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## Czech FDI Performance: Between Global Value Chains and Domestic Reforms

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### Introduction

The Czech Republic had attracted significant amounts of FDI during its transition process. Investors benefited from the country's stable political and economic environment, the above-average pace of its transition process, as well as its geographic proximity to EU markets. Even though the Czech Republic showed a relatively reserved attitude towards foreign direct investment during initial stages of its transition, investors soon found their way to the country. Besides the benefits that FDI usually brings, the Czech Republic soon started to pay attention to the harm that these flows can cause, namely, the negative impacts which large-scale profit repatriation has on the current account, as well as limited value added in production for exports—both clearly linked to problems with national competitiveness and the business environment.

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Foreign direct investment fulfilled an important role in the country's transition process, namely, as "an important source of financing and supplement of inadequate resources to finance both ownership structure and capital formation. Compared to other financing options, FDI also facilitates transfer of technology, know-how and skills, and helps local enterprises to expand into foreign markets" (EBRD 2001, 1). The main determinants of FDI in the transition countries of the Central and Eastern European (CEE) region, which include domestic and potential export market size, gravity factors, resources or skills endowment, progress in transition reforms and economic and political factors, were especially favourable in the case of the Czech Republic. As a result, together with its peers among the Visegrad Four (V4) countries, the Czech Republic has attracted the majority of FDI flowing into the CEE region in the initial stages of economic transition. If measured by share of gross capital formation or by FDI inflow per capita, it was the Czech Republic which attracted the highest relative amount of FDI in comparison to other V4 countries.

Both privatisation and restructuring processes markedly influenced the structure of inward FDI flows in the Czech Republic. Even though the country started with the highest share of state-owned enterprises among the V4 countries, the speed of its transition (namely, in terms of small-scale privatisation) soon outperformed the others. Gravity factors and skilled labour eased the country's restructuring towards a more modern service-based economy, which was soon reflected in the structure of FDI inflows. Since 1995, FDI inflows into manufacturing industries have accounted for less than a half of the total. Within industry, the chemical industry (from 5% to almost 20% of annual FDI inflows), and the food processing and tobacco industries (from 14% to 63% of annual FDI inflows) played the most significant role. Most FDIs were however attracted by services: namely, financial services (more than a third of non-manufacturing FDI) and tourism.

The aim of this chapter is to analyse the flows and stocks of FDI in the Czech Republic, with special regard to post-2000 period, and identify potential structural or trend breaks connected to the global financial and debt crisis. The chapter will briefly identify the main drivers of the FDI during the Czech Republic's transition process (1993–1999), followed by an analysis of more recent developments, that is, those where EU

accession and financial globalisation are seen as the main drivers (2000–2012). After identifying whether Czech FDI inflows exhibit a major structural shift after the crisis or not, the paper will focus on disaggregating FDI by source countries. First, it examines “traditional” FDI from OECD countries, which are driven mainly by value added, value chains, and where the negative effects of profit repatriation played a significant role. Since the global crisis, the role of the BRICS countries (Brazil, Russia, India, China and South Africa) as outward investors has been increasingly prominent, and the second part of the chapter explores their increasing significance in Czech FDI inflows. The role of these countries in CEE FDI processes has not been thoroughly studied yet and will serve as a case study of a potential shift in the regional structure of the Czech FDI inflows.

Unless otherwise stated, data cited in the chapter on FDI flows and stock, and their geographical and industrial breakdown, are from UNCTAD and the Czech National Bank, and are mostly measured in USD or EUR in current exchange rates and prices. Some more detailed regional data however is only available in Czech crowns.

## Investment Performance of the Czech Republic

Developed countries clearly dominated FDI inflows into the Czech Republic between 1993 and 1999. Due to geographical proximity and anticipated accession to the EU, other EU countries have accounted for more than 80% of FDI inflows during the transition period. Germany (20.6% of FDI flows in 1999) and the Netherlands (17.9% in 1999) were by far the most important sources of Czech FDI inflows. Significant US participation in large FDI inflows is only connected with privatisation projects in the early 1990s; since then, FDI from the United States has not played an important role in the Czech Republic, and the US investors have been focusing on larger transition countries, such as Russia (34% in 2000) (UNCTAD 2003, 9). Also, Asian investors were clearly underrepresented in the Czech Republic between 1993 and 1999, as they were in the rest of the transition region; although, Japan and Korea have carried out some important acquisitions (Table 3.1).

