Chapter 2
Is a live dog better than a dead lion? Seeking alternative growth engines in the Visegrad countries

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1. Introduction[1]

After the crisis years, there was an overall disenchantment with the foreign direct investment (FDI)-based growth models in the Central European post-socialist countries. FDI resulted in lower than expected convergence and in over-high exposure to foreign economic and political forces, inducing Visegrad governments (and governing parties) to seek new economic policies, either to catch up or at least to achieve stable political success despite relatively low post-crisis economic growth. Obviously, the previous growth engines – foreign multinational companies and their local subsidiaries – are still expected to play albeit a smaller role in these new policies, and some of them are now discriminated. Alternative or supplementary 'growth-driving' (or 'growth-illusion-driving') companies are being sought by the governments, possibly groups of domestically-owned or -controlled enterprises. Their main role will be to stimulate growth or at least provide the illusion of catching up economically (or in welfare terms) with the core European Union countries.

In this chapter, I will concentrate on four Visegrad countries (Czechia, Hungary, Poland and Slovakia), the economies which opened up earliest and to the greatest extent to FDI in the Central and Eastern European (CEE) region. However, because the changes in the economic role foreign-owned subsidiaries are 'allowed' to play are the most pronounced in Hungary, the qualitative analysis will focus on this country.

I start by briefly presenting the FDI-based models of the Visegrad countries, moving on to look at how the emphasis on the role of the local subsidiaries of multinational companies has changed recently in the Visegrad countries. I then go through the possible other groups of economic players who could replace them in an attempt to stimulate these economies: state-owned enterprises (SOEs), regional multinationals, and large domestic companies and small and medium-sized enterprises (SMEs). The last section draws conclusions.

1. Research on regional multinationals was supported by the Hungarian Research Fund OTKA (109294).

2. FDI-based growth models in the Visegrad economies

The problem of convergence and catching up with more developed countries has always been a key topic in Central and Eastern European (CEE) countries and among them in the four Visegrad countries. Throughout their history, their distance to the dynamic and wealthy European regions has constantly fluctuated.

After the post-1989 transition process, all countries opened up their economies to FDI, albeit at different times. FDI inflows accelerated shortly before they joined the European Union. Governments (and experts) expected that, besides providing capital and creating numerous jobs, FDI would contribute significantly to economic restructuring, boosting growth and helping the CEE countries catch up with their Western counterparts. This would be achieved directly through backward and forward linkages impacting domestic companies as well as indirectly through intensifying competition and thus raising company competitiveness and productivity. Early experiences in two countries, Estonia and Hungary, and later in other CEE economies, seemed to support that expectation (Neuhaus 2006; Kornecki and Raghavan 2011), although even then certain analyses questioned the size and thus the significance of the impact (see e.g. Mencinger 2003).

However, looked at from a longer-term perspective, while the inflow of FDI contributed considerably to the restructuring of the economies in question, most of the expectations concerning their beneficial impact on domestic companies and thus enhanced competitiveness, growth and convergence with the more developed member countries of the European Union were only partially fulfilled. This was due to a number of factors: over-high expectations, economic policy mistakes, the inability of domestic firms to become partners of local MNC subsidiaries, and last but not least the generally low inclination of MNCs to rely on local firms. Furthermore, other global economic developments connected to the appearance of mainly Asian competitor countries with substantially lower wages and the shrinking of distance due to technological developments further complicated their situation (more details in e.g. Bohle and Greskovits 2007; Galgóczi 2009; Narula and Bellak 2009; Farkas 2013 or Szanyi 2016). Furthermore, this FDI-based strategy resulted in changes in the economies which were not helpful from the point of view of longer-term growth (Lane and Myant 2007; Nölke and Vliegenhart 2009).

By the time the financial crisis broke out, there was overall disenchantment in the CEE region with the 'liberal' convergence strategy and its reliance on FDI (see e.g. Farkas 2013 or Hunya 2015). The main reason was that this did not result in a sustained high level of growth and thus in a perceptible (or even spectacular) narrowing of the income gap with developed EU Member States, and high-growth years were not numerous enough in all CEE countries for substantial catching up. The problems caused by the crisis further deepened this disillusionment, as many of them were related directly or indirectly to FDI, for example, the high integration of CEE companies in global or European value chains in hard-hit industries, or increased repatriation of profits by crisis-ridden multinational companies. Moreover, FDI inflows substantially declined during the crisis and post-crisis years, and this now seems to be a lasting phenomenon (Hunya 2015; Kalotay 2017).

3. Reducing the role of foreign-owned companies in the Visegrad economies

In this section, we analyse whether there have been efforts to reduce the role of MNC subsidiaries in the countries in question, taking a look at which sectors, industries or activities are targeted.

Already during the crisis years, over-high foreign exposure, including through FDI, emerged as a risk factor in numerous analyses, increasingly questioning the previously almost unequivocally positive approach to FDI. Profit repatriation and capital withdrawal hit certain CEE countries hard during the crisis years (see e.g. Mencinger 2013), leading to political debates about differentiating between 'good' and 'bad' FDI (see e.g. Zimny (2015) for Poland, or Drahokoupil and Galgóczi (2015)). These distinguished between 'bad' market-seeking, horizontal FDI aimed at replacing domestic producers or service providers and repatriating profits and thus 'not beneficial' for the host economy, and 'good' vertical FDI resulting in many new jobs and exports and allowing domestic companies to benefit from becoming part of global or European value chains.

In the post-crisis years, there have been various signs of the business environment turning against FDI in the analysed countries, as seen by an increase in governmental instability in the Czech Republic, in Poland and temporarily in Hungary. Moreover, governments are increasingly using anti-FDI rhetoric and populist tendencies are gaining ground (Havlík and Pinková 2012). Anecdotal evidence points to cases of anti-FDI measures where certain foreign-owned enterprises are discriminated against, for example in public tenders or when regulatory changes force them to 'voluntarily' leave the country. According to Becker (2016), the current Hungarian and Polish governments are striving to expand the role of domestic capital, primarily in the services sector, and within the latter, in the banking sector. Tóth (2014) has described the policy change as a turn towards selective economic policy nationalism, present everywhere except in industry and private-sector business services, where a neoliberal-leaning policy is still pursued. Other authors describe the changes in the region as moving in a 'national capitalist' direction (Szent-Iványi 2017) or in Hungary as 'corrupt crony capitalism' (Benczes 2016; Kornai 2015).

Nevertheless, aggregate data illustrating changes in the overall restrictiveness of government policies towards foreign investors and foreign-owned subsidiaries and in the overall deterioration of the business climate for foreign investors are hard to find.

3.1 Changes in FDI policies

It is not easy to compare the FDI policies of the various governments, in our case looking at the level of restrictiveness and changes made. In this section, we use various indexes to check for changes in the analysed countries. We then briefly present the case of Hungary, which – as already indicated – has made the most efforts to reduce the role of foreign subsidiaries in certain areas and activities.

The OECD's FDI Regulatory Restrictiveness Index facilitates international comparisons over time, looking at four main restrictions on FDI:

— foreign equity limitations;
— screening or approval mechanisms;
— restrictions on the employment of foreigners as key personnel;
— operational restrictions, e.g. restrictions on branching and on capital repatriation or on land ownership.[2]

Though obviously not giving a full picture, the index does provide a good indication of the main developments in FDI restrictiveness in a given country.[3] Figure 1 shows the index for the Visegrad countries and the unweighted OECD average in 2006, 2010 and 2015. We note that the index values for the analysed countries – with the exception of Poland – are well below the OECD average. Czechia stands out with an exceptionally non-restrictive FDI policy, while Hungarian restrictiveness has declined over the period analysed to approach the Czech level. With the exception of Slovakia, FDI regulatory restrictiveness decreased in the Visegrad group between 2006 and 2010, and plateaued (with the exception of Czechia) between 2010 and 2015. However, compared with other countries examined by the OECD, the Visegrad countries still offer an outstandingly liberal FDI climate, with the exception of Poland. There are few areas where restrictions remain in force: agriculture and forestry in Czechia and Poland; transportation, financial services, other finance and real estate investment in all four countries; and the media (radio & TV and other media) and telecommunications (fixed and mobile) in Poland. The latter explain the higher index level for Poland. At least according to this index, the apparent anti-FDI attitudes do not seem to be present or to have materialised in regulatory terms in the analysed countries up till 2015.

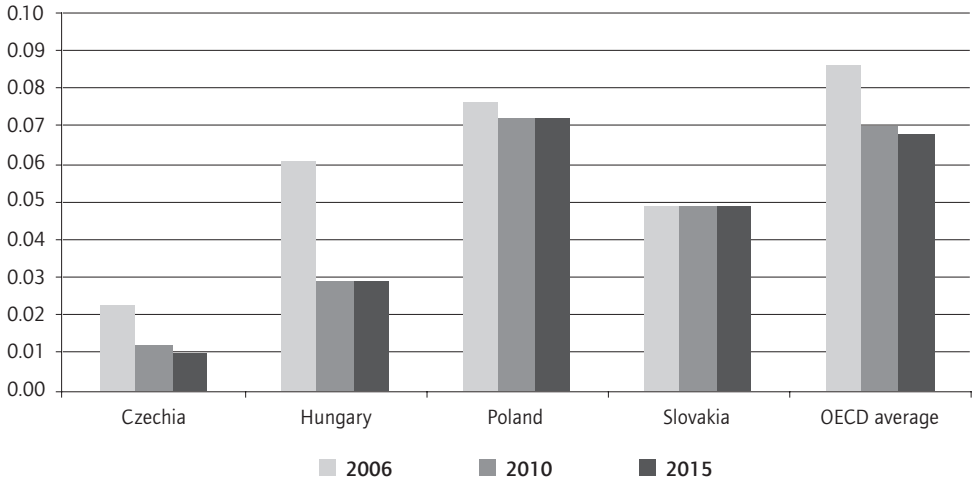
A similar index, part of the Product Market Regulations Index constructed by the OECD, tries to measure FDI barriers in an internationally comparable way (Figure 2), and arrives at results similar to those of the previous analysis. By 2013, FDI barriers were seen to reach a level significantly (Czechia, Hungary and Slovakia) or slightly below (Poland) the unweighted OECD average. This indicator shows a clearly declining trend between 1998 and 2013, i.e. even here we found no trace of an increased anti-FDI stance in Visegrad policies.

