LAPPEENRANTA UNIVERSITY OF TECHNOLOGY
Northern Dimension Research Centre
Publication 27

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FOREIGN INVESTORS IN TRANSITIONAL ECONOMIES: CASES IN MANUFACTURING AND SERVICES

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Lappeenranta 2006

ISBN 952-214-151-8 (paperback)
ISBN 952-214-152-6 (PDF)
ISSN 1459-6679

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Contents

List of tables and figures

Foreword

The Northern Dimension Research Centre (NORDI) is a research institute run by Lappeenranta University of Technology (LUT). NORDI was established in the spring of 2003 in order to co-ordinate research into Russia.

NORDI's mission is to conduct research into Russia and issues related to Russia's relations with the EU with the aim of providing up-to-date information on different fields of technology and economics. NORDI's core research areas are Russian business and economy, energy and environment, the forest cluster, the ICT sector, as well as logistics and transport infrastructure. The most outstanding characteristic of NORDI's research activities is the way in which it integrates technology and economics.

LUT has a long tradition in conducting research and educating students in the field of communist and post-communist economies. From the point of view of these studies, LUT is ideally located in the Eastern part of Finland near the border between EU and Russia.

This book deals with foreign direct investment (FDI) in transitional economies. The analysis covers car manufacturing and retailing, both of which show dynamic development in post-communist societies.

I want to express my gratitude to Ms. Riitta Salminen and Ms. Rita Sergeeva, both of whom have helped me to finalize the book.

Lappeenranta, February 2006

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1 Introduction

The communist period in the former Soviet Union and former Eastern Europe showed that foreign trade fits very poorly into the traditional model of a planned economy. Central planners first define the resources that the economy has in its disposal, and then they decide what can be done with these given resources. Prices are fixed in advance. For such a system, foreign trade is a risk factor whose effects cannot be controlled by the planners in advance. Thus, it is understandable that efforts were made in planned economies to minimize the risks involved in foreign trade.

Thus, it was clear in the Cold War period that centrally planned economies were unable to use the potential welfare effects of the international division of labour optimally. International mobility of production factors was strictly limited in centrally planned systems.

According to communist ideology, foreign direct investment (FDI) to the socialist economy was highly suspicious: it was maintained in the communist propaganda that internationally mobile capital is a weapon of the enemy to exploit labour and natural resources in the developing world. Thus, FDI activity by Western companies was basically prohibited in the communist bloc.

However, this ideologically based rule was modified in the 1970s and 1980s. In the communist bloc, Romania and Hungary allowed FDIs in their respective territories in the 1970s in the form of mixed ventures. As a result, some companies partly owned by communist states and partly by capitalist enterprises came into being.

Sharing equity between communists and capitalists in a centrally planned economic environment was not an easy task. Thus, it was not surprising that FDI activity in the former communist countries had hardly any real substance. Several mixed ventures came into being especially in Hungary in the Cold War period, but FDI-capital was generally not very mobile toward centrally planned economies. One of the very concrete difficulties in this context was in the sphere of currency issues: communist economies had all non-convertible currencies.

The systemic change took place in two waves: in 1989, the centrally planned system collapsed in the former Eastern Europe; the Soviet Union was dismantled in 1991. Revolutionary change comprised the political, as well as the economic scene. Transition from central planning to decentralized market altered the FDI environment fundamentally.

FDI-inflow to post-communist countries after the systemic change has been extremely dynamic. This part of capital movement has not been evenly distributed within the region of transitional economies (TEs). Investment decisions have naturally been made by multinational enterprises (MNEs). Profitability expectations have played a decisive role (for details, see Tiusanen-Kinnunen-Kallela: EU´s Enlargement Process: Investment Climate in 10 Transitional Economies. NORDI publication n:o 7, Lappeenranta, 2004).

In the early period of transition, there was a rather general expectation that Western investors would concentrate on manufacturing in order to take advantage of cheap cost factors, especially labour, when investing in post-communist economies. Thus, it was assumed that FDIs in TEs would be mainly supply-oriented.

In the second half of the 1990s, it became clear that many TEs, especially those with willingness to join the EU, started to have increasing purchasing power. This trend of increasing affluence has altered the FDI-scene radically in TEs: market-seeking investors have shown growing interest in TEs.

Obviously, it is impossible to categorize FDIs in an exact way. Some foreign investors in TEs are clearly supply-oriented: Ford started to produce car engines in Hungary in the 1990s, and sold all end-products to her own affiliates in Western Europe. This kind of activity is called off-shore: local (Hungarian) demand is not considered in this strategy.

Volkswagen (Germany) owns Skoda car manufacturing enterprise in the Czech Republic. Over 80% of Skodas are exported. Thus, the operation is supply-oriented, because VW sells the big bulk of Czech-made vehicles via export. However, Skoda is the major brand (new car segment) in the Czech Republic. Therefore, the western investor has also market-seeking motive: it conquered the local market conveniently by the local brand.

FDIs in retailing, hotel business, fast food restaurants, etc. are obviously market-seeking. In this category, investors look for affluent environment (clients with purchasing power). Supply-oriented FDIs look for cheap production costs. Market-seeking investors obviously look for places, which are important tourist destinations. So far, TEs have been able to offer attractive prices for Western visitors. FDI activity in spheres involving tourism is comprehensible.

This short study deals with FDIs in ten TEs, eight of which joined the EU in 2004. Bulgaria and Romania are likely to join the Union rather soon. Therefore, these two countries are included here.

The aim of this study is not to cover all details of FDI scene in countries under review. Only some major FDI-trends in post-communist societies are described below. Car manufacturing and retailing are chosen as spheres, in which Western capital is actively invested in the TE-region.

2 Foreign Direct Investment (FDI) in Transitional Economies (TEs)

2.1 Quantitative Assessment of FDI in TEs

In the early period of post-communism it was rather often asked, whether newly established capitalism in the formal centrally planned economies is possible without capital. It was commonly assumed that transitional economies need large capital injections from external sources. However, no new “Marshall Plan” of economic aid ever took place to help the former Comecon-countries. (Comecon was the name of the trading bloc of European communist countries which was also called Council of Mutual Economic Assistance or CMEA.)

Thus, it was rather important in the 1990s for TEs to attract private capital from the outside world to build up market economies after the collapse of communism. It can be assumed that inflow of risk capital in FDI-form was the optimal alternative from the point of view of TEs: FDI includes not only capital injection, but contains also technology component and management know-how ingredient, which were in short supply in the former system of central planning. Therefore, it can be assumed that FDIs have been a very valuable factor in TEs from the point of view of host country development.

In the immediate aftermath of communism, gross domestic product (GDP) decreased in every TE. Alongside with institutional reforms, economic recovery started to take shape in TEs. However, this recovery has not been even in ten countries under review.

Table 1 GDP, 2004

	Index 1 1990=100	Index 2 2000=100
Czech Republic	114,8	112,1
Hungary	124,1	115,0
Poland	160,4	112,0
Slovakia	123,6	119,5
Slovenia	135,7	113,3
Estonia	116,0	127,4
Latvia	85,8	133,4
Lithuania	94,5	132,8
Bulgaria	97,5	120,3
Romania	105,6	125,5

Source: WIIW

The first index in the above table describes the “long-term” trend of GDP development in TEs (year 1990 is marked with 100). In this trend, Poland has the highest marking with over 160 indicating that the overall economic growth in real terms in transitional period has been over 60%. Slovenia's economy shows a 36% growth in the same period of time, while Hungary and Slovakia have 24% each. Three countries (Latvia, Lithuania and Bulgaria) have experienced an actual decline in their economic activity during the transitional period.

In the second index, 2000 is marked with hundred. All countries involved exceeded the level of the base year in 2004. The most vigorous growth has taken place in the Baltic States: Latvia and Lithuania have grown in the early period of the new century over 30%, and Estonia is not far behind. Romania and Bulgaria, both with postponed EU-entry, show better growth results than their Central-East European neighbours in the light of the second index. Poland has at the beginning of the 21st century experienced a clear deceleration in her growth. However, the overall picture in the light of the second index is very positive.

Gross fixed capital formation (investment) development can be illustrated in a similar manner, via two separate indicators. Unfortunately, information in this sphere is not complete.

Table 2 Gross Fixed Capital Formation

	Index 1 1990=100	**Index 2 2000=100**
Czech Republic	144,8	125,6
Hungary	186,1	129,0
Poland	209,8	89,8
Slovakia	94,7	116,0
Slovenia	234,5	121,9
Estonia	N.A.	149,4
Latvia	85,5	160,6
Lithuania	N.A.	163,9
Bulgaria	144,7	171,1
Romania	158,8	147,1

Source: WIIW

As pointed out above, Poland and Slovenia had the highest GDP growth rates since 1990. In these two TEs, investment activity has more than doubled between 1990 and 2004, while two countries, Slovakia and Latvia, show declining investment tendency in the same period of time. Estonian and Lithuanian figures are not available. In this "long trend" (1990=100) investment development, Bulgaria and Romania have rather positive results, even if their GDP (overall) economic growth figures are very meagre.

The second investment index (2000=100) shows positive results (growth since the turn of the century) in every country of the table, except in Poland. After a very long and strong investment boom, investment in Poland dropped in 2001-2003, but recovered somewhat in 2004. However, the investment level in 2004 was about 10% below the base year (2000) marking.

The fastest investment growth in the light of the second index can be found in Bulgaria with an over 70% increase. Lithuania and Latvia are not far behind. Also Estonia and Romania show vigorous investment boom signs in the early years of the 21st century.

Obviously, investment growth is an indication of positive spirit and confidence in the future. In many emerging market of the world, substantial capital flight has taken place. If the local economy is regarded too risky for investment and money starts escaping, there is always the danger that human capital starts flowing out. This phenomenon is called brain drain. Local economy cannot develop if capital and competence escape. Downward spiral is a realistic option in emerging markets, including TEs. The danger of permanent decline has very clearly been avoided in countries under review.

Foreign investors are undoubtedly watching investment climate before putting their money into new markets. In those TEs selected to this research report, the aim to join the EU has obviously boosted institutional reform. This process has clearly been monitored carefully by potential movers of risk capital.

In the early period of transition, there were certain special factors visible in the FDI-game. It can be assumed that many internationally active companies knew that Hungary was a special case among TEs: economic reforms containing aspects of market mechanism started in Hungary already in the late 1960s. These reforms certainly had plenty of ideological handicaps, but still the economic environment was more liberal in Hungary than elsewhere in the former Eastern bloc. Therefore, it is no wonder that Hungary became a favoured playing ground for multinational companies after the systemic change.

Post-communist privatization process was an extremely complicated issue involving political, economic and emotional features. In discussions on this important matter, it was widely argued that capital created in communist societies ought to be divided evenly among adult citizens of every post-communist country. Various so called “voucher schemes” became into being.

The idea was that everybody was entitled to get "privatization coupons" for a small sum of money. Vouchers thus allocated were exchanged for shares of local companies or accepted as means of payment when properties moved from public sector ownership into private hands.

It is not the aim of this study to cover details of this historical event of post-communist ownerships deals. It suffices to state here in very general terms that there were two countries, in which the state sold the big bulk of communist-created capital: Hungary and Estonia. Other TEs had mixed privatization schemes (in this context, it is worth to notice that after the unification of two German states, East German productive assets were straight sold to best bidders).

It is assumed here that Hungary and Estonia obtained a special advantage in attracting FDIs in the early period of transition via offering assets for sale in massive scale for best offers. No empirical evidence is provided to prove this hypothesis.

In the mid-1990s, Hungary was in the lead in FDI statistics in the TE-region even in absolute terms. In those ten TEs under review here, Hungary was far superior in relative FDI-terms in 1995.

Table 3 Foreign Direct Investment Stock (EUR Million)

	1995	**2004**	**Growth 1995-2004 (%)**
Bulgaria	273	5.700	2.088
Romania	642	13.000	2.025
Lithuania	274	4.600	1.679
Estonia	574	6.300	1.098
Slovakia	1.013	10.500	1.037
Poland	6.121	47.000	768
Czech Republic	5.741	42.000	732
Latvia	480	3.400	708
Hungary	8.817	47.000	533
Slovenia	1.376	5.500	400

Source: WIIW

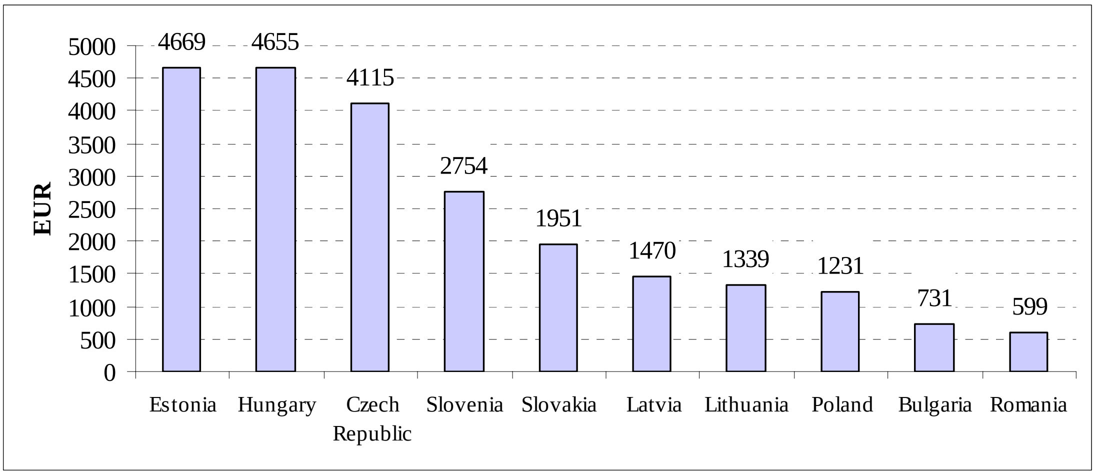
In 1995, the overall FDI stock in ten TEs under review is € 25,3 billion. Hungary had a slice of almost € 9 billion of this FDI-"cake".