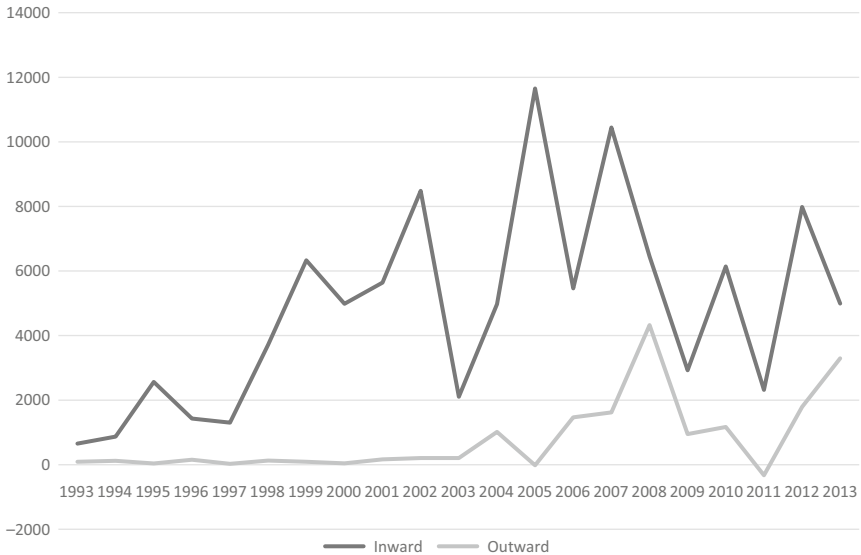
**Table 3.1** Czech inward FDI flows by home country, 1993–2012 (in percentage)

Country	1993	1995	1997	1999	2000	2004	2007	2012
Western Europe								
Belgium	4.9	1.0	4.3	21.8	1.1	...	2.6	7.7
Denmark	0.3	0.5	0.2	0.7	2.1	...	2.2	1.0
France	5.2	6.6	7.8	3.7	4.7	...	0.5	3.7
Germany	12.5	22.1	30.1	20.6	26.5	15.2	11.5	15.5
United Kingdom	0.0	2.1	15.1	1.6	3.2	0.4	...	1.9
Italy	1.8	0.0	-2.8	0.7	0.7	1.0	0.5	1.2
Netherlands	4.6	28.7	10.3	17.9	20.8	40.2	21.2	43.1
Austria	8.4	3.4	7.3	13.2	14.8	8.8	10.5	13.0
Switzerland	2.1	26.5	3.6	5.6	4.6	3.7	9.3	3.2
Canada	3.1	0.0	0.0	0.2	3.1	...	0.2	...
United States	39.0	3.9	7.6	9.2	6.1	10.2	4.0	5.0
Japan	0.0	0.0	0.8	0.1	0.9	0.8	3.9	...
Other	16.2	4.3	8.7	2.8	8.6	28.3	35.4	5.7

Source: Calculations of the authors, based on CNB (2013)

Figure 3.1 suggests that the inward FDI flows markedly increased after the main components of the transition process were completed. By the late 1990s however, FDI inflows into the Czech Republic were limited by a postponed banking sector privatisation. Significant FDI inflows were also later connected with major balance-of-payments issues. Specifically, a negative effect of profit repatriations from previous FDI inflows on the balance of payments can be seen, which points to long-term competitiveness problems arising due to the transition process. As a result of significant profit repatriation by foreign investors, the Czech Republic's current account has shown a deficit since the start of the transition process. Since 2004, when the Czech Republic turned its trade balance into a surplus (the balance of trade in services has shown a surplus even before), this striking fact has been even more obvious. Creating a more attractive investment and business environment, not as a part of the transition strategy but as a part of a developed country's competitiveness strategy, thus seems to be a crucial factor, which can improve the current account position of the country by stimulating re-investment.

After 2000, the Czech Republic has continued to be a magnet for foreign direct investment, and has even increased its FDI performance compared to its V4 peers, especially due to the relative decline in inward



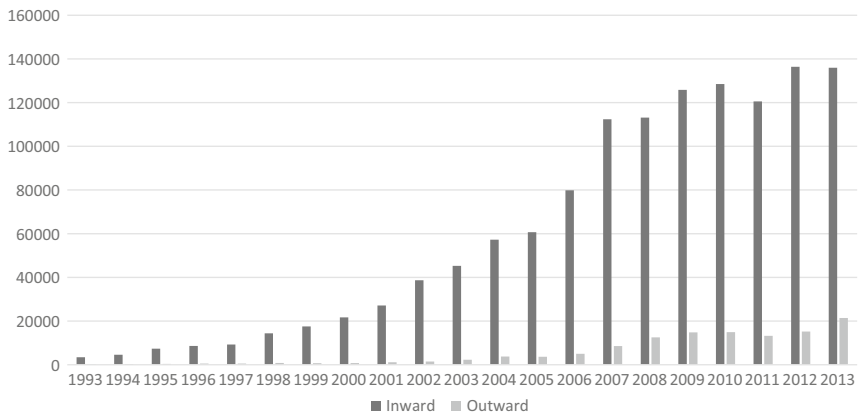
**Fig. 3.1** Inward and outward FDI flows in the Czech Republic, 1993–2013 (US dollars at current prices and current exchange rates, in millions) (Source: Calculations of the authors, based on data from UNCTAD (2014b))