Provided by UNCTAD, another source of information looks at the number of international investment disputes. Problematic investment cases and disputes between states and foreign investors have clearly increased in the four Visegrad countries since the crisis (as seen in Figure 3), hinting that the business climate has worsened for certain foreign investors.

2. See http://www.oecd.org/investment/fdiindex.htm

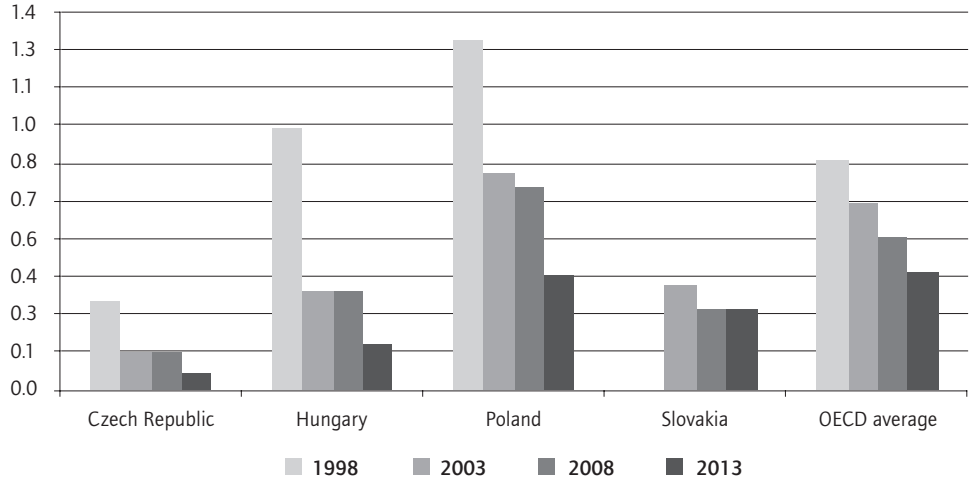
3. The difference between restrictiveness according to 'more visible' and 'less visible' measures may differ widely: 'less-visible' (i.e. internationally less regulated) measures may result in a different level of restrictiveness, see e.g. the comparison of UNCTAD on restrictions on FDI in services in developing countries and transition economies. Even in this international comparison, the Visegrad countries exhibit a low level of restrictiveness towards FDI in services in 2004, with Czechia being the least restrictive among 50 countries, Hungary ranked tenth and Poland sixteenth (UNCTAD 2006).

Figure 1 **FDI Regulatory Restrictiveness Index of the Visegrad countries, 2006, 2010, 2015**



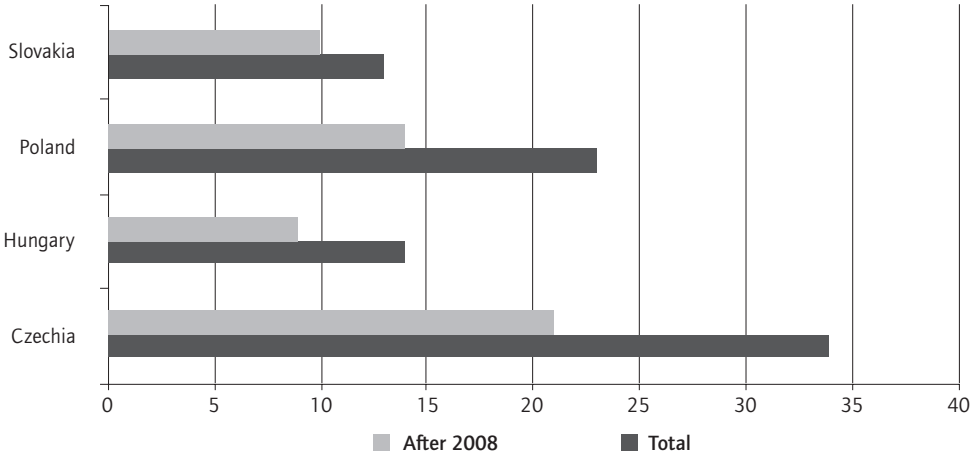
Note: higher values of the index indicate more restrictive FDI policies.
Source: OECD

Figure 2 **Development of the Barriers to FDI indicator in the four Visegrad countries, 1998, 2003, 2008, 2013**



Note: higher values of the index indicate higher barriers to FDI.
Source: OECD

Figure 3 **Number of investment disputes with the Visegrad countries as respondent states, 1994-2016**



Note: 'Total' refers to the number of disputes between 1994 and 2016 (22 years) ; 'After 2008' between 2008 and 2016 (8 years).
Source: http://investmentpolicyhub.unctad.org/ISDS/FilterByCaseName

The overall FDI environment is thus much less restrictive in the Visegrad countries than the OECD average and there have been no negative changes at macro level – at least until 2015. However, as already mentioned, anecdotal evidence and the increased number of state-foreign investor disputes may point to a worsening policy environment, at least for certain FDI projects.

3.1.1 The Hungarian case

The Hungarian case illustrates the ambiguity of this worsening FDI environment. Several legislative changes specifically target foreign-owned subsidiaries in certain sectors and industries[4], mainly those focused on the domestic market and operating in the services sector, and thus considered to be 'bad' FDI in government-speak. Changes in the laws meant *inter alia* that foreign-owned companies issuing social vouchers were forced out of business in Hungary.[5] In 2016, the EC ruled against the Hungarian government, as through this legislation it had infringed EC directives on freedom of establishment for service providers.[6] In the media sector, advertising revenues were taxed at 50%, hitting mainly foreign–owned companies.[7] In the same sector, the government commissioner in charge of the Hungarian film industry acquired one of the two large foreign-owned commercial TV channels.[8] Through not extending radio broadcasting licences to foreign or domestic privately owned channels, only state-run

4. See https://www.ft.com/content/e0c44550-0ad2-11e6-b0f1-61f222853ff3 or European Commission (2015) underlining the high frequency of legislative changes impacting negatively on certain economic actors.
5. See http://investmentpolicyhub.unctad.org/ISDS/Details/599
6. See http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=ecli:ECLI:EU:C:2016:108
7. See https://www.wsj.com/articles/hungary-adopts-tax-on-advertising-revenue-1402511876 or https://www.ft.com/content/b86018ca-2c7d-11e5-acfb-cbd2e1c81cca
8. See http://bbj.hu/business/report-andy-vajna-will-own-tv2_105497

radio stations (quite strictly controlled by the government) can broadcast nationally.[9] Banks have been taxed at high rates based on their assets and not on profits: changing the base from profit to assets and the special tax deductions rules for losses in Ukraine and Russia increased the tax burden for foreign-owned banks, while decreasing it for their domestically-owned or -controlled counterparts.[10] Due to the EC objection to their discriminatory nature, the bank tax rules had to be modified in 2016.[11] The introduction of government regulations on energy prices paid by households, setting price levels too low for profitable operations, forced foreign-owned service providers to sell their stakes in related companies to the state.[12] Changes in regulations caused and are planned to cause competitive disadvantages to foreign-owned retail chains vis-à-vis their domestically-owned counterparts.[13] It is important to note that two EC rulings have already underlined the discriminating nature of the new regulations targeting mainly foreign-owned subsidiaries. On the other hand, vertical, export-oriented manufacturing (in government-speak: 'productive' or 'good') FDI enjoys generous incentives, as witnessed by the automotive industry where foreign investment projects enjoy major privileges.[14]

The ambiguity of Hungarian government policy is underlined by the fact that, by lowering corporate tax, there are more and more incentives for multinational companies to transfer their profits to Hungary and thus save tax. One outstanding example was when the corporate tax paid by General Electric helped improve the Hungarian budget situation.[15] Certain foreign-owned subsidiaries pay corporate taxes at rates well below the 10% threshold characterizing tax constituencies as tax havens. 'German carmaker Audi, for example, did not pay any corporate tax in 2015, as it benefitted from R&D tax allowances. Wizz Air, Suzuki, GE, Mercedes and Bosch paid 1-2% corporate tax, while South Korean electronics producer Samsung was the only one out of the top 10 revenue companies in Hungary whose corporate tax payment (15.9%) was close to the headline corporate tax rate.'[16] At the same time, domestically-owned companies usually face a higher effective tax rate than large multinationals. In 2017, corporate tax rate was further reduced to 9%[17], benefitting mainly large companies[18] and incentivizing multinational companies to further indulge in tax optimisation.

