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Foreign Direct Investment and Economic Transition:

Assessing the Impacts on Hungarian Economy

Carl H. McMillan and Masumi Hakogi

1. Introduction

The transition from central planning to market economy in the former communist countries of Europe is now long enough underway that there is increasing talk of their entering a second phase. [1] One of the dimensions by which their bittersweet progress through the transition is measured and compared is foreign direct investment (FDI). Apart from any direct economic benefits it may yield, FDI indicates how the international business community assesses the transition economies and their prospects. Foreign investers are concerned with political and economic stability and openness, laws and regulations that are fairly and transparently enforced, equal access to inputs at reasonable prices. These conditions in the host countries are determined by policy choices in the course of the transition (World Bank 1996, p. 64).

When the transition began, there was widespread expectation that FDI would play a critical role in its success. At the time, one of us attempted to explore this proposition and to sketch out the role that FDI potentially might play (McMillan 1993). While the analysis confirmed that its potential impact could indeed be significant, although not uniformly positive, it concluded that the transition experience thus far suggested that FDI was unlikely to play the major role as envisaged.

Unfortunately, in the majority of cases to date, this early conclusion still holds. Flows of FDI to the transition economies have been of insufficient magnitudes to make much impact. There are, however, some notable exceptions to the general rule. The experience of these economies is therefore of special interest, with important implications for those who have failed (willingly or unwillingly) to attract significant amounts of FDI.

The greater part of the stock of FDI in the European economies in transition has gone to the three Central European destinations: Hungary, Poland and the Czech Republic. Although inflows to Poland have increased rapidly since 1995 (million US$1493, 2511, 4000, 5678, respectively in 1994, 1995, 1996 and 1997), Hungary has received, relative to its size, by far the most FDI of any of the European countries in transition (i.e. million US$1319, 4571, 2069, 2307, respectively in 1994, 1995, 1996, 1997). (Table 1).

Table 1 Estimated Inward Stock of FDI in CEECs in the end 1997

	US$ million (%)	Stock as % of GDP
Czech Republic	6763 (13.6)	13.0
Hungary	17529 (35.2)	39.3
Poland	15305 (30.7)	11.5
Slovakia	1410 (2.8)	7.2
Slovenia	2400 (4.8)	13.7
Bulgaria	1252 (2.5)	12.5
Romania	2800 (5.6)	8.1
CEEC-7	49859 (100.0)	

(Source) Gabor Hunya, "Integration of CEEC Manufacturing into European Corporate Structures via Direct Investment", WIIW Research Reports No.245, May 1998, p.6.

Why has Hungary been so exceptional in these terms? A full answer to that important question would require separate analysis. The causes appear to lie both in the legacy of the communist period and Hungary's post-communist experience. Hungary, from 1968, was in the forefront of attempts to reform the institutions of the "classical" Soviet-type economy. The post-1989 reforms have thus been an expansion and acceleration of a process long underway. This history has created a business environment in Hungary that surveys show investors to regard Hungary as more congenial than in other transition economies. A recent *Economist* article calls Hungary "the most western of East European economies" (16 May 1998, p.52).

Perhaps even more important, FDI is typically the culmination, not the commencement, of investor relations with the host economy. In the 1970's and 1980's, Hungary was the most open of the Comecon countries to external trade and other relations with the non-communist world, and one of the first to permit limited forms of foreign investment. When, after 1989, the door to FDI in Hungary was opened widely, there was a substantial basis of experience to build upon.

In the 1990's, Hungary has offered investors the prospect of greater political stability than its major competitors for FDI among the more reformist transition economies. Post-communist Poland experienced a succession of short-term governments and attendant political crises in its first four years. Czechoslovakia has split into the two independent countries in 1993. Moreover, in contrast to the others, Hungary chose a method of large-scale privatization (direct sale of state assets) which accorded a major role to foreign bidders (Hakogi and Bakos 1993). Meanwhile, Poland's privatization lagged; which offered little scope for direct foreign acquisition of assets and created a financial climate that

was complex, opaque and ultimately unstable.

In this paper, we examine the complex and often ambiguous linkages between FDI and the post-communist transition, in theory and in practice. Our purpose is to look broadly at the ways in which FDI may affect the processes of transition and to explore some of the evidence on its actual impact. We shall review works carried out to date, especially in the countries principally concerned, and shall try to bring out some of the pitfalls in any impact analysis. We hope that this overview may serve as a useful introduction to the subject and as a guide to further research.

