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Globalización del desarrollo desigual a través de las inversiones extranjeras directas en las economías en transición

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Resumen:

La inversión extranjera directa (IDE) se analiza como un factor de integración de las economías en transición (ETs) en la globalización. Sin embargo, el crecimiento de las empresas multinacionales (EMNs) acelera tanto la globalización como el desarrollo desigual. Así, se observa una clara correlación entre las entradas de IED y el nivel de desarrollo económico (PIB por habitante) en los países del Tercer Mundo y las ETs que se explica en términos de desequilibrio de las IED en el mercado mundial y de desvanecimiento de la capacidad de negociación de los estados nacionales. Las consecuencias de este análisis se obtienen a través de la comprensión de las estrategias de las EMNs en las ETs y en el posible futuro de las IED en estos países, incluyendo Cuba. La conclusión enfatiza el *trade-off* existente hacia las IED para cualquier país (incluidas las ETs), entre una política atractiva y restrictiva, en una economía mundial en la que la dominación de las EMNs descansa básicamente en su capacidad para cortar los flujos de capital a aquellos países políticamente "poco receptivos".

Globalization of uneven development through foreign direct investment in transition economies

Summary:

Foreign direct investment (FDI) is analyzed as an integrating factor of transition economies (TEs) into globalization. But growing multinational corporations (MNCs) accelerate both globalization and uneven development. Thus we exhibit a significant correlation between inward FDI and the level of economic development (GDP per capita) in Third World countries and TEs which is explained in terms of a disequilibrium on the world market for FDI, and in terms of the vanishing nation-state bargaining power as well. Consequences of this analysis are drawn as regards the understanding of the strategies of MNCs in the TEs and the possible future of FDI in such countries, including Cuba. The conclusion stresses the trade-off, for any country (TEs included), between a restrictive and attractive policy towards FDI, in a world economy in which MNCs' domination basically relies on their capacity to sever capital flows to "not enough friendly" countries.

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GLOBALIZATION OF UNEVEN DEVELOPMENT THROUGH FOREIGN DIRECT INVESTMENT IN TRANSITION ECONOMIES[*]

Wladimir Andreff [**]

Foreign direct investment is analyzed in the present paper as an integrating factor of transition economies [1] into globalization. From this point of view, all developing countries are also, to some extent, "in transition" towards their integration into globalization. But this integration is uneven according to the level of economic development of each country, reminding us that we are witnessing, in the last twenty years, a globalization of capital and capitalism which is based on a process of uneven development discriminating among the different countries of the world economy. Today, transition economies compare to developing countries insofar as, by the same token, foreign direct investment integrate the most developed and marginalize the least developed of them from the process of globalization. Such a process is magnified - as we suggest it here - by the global strategies elaborated on by multinational corporations in the framework of which they evaluate the host countries for their investment. Depending on their mode of entry into the transition economies, multinational corporations provide more or less economic restructuring and technology transfer, and have more or less impact on the host country's foreign trade. A last proof of the uneven integration of transition economies into globalization through foreign investment is that some Eastern European firms start yet to invest abroad, just like some enterprises from the newly industrializing Third World countries have achieved it a few decades ago. It seems that it still remains promising perspectives for foreign investors in various transition economies and such forecast must apply to Cuba as well.

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[1] Under the label of "economies in transition " we focus here on a sample of 27 countries which have, at least once, belonged to the former CMEA (Council of Mutual Economic Assistance) or to the former Yugoslav Federation, with the exception of three less developed countries: Cuba, Mongolia and Vietnam. Cuba will briefly be refered to in the conclusion of the paper.

1. Globalization and uneven development: the role of foreign direct investment

Globalization of capital, considered as a new emerging phasis of capitalist development, has not closed the gap between developing and developed countries in the last twenty years. The empirical evidence exhibits quite the contrary and clashes with the claims of globalization propagandists. Uneven development is inherent in capitalism and globalization extends and deepens it, superseding an increasing number of national economic regulations. If we take a minimalist measure, based on the GNP per capita, of the gap in economic development between the poorest country in the world economy - Ethiopia - and the United States, it appears to be from 1 to 293 in 1998 (Table 1b). On the other hand, growing multinational corporations (MNCs) accelerate both globalization and uneven development by means of their foreign direct investment (FDI); such an acceleration is exacerbated through the global strategies adopted by MNCs in the last two decades (Andreff 1996a). Thus, we must expect an existing relationship between the level of economic development of a host country and its penetration by inward FDI. A first empirical evidence pointing at this relationship is the fact that three-quarters of the world inward stock of FDI are welcomed in the developed countries of the so-called Triad (Europe, North America, Japan). However, uneven development brought in by globalization does not stop at the borders of Third World. Quite the contrary. MNC-driven FDI is markedly more attracted toward developing countries enjoying the highest levels of GNP per capita - newly industrializing countries, fiscal paradises - than it is toward the least-advanced countries and intermediary-income developing countries, both of these latter being rather marginalized from globalization by FDI.

