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IS POLAND STILL ATTRACTIVE FOR FOREIGN INVESTMENTS?

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Abstract

Since the economic transition Poland has faced many changes. Accession to the European Union improved the Polish economy and made it more attractive for foreign investments. Since 2004 Poland has been one of the major destinations of FDI in East and Central Europe Countries. Also during the global economic crisis Poland was a good location for foreign capital. The main aim of this article is an attempt to assess whether Poland is still attractive for the location of foreign direct investment. This article is a preliminary study. It is based on statistical analysis describing changes in foreign capital flows in Poland and its position in relation to other European Union countries. Results show that the position of Poland on the map of foreign investment has dramatically changed.

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INTRODUCTION

The global economy is characterized by a strict system of linkages between the economies of individual countries. Each country has its own variability of business cycle. The very large openness of economies causes the transmission of economic phenomena – positive and negative as well. Due to globalization, economic changes are more tangible and move faster between particular countries. This has an impact on transnational corporations – on the one hand they are strongly influenced by the economic changes in their home country and also in host countries – via directions of foreign direct investments (FDI).

Since the economic transition, the Polish economy has been influenced significantly by two major occurrences – the accession into the European Union (EU) and the global economic crisis. With no doubt, the accession (and previously only the perspective) helped to improve the economy of the country, raise economic growth, and was a strong impulse to the modernization of Polish companies. In addition it had an indirect effect on Polish currency appreciation – which has strengthened the credibility of the Polish economy. The Polish accession to the EU had also influenced foreign capital value flows – since 2004 Poland has been an attractive place for foreign direct investments. During the crisis Poland suffered from FDI decline, however, it was rather short-term and at a lower range than in the case of many EU countries. After the recovery in 2010 and the past few years, the rapid decline of foreign capital flows may be observed again despite global FDI flows return to growth. Therefore, can we state that Poland is still attractive for foreign investments?

This article is a preliminary study of the analysis related to the changes observed in foreign capital flows and its determinants. The main aim of this article is an attempt to assess whether Poland is still attractive for foreign direct investment.

The first part of this article describes the Polish economy in the context of its investment attractiveness. In the second part the author analyses foreign capital flows into Poland and its position in relation to European Union countries.

THE INVESTMENT ATTRACTIVENESS OF POLAND

Foreign capital is essential for economic development. Poland, in an effort to lower the disparities in relation to highly developed economies, should attract foreign investors (Stawska, 2014a). As many studies confirm, within Central and Eastern Europe (CEE), Poland was one of the major destinations for foreign investors since the economy transition which is outlined by many authors in the literature.

Sinn and Weichenrieder (1997) state that “the liberalization of the capital flows in 1990 led automatically to FDI inflows to Central and Eastern Europe, but distribution was uneven among the countries. Poland was one of the countries that has attracted foreign investors from the start.” Hunter and Ryan (2013) agree that from the beginning of the economic transformation in 1989-1990 Poland was considered as an attractive destination for foreign direct investment. Three inter-related factors were mentioned as major FDI determinants: low cost but qualified labour; long-term market potential or yields greater than could be achieved domestically; and access to a wide variety of natural resources. As Hunter and Ryan state these are still considered as essential pre-conditions to any successful effort at attracting FDI today.

In 2004 Poland joined the European Union. It was not an easy process. Poland had to face many macro and micro challenges relating to public sector financing, transparency, infrastructure, and social policy. However, Poland improved significantly after 2005 according to growing investment from European Union investment funds and other foreign sources in the period directly before the crisis (Reichard, 2011).

