving the Polish economy more and more features characteristic to that of a developed market economy.

---

[1] University of Economics, Katowice.

In the years of the transformation breakthrough (1988-1990) the most important reasons of investing in Poland were: [1]

- will to capture a totally new, large consumer market of 40 million people,
- cheap labour force and an access to relatively cheap natural resources,
- very high rate of return exceeding the also high risk of investing in Poland,
- lack of competition,
- low requirements and environmental protection standards, allowing to transfer "dirty technologies" into Poland.

In the mid nineties there was a shift in the main motives of investing towards – strengthening the position of international corporations already present on the Polish market and next creating an export base to third countries (especially Eastern Europe), expected financial relieves, as well as still rather low cost of well-qualified labour and relatively cheap production. At present the most important factors, that attract foreign capital are: market potential, economic growth, and opportunities created by Poland's prospective membership in the European Union. However in view of joining the EU a decrease in meaning of the factor of cheap labour force can be observed. In 2000 an increased inflow of investors, who wished to locate their companies in Special Economic Zones (SSE) was recorded.

This preceded the change of law (in line with EU regulations) regarding conditions for granting tax exemptions in Polish SSE.

It is unsettling that the structure of foreign investment has changed away from greenfield projects, toward investment in the purchase of existing companies, primarily as a result of privatization of state-owned enterprises. Privatization of the key sectors of the economy (e.g. telecommunications, petrochemical, banking and insurance sectors) has been in recent years the major factor contributing to foreign direct investment inflow to Poland.

A question can be asked here of what will the inflow of foreign investment look like as soon as the privatization of the economy is completed. Poland is an undisputed leader among the countries of Central and Eastern Europe both in terms of the value of foreign direct investment attracted annually and in terms of the cumulative FDI stock. According to PAIZ [2], over the last decade cumulative foreign direct investment on the Polish market has exceeded US $ 49.4 billion. Investment of the EU countries reached almost $ 30.7 billion at the end of December 2000, which accounts for 67 % of the overall capital (Table 1).

TABLE 1

Value of foreign direct investment realized by European Union countries in Poland between 1993 and 2000

Country of origin	Investment value in USD mln							
	1993	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**
Austria	195,0	159,7	248,0	315,3	660,3	758,3	799,4	1172,1
Belgium	0,0	38,3	41,0	46,5	115,2	156,8	289,8	587,5
Denmark	24,0	60,2	124,0	238,2	306,8	558,4	541,4	741,2
Finland	18,0	21,9	38,0	92,9	137,9	191,2	214,0	256,0
France	177,0	268,1	574,0	899,9	1616,4	2398,9	3854,7	7901,0
Germany	212,0	386,4	683,0	1524,4	2104,9	5117,3	6077,3	5903,7
Greece	2,0	2,1	2,0	3,6	3,6	3,6	1,5	501,5
Ireland	7,0	7,0	47,0	105,7	191,2	226,1	813,7	1025,0
Italy	270,0	365,8	459,0	1223,8	1636,3	2037,6	3208,0	3417,6
Luxemburg	2,0	2,3	2,0	2,3	2,3	2,3	11,6	17,2
Portugal	0,0	0,0	0,0	0,0	0,0	147,2	288,2	338,7
Spain	43,0	47,0	88,0	94,3	5,0	62,3	259,3	377,9
Sweden	71,0	86,7	179,0	361,3	565,8	691,5	789,2	2027,8
the Netherlands	233,0	240,4	408,0	951,7	1213,6	1878,9	3233,2	4224,9
United Kingdom	68,0	112,2	568,0	509,0	1002,0	1929,5	2068,0	2181,1
European Union countries investment								
in USD mln	**1322,0**	**1798,1**	**3461,0**	**6368,9**	**9561,3**	**16159,9**	**22449,3**	**30673,2**
as a percentage of total FDI	**46,7**	**41,6**	**50,7**	**45,4**	**54,0**	**59,2**	**63,8**	**67,0**
Total FDI in Poland								
in USD mln	**2828**	**4321**	**6832**	**14027**	**17705,4**	**27279,6**	**35171**	**45772**

Source: own calculations based on PAIZ data available at www.paiz.gov.pl

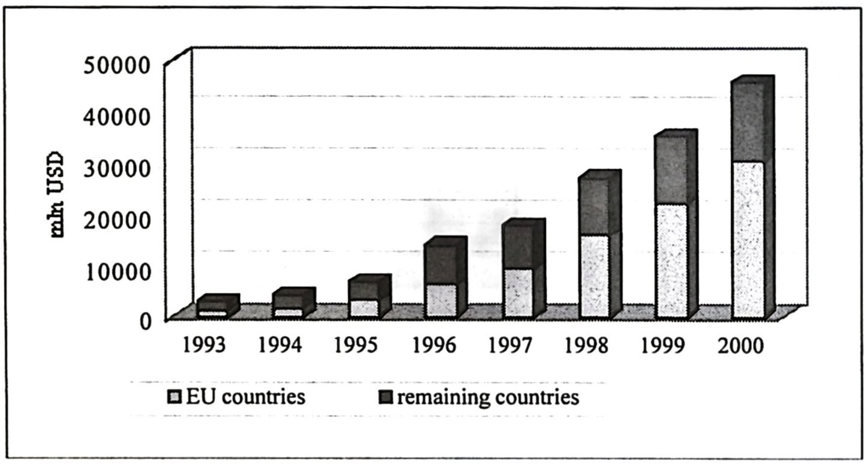
[2] PAIZ stands for Polish Agency for Foreign Investment. Since 1993 PAIZ has been monitoring foreign capital inflow to Poland. On semi-annual bases PAIZ compiles a list of major foreign investors in Poland. However the list published by PAIZ only covers firms having invested more than $ 1 million worth of assets.