The above mentioned role of FDI in uneven development can simply be tested from the data gathered in Tables 1a and 1b. A linear regression of inward FDI stock per capita on GNP per capita, for 136 developing and transition countries, is not statistically significant and shows [2] an adjusted correlation coefficient equal to 0.40. It is usual in most studies that the correlation between FDI and economic development does not exhibit a very high correlation coefficient because the relationship between the two variables is disturbed by a size effect (different among countries), by the fact that some developing countries are fiscal paradises or free zones and by the rich endowment in raw materials which attracts MNCs even in the least-developed countries. Thus, it is quite common to rather estimate a rank correlation between inward FDI stock per capita and GNP per capita (M.

[2] The result of the regression is : FDI per cap. = 0.43 GNP per cap. - 119.48.

Andreff, W. Andreff 1997), *i.e.* to calculate a Spearman coefficicient of rank correlation given by : $r_S = 1 - \frac{6\sum_i d_i^2}{n(n^2-1)}$

where d_i stands for the difference between the rankings of a country according to the two variables and n for the sample size. We can then conclude at a concordance (a positive coefficient close to 1) or discordance (a negative coefficient close to -1) or no relation (a coefficient close to zero) between the ranks of two variables. If the coefficient of rank correlation is not significant, then the two variables are independent. Calculated for the 136 developing and transition countries (Tables 1a and 1b), the coefficient is significant and its value is 0.76. There is a good concordance between FDI and the level of economic development, in spite of the disturbances introduced by the existence of fiscal paradises, free zones and so on. The same calculation on the sample of only 24 transition countries (Table 1c) gives the following results:

. a better adjusted correlation coefficient (0.51) for the linear regression of FDI per capita on GNP per capita;

. a slightly lower rank correlation (0.65) between the two variables.

However, two causalities may underlie the observed correlation between FDI and economic development. The interpretation provided by mainstream liberal economists is that economic development is caused and triggered by foreign investors. What such an assumption means must be underlined: the other side of the coin is that economic under-development in the least developed countries is caused by the abstention of foreign investors. This logical consequence of the mainstream liberal interpretation is not often stressed on while it reveals that globalization is not good for everyone, a conclusion steadily denied by the economic mainstream. The strategies of MNCs are thus called into question. An alternative understanding of the correlation between FDI and economic development, on the contrary, would contend that only those countries which have reached a rather high level of economic development are likely to attract a significant inflow of FDI whereas MNCs desert - and by the same token turn into an economic desert - the poorest countries of the world. We will keep such a view in mind in order to interpret the impact of FDI on economic development since it is quite consistent with the global strategies adopted by MNCs (Andreff 1996a) in the phasis of capitalist globalization. Crowding in the most developed countries and crowding out the least developed countries is the unavoidable result of the economic evaluation of potential host countries by MNCs on profitability criteria before any investment decision making.

2. The integration of transition economies into globalization through foreign direct investment

Think first of FDI as being supplied on the world market by MNCs and other potential foreign investors. The demand for FDI is coming from host countries. Until the 1970s , in a period usually pointed at as one of internationalization of capital, there was an excess supply of FDI by MNCs eager to enter newly independent States and new industrializing countries in the Third World, and to develop their market shares in the Triad countries, while the world economy was in excess liquidity after Keynesian policies and the oil shock. Financing FDI was an easy task. On the other hand, most developing countries were conducting restrictive policies towards FDI inflows, for the sake of maintaining their newly reached independence. In terms of disequilibrium economics, host countries were on the short side of the FDI market and, in terms of political economy, their nation-states were capable to impose their strong bargaining power to foreign investors.

Since the 1980s, and even more so in the last decade, with the emerging process of globalization, it has appeared an excess demand on the world market for FDI. Facing foreign debt constraints and unemployment, nearly all developing and developed countries started to strongly compete for attracting FDI and elaborated on very friendly attractiveness policies in the framework of overall neo-liberal economic policies. On the other hand, the world economy became shorter in liquidity, due to stabilization and adjustment programmes based on restrictive monetary and fiscal policies, while MNCs started to react to any kind of restrictions imposed on FDI by host countries in the 1970s, such as TRIMs (trade-related investment measures), strategic sectors closed to FDI, participation of local capital into the foreign affiliates and even nationalization of affiliates in the Third World. The MNCs' reaction consisted in shortening their supply of FDI to the most hostile host countries and concentrating it in the most friendly countries, namely developed countries, newly industrialized countries and fiscal paradises. In terms of disequilibrium economics, MNCs have moved on the short side of the world market for FDI and, in terms of political economy, they are now increasingly imposing their trade-offs to competing host countries. Such a strategy adopted by MNCs has strengthened the uneven distribution of capital, via FDI, and has therefore reinforced uneven development detrimental to developing countries, primarily to the least developed of them.