9. See http://budapestbeacon.com/media-issues/ly-state-run-radio-to-broadcast-nationally-in-hungary-from-today/42191

10. See http://www.reuters.com/article/hungary-banks-idUSLDE6AB05520101112 or https://www.ft.com/content/e0c44550-0ad2-11e6-b0f1-61f222853ff3 , and on rate cuts in 2017: http://www.reuters.com/article/hungary-tax-banks-idUSB3N14Q026

11. See https://bbj.hu/economy/hungary-to-change-bank-levy-rules-following-ec-objection_107595

12. See http://bbj.hu/economy/eon-sells-hungary-natural-gas-firms-to-state-owned-mvm_65251 and Szanyi (2016).

13. See http://www.euractiv.com/section/central-europe/news/foreign-supermarket-chains-threatened-by-hungary/ and http://bbj.hu/business/multinational-food-retailers-to-face-strict-regulations-in-hungary_129928

14. See https://www.ft.com/content/e0c44550-0ad2-11e6-b0f1-61f222853ff3

15. See https://bbj.hu/business/ge-hungary-details-impact-of-involvement-in-alstom-acquisition-in-report_117072 and http://bbj.hu/business/ge-hungary-revenue-huf-4452-tln-last-year-following-alstom-merger_116978 and http://www.mkik.hu/en/magyar-kereskedelmi-es-iparkamara/cikkek/hungary-ecomin-secret-revealed-a-single-company-pays-giant-tax-91826

16. See http://www.intellinews.com/hungary-aims-to-become-central-europe-s-tax-haven-110896/

17. See https://www.ft.com/content/302fa4b4-acda-11e6-9cb3-bb8207902122

18. European Commission (2017).

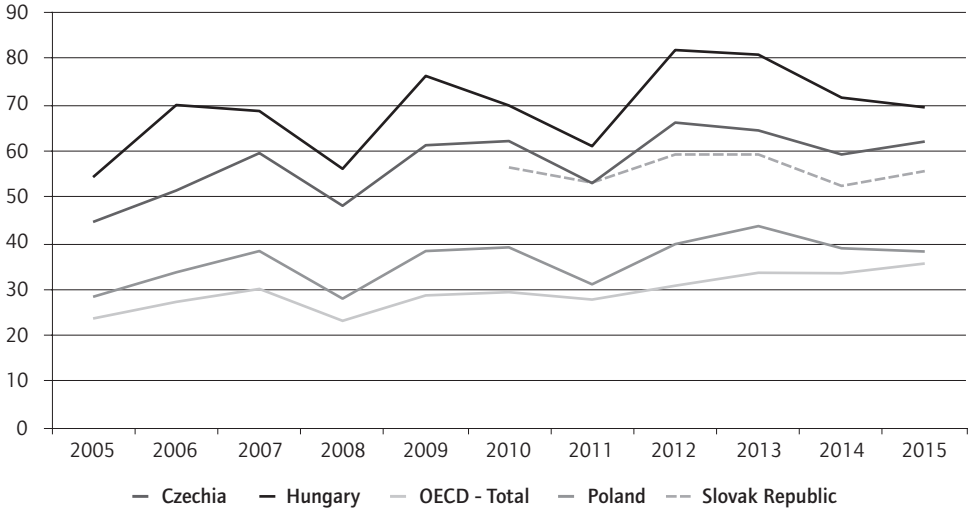
3.2 Changes in FDI inflows

Changes in FDI inflows may indicate that the attractiveness of the countries in question has changed, including the 'welcoming' stance of government policies, or conversely reflect changes in the supply side when less FDI is available to the analysed countries. According to Hunya's chapter in the present book, FDI inflows to the CEE region have clearly decreased. He shows that between 2010 and 2015 the FDI/GDP rate hardly changed in countries with high FDI penetration, but increased in Poland, a country with previously lower exposure to FDI. Furthermore, uniform changes in the Visegrad countries (Figure 4) give a hint of the dominance of the supply-side factor in the smaller FDI inflows. This is supported by the World Investment Report (UNCTAD 2016), which showed that world FDI flows have not regained their pre-crisis levels, or, when they have, that this was due to corporate reconfigurations.[19]

Another important change reported by Hunya in the present book is that domestic private and public investments are becoming more important throughout the CEE region (with the possible exception of Slovakia), meaning that the share of FDI in investment is declining.

However, we call attention to a fact relativizing the role of FDI in the Visegrad countries: the FDI stock/GDP ratio is still much higher than the OECD average in Hungary, Czechia and Slovakia (Figure 4).

Figure 4 **Inward FDI stocks in % of GDP in the analysed countries and in OECD, 2005-2015**



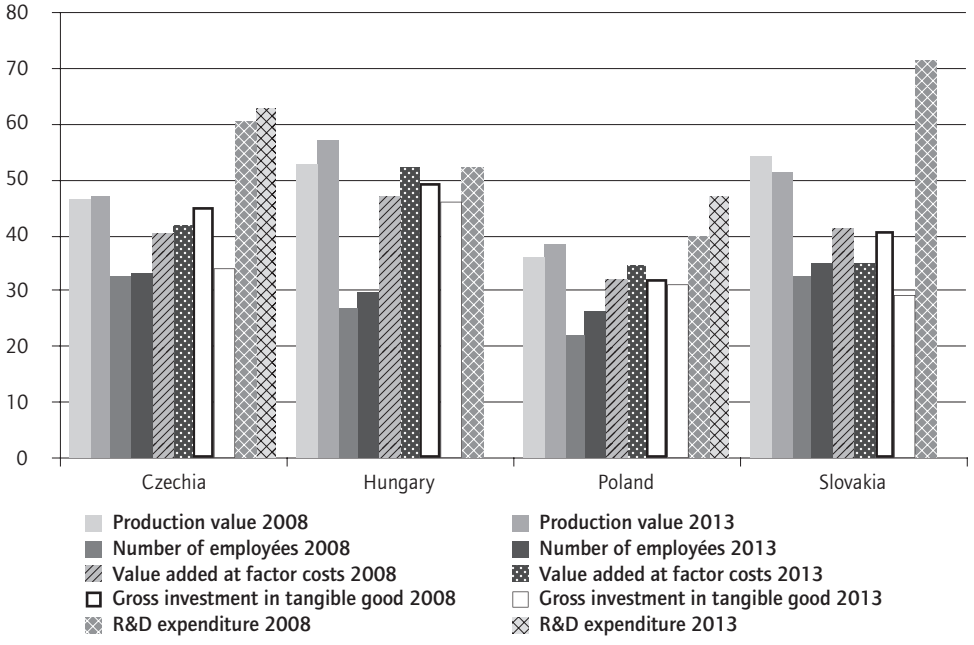
Source: OECD

19. These should be recorded as FDI but they do not comply with the definition of FDI in a strict sense.

Furthermore, the share of foreign-owned companies in production value, employment and value added increased in the analysed countries during the crisis – as already mentioned in the Gábor Hunya chapter (Figure 5). Foreign-owned companies are dominant (i.e. with a share above 50%) in certain areas, e.g. in R&D expenditure, in Hungarian and Slovakian production value, etc. Thus, even with smaller FDI inflows, the better during-crisis performance of foreign-owned subsidiaries compared to domestic companies led to these higher shares and thus greater dominance in the analysed economies. However, it is important to note that by 2013 the share of foreign-owned companies in gross investment in tangible goods declined in all analysed countries, and significantly in Slovakia and Czechia. This underlines the decrease in FDI inflows.

From the point of view of economic growth, it is also apparent from Figure 5 that foreign-owned companies are – and have always been - dominant in R&D in all Visegrad countries – pointing to the relatively low inclination of domestic firms to invest in R&D and innovation. In Hungary for example, domestic companies differ significantly from their foreign-owned counterparts in their inclination to innovate, with their focus solely on low-technology sectors, but not on high- to medium-technology industries. Thus, the different industry composition of subsidiaries and domestic companies may explain the differences in their inclination to innovate (Halpern, Muraközy 2012). This explanation may also apply to the other Visegrad countries.

Figure 5 **The share of foreign-owned enterprises in total production value, number of employees, value added, gross investment in tangible goods and R&D expenditure in the analysed countries, 2008 and 2013 (%)**



Note: ISIC B to N (basically all activities excluding Agriculture and certain Service activities), excluding K (Financial and insurance activities).
Source: OECD AMNE

Overall, FDI inflows to Visegrad countries declined after the crisis, though seemingly as a result of a worldwide decline in FDI flows. On the other hand, the significant – and in certain activities outstandingly high – role of foreign-owned companies has not changed considerably since the crisis. Overall, the FDI climate is still very liberal in OECD comparison. However, anecdotal evidence points at increased pressure being put on 'bad' FDI – as seen in Hungary.

4. Other potential 'growth engines' for the economies

In this section, we look at those groups of companies with the potential to replace – at least partly in certain sectors and industries – foreign-owned companies as economic growth engines. We will take a closer look at state-owned enterprises, (regional) multinationals originating in the analysed countries, large domestic companies and domestic SMEs in terms of their share in the economy and of their performance.

4.1 Changing role of state-owned enterprises

State-owned enterprises (SOEs) allow direct government intervention in the economy on economic and non-economic grounds. Such companies were expected to disappear after the socialist economies of Central and Eastern Europe started embracing capitalism through massive privatisation. However, certain SOEs have survived and have been playing an increasingly important role in the national economies – and some of them even internationally. In certain countries, their role has even increased, alleviating the negative effects of the financial crisis (Götz and Jankowska 2016; PWC 2015).

4.1.1 Importance of SOEs in the Visegrad economies

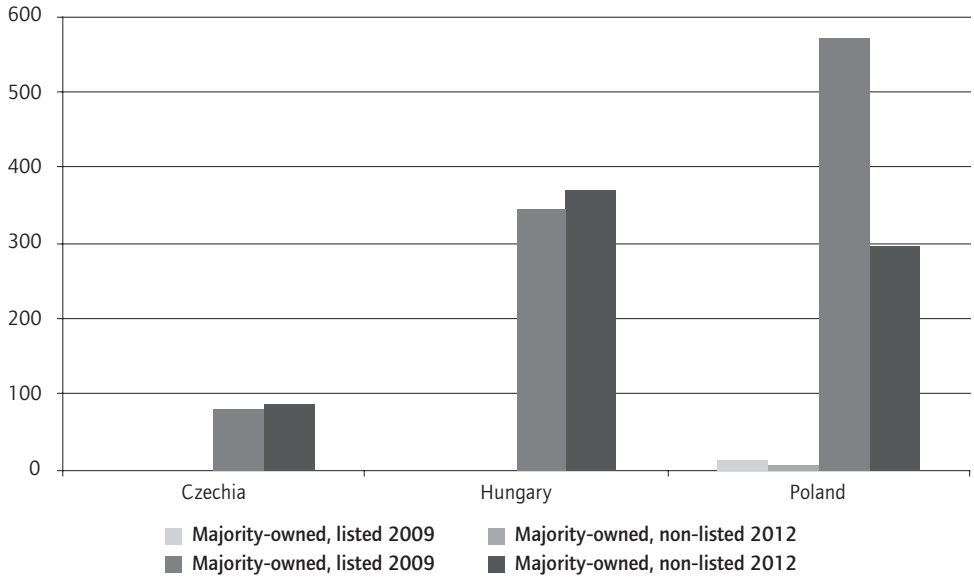
There are different definitions used for determining whether a company can be considered as state-owned or not. According to the OECD, SOEs are enterprises where the state has significant control through full, majority, or significant minority ownership. This can be realised by the central or federal government, as well as by regional and local governments.[20]

Overall, the number and share of SOEs in the Visegrad economies is relatively low, especially considering their recent histories as socialist economies. Based on an analysis of the largest companies (Forbes Global 2000), Kowalski *et al.* (2013) found that the share of SOEs in sales, profits, assets and market values as a % of GNI is not exceptional

20. For analytical purposes, other definitions may be used. For example, in the empirical analysis presented, firms where the state holds at least 20% of the shares are considered as SOEs. However, the authors note that changing to a 50% threshold would not significantly change the results of their calculations. The OECD uses a 50% threshold, distinguishing majority and minority state-owned companies and including both groups of companies in the analysis. (Christiansen 2011) Furthermore, Büge *et al.* (2013) show that a more nuanced analysis may take into account both direct and indirect state ownership. They also use the 50% threshold of (combined direct and indirect) ownership share.

in Poland and Czechia in OECD comparison and is lower than in the BRIICS[21] countries.[22] In the OECD, in terms of the 'economic weight' of SOEs, the Visegrad countries are similar to Scandinavian countries – with a declining trend since 2005 (Christiansen 2011). In the European Union[23], Hungary was ranked sixth, Czechia seventh, Slovakia eighth and Poland 13th based on the share of government participation in the capital of corporations as a % of GDP in 2014. Their shares were not substantially higher than those of the Netherlands, Austria or Ireland from the EU-15. (European Commission (2016) Graph I.2.1, p. 12).

