DIRECT INVESTMENTS FROM HUNGARY TO SOUTH EASTERN EUROPE: MOTIVATIONS, EFFECTS AND BARRIERS

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Abstract

Recent trends related to foreign direct investments (FDI) indicate that Hungary has reached a level of economic development where less dynamic inflows of FDI are coupled with the growing importance of outward FDI. Low growth potential of the domestic market and increasing regional competition 'push' more and more companies located in Hungary to invest abroad. Due to geographical and cultural proximity, most of them prefer to establish a subsidiary in the neighbouring South and Eastern European (SEE) region, which offers favourable 'pull' conditions. The objective of the paper is to highlight the main motivations and effects of direct investments by Hungarian companies as well as the barriers to their further expansion in the Balkan countries. Results of a questionnaire survey and interviews with managers of the most well-known investors verify the hypothesis that growth of OFDI to SEE strengthens Hungary's international competitiveness. Direct investments of Hungary-based 'regional multinationals' in SEE are mainly motivated by searching for new markets, negative impacts on domestic investments and employment are not evident. Experience in post-socialist economic transition and cultural factors create important competitive advantages for them against Western European companies having more capital and being politically more acceptable in SEE.

Keywords: outward FDI, investment development path, Balkans, Hungary

1. Introduction

The promotion of internationalisation of domestic enterprises has become one of the key priorities of Hungarian government's new foreign economic policy. It has been declared that, besides further integration with the Western European economies, regional expansion of Hungarian companies through direct investments can also enhance the country's international competitiveness.[1]

Recent years, the underdeveloped but dynamically developing South Eastern European (SEE) countries play more and more important role in foreign direct investments of Hungary-based companies.[2] The main objective of this paper is to highlight the motivation factors of these Balkan investments and their potential effects on Hungary's economic development. The main political and economic barriers to further SEE expansion of Hungarian firms are also discussed.

The research has been devoted to examine the following hypothesis. First, comparing to Balkan countries, Hungary has already reached a higher stage of investment development path, where the outward direct investments have more important role in international economic integration. Second, the simultaneity of slowing economic development in Hungary and dynamic economic growth coupled with the improvement of business environment in SEE countries accounts mainly for the 'boom' of Balkan investments recently made by Hungary-based companies. Third, these investments have overall positive macroeconomic effects. Searching for new markets is the main driving force of regional expansion, which

[1] See the strategic documents of Ministry of Foreign Affairs for the Republic of Hunga-ry (2008) and Ministry of Economy and Transport for the Republic of Hungary (2007)

[2] The SEE region is defined in the paper as the countries of Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia FYR, Montenegro, Romania and Serbia (still including the newly-independent Kosovo)

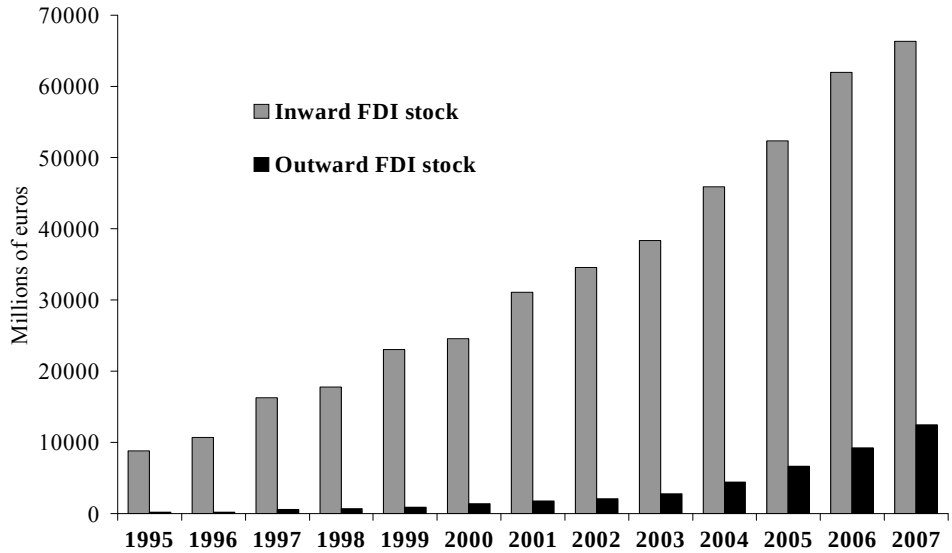
contributes significantly to improve the competitiveness of Hungary-based investors. The effects on domestic investment and employment are neutral. Fourth, most of the SEE countries now face the same problems related to economic transformation as Hungary did 8-10 years ago. So, the 'transition experience' of Hungarian managers ensures important competitive advantages for their companies in the SEE markets. Fifth, cultural factors can also counterbalance the disadvantages of Hungarian firms against their wealthier and politically more acceptable Western European competitors.