It is the world economic context in which centrally planned economies broke up and newly transitional countries entered as newcomers on the world market for FDI, thus widening the gap between excess demand and short supply. These newcomers have a level of economic development (Table 1a and 1b) which ranks them somewhere between the newly industrialized countries (as regards, for instance, the Czech Republic or Hungary [3]) and , at the other end, the least developed

[3] With the noticeable exception of Slovenia whose level of economic development is over the one of Greece and Portugal.

countries (Kyrgyzstan and Tajikistan have a GNP per capita of about $350). They have immediately had to compete among themselves and with the rest of developing countries all over the world economy in order to attract FDI. Given the distorted industrialization, the under-development of commercial services and the low-productivity agriculture inherited from central planning, there was no economic grounds - in the early nineties - on which could be based a very high initial expectation as regards the capacity of Eastern Europe to attract a large amount of FDI likely to help and sustain the transition process. Western business optimism as to the FDI potential in transition economies has developed more on the ground of political will and wishful thinking than on the basis of a sound economic analysis of MNCs' strategies and the harsh competition between host countries. Besides, such an optimism did not pay attention to the fact that FDI is a magnifying factor of uneven development because it concentrates on the most developed economic areas (Central Europe) and deserts the least developed (the Balkans and the former USSR) [4] .

The empirical evidence confirms our statement (Table 2). In 1998, Central Europe (the Czech Republic, Hungary, Poland, Slovakia, Slovenia) was attracting 58% of the overall inward FDI stock (99 billion dollars) entering the sample of 27 transition economies; the ten CEECs were concentrating 69% of the overall stock while the CIS countries - Russia included - were attracting only 29% of it, and the Balkans 2%. The more developed an economy, the more attractive it is to FDI: the Central European countries (except Slovakia) and Estonia exhibit the highest inward FDI stock per capita (Table 3) in our country sample. As regards the ratio of inward FDI stock to GDP, some of the former five countries are only outstripped by countries (Azerbaijan, Kazakhstan) well endowed with hydrocarbons and other raw materials attractive to MNCs. Finally, if we consider the inward FDI stock per capita in 1998 (Table 1a and 1b), the Czech Republic, Estonia and Hungary compare to newly emerging (industrialized) countries, being ahead of Argentina, Tunisia or Brazil, but lagging behind Malaysia or Chile. Poland, Slovakia and Lithuania are in the range of Mexico, Bolivia, South Korea and Colombia. Romania and Bulgaria match China, Ivory Coast and Morocco while Russia appears as open (*i.e.* rather unattractive) to FDI as Sri Lanka, Togo and Cameroon.

3. The strategies of multinational corportations towards transition economies

[4] In the following, we distinguish three sub-areas among the whole sample of transition economies. Central Eastern European countries (CEECs) gather Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia. The members of the Commonwealth of Independent States (CIS countries) are Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan. We count in the Balkans Albania, Croatia and Macedonia (Bulgaria and Romania are already included in the CEECs) since there is no significant inward FDI in Bosnia-Herzegovina and Yugoslavia until now.

There are four stylized strategies of MNCs today: 1/ outsourcing, 2/ market-seeking or demand-oriented FDI, 3/ production relocation in search of lower costs abroad, namely lower unit labour costs, 4/ a global strategy mixing and trading-off between the three previous strategies with an attempt at flexible worldwide location in order to implement global networking, global switching, and global focusing (Andreff 1996a).

Facing MNCs with an outsourcing strategy, the host country comparative advantage basically relies on the supply of cheap sources of adequate inputs. A good example in Eastern Europe is the Russian endowment with fuels so that fuel production attracts 13% of inward FDI stock in Russia, whereas the primary sector gathers hardly more than 2% of FDI stock in the CEECs. The comparative advantage of a country for a demand-oriented foreign investor consists in a large market size and a high level consumer wealth (usually measured by the domestic income per capita). In various studies (namely Maroudas, Rizopoulos 1995, Meyer 1998), these factors appear to be the main determinants of FDI in Eastern Europe: taking over new outlets, putting a foot in the door and utilizing a window of opportunity express this market-seeking approach of MNCs. Demand has obviously determined FDI in the food and automotive industries and in most services (trade, hotels, resraurants, real estate), *i.e.* the great bulk of FDI in the CEECs, and namely over 40% of the overall inward FDI in the Czech Republic, Hungary, Poland and Slovenia. We have found (M. & W. Andreff 1997) a good correlation between inward FDI stock per capita and GDP per capita on the whole sample of transition economies, as well as a significant coefficient for the regression of inward FDI stock on GDP per capita and an index of FDI attractiveness (see below) for the same country sample.