FDI to Hungary. Poland, on the other hand, started to attract significantly more FDI than before, but if compared to GDP, the performance of Poland still lagged behind that of the Czech Republic and Hungary. In the peak year of 2005, which was closely linked to the EU accession and is common to all V4 countries, the Czech Republic attracted almost 12 billion USD in FDI, while Poland accounted for some 10.3 billion, Hungary for 7.7 billion and Slovakia for 3.1 billion. As a publication by A. T. Kearney (2007, 30) suggested, “the 2004 entrants to the European Union continue to attract investors, although they may soon be eclipsed by the new 2007 members, Bulgaria and Romania. From 2000 to 2006, FDI inflows to the 10 states which joined in 2004, increased by 78 percent to about 39 billion USD.” When assessed by A. T. Kearney’s FDI Confidence Indicator, both Poland and the Czech Republic remained in the top 25 in 2007, but Poland slipped 17 spots from 5th to 22nd, and the Czech Republic slipped from 12th to 25th. “These countries continue to enjoy advantages as production centres for goods destined for markets

inside the EU's Common Market, and wages remain far below Western European labour market standards. Indeed, 48% of respondents cite low labour costs as a factor in pursuing investments in Central and Eastern Europe. Another attraction is the EU-10's flat-tax regimes: the average implicit tax burden in the EU-10 is approximately 19.4 percent, compared with almost 27.6 percent in the EU-15" (A. T. Kearney 2007, 30).

During the global recession after 2008, FDI inflows into the Czech Republic markedly slowed down—see Fig. 3.1—but returned to almost as high levels as before the crisis in 2012 (10.6 billion USD). In 2012, the Czech Republic was only outperformed by Hungary (13.5 billion), where inflows were however driven by intra-company capital shifts. Poland slipped into recession and Slovakia suffered the most in terms of FDI performance during the crisis. Moreover, as FDI projects are maturing in the Czech Republic, the relative importance of new equity investments has fallen: reinvested earnings have replaced equity capital as the main component of FDI inflows (UNCTAD 2011a, 1).

The Czech Republic's inward FDI stock reached almost 130 billion USD in 2010, a volume equivalent to two thirds of total GDP, and rose again in 2012 to 136 billion (see Fig. 3.2). Among the V4 countries, total FDI stock was higher only in Poland, but when measured as a share of



**Fig. 3.2** Inward and outward FDI stock of the Czech Republic, 1993–2013 (US dollars at current prices and current exchange rates in millions) (Source: Calculations of the authors, based on data from UNCTAD (2014b))

GDP, the Czech Republic's performance exceeded that of Poland (69.6% and 47.3%, respectively, in 2012). Quite paradoxically however, especially in light of Hungary's economic downturn in recent years, Hungary was still the top performer in terms of inward FDI stock per GDP (81.7% in 2012).

An ongoing trend, which began in the mid-1990s and is confirmed by Table 3.2, is the increasing role of the service sector, which accounted for more than 70% of inward FDI flows, with financial services representing more than 40% of total non-manufacturing investment in 2012. Logistics and telecommunications, as well as tourism are also sectors where the Czech Republic clearly benefits from its favourable geographical location. Manufacturing has attracted about one third of the inward FDI stock. With this being said, it should also be noted that the global slowdown

**Table 3.2** Czech inward foreign direct investment stock by sector, 2000–2012 (in percentage)

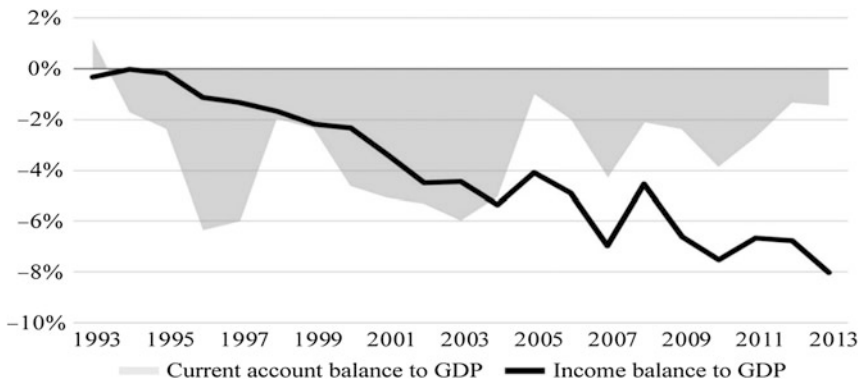
	2000	2004	2007	2012
<b>Non-manufacturing</b>				
Agriculture, hunting and forestry	0.3	2.1	0.1	0.4
Mining and quarrying	2.6	3.3	...	1.8
Electricity, gas and water supply	7.0	7.3	...	−0.8
Construction	3.4	0.3	0.5	1.5
Trade, hotels and restaurants	18.7	18.7	19.1	24.7
Transport, storage and communications	8.7	6.8	11.6	27.2
Financial intermediation	31.8	19.3	35.1	39.8
Real estate and business activities	25.5	41.5	42.5	4.8
Education	0.0	0.0	0.0	0.0
Health and social work	0.6	0.0	0.1	0.5
Other social and personal services	1.4	...	3.6	0.3
<b>Total</b>	<b>58.9</b>	<b>79.7</b>	<b>63.0</b>	<b>71.2</b>
<b>Manufacturing</b>				
Food and tobacco	8.6	0.8	9.0	10.7
Textiles, wearing apparel, leather	3.3	...	3.0	2.2
Wood, paper and publishing	2.5	27.4	0.8	0.7
Refined petroleum and chemicals	14.5	26.3	10.2	16.7
Non-metallic products	5.6	0.1	13.7	0.0
Basic metals and metal products	12.2	49.9	20.7	9.5
Machinery and equipment	51.3	−3.8	40.6	42.9
Recycling and other manufacturing	1.9	0.4	2.0	17.3
<b>Total</b>	<b>41.1</b>	<b>20.3</b>	<b>37.0</b>	<b>28.8</b>