Certainly greater stability of the economy has a positive effect on its competitiveness. Thus, the Polish Government attempted to reduce the effects of the global economic crisis impact by introducing anti-crisis programs aimed at stimulating the economy, attracting foreign investors to the country and the maintenance of macroeconomic stability. As a result Poland seemed to be resistant to global shocks (Stawska, 2014b). The following reasons are outlined in the literature:

1) the country met the crisis with an already stable fiscal structure and banking sector,

2) the zloty, not being pegged to the euro allowed for significant room to manoeuvre in response to the global downturn,

3) the considerable currency depreciation (the zloty is still about one-fourth cheaper than it was in mid-2008) facilitated not only increasing competitiveness of exports, but also an enhanced significance for EU-funded public investments,

4) in comparison with the other CE countries, the Polish economy has a lower degree of openness. While exports currently make up approximately 60% of GDP in Hungary, the Czech Republic and Slovakia—and accounted for as much as 80–90% before the crisis—

they represent a third of the Polish GDP,

5) finally, due to certain structural characteristics, as well as the size of the Polish economy, there was robust domestic demand and consumption that did not wane after the outbreak of the crisis (Sobják, 2013). Without a doubt, these factors could also have a significant role in attracting foreign investors. In most countries global economic crisis has caused i.e. the reduction of Foreign Direct Investment (FDI). Laven (2012) states that “in Poland’s case, this reduction was short-lived and after some structural adjustment, FDI continued flowing, positively affecting Poland’s growth.”

Table 1 presents Poland and chosen Central and Eastern Europe countries (members of the European Union) and their global competitiveness index.

Tabela 1: The Global Competitiveness Index of chosen EU countries in 2007, 2010 and 2013

No.	Country	Global Competitiveness Index		
		2007 rank	2010 rank / (score)	2013 rank / score
1	Estonia	27	33 (4,61)	32 (4,65)
2	Poland	51	39 (4,51)	42 (4,46)
3	Czech Republic	33	36 (4,57)	46 (4,43)
4	Lithuania	38	47 (4,38)	48 (4,41)
5	Latvia	45	70 (4,14)	52 (4,40)
6	Hungary	47	52 (4,33)	63 (4,26)
7	Slovak Republic	41	60 (4,25)	78 (4,10)

Source: Own elaboration based on *The Global Competitiveness Reports*, <http://www.weforum.org> (17.11.2014)

In 2007, at the beginning of the crisis, Poland was in 51st place – the last within the chosen countries. As it was stated in the literature, Poland rapidly improved its competitiveness and in 2010 was at the top of CEE countries. In 2013 Poland fell down to 42nd place, however, within CEE countries it still remains attractive.

This suggests that Poland should attract foreign investors. On the other hand it is difficult to indicate what characteristics of the economy have a decisive influence on FDI location, especially in terms of economic crisis. Various authors come to contradictory results. The same factor that appears to affect FDI in some cases seems to have a positive influence, in others – negative or turns out to be statistically insignificant. As Cywiński and Harasym (2014, p. 11-12) indicate, one of the main factors that influence investment decisions is the investment cost related to investment risk and expected outcomes, opportunity costs and marginal costs associated with the ability to produce a particular good or service at a competitive rate.

Research conducted by Stawicka (2013) suggests that the variability of motives for international expansion to the European Union markets in the last seven years is rather low. However the differences clearly indicate that foreign companies are affected by the economic crisis. Among the factors identified as a key determinants of foreign investment in Poland, in both 2005 (before the crisis) and 2011 (during the crisis) were i.a.: seeking new markets and lower prices of productive factors. In should be noted that external factors defined as economic and political stability of the host country economy were declared as not important in 2005 while in 2011 they appeared significant. In turn, in 2005 determinants such as investment incentives and the willingness to maximize profits were most important while in 2011 the importance of these factors was considered as average.

Moreover, Polish success in weathering the worldwide economic crisis by the mid-point of 2011 has been largely depreciated. The economic stability, which had been a hallmark of Poland’s economy over the past

two to three years, has returned to most of the European countries (with the exception of Greece, Ireland, Italy, Spain, and Portugal). Since then, Poland is not the only opportunity for foreign direct investments and expanding business (Hunter et al., 2012). This is reflected in foreign capital flows.

FOREIGN INVESTMENTS IN POLAND

Until the economic transition, Central and Eastern Europe was unknown as a place for investing so at that time, in most cases, foreign investors entered the market through acquisitions (also by privatization) in order to benefit from the local companies' knowledge of the local market. "As the years passed, the FDI restrictions reduced and until 1995, 45% of privatization in Poland was made through FDI" (Sinn et al., 1997).