Figure 6 **Number of majority-owned, listed and non-listed SOEs in Czechia, Hungary and Poland, 2009 and 2012**



Note: listed companies: their shares are traded on a stock exchange; non-listed: shares are not traded on a stock exchange; the OECD presents data for listed and non-listed companies separately.
Source: own calculations based on the OECD database, available at http://www.oecd.org/corporate/oecd-dataset-size-composition-soe-sectors.htm

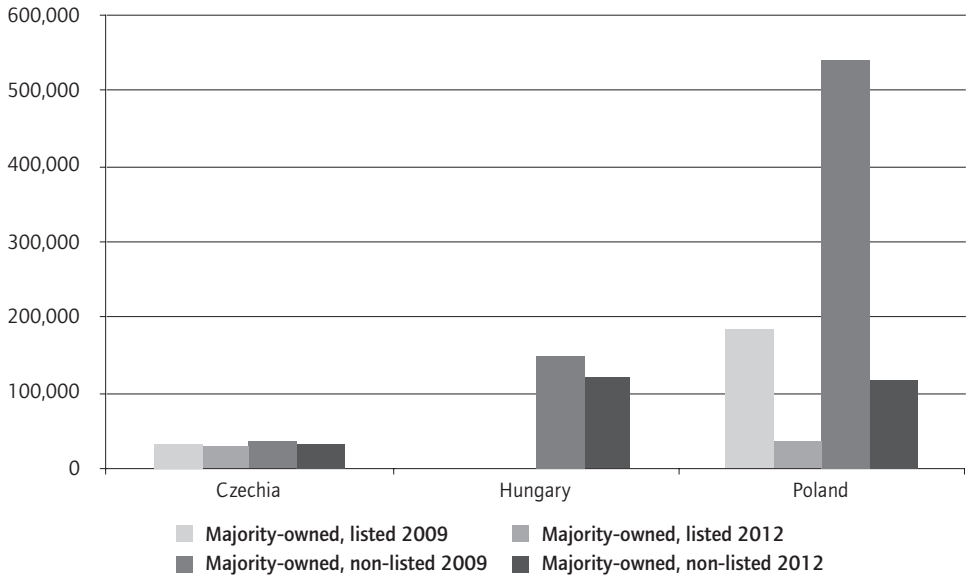
Pre-2010 privatisation, carried out using different methods, led to a decline in the number of non-listed SOEs in Czechia, Poland and Hungary.[24] At that time, SOEs were basically those enterprises which had not been privatised. Furthermore, the state had a minority stake in a number of companies (Christiansen 2013). The number of SOEs dropped further in Poland after 2010, but increased in Hungary, with the result that Hungary, by 2012, had the highest number of SOEs compared to the other two countries (Figure 6) – but their economic significance was still not high in OECD comparison, as many of these companies were quite small and economically insignificant (Christiansen

21. Brazil, Russia, India, Indonesia, China and South Africa.
22. Tables 3 and 4 on pp. 21 and 22 in Kowalski *et al.* (2013).
23. Without data for Belgium, Cyprus, Croatia, France, Greece and Luxemburg.
24. Slovakia did not provide data.

2013). Looking at their market value, they are tiny compared to for example the GDP of the analysed countries. In the case of Hungary, the one majority-owned, listed enterprise accounts for no more than 0.04% of 2012 GDP. In the case of Czechia and Poland, understandably, these shares are even lower: 0.014% and 0.005%, respectively.

Declining between 2009 and 2012, the economic 'weight' of the SOEs is negligible with regard to the number of employees, especially in Czechia and Hungary (Figure 7).

Figure 7 **Number of employees of listed and non-listed SOEs in Czechia, Hungary and Poland, 2009 and 2012**



Source: own calculations based on OECD database, available at http://www.oecd.org/corporate/oecd-dataset-size-composition-soe-sectors.htm

As for more recent developments, Deloitte (2016) points to a continuing decrease in the number of SOEs among the top 500 firms in 18 countries in Central Europe[25]. In 2015, their number was nine in Czechia, nine in Hungary, 34 in Poland and five in Slovakia – altogether 57 enterprises, representing more than two-thirds of the total 85 SOEs in the 18 analysed Central, Eastern and South-East European countries. In Hungary after 2010, their increase was the most pronounced in certain sectors (banking and public utilities), with explicit political aims targeting the 're-nationalisation' of these industries (Mihályi 2015).

The role of SOEs is suspected to be similar to or even higher in Slovakia than in the other three countries. As we see, Slovakia is not usually covered by the OECD analysis

25. The 18 analysed countries are: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Czechia, Estonia, Hungary, Kosovo, Latvia, Lithuania, Moldova, Montenegro, Poland, Macedonia, Romania, Serbia, Slovakia, Slovenia and Ukraine.

of SOEs. The non-transparent nature of SOEs in this country is however underlined in various publications.[26] According to Transparency International, five of the ten biggest employers in Slovakia are SOEs, while the 80 most important SOEs manage assets totalling EUR 9.5 billion, equal to about half of state budget expenditure.

Overall, with the possible exception of Slovakia, the number and especially the economic significance of SOEs tends to be low in the Visegrad countries, meaning that they cannot be considered as alternative growth engines.

4.1.2 Hybrid Visegrad SOEs

The various databases use the traditional definition of SOEs as presented above. However, an important feature of today's SOEs is that the state has a much smaller share of ownership and private entities a much larger share than was previously the case. Furthermore, a new type of SOE has emerged, where state ownership does not necessarily result in state control, and where the latter may be exercised without significant state ownership (Diefenbach and Sillence 2011; Bruton *et al.* 2015). These changes are also to be seen in the Visegrad countries (see e.g. for Poland Baltowski and Kozarzewski 2016, for Hungary Szanyi 2016 or, for one Hungarian state-owned company, Antalóczy and Sass 2016). Why is this distinction important? SOEs were previously established for certain social or economic purposes (employment creation in general or for certain groups of people, carrying out R&D of strategic importance, providing public services etc.). Nowadays, with the higher share of private ownership, certain SOEs operate as if they were completely private, with a focus on profit maximisation. Overall, SOEs often combine commercial and non-commercial objectives (European Commission 2016).

These recent changes justify why SOEs are defined on the basis of state control rather than state ownership. According to the European Commission (2016), direct state control over business enterprises has decreased significantly in Czechia and Hungary among the analysed countries. We can thus assume that at least part of Visegrad SOEs are operating on lines more similar to private enterprises. On the other hand, we have anecdotal evidence that Visegrad governments have strengthened their influence on the governance structure in mixed ownership companies (Szanyi 2016). Hybrid SOEs – in circumstances of changing regulations and policy stances – consequently provide, in countries with less strong protection of minority ownership rights, an opportunity to increase government influence in the SOE sector and the role of the state as proprietor.

4.1.3 Concentration in sectors – industries

SOEs are generally active in certain sectors providing public services, including health and social insurance, and in 'natural monopolies' such as railways and electricity

26. See e.g. the report of the Transparency International Slovakia http://www.transparency.sk/en/slovenske-statne-firmy-su-netransparentne-a-spolitizovane/ or Nechala *et al.* (2015), which concentrated on the operational transparency of publicly-owned companies in Slovakia. In the various fields related to transparency, the score was lowest for Slovak SOEs compared to Czech, Slovak private and foreign companies. 81 state-, city- or county-owned companies were analysed. State-owned ones dominate (a total of 43), followed by city-owned (34) and county-owned (4).

transmission, and Visegrad countries are no exceptions to this rule. In 2015, the overwhelming majority of the 85 large Visegrad SOEs were active in the energy and resources sector (59 companies) and consumer business and transportation (15 companies) (Deloitte 2016).

Other information sources further highlight the dominance of these sectors. Looking at data on listed entities, we find for example that CEZ, a Czech company in which the state has a 63+% stake, operates in the generation, trading and distribution of power and heat, as well as coal mining.[27] According to the Czech Ministry of Finance[28], Eximbank and the Export Guarantee Agency, CEZ, the Congress Centre Prague, CEPRO (fuel trade), Czech Airlines and MERO (crude oil pipelines) are by far the largest Czech SOEs based on their base capital. All these companies are focused on the domestic market, with negligible exports.

In Hungary, two important listed minority SOEs are significant exporters and foreign investors: MOL (oil and gas) and Richter Gedeon (pharmaceutical industry). The other companies mainly serve the domestic market. Despite the high level of internationalisation of the industry in which it operates, Rába Holding, a company with 74.34% state ownership and producing (parts for) commercial vehicles, agricultural machinery and earthmovers as well as automotive components and specialty vehicles, only operates on the domestic market.[29] There are 370 majority-owned, non-listed SOEs with negligible market values, except those in finance (mainly EXIMBank-MEHIB), electricity and gas (mainly the Paks nuclear plant and other power stations) and transportation (Hungarian Railways, bus companies) (OECD 2014), again mainly serving the domestic market.