Source: Calculations of the authors based on CNB (2013)

affected services more markedly, returning industrial investment to 37% of total in 2007. Within the manufacturing industries, machinery accounted for most FDI inflow in 2012, followed by the chemical, food and tobacco industries. Due to its high FDI exposure, the Czech Republic ranks among the most globalised countries of the world: according to UNCTAD (2011a), foreign affiliates in the Czech Republic employed 694,728 people in 2006 and generated sales of CZK 3.3 trillion (about 148 billion USD).

Even after a marked increase in investment after 2000, the EU countries have continued to account for most of the FDI inflows into the Czech Republic (88% in 2009; see Table 3.1). The Netherlands (with its favourable tax conditions for global holdings) was the largest investor in 2012 (43.1%), followed by Germany (15.5%) and Austria (13%). As a result, the relative position of the US or Asian investors did not change significantly after 2000. All other investors only accounted for 5.7 of the Czech FDI inflow in 2012.

As a common factor to most CEE countries, rapid inflows were soon accompanied by major profit repatriations that drove the current accounts of these countries into deficits. Figure 3.3 clearly suggests that the negative current account balance has been mostly driven by profit repatriation; reinvested earnings only played a limited role in the Czech balance of



**Fig. 3.3** The Czech Republic's current account balance, 1993–2013 (in percentage of GDP) (Source: Calculations of the authors, based on UNCTAD Handbook of Statistics (2015) and ČNB Statistics (2015))



payments. These developments have several important implications for the Czech economy. First, even though the trade balance does not suggest major export performance or competitiveness problems, the overall current account shows similar symptoms as those observed in the rest of the EU's periphery, which was hit severely by the global financial crisis. In the EU's periphery, empirical estimates of the determinants of government bond yield spreads relative to Germany during the sovereign debt crisis suggest a "greater importance of market liquidity in times of uncertainty, and suggest a shift from a fiscal to a balance-of-payments crisis driven by labour productivity differentials between north and south" (Alessandrini et al. 2012). De Santis and Lührmann (2006) add the importance of net portfolio flows: the demographic profile and civil liberties in the country determine net portfolio flows, which may enable the country to finance its current account deficit by a surplus in the financial account for an extended period of time. Moreover, a current account deficit worsens real GDP growth when it is an evidence of weak macroeconomic competitiveness. The size of the current account balance depends on the nominal exchange rate and the relation between foreign and domestic price levels. In the Keynesian approach, the size of current account deficit refers to the difference between domestic expenditures and (lower) national production (Jiráňková and Hnát 2012).

The reluctance of investors to reinvest earnings in the Czech Republic is mostly explained by the institutional weaknesses of the Czech economy. For instance, the World Economic Forum's Global Competitiveness Report (WEF 2014) repeatedly mentions institutions and innovativeness as the most important barriers for the innovation-driven competitiveness of the Czech Republic. The following quote sums this position up well (WEF 2014, 24):

The Czech Republic needs to explore ways to transition to a knowledge economy in view of its stage of development: compared with other economies at the same stage, technological readiness remains low (36th) and Czech businesses — although doing comparatively well in a regional context — are less sophisticated and innovative than other economies in the European Union. The country's competitiveness would be further enhanced by improvements to its higher education system, where the Czech Republic, at rank 35, features among the 10 lowest ranked EU economies.

The managers at multinational affiliates mostly state inefficient government bureaucracy, corruption, policy instability and restrictive labour regulations as the most problematic factors for doing business in the Czech Republic (WEF 2014, 166). According to the OECD (2014, 54), “Czech firms are well integrated into the international supply chain, with 90% of large firms active in the export market, a proportion falling to half for mid-sized enterprises and quarter for small firms. A relatively high proportion of all firms use material inputs/supplies of foreign origin.” A principal factor behind the rapid technological catch-up has been the rapid and deep integration of the Czech economy into German-led supply chains. Bilateral trade with Germany alone amounts to nearly half of Czech GDP and Table 3.1 suggests that Germany (and other core European countries with favourable tax conditions for multinationals) are the most important home countries of the Czech Republic’s FDI inflows. Additionally, machinery and equipment plays the most important role in the industrial structure of FDI inflows (42.9% in 2012; see Table 3.2). As a result, Czech manufacturing is focused on final products with a relatively large amount of imported intermediate inputs, while intermediate goods produced in the country figure less prominently in Czech exports and thus as intermediate inputs in international production. “Likewise, the domestic service sector is poorly integrated as its content in exports is among the lowest in the OECD countries” (OECD 2014, 26). Table 3.2 further shows that financial intermediation has the highest share in FDI inflows to the Czech Republic (39.8% in 2012), and the share of repatriated profits is generally high in the Czech banking sector.