The change of the political and economic system in 1989 triggered the significant increase of foreign investors wanting to invest in Poland (Figure 1) (Kuzel, 2007). By the year 1990 the share of Poland in foreign capital inflow value barely amounted to 0,04%, that is 89 mln USD, but in 1991 as a result of opening the Polish economy, foreign capital value reached 291 mln USD, that is by 227% more than in the previous year (World investment Report, 1992). Since the economic transition Poland was a leader of FDI inflows in CEE.

At the same time Poland made association relationships with the EU which came into force at the beginning of 1994. Within this relationship the member countries were obliged to make foreign capital inflow free and treat domestic and foreign investors equally. The mentioned capital inflow was to manifest itself in the form of foreign direct investments.

In the years 1990 – 1995 foreign developers got interested in investing their capital in Poland. There is a visible upward trend in value of capital flowing into Poland: from 89 mln USD in 1990 (0,04% in comparison with world's countries) to 7270 mln USD in 1999 (0,67%). In the 1990s nearly the total of 31 500 mln USD of foreign capital flowed to Poland in the form of direct investments, out of which 1 mln USD was in the years 1993, 1995 and 1998. In the same years the share of Poland in FDI (foreign direct investment) compared to other countries was the highest and it reached 1,1% in 1995 (the value of investments was by 1784 mln USD higher than in the previous year) and respectively 0,92% and 0,79% in the years 1998 and 1993. In that period an average foreign capital inflow value accounted for 3144 mln USD annually. The significant and substantial foreign investors' interest in investing capital in Poland may be justified by political and economic changes which took place at that time. These alterations gradually abolished a great deal of restrictions towards foreign investors.

The meaningful abolishment of restrictions and limitations towards foreign investors in the scope of business activity took place just after passing the Business Activity Act in 1999. (act, 1999.101.1178), in which the Art 5 states that "taking up and running business activity is equal for everybody, with the retention of conditions defined by law regulations". The article gave all foreign investors the right to run business activity on the territory of Poland in the same scope and based on the same law as domestic developers. However, setting up branches and subsidiaries of international enterprises was possible exclusively for the purposes of advertising, promotion and making a good image of an enterprise.

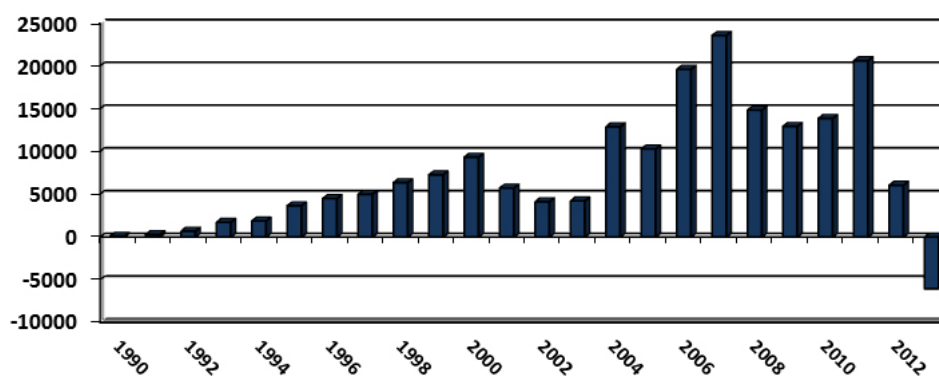


Figure 1. Foreign capital inflow to Poland in 1990- 2013 (in mln USD)

Source: Own elaboration on the basis of UNCTAD data (Retrieved from: www.unctad.org, 30.10.2014)

In 2000 foreign capital inflow value grew to over 2000 mln USD, which accounted for 0,67% of foreign investments share in other countries (World Investment Report, 2004). In the next two years interest in Poland as a country for capital investment was not so considerable. One year before Poland entered the EU the value of investments slightly increased. In 2004 foreign capital inflow reached 12 890 mln USD, which accounted for a record-breaking share in foreign capital flowing into countries – 1,74% and to European countries – 6,31% (World Investment Report, 2004). In 2004 the Freedom of Business Activity Act (act, 2004.173.1807) was passed. The law has been applicable since then. According to the new legislation, foreigners meeting the requirements of this Act are allowed to take up and run business activity with the same rights as Polish citizens.