In view of relocating their production abroad, MNCs are looking for host countries with low unit labour costs (ratio between real wages in hard currency and labour productivity). In this respect, the CEECs have exhibited a low unit labour cost in the first years of transition due to a dramatic drop in real wages not compensated by the fall in labour productivity. Such a comparative advantage has attracted foreign producers in the CEECs in early 1990s, by means of either FDI or subcontracting with local firms. By mid-1990s, with the economic recovery, wage increases were often more rapid than the growth of labour productivity, so that the unit labour cost advantage started to shrink and it would probably vanish in the long run. The calculation of a correlation between inward FDI stock and an index of unit labour cost on the whole sample of Eastern European countries gives a non significant result (Andreff 1999a). However, some studies have found a significant relationship between these two variables (Lansbury *et al.* 1996). The industries most concerned with production relocation in transition economies are textile and clothing, leather, machine building and electrical equipment. In the CIS countries, the unit labour cost was not as much friendly to FDI as expected from the collapse

of nominal and real wages. This is due to a very low and sharply decreasing labour productivity following the output fall. This is confirmed by the fact that production relocation seems to have developed only in machine building in Russia for instance.

Global strategies are exemplified by MNCs looking for all the three comparative advantages but also by the integration of their local plant in their worldwide network of affiliates as, for instance, all the motor car companies that have invested in Eastern Europe. This applies also to MNCs investing in electronics, precision tools and services. With a global strategy, a MNC can threat to leave the country if some comparative advantage disappears (Andreff 1996b). The few disinvestments that have occurred yet from Eastern Europe provide a proof of existing global strategies, though they have often been triggered by managerial and corporate governance difficulties with the local partner or the state.

In the context of globalization, MNCs assess the comparative attractiveness of various potential host countries before any investment decision making. In addition to comparative advantages, the host country attractiveness encompasses a good investment climate, a low country-risk and a fair treatment of foreign investors, all dimensions that can be indirectly influenced by economic policy in the host country. When assessed with the basic macroeconomic variables such as inflation rate, interest rate, the GDP rate of growth, unemployment, the variation of investment and foreign trade balance, the investment climate of a host country is one important element of its attractiveness to FDI. IMF-sponsored economic policies are supposed to improve at least some of these variables and thus upgrade the attractiveness of transition economies. We have tested (Andreff 1999a) a good correlation between an aggregated index of investment climate (macroeconomic variables) and inward FDI stock per capita on the whole sample of transition economies up to 1996. The correlation is even better when the variable FDI stock per capita is delayed, meaning that inward FDI does react to the investment climate with roughly a one year delay.

Country-risk has improved in all the region during the 1990s but it remains rather high in the CIS countries most of which are not ranked among the 100 better risks in the world. Slovenia, the Czech Republic and Hungary are usually among the 40 better risks, and they are (with Estonia) the countries that have attracted the largest FDI stock per capita so far. The other CEECs are between the 40th and the 80th rank with Third World emerging market economies, lagging behind developed countries and being ahead of developing countries, in an intermediary position in terms of country risk. The treatment of FDI has liberalized and adjusted to foreign investors' requirements all along the 1990s in transition economies. This treatment refers to the content of the foreign investment code of the host country, tax incentives and tax holidays, profit repatriation, securing private property rights and a fair juridical treatment of foreign investors compared with their local competitors. In particular, a fair treatment consists in opening domestic privatization programmes to FDI.

In the early 1990s, Poland and the Czech Republic have lagged behind Hungary and Estonia in attracting FDI due to the primary use of privatization techniques (employee-management buy out and mass privatization) leaving no room to foreign investors, while Hungary and Estonia have proceeded with privatization based on asset sales open to foreign stakes. As a result, the two latter countries have got both the most successful privatization drive and the highest share of FDI in GDP and in domestic privatized companies. In Hungary, the overall number of enterprises with foreign participation was over 34,000 in 1997, including 150 out of the first 200 biggest firms in the country. The low attractiveness of most CIS and Balkan countries results in their low ranking as regards inward FDI stock per capita and the ratio between FDI and GDP (with the exception of Azerbaijan and Kazakhstan - hydrocarbon producers). Attractiveness variables thus have a good explaining power of FDI concentration in a few most developed CEECs and of MNCs' abstention in the least developed CIS countries of Caucasus and Central Asia. In transition economies, FDI exactly follows the slope of uneven development.