Only preliminary data for 2014 show that the trade balance outweighed the profit repatriations for the first time in modern Czech history; but export volumes are clearly connected with the Czech National Bank’s efforts to devalue the koruna in this period. Besides export volumes themselves, the export performance of Czech industries should have greater value added than is often the case today. As a result, long-term structural reforms and adjustment such as industrial upgrading must play a more important role. Industrial upgrading (Romer 1990; Grossman and Helpman 1991) is a way to increase the value of activities and in general increase the benefits associated with participation in global value

chains (Gereffi 2001). The Czech Republic is a small export-oriented economy, which is significantly linked to global value chains (the GVC participation index reaches around 60%, which is the highest in the world). However, the backward linkages (foreign value added in exports) are more important than forward linkages (intermediate exports used for production in other countries). Overall, the share of domestic value added in Czech exports reaches only 60% and activities that are performed in the country are in general not the ones with highest value added. So far, research has mainly focused on the Czech automotive industry (e.g. Pavlínek et al. 2009; Pavlínek 2012), and upgrading (mostly process upgrading) was found to be highly selective and uneven among Czech automotive suppliers.

The data presented thus far suggests no structural breaks in Czech FDI inflows. Long-term trends seem to prevail both in the regional and the structural breakdown of FDI inflows to the country. This suggests that the Czech Republic's position in global value chains, as well as its geographical location has played the most significant role among the drivers of FDI, and the crisis has not had significant impacts. These determinants are not about to change unless Czech institutional weaknesses are addressed to increase the share of reinvested earnings and value added in Czech exports. Even though FDI to the developed countries which are the most important sources of Czech FDI inflows has dropped dramatically, the Czech Republic has kept its stable position. According to UNCTAD (2014a, 77), "after the sharp fall in 2012, overall FDI of the 39 developed economies resumed its recovery in 2013, albeit marginally in the case of outflows. Inflows were \$566 billion, rising 9 per cent over 2012. Both inflows and outflows were still barely half of the peak level in 2007. In terms of global share, developed countries accounted for 39 per cent of total inflows and 61 per cent of total outflows – both historically low levels." Given this context, it makes sense to investigate whether the Czech Republic was able to diversify its sources of FDI in the aftermath of the crisis towards less traditional home countries.

## The BRICS Countries as New Sources of FDI?

Since the beginning of the new millennium, the rapidly growing BRICS emerging economies have not only become top destinations for FDI but have also gained importance as capital exporters. The fast economic growth and development of the BRICS enabled their companies to expand beyond their countries' borders in search of new markets, both in developed and developing countries (Sauvant 2005). The topic of outward FDI from these countries has gained prominence in the literature (see e.g. Gao 2005; Gammeltoft 2008; Hernández 2008; Pradhan 2011). However, there have not been many efforts to map the investment activities of these "non-traditional" FDI home countries in case of the CEE region or more particularly the Czech Republic.

Some more recent research has focused on the presence of China in the CEE region (see e.g. Szunomár and Biedermann 2014; Liu 2013; Jacoby 2014), a clear result of China's "going out policy," which has been impacting Chinese investment outflows to Europe, including the CEE region, since 2010. The Czech Republic has become one of the top five Chinese investment recipients from the CEE region along with Poland, Romania, Hungary and Bulgaria (CEED 2012, 22). Moreover, the 16+1 (Central and Eastern European countries plus China) initiative proposed by China in 2012 aims to further promote political and economic ties, including ties in trade and investment.

This part of the chapter reflects on trends in FDI outflows from emerging markets towards the CEE region and the Czech Republic in particular and adds to the existing discussion about the increasing role of non-traditional investment home countries such as the BRICS. The share of the BRICS countries in global outward investment rose from 1% in 2002 to 9% in 2012. Over one third of their outward FDI was oriented towards Europe (UNCTAD 2013, 3). During the economic and financial turmoil, BRICS investors proved to be more resilient. In 2013, companies from China, India, Russia and Brazil announced 313 investment projects in the EU (153, 103, 44 and 13 projects, respectively). This is almost three times as the number of projects in 2004 (Ernst and Young 2014, 6). This trend of increasing presence of fast-growing multinationals from the

BRICS may be expected to continue as their economies continue to grow and develop. Companies from the BRICS are investing particularly heavily in Germany and the UK, where 62% of all their investments in Europe go to, but are also present in the CEE region (Ernst and Young 2014, 25). Table 3.3 displays the FDI inflows to the Czech Republic from the BRIC countries (excluding South Africa). These statistics reveal that the amounts were rather volatile and no general trend in their development was easily visible. This reflects the general characteristics of FDI inflows from less traditional home regions. FDI inflows from the BRIC countries into the Czech Republic were very unstable, turning from positive investments to divestments very easily. Only 2013 saw a positive inflow from all four BRICs. Chinese and Russian investments were predominantly positive. On average, the highest FDI outflows from the BRICs to the Czech Republic were also from China. This confirms China's leading role as the BRIC's emerging investor in the Czech Republic.