Between 2005 – 2007 rapid increase in foreign capital flows into Poland was observed – despite the reduction in foreign direct investment in the global economy which had begun. At least after 2007 the range of foreign investment capital significantly decreased in Poland as well. However, the decline is observed till 2009 when Poland started to attract foreign investors again. The first newly worrying symptoms appeared in 2012 when rapid decline was observed. Comparing to the year before, in 2012 the value of foreign capital inflows was about 70% lower. This tendency seems to have been

maintained in 2013. It should be noted that “after the 2012 slump, global FDI returned to growth, with inflows rising 9 per cent in 2013, to \$1.45 trillion. UNCTAD projects that FDI flows could rise to \$1.6 trillion in 2014, \$1.7 trillion in 2015 and \$1.8 trillion in 2016, with relatively larger increases in developed countries” (World Investment Report 2014, p. 14).

Comparing the foreign direct investment flows in Poland and the European Union in last years it appears that while the decline in 2012 was consistent with EU tendencies, the rapid decline in 2013 is in contradiction (Figure 2).

At the beginning of the crisis 2006 – 2007 Poland attracted foreign capital, however, the dynamic was lower in comparison in EU tendencies. Between 2008 – 2011 Poland was characterized by a higher dynamic of foreign capital flows - comparing to EU countries. At that time, despite global economic changes, Poland was one of most attractive EU countries according to foreign capital absorption. After that period the declining tendencies occurred, especially in 2013 when the huge disproportion between Poland and EU is observed. It suggests that the position of Poland as a beneficent of foreign capital is changing.

An important issue related to foreign capital flows is the value of reinvested profits, presented in Figure 3.

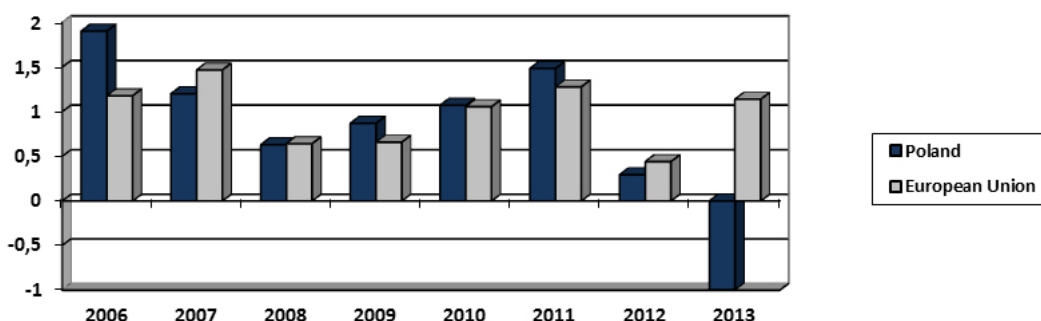


Figure 2: The dynamic of foreign capital inflow to Poland and European Union in 2006 - 2013

Source: Own elaboration on the basis of UNCTAD data (Retrieved from: www.unctad.org, 30.10.2014)

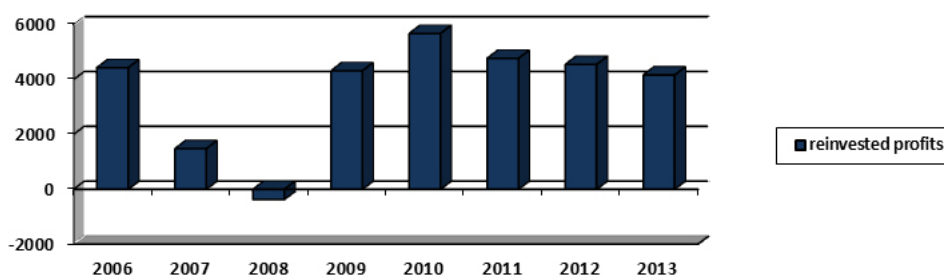


Figure 3: The value of reinvested profits in Poland in 2006-2013 (mln EUR)