It can be easily observed, that European Union investors have been increasing the value of their investment every year, but what is more, since 1997 the growth rate of EU investment in Poland has outpaced that of the whole population of foreign investors recorded by PAIZ (Figure 1).

This allows to formulate a hypothesis that the more and more advanced process of Poland's adjustment to EU integration system may provide additional, stronger incentives for investors from this particular region than for the whole population of investors.

FIGURE 1

Share of EU countries in total FDI in Poland in the years 1993-2000

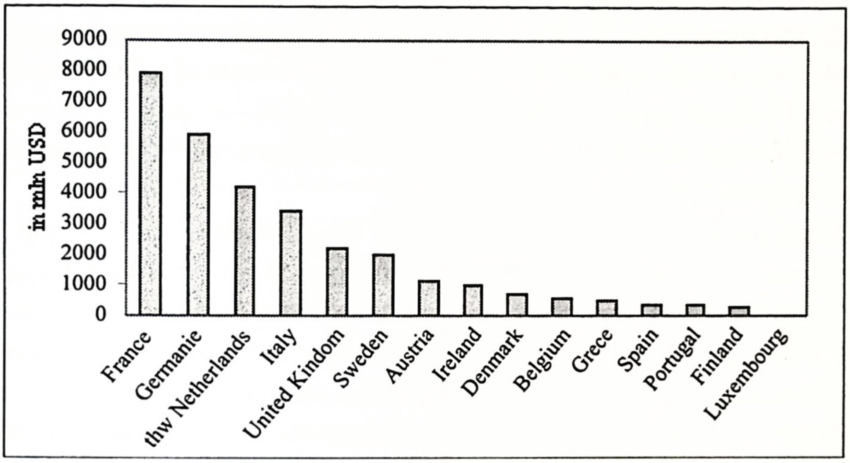


Source: based on Table 1

At the end of 2000 French investors ranked first in terms of investment expenditure (Figure 2) with that year's biggest investor France Telecom having invested USD 3,2 billion USD.

FIGURE 2

EU countries total investment in Poland (as of December 31, 2000).5



Sources based on Table 1

In 2000 the French capital has for the first time taken the lead over the German capital.

Among numerous advantages that are carried by the inflow of foreign direct investment ones that need to be emphasized are accelerating the transformation process and positive influence on the competitiveness of Polish enterprises and Polish foreign trade.

When analyzing latest trends in foreign trade of entities with foreign participation operating in Poland there is a lack of direct link between an increase in investment and increase in exports. However, foreign companies recorded a faster growth rate of exports than entities with exclusively Polish equity, which confirms better quality and higher level of international competitiveness of these enterprises. Stronger export-orientation of companies with foreign participation compared to enterprises with exclusively Polish equity can also be attributed to the fact that the former utilize foreign distribution channels and apply state-of-the-art marketing techniques [2].

As far as the share of entities with foreign participation in Polish foreign trade is concerned, according to specialists from Polish Agency for Foreign Investment and Polish Foreign Trade Research Institute imports carried out by foreign investors almost exclusively involve capital and not consumer goods. Usually, several years after a project is started, imports begin to fall while exports rise; this so called "exports harvest", meaning increased foreign sales by companies with foreign participation, is about to start or has already started in many such companies [3].

Since the very beginning of the foreign direct investment in Poland, the manufacturing sector enjoyed the greatest interest of foreign investors. Financial intermediation was the next sector to absorb the largest share of foreign investment inflow to Poland. That is why two representatives from these sectors: the banking and food sectors were chosen for further analysis.

Throughout the 10 years of reforms in Poland one of the fastest segments to develop was the banking sector. Foreign financial institutions, especially from the EU countries have played a major role in transformation of Polish banking system, using different methods of entering the market and gradually increasing their share and their importance in its functioning. Among 13 countries, whose share capital in the Polish banking sector is the largest, 10 are the members of the EU (Table 2). Their share capital constitutes almost 70 % of the total share capital of foreign entities in Polish banking sector and 40 % of the whole share capital in Polish banks.