All the four BRIC countries are among priority markets for Czech exports, and the government prioritises the enhancement of future cooperation. The Czech Republic sees itself as an entry point to Western Europe for non-traditional FDI home countries. Moreover, as cheap production remains based in the BRIC countries, there is a potential in sectors such as services or research and development due to close proximity to European end markets (CzechInvest 2009). The Czech Republic provides a series of incentives for foreign investors (see Chap. 9 for a full discussion), and Table 3.4 contains information on how the granted incentives can be broken down according to the investor's home country. It is visible that the incentives are mainly granted to traditional investors from Germany and the Netherlands, but there are also three developed non-European countries, Japan, Korea and the United States in the top five. BRICs investors which have been able to capitalise on Czech incentives are represented only by five Chinese companies and one Indian company. Their investments and new job creation is still relatively small in comparison to the traditional investors, but it is likely that these countries will be able to gain more Czech support in the future for their investments.

Details of the Chinese and Indian companies which have been granted investment incentives are presented in Table 3.5. All these incentives were

**Table 3.3** Inward FDI flows to the Czech Republic from the BRIC countries, 2000–2014 (in thousand USD)

Country	2000	2004	2008	2009	2010	2011	2012	2013
Brazil	0.3	-689	-2520	23,324	...	-14,404	-3002	21,376
China	-2667	31,630	164,115	-40,477	31,595	54,579	-92,065	193,078
India	-14	415	-17,152	31,703	1262	-24,949	-59,202	7518
Russian Federation	1346	633	-19,270	-26,604	12,318	-117,749	43,690	8380
BRICs total	-1336	31,990	125,173	-12,055	45,175	-102,523	-110,580	230,352

Source: Calculations of the authors based on CNB (2015)

**Table 3.4** Investment incentives granted to foreign companies, by country of origin (up to March 2015)

Country of origin	Number of projects	Total investment (million euros)	New jobs created
Germany	164	4518.5	36,453
Netherlands	57	2385.9	24,184
Japan	50	1916.8	15,569
Korea	12	1521.5	7494
United States	30	621.8	5466
...			
China	5	43.56	857
India	1	7.2	60

*Source:* Compilation of the authors, based on statistics from CzechInvest (2015)

granted relatively recently. Chinese investors have already utilising Czech investment incentives prior to the economic crisis, but Apag Electronic is the first Indian company in recent history to capitalise on Czech incentives. Generally, the investment activities from the BRICs specialise rather in assembly, and the main sectors include electronics, the food industry and the manufacture of transport equipment. These are rather traditional sectors in the Czech Republic, and can generally be seen as activities with limited skill content and lower value added.

Table 3.6 lists selected investors from the four BRIC countries. Most of them are located in the regions which offer incentives for investors. It is obvious that investments in manufacturing, the metal and machinery sectors prevails, and only two companies, Infosys Technologies and Majak-Software, represent services, specifically the IT sector. This confirms that, contrary to expectations, BRICs investments in the Czech Republic are directed towards the traditional sectors rather than services or research and development which generate higher added value and contribute to the country's upgrading (Capik and Drahokoupil 2011). There are two possible explanations for this: first, BRICs investors do not have sufficient knowledge and expertise to focus on activities with higher added value; second, if they were to possess such abilities and technical skills, they might not be willing to share them.

Brazil is the Czech Republic's most important trading partner in Latin America; however, most Brazilian FDI flows to Western European countries. But even these amounts are quite small in comparison to those of

**Table 3.5** Czech investment incentives granted to Chinese and Indian companies (up to March 2015)

Country	Company	Sector	Type of investment project	Granted	Investment (million euros)	New jobs created
China	Changhong Europe Electric s.r.o.	Electronics and electrotechnic	Production	2006	7.0	300
China	Shanghai Maling (Czech) a.s.	Food industry	Production	2007	8.1	200
China	Shanghai Maling (Czech) a.s.	Food industry	Production	2008	12.8	200
China	Solar Express s.r.o.	Electronics and electrotechnic	Production	2011	6.1	77
China	Yapp Czech Automotive Systems Co., s.r.o.	Manufacture of transport equipment	Production	2011	9.6	80
India	Apag Elektronik s.r.o.	Manufacture of transport equipment	Production	2013	7.2	60

Source: Compilation of the authors, based on statistics from CzechInvest (2015)