Let us finally note that German MNCs are the most important investors in the Czech Republic, Hungary, Poland, Slovakia and Belarus, while their presence is still important in Bulgaria, Romania, Russia and Slovenia. American firms have the lead in Croatia, Russia, Ukraine and Lithuania, and a good share of FDI in Hungary (after German MNCs). Dutch MNCs have a significant share of inward FDI stock in the Czech Republic, Belarus, Poland, Romania and Hungary, British MNCs in Slovakia, Hungary and Latvia, French MNCs in Poland, Slovenia, Romania and Slovakia, Swiss MNCs in Croatia, Ukraine and Moldova, Finnish and Swedish MNCs in Estonia and Lithuania, and Danish firms in Latvia. Note also that South Korean firms have the third rank as foreign investors in Romania.

4. Modes of entry and economic impact of multinational corporations on transition economies

Three modes of entry are usually distinguished: 1/ greenfield investment and reinvested profits; 2/ merger and acquisition; 3/ the so-called 'new forms of investment', in the OECD parlance, which spread from joint venture to minority-owned affiliates, technical assistance, licensing, franchising, international subcontracting, industrial cooperation, turnkey projects and so on. MNCs prefer joint ventures to acquisition when the local firm bears heavy sunk costs, when they can access to knowledge or tangible assets of local firms and when they hold up important technological or organizational advantages. In transition economies, acquisitions are mostly related to the privatization process and are undertaken by MNCs with capabilities to restructure local plants. The cumulative FDI related to privatization peaked up in 1995 when it reached 60% of overall FDI in the region (73% in

Hungary). Afterwards, it strongly dropped and the major tendency, at least in the CEECs, is towards greenfield investment, contrasting with a worldwide trend towards merger and acquisition FDI (Meyer 1998, UNCTAD 2000). MNCs with specific assets and unique competencies prefer greenfield operations. The rise of the latter probably means an inflow of competencies and assets, brought by MNCs, likely to adapt transition economies to the requirements of globalization.

Even though it is not a specific mode of entry, properly speaking, "brownfield" FDI must be mentionned as the result of the low attraction of the physical assets in Eastern Europe. MNCs acquire a local firm or form a joint venture, but establish completely new production facilities close to the old factory and utilize this latter as a reservoir of skilled employees. Brownfield projects are explained by the low attractiveness for MNCs of obsolete physical assets inherited from the planning period and the highly skilled manpower available in transition economies. We cannot refrain from calling into question what appears to be a somewhat predatory behaviour of this mode of entry adopted by some foreign investors.

Joint ventures and subcontracting are primarily considered by MNCs as temporary arrangements and are privileged in more risky countries. They usually are phased out to leave the country in case of worsening risks or substituted with majority or full ownership of affiliates when the investment climate improves. Joint ventures are in the range of roughly 35% of overall FDI in most advanced CEECs (Central Europe), 50% in other CEECs and 60% in CIS countries in 1995, according to an EBRD survey. Subcontracting and licensing accounts for 7% in most advanced CEECs, 10% in other CEECs and 20% in CIS countries, *i.e.* in the most risky countries of the region. Joint ventures are concentrated in the automotive industry, construction and energy production. Subcontracting is mainly resorted to in textiles, machine building and electrical equipment. It has been a very active strategy of German and Italian firms in the CEECs triggered by low unit labour costs in the first years of transition and the opportunity of developing outward processing trade with EU countries in the framework of association agreements (M. Andreff, W. Andreff 2001). This empirical evidence demonstrates that the mode of entry is strongly influenced by legal arrangements and the determinants of FDI which prevail for each industry and each country.

However, in case of minority control or joint venture, the foreign investor may be confronted to a problem of weak corporate governance as it has been exhibited in a sugar refinery acquired by Feruzzi in Hungary for instance. Thus, control structures matter. According to an EBRD survey (Lankes, Venables 1996), in 1996, on average, wholly-owned affiliates were making for 38% of the sample as against 51% for joint venture and 11% for subcontracting and licensing in transition economies. In most advanced CEECs, full ownership had been yet substituted to temporary and less

involving arrangements, and its share was reaching 58%. The choice of control structure appears to be much influenced by the host country economic environment.

The economic literature on privatization and restructuring in Eastern Europe provides here some robust findings (a litterature surveyed in Andreff 2000, 2001). Firms privatized by means of asset sales to foreign investors are those which have the most improved performance in terms of profitability, productivity and labour shedding, compared with public enterprises and privatized firms under the control of insiders (personnel and managers) or even local outsiders. Acquisition FDI is thus supposed to have brought a clear contribution to strategic restructuring at the microeconomic level, in other words to have adjusted newly privatized firms with a foreign stake to the world norms of competition imposed by globalization.