The remainder of paper is organized as follows. Section 2 analyses how Hungary's international investment position has changed in last couple of years. Section 3 describes the main trends in outward FDI from Hungary to the Balkan countries. Section 4 summarizes of the results of a questionnaire survey carried out among the 'TOP companies' of Hungary and the main conclusions drawn from interviews made with managers of firms known as the most important Hungarian investors in SEE. Section 5 concludes.

2. The Investment Development Path of Hungary

In Hungary, like in other more developed countries of Central and Eastern Europe, inward foreign direct investment (IFDI) became the most important vehicle of reintegration into the world economy in the second half of 1990s (Kalotay, 2005), and contributed significantly to the economic restructuring. In 2000, owing to its relative competitiveness and 'foreign investor-friendly' privatisation policy followed, the IFDI stock per capita of Hungary was the highest among the post-socialist countries joined the EU in 2004 (EU8). In the last decade, outward foreign direct investment (OFDI) of the country was negligible. Nevertheless, the annual growth rate of IFDI has been declined, while OFDI has gained more importance after 2000. As a result, the ratio of OFDI to IFDI has been more than tripled, increased from 5.6 to 18.8 per cent between 2000 and 2007 (see Figure 1).

Figure 1
Development of inward and outward FDI of Hungary, 1995-2007 (end-of-year data, in millions of euros)



Note: stocks of equity capital and reinvested earnings
(reinvested earnings for 2007 are estimated)
Source: National Bank of Hungary

This trend is accordance with the Investment Development Path (IDP) theory developed by Dunning (1981). As the cases of rapidly developing countries like Ireland and Spain show (see Barry, 2006; Galan, Gonzalez-Benito and Zuniga-Vincente, 2007), after a certain level of economic development, OFDI catches-up with IFDI and then exceeds it. Now it seems that Hungary reached the third stage of IDP, where the OFDI is growing faster than IFDI. Recent years, inflows of FDI have been increasing more dynamically in some other EU8 countries (mainly in the Baltics and the Slovak Republic) than in Hungary, indicating also the deterioration of international competitiveness in some areas, but Hungary still had the second highest IFDI stock per capita (after Estonia) in the region at the end of 2006. In parallel, the country has retained its regional leader position in absolute terms, while holds the third place (after Estonia and the Czech Republic) in terms of per capita OFDI.[3]

Antalóczy and Éltető (2002) points out that internalisation of state-owned Hungarian companies through OFDI existed even in the era of communism, although then it was concentrated on specific branches (e.g. medical equipment, pharmaceuticals, electrical equipment) and was to support sales mostly in Western European countries. In the 1990s, an increasing number of domestic enterprises (that survived the 'transformational recession') established foreign subsidiaries to make their exports easier and/or avoid taxes. This 'premature' OFDI was also promoted by the change in legal system[4] and its main destinations were the Netherlands (with the share of 40.1 per cent in OFDI stock at the end of 1999)[5], Austria (12.4 per cent), Romania (8.0 per cent) and the United States (5.3 per cent). However, the structure of the Hungarian OFDI has been modified fundamentally after 2000. One of the most observable changes is the increasing share of Hungary's neighbouring, among them the South Eastern European countries.