In the case of Poland, according to the OECD database (2014), among the six majority state-owned listed entities in 2012, three operated in the primary sector, one in manufacturing and two in electricity and gas. Among the ten minority-owned and listed firms, two were active in mining, three in manufacturing, three in finance, one in electricity and gas and one in other utilities. Companies in the primary sector and in finance have the highest market value.

In Slovakia, it is mainly public services which are operated by the state. We have detailed information on the energy sector, where combined state and private ownership is common. The state owns 100% of the shares of the national gas supplier Slovak Gas Industry, 51% in all electricity distribution companies, and 49 % in the gas transmission system operator.[30] As stated by Nechala *et al.* (2015), the 'usual' public services (transport, forests, water and electricity management, power plants, post, the exim- and

27. https://www.cez.cz/en/cez-group/cez-group.html

28. http://www.mfcr.cz/en/themes/state-property-management/2016/the-shareholdings-of-the-czech-republic-26340

29. http://www.raba.hu/english/our_profile.html, according to its balance sheet, the company had no exports in 2015, while 0.3% of sales were realised abroad in 2014.

30. Furthermore, in December 2015 the Italian (actually state-owned) utility company Enel signed an agreement with the Ministry of Economy granting the state an option to increase its stake in Slovenske Elektrarne, which controls 73% of the domestic electricity generation market, by an additional 17% (thus reaching a 51% majority), see https://www.export.gov/article?id=Slovakia-Competition-from-State-Owned-Enterprises

development bank, radio and television, the national lottery, airports etc.) can be found among state-owned companies.[31]

Overall, SOEs in the Visegrad countries are active in certain public services and utilities, with a few exceptions, especially in Poland and Hungary.

4.1.4 Performance of SOEs

Looking at country-level data for the Visegrad economies (European Commission 2016), SOEs perform considerably worse than their private counterparts, limiting – together with their sector and industry distribution and export intensity - their potential role as growth engines. This is to be expected given the *raison-d'être* of SOEs, as some of them have motives other than profit. In the period between 2004 and 2013, the return on equity in private firms was in most cases substantially higher than in SOEs, though the difference narrowed during the crisis years, due to a severe decline in private company profits. Furthermore, the average return on equity for SOEs turned negative during the crisis years in Hungary and Poland. For the same period, another sectoral analysis[32] (European Commission 2016) showed that the return on equity for SOEs was significantly lower in all industries, except for transport and storage. Underlining political influence, one interesting finding is that the profitability of state-owned enterprises in energy and public utilities is significantly lower in election years. Using TFP[33], SOEs perform worse than private companies in certain industries where their presence is not common: in consumer staples, chemicals and metal processing, i.e. mainly in manufacturing industries. However, in other industries the difference is either small or basically disappeared during the crisis. At country level, Visegrad SOEs underperform private ones in consumer staples in Hungary, and in public utilities in Czechia. This is backed by the result of an analysis of Hungary, where in 2015, the majority of SOEs were still loss-making.[34] In Czechia, CEZ Group is the most profitable and the least indebted power company.[35] Looking at labour productivity, the situation was similar to TFP. This analysis also showed that improved governance has a positive effect on both SOE productivity and profitability. SOEs negatively impact allocative efficiency in the industries where they are present, especially in Hungary and Slovakia. According to one analysis, similar to those of the other three Visegrad countries, Slovakian SOEs perform weakly.[36]

As for their impact on exporting, the industry breakdown of SOEs and their limited presence among manufacturing companies in the Visegrad countries indicate that their share in total exports is quite low, except for certain industries, especially in Hungary.

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31. http://www.transparency.sk/wp-content/uploads/2015/12/statne_firmy_web_a5_eng.pdf
32. This analysis was carried out on eight countries, the Visegrad countries + Bulgaria, Croatia, Romania and Slovenia.
33. TFP: total factor productivity, measures the efficiency of the contribution of the inputs (labour and capital) to production.
34. https://www.opten.hu/kozlemenyek/javuloban-az-allami-cegek-eredmenyessege-de-donto-tobbseguk-meg-mindig-veszteseges
35. https://www.cez.cz/en/cez-group/cez-group.html
36. https://www.export.gov/article?id=Slovakia-Competition-from-State-Owned-Enterprises

4.1.5 The regulatory role of SOEs

As stated by Christiansen (2013) in an interesting analysis, the main purpose of state ownership in Hungary is as an alternative to overregulation, and in certain sectors this assures sufficient investment. This contrasts substantially with the other, more developed countries analysed in the cited paper (Israel, the Netherlands, New Zealand and Norway), but may be similar in other Visegrad countries. It is also stated that Hungarian SOEs are directly monitored by the state (in contrast to other developed OECD countries), with specific targets set for them and possibly with instructions to depart from normal earnings targets (i.e. fulfilling non-commercial aims). This points to the hybrid nature of Hungarian SOEs, allowing them to be classified as for-profit or non-profit organisations. For–profit organisations are expected to perform well compared to comparable private firms, while non-profit companies can supplement their market earnings with various sources, including subsidies and levies. 'Hungary is very transparent about non-commercial objectives in designated public interest companies, but much less so in the case of for-profit SOEs with certain non-profit assignments' (Christiansen 2013: 15). We can suspect this increased state involvement to be found in the other three Visegrad countries as well, leading us to the next 'role' played by government: as a regulator.

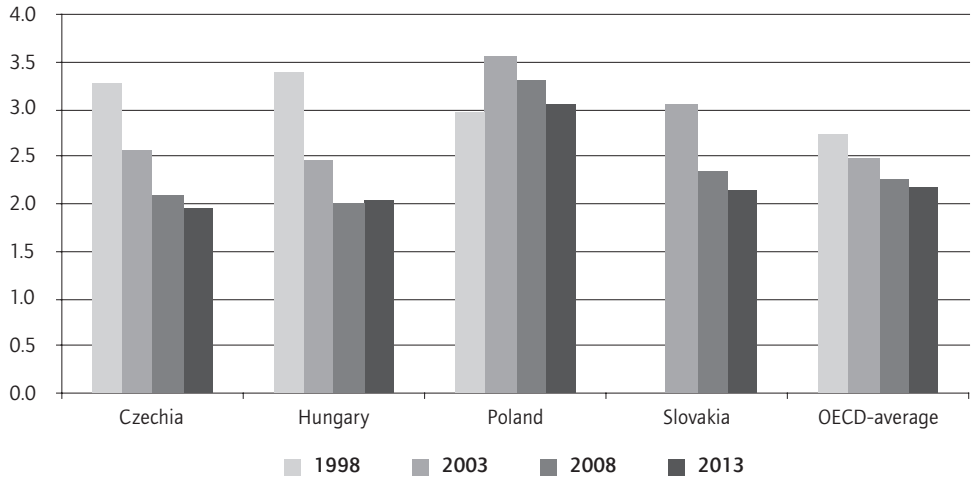
The role of the state as a regulator, shaping the business environment of the individual Visegrad economies, may also be important – as it indirectly impacts FDI and foreign-owned companies operating in the countries in question[37]. The higher state activity in this area can partly be attributed to the heritage of the socialist era. Measuring and comparing the extent of the regulatory role of the state are problematic, given the lack of aggregated data. However, the OECD Indicators of Product Market Regulation provide a comprehensive and internationally comparable set of indicators,[38] measuring the degree to which government policies hinder or promote competition in various product markets. They are currently available for 4 years: 1998, 2003, 2008 and 2013 and for all four analysed countries. We look specifically at the indicator on state control (Figure 8), an index based on two sets of data: data on public ownership (sub-indicators: scope of SOEs, government involvement in network sectors, direct control over enterprises, governance of SOEs) and involvement in business operations (price controls, command and control regulations). It thus partly reflects the role of SOEs in the economies in question, and partly the role of the state.

In terms of trends between 1998/2003 and 2013, all four countries significantly diminished state control in product markets, though this trend seems to have been broken (maybe reversed?) in 2013 in the case of Hungary. However, it is important to note that in 2013, Czechia and Hungary were below, Slovakia around the unweighted OECD average, while Poland's indicator was substantially higher.

Thus, in an OECD comparison, the 'level' of state control can be assessed as low or average (with the exception of Poland) in the Visegrad countries.

37. As could be seen in the section on anti-FDI regulatory government measures in Hungary.
38. See http://www.oecd.org/economy/growth/indicatorsofproductmarketregulationhomepage.htm

Figure 8 **Product market regulation: indicator of state control**



Note: index scale 0 to 6 from least to most restrictive.
Source: OECD

4.2 Visegrad multinationals

Multinational companies are by definition especially competitive, as they can internationalise successfully and perform well in international competition.

4.2.1 Limited outward FDI

According to data on outward foreign direct investment (OFDI), the Visegrad countries can be considered as the most active outward investor countries among the New EU Member States. However, compared to developed countries, their OFDI stock is quite small (Table 1). With the exception of Slovakia, around one quarter of the total outward FDI stock went to other New Member States, pointing to the existence of regional multinationals, while also indicating the importance of non-CEE markets for Visegrad investors. For Slovakia, that share is much higher, mainly due to the high value of OFDI stock in Czechia, partly 'inherited' from the pre-secession period, partly explained by remaining strong economic and cultural ties between the two countries. (Ferencik 2012 or Sass 2017).

However, not all FDI stock can be considered as foreign investments by domestic companies. The data of the national banks on outward foreign direct investments contain values of transactions realised by resident entities, regardless of their ultimate controlling owners. Thus, both direct and indirect (i.e. realised by local subsidiaries of foreign multinational companies) OFDI is included in these data. For example, in Sass (2015) I showed that, of the outward FDI in the electronics sector, the share of domestically-owned companies was around one-third in Hungary and Poland. The majority of OFDI in this industry is realised by local subsidiaries of foreign multinational

companies, such as the Korean company Samsung, the Taiwanese Foxconn or the US General Electric in the case of Hungary. According to Rugraff (2010), in the case of Poland, it may be more domestically-owned and -controlled companies which invest abroad, whereas, in the case of Czechia and Hungary, the share of indirect OFDI, i.e. OFDI realised by local subsidiaries of foreign multinationals, is higher than that of domestically-controlled firms.