In 2004, the FDI stock in ten TEs was no less than € 185 billion, or over seven times more than in 1995. The expansion has been striking.

The most impressive growth rates in FDI stock statistic can be found in Bulgaria and Romania (non-EU-members) between 1995 and 2004: in these two locations growth is no less than factor 20. Lithuania is not far away. Estonia and Slovakia have both tenfold expansion of FDI. Poland, the Czech Republic and Latvia show about average growth rates of the region, while Hungary and Slovenia reach lower increase in the same period than the average figure of the region.

National markets differ essentially from each other in our selection of TEs. Estonia has about 1,4 million inhabitants, while the equivalent figure is about 39 million in Poland. Thus, it is appropriate to clarify the FDI stock in TEs in relative terms. Usually, per capita figures are taken to measure FDI influence in various national economies.

Figure 1 Foreign Direct Investment Stock per Capita in 2004



Source: WIIW

Estonia, Hungary, and the Czech Republic have FDI stock per capita over € 4.000 each in 2004. Slovenia's equivalent figure is about € 2.000 lower than in Estonia. However, Slovenia in her fourth place has attracted FDIs per capita almost five times more than Romania at the bottom of the scale.

Poland with a population of 39 million has far more than half of new EU-citizens after the Eastern enlargement of the Union. The Polish figure in the above table is rather modest, only about one quarter of the Estonian and also Hungarian equivalent. However, Poland has received about twice as much FDIs per capita as Romania.

In sum, in the relative FDI assessment there are essential differences between ten TEs scrutinized in this report. However, the laggards (Romania, Bulgaria) have shown very high FDI growth rates recently.

Many empirical studies (e.g. UNCTAD's yearly investment reports) show that the big bulk of FDI moves from one rich country to another, even if the neo-classical economic theory assumes that capital moves from those places, where it is abundant to locations with capital scarcity. This theory assumes that the global market is perfect: however, there are essential differences between countries in infrastructure, functioning of the legal system, etc. FDI decisions are made on the basis of a huge variety of indicators, one rather modest factor being the relative scarcity of capital.

Furthermore, there is plenty of evidence that more and more FDIs are market-seeking and less supply-oriented. Service sector FDI development is getting more dynamic than manufacturing FDI. Thus, the assumption that the main motive in investing abroad is to find cheap labour for manual work is getting hopelessly outdated.

In the early period of transition, it was often pointed out that post-communist societies are hopelessly behind in living-standard competition in comparison to the West. Since the mid-1990s, TEs have shown good growth performance, while Western Europe (EU 15) has not been a schoolmaster of economic dynamism. Thus, living-standard gap between East and West has become less and less dramatic. General living standard comparisons are normally made by using GDP figures per capita calculated in US-dollars or euros.

Table 4 GDP per Capita, 2004 (Euro-Based)

	A	**B**	**B/A**
	GDP nominal	**GDP at PPP**	**ERDI**
Slovenia	13.042	17.436	1,33
Hungary	8.172	13.892	1,70
Estonia	6.558	11.279	1,72
Czech Republic	8.368	15.565	1,86
Slovakia	6.161	12.138	1,97
Latvia	4.696	9.674	2,06
Poland	5.112	10.582	2,07
Lithuania	5.195	10.857	2,09
Russia	3.291	8.360	2,54
Romania	2.633	6.977	2,65
Bulgaria	2.520	6.830	2,71
Greece		18.270	
EU-15 average		24.251	
EU-25 average		22.288	

Source: WIIW

In the light of the “original” GDP per capita figures, there is a very deep gulf in living standard between the new (TEs) and old (15 countries) EU-members. The level reached in the Czech Republic and Hungary is less than one third of that in the old EU-members (on average). Bulgaria and Romania, which did not get the EU-accession in 2004, seem to have living standard of only one tenth of the EU (15) nouveau.

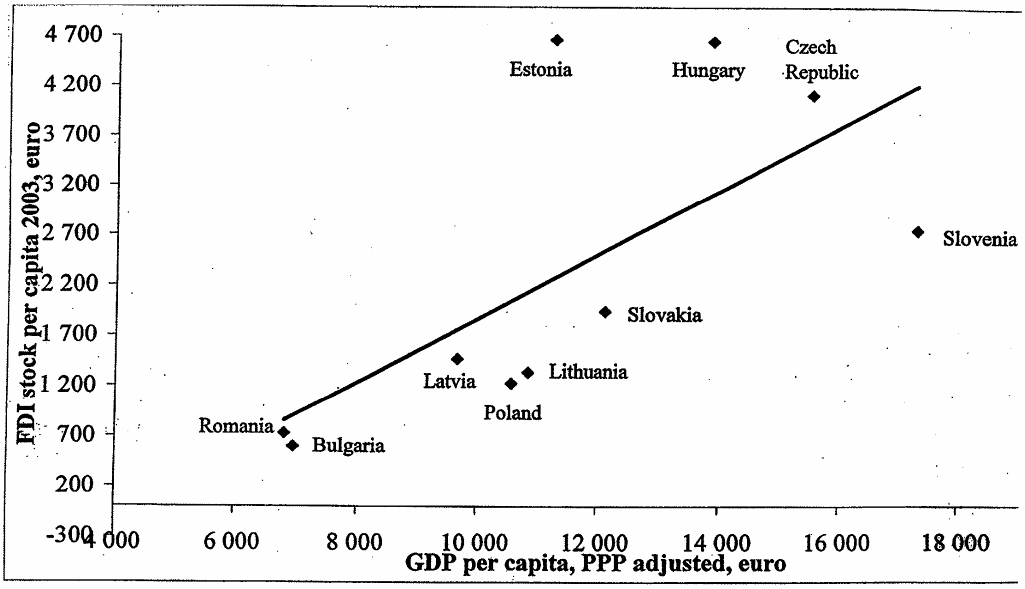
Evidently, the original GDP figures (marked with A) have biases caused by official exchange rates, which reflect different price levels in an extremely imperfect manner. Therefore, it is appropriate to use a special tool called the purchasing power parity (PPP) adjustment, in order to reach more realistic figures (marked with B). In this adjustment the fundamental fact of relatively low prices in TEs is taken into consideration: PPP corrected figures give a more realistic picture of living standard differentials between East and West than the ”raw” figures.

In all TEs in the above table, the PPP adjusted figures (B) are higher than the original GDP numbers indicating that all currencies in TEs are undervalued. After the PPP correction, TEs show still lower welfare than the EU (15) average. However, the gap is essentially more modest than in the light of the original GDP per capita figures calculated by using official exchange rates.

By dividing the B-figures by A-figures, exchange rate deviation indexes (ERDI) can be established showing, how much the official exchange rate in each TE deviates from the “equilibrium rate”. In the Polish case, the ERDI value is about two, which means that every euro buys about twice as much goods and services in Poland in comparison to euro-area (on the basis of an average consumer goods basket). Other way around, it can be maintained that prices in Poland are about 50% cheaper than in the euro-region. The low price level (undervaluation) in TEs gives price competitiveness to transitional economies: this is also called “exchange-rate protectionism”. ERDI value, which is the higher, the lower the development level of the economy is, measures the degree of this exchange rate protectionism: it gives price competitiveness to exportables and keeps importables relatively expensive (calculated in local currency).

Figures marked with B in the above table reflecting “real” living standard in 10 countries under review are put on the horizontal line in the graph below. The vertical axis measures FDI stocks per capita (in euro) containing information discussed above. The calculation below shows that in the TE-region there is a clear positive correlation between living standard and FDI attractiveness: the higher the welfare in a TE, the keener is the interest of foreign investors to select the location for business operations.

Figure 2 FDI/GDP per Capita 2004



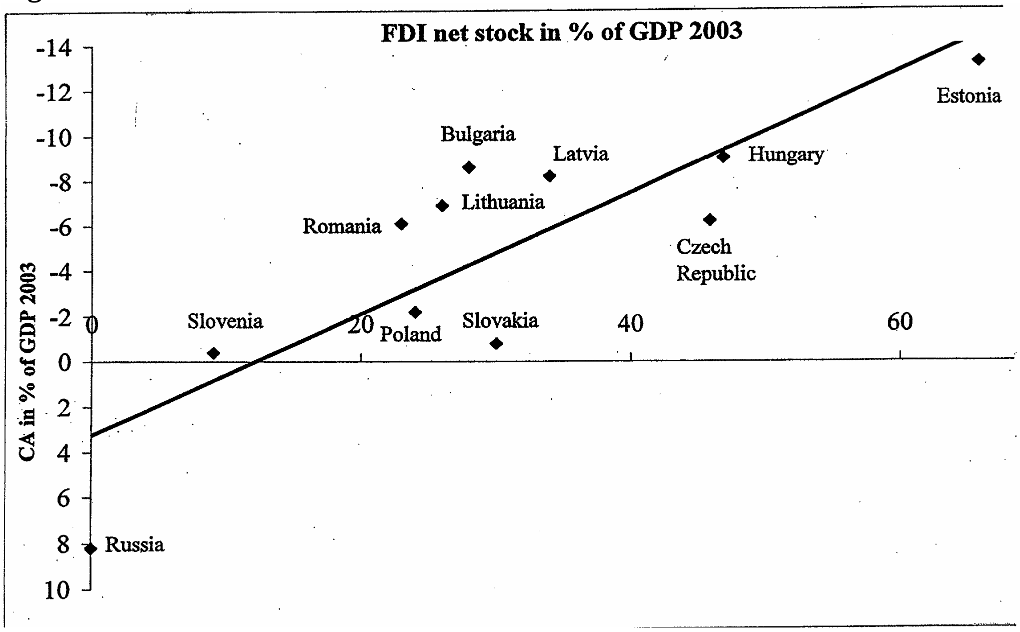
Source: WIIW

The leading FDI-destinations in the TE-region – Estonia, Hungary and the Czech Republic – are above the drawn line. Slovenia, the highest living standard TE in our sample, has an over average FDI concentration. Estonia with high relative FDI stock has a living standard, which is more or less in line with the Slovakian wellbeing: difference in FDI figures between these two countries is remarkable.

The graph above allows the assumption that potential foreign investors' primary concern in selecting a location in the TE-region is not the cheapest possible labour cost component, which normally can be found in the lowest living standard environment. Furthermore, it can be assumed that FDI actors are market-seekers, who want to have the highest possible purchasing power in their playing field. Retailers, mobile phone operators, bankers, etc. look for "rich", not "poor" economic environment. If the supply-orientation would be predominant aspect (with cheap labour) in investment decision, Bulgaria and Romania would be high up in the vertical scale and the correlation in the graph negative.

Relative macro-economic importance of FDI can also be measured by taking the net FDI stock as a percentage of local GDP. Net FDI stock equals FDI inflow minus FDI outflow. FDI outflows in TEs under review have little substance: TEs have the tendency to import – not export – capital in the sphere of FDI. In this respect, Russian economy in transition is an exception: her FDI outflow and inflow are identical. Thus, Russia does not have any net inflow of FDI-linked capital.

Figure 3 FDI Net Stock and CA in % of GDP in 2003



Source: WIIW & UNCTAD

In the above graph, the horizontal line measures net stock of FDI as a percentage of GDP. In the vertical axis current account deficits (surpluses) are measured.

Some TEs have critically high deficits in their CA bookkeeping. Estonia has lately had CA deficits exceeding 10% of local GDP. Fortunately, Estonia has been able to finance continuously a big part of her CA deficit via FDI inflow.

FDI is said to be a form of long-term investment, which is not quickly reacting on changes in inflation, interest rates, and stock exchange. Thus, FDI is ideal form of importing capital in countries with high CA deficits: “hot money” (short-term speculative capital) normally reacts quickly on critical CA deteriorations. In the 1990s, a series of CA crises took place in the global economy. In these events involving currency devaluations, withdrawal of speculative funds triggered economic slump.

Estonia’s CA deficit has reached about 14% of GDP, which actually is a rather critical figure. However, Estonia’s FDI stock is clearly over 60% of local GDP value. Therefore, no currency crisis has taken place so far in this country.

Hungary, Latvia, and Bulgaria also have high CA deficits of some 8–9% of GDP. Hungary has rather high FDI stock of almost 50% of GDP. However, FDI inflows have not been too dynamic lately. Latvia and Bulgaria show FDI stock figures approximately 30% of GDP, but in both cases FDI inflows show strongly increasing tendency. Slovenia is the best-off country in our sample of TEs. Her CA has in the new century been in relative equilibrium. One important reason behind that fact is high tourist income Slovenia is able to generate. Slovenia's FDI stock as a percentage of GDP is low, but from the point of view of CA balance this low share is not of a great importance.

Russia is taken into the above graph for comparison. This huge country with plentiful natural resources has lately earned considerable annual surpluses in her CA. The most important background factor is the high world market price of oil, the main exportable of Russia. Thus, Russia deviates from other TEs in the above graph extremely clearly: the net impact of FDI is close to zero (in quantitative term), while CA is easy to take care of via mighty export earning generated by wide resource base.

2.2 Some Structural Issues of FDIs in TEs

Since the mid-1990s, FDI stock has increased much more rapidly than real GDP and overall investment in real terms. Thus, it can be assumed that foreign investment enterprises (FIE) have had an essential influence in TEs under review. FIE is a term used by WIIW describing the sector in which FDI have taken place (FIE is a firm dominated by foreign owner).

Manufacturing is not the main branch of FDI activity in TEs in the early years of the 21st century. The importance of this branch varies within TE-group of ten countries.