Our focus will be mainly on the economy with the richest experience to date, notably the Hungarian and occasional reference will be made to the case of Poland. Hungary has not only received the relatively large amounts of FDI, but is commonly regarded to be in the forefront of progress in the post-communist transition.[2] The *Economist* (op. cit.) asserts that, in Hungary "the state's retreat and the advance of foreign investors have worked wonders" and adds that, "among the East European countries set to join the EU in the first intake, Hungary is now almost certainly the best qualified". If indeed FDI plays the strong, positive role in the transition that is generally supposed, that should be most apparent in Hungary. This is our underlying hypothesis.

Foreign direct investment in an economy in transition can bring to the host economy more than the capital, technology and know-how with which it is traditionally associated. Analysis of its impact therefore requires somewhat different approaches from those customarily employed in analyzing the effects of FDI on a host economy.

FDI can affect the processes of transition in a variety of ways. The presence of foreign-owned firms within the host economy may not only alter business thinking and practice, but also change the attitudes and values of those directly engaged and of the population at large. It may, for example, raise the value attached to individual initiative and increase respect for private property. The links between FDI and corruption in the host transition economy, and whether their net effect is positive or negative, is another subject that is important, but generally neglected by economists. And the four major tasks, the more economic aspects, of the post-communist transition; stabilization, marketization, privatization and economic restructuring, are closely linked with inflow of FDI through various channels.

Assessment of the impact of FDI thus faces the methodological problems common to all complex assessments. There are a variety of measures; some subject to quantification, many not. The data for measuring even the quantifiable variables are often inadequate. The effects of FDI on the host, transition economy can be negative as well as positive. Finally, there is the problem of weighing the net effects revealed by the different indicators, in order to come up with an overall assessment.

2. The Major Tasks; Stabilization, Marketization, Privatization, and Economic Reconstructuring

Stabilization

Stabilization has been the most urgent problem of the early transition years. The transition has been universally accompanied by a deep and prolonged fall in the level of economic activity. At the same time, the transition economies have had to combat serious inflationary pressures, in many cases threatening hyper-inflation. Any discussion of the effects of FDI on Hungary must take account of the severe stagflation that the Hungarian economy has experienced after 1989. Following four years (1990-93) of diminishing national output, Hungary's GDP grew at an annual average of somewhat over 2.0% in the successive four years. The level of output in 1997 was, however, still only 90.5% of the 1989 level (WIIW data base). The consumer price level continued to rise at relatively high rates—23.6% in 1996 and 18.3% in 1997 (WIIW data base).

Hungarian economists believe that the recession would have been much more severe without FDI. Foreign-owned firms have been found to invest more intensively than domestic firms, and their share in investment in manufacturing accounted for 79% of total in 1994 (Szanyi and Szemler 1997). Hungarian enterprises experienced severe shortages of working capital after the demise of the old system. A new commercial banking system was just being established. Injections of financial capital from foreign investors was crucial to their survival. Without that support, bankruptcies would have been much more frequent.[3]

At the same time, it is interesting to note that major inflows of FDI are not a necessary condition for recovery from transitional recession and subsequent economic growth. The Polish economy was the first Central European economy to move into the positive growth range (in 1993) and its growth has been faster than in neighboring economies in the mid-1990s. A recent exposition of the Polish model makes no reference to FDI (Gomulka 1998), while some researchers think that the impact of FDI on Polish economy is significant and easily noticeable (Nowakowski 1996).

The impact of FDI on the fiscal position of a host country is difficult to measure. The revenues received by the Hungarian government from the sale of assets to foreign investors have increased its macro-economic policy flexibility and have in this way helped its efforts to stabilize the economy.[4] On the other hand, tax concessions to foreign firms and expenditures to attract foreign investments have probably been more than offsetting.[5]

For Hungary, which entered the transition with the highest per capita foreign debt, stability of external capital inflow has also been a particular problem. Annual inflows of funds in the form of FDI (amounting to an average $2.2 bln in 1991-97) have financed Hungary's current account deficits (National Bank of Hungary 1998, p.15). FDI has thus been the main source of financing Hungary's

external debt. [6] Cumulative inflows of FDI (US$ 17,529 mln) amounted to almost three-quarters (73.8%) of Hungary's gross foreign debt by the end of 1997. Meanwhile, outflows in the form of repatriation of profits have remained relatively insignificant, although growing. [7]