Source: Own elaboration on the basis of NBP data (Retrieved from: www.unctad.org, 30.10.2014)

Reinvested profits have an important role in creating balance of payments. This part of foreign capital improves the foreign companies' assets and is a source of financing host country deficit. From the host economy point of view more preferable is stable growth of this factor than a situation where foreign companies transfer profits to the home country. In the case of Poland, in 2006 – 2008 rapid decline in reinvestments is observed. After a short recovery, since 2010, the value of reinvestments is declining. It may suggest that foreign companies avoid development in the Polish economy and more capital is transferred to the home countries. On the other hand, the ability to generate profits by foreign investors may decrease, however, this is the subject of another study.

The changing tendencies in Polish attractiveness are also observed in the dynamic of greenfield projects (Figure 4).

Greenfield projects are usually more preferred due to their positive impact on the host country economy – stronger than in the case of acquisitions. As Figure 5 shows, during the crisis (2007-2008) the dynamic of greenfield project value in Poland was much higher than in European Union countries. Also in 2011-2012 Poland gathered more greenfield projects. However in 2013 the proportion between Poland and the EU changed rapidly.

Table 2 presenting the share of European Union countries in FDI flows confirms that in the last years the directions of FDI flows have been changing and the position of Poland dramatically falling.

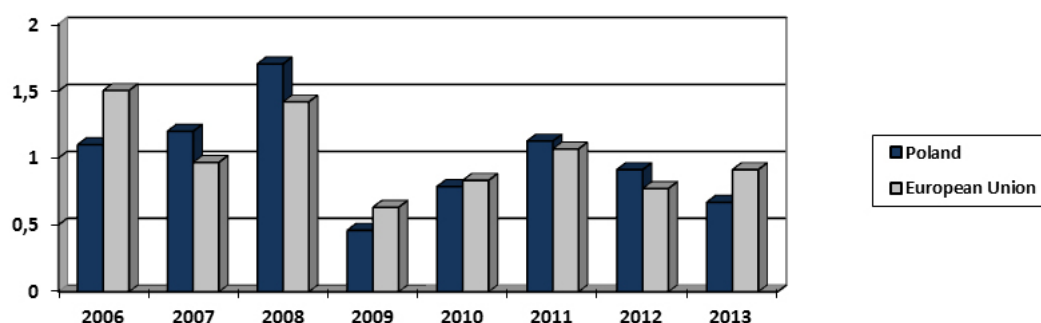


Figure 4: The dynamic of greenfield project value in Poland and European Union in 2006 - 2013

Source: Own elaboration on the basis of UNCTAD data (Retrieved from: www.unctad.org, 30.10.2014)

Tabela 2: The share of EU countries in total FDI flows in 2007, 2010, 2013

No.	2007		2010		2013	
	Country	Share	Country	Share	Country	Share
1	United Kingdom	23,3%	Belgium	20,1%	Spain	15,9%
2	Netherlands	13,9%	Germany	17,1%	United Kingdom	15,1%
3	France	11,2%	United Kingdom	12,9%	Ireland	14,4%
4	Belgium	10,9%	Ireland	11,2%	Luxemburg	12,2%
5	Germany	9,3%	Spain	10,4%	Germany	10,9%
6	Spain	7,5%	Luxemburg	10,4%	Netherlands	9,9%
7	Italy	5,1%	France	8,8%	Italy	6,7%
8	Austria	3,6%	Poland	3,6%	Austria	4,5%
9	Sweden	3,4%	Italy	2,4%	Sweden	3,3%
10	Ireland	2,9%	Finland	1,9%	Czech Republic	2,0%
11	Poland	2,7%	Czech Republic	1,6%	France	2,0%
12	Finland	1,4%	Romania	0,8%	Romania	1,5%
13	Bulgaria	1,4%	Portugal	0,7%	Portugal	1,3%
14	Denmark	1,4%	Hungary	0,6%	Hungary	1,3%
15	Czech Republic	1,2%	Slovakia	0,5%	Greece	1,0%
16	Romania	1,2%	Estonia	0,4%	Denmark	0,8%
17	Slovakia	0,5%	Bulgaria	0,4%	Bulgaria	0,6%
18	Hungary	0,5%	Malta	0,2%	Estonia	0,4%
19	Portugal	0,4%	Austria	0,2%	Latvia	0,3%