3. Trends and implications of OFDI from Hungary to the Balkan countries

At the end of the 1990s, stock of OFDI from Hungary to the eight SEE countries did not reach the amount of 100 million euros, representing only 9.7 per cent of the country's total OFDI. Between 1999 and 2006, however, this amount increased by more than 2.5 billion euros and the share of the Balkan countries has gone up to 29.8 per cent.[6] Table 1 also reveals that, considering the capital invested, Croatia is the most popular destination country in SEE, while stocks of OFDI related to Bulgaria, Romania, Serbia (and Montenegro)[7] and Macedonia are almost equal. Investments related to Albania and Bosnia-Herzegovina are not significant (or not registered yet).

[3] Source of IFDI and OFDI data of EU8 countries is the database ('Country Fact Sheets') published by UNCTAD on http://www.worldinvestmentreport.com/
[4] Hungarian residents did not need permit to invest abroad from 1996
[5] Most of these Dutch investments was related to the Netherlands Antilles functioning as tax haven (Antalóczy and Éltető, 2002)
[6] According to the data of National Bank of Hungary, total OFDI stock of Hungary was amounted to 8855.5 million euros at the end of 2006.
[7] Data are not available for Montenegro separately.

Table 1
Stocks of direct investments from Hungary to SEE countries, 1998-2006
(end-of-year data, in millions of euros)

	1998	*1999*	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*	*2006*
Albania	0.0	0.0	0.1	0.1	0.0	0.1	0.0	0.0	0.0
Bosnia-Herzegovina	..	..	..	..	..	..	..	..	..
Bulgaria	0.0	1.5	4.1	0.8	11.4	136.4	218.2	306.6	431.0
Croatia	7.7	12.2	17.6	23.5	51.7	323.4	359.9	522.4	969.7
Macedonia FYR	0.0	0.0	0.0	319.9	281.2	255.6	355.4	397.5	404.6
Romania	61.2	64.6	65.7	95.4	151.6	165.9	202.5	312.9	429.5
Serbia and Montenegro	0.0	0.0	0.0	0.4	0.3	5.0	14.9	146.6	405.0
Total	*68.9*	*78.3*	*87.5*	*440.1*	*496.2*	*886.4*	*1150.9*	*1686.0*	*2639.8*

Note: stocks of equity capital and reinvested earnings
Source: National Bank of Hungary

Table 2 shows that we cannot say about permanent trends, annual flows of OFDI to Balkan countries are highly volatile and dependent on individual investment projects. Comparing data for 2001 and 2006, a significant increase (from 1.4 to 18.9 per cent) in share of reinvested earnings in total investments can be observed. It is also obvious that the profit generating ability of Balkan subsidiaries owned by Hungarian companies is still relatively low. The total income realized on investments was only 303 million euros between 2001 and 2006, 20 per cent of which was repatriated in the form of dividends. The low repatriation rate indicates that the SEE expansion of Hungary-based firms requires additional capital to invest.

Table 2
Flows of direct investments from Hungary to SEE countries (by type of transactions)
and income on investments, 2001-2006 (in millions of euros)

	Flows of OFDI				Income on OFDI		
	Equity capital (net)	Reinvested earnings	Other capital (net assets)	Total	Divi-dends	Reinvested earnings	Total
2001	332.3	4.9	5.0	342.2	0.2	4.9	5.1
2002	35.2	-4.0	5.3	36.6	0.4	-4.0	-3.6
2003	790.7	25.4	15.9	832.0	4.1	25.4	29.5
2004	147.5	78.7	3.1	229.3	19.0	78.1	97.1
2005	551.4	5.8	20.4	577.6	20.6	5.8	26.4
2006	505.6	132.8	64.0	702.4	16.1	132.8	148.9
2001-2006	2362.7	243.6	113.7	2720.0	60.4	243.0	303.4

Source: National Bank of Hungary, author's calculations

However, data presented presumably do not give a real picture of OFDI made by Hungarian companies. The time series published by the National Bank of Hungary are based on questionnaire surveys and give information only on transactions that reach a certain amount of money.[8] Moreover, there are some firms known that operates in Hungary but their official headquarters are in one of the tax havens (e.g. Cyprus), so their investments are not registered as originated from Hungary.