As regards greenfield FDI, its impact on economic restructuring is more significant at macroeconomic and sectoral levels. First, it was the launch pad for developing the tertiary industry of marketized services which was absent in the sectoral legacy of former centrally planned economies. Services attract roughly 50% of inward FDI in the CEECs (Table 4) going along with the worldwide trend towards more tertiary than industrial FDI. Greenfield FDI has also created from scratch some absent manufacturing industries in Eastern Europe, like the car industry in Hungary and a Western-style food industry and fast-food services everywhere. As a result, the changing way of life and consumption in transition economies has been much appreciated by those citizens that are rich enough to enjoy it, but increasing income unequalities have triggered, in various countries, a social and political resentment against foreign investors and political decision makers that have favoured inward FDI (Sinn, Weichenrieder 1997). In particular, privatization through selling assets to foreign investors has often been felt as the sale of "family silver" and criticized, even though it is this kind of privatization which has provided the most substantial restructuring.

Criticisms have also been addressed to the insufficient transfer of technology, know how and tacit knowledge by MNCs, at least compared with the hopes of transition countries' leaders. Foreign investors are supposed to transfer updated technology and to upgrade somewhat outdated technologies still at work in Eastern European enterprises, but the transfers have not been yet enough to really modernize the great bulk of them. No one can deny that MNCs have proceeded to some technology transfers. But, in number of cases, they have been attracted by the prospects of "cherry picking" the best local enterprises in terms of technological levels (Radice 1993). MNCs' policy in relation to the transfer of product and process technologies has varied from liberal to extremely restrictive. In the first case, the affiliate (or subcontractor) located in a transition economy is allowed to freely use the mother company's technology. In the second one, the MNC attempts to minimize the actual technology transfer to the host country through restrictions on the use of technology by its foreign affiliate.

Moreover, the fact that we do not yet see so many spillovers being generated from FDI in transition countries (Radosevic 1998) is an issue with important policy implications. Most MNCs are big in the context of small transition economies and have sometimes abused of their monopolistic market power, namely in offering to highly trained personnel and scientists wage rates which are good by local standards, but peanuts by Western standards, and in using host countries for ecological dumping (Dyker 1998).

Both MNCs' research needs and their R&D capacities have competed with and indirectly accelerated the collapse of local science and technology institutions (Andreff 1998). For example, in Hungary, R&D expenditures by foreign firms were already accounting for 41% of overall research spendings in the business sector in 1993. Some MNCs have encouraged the brain drain of engineers, scientists and highly trained personnel from transition countries. All these issues are of social concern and political resentment, not to say that they can widen the technological gap between OECD countries and Eastern Europe in the long run, so that some local experts raise their voice to claim a stronger domestic industrial and technological policy (Farkas 1996).

Knowledge transfer by TNCs to Eastern Europe refers to information, patents, trademarks, know how, skills, but also social and organizational structures, tacit and specific knowledge on how use the market mechanism, management, marketing and financial know how. What is badly needed in former socialist enterprises, if one wants them to adjust to globalization, is to import from MNCs a Westernized management culture and practice based on accountancy, finance, project management, quality control and so on. The transfer of this soft management technology has been much more widespread than the transfer of 'hard' technology. Mainly focusing on the generalized introduction of Western office technology and the improvement of X-efficiency, MNCs' soft technology transfer has neither been much asset creating, nor technologically sector-specific, so that it has not changed either the existing pattern of resource endowment or comparative advantages of Eastern European countries on export markets (Dyker 1999).

We thus reach the issue of the relationship between inward FDI and the foreign trade of transition countries. There is obviously a strong link between subcontracting and outward processing trade (Naujoks, Schmidt, 1995, M. & W. Andreff 2001). On the other hand, the growth of CEEC exports coincides with a strong presence of FDI in some sectors, automotive industry being the best example (Lemoine, Freudenberg 1999). This raises once again the question: are trade and FDI complementary or substitute, in particular in the context of Eastern Europe? If FDI is market seeking we must expect FDI and exports to be substitutes. They must be complementary if efficiency seeking MNCs relocate their production or use outward processing trade. Some recent econometric exercises (Alessandrini, Bosco 1998) have not been able to demonstrate that globally complementarity is larger

than substituability in the CEECs. Complementarity is significant in some branches such as chemicals and electrical machinery. Substituability prevails in food, milk and derivatives, metals, rubber and plastic. Evidence is mixed in machine building, textiles and clothing. These results highlight the non-linearity of the relationship between trade and FDI which is usually assumed outside the context of Eastern Europe (Markusen, Venables 1995).