The effects of FDI on Hungary's external accounts have also been felt indirectly through the impact of foreign owned firms on the balance of trade. Hungarian analysts have focused especially on this aspect, attempting to compare the foreign trade performance of foreign-owned and domestic firms producing tradeable goods. [8] They have employed tax data for foreign and national firms in different branches of the national economy to draw these comparisons. Such studies have shown foreign-owned firms to be more successful exporters than their Hungarian-owned counterparts and they are reported to account for a significant share (two-thirds) of Hungary's manufactured exports. Their net trade effects, however, are less clear. Hungarian studies have shown foreign-owned companies to have exceeded imports in 1995 and 1996 (HCSO 1998). Here, however, the results appear to be highly dependent on the treatment of high-value energy imports. The inclusion of the Hungarian national oil company MOL, in which there is a minority foreign stake, and which accounts for a large share of Hungary's imports, significantly affects the results and makes them contentious.

One of the urgent transition tasks facing the smaller countries who were members of the now defunct CMEA has been to reorient their foreign trade westward. This reorientation was forced not only by the demise of the regional cooperation but more particularly by the collapse of the Soviet economy in the 1990s. FDI has assisted this geographic restructuring of foreign trade, by making Hungarian firms more competitive internationally and by opening up to them foreign markets through equity ties to multinational companies already well established on such markets, especially in Western Europe. To take mechanical engineering industry in Central Eastern Europe as an example, the region's share of EU imports has tripled compared with 1989 (2.5%). The main driving force for this is the relative cheapness of the products. However, most mechanical engineering exports from the region are in the mid to low quality segments. The major foreign investors in mechanical engineering in the region include Asea Brown Boveri, Daewoo and Bosch-Siemens. As the countries of Central Europe become more integrated in the EU and their wage levels start to be equalized in stages to those of the EU, bringing about a gradual loss in their price-competitive edge, they should manage to position themselves more effectively in the EU market on the basis of higher-quality products. [9]

Marketization

Developing market mechanisms in the countries where they were totally absent or only partially functioning under the pre-transition economic system requires more than the dismantling of former

restrictions and controls. Liberalization, a priority in the first phase of the transition, is the less difficult part of marketization; what has proved harder and slower is the creation of the institutions upon which markets are based. Such institutions comprise not only formal economic organizations, but legal and social norms, ways of thinking, patterns of behavior. Institution-building has become a major task in the new phase of the transition to a market economy.

FDI can contribute on both the demand and on the supply side to the development of institutional infrastructure for effective market functioning. The presence of foreign firms in a transition economy create demands not only for liberalization (such as the relaxation of foreign exchange controls) but also for an equitable and transparent system of laws and regulations governing the new market relations in the economy. Foreign firms can in a variety of ways exert pressure for the adoption of policies to these ends. They can, for example, create associations which lobby for new laws or changes in existing laws. [10] The revision of laws in Hungary and other Central European countries in preparation of membership in the European Union (Palankai 1998) opens up new opportunities for such pressure.

A unique opportunity to pressure for modifications in the regulatory framework is presented when negotiating the terms of the investment with the host government. In Hungary, firms acquiring assets under the privatization program could negotiate with the responsible state agency (most recently the Hungarian Privatization and State Holding Company). Further investments open further such opportunities. The larger and better known the foreign company, and the more significant the proposed investment, the greater its potential influence. Case studies provide evidence of resulting changes in regulations ranging from environmental protection to accounting procedures (Connor 1993, Marer and Mabert 1996). It is an open secret that in the initial stage of Magyar Suzuki, because of its importance to Hungarian industrial policy, the firm had a great influence on the automotive import policy, especially for used passenger cars, of Hungary.

FDI can also generate demand for and supply of business and financial services, which had been little needed in a planned economy. Accounting services are one example. Large multinational accounting firms, such as Pricewater House, etc., hired to participate in the audits of major privatization projects, are now operating in Hungary and other transition economies. They provide a range of business services to foreign and national firms.

FDI has played a major part in the development of a commercial banking system in Hungary that is considered the most developed and stable in Central Europe. The banking sector has made a major leap forward from the monobank system that existed in Hungary until the late 1980s. The new multi-tier system is now largely privatized, and about half of total bank assets are foreign-owned. (This probably underestimates the degree of foreign control). Foreign capital has contributed to the

privatization, restructuring and modernization of Hungarian banking. Through the financial services the banking sector contributes to the economy as a whole, and this is undoubtedly one of the major ways in which FDI has contributed to the marketization of the Hungarian economy. Foreign presence in the Hungarian banking sector is likely to increase further, as from 1998 foreign financial firms are allowed under OECD rules to establish branches in Hungary.