Table 1 **Outward foreign direct investments of the Visegrad countries in international comparison, 2012**

	Total OFDI stock (million euros, 2012)	Per capita (euros)	OFDI stock in NMS12	NMS11 in % of total
Czechia	13158	1253	4085	31
Hungary	26592	2686	7217	27
Poland	43644	1143	9875	23
Slovakia	3612	669	2495	69
Austria	158806	18683	...	...
Estonia	4548	3498	3127	69
Latvia	850	425	365	43
Lithuania	1903	595	942	50
Slovenia	5676	2703	212	4

Note: NMS11: Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia.
Source: calculations based on Eurostat data (for Hungary, data of the Hungarian National Bank were used due to missing Eurostat data)

To identify 'real' Visegrad multinationals, we have to go down to company level. For Hungary and Poland, this is easier, because the EMGP[39] reports, respectively Sass and Kovács (2015) for Hungary and Kaliszuk and Wancio (2013) for Poland, of the Columbia Center on Sustainable Investment prepared on the domestic multinationals of these countries list the largest domestic(ally controlled) multinational non-financial companies, based on the size of their foreign assets.

4.2.2 Few domestic multinationals

Overall, relatively large-sized companies with foreign subsidiaries are quite rare in the Visegrad countries. In Czechia, CEZ constitutes a state-owned regional multinational, with subsidiaries in Bulgaria (4 acquisitions in 2005 and 2006), Romania (since 2005), Poland (since 2006), Hungary (close to 8% ownership share in MOL, the petrol company), Slovakia, Turkey and Albania.[40] Other important foreign investors include Zentiva in the pharmaceutical industry and Skoda in the automotive industry, both of which were originally Czech companies, but are now respectively owned by the French Sanofi and the German Volkswagen, i.e. they are no longer Czech-controlled companies (Zemplinerova 2012).

39. Emerging Markets Global Players project at the Columbia Center on Sustainable Investment, see http://ccsi.columbia.edu/publications/emgp/ , analysing multinational enterprises from emerging markets.
40. https://www.cez.cz/en/cez-group/cez-group.html

Turning to Hungary, the OTP bank, the petrol company MOL, the pharma company Richter Gedeon and electrical manufacturer Videoton are multinational companies with substantial foreign assets (more than 100 million USD) (Sass *et al.* 2012; Sass and Kovács 2015). Lowering the threshold to 20 million USD, they are joined by eight other companies (Waberer's and MPF in transportation, Mediso, a manufacturer of medical instruments, Masterplast, producing building materials, Jász-Plasztik in plastics production, Arcadom in construction and Vajda-Papír in paper production). They are however much smaller in both total size and foreign assets than their developed-country counterparts. Expressed in terms of GDP, the foreign assets of the top 20 foreign-investing Hungarian firms represent less than 0.02%.

In Poland, multinational companies are on average larger. There are 12 companies with more than 100 million USD foreign assets (Kaliszuk and Wancio 2013). The two largest and the fifth are active in oil and gas exploration and distribution. The third, Asseco, provides software and IT services. The rest are two chemical and one pharmaceutical companies, two machinery manufacturers, two building materials producers and one wholesale trade and IT services company. Eight more companies have foreign assets exceeding 20 million USD, among them mining, metallurgy, building materials, pharma, software-IT and machinery companies. In terms of GDP, the foreign assets of the top 30 foreign-investing firms represent less than 0.002%.

Small multinationals, among them born globals or international new ventures, exist in all Visegrad countries. They differ from the above-described firms in terms of their target countries, often developed countries. However, their size is much smaller than the above-mentioned top Visegrad multinationals (See e.g. Nowinski and Rialp 2013; Kiss *et al.* 2012; Lamotte and Colovic 2015; Danik *et al.* 2016).

Why do Visegrad companies go abroad? Most often in search of new markets (see e.g. Svetlicic *et al.* (2007) for SMEs or the overview of the literature in Trąpczyński (2016)). As a basis for internationalisation, Visegrad companies can rely on their specialist knowledge on restructuring enterprises previously operating in a planned or an evolving market economy environment, or on brands known from the pre-transition era. Some of them rely on efficiency-seeking investments in geographically close countries with significantly lower wages, transferring labour-intensive activities there. The existence of the efficiency-seeking motive points to the probability of a stronger impact on exports in the analysed countries. The existence of this type of domestic multinationals is featured in a few articles for all four countries (see e.g. Zemplinerova (2012) for Czechia; Sass *et al.* (2012) for Hungary; Gorynia *et al.* (2014); Gorynia *et al.* (2015) or Trąpczyński (2015) for Poland; Ferencik (2012) for Slovakia or Sass (2016) for the electronics industry in Hungary, Poland and Slovenia). However, they are in a clear minority compared to market-seeking firms.

4.2.3 The impact of Visegrad multinationals on their home economies

While relatively understudied, especially in economics literature, certain political economy approaches underline the national character of multinational companies and their positive impact on the development of their home country (see e.g. Doremus *et al.* (1998) or Gilpin (2001)).

First of all, of course, OFDI must be relatively high in order for it to have any sizeable impact on the home economy, which is not really the case in any Visegrad country. Furthermore, the impact on the home economy is rarely analysed, especially in the case of emerging economies and even less in the case of the former transition economies. Empirical evidence is also lacking (Gorynia *et al.* 2015).

Multinational companies can have various positive and negative impacts on their respective home economies. An important beneficial impact can be the increase in the productivity of the investing company through reverse spillovers (Gorynia *et al.* 2015), the extent of which depends on the absorptive capacity of the company in question. There is no conclusive empirical evidence on the existence of these benefits and no analysis exists for the Visegrad countries.

Furthermore, profit repatriation may positively affect the balance of payments of the sending countries. A closer look at the host country composition of OFDI from the four Visegrad countries (Table 2) however reveals that the foreign-investing Visegrad companies quite often target tax havens. This indicates that OFDI can lead to the erosion of the domestic capital and tax base: Visegrad companies and subsidiaries of foreign multinationals investing in third countries are increasingly relying on the tax optimisation opportunities offered by various countries, such as the Netherlands, Cyprus, the Dutch Antilles or Luxemburg (in the Czech statistics, a separate row deals with OFDI to offshore financial centres). However, this is in line with worldwide trends, as pointed out by the 2016 World Investment Report (UNCTAD 2016). Nevertheless, Visegrad OFDI is so tiny compared to that of developed countries or the BRICS that it is hardly visible in global comparison.[41] Though such tax 'optimisation' efforts by multinationals are no new phenomenon, they increased during the crisis years, as pointed out by Hunya (2015) or Antalóczy and Sass (2015). The tax erosion problem is similarly indicated by UNCTAD (UNCTAD 2016), calling attention to the fact that ratios of income attributed to foreign subsidiaries of outward-investing countries to the gross domestic product (GDP) of the economy where these subsidiaries are domiciled reveal profits out-of-line with economic fundamentals.

Thus overall, OFDI is possibly leading to the erosion of the tax base in Visegrad countries, with the possible exception of Hungary which itself acts as a quasi tax haven due to its exceptionally low corporate tax rate.

41. In Hungary, besides this type of 'tax optimisation' OFDI, Special Purpose Entities play a significant role in both inward and outward direct investments, but the Hungarian National Bank calculates FDI data both with and without such entities (Antalóczy, Sass 2015).

Table 2 **Top 10 host countries of Visegrad OFDI and their shares in total OFDI in %**

	Czechia		Hungary		Poland		Slovakia	
	Top host countries	In % of total OFDI stock	Top host countries	In % of total OFDI stock	Top host countries	In % of total OFDI stock	Top host countries	In % of total OFDI stock
1	Netherlands	34.23	Central America (Dutch Antilles)	29.47	Cyprus	37.50	Czechia	31.50
2	Slovakia	18.35	Israel	12.99	Luxembourg	20.63	Cyprus	24.52
3	Germany	7.10	Belgium	10.06	Czechia	7.80	Luxembourg	13.94
4	Cyprus	5.87	Cyprus	7.79	Netherlands	7.54	Poland	7.40
5	Greece	5.43	Croatia	6.95	Switzerland	7.13	Turkey	5.25
6	Ireland	4.15	Slovakia	6.28	Germany	5.43	Netherlands	3.36
7	Offshore financial centres	3.87	Luxemburg	3.48	United Kingdom	4.51	France	2.49
8	Bulgaria	3.12	Bulgaria	2.74	Lithuania	3.61	Austria	2.37
9	Romania	2.01	United States	2.67	Canada	3.14	Hungary	1.72
10	Croatia	1.92	Netherlands	2.38	United States	2.97	Belgium	1.36

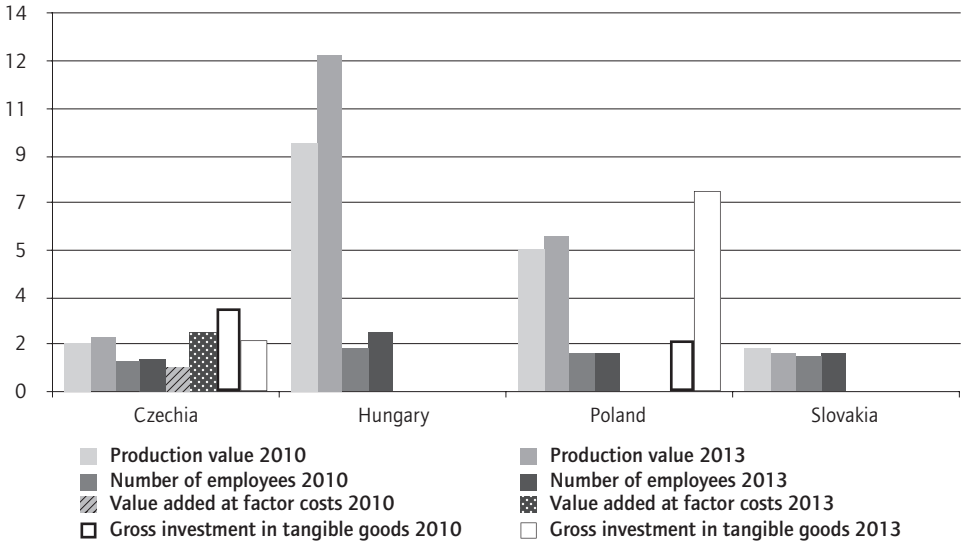
Notes: Czechia: 2014; Hungary: 2015; Poland: 2015; Slovakia: 2014.
Source: national banks of the analysed countries, data on foreign direct investments for Slovakia: OECD FDI database (http://stats.oecd.org/Index.aspx?QueryId=64238#)

One positive effect identified in the case of emerging multinational companies is that, through outward investment, they can acquire hitherto lacking ownership advantages, thus making them more competitive internationally (see e.g. Child and Rodrigues 2005 in the case of Chinese multinationals). Given the characteristics of the companies, such foreign investments may be present in the Visegrad countries as well, though this aspect has not (yet) been examined.