Table 5 The Share of Manufacturing (% of FDI Stock) in 2002

	(%)
Hungary	46,1
Slovenia	43,3
Czech Republic	37,6
Slovakia	36,6
Poland	35,8
Bulgaria	33,4
Lithuania	29,3
Estonia	18,8
Latvia	15,2
Romania	N.A.

Source: WIIW

Hungary has the highest figure with 46,1%, and Latvia the lowest one with 15,2% in the above table. Thus, less than half of FDIs located in 10 TEs is invested in producing industrial goods. Alongside with Hungary, Slovenia exceeds the 40% mark in the table. In the Czech Republic, Slovakia, Poland, and Bulgaria manufacturing makes up about one third of FDI stock. The Baltic states are at the bottom of the list: Lithuania's figure is below 30%, Estonia's under 20%, and Latvia's about 15%. Romania's figure is not available.

It can thus be concluded that services dominate the FDI scene in TEs. Substantial penetration by foreign firms has taken place in infrastructure services (e.g. banking, telecom, water, electricity). Retail trade, hotels, restaurants, and various transport services have also attracted FDI in the TE-region.

Table 6 FDI Stock in Services, 2002 (% of Total Service FDI Stock)

Service	(%)
Electricity, gas and water	6
Construction	5
Trade	21
Hotels, restaurants	2
Transport, storage, communication	24
Finance	29
Business activities	10

Source: UNCTAD (the table covers all European TEs, including former Soviet Union)

Finance dominates the above table with an almost 30% figure. Banks have really been transferred into foreign hands in transitional economies. Transport, storage, communication is with 24% on the second place. In many TEs, foreign involvement in telecom operators is heavy. This segment with exponential growth in TEs, calls for substantial capital input. Obviously, the number of operators is very limited in every TE, but each investment in this field involves plenty of cash.

Trade takes over one fifth of the service FDI stock in the TE-region. Big Western retailers have become a very visible feature of post-communist transition. Big international players move big sums of money.

Hotels and restaurant category has a rather modest marking of 2% only, although Western brands in this sphere are rather visible. It can be assumed that many brand owners have entered the scene of hotel and restaurant business without owning properties: renting and leasing of suitable places has occurred in this branch.

Table 7 Foreign Share of Banking Assets in TEs, 2001

	(%)
Estonia	99
Czech Republic	90
Hungary	89
Slovakia	86
Lithuania	78
Bulgaria	75
Poland	69
Latvia	65
Romania	47
Slovenia	21

Source: UNCTAD

In Estonia, only one percent of banking assets is in local ownership, while the equivalent figure in the Czech Republic is 10%, and in Hungary 11%. In eight countries out of ten, more than half of banking assets are in foreign hands. Only Romania (47%) and Slovenia (21%) are below the 50% mark in this comparison. The situation in Slovenia is exceptional: almost 80% of banking assets are in local ownership.

In the important sector of manufacturing, the influence of foreign capital has increased in TEs with time. WIIW databank provides interesting material on this topic. Unfortunately, this material is not always available on all ten TEs under review here. In spite of that, several interesting pieces of information can be picked up from the mentioned source.

Foreign investment enterprises (FIEs) are units, in which foreign capital is 10% or more (of the equity ownership). Domestic enterprises (DEs) are compared with FIEs. Information below deals only with the manufacturing sector.

Table 8 Share of FIEs of Equity Capital (Manufacturing) in 1998 and 2001 (%)

	1998	2001
Estonia	36,8	46,3
Czech Republic	28,4	54,5
Hungary	72,7	67,6
Poland	43,2	53,1
Slovakia	35,2	55,9
Slovenia	21,6	24,6
Romania	19,8	54,2

Source: WIIW

The equity capital share of FIEs shows in the above table clearly increasing tendency between 1998 and 2001. In countries available for this comparison all, except Hungary, have increasing figures. In 1998, the Hungarian figure was with 72,7% very high: moderation to 67,6% has taken place, but in 2001 Hungary still has the highest figure in the table. High growth occurred in the Czech Republic: the FIE share of equity capital doubled from 28,4% to 54,5% 1998–2001. Even higher increase has taken place in Romania: the FIE share in 1998 was about 20% and over 54% in 2001. In Slovenia, the FIE share was in 1998 rather modest with 21,6%, and remained in 2001 on a rather low level of about 25%. Only in Estonia and Slovenia, the 2001 figures remain under 50% line.

Obviously, figures in the above table do not necessarily reflect increasing involvement of foreign capital. It is possible that a FIE (say, with 20% foreign equity share) increases her capital by issuing shares in the local stock exchange. If all these new shares are bought by local investors, the company still is FIE (with higher equity capital, but lower foreign ownership share). However, the figures above indicate that FIEs increase in importance in comparison to DEs.

In the early period of transition, foreign investors were watched very carefully: everybody was eager to know what kind of role foreign owners will play as employers in TEs. This curiosity has not disappeared.

Table 9 Share of FIEs of Employment (%) (Manufacturing)

	1998	**2001**
Estonia	20,8	30,8
Czech Republic	19,2	34,1
Hungary	44,9	45,2
Poland	26,0	32,9
Slovakia	18,5	36,4
Slovenia	13,1	17,6
Romania	13,7	30,7

Source: WIIW

Also labour market figures show increasing influence of FIEs in TEs. The FIE share of employment has increased in every TE listed in the above table. The most dramatic growth rates can be observed in Romania and Slovakia. The Czech Republic is not far away from these two TEs: FIEs share has jumped 15% or more in these three TEs between 1998 and 2001. In both years of the table, Hungary has the highest figures: FIEs count roughly half of the manufacturing labour force. There is hardly any change in the Hungarian figures between 1998 and 2001. Slovenia has the lowest markings of the table in both years. Over 80% of work was provided by DEs in Slovenian industry in 2001. In very rough terms it can be maintained that FIEs employ approximately one third of manufacturing workers in TEs.

Table 10 FIEs Share of Investment (%) (Manufacturing)

	1998	2001
Estonia	N.A.	N.A.
Czech Republic	41,6	69,3
Hungary	78,7	77,9
Poland	51,0	64,0
Slovakia	50,1	73,1
Slovenia	24,3	22,4
Romania	35,6	57,8

Source: WIIW

FIEs have invested eagerly in TEs. The table on investment shows very strong growth rates between 1998 and 2001: the FIE share has increased over 20 percentage points in the Czech Republic, Slovakia, and Romania. The equivalent figure in Poland is 13%, while in Slovenia and Hungary, FIE share in investment was in 1998 very high (almost 80%) and still over three quarters of all investment in 2001. Slovenia's figures are clearly different: in 1998, FIEs made only about one quarter of all manufacturing investment; the equivalent figure in 2001 was even two percentage points lower. Estonian figures are not available.

Table 11 FIE Share in Sales (%) (Manufacturing)

	1998	2001
Estonia	28,2	36,7
Czech Republic	31,6	53,3
Hungary	70,0	72,5
Poland	40,0	52,0
Slovakia	36,2	59,3
Slovenia	24,4	29,3
Romania	24,2	48,9

Source: WIIW

The above table covers – so to speak – the market share competition between FIEs and DEs in TEs. FIEs had a very dominant position already in 1998 in the Hungarian manufacturing with a 70% overall market share, which in 2001 was even 2,5% higher. In the Czech Republic, Slovakia, and Romania, FIEs share in industrial sales has jumped by more than 20% from 1998 to 2001. The equivalent growth rate in Poland is over 10% and in Estonia less than 10%. Even in Slovenia, where FIE influence is rather modest overall, a 5% increase in sales share can be observed. However, FIEs have a market share of less than 30% in Slovenia.

Table 12 Share of FIEs in Export Sales (%) (Manufacturing)

	1998	2001
Estonia	35,2	48,5
Czech Republic	47,5	69,3
Hungary	85,9	87,9
Poland	52,3	66,2
Slovakia	59,0	74,9
Slovenia	32,9	36,8
Romania	22,4	23,9

Source: WIIW

FIEs in TEs have clearly an export orientation: the figures in the above table are higher than in the previous one. In every single country of the table, the export sales share of FIEs has increased between 1998 and 2001. Hungary has far the highest FIE figures in both years mentioned: her DE manufacturing sector produces at the beginning of the 21st century only about 12% of export sales. In comparison, domestic enterprises still produce about three quarters of manufacturing exportable in Romania. The equivalent figure in Slovenia is less than two thirds.

Some concluding remarks can be made on the basis of five above tables covering TEs manufacturing sector. FIE sector had already in the late 1990s a strong influence, which has been increasing lately. Hungary is in the lead in these figures: the impact of FIEs in her manufacturing is very strongly dominant. On the other side of the scale is Slovenia, the richest TE of the tables: FIEs have not been able to play a decisive role in her industry.

It can be assumed that foreign capital has essentially contributed to current account balancing in TEs: FIEs have obviously created plenty of import-substituting activities in TEs, and at the same time, FIE influence in increasing export competitiveness seems to be strong.

Table 10 shows high FIE shares in investments. This indicates that FIEs are more eager than DEs to renew, improve, and extend capacities. Therefore, it can be predicted that in the near future the relative market power (in comparison to DEs) will increase.

3 FDI Experience in TEs – Manufacturing and Service Sector

3.1 Car manufacturing in the TE-region

Automotive industry has been one of the backbones of the industrial development. For more than hundred years car-making has given employment for a big number of blue-collar workers in the rich part of the world. Car has become a means of transportation, but also a status-symbol – as well as a pillar of personal freedom in democratic society.

In the Cold War period communist policy-makers had one major goal: overall industrialization. Turning mainly agrarian societies into industrial ones demanded protectionism. Thus, foreign trade was a state monopoly in every CMEA-country. This protectionist system was supposed to help local “infant industries” to reach maturity, car manufacturing included.

In this context it is important to note that in the CMEA-region former Czechoslovakia was the only country with extensive industrial tradition. Naturally, the former East-Germany (GDR) was part of the industrialized world in pre-war Europe. However, that part of Germany was relatively rural in her economy. Some industrial units of East Germany, for example, Adam Opel car factory, was dismantled by the Soviets in the post-war period and removed to Moscow. Four decades this production line turned out Moskvitch cars, which were in fact Opel models of 1938!

Consumer satisfaction was a secondary issue in communist planning. Cars were available for personal use, but not easily available. Waiting time for a car was 5-10 years in communist economies. Car imports from the West were virtually prohibited – excluding luxury cars for communist elite.

It was obvious that all centrally planned economies had sellers’ market in car branch. The buyer had to decide beforehand what kind of a car he/she wants to have after the waiting time. Non-existent competition was not optimal from the point of view of quality. Western visitors coming by car were deeply envied by locals in Eastern bloc.

In the West, a very rapid consolidation of car manufacturing took place in the post-war decades. Japanese manufacturers turned car-markets in the USA and Western Europe upside down. Fierce competition created global oligopolistic market with an estimated overcapacity of 20% in the turn of the century. Improvement of quality and cost minimization became essential ingredients of the car-market game.

In the Cold War period, the Iron Curtain did not separate communist car market from the capitalist one completely. Marginal amounts of Eastern cars were sold in the West. It was allowed for West German citizens to give Western cars to their East German relatives as a gift. Mercedes and Volvo were used by high officials in the East.

Technology exchange in car manufacturing took place in communist era. The most spectacular case was the creation of Lada car manufacturing unit in Togliattigrad in the former Soviet Union. This huge factory was established with technical help of Italian Fiat, which licensed its car model. Licensed Fiat with the Lada brand appeared also in some Western markets – especially in Finland.

Fiat concluded a licensing deal also in communist Poland. Mini-car called Polski-Fiat was manufactured in massive scale. A medium-sized car called Polonez was also produced with Fiat license in communist Poland.

Renault (France) licensed one of her car models in the former Eastern bloc: Romanians produced Dacia cars with Renault's blueprint. This Romanian-made Renault had a good reputation in neighbouring communist markets.

Capital import in the communist east was not only an economic, but an ideological issue. In the communist parlance, the industrialized West was an arch-enemy aiming at global dominance via her "monopoly capital". Inviting Western MNCs to make FDIs in communist economies was not in line with communist orthodoxy, which maintained that internationally mobile capital is per definition exploiting workers in emerging markets.

However, centrally planned economies started to make compromises with the ideology in the 1970s. Romania and Hungary accepted FDIs in their respective territories. In both cases the original rules allowed the involvement of alien risk capital in joint ventures only. The local shareholders (the host-country state) were supposed to be the dominant partner in every mixed venture. Before the ultimate collapse of European communism mixed ventures between Western capitalists and communists states became possible (with the exception of German Democratic Republic). Western capitalists, however, were very reluctant to take risks involved in direct investment beyond the Iron Curtain. According to anecdotal evidence, a

Western car-maker was relatively close to conclude a mixed venture deal in Romania. No joint production unit was ever established.

Thus, Western know-how and capital had a very limited influence in Eastern car manufacturing branch in the Cold War period. As a result, car density remained on a very low level in the communist societies of Europe. It is not surprising that in the transitional period potential demand in TEs has continuously been on a high level.

Naturally, the wish to acquire modern cars in TEs can become true only through increasing income level. Nouveau rich class in TEs has been able to get luxury vehicles immediately. Many people with moderate income have in between bought second-hand cars, which are easily available in Western Europe. This has hampered sales of new cars in the TE-region.

Under present circumstances it can be predicted that demand for new cars in the TE-region will be high for several years to come, provided that overall economic growth will increase income level in the future. Convenient price-quality relationship can be assumed to be the focal point in purchase decisions. Thus, TE-region as an expanding production base in car manufacturing is not a futile dream.