Using company data available, one can conclude that the concentration of OFDI from Hungary to SEE is very high. As can be seen from Table 3, investments in Bosnia-Herzegovina, Macedonia and Montenegro are linked to only one or two Hungary-based investors. Although this number is higher in the case of Bulgaria, Croatia and Serbia, but the share of the largest companies reaches 60-90 per cent and the 'TOP5' investors have almost 100 per cent of all stocks. It can be also observed that the investments related to Romania are the least concentrated.

Table 3
Concentration of OFDI from Hungary to SEE countries, 31 December 2006

	Number of direct investor companies	Share of the largest investor company in total investment (%)	Share of the TOP5 investor companies in total investment (%)
Albania	0	-	-
Bosnia-Herzegovina	1	100	100
Bulgaria	13	87	96
Croatia	21	81	95
Macedonia FYR	2	99	100
Montenegro	2	91	100
Romania	76	32	77
Serbia	14	61	93

Source: National Bank of Hungary

Table 4
Share of Hungary in SEE countries' inward FDI stocks, 2000-2006 (end-of-year data, percentages)

	2000	*2001*	*2002*	*2003*	*2004*	*2005*	*2006*
Albania	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bosnia-Herzegovina	..	..	..	0.0	0.0	0.1	0.1
Bulgaria	0.2	0.3	0.5	3.5	3.0	2.7	3.2
Croatia	0.4	0.4	0.5	5.9	5.8	8.0	6.7
Macedonia FYR	0.4	28.9	25.9	24.3	22.0	19.8	16.7
Montenegro	..	..	..	0.0	1.4	26.3	22.1
Romania	..	..	..	1.4	1.8	1.9	1.9
Serbia	0.0	0.6	0.4	0.4	1.0	1.3	3.7

Source: central banks, author's calculations

[8] 10 million HUF (cca. 40 thousand EUR)

Considering the share of Hungary in their inward FDI, the SEE countries can be grouped in four categories (see Table 4).

1. In Macedonia and Montenegro, due to acquisitions of only one company, Hungary is the largest investor country (at the end of 2006). In Macedonia, however, the share of Hungary shows a declining trend since 2001.
2. In the case of Bulgaria and Croatia, Hungary's weight in countries' inward FDI exceeds its proportion in their imports of commodities (1.7 and 3.8 per cent in 2006, respectively)
3. Strength of economic relation through trade (measured as share in countries' commodity imports) is higher than through direct investments with the other countries. Nevertheless, Hungary's significance is increasing in capital import of Romania and Serbia.
4. Direct investments originated from Hungary are not significant (Hungary's share is below 1 per cent) in Bosnia-Herzegovina Albania.

What are the main reasons behind the growing willingness of Hungary-based companies to invest in SEE countries? Firstly, it should be considered that there are two main groups of the most important direct investors. One of them consists of firms, which are typically not Hungarian-owned (most of them are listed on the stock exchange) but governed by domestic management. These enterprises strengthened their (usually market-leading) position in Hungary in the 1990s, but then they faced the challenge caused by the low growth potential of the Hungarian market. In order to keep their competitiveness, they were forced to expand beyond the border. Foreign expansion has become vital to survive especially for companies, which operate in sectors (e.g. banking, oil and gas industry, pharmaceuticals) where a significant wave of consolidation can be seen in recent years. The other group of companies having subsidiaries in the Balkan are firms owned by foreign strategic investors. This implies that a part of OFDI from Hungary to SEE is 'indirect', i.e. some multinationals use their Hungarian affiliates, leaning on its managers' local knowledge and relationships, to invest in the Balkan countries. Furthermore, there are also several foreign-owned firms located in Hungary that, without having ownership, manage and control the SEE subsidiaries of their parent companies. The phenomenon of 'indirect' OFDI and/or management of SEE companies through Hungary-based affiliates of global firms indicates that Hungary has closer business and cultural ties with the Balkans than the more developed Western countries have.