Most MNCs are, on average, more export-oriented than local firms (Paas, Varblane 1999). But there is no significant correlation between the share of foreign capital invested in each sector and its export performance (Hoekman, Djankov 1997). Such an evidence confirms that MNCs are attracted by domestic market in the CEECs and not merely by using these countries as a cheap labour export base. The share of export-oriented FDI is estimated to only one fifth of overall inward FDI in Hungary, in spite of industrial free zones that have been established to welcome it. Moreover, no crystal clear correlation between FDI and an excess in trade balance at a sectoral level has been discovered in any study so far. MNCs are major exporters from the CEECs, but they have also a strong import propensity which negatively affects trade deficit. A large share of imports generated in Eastern Europe by FDI consists in spare parts and components which circulate in the intra-company trade of MNCs, and this may explain a part of the increasing intra-industry trade in transitional economies. Intra-company trade offers opportunities for MNCs to use transfer pricing. Very few studies have been devoted to this issue in Eastern Europe. Three of them show that, in Hungary, companies with foreign participation increased export prices much slower than import prices, giving some grounds to the hypothesis that MNCs repatriate their profits via transfer pricing (Sass 1999).

5. Outward foreign direct investment from transition economies

The outward FDI stock achieved by former "red multinationals", as they were named earlier, has been studied in the 1980s (Hamilton 1986, McMillan 1987). These strange MNCs were controlling a rather tiny FDI stock, by world standards, but actually behaved as any other foreign investor, thus resembling the emerging Third World multinational corporations of this time. The financial austerity in the first years of transition has dried up the outflow of FDI from Eastern Europe. However, this flow never stopped definitely, even though it fell down to 100 million dollars from the CEECs, CIS and the Balkan countries in 1992 (Table 5), during the heat of the transition crisis. FDI outflow started to grow more significantly after 1995, in particular from Russia, then Hungary, Poland and Croatia which are the four major home countries of the outward FDI stock in 1998. The expansion of MNCs from transition economies seems to be a phenomenon similar to the growth of MNCs from newly

industrialized countries, which occurred more than twenty years ago. The problem is that there is very few information about foreign investors from transition countries. Russian firms like Gazprom, Lukoil, Sidanco, Yukos do own pipe networks and plants abroad, primarily located in the other CIS countries. FDI outflow from Hungary is usually attributed to big firms such as MOL, Richter Gedeon, Pharmavit, Zalakeramia (Csaki 1998).

A question is to be clarified through future research: how much of these FDI outflow from transition economies have been achieved by foreign affiliates of Western MNCs now located in the CEECs and CIS countries and how much is resulting from a new strategy of foreign investor adopted by East European enterprises - I mean with a majority or full ownership by Eastern European citizens and capital. Thus, a promising area for further research is the study of outward FDI from Russia and the CEECs, as well as the strategies of emerging MNCs from transition countries. The main determinants that must be confirmed by deeper analysis are: 1/ the small size of domestic markets in many Eastern European economies and the search for new markets; 2/ the corporate competitiveness advantage of Eastern European firms; 3/ the desire of investors to diversify assets as a safeguard against domestic instabilility (in the case of Russia in particular); 4/ the loss of comparative advantage based on low wages in industries such as textiles, footwear, and other labour intensive industries (UNCTAD 1998). Whatever the results of further research could be, outward FDI is a proof that transition economies are increasingly integrating themselves into the process of globalization, just like the emergence of MNCs from newly industrialized countries has been the sign of their growing integration into the world economy. Since globalization is an uneven development process, some transition economies nevetheless are exposed to a possible marginalization from the world economy.

6. Is there still a potential for future foreign direct investment in transition economies? What about Cuba?

The basic issue here is to know whether transition economies have indeed attracted as much inward FDI as one would expect, once their level of economic development is taken into account. Some exercises with the gravity model (Brenton, di Mauro 1998) have attempted to explain bilateral FDI flows by country characteristics such as economic size (GDP and population) and distance in view of assessing whether current flows are above or below potential flows. The results show that, up to 1995, FDI by Germany, France, the UK and the USA in the CEECs is already greater than the potential FDI flow predicted with the gravity model, except in Bulgaria and Romania where FDI is still low relative to the potential. The two latter countries would thus be the only CEECs with a clear

perspective of FDI increase in the coming years. Another argument geared towards the same pessimistic conclusion is that the great bulk of the privatization drive is over now, in particular in the most developed transition economies, and privatization will not trigger FDI any longer. But, in fact, the region's share in the world FDI stock is still rather low (1.5%), much lower than the region's share in world GDP (2.4%), world population (6.1%), or world imports (2.3%) - figures are for 1996. A catch up has been observed in 1996 and 1997 when the region's share in world FDI inflows peaked up at 4.0%, and the Russian crisis has not triggered this figure back in 1998. So that the region's share in world FDI in 1998 has reached 2.3%.