Another impact of OFDI on the home country is the possible reduction of capital available for investment in the home country and the transfer of jobs abroad. However, on the one hand the relatively limited size of OFDI, on the other hand the dominance of the market-seeking motivation over the efficiency-seeking one leads us to the assumption that job losses may be very limited.

The potential magnitude of the impact on domestic economic development can be assessed on the basis of the sporadic data available on foreign subsidiaries of Visegrad MNCs (Figure 9). Their shares are only non-negligible in the case of Hungary's production value and Poland's production value and investment.

Figure 9 **Visegrad-owned foreign subsidiaries' production value, number of employees, value added and gross investment in tangible goods compared to domestic totals, 2010 and 2013 (%)**



Source: own calculations based on data from OECD AMNE

Thus, while the existence of Visegrad multinationals is a fact, they remain quite small compared to their respective economies, with the possible exception of Hungary and maybe Poland, while their characteristics are such that they have yet to have a sizeable overall growth impact on their home economies. Nevertheless, given their concentration in certain industries, they may positively impact these industries in the individual Visegrad countries.

4.3 Are there signs of an increasing role of domestically-owned companies?

These companies may be 'natural' candidates for taking over the driving seat from the foreign-owned subsidiaries of multinational companies – especially if the latter are now less welcome in certain sectors, industries or activities. In this section, two sub-groups of 'natural' candidates are looked at: domestically-owned or -controlled large companies and small and medium-sized companies (SMEs).

4.3.1 Large domestically-owned (or -controlled) companies

There is considerable overlap between large companies on the one hand and state-owned companies and Visegrad multinationals on the other hand, as demonstrated by the Deloitte study (2016) on large (based on their revenues) companies. The following table (Table 3) contains the Deloitte data for the four Visegrad countries. Out of the

500 largest companies of the CEE and SEE region[42], 355 (71%) come from the Visegrad countries (74 from Czechia (14.8%), 67 from Hungary (13.4%), 182 from Poland (36.4%) and 32 from Slovakia (6.4%)), underlining the dominant economic role of these countries in the region.

Furthermore, among large companies, local subsidiaries of foreign-owned multinationals dominate in all four countries, with their share among large-sized companies outstandingly high in Hungary and Slovakia (almost 80%), relatively high in Czechia (more than 60%) and slightly more than half in Poland.

Among domestically-owned companies, SOEs are very important. The share of domestically-owned companies is the highest in Poland (87 firms (48%), of which 34 are SOEs (19% of total)), followed by Czechia (25 firms, 34%, including 9 SOEs (12% of total)). By contrast, domestically-owned companies are almost exclusively SOEs in Hungary (11 firms, 16 %, of which 9 are SOEs (13% of total)) and exclusively SOEs in Slovakia (5 firms, 16%). Different privatisation schemes and speeds clearly have an impact in this respect.

In the cases of Hungary and Poland, a few foreign majority-owned companies can be considered as domestically-controlled and thus as indigenous companies. The reason is that their shares are traded on the local stock exchanges and, though in majority foreign ownership, their ownership structure is dispersed, i.e. no single foreign owner owns more than 10 per cent of the shares. A few of them feature among the top companies as well, such as MOL, Richter Gedeon or OTP Bank in the case of Hungary (Sass *et al.* 2012). However, even with these, the number of domestically-controlled, but not state-owned firms is very low in Hungary and Slovakia, moderate in Czechia and relatively high solely in Poland.

Table 3 **Breakdown of the top companies by ownership (number of companies)**

	Central European company	Foreign individual	Local company	Local individual	Multinational company from outside Central Europe	State-owned	Central European individual	Total
Czechia	3	0	4	12	45	9	1	74
Hungary	3	0	0	2	53	9	0	67
Poland	0	3	21	32	92	34	0	182
Slovakia	2	0	0	0	25	5	0	32

Source: based on Deloitte (2016)

42. The analysis covers the Visegrad countries, the Baltic countries (Estonia, Latvia, Lithuania), Bosnia-Herzegovina, Bulgaria, Croatia, Macedonia, Romania, Serbia, Slovenia and Ukraine.

In the financial services sector, Visegrad countries similarly dominate the list of the top 50 banks in the region with a total of 33 banks (two-thirds of the total). Poland has 15, the Czech Republic 8, Hungary 6 and Slovakia 4. Here again, foreign-owned banks dominate. Only two domestically-owned banks stand out. While the second-placed bank, the Hungarian OTP, can be classified as the only regional multinational (Raiffeisen Research 2016), the top bank, PKO Bank Polski, is 30% state-owned and has the highest market share in the CEE region with 8.2% (mainly due to domestic operations) (OTP Bank 2.9%) (Raiffeisen Research 2016: 63).

Similarly, in the manufacturing sector, the Visegrad dominance is clear among the top 10 firms in the CEE region: we find only two non-Visegrad-based ones. Of the Visegrad companies, three are Czech, three Hungarian and two Slovakian, with subsidiaries of foreign automotive multinationals dominant (Skoda Auto and Hyundai in Czechia, Audi and Mercedes-Benz in Hungary and Volkswagen and Kia in Slovakia). The privately-owned Agrofert from Czechia (food, chemicals and other industries) and the Hungarian subsidiary of the US General Electric also feature in the list of top manufacturing firms.

Overall, 2015 data show the overwhelming dominance of foreign subsidiaries among large companies. Domestic, privately-owned companies are only present in Czechia and especially in Poland in significant numbers.

4.3.2 Domestic(ally-owned) small and medium-sized enterprises

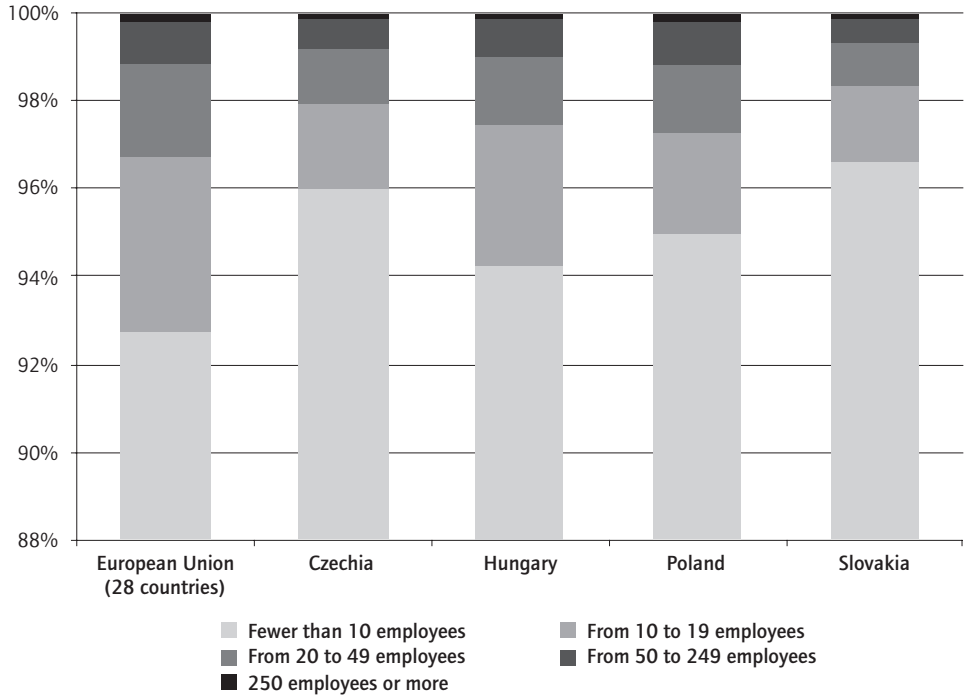
The experience of certain countries and regions shows that the activities of dynamically growing, competitive SMEs can be a basis for dynamic economic growth. In terms of the distribution of the number of companies, the Visegrad countries have a large SME sector, even in an EU comparison (Figure 10).

However, the company population of all four Visegrad countries is skewed towards the dominance of micro-companies with less than ten employees. Compared with the EU, it is apparent that in all four countries the share of micro-companies accounts for more than 94 % of the total number of companies. It is also apparent that the number of companies with 10 to 19 and 20 to 49 employees is less than in the EU28 as a whole. With the exception of Poland, the share of the medium-sized (50 to 249 employees) and large companies (> 250 employees) is also slightly smaller than in the EU28 (Figure 10).

Concerning the sector-industry composition of SMEs in the Visegrad countries, it differs greatly from that of the EU-28 overall (Figure 11). The share of manufacturing and construction SMEs is relatively high (substantially higher than the EU-28 average) in all Visegrad countries except Hungary. Everywhere, the number of wholesale and retail trade companies is the highest, though in Czechia and Hungary it is below the EU average. The number of companies in information and communication, in professional, scientific and technical activities and especially in administrative and support service activities and their share in total is by far the highest in Hungary. Especially in the two latter categories, this high share can be attributed to micro-companies (below 10 employees) in Hungary. Another analysis drew similar conclusions, seeing Czech SMEs as skewed towards manufacturing, Hungarian ones as being mainly involved

in wholesale and retail trade, manufacturing, professional activities and construction, Polish ones concentrated in lower value-added sectors, and Slovakian ones in manufacturing (Daszkiewicz 2014).