Table 3.6 Selected investors from the BRICs in the Czech Republic

Investor	Region	Name of the Czech subsidiary or partner	Country of origin	Sector of investment
Atomenergomaš	Moravia-Silesia	Arako spol. s r.o.	Russia	Machinery and equipment
ArcelorMittal Holdings AG	Moravia-Silesia	ArcelorMittal Ostrava, a.s.	India	Metal industry
Baolong	South Bohemia	Longway Czech s.r.o.	China	Manufacturing of motor vehicles
Evrz Group S.A.	Ostrava	Evrz Vítkovice Steel, a.s.	Russia	Metal products
Hinduja Group	Prague	n.s.	India	Manufacturing of motor vehicles
Infosys Technologies	South Moravia	Progeon s.r.o.	India	Other
Majak-Software, spol. s r.o.	Karlovy Vary	Majak-Software, spol. s r.o.	China	IT, software development
Shanghai Maling Aquarius Co., Ltd.	Ústí nad Labem	Shanghai Maling (Czech) a.s.	China	Food processing
Shanxi Yuncheng Plate-Making Group	Central Bohemia	n.s.	China	Metal products
Sichuan Changhong Electric	Central Bohemia	Changhong Europe Electric s.r.o.	China	Electronics, electrotechnics
Yapp Automotive Parts Co., Ltd.,	Central Bohemia	Yapp Czech Automotive Systems Co., s.r.o.	China	Manufacturing of motor vehicles

Source: Compilation of the authors, based on statistics from CzechInvest (2013)

other outward investor countries with similar characteristics. A possible explanation might be the lack of capital in the Brazilian market, large investment possibilities in the Brazilian market itself and, simply, geographical distance. The declining trend of Brazilian foreign investment outflows was further endorsed by the recent global crisis, and the Brazilian economy's crisis in 2014/2015. As far as the sectorial division is concerned, there has been an increase towards the natural resources sector (metals, mining, oil, gas and steel) (Resende et al. 2010). Investments directed from Brazil to the Czech Republic are relatively negligible. However, there are possibilities for mutual cooperation. In the aerospace sector, Brazilian aircraft producer Embraer began cooperation with the Czech company AERO Vodochody, specialising in aviation technology. Together they have been working on the development and production of a new multipurpose military transport aircraft, the KC-390 (CzechInvest 2011).

Russia faces investment outflows in the long term, due mainly to its unpredictable business environment (see e.g. Kalotay 2010). A very large share of these investments is carried out through tax havens. South East Europe and the Commonwealth of Independent States (CIS) represent the majority of the FDI outflow destinations (UNCTAD 2011b). Russian investments are present particularly in the oil, gas and metal industries. In the Czech Republic, Russian investments are targeting a number of different sectors ranging from traditional engineering, metallurgy and nuclear energy to the hotel industry and tourism. The hotel industry is particularly linked with the spa town of Karlovy Vary, other spa and historical towns, and Prague. There is also an ongoing political discussion about the involvement of Russian companies in the expansion of the nuclear power plant at Temelín; however, the crisis in Ukraine may have a negative impact on this and the investment environment for Russian firms in general (European Business Consortium 2014).

Indian investments are generally oriented towards light industries (textile, engineering, automobile components, etc.), pharmaceutical and IT sectors, which are also represented in investments in the Czech Republic. One of the most significant Indian investors is ArcelorMittal, and investments in the IT sector are represented by Infosys/Progeon, which provides services aimed at banking, insurance, telecommunication and other firms. The Czech Republic's location and its qualified and

cheap workforce offer a base for the company's expansion towards Western markets (CzechInvest 2009). Indian investments were present also in the automobile industry (e.g. Avia Ashok Leyland).

China represents one of the fastest growing investors with a potential for further investments in the Czech Republic. Emerging Europe, including the Czech Republic, can develop its growth potential by turning to new, dynamic markets in the East (CEED 2012). In fact, as Chinese investment shift away from natural resources towards higher value-added tech goods, CEE countries and firms have much to gain from entering into partnerships with Chinese firms. CEE is well placed to deliver opportunities for growth and return on investment, as well as the stable regulatory framework of the EU (CEED 2012, 17).

According to CEED (2012, 16), the institutional background surrounding Chinese investments in the CEE region largely corresponds to its volatile nature. Since 2003, there have been a number of high level visits between China and CEE countries; however, it is hard to find any documents on China's current strategy towards the region. About a decade ago, Chinese investments in the region were almost non-existent. However, in recent years, China has significantly increased its foreign investments in the whole CEE region. China's outward FDI stock in the area, which was only 43.67 million USD in 2004, increased to 821.28 million in 2010 (CEED 2012, 21). Nonetheless, Chinese investments in the Czech Republic and the CEE region remain rather low (also in comparison with other Asian investments, mainly from Taiwan, South Korea or Japan). In general, Chinese companies invest mainly in the manufacturing industry (electrical machinery, foodstuff, telecommunications and transport equipment) and mining. On the whole, the sectoral structure of the Chinese investments in the Czech Republic corresponds to these patterns. The biggest Chinese investor in the Czech Republic is Changhong Electric from Sichuan province, one of the world's largest LCD TV producers. Its factory in central Bohemia, established in 2005, can produce more than 1 million LCD TVs a year. Changhong's investment has totalled 22 million USD. Another noteworthy investor is Shanghai Maling Aquarius, a food company from the Shanghai region, primarily engaged in food processing and distribution (mainly canned meat). Its investment in the Czech Republic was its first

in Europe. Only 10% of the factory's total production is sold on the local Czech market, the majority is exported all over the world.