In the present-day oligopolistic market of car-making, there are some basic rules of the game. One of them is called economies of scale. The capacity of every participant must be big enough to qualify to the group of the remaining few. In the 1990s, one of the newcomers was the car-making unit of South-Korean conglomerate Daewoo. It wanted to get a market share in the very competitive European car market and invested heavily in the TE-region. The operation failed and the car-making unit of Daewoo was acquired by General Motors. Kia was another Korean car manufacturer, who failed. Hyundai, also from Korea, acquired Kia.

In Great Britain, there are no independent car-makers left. Vauxhall is in the hands of GM, Jaguar is part of Ford, and in Sweden, SAAB belongs to GM, while Volvo car-making unit was acquired by Ford some years ago. SEAT in Spain belongs to Volkswagen. In Japan, Nissan is dominated by Renault, Mazda by Ford, Mitsubishi by Mercedes, Suzuki by GM, Honda and Toyota are independent. In the 1990, Chrysler – one of the “big three in America” – merged by Mercedes.

The list is not necessarily complete. The aim here is to demonstrate with rather simple facts that surviving in the global car market is not easy. Therefore, car manufacturing units in post-communist countries of the former Eastern bloc faced a stony road in the early 1990s: either to become internationally competitive independently, or get acquired by global players. A further option was naturally to exit the market.

Some interesting acquisitions have taken place in TEs car-making scene. Furthermore, TE-region has been able to attract several Greenfield investments in car manufacturing. Thus, the whole branch under review here shows an exciting trend in the early years of the 21st century.

3.1.1 Skoda-Volkswagen

Skoda Company belongs to the pioneers of European car industry. In 1895, two founders, V. Laurin and V. Klement started to produce bicycles in Mlada Boleslav, a small city about 100 km North-East from Prague, in that time Austro-Hungarian monarchy. A few years later, motorcycle production started. In early years of the 20th century, the company started producing cars.

In the aftermath of the First World War, the empire of Austria-Hungary was split, and Czechoslovakia became an independent state. In 1925, the company merged with Skoda Plzen with truck, bus, and agricultural machinery production departments. A separate joint stock company in car-making was created in 1930. In that decade, Skoda was successful in the international car market.

In the late 1940s, Czechoslovakia became communist. The company was transformed into a state-owned enterprise named AZNP Skoda, which in line with the communist economic model was the monopoly producer of passenger cars.

As mentioned above, former Czechoslovakia was clearly the most advanced country in terms of technology within the former Eastern bloc. Thus, Skoda had a convenient life in the communist time: a virtual monopoly in the local market and excellent prospects in the export sphere within Comecon.

Under circumstances of central planning, there was no urgent need to create new models and improve quality of the cars. However, in the communist period, Skoda was permanently regarded as the best “communist” car in the whole CMEA region, even if Skoda did not enter any technology exchange programme with Western companies, unlike Romanian Dacia, or “Polski Fiat” (with licensed production).

In the decades of the communist rule, Skoda sold part of its products in Western Europe, because the country was eager to earn hard currency. The reputation of Skoda brand was reasonable in the 1950s and 1960s, when cars in Europe were still in relatively short supply. After that, Skoda's role in the West was marginalized. The market share of Skoda in the late 1980s was a meagre 0,7%. The most important selling argument was the low price in the extremely competitive West-European market. In that period, Skoda produced 160.000-180.000 cars annually.

These are amazing figures. The company had long tradition and a reasonable brand image in the early years of communist period. However, car production was obviously not high in the priority list of central planners of Czechoslovakia. Both quantity increase and quality improvement were neglected in state-run Skoda. In plain language it can be stated that Skoda's international reputation was badly damaged in the communist era.

Therefore, after the systemic change of 1989, the state was facing a tough question: how to deal with Skoda – still the best-known industrial product of the country – in the new market circumstances. One option was naturally to keep "the family silver" (as Skoda was called in that time) in local ownership. A huge modernization package was in need in this scenario with high risks involved. The second obvious alternative was to sell Skoda to a potential Western strategic partner. The latter option was taken and international bidding was organized.

The most spectacular deal of the early post-communist period was made in 1991 when Volkswagen (Germany) acquired Skoda. In this deal, VW bought a 30% stake in Skoda for the equivalent of US $ 300 million and pledged to invest in the plant US $ 5 billion in the first ten years. In addition, it was agreed that VW's stake in Skoda would be gradually increased. Volkswagen promised to maintain the Skoda brand.

Naturally, this deal was widely discussed in media and in various seminars. In the Czech Republic (in 1991 Czechoslovakia still existed; in 1992 the federal state was split and the Czech Republic and Slovakia became independent states) many people were strongly against the deal. It is a well-known fact that the recent history in German-Czech relations is not a happy one. Many locals pointed out that half a century earlier the Germans occupied the Czech land by military force. In the 1990, the Germans were said to enter the neighbour with the deep pockets and buying the country, or her "family silver". Also the opposite argument was voiced: it was said that Skoda got a strong partner, who will be able to make the company competitive, and thus, contribute to Czech transition after decades of devastating communist rule. Several people mentioned that the long-term investment plan was the most decisive factor in acquisition competition. The asset price was of secondary importance. (The author has visited Skoda plant every year since 1992).

In the autumn of 1993, VW cancelled a major investment package in Skoda plant. Consternation and anger greeted the move to pull out of the US $ 0,7 billion plan hours before it was due to be signed in London. In a statement issued by VW it was said that enhanced productivity level meant that the planned investment programme could be scaled down. The investment package had been negotiated with an international banking consortium. Officially, banks involved did not comment on Skoda investment scheme. However, privately banking circles made it clear that institutions involved were seething (The European, 1993).

Volkswagen's withdrawal, made without prior warning to the Czech government, sent shockwaves through Prague and soured a relationship that had begun with high hopes. Volkswagen argued, however, that the revision of its plans for Skoda will enable the Czech unit to avoid the costly disasters that had beset SEAT, the group's Spanish subsidiary, which was pushed to the edge of financial collapse in 1993 by the combination of recession and overambitious investment plans.

In 1990, Volkswagen had just begun a ten year, Pta 600 bn (US $ 5 billion), investment programme at SEAT and presented its spending on the Spanish operation to the Czech government as a model for Skoda. In 1993 it became clear that the Spanish model was flawed. Huge losses at SEAT in 1993 helped to pull the whole of the VW group deep into the red (US $ 1,2 billion). Instead of a model, SEAT was cited by Volkswagen as a warning of the perils of profligate over-investment. (Handelsblatt, 1994).

After a long wrangling over the future of Skoda, the Czech government and Volkswagen declared peace at the end of 1994. Under a new agreement, the German auto giant was granted a 50,5% majority stake in Skoda in exchange for capital and production commitments. Investments in total value on DM 0,7 billion were agreed upon. Volkswagen's share rose to 70% in 1995. In the turn of the century VW became the sole shareholder of Skoda. In the 1990s, VW invested about US $ 2 billion in Skoda plant before acquiring the remaining 30% share of Czech car-maker.

In 1991, Skoda produced 170.000 cars. The equivalent figure in 1996 was already 263.000 – about 55% more than five years earlier.

Obviously, in the first decade of VW-Skoda co-operation certain aims were carefully set. The VW-group comprising VW, SEAT and Audi brands acquired Skoda as a cheap production base, in order to compete against cheap Asian models in the budget brand category. In this market segment, a relatively small Skoda Felicia was launched. The new mid-sized Skoda Octavia, placed on the same platform as other medium-sized vehicles of VW family, was mainly aiming at export markets with an advantageous price-quality relationship.

In every car manufacturing plant, economies of scale is one of the key points. In the 1990s, it was pointed out that in the medium term Skoda aims at annual capacity of half a million vehicles. Rationalization within the VW-group has caused sharing of major components such as chassis and engines.

Skoda Auto's annual report of 2004 celebrates the 100th anniversary of automotive production in Skoda plant. This report provides plenty of details of Skoda's development in the 21st century.

In the turn of the century, the name of small Skoda car was changed from Felicia to Fabia. A new luxury model "Superb" was launched in 2001. In both Fabia and Octavia, there are several varieties available.

Table 13 Skoda Deliveries by Model

	2000	2001	2002	2003	2004	Growth 2000-2004 (%)
Fabia *	276.900	295.941	262.641	260.988	247.600	-10,6
Octavia	158.503	164.134	164.017	165.635	181.683	14,6
Superb	-	177	16.867	23.135	22.392	-
Total	435.403	460.252	445.525	449.758	451.675	3,7

Source: Skoda annual report 2004
* In 2000-2001, Fabia and Felicia together, in 2002 Felicia was not produced anymore

In 2004, Skoda sold over 450.000 vehicles, which is almost three times more than in 1991, the year of signing the VW-Skoda acquisition deal. In the light of this growth, it can be maintained that the rescue operation of car manufacturing in the Czech Republic has been successful. In 2004, Skoda Auto was the biggest exporter of the country with 7,7% of total Czech export.

Some interesting changes in the internal structure of Skoda-making can be observed. The small model (Fabia, previously Felicia) had about ten percent less deliveries in 2004 than in 2000. At the same time, Octavia showed an increase of almost 15%. In 2004, production of

New Octavia started with about 40.000 vehicles. The Superb luxury car, production of which started in 2001, found about 22.400 clients in 2004. Thus, the production structure of Skoda moves relatively slowly from the small car-making to better quality direction.

Obviously, it is interesting to observe what the destinations of Skoda deliveries are. In this context, it is rather easy to assume that Skoda is a very popular brand in her home base, in the Czech market.

Table 14 Skoda Deliveries in Selected Countries/Market Share (%)

	2000	**2004**	**2000 (%)**	**2004 (%)**
Czech Republic	80.882	64.676	52,6	48,5
Slovakia	32.095	23.150	57,2	40,1
Poland	39.326	39.693	7,9	12,5
Hungary	7.707	17.350	5,3	8,2
Central Europe	**170.399**	**151.815**	**17,6**	**17,8**
Germany	65.219	78.051	1,9	2,4
France	12.053	13.013	0,6	0,7
United Kingdom	30.509	34.236	1,3	1,3
Italy	23.005	20.478	0,9	0,9
Spain	14.834	16.605	1,1	1,1
Austria	19.466	15.601	6,1	5,0
Denmark	5.921	8.362	5,3	6,9
Sweden	18.827	8.763	5,0	3,3
Western Europe	**229.109**	**240.672**	**1,5**	**1,7**

Source: Skoda annual report 2004

In 2000, about 81.000 Skodas were sold in the Czech Republic, which is almost 19% of overall deliveries. In 2004, the equivalent figures were 64.700 pieces and 14,3% of total sales. Skoda had a market share on her home ground over 50% (52,6%) in 2000, and less than half (48,5%) in 2004.

These figures show clearly that Skoda has an excellent position in the local market, even if the market share has slipped down a bit in the early years of the 21st century. This dominant position of Skoda is clearly visible on the streets of the Czech Republic.

However, Skoda Auto is predominantly an export-oriented operation from the point of view of Volkswagen. This point is obvious in the light of above figures: the local market takes about 15% of Skoda's total sales; the rest (85%) of vehicles produced by Skoda is exports.

Germany with her huge car market is the most important destination of Skoda cars with almost 80.000 units sold in 2004. Skoda's market share in this home country of VW is a rather modest figure of 2,4%, but in this context it is useful to bear in mind that German market is fiercely competed by all global players of car-making.

Occasionally, the term “cannibalism” is used in business studies. It means in the light of an example that a MNC acquires several brands, which compete with each others in the global market: Volswagen’s daughter, Skoda, eats up mother company’s market share. A cheap VW has become available in the West called Skoda. The market share of Skoda in Western Europe was a modest 1,7% in 2004, which means that Skoda is not a major brand in VW’s decisive market area (Western Europe).

In Central (Eastern) Europe, Skoda had a market share of almost 18% in 2004. This region comprises both parts of the former Czechoslovakia (the Czech Republic and Slovakia), as well as Poland and Hungary. In Slovakia, Skoda’s market share has decreased from no less than 57,2% in 2000 to 40,1% in 2004. In the same period, Polish figure has increased from 7,9% to 12,5%. Equivalent figures in Hungary were 5,3% and 8,2%, respectively. More than 150.000 Skoda cars were sold in these four TEs (altogether) in 2004.

Skoda Auto has some subsidiaries, which are mainly involved in selling Skodas in export markets. Skoda Auto Slovensko is a 100% Skoda owned daughter in neighbouring Slovakia, in Bratislava. Skoda Auto Polska is in Poznan, Poland. Skoda’s stake in this outlet is 51%. Skoda Auto Deutschland is active in Germany, and wholly owned by Skoda. Skoda Auto India Private Ltd. is 99,99% owned by Skoda: it is the only non-European subsidiary of Skoda.

Skoda’s annual report points out that the car manufacturing plant has a considerable spill-off effect on the local economy: Skoda has 20 key suppliers, 18 of which are from the Czech Republic, mostly situated in Mlada Boleslav (the home town of Skoda plant) and the surrounding area. The share of Czech suppliers in overall purchases of production materials has decreased from 67% to 63% between 2000 and 2004. However, at the same time Czech suppliers’ volume of sales to the entire Volkswagen group have increased strongly. No exact figures are mentioned in this context. Some hints are made on exchange rate hampering the Czech competitiveness. The Czech crown (koruna, CZK) appreciated rather strongly against euro in 2002. Some depreciation of CZK took place in 2003-2004, but the Czech currency remains “more expensive” than in 2000-2001.

Some main indicators can be picked up from the profit and loss account. In the first years of 21st century, Skoda has permanently been profitable.