An UNCTAD study (UNCTAD 1998) has compared FDI in transition economies with a comparable group of countries at roughly similar levels of economic development. In 1996, the ratio of inward FDI stock over GDP was 26% in the reference group while it was only 6% in Eastern Europe on average; inward FDI stock per capita was 848 dollars in the reference group and 151 dollars in Eastern Europe; the ratio of FDI inflows over gross fixed capital formation was 15% in the reference group and 8% in Eastern Europe. Thus, there is still a potential for FDI flowing into the region. Only Hungary, the Czech Republic and maybe Estonia, might have exhausted the great bulk of their potential attractiveness to FDI. The same conclusion derives from Tables 1a and 1b: Hungary, the Czech Republic and Estonia have a higher inward FDI stock per capita than many countries with a comparable GNP per capita. The last say might well come from MNCs and the place they would like to give to Eastern Europe in their new strategies of global networking, global switching and global focusing.

A brief look at Cuba shows that inward FDI stock per capita is very low in the country in 1998, in spite of the Law 77 on foreign direct investment passed on in 1995 (replacing the less efficient decree-law 50 of 1982) that has opened the opportunity for creating majority-owned foreign affiliates in Cuba (Fogel 1996). Inward FDI stock per capita in Cuba compares to the level reached for this ratio by much less developed countries like Tajikistan, Madagascar, Burkina Faso or Sierra Leone. On the other hand, if we compare Cuba to countries with approximately the same level of economic development (in termes of GNP per capita), it appears that the potential for Cuba is between 1320$ (Tunisia) and 335$ (Thailand) or even 195$ (El Salvador) for inward FDI stock per capita. Instead, in 1998, it actually is of about 9.10$ per capita, corresponding to an inward stock of roughly 100 million dollars, divided into some 370 foreign affiliates and joint ventures (Adrian 2000), most of them concentrated in tourism, and the rest in nickel, tobacco and citrus fruits. Even if one accept the maximum evaluation of a 700 million dollar stock of inward FDI (64$ per capita), instead of the 100 million dollar estimation by UNCTAD, Cuba seems to be still far from its attractive potential. The potential inward FDI stock, according to the Cuban level of economic development is between 2150

million dollars (if one refers to El Salvador) and 14500 million dollars (if one refers to Tunisia). An amount of 4 billion dollars - *i.e.* 40 times the current UNCTAD figure, six times the highest estimation, or three times the amount of touristic receipts (1354 million dollars in 1997) - should be realistic if Cuba were to alleviate the strict TRIMs that it imposed on FDI as regards the transfer of know how, the finance and new markets which must be brought in by foreign investors, as well as the constraint of reexporting 70% of the local production that must be accepted by any foreign candidate to invest in Cuba [5]. Once some of these restrictive measures would be given up, Cuba should attract a strong FDI inflow from European MNCs that would be so happy to benefit of the US embargo definitely hindering any FDI by American MNCs.

7. Concluding policy implications

In a context of globalization, any potential (or actual) host country has a trade-off between a restrictive or an attractive policy towards MNCs and FDI. The biggest apparent benefit drawn from a restrictive policy is economic (and somewhat political) independence from abroad. On the other hand, the host country remains cut, to some extent, from the outcome of international technological progress, international producer norms and international living standards (and fashions of course). Such an isolation from the world technical and trade flows has often been assessed as a major cause for the collapse of centrally planned economy in Eastern Europe. Moreover, the least open countries to FDI in the world are recruited among sub-Saharian countries and the poorest Asian economies. The question is thus raised to know whether closing the door to FDI is more or less damageable for the host country economic development than an attractiveness policy. In other words, does the old theory of imperialism still hold (FDI and MNCs exploit the host developing countries)? Or should not we think - in a context of globalization - of a theoretical renewal in which MNCs' domination is not channelled through their FDI flows, but instead through their outrageous bargaining power with the nation-states and their capacity to sever capital flows to any "not enough friendly" country?

This is not to say that there is no other way out except the most attractive policy towards FDI. We witness today (Andreff 1999b) a tendency among host countries to overbidding with ever more attractive measures offered to MNCs. Such an overbidding is partly self-destroying and finally not much efficient in terms of actually attracting big FDI inflows in transition and developing countries.

[5] Not to speak of the declaration made by Mr. Octavio Castilla, deputy-Minister for Foreign Investment and Economic Co-operation, to the *Wall Street Journal*, on the 9th of August 1995, saying that any foreign investment which reveals opposed to the national interest will be nationalized. This does not create an investment-friendly climate, as many MNCs understand it.

On the other hand, a truly attractive policy has a cost of building infrastructures for MNCs, of alleviating foreign investor tax burden (then shortening the fiscal revenues in the host country), of controlling for friendly wage increases and so on. Therefore, a careful cost-benefit calculation is required in each host country to compare advantages and costs involved in a restrictive and in an attractive policy.

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