It should be emphasized, that the development of retail banking is much more dynamic and innovative than corporate banking. Technology is crucial in this regard. All major banks operating on this market are in the middle of or have already introduced central information systems. The participation of foreign banks has undoubtedly contributed to accelerating technological development of the sector and bringing it nearer to European standards. The foreign presence in Polish banks has also been an advantage in terms of know-how, as far as marketing risk management and product development is concerned and introducing strategies created by foreign partners. Furthermore the engagement of

TABLE 2

Foreign share capital by country of origin

Country of origin	Foreign share capital		
	Amount (in mln PLN)	Capital share of foreign entities (in %)	Share in total capital of commercial banks in Poland
USA	1208,8	26,87	15,16
Germany	1077,2	23,95	13,51
Netherlands	585,3	13,01	7,34
France	348,5	7,75	4,37
Austria	317,3	7,05	3,98
Ireland	300,2	6,67	3,76
Portugal	182,3	4,05	2,29
Belgium	167,2	3,72	2,10
Italy	72,8	1,62	0,91
South Korea	60,4	1,34	0,76
Czech	35,2	0,78	0,44
United Kingdom	33,1	0,74	0,42
Denmark	25,2	0,56	0,32
Others	85,1	1,89	1,07
Total	4498,6	100,00	56,40

Source: [4]

reliable financial institutions from the EU countries (e.g. UniCredito, Hypo Verainsbank, Commerzbank, ING, KBC, Allied Irish Bank) strengthens Polish banking sector and in most cases increases the rating of the banks. A similar process can be observed in other Central and Eastern European countries, where the transfer of capital and accompanying know-how positively influences the banks' image [5].However promises of foreign financial institutions concerning accompanying know-how are often not kept. The majority of foreign investors entering Polish insurance companies contributed mainly capital; few of them introduced new products or well-operating damage liquidation system [6]. Another factor to complain about is the fact that foreign companies operating in our country rarely invest in research and development, being primarily interested in production and sales. As a result the domestic scientific and research base is decreasing dramatically.

Another sector to analyse, the Polish food industry, may become the country's trump card after integrating with the EU, considering its rich natural recourses and quite good technical equipment of the plants. The industry's privatization could prove a good example of indicating advantages and drawbacks of foreign capital presence. Since the beginning of the nineties the privatization of Polish food industry has been of great interest to foreign investors. Initially the attention focused only on four branches: beer production, tobacco, confectionary and concentrates, where the share capital exceeds 65% [7]. As a result of privatization a real market mechanism has been created, quick development of new segments on the food market has occurred, new products have entered the market and the share of processed food products in the stricture of Polish food industry production has significantly increased. The effect of the privatization has also been an intensive modernization of production plants.

However there are also some negative aspects of the foreign capital presence in Polish food industry such as legal transfer of profits abroad, often accompanied by transfer of best Polish specialists, increased import absorption of food production and the fact that great international concerns, which have acquired Polish enterprises, follow a global policy not paying much attention to its local consequences and hence the decision centers are often outside Poland, which is just another country for them to penetrate.

Studies show however, that those Polish companies, which face competition from enterprises with foreign capital are modernizing, rationalizing employment, improving management methods and introducing marketing approach [8]. This is described in the subject literature as the imitation effect, or emulation by Polish enterprises of the operating methods of firms with foreign capital. Therefore FDI is definitely a catalyst to economic growth and generally contributes to the improvement in the quality of Polish goods and services on the domestic and export market. In order however to maintain the inflow of foreign direct investment on an appropriate level, the authorities should work out a concept of financial instruments supporting the inflow of new investment (especially greenfield), in conformity with EU regulations.

BIBLIOGRAPHY

[1] A. Szymaniak: Motywy podejmowania bezpośrednich inwestycji zagranicznych w Polsce na tle innych krajów Europy Środkowej i Wschodniej, Europa Wschodu i Zachodu, Wydawnictwo Fundacji
Humaniora WSB w Poznaniu oraz WSZiB w Poznaniu, Pozna_ 200, nr 4

[2] B. Durka: Share of companies with foreign participation in Polish foreigń trade, in: Foreign investment in Poland, Foreign Trade Research Institute, Warsaw 2000.

[3] Zaczęły się "żniwa eksportowe", Rzeczpospolita no 98, April 26, 2001 and: A bumper crop of FDI, Warsaw Voice, March 4, 2001

[4] T. Loose: Banki zagraniczne w Polsce, Wspólnoty Europejskie, nr 3, 2001

[5] R. Lukášová, T. Urbánek: The image of Czech Banks – contents and structure, in: Zachowania podmiotów rynkowych w Polsce a process integracji europejskiej – materiały konferencyjne, AE w Katowicach, Katowice 2001

[6] A. Szczecińska: Know-how w zapowiedziach, Rzeczpospolita no 48, February 26, 2001

[7] E. Szot: Polski atut, Rzeczpospolita no 139, June 16-17, 2001

[8] B. Jarzembowska: Influence of direct foreign investment on the competitiveness of Polish enterprises, in: Zeszyty Naukowe no 8, Kolegium Gospodarki Światowej, Warszawa 2000