Table 15 Selected Figures

Profit and loss account		2000	2001	2002	2003	2004
Production	vehicles	450.910	460.886	442.469	437.554	444.121
Employees (as at 31st December)	persons	25.833	24.129	23.470	22.798	24.561
Total revenues	CZK mln	136.283	153.271	145.694	145.197	153.550
Profit after taxation	CZK mln	3.336	2.129	1.825	1.478	3.497

Source: Skoda annual report 2004

Skoda's production has decreased slightly from the 2001 record level. The number of employees dropped clearly between 2000 and 2003, but recovered somewhat in 2004. Total revenue grew in 2001, but declined in 2002 and 2003 moderately. Some recovery took place in 2004.

This short overview of Skoda's activities in a five-year period does not tell a story of overwhelming dynamism, although net profits have been reasonable every year under review. Production and sales figures show a stagnant or even slightly decreasing tendency.

Skoda Auto is not the only substantial operation by Volkswagen in the former Czechoslovakia, which was divided in two parts in January 1st, 1993. The Czech Republic with about 10 million inhabitants inherited Skoda. Slovakia with about 5,4 million citizens was not regarded as a potential host of large-scale car manufacturing in the early period of transition.

Slovakia has not a similar, long tradition in industrial activities as the Czech part of the former two-state federation. In communist era, some commercial vehicle and car part production took place in automotive branch in the Slovak part of the formal federation. Thus, there was no Skoda equivalent available in Slovakia.

In the early period of Slovakian independence, the political situation was very unstable. The most powerful politician, Vladimir Meciar, and his party, Movement for a Democratic Slovakia (HZDS), were stamped as nationalistic and authoritarian by EU officials. When the first "shortlist" of the Eastern enlargement of EU was published, 5 out of 10 TEs were listed as potential new EU-members. Slovakia was relegated in that context in 1999, but became a Union member in 2004 alongside with 7 other TEs.

Thus, it can be maintained that Slovakia was regarded as a high risk country among Western investors in the 1990s. In the early years of the 21st century, Slovakia's reputation has improved essentially in the eyes of Western business people.

Volkswagen acquired a majority stake in Bratislava Automobile Plant (BAZ) in 1991, when Slovakia was still a part of former Czechoslovakia. BAZ was an important supplier of Skoda in the communist period. In 1995, the German company became the sole owner of BAZ in Slovakia. After this acquisition, BAZ became an assembly plant, building versions of the VW Golf from imported parts, but also made gearboxes and gearbox components.

In the early 1990s, VW moved all production of its 4-wheel drive Golf Synchro hatchbacks and estate cars for the European market from Germany to Slovakia. That was a part of VW's efforts to develop plants in TE to offset her high cost structure in Germany.

In the second half of the 1990s, BAZ began producing the new Passat B5, which was also manufactured in German plants. However, production units in Germany were unable to meet demand for this model. Instead of expanding capacity in Germany, production was partially shifted to Slovakia.

In 1996, VW established her second plant in Slovakia located at Nitra, 90 km east of Bratislava. This daughter company supplies car cabling systems to VW group.

Thus, it can be maintained that VW opted for a gradual entry in Slovakia with a clear off-shore strategy: VW production in Slovakia was in the 1990s exported almost entirely. Cost saving was the core of the operation.

After the BAZ acquisition, VW has invested about US $ 1,3 billion in her Bratislava plant. Currently, the labour-intensively manufactured off-road Touareg is its main product, but BAZ with a capacity of 300.000 vehicles a year also turns out VW Polo and Audi Q7. BAZ employs about 11.000 people, while its first-tier suppliers employ a workforce of more than 9.000. VW Slovakia is far the largest firm in the country with a turnover of US $ 5 billion a year and exports of US $ 4,5 billion – almost one quarter of national total. Thus, BAZ is from VW's point of view an export-oriented operation.

VW's Bratislava operation has caused considerable cumulative effects. In 1997, the total value of Slovak automotive supplies was less than US $ 0,5 billion. By 2003, it had increased by factor five to about US $ 2,5 billion, 60% of which was sold to VW's BAZ.

In the eyes of an outside observer, VW’s operation in Slovakia is spectacular: a modest car-parts producer in Bratislava has been turned into a large-scale car manufacturing unit in a bit more than a decade. This case is even more striking than VW’s acquisition of Skoda and its modernization.

The most important background factor in both VW cases under review here is labour cost. In this context, differences between TEs and Western Europe are remarkable (for details, see Tiusanen-Kinnunen-Kallela: “EU’s Enlargement Process: Investment Climate in 10 Transitional Economies”. Lappeenranta 2004, NORDI publication no.7). According to Business Week (European edition, 2005c), automotive labour costs are in Germany about € 30 per hour, some € 5 in the Czech Republic, and only € 3 in Slovakia.

These figures may give a partial explanation of the relative stagnation in Skoda development and expansion in BAZ. In TE-comparison, Slovakia with skilled and flexible labour is more advantageous for VW than the Czech Republic. Skoda’s market share in Slovakia is decreasing, as pointed out above.

Volkswagen’s activities in the former Czechoslovakia, which now is part of EU, have created a remarkable automotive industry cluster, which is in an expansion course. The fact, that BAZ is the most profitable of VW’s 42 factories worldwide is obviously noticed by competitors. Skoda acquisition has certainly not been a failure.

In the springtime 2002, it was announced that French car-maker PSA (Peugeot-Citroen) and Toyota (Japan) will jointly build a factory in Kolin, a Czech town of 30.000 inhabitants, not far from Skoda plant. In May 2005, the new factory with a capacity of 300.000 cars a year was inaugurated. This US $ 1,8 billion project will concentrate on mini-car production bearing brands of the co-owners. The plant employs 3.000 workers at the beginning of its operations. The price tag in the vehicles is said to be between US $ 7.000-8.000, below the price of the cheapest Skoda Fabia.

In 2003, PSA announced that it will construct a US $ 1,3 billion plant in Trnava, Slovakia, east of Bratislava with an annual output of 300.000 cars and a workforce of 3.000. This new capacity will start production in 2006.

Toyota is a well-known Japanese company with the highest volume in car-making among Japan’s giants. About a third of Toyota’s vehicles sold in Europe are assembled in EU area, at factories in France (Valencienne) and in Great Britain (Burnaston). This share will rise via Toyota's investment in the Czech Republic.

In the last decades of the 20th century, several South Korean car brands were launched in the European market. The Korean economy is traditionally dominated by conglomerates, many of which in the last decades of the previous century had big car-making units.

Daewoo car-making unit invested heavily in the TE-region. In 1999 this unit became insolvent and was taken over by General Motors (GM).

Kia is another Korean car brand, which failed, and was acquired by Hyundai (Korea), whose car-making business was established in 1967. The Hyundai Kia Automotive Group posted US $ 20 billion in sales in 2003. Hyundai vehicles were sold in 193 countries in 2003. Thus, Hyundai-Kia is a global player in vehicle manufacturing.

In early 2004, Hyundai announced that it will invest US $ 1,3 billion in a car plant in Zilina, another town in Western Slovakia. After going on-stream in 2006, the Kia plant will employ 2.400 workers manufacturing Kia's Sporting SUV. It is estimated that Kia's suppliers in Slovakia will employ some 4.000 people. The annual capacity will be 200.000-300.000 cars.

Renault (France) has established a new capacity of 200.000 cars a year in Nove Mesto, not far away from Slovakia's capital city, Bratislava.

In the early period of transition, the former Czechoslovakia produced about 170.000 cars a year. Skoda brand had a very marginal share in Western European car market, where the brand-name had a rather low prestige. In the middle of the first decade of the 21st century, the Czech Republic, together with her former federation partner, has a car-making capacity of about 2 million a year. Thus, the development in quantity and quality has been breathtaking.

3.1.2 Fiat in Poland

In the communist era, Poland had two car manufacturing units, FSM in Bielsko-Biala and FSO in Warsaw, both of which naturally were state-owned. As mentioned above, the Italian car-maker, Fiat, co-operated with Polish automotive sector in the period of central planning. Licensed Fiat mini-cars were produced in large scale in Poland, which in the days of the old system had a very low car density. Hardly any other cars but locally-made Fiats were visible on the streets and roads of Poland of the 1970s and 1980s.

Therefore, it was no wonder that one of the major acquisition deals in the early period of Polish transition was made in car-making branch: Fiat took over FSM in 1992 committing to invest US $ 1,4 billion in the 1990s in the Polish unit. According to anecdotal evidence Fiat had some (substantial) unpaid license fees in Poland originating from the communist period. Therefore, it is rumoured that Fiat's acquisition price was partly settled with these unpaid bills.

Obviously, one of Fiat's main reasons for investing in Poland was the country's low labour costs combined with workers' skills in making (licensed) Fiats. The market-seeking aspect of the Polish investment, however, should not be overlooked in Fiat's case. Poland is far the most populous (almost 40 million people) country in Central Eastern Europe with high potential demand for small cars.

Since early 1990s, Fiat's smallest car Seicento (600) is exclusively built in Poland serving the local market, as well as West European markets from there. Other Fiat models were after the FSM acquisition deal added to the Polish production rage. In the late 1990s, Fiat Poland employed 14.000 workers, and was the market leader on the local market.

In the springtime of 2000, it was announced that General Motors took a 20% stake in the car division of Fiat, which in return got GM shares worth US $ 2,4 billion. These two partners agreed to create two joint ventures: one to handle combined purchasing of materials and the other to jointly produce components and engines to be used by their respective car divisions in Europe and Latin America. This GM-Fiat deal included an option to sell the rest of Fiat's car-making unit to GM in 2004. This option was not used.

Fiat conglomerate, dominated by Agnelli family, has been in headlines in the financial press in the early years of the 21st century. Under new management, Fiat has sold various assets with the intention to concentrate on her traditional core business in automotive branch. In the car manufacturing, Fiat's traditional role is in small car business.

In 2003, 358.432 new cars were sold in Poland. Market leader was Fiat with 65.951 units sold (or 18,4% of total). Skoda was on the second place with 43.419 units (12,1%). According to Polish Voice (no. 55), sales of new cars in Poland dropped by about 10% to 318.111 units in 2004. This reduction in sales is said to be caused by increasing popularity of second-hand cars Polish travellers buy in Western Europe. The same publication (no. 51) states that only 11,7% of Polish-made cars reached domestic market in 2004. Fiat has a 60% share of circa 500.000

cars produced in Poland. More than 80% of Polish made Fiats are exported, primarily to Italy and other EU-countries.

Daewoo (South Korea) started its car sales in the early 1990s with the aim to conquer a reasonable share in Western Europe’s 15 million new car annual sales. The Korean company took control of FSO in Warsaw, the other major car-making unit in Poland. After this acquisition, the new owner promised to invest US $ 1,12 billion in the second half of the 1990s to upgrade FSO.

The Daewoo Group is a typical Korean conglomerate with about 20 divisions. During the South-East Asian financial crisis of 1997, Daewoo with a huge debt burden of US $ 50 billion was forced to carry out a radical restructuring plan. In the turn of the century, the car-making unit of Daewoo was sold to GM. In this acquisition deal, GM refused to rescue all foreign units of Daewoo car-making, among them FSO in Poland.

When Daewoo-FSO was established in 1996, Daewoo took a 70% in the new entity, the Polish Treasury 15% and the FSO employees another 15%. In the late 1990s, this unit turned out some 200.000 cars a year by a workforce of 3.000.

In September 2003, partners involved in Daewoo-FSO reached an agreement on restructuring of FSO, which helped to maintain car production on a lower level. The need to find a new strategic investor to rescue FSO became obvious. In the springtime of 2005, the Polish Finance Ministry announced that it may sell a 20% stake of FSO to Ukrainian car-maker AvtoZAZ (Warsaw Voice, 2005). Obviously, this potential investor is not a major player in the oligopolistic market of global car-making.

Opel is one of the oldest brands in German car-making, which was acquired by GM in the 1960s. For several decades, Opel has been GM’s major European operation.

In 1996, Opel decided to have a Greenfield investment in Gliwice, Southern Poland. This US $ 0,5 billion project went on-stream in 1998. It is considered to be Opels’s best factory in Europe. It is made up of modules, which can be freely expanded depending on market demand and can produce different Opel models, Agila, Astra and Zafira. The plant has a capacity of 180.000 vehicles a year.

In 2004-2005, GM announced that cost savings in European operations are necessary. In this context, it was made clear that the Polish unit provides about € 500-600 advantage per car in comparison to German Opel plants. The message is clear: German Opel plants and SAAB factories in Sweden have cost disadvantages in comparison to Central Eastern Europe.

3.1.3 Renault in Romania

Romania had probably the worst communist regime with a really catastrophic economic scene in the 1970s and 1980s. After the systemic change, economic reform in Romania has been rather slow. Thus, it was understandable, that Romania together with neighbouring Bulgaria were relegated in the Eastern enlargement of EU in 2004: these two TEs will be able to enter the Union with a delay, probably in 2007.

In the 1970s, Romania borrowed plenty of money from the international financial markets. The communist management was unable to create new manufactured exportables with the borrowed money. In the 1980 Romanian leadership decided to pay back the external debt by exporting mainly primary products. That strategy had devastating effects on the home market: even groceries were in short supply. Western companies had very little interest in dealing with this impoverished country. Romania was regarded as a poor relative by other communist countries.

However, in the Cold War period there was one Romanian product, which was appreciated in other Eastern bloc countries: Dacia car. Dacia plant became operational in 1968 and started to manufacture under license a local version of Renault 12 in Pitesti. Dacia employed nearly 30.000 workers to produce about 100.000 cars a year. This high labour input can probably be explained by self-sufficiency: Dacia had hardly any outside suppliers.

In the early period of Romanian transition, the state had the obvious aim to keep this large employer in state’s control. 49% of Dacia was privatized and shares were allocated to 350.000 small investors, Dacia’s employees among them. The state kept 51% of Dacia’s shares.

Obviously, this solution was very expensive from the point of view of local taxpayers. Outdated technology and a car model designed in the early 1960s were hardly right ingredients to make profits in the 1990s.