Privatization

Although privatization is typically used to designate the transfer of state assets to private ownership, it can be used more generally to refer to the overall growth of the private sector in a transition economy. FDI in Hungary has played an important part in both aspects, in the privatization of state assets in the first years of transition and more recently in the growth of the *de novo* private sector.

As noted earlier, Hungary chose a method of privatizing state assets in large scale that enhanced the potential role of foreign capital. Foreign investors responded to the opportunity and sales to foreigners that dominated in the early years of Hungary's privatization program. As mentioned earlier, acquisitions by foreign investors accounted for the bulk of the sales by the State Property Agency (SPA) in the early years of the large-scale privatization program. Acquisition of some of Hungary's largest and best known firms such as Tungsram (lighting equipment), Chinoin (pharmaceuticals), Ganz-Mavag (transport equipment), Lehel (refrigerators), Matav (telecommunications), Budapest Bank (financial services) etc. by foreign investors has been through the direct sale of a controlling interest.

As the program of large-scale privatization has neared completion in Hungary (the Hungarian Privatization and State Holding Company is scheduled to shut down operations at the end of 1998), greenfield investments have grown in relative importance. One of the best known of these is the automotive assembly plant established by the Japanese Suzuki company through its subsidiary in Hungary (Magyar Suzuki). Another is Ford Hungary. Greenfield investment is now estimated to account for some two-thirds of the stock of FDI in Hungary. [11] In terms of numbers of foreign-owned companies, the proportion of newly formed companies is even higher.

Clearly FDI has played a fundamental role in the major shift that has occurred in the ownership structure of the Hungarian economy. In the transition years from 1990 to 1997, the private sector rose from 35-40% of assets to an estimated 75% (EBRD 1997).

Economic Restructuring

Economies in transition have faced a major need for restructuring, at the branch and enterprise

level, in order to develop efficient, internationally competitive production of goods and services. Closely related to this has been the task of modernization, the technological updating of production and management.

According to current economic thinking, private investors are superior to bureaucratic planners in detecting and exploiting potential areas of strength. Table 2 provides data on the distribution of FDI by industry in Hungary. Nearly half of foreign investment has been directed to the service sector, especially retail trade, transport and communications, financial and business services. These are areas which were neglected under the old regime, with its strong planners' preference for investment in material production. Within manufacturing, Hungarian official data show a concentration in food, beverages and tobacco and in machinery and equipment. In the latter, FDI has been concentrated in the automotive industry, a branch which has been virtually created in the transition period by the greenfield investment of major foreign firms (Audi, GM, Ford, Suzuki).

There is thus some macro-economic evidence that FDI has been important in the restructuring at the sectoral and branch levels that have occurred to date in the Hungarian transition. And Hungary

Table 2 Allocation of FDI in Hungary

Branch	Percent
Agriculture and mining	2.5
Manufacturing, of which:	37.4
Food and beverages, tobacco	8.3
Textles, tanning	1.7
Wood and paper; printing	2.2
Chemicals, incl. Petrochemicals	10.9
Non-metallic mineral products	2.3
Base metals and products	2.2
Machinery and equipment	9.5
Motor vehicles, parts and accessories	3.4
Other manufactures	0.4
Wholesale and retail trade; equipment repair	10.3
Hotels and restaurants	2.5
Transport, storage and communications	8.9
Financial intermediation	9.5
Real estate; business services	7.0

Education, health and social work	0.2
Other community, social and personal services	0.4
Total	100.0

Note: based on enterprises in which the foreign share of subscribed capital is more than 10%. Figures rounded, so they may not sum exactly.

(Source) HCSO 1997.

is regarded to be in the forefront of transition economies in this regard (EBRD). The impact of FDI on Hungary's economic structure is a subject of some dispute, however.

There is the criticism, for example, that foreign investment in Hungarian manufacturing, especially greenfield investment, has concentrated on production for export on the basis of imported components, with little Hungarian value added, though it has to meet with the local contents requirements. One analyst draws some sharp parallels between the development of manufacturing through FDI in Hungary and the maquiladora economy of northern Mexico (Ellingstad 1997).

There is also controversy over the role of FDI in restructuring at the enterprise level. A fascinating case study of GE's acquisition of one of Hungary's largest, oldest and best known firms, Tungsram, argues strongly that the strategic investment by GE has succeeded in turning around a company that faced bankruptcy and in bringing its operations to world competitive standards (Marer and Mabert 1996). [12] The study reports that one of Tungsram's plants is now the world's largest and reportedly best producer of lighting sources. By 1994, Tungsram had become Hungary's largest industrial exporter, and accounted for 90% of GE's sales in Europe. More general surveys of Central European firms have also found positive effects of FDI on the efficiency of their operations (Hunya 1997, Rojec 1997).