20	Estonia	0,3%	Lithuania	0,2%	Slovakia	0,2%
21	Latvia	0,3%	Cyprus	0,2%	Croatia	0,2%
22	Cyprus	0,3%	Latvia	0,1%	Cyprus	0,2%
23	Greece	0,2%	Slovenia	0,1%	Lithuania	0,2%
24	Lithuania	0,2%	Greece	0,1%	Slovenia	-0,3%
25	Slovenia	0,2%	Sweden	0,0%	Finland	-0,4%
26	Malta	0,1%	Netherlands	-1,9%	Malta	-0,9%
27	Luxemburg	-3,3%	Denmark	-3,0%	Belgium	-1,0%
28					Poland	-2,5%

Source: Own elaboration on the basis of UNCTAD data (Retrieved from: www.unctad.org, 30.10.2014)

In 2007, at the beginning of the global crisis, the role of Poland in attracting FDI was relatively high – 11th place among EU countries (27) and it was strengthening up to 2010 when Poland achieved 8th place and was at the top of FDI destination within CEE countries. In 2013 the position of Poland was dramatically lower. However, other changes in FDI directions are observed. While in 2007 mainly the United Kingdom, Netherlands, France, Belgium, and Germany attracted FDI, in 2013 only the United Kingdom and Germany remained as the top directions. The role of the remaining above-mentioned countries declined in contrast to Spain, Ireland, and Luxemburg (last place in 2007) that have become more attractive in terms of foreign investments. In addition, the rapid decline of Belgium (from 4th place in 2007 to 27th in 2013), and Finland (from 12th place in 2007 to 25th in 2013) is worth mentioning. It confirms that foreign direct investment flows are changing direction and the role of particular European countries, including Poland, as host countries is changing.

CONCLUSIONS

Since economic transition Poland had opened its market to foreign investors. The Polish accession to the European Union strengthened its position among Central and East Europe countries. As a result, during 2003-2007, Poland attracted record levels of foreign direct investors that influenced Polish economic growth by increasing the export competitiveness of the country and contributing significantly to cover the current account deficit.

During the crisis Poland appeared to be resistant to global shocks. Therefore Poland was one of the top destinations of foreign direct investment. Researchers outlined the attractiveness of this country even in foreign literature. However, since 2012 the absorption of foreign capital is decreasing in the case of Poland although global flows have returned to the path of growth.

European Union countries are still attractive for foreign investors, but Poland, despite its relatively good economic condition and relatively good attractiveness in terms of GCI, seems to be losing its attractiveness according to foreign direct investments. This phenomena has been observed for last two years therefore it is too early for unequivocal conclusions about the reasons. However, there are some presumptions worth considering.

The decrease of foreign capital flows might be the result of earlier flows. The significant flows of FDI in 2010 – 2011 probably fulfilled the market demand for some time resulting in declining tendency in foreign capital flows in further years. Secondly, in recent years the strengthening competitiveness of Polish companies might be observed. Since 2006 there has been an essential rise in Polish companies performing abroad in the form of foreign direct investment. In the last decade Poland became a leader of receivables among new European Union countries. It suggests that Polish companies became competitive on an international scale which makes the Polish market more competitive.

This is a presumption to further analysis that should concentrate on analyzing the main determinants of foreign direct investments in a changing economy and its role in attracting new investors. It is also essential to verify whether the absorption of the Polish market is still sufficient. This could support the creation of policy recommendation and strengthen position on the global market.

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