In the mid-1990s it became clear that Dacia cannot exist without a large injection of fresh capital. Several suitors came by, Renault and Peugeot from France and Hyundai from Korea. No deal with these potential investors was clinched. Dacia continued to produce a small number of cars with a high number of workers.

In the turn of the century Renault reappeared as a suitor, and an acquisition deal was signed. Obviously, the price paid by Renault was very moderate. Renault, the licensor in the Dacia deal of 1960s, bought her licensee.

After the signing of the acquisition deal, Renault spent some US $ 600 million to modernize and retool ailing Dacia. This modernization package was done almost entirely without robots: obviously, one of the main motives of Renault in the take-over of Dacia was to benefit from cheap Romanian labour. Gross pay for Dacia worker is about US $ 320 versus an average of US $ 4.700 in Western Europe (monthly pay).

In 2005, Dacia's new Logan model made headlines in the Western press. The large sensation in these headlines was the price: Renault has a € 5.000 tag on a car (see, e.g. Financial Times, June 9, 2005; Business Week, July 4, 2005). Dacia's new Logan is a roomy sedan, half the price of a comparable Western car. Renault's Logan adapted the platform used for its other small cars (Clio, Modus) and slashed the number of components by more than 50%. The dashboard is one continuous injection-moulded part, versus up to 30 pieces for a top-of-the-line Renault. Mirrors are symmetrical, and, thus, can be used on both sides of the car. Logan's windshields are flat, because curves result in more defects and increase costs. In summer 2005, Renault began delivering the roomy, five-seater to Western Europe (France, Germany, Spain). This version includes a passenger-side airbag and a 3-year warranty and has price tag of € 7.500. Logan in this form is still an extremely affordable mid-size-car, € 4.000-5.000 cheaper than SEAT Cordoba, Ford Focus and VW Golf.

According to Business Week, production costs for Logan are US $ 1.100 per car, less than half the US $ 2.500 estimate for an equivalent Western vehicle. Thus, Logan's basic model, stripped of costly design elements and superfluous technology, is targeted at emerging markets, Romania and other TEs included. Logan sales between September 2004 and May 2005, totalled 70.000, including 57.000 in Romania. The annual production target of Dacia plant is 175.000 cars, growing to one million by 2010.

In the news covering the Logan story there is one extremely interesting point: Renault sends a message to its French workers by investing in the TE-region. Automotive labour costs per hour are in France about € 28 in comparison to € 4 in Romania. Dacia's ambitious plan to produce one million Logans in 2010 obviously means that Renault's West European operations will not be expanded heavily in the second half of this decade.

It can be assumed that Renault will have some difficulties in overcoming Dacia's historical burden. In the communist era, Romania had the reputation of being the real backyard of Eastern bloc. Renault must find means to convince its Dacia buyers that cars made in Romania have a reasonable price-quality relationship.

Obviously, Dacia is facing the same problem in the local market, as all car-makers in TEs have: imports of second-hand cars from Western Europe. The extremely low price of Logan's basic model might offer a decisive advantage in the competition with old imported vehicles.

3.1.4 Suzuki in Hungary

In the communist era, Hungary had no car production in her territory. Ikarus busses and Raba trucks were produced in large scale in the Hungarian automotive industry. Cars were imported mainly from other centrally planned economies. Therefore, no acquisition deals were possible in car manufacturing branch in the early years of Hungarian transition.

Hungary started welcoming FDI immediately after the collapse of communism. Privatization was carried out extremely rapidly. Greenfield investment in Hungarian territory was supported by active measures: special tax advantage schemes and other perks were established to lure FDI, especially in manufacturing. Thus, it is no wonder that Hungary was the most successful TE in attracting MNCs with investment in the early period of transition. In this context, Hungary made it very clear that it was aiming at EU-membership as early as possible.

In car manufacturing, Hungary is neither able to offer experience, nor big internal market (with 10 million inhabitants). However, the Japanese car-maker, Suzuki, chose Hungary as a production base in the relatively early period of transition. GM has a 10% stake in Suzuki Motor.

This Japanese car-maker established a car assembling plant, Magyar Suzuki, in Hungary in 1992. The Hungarian state and IFC (the private capital outlet of the World Bank) became shareholders of this factory producing small cars called Swift. In 1993, the company suffered heavy losses because of devaluation of the Hungarian forint: imported car parts became essentially more expensive via depreciation of the local currency. Magyar Suzuki had to increase her equity, in order to survive. In the mid-1990s, this company produced about 40.000 cars a year, half of which were exported. Ten years later, Magyar Suzuki had an annual capacity of 150.000 cars. The use of local suppliers has increased considerably.

Audi is the upmarket brand of VW Group, which started producing car engines in Hungary in 1994. Audi's Hungarian daughter, Audi Hungaria Motor (AHM) started assembling certain Audi models to be exported. Audi's engine manufacturing in Hungary has grown rather rapidly. Car manufacturing capacity has increased to 55.000 cars a year. General Motors has some assembling and car part production via Opel in Hungary. Ford invested US $ 100 million in a car engine plant in Hungary.

In the early 1990s, Hungary seemed to have a promising start in creating a car manufacturing base from nothing via FDI. In the beginning of the 21st century it has become obvious that Hungary was unable to become a hub of car-making in the TE-region. In comparison to Slovakia and especially to Romania, Hungary has relatively high labour costs. The actual centre of car-making in post-communist Central Eastern Europe is the former Czechoslovakia.

Car component making is a US $ 160 billion business a year. This part of the car-making cluster is more labour intensive than the actual car-making. The labour content in the latter is about 15-20%, while the equivalent figure in the former is 30-40%. Thus, it is understandable that suppliers of car manufacturing companies have moved into the TE-region in herds.

3.1.5 BMW in Leipzig

VW Group is the biggest car-maker in Europe, while her German rival, BMW, is the most profitable one. This star of car-making was looking for a new production site in the turn of the century. It is a well-known fact that BMW considered several TE-locations seriously. In 2003 it was announced that the new BMW plant will be built in Leipzig, in the former communist East Germany (GDR). Newspapers did not save ink when headlines of this story were printed. Restructuring the area of the former German Democratic Republic has been a long and costly process, even if privatization of industrial assets was done very rapidly after the unification of two German states.

German's post-war history from partition to reunification is naturally an extremely complex issue, which cannot be dealt with here. It suffices to say here that all TEs in the former Eastern bloc have maintained their national currencies, every single one of which have been clearly undervalued under the new market conditions. In this respect GDR is an exception.

When GDR and the former West Germany merged in the early 1990s, also the currency units merged. After the "monetary union" of two Germanies it became impossible to improve East

German competitiveness via devaluations. Wages, prices, old age pensions, etc. increased rapidly close to West-German level in the former GDR, where productivity level was essentially lower than in the Western part of the country. Using East German labour under these circumstances became unfeasible in too many cases. Unemployment expanded extremely rapidly in the former GDR and remained permanently high causing increasing social costs.

When BMW's investment decision concerning Leipzig was announced, it was mentioned that the company receives public sector aid, which was justified by the local unemployment rate of over 20%. This help package of € 350 million was obviously an important background factor in the final investment decision.

BMW's € 1,3 billion factory in Leipzig, a rare case in West European car-making lately, went on-stream in 2005. This cutting edge plant full of robots equipped with lasers is able to check possible defects automatically. The plant full of latest technology employs 5.500 workers.

In the news covering the new miracle factory of BMW, flexibility is underlined. The extremely strong trade union (IG Metall) has agreed that the workweek can be 38 hours, compared with 35 in West German car plants. Saturdays work is allowed without extra pay. Depending on demand, BMW can run the facility as many as 140 hours a week without having to pay overtime, which cost in BMW's other units in Germany 50% extra (Handelsblatt, 2005).

The assembly line in Leipzig plant can handle any BMW's 10 models, allowing the company to react flexibly on demand fluctuations. The aim of the company is to have plants flexible enough to extend running hours without new investment. The new unit in Leipzig is a benchmark plant in European car-making (Business Week, 2005a).

BMW car is a symbol of German technology and workmanship: BMW cars are not selling by low price, but via luxury image and reliability. Therefore, it is understandable that BMW vehicles are designed and also manufactured in Germany: quality, not low price is the most important selling argument.

Obviously, BMW's Leipzig plant is a test case for West European car-making business. If it will be successful, it will become a model for other companies producing upmarket cars. If it fails to earn profit, car-making exodus from Western Europe will continue.

Western Europe produces plenty of luxury cars: Mercedes (Daimler-Chrysler), Alfa Romeo and Ferrari (Fiat), Jaguar and Volvo (Ford), SAAB (General Motors), Porsche, etc. The car-making landscape of Western Europe is thus not empty.

Car-making cases in TEs described above deal basically with mass-market vehicles with price-sensitivity. Fiat produces small cars with affordable price for the local Polish market, and also for export. Suzuki in Hungary is in the same market segment with a modest capacity. Daewoo entered Poland for cost reasons in her mini-car production, but failed. Renault's Dacia attempts to offer a roomy alternative with sensationally low price. VW's Skoda is producing her small model, Fabia, in massive scale, but the mid-size Octavia seems to grow in relative terms in Skoda plant. Peugeot and Toyota in the former Czechoslovakia seem to aim at producing small vehicles with price-sensitive demand.

VW Group turns out Audis on her Hungarian plant, in which capacity (55.000 a year) is rather modest. In this operation cost savings are obviously more important than local demand. The same company manufactures Touareg and Audi Q7 in its Slovak unit. Hyundai's Kia project in Slovakia with an annual capacity of 300.000 concentrates on Sportage SUV model: sport utility vehicles normally sell in the upmarket segment.

In the transitional markets of Central Eastern Europe, new car demand has been for several years rather disappointing: in this context, second-hand car market seems to be a disturbing factor. Import of used cars has naturally become more feasible for TE-citizens living in EU-area since 2004.

Therefore, car companies investing in Eastern part of Europe must have a carefully thought-over strategy for export business. Cost factors are naturally very convenient for this kind of activity in the TE-region. In this context, it is interesting to observe that Toyota, the most successful Japanese car-maker in Europe with a rather high market share, is not expanding production in Western, but in Eastern part of Europe.

The expansion of Central Eastern European car manufacturing has had very dynamic cumulative effect: suppliers of car parts have invested heavily in the TE-region, which now has a real car-making cluster. Cheap labour costs are appreciated by investors, who maintain that skill and motive to work are available in the TE-region.

It is self-evident that FDI-receiving countries are extremely satisfied with car manufacturing companies, who via local investment create productive working-places, increase the prestige of the local economy and contribute considerably to export activity, as well as import-substituting part of the local GDP. As pointed out above, FDI in this crucial industrial branch is not allocated evenly in the region under review.

3.2 Service Sector

3.2.1 Internationalization of Retail Trade

Fortune magazine publishes annually the list of 500 biggest companies in the world (according to revenues). The number one company is Wal-Mart with US $ 288 billion revenues in 2004. Wal-Mart employs 1,7 million people (Fortune, 2005). This American retailing giant was on the top of the list for the fourth year in a row. The same issue of Fortune carries a long story about Wal-Mart's first super centre in China, the country with the highest population in the globe. The American retailer plans to open 15 new units in China in the near future.

A couple of decades ago it was not predictable that a retailer will be on the top of the list of world's biggest companies. Oil and car companies alongside with financial institutions have traditionally dominated the list of giants.

Among sixty biggest units in the global ranking are further four retailers: Carrefour (France) on the 22nd place, Metro (Germany) with 42nd position, Royal Ahold (Netherlands), 49th and Tesco (UK), 54th. These super- and hypermarket retail chains replace traditional grocery stores and sell in large scale products of FMCG industry (fast moving consumer goods). There are estimates that 5 biggest customers (the biggest retailers) buy about one third of FMCG industry's products.

In the globalization process retailers selling "everyday products" are not the only ones, who have large-scale operations in the retail sector. Gab (USA), Hennes & Mauritz (Sweden) and Zara (Spain) have established fast-growing clothes chains. IKEA (Sweden) is selling furniture and house decoration items in her international network. Home Depot in "Do it yourself" (DIY) business replaces hundreds of iron mongers in the USA with its yearly turnover of over US $ 70 billion.

This list is incomplete: the aim here is to illustrate that retailers in a variety of branches grow bigger and more dominant. This trend seems to be still in a relatively early stage, but strengthening. Retailers have started their globalization drive with a delay (in comparison to manufacturing companies).

Some decades ago retailing and more generally distribution altogether, had an image of a simple, low prestige business. Textbooks on international business and teaching in this topic in academia paid attention to international operations of manufacturing enterprises and financial institutions. The development of retailing as a part of the globalization process was neglected or dealt with only marginally in the 1980s and still in the 1990s.

In the traditional perception, strong manufacturers with well-known brands organised their trade relations with small, vulnerable distribution partners using their superior coercive power over resellers in order to maximise their profits.

Presently, this concept is hopelessly outdated. Global consolidation in the retail sector means that the giants of super- and hypermarket chains have gained tremendous negotiation power and are ready to exploit it aggressively. One important point in this context is the demand by global retailers to get uniform worldwide prices from their suppliers. Thus, FMCG industries have the obvious need to develop globally competitive cross-border supply chains to cope with their oligopolistic customers (big retailers).

Obviously, FMCG manufacturers have several options to deal with the consolidating retail business. Producers with strong brands recognised widely in global market may look for partnership with global retailers. Locally strong brands may become globally known via this strategy.