There are some other interesting Chinese projects and new investments such as the Shanxi Yuncheng Plate-Making Group (metal-working), Shandong Linyi Yuli Foodnuts and Beijing Fight Company (food processing), and last but not least Baolong (glasswork) (CzechInvest 2009). Nevertheless, their value, extent and impact on the total production and employment in the Czech Republic are still limited (see Hnát and Stuchlíková 2014, Zapletal et al. 2013 or Potuzakova and Demel 2011).

Some Chinese companies are locating higher value-added activities to the Czech Republic. For example, Noark Electric Company, a producer of electrical devices and components, has established a regional centre in Prague (besides its existing centres in Shanghai and Chicago) to manage its business operations in Europe, without any production capacity. This company is planning to establish a special department for research and development in the Czech Republic as well. The increasing interest of Chinese investors in common research projects (e.g. in biotechnology) in the Czech Republic is of special relevance. It is important to note that the majority of the Chinese investments are conducted by stated-owned enterprises, while Indian investors are private companies.

Among the BRICS countries, China and India are the two investors which hold the greatest potential for the Czech Republic, due to their relatively fast economic growth and development during the past years. As a result, they are now tending towards expansion more into Western markets via the CEE region. This is particularly true for China, which proposed the 16+1 initiative to ensure mutual cooperation with the CEE countries. The investments from Brazil are the most negligible of all the BRICs, discounting South Africa. Russia continued with the trend of strong investments in South East Europe and CIS economies but also has a presence in the Czech Republic due to relative proximity and language affinity. However, Russian FDI flows to Europe are likely to be affected by the consequences of the crisis in Ukraine.

## Conclusions

During its transition process, the Czech Republic attracted a significant amount of foreign direct investment, which played an important role in the country's transition as a source of financing to compensate for inadequate domestic resources to fund capital formation. Compared to other financing options, FDI facilitated the transfer of technology, know-how and skills, and helped local enterprises to expand into foreign markets. If measured by the share of gross capital formation or by FDI inflows per capita, the Czech Republic attracted the highest relative amount of FDI in V4 comparison. On the downside however, the large inflow of FDI had negative long-term effects on the country's current account, where large profit repatriations pointed to the weak points of the Czech business and investment environment.

After 2000, the Czech Republic has continued to attract foreign direct investment and even increased its FDI performance compared to its V4 peers in the enlarged EU. After 2004, its trade balance also turned into a surplus, but has been outweighed by massive profit repatriations until 2014. Moreover, as FDI projects matured in the Czech Republic, the relative importance of new equity investments has fallen: reinvested earnings have replaced equity capital as the main component of FDI inflows. Even after a significant increase in investment after 2000, the EU countries account for most FDI inflows into the Czech Republic. With the EU membership, relatively low wages and a favourable geographical (logistical) position, the Czech Republic should be an optimal location of production destined for the EU countries. Still, the Czech position in global value chains remains somewhat below par: export-oriented manufacturing is focused on final products with a relatively large amount of imported intermediate inputs, while intermediate goods are relatively lacking from Czech exports or as intermediate inputs in international production. Likewise, the domestic service sector is poorly integrated as its share in exports is among the lowest in the OECD countries.

The crisis did not seem to have had a lasting structural impact on Czech FDI inflows. The Czech Republic's position in global value chains, as well as its geographical location, plays the most significant role among the

drivers of FDI and is not about to change unless institutional weaknesses are addressed to increase the share of reinvested earnings and value added in Czech exports. Inefficient government bureaucracy, corruption, policy instability and restrictive labour regulations are the most problematic factors for doing business in the Czech Republic, which limit the share of reinvested earnings and drive the Czech current account into deficit.

In looking for further evidence of structural shifts, the chapter has also aimed to analyse the Czech Republic's performance in attracting FDI from non-traditional home countries, focusing on four of the BRICS countries, Brazil, Russia, India and China. FDI inflows from these countries are rather volatile and clear trends in their development are difficult to identify. While the four countries have so far only been responsible for a small portion of inward FDI in the Czech Republic, their amounts have been increasing and thus confirm the growing global importance of non-traditional home countries as a source for FDI outflows. The Czech Republic proves to have an ability to attract FDI, and the firms from the four BRICS countries are slowly capitalising on Czech investment incentives. Overall, the Czech Republic seems to be a suitable host country for FDI from the four countries, particularly due to its proximity to other EU markets. A shift in the BRIC's FDI from the manufacturing sector towards services has not really been observed in the Czech Republic yet, but there are perhaps embryonic trends which point in this direction. So far, firms from the BRICS have allocated most of their investments in traditional, lower value-added sectors, investments creating higher added value have not been really present, mostly due to insufficient technological maturity of BRICS investors or their unwillingness to share it. Nonetheless, the FDI from the four BRICS countries to the Czech Republic is still too small to represent any structural break in terms of home countries.

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