The impact of FDI on Hungary's technological capability is also a subject of controversy. There are considerable concerns that foreign investors have had little respect for Hungarian technology and have curtailed or abolished R&D operations in the Hungarian companies they have acquired (Farkas 1997). Greenfield investment has brought modern equipment and processes to Hungary but based on foreign technology.

The Tungsram case is in some ways the exception that proves the thrust of the argument. Tungsram possessed a historically strong R&D capability that was a source of national pride, although company spending on R&D had eroded rapidly in the 1980s owing to growing financial difficulties. After an initial period following the GE acquisition, in which there was a tendency to concentrate R&D operations outside of Hungary, GE Europe's R&D facilities have been located in Hungary and serves

GE's world-wide R&D needs in lighting, with approximately half of GE Lighting's professional R&D personnel in Budapest (Marer and Mabert 1995).

Another legacy of the communist past that has complicated the task of restructuring in the transition economies are extensive, inherited environmental damage and the related problems of health and safety in industry. Foreign investors acquiring existing plant have been faced with major problems in these areas. Environmental costs were therefore a common subject of negotiation between the foreign company and the Hungarian state. In the GE-Tungsram case, for example, Marer and Marbert report that the state originally assumed all legal liabilities for inherited environmental damage, but later in negotiating purchase of the remaining state holdings in Tungsram, GE agreed to forego all demands to obtain reimbursement for the costs of clean up. During 1990-94, GE-Tungsram spent tens of millions of dollars on environmental improvements and on measures to improve the health of workers (Marer and Marbert, p. 164). This is not the only case where Hungary has been able to obtain foreign investor participation in environmental clean up (Connor 1993).

The host country must also be concerned about the maintenance of desired environmental, health and safety standards in new production facilities. Ellingstad (1997) notes the disregard of maquiladora factories in Mexico for environmental standards, which has resulted in cross-border pollution problems. But if a host transition economy raises the environmental costs associated with FDI (acquisitions or greenfield investment) too high, it may discourage potential investors. Ultimately, the outcome will depend upon the state's willingness and ability to impose standards on these aspects of production. The priority accorded in Hungary and other transition economies in Central Europe to membership in the European Union will help to raise and maintain such standards and to ensure that they are applied equally to foreign-owned and national firms.

As is well known, the EU adopted Community environmental law in 1997, and is further preparing various directives on water policy, waste management, strategy to combat acidification, to limit the sulphur content of certain fuels, release of genetically modified organisms (GMOs), and has submitted communications on the environment and employment and on environmental taxes and charges. Thus the EU is steadily making progress in the field of environmental protection. Central and Eastern European economies in transition which wish to become the members of the EU, sooner or later, need to conform themselves with the *acquis communautaire*.

3. Conclusion

We have sought in this paper to explore the links between foreign direct investment and the post-communist economic transition in Europe, drawing especially on the rich experience of Hungary in

both respects. We have tried to cast a broad net, observing the impact of FDI on the four major processes that have comprised the transition in the 1990s. Under each of these, we have sketched out the desired (potential) role of FDI in the transition before examining its actual role, as exemplified by the Hungarian case. Our review in no way, however, constitutes a full blown assessment of the impact of FDI on Hungary or any other transition economy. Systematic, comparative assessment of that impact remains a long-term research goal, awaiting the availability of sufficient body of analysis generated on a country-by-country bases. [13]

We have seen that the form of FDI in Hungary has evolved over time. This evolution is not uncharacteristic of transition economies generally. In a first phase, in which the legacies of the pre-transition system remain strong, joint ventures between foreign and national companies are the principal form. In a second phase, as state assets are sold under privatization programs, acquisitions predominate. Finally, as the more attractive opportunities under privatization are exploited, greenfield investment are increasingly the chief form of FDI.

We have found evidence that FDI, especially in the last two phases, has indeed contributed in important ways to stabilization, marketization, privatization and economic restructuring in Hungary. It has no doubt been a major factor in Hungary's comparatively successful progress along the transition path.