Multinational consumer packaged-goods companies with rather weak brands may turn into private (own) label suppliers to global retailers. Private label business is a relatively new trick used by large retailers: the chain creates high-quality, low price alternatives to expensive branded goods. This strategy, which seems to have increasing application, exercises pressure on manufacturers. In more and more categories, own (private) label products of the retail chains are on offer putting pressure on the branded alternative price. Typically, the list price is subject to quantity discounts demanded by big retailers. If manufacturers of branded goods are unwilling to reduce the price, there is a high likelihood that the big retailers replace the product in question with private label alternative. Thus, producers are under increasing pressure via the consolidation process in retailing.

It is impossible to predict, whether this process will continue in the same manner, as in the last 10-15 years. Food and general merchandise retailers face local tastes and local habits. The mighty Wal-Mart set up some super centres in Indonesia in the 1990s, and pulled out some years later. Local shoppers preferred traditional open markets and small local shops, where they can haggle and buy local foodstuff fresh. Building trust and changing habits may take a long time in many emerging markets.

Yet multinational retailers have potential advantages, e.g., economies of scale affecting prices of an average consumer basket. Know-how in creating optimal supply chains with electronic links to suppliers seems to be a clear advantage of big multinational retailers. Therefore, the consolidation process of retailing business is not necessarily over yet.

Obviously, saturation of certain Western markets may drive big retailers to globalization. Wal-Mart acquired Asda, the second-biggest British supermarket chain for US $ 11 billion in 1999. Tesco, Britain's biggest retailer had rather little leeway for expansion in her home base after the arrival of the American behemoth. It can be assumed that Wal-Mart-Asda deal has speeded up Tesco's globalisation process.

In international retailing business, profit margins seem to be relatively modest because of oligopolistic market structure. Every big player must be ready to compete with price. In order to be able to offer competitive prices, every competitor must have a reasonable size: otherwise quantity discounts cannot be achieved in negotiations with important suppliers. Thus, newcomers in the global retailing game will not have an easy start.

Tesco is the fourth-biggest retailer in Europe. It entered the TE-region relatively early in the post-communist period with a clear vision of regional expansion. Therefore, this British company is selected as an example, how Western retailing is restructuring the post-communist business scene.

3.2.2 Retailing in Communism

The main aim in communist economies was the industrialisation of the economy. In the system of central planning, industry was divided in two "departments": department A was producing input goods and department B consumer goods. The former was continuously favoured in planning on the expense of the latter. Therefore, it was evident that there was a permanent shortage of consumer goods. Retail trade, as all other sectors of the economy, was dominated by state. Imbalances and shortages gave rise to many undesirable side-effects: corruption, bribery, under-the-counter sales, hoarding, disregarding of customer requirements, moonlighting.

Basically, all prices were centrally fixed. However, there was no guarantee that foodstuffs offered to a low price were available on the market. Therefore, in every country of central planning, there was a phenomenon known as "forced savings". People were forced to save part of their incomes, because supply did not satisfy demand. There was also something, which was called “forced substitution”. If a consumer wanted to have, e.g., mince meat for the weekend and could not find any at the market, but found some cheese instead, he/she bought a piece of it. That is what forced substitution under communist rule was all about.

It is not the aim here to cover the economic history of communism, which is a complicated issue. It suffices here to underline that the former system in the Eastern bloc was not advantageous for customers.

Retail trade in the communist bloc had one speciality hardly covered in the literature. Every centrally planned economy had a special retail chain called “hard currency shop”. The name of that retail unit was “Intershop” in East Germany, “Pevex” in Poland, “Tuzex” in the former Czechoslovakia, etc.

These special retail chains were originally created for Western visitors, who were able to get their chocolate, cigarettes, cognac, coffee etc. locally, but buying everything with Western money, with so called “hard currency”. Via these special shops, many Western FMCGs became known to locals.

All communist countries started printing their own “hard currencies”. This odd point means that local “currency shop coupons” started to appear to circulation. Part of the communist elite got their salaries paid in these vouchers or coupons, which were accepted as equivalent of US dollar or German mark. This system divided the population in two parts: those, who had access to Western consumer goods, and those who had not. Obviously, this kind of system is impossible in any democratic society.

The existence of local hard currency shops in communist countries partially explains the extremely dynamic black market of currency exchange. Citizens of every communist country offered about 5-10 times more for all hard currencies in comparison to official exchange rates. With Western banknotes thus acquired, local citizens had access to goods offered in hard currency shops. Part of these Western goods entered black market with considerable profit. With this unofficial – basically criminal – activity, Western consumer goods reached a large part of communist consumers. Forced savings were in large scale mobilized: accumulated local banknotes were exchanged for something valuable. Black-marketeers naturally became rich or extremely rich. In the 1980s, black market in every communist country was rampant.

However, every purchase on the black market was very expensive in the eyes of average income earner. Thus, in the early period of transition, there was a huge bent-up demand of all Western consumer goods.

In the first years of the 1990s, all transitional economies were suffering of a severe slump combined with high inflation rates. Purchasing power was on the low level.

The first period of post-communism was often called “bazaar capitalism”. Retailing took to the streets as kiosks, stalls and mobile markets started to appear. Western goods started to flow in via various channels.

Alongside with post-communist privatization, economic growth prospects improved already in the first half of the 1990s in some countries of the TE-region. Simultaneously, interest of Western investors in TE-countries increased. In that time, Western food and general-merchandise retailers faced saturated home market, and thus, started looking for options abroad. New opportunities in the post-communist Europe were seriously considered by several big retailers.

3.2.3 Tesco in Central Eastern Europe

In the communist era economies of Eastern Europe had some remarkable market experiments. A series of economic reform programmes were put on paper. Concrete results were in general terms very meagre.

In this respect, Hungary was an exception. In the very important reform period of the late 1960s, the former Czechoslovakia was invaded by Warsaw Pact troops stopping the reform scheme. At the same time, in 1968, Hungary was able to start her economic restructuring. Certain elements of the market were launched. This system with some liberal elements got the label “goulash communism”, because it improved everyday supplies dramatically.

It is not the aim here to cover details of goulash communism in Hungary. The crucial point here is that all potential investors entering central Eastern Europe from the West in the early 1990s knew that Hungary’s experiment with the market in the communist era gave a huge advantage to apply full-scale capitalism.

In the early period of transition, Hungary offered a second advantage for potential investors: all important assets were privatised as quickly as possible by selling them. All other CEEs applied a complicated system of “voucher privatisation”. This meant that citizens were given a certain amount of coupons, everyone of which could be invested in shares of newly privatised companies, or in some other objects with value. Many countries had a mixed system: some assets were sold, others given away free (via vouchers).

Therefore, it is no wonder that Hungary attracted more FDI than any other TE in the first half of the 1990s. One of the early substantial investments in transitional Hungary was made by Tesco, which took the acquisition route. This UK retailer developed already in the mid-1990s its regional vision for CEE (Hungary, Czech Republic, Slovakia, and Poland).

Tesco opened its first store in UK in 1929. In 2005, Tesco had 1.780 stores through 4 formats – Express, Metro, Superstore and Extra, employing over 250.000 in Great Britain. In the financial year 2004-2005 (ending February 25th, 2005), Tesco had overall sales of £ 37,1 billion, of which £ 27,1 billion in UK. Tesco is the biggest retailer in its home country (Tesco, 2005). In terms of euro, annual sales of Tesco are about € 55 billion.

Tesco defines its vision as follows: “The successful development of Tesco Stores is primarily based on a plain vision. We pride ourselves on selling high quality goods, improving the standard of services provided continuously, thus responding to customers’ needs. As far as the goods layout is concerned, Tesco Stores takes into account actual customer needs, thus offering a wide range of high quality goods for reasonable prices. The offer structure reflects a new lifestyle, stressing health and environment. These very two spheres are considered to have the key position, both in relation to the customers and to the employees and partners. Not only adhering to strict quality standards and to using environment saving technologies, but establishing long-term contacts with suppliers is emphasized as well”.

According to Financial Times (2005a), Tesco has not only size, but also quality: Tesco is the third most trusted brand in the UK, after Google and Nokia. With multiple ranges and an unparalleled spread of formats, as well as the largest online grocery sales in the world, Tesco has profited from the cash-rich, time-poor social situation in the UK. The same FT story points out, that Tesco’s distribution system is unique in terms of speed and efficiency and its selling techniques set it apart from its competitors. It is maintained that Wal-Mart is a great buyer, but Tesco is a great seller. Tesco is offering relative price stability – even at competitive prices – whereas its rivals’ prices fluctuate more.

However, Tesco is said to be relatively slow in her international operations: only one fifth of its sales comes from overseas operations, while the equivalent share in Carrefour is 50%

(Carrefour from France is the biggest retailer in Europe with 2004 revenues of US $ 90 billion). Tesco studies new markets carefully before entering them.

Tesco started its TE-region operation in 1995 by acquiring Global, a state-owned supermarket chain in Hungary with 43 operating units for the cost of building one hypermarket in the UK. After this acquisition, all existing Global's outlets have been refitted and converted to the Tesco fascia.

Simultaneously with this takeover operation, Tesco did its first Greenfield operation in Hungary. The first purpose-built Tesco supermarket of 12.000 sq meters opened in the Western Hungary, in Szombathely, in the mid-1990s.

In the early 1990s, internationally active developers entered Central Eastern Europe and started changing the commercial architecture of the region. One of the very first monuments of this activity is Polus Centre in Budapest. This American style shopping mall is located in north-eastern suburb to M3 highway with fast access to downtown of the capital city.

Polus Centre comprises over 140.000 sq meters with 52.000 sq meter of retail floor space, an entertainment complex with several cinemas, an indoor ice-skating rink, several restaurants, etc. Tesco reserved 8.200 sq meter floor space for her superstore within this first shopping mall miracle in post-communist world, which opened its gates in 1996.

Amid its expanding retail operation in Hungary, Tesco built a large distribution centre of 430.000 sq feet and a 225.000 sq feet fresh food distribution centre with radio frequency technology instead of paper to keep track of products and sort orders. This fresh food centre now accounts for over 95% of the volume of the fresh food in Tesco's Hungarian business. According to Tesco's Annual Report (2005), the company is boosting her own-brand items in Hungary, including over 400 value products, more than 1.000 standard own-brands and 60 Fitt healthy-living products.

After establishing itself in Hungary, Tesco entered Poland, also via an acquisition. The target in Poland was Savia, a privately owned supermarket chain with 36 outlets in ten principal towns of southern Poland with relatively high living-standard (in comparison to Polish average). Two entrepreneurs, who had established Savia, were hired as executives. However, the CEO came from the UK.

Tesco's outlets acquired from Savia represent "neighbourhood" supermarkets well located for local shopping. The first Tesco superstore in Poland was opened in 1998. In 2002, Tesco acquired HIT, a Polish hypermarket chain with 13 stores. In the first years of the 21st century, Tesco has built two distribution centres in Poland handling 95% of Tesco's overall volume.

One of the big sensations of the very early transition was Kmart's (USA) arrival at the former Czechoslovakia. In the early 1990s Kmart was one of the really big retailers in the USA. This giant bought outlets in Prague and Bratislava.

After a period of rapid expansion, Kmart started losing ground in its home market, and thus, sold assets abroad. In this context, Tesco bought Kmart's stores in both Prague and Bratislava, which in between had become capital cities of new nations, Prague in the Czech Republic and Bratislava in Slovakia. The total portfolio thus acquired by Tesco contained 13 stores, 6 in the Czech side, and seven on the Slovak territory. The combined sales area was about 90.000 sq meters.

Presently, Tesco operates 25 stores employing 8.000 people in the Czech Republic. Also in the Czech case, the strengthening of Tesco's own-brand range is underlined: 1.500 value lines and 1.600 standard own-brand lines are launched.

In the neighbouring Slovakia, Tesco employs 7.000 in 30 stores. Tesco's Annual Report (2005) contains the following remark concerning Slovakia: "We extended our value and own-brand lines by 1.100 and 1.050 respectively and our business was named 'Top Retailer for 2004' by the Association of Trade in Slovakia."

In the light of 2003 figures (Retail Trends for Emerging Europe, PMR Ltd, 2004), Tesco is not in the top position in Poland, Hungary and the Czech Republic.

Table 16 Top Ten Retailers in Poland, 2003

Position	Company	Origin	Turnover 2003 in mln EURO
1	Metro Polska	Metro/D	2.629
2	Jerónimo Martins Dystrybucja Polska Sp.z.o.o	Jeronimo Martins/P*	964
3	Tesco Polska Sp.z.o.o.	Tesco/UK	960
4	Auchan Polska Sp.z.o.o	Auchan/F	887
5	Ruch SA	PL*	825
6	Carrefour Polska Sp.z.o.o.	Carrefour/F	819
7	Géant Polska Sp.z.o.o.	Casino/F	751
8	Rewe Sp.z.o.o.	Rewe/D	572
9	Ahold Polska Sp.z.o.o.	Ahold/NL	561
10	Plus Discount Sp.z.o.o.	Tengelmann/D	489
11	Milo S.A.	Lekkerland /D/PL	496

Source: PMR Ltd, 2004
* P=Portugal, PL=Poland

Table 17 Top Ten Retailers in the Czech Republic, 2003

Position	Company	Origin	Turnover 2002 in mln EURO
1	Makro CR	Metro/Germany	1.051
2	Ahold Czech Republic a.s.	Ahold/Netherlands	992
3	Kaufland v.o.s. CR	Schwarz/Germany	750
4	Skupina Rewe	Rewe/Germany	690
5	Tesco Stores CR, a.s	Tesco/UK	605
6	Skupina Tengelmann	Telgelmann/Germany	525
7	Globus CR k.s.	Globus/Germany	508
8	Carrefour CR	Carrefour/France	360
9	Delvita a.s.	Delhaize Groupe /Belgium	344
10	Spar Ceska obchodni spolecnost s.r.o.	Spar/Austria	266

Source: PMR Ltd, 2004

Table 18 Top Ten Retailers in Hungary, 2003

Position	Company	Origin	Turnover in mln EURO
1	Metspa Supply and Trade Co.Ltd	Metro/Germany, Spar/Austria	1.613
2	CBA Kereskedelmi Kft.	Hungary	1.597
3	Tesco-Global Aruhazak Rt.	Tesco/UK	1.397
4	CO-OP Hungary Rt.	Hungary	1.321
5	Provera	Cora/France, Louis Delhaize/Belgium	0.843
6	Reá Hungária Elelmiszer Rt.	Hungary	0.754
7	Tengelmann Csoport	Tengelmann/Germany	0.688
8	Auchan Magyarország Kft.	Auchan/France	0.611
9	Rewe Csoport	Rewe/Germany	0.532
10	Honiker Kft.	Hungary	0.517

Source: PMR Ltd, 2004

Metro is the biggest German retailer, which is ahead of Tesco in Fortune's list of 500 largest global companies. This German giant is very clearly in the leading position among Poland's retailers with a turnover of about € 2,6 billion. On the second place is Jeronimo Martins from Portugal with a turnover of under € 1 billion. Tesco is very close to that Portuguese rival on the third place.