Figure 10 **The size composition of companies in the Visegrad countries, 2013**

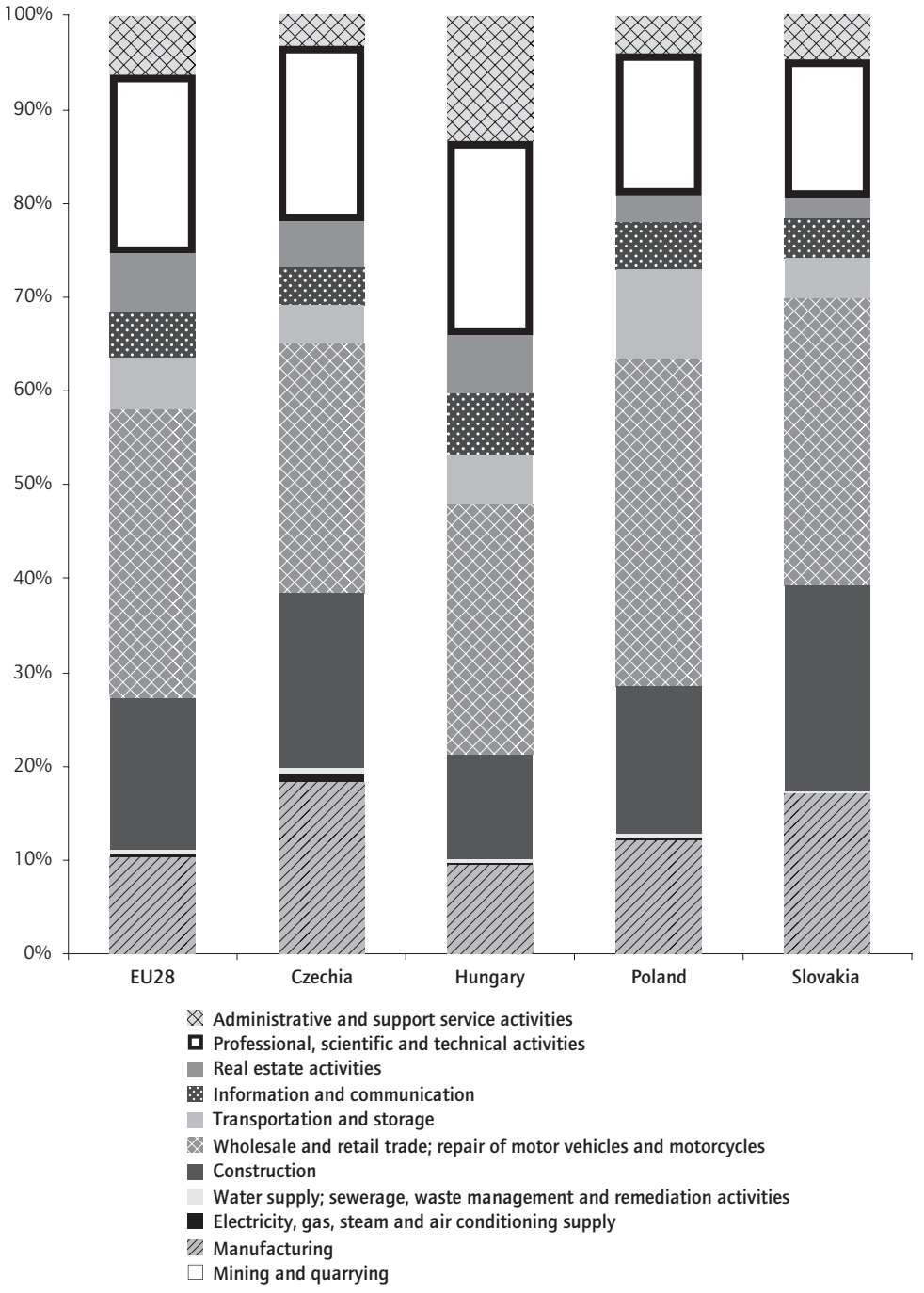


Source: author's calculations based on Eurostat data

The sector-industry composition determines to a great extent the exporting potential of SMEs, meaning that there are wide differences within the country group in the extent to which SMEs contribute to exports. For example, the share of manufacturing SMEs is the highest in Czechia, with Czech SMEs representing more than 50 % of total exports in 2011 (Helisek 2013). In Poland, SMEs were responsible for around 44-45% of total exports in 2012 (45 % to EU and 43 % to non-EU countries) (Lapinski 2013: 38, Figure 5), maybe a result of their relatively high shares in manufacturing. On the other hand, the SMEs of the other two countries perform differently: in Hungary, their share of exports is 26.4% (Mikesy 2013), while in Slovakia – in spite of their relatively frequent presence in manufacturing - it is just 18 %.[43] Part of SME exports can be attributed to foreign-owned enterprises. Unfortunately, the breakdown of the SME group into foreign-owned and domestically-owned was not available for the analysed countries. One reason for the low export contribution could be that micro-enterprises, the dominant company size in all Visegrad countries, generally exhibit very low export/sales rates throughout the European Union (European Commission 2014).

43. http://spectator.sme.sk/c/20049699/sme-exports-remain-low.html

Figure 11 **The sector-industry composition of SMEs (0-249 employees), according to the number of companies, 2013**

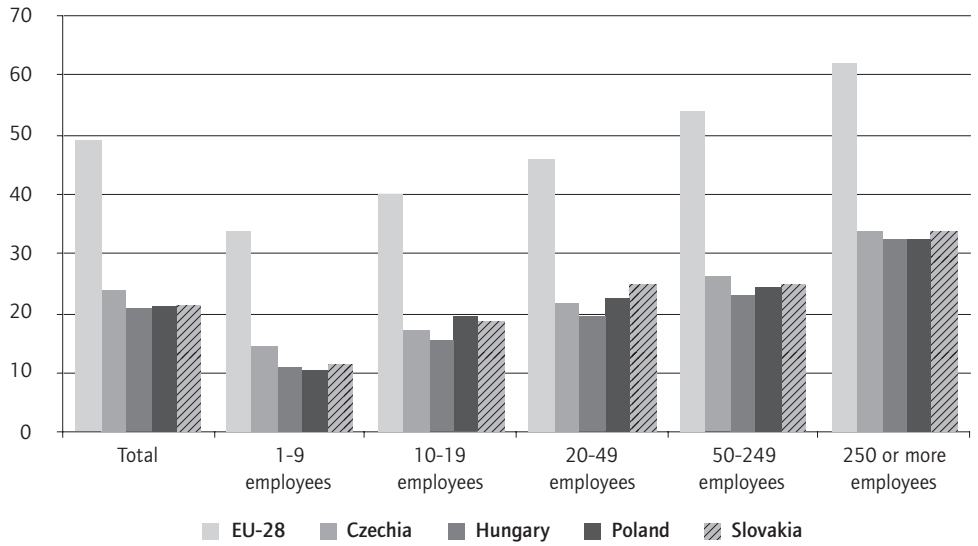


Note: EU-28: 2012 data.
Source: own calculations based on Eurostat data

Overall, the internationalisation of Visegrad SMEs is relatively low. One of the few comparative studies in this area, Gubik and Bartha (2014) base their findings on a survey of Visegrad SMEs resulting in a database on 1124 companies. Important findings in our view are that company size and foreign ownership positively influence internationalisation.

Finally, the performance indicators of SMEs point to their potential role in driving growth in the economies in question. However, the lack of internationally comparable data makes this exercise quite problematic.

Figure 12 **Gross value added per person employed (thousand euros, 2014)**



Source: Eurostat, structural business indicators, Annual enterprise statistics by size class for special aggregates of activities (NACE Rev. 2)

The productivity of all company groups, based on their size, is well below the EU28 average in the Visegrad countries. Productivity correlates with the size of the company (Figure 12), as in other countries. However, beside the similarities, there are some country differences: Hungarian SMEs seem to be the lowest performers of the four Visegrad countries. Czech micro, medium- and large-sized enterprises perform relatively well, together with Polish and Slovakian small-sized ones.

5. Conclusions

The problem of convergence is of paramount economic and political importance for the Visegrad countries. After 1989, with different starting times, all of them relied to a great extent on FDI to catch up with the more developed countries of Europe. In this process, the share of foreign-owned subsidiaries in the respective economies grew well above the OECD averages, with the exception of Poland. Disenchantment with the performance of these MNC subsidiaries in driving growth in the Visegrad economies and accelerating their catching-up with the core EU countries within a foreseeable period can be seen in all four countries. Furthermore, after the short inward FDI 'honeymoon', the crisis years showed that certain forms of FDI increased the vulnerability of the economies in question. In the ensuing low-FDI post-crisis environment with increased profit repatriation, the 'dark sides' of being exposed to foreign capital were witnessed in the region.

In this environment, Visegrad governments are increasingly looking to other potential candidates to drive their economic growth. The rhetoric has changed, with a differentiation increasingly being made between 'good' and 'bad' FDI. However, the generous incentives for and the good treatment of subsidiaries already operating in these countries, especially in export-oriented manufacturing industries, have not changed considerably.

Otherwise very similar, Visegrad countries differ in terms of changes in their approach to FDI and the availability of a 'non-FDI' group of companies to help them catch up. We have shown that there are not many alternatives to foreign-owned subsidiaries and that even these may work differently in the four Visegrad countries. Hungary (and Poland) seem to be the most active countries in trying to reduce the share of and reliance on foreign-owned companies in certain sectors of the economies. As for alternative 'growth engine' groups of companies, Hungary has a small group of strong regional multinational companies, dominating a few industries, while Czechia and especially Poland have a relatively high number of domestically-owned large companies. Czech micro- and medium-sized and Polish and Slovakian small-sized firms seem to be quite competitive.

However, up till now, none of these groups of companies have come to the fore, whether as subjects of economic policy or in economic performance.

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