We have seen, however, that contrary to the impression often given, the impact of FDI has not been unequivocally positive. It has contributed to economic recovery in Hungary and has financed the external debt, but its overall impact on the government's budget is probably negative. While it has boosted Hungarian exports and assisted the reorientation of Hungarian foreign trade following the collapse of the trade patterns that had emerged under Comecon, it has also raised imports, so that its net effect on the balance of trade (and its impact on the value-added content of exports) are less clear. It has contributed to the growth of an institutional infrastructure necessary for a market economy and directly to the development of some markets, but its impact on others has been more ambiguous. It is also not clear whether its net effect has been to generate competition on newly established markets or to reinforce non-competitive business concentrations. It has made possible a relatively rapid shift of ownership from the state to strategic investors, but at the price of incurring future balance of payments liabilities and of placing major areas of the economy under foreign control. The injection of foreign capital and know-how has helped many Hungarian to survive the recession associated with the transition, and foreign ownewrship has helped to turn around large, ailing firms. It is less clear, however, that foreign firms operating in Hungary are generally more efficient than national firms. Whether overall FDI has had a positive or negative impact on Hungary's R&D capability is also a sub-

ject of dispute, despite some success stories. FDI has been concentrated in Budapest and areas West of the Danube, widening regional disparities. [14]

Further analysis will help to resolve some of these issues. The most fundamental question is whether Hungary has unwisely opened the door to FDI too widely, as some believe. [15] **Hungary has chosen a transition starategy which links it especially closely to the West. For the foreseeable future the European Union and foreign capital seem positioned to determine much of Hungary's economic agenda. It is scarcely surprising, therefore, that popular and political attitudes towards FDI should be mixed.**

Is Hungary merely an exceptional case, or is it a path-breaker and an indicator of the future of other economies in transition? Only time can tell, but Hungary no longer dominates the statistics on inflows of FDI to the area as it once did. The surge of FDI in Poland since 1995 has already resulted in its surpassing Hungary in the absolute magnitude of FDI received since 1980. [16] **In relative terms, the impact of FDI remains far less powerful on the much larger Polish economy, but it is rapidly growing. The stock of FDI is also growing in significance in Slovenia and in the Czech Republic. Other transition economies seem poised to follow. These trends, taken together with Hungary's experience, suggest that FDI will play a larger part generally in the second phase of the transition, as more stable economic and political conditions provide an increasingly attractive climate to foreign investors.**

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Endnotes

1. The tasks that dominated the initial phase (liberalization of markets, privatization of assets and the restoration of a degree of macroeconomic stability) are regarded as having been largely achieved (EBRD 1997).
2. In its most recent annual assessment, the EBRD gives Hungary highest scores in all of its nine checks of

progress through the transition (EBRD 1997).

3. This point was stressed by several Hungarian experts interviewed in October 1997.

4. In the first years of the state privatization program, sales to foreign investors accounted for between 59 (in 1992) and 90 (in 1990) percent of total sales (Hakogi and Bakos 1993).

5. For a discussion of the budgetary effects, see Szanyi (1997).

6. On this point see, for example, Szanyi (1997, p. 12) and UNECE (1998, p. 157).

7. These calculations are based on figures taken from the monthly and annual reports of the Hungarian National Bank.

8. Particularly active in studying the comparative performance of foreign-owned firms in Hungary have been researchers at the Institute of World Economy (Hungarian Academy of Sciences), Kopint-Datorg (Budapest) and the Vienna Institute for Comparative Economic Studies (WIIW).

9. Verena Ebner, "Mechanical Engineering in Central Eastern Europe", Bank Austria East-West Reports 3/98, p. 27.

10. One of the authors was present at a meeting of government officials and foreign businessmen in Budapest, in the Fall of 1997, at which a new corporation law (to replace the 1989 law) was discussed. This provided a forum for direct feedback of opinion from the foreign business community to those responsible for drafting the new law.

11. The estimates are derived by subtracting from the value of cumulative inflows of FDI the value of foreign acquisitions under the program of privatization of state assets.

12. The authors note that the Tungsram investment is the largest US manufacturing investment in Central and Eastern Europe to date and that GE is the world's biggest multinational corporation. They separately visited this company and interviewed workers and executives.

13. We understand that a group of researchers in the countries concerned, under the leadership of Gabor Hunya at the WIIW, is actively working towards that goal.

14. As of 1996, over 82 percent of FDI was located in the central and western regions (HCSO 1997).

15. Among countries in the forefront of the transition, Slovenia has chosen a more cautious approach (see *Economist*, 6 June 1998, p.51, and Rojec 1997).

16. According to the Polish Agency for Foreign Investment (PAIZ), the total stock of FDI exceeded US$20 billion by end-1997.

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