In Hungary, Metro in alliance with Austrian Spar is number one retailer with € 1,6 billion, followed by the Hungarian CBA chain. Tesco is in the third place, not far from the top (€ 1,4 billion turnover). Also in the Czech Republic, Metro is on the top of the list, followed by Ahold (Netherlands), which is the third biggest retailer in Europe (after Carrefour and Metro). Schwarz and Rewe (both Germany) are ahead of Tesco in the Czech retailing competition.

The most remarkable detail in the three tables above is that international players dominate the scene in TE-retailing in the second decade of post-communism. In the Czech table, there are no local competitors left in the top ten list. In Poland, there is only one, while the equivalent figure in Hungary is four. It is interesting to watch in the near future, whether the remaining local competitors will be swallowed by German, British, Dutch, or French international giants. It can be assumed that the consolidation of retail business in the TE-region is not over yet.

The biggest country under review, Poland, with almost 40 million inhabitants is relatively underserved by hypermarkets and supermarkets, which account for only 35-40% of its food and personal care market (AC Nielsen, retail research firm). The equivalent figure in the Czech Republic is 60%. Moreover, the sector is still fragmented in Poland with the top ten chains accounting for only one quarter of the market, far below the 87% and 83% shares in Germany and Spain, respectively.

The Economist (2005) covers a story on Polish retailing, in which low prices and abundant supplies offered by foreign companies are appreciated by local clients. However, international retailers have come under five from an alliance of small shopkeepers, populist politicians and unhappy workers. The core of the article is as follows:

Ms. Lopacka, an ex-manager of a Biedronka discount store in northern Poland owned by Portugal's Jerónimo Martins, is suing her former employer for 2.600 hours of unpaid overtime. Having formed the "Association of Victims of Jerónimo Martins" – which aims to "fight the system of abuse" by large retailers – she has become the poster child for employees who claim they are poorly paid and overworked.

Under pressure, Biedronka has become more attentive to its employees, investing 10 million zloty (US $ 3,1 million) in recent months in new equipment and training. It even awarded workers a 20% pay rise. Yet the firm claims that it is being unfairly singled out because of its sprawling network of 730 stores in over 400 Polish towns, many of them in depressed regions of the country. "In some of these places, half the people are jobless and the other half work for us" says Anna Sierpinska, Biedronka's communications chief.

All international retailers active in the TE-region emphasize the positive labour market effect. Tesco employs about 50.000 people in four TEs under review. At the same time, local supplies are underlined, especially in the fresh food segment. Tesco points out that some 95% of this group of goods come from local sources. Thus, there are considerable spill-off effects caused by international retailers who have modernized the sector on very short period of time. Naturally, this restructuring process has swallowed plenty of capital which had not been available from local sources only. Cheap prices are directly linked with efficiency.

It is obvious that manufacturing FDIs in the TE-region contain less emotion than service sector equivalents. Greenfield investment in concrete production normally creates new, well-paid working places. In acquisitions the situation is not necessarily the same: in many cases, ailing industries have been rescued by foreign investors. Restructuring normally means making part of the existing workforce redundant. This is in many cases not emotionally acceptable.

In the retailing sector, small shops, kiosks and bazaars were created with enormous speed in the early period of transition. In this sector, international competitors with their big units drove many local entrepreneurs of the early days of post-communism out of business. Some local retailers (as shown in table 18) have been successful in the intensifying competition – especially in Hungary. However, this seems to be more the exception than the rule.

In the retailing circumstances of the second decade post-communism, economies of scale is necessary. In order to achieve competitive size, capital is needed. Newcomers will realize that there is a high “entry fee”: start-up capital is difficult to find. Therefore, it can be assumed that the further consolidation of the retail business in the TE-region will take place with further involvement of external money.

Tesco’s Annual Report (2005) contains a five-year record which shows that group sales increased by 64% between 2001 and 2005. In that period Rest of Europe turnover (excluding VAT) more than doubled (120% growth). This position covers the Republic of Ireland and Turkey. However, it can be assumed that dynamism in this position reflects the rapid growth in TEs under review. However, in the same period, operations in Asia increased threefold. UK’s share of turnover in 2001 was 80,6%, while the equivalent figure in 2005 was 73,2%. Thus, globalisation of Tesco advances, but not with enormous speed.

Tesco underlines in its Annual Report the expansion of own-label products in her Central Eastern European operations. Obviously, price is a very decisive factor in retail competition in TEs. Own-label products are an important element in catching long-term clients with price consciousness in a region, where purchasing power is more limited than in Western Europe. Tesco itself is a valuable brand, as pointed out above.

4 Conclusions

In 1989, centrally planned economic system collapsed in the former Eastern bloc. Systemic change in the former Soviet Union took place with a delay, in 1991.

In the early period of transition, all post-communist economies suffered a severe slump. At the same time, foreign trade regime was essentially liberalized. Western consumer goods started flowing in, but people in the TE-region had rather low purchasing power to buy Western goods they had been waiting for decades. Bent-up demand was obvious: several Western firms started to create a foothold in the TE-region because of the new potential offered by post-communist consumers.

FDIs started to flow rather rapidly toward the TE-region in the early 1990s. In manufacturing low wages for experienced workers was an obvious attraction for potential investors.

Relatively soon Western investors in the service sector became interested in restructuring TEs. Banking sector in TEs badly needed modernization. Thus, it is no wonder that financial mediation has attracted big movement of FDI-money from the West to the East. Telecom branch was in the TE-region badly outdated. Large-scale investment has been done by Western telecom operators with interest in the TE-region. In retail trade, Western giants started to regard post-communist societies as virgin land full of long-term prospects. Invasion in this branch started to take shape already in the first half of the 1990s.

Opinion polls were hardly made in communist societies. After the systemic change, Western social scientists entered the TE-region. Also market research companies got interested in new opportunities in post-communist area. Numerous studies made in the early 1990s showed that almost all citizens in the TE-region had the dream to get a car of Western quality. Therefore, it is not an accident that car manufacturers discovered new opportunities in formerly communist countries. Volkswagen, Europe’s largest car-maker, became a pioneer in investing in the TE-region.

– VW acquired Skoda (in the former Czechoslovakia) with a relatively modest price. It is assumed that VW’s investment plan was the most decisive factor in the Skoda deal. Skoda brand has been maintained, even though the German company is the sole owner of Skoda. There is anecdotal evidence that VW agreed to keep the Czech name of her daughter company in the Czech Republic. In Skoda’s marketing efforts, it is not mentioned that the brand is part of VW Group. It can be assumed that the majority of Skoda's potential customers know that Skoda is actually Volkswagen which can be acquired to a relatively low price.

- In the early period of transition, VW entered also Slovakia via acquisition. In Slovakia VW produces Volkswagens (no local brand is involved). VW's Slovakian operation has expanded rapidly.

- In both cases (in the Czech Republic and Slovakia), VW's FDIs are mainly supply-oriented: export of cars is the main business. VW's Skoda in the Czech Republic is the most important company in the national economy. The relative importance of VW in Slovakia is even much higher for the local economy.

- In car manufacturing, labour cost differences between the East and the West are continuously striking. In Slovakia, workers earn less than their colleagues in Skoda plant. VW is partially owned by the public sector (the German State of Lower Saxony has a 20% stake). Therefore, the company must pay special attention to German labour market: all operations cannot be moved to the TE-region. VW is the main investor in car branch in the TE-region, but not the only one. The branch has shown extreme dynamism in the TE-region lately.

- Poland has not been too lucky in her efforts to restructure automotive industry. Fiat's operation in Poland seems to bee on a healthy basis, but the mother company is struggling in the tough global car market. The other investor on Polish car market went bust (Daewoo). On the long run a new strong strategic investor is in need. GM has entered the Polish market in slow motion. The company seems to restructure her European operations, while production in Poland gives a clear sign to GM's plants in Western Europe: costs must be cut, or the Polish operation will be expanded. Peugeot and Toyota established a JV in the Czech Republic. The aim is to get cost advantages in the main mini-car market. Toyota invested in Slovakia as well. For this strong Japanese company it is essential to be cost-effective within EU-market. Hyundai (and other Korean companies) have not been too successful in the European car market. For the company, which is competing in the price-sensitive segment, it is essential to minimize labour costs. Thus, Hyundai invested in Slovakia, which is now the most important hub of car-making in the TE-region. Renault has shown impressive results in the last ten years. The company was not in a hurry to acquire her former licensee, but got it obviously advantageously after a trial and error game by Romanian state.

A dramatic change of the retailing sector is under way in the TE-region. In the communist era, the sector was badly neglected. Therefore, in the early period of transition, a multitude of small private shops started to emerge in all TEs in the early 1990s. Very soon big western retailers, who suffer from saturated traditional markets, started to invade the TE-region with their deep pockets and very competitive business schemes.

Therefore, a real retailing revolution has taken place in the TE-region in a very short period of time. In the rapidly growing economies of Central Eastern Europe, purchasing power is still limited in Western comparison. Price is an extremely important tool in retail competition. In order to be competitive, the winners must have economies of scale, and an efficient storing and distributor system. Therefore, the sector started to consolidate already in the 1990s in the richest TEs.

- Tesco is the biggest retailer in her home base, Great Britain, with an extremely sophisticated market. In 1990 Wal-Mart, the biggest retailer in the world, acquired Asda, a big British retailer. This single deal aggravated competition in the mature British market. Therefore, Tesco has been forced to seek opportunities overseas.

- Tesco entered the TE-region in the relatively early period of transition. In this context, the British company decided to invade several TEs simultaneously (the Czech Republic, Slovakia, Hungary, and Poland). This strategy obviously brings economies of scale. In the TE-region, Tesco has used both acquisitions and Greenfield investment. The ultimate aim of Tesco’s TE-operations is to advance its own concept and image.Central Eastern Europe is not the only target of Tesco’s internationalization strategy: the company has presence also in some Asian locations.

- In 2005, it was announced that Carrefour, the French retailer, gave up its operations in the Czech Republic and Slovakia via an asset swap with Tesco. The latter received in this deal Carrefour’s 11 outlets in the Czech Republic and 4 stores in Slovakia valued at € 190 million. In exchange, Carrefour received Tesco’s 6 stores and 2 sites in Taiwan, worth € 132 million. This deal makes Tesco the leading retailer on the Slovak market and the fourth largest in the Czech Republic. After this extremely interesting asset swap between the biggest European retailer (Carrefour) and the fourth one, Tesco essentially strengthened her position in the TE-region. However, in CEE-group of countries (Poland, Hungary, Slovakia, the Czech Republic), Tesco is still behind Metro, her German competitor (the second biggest European retailer after Carrefour).

– The Dutch retail giant Ahold (the third in Europe) bought in the summer 2005 no less than 56 supermarkets in the Czech Republic from the Austrian retailer Julius Meinl. However, Ahold has not as strong position in other CEE-countries as Tesco and Metro.

– In the second half of this decade, the retail market of CEE-region has a high level of consolidation. Metro, Tesco and Ahold dominate the scene after Carrefour's withdrawal from the region. Obviously, these three European competitors are watching Wal-Mart's intentions carefully. In 2005, Wal-Mart opened 15 outlets in China. It may, or may not, mean that the real giant of global retailing is about to enter the CEE-region.

– In the region under review, there are some strong contenders present, e.g., Rewe, Tengelmann, Schwarz Group (all from Germany), Auchen, Delhaize (France). Some TE-retailers, especially Hungarian ones, have grown rather large in TEs. Therefore, competition in the TE retailing market still continues. Potential newcomers will not have an easy start. Continuous competition is good news for local consumers. Retailers must watch their prices carefully. Not even the Big Three (Metro, Tesco, Ahold) have a monopoly position in the CEE-region allowing skimming in price-setting.

Western car-making in the CEE-region has revolutionized one of the most important manufacturing branches. In this revolution, relatively low wage has been a crucial element. Development in retailing has transformed post-communist countries in an extremely visible way.

FDI in manufacturing is appreciated by citizens of TEs, while retail FDI is facing mixed feelings. In the former case, foreign input has brought in clean and well-paid working places. In watching retail sector development, many locals in TEs have got the feeling that foreign invaders have brought in their know-how, but also the merchandise on offer from the West. Local retailers and producers are suffocated by international companies. However, prices offered by big super- and hypermarkets are appreciated. In actual fact, an increasing share of goods on offer on the shelves of the foreign retailers is produced locally.

However, local (TE) production of everyday products must be rational and often made in highly automated plants. Therefore, local unemployment in TEs is presently high or even very high. Thus, transformation in post-communist countries has positive and negative aspects. This is a fact no investor in TEs can ignore.

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