Higher intensity of 'push' factors, on the other hand, has been coupled with more favourable conditions offered in SEE. Balkan countries achieved political and economic stability by the end of the last decade, and a dynamic economic growth has been taking place. The increasing purchasing power as well as the significant improvement of business environment in SEE have given strong impetus to the investments of not only the 'flagships' of the Hungarian economy but also of small and medium enterprises seeking new markets and/or searching for locations with lower costs. Most of the Balkan investments by Hungarian SMEs in, however, are not 'visible' in official statistics. For instance, in the case of Romania (the most popular investment destination of Hungarian companies in SEE) the National Bank of Hungary has data only on 76 companies (see Table 3), while at the end of 2006, there were already 6535 firms registered in Romania with capital from Hungary.[9] Considering the possible motives of SMEs to establish firms in SEE, it can be assumed that, besides market-seeking, opportunity for tax savings is also an important factor.[10]

[9] See http://www.onrc.ro/statistici/is_december_2006.pdf

[10] Recently, as an element of stabilisation policy aimed at reducing high fiscal policy, tax burden of Hungarian enterprises has increased. Meanwhile, flat-rate tax systems and reductions of taxes were introduced in most of the SEE countries.

4. Results of a company survey

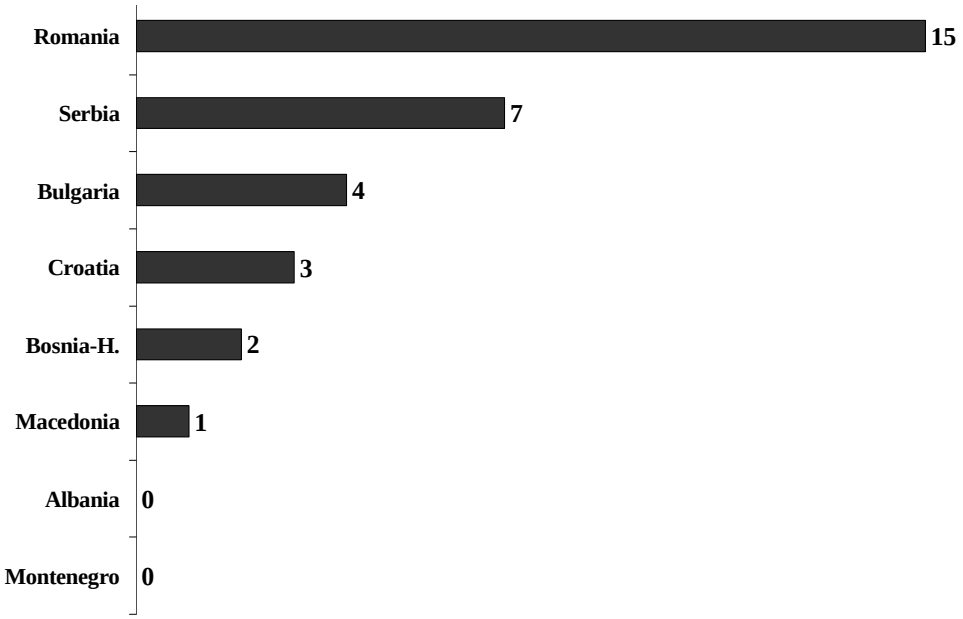
In order to examine empirically the motivation factors of Hungary-based firms' expansion in SEE, as well as the impacts of direct investments on their performance, the Public Foundation for European Comparative Minority Research (PFECMR) carried out a questionnaire survey among the largest Hungarian companies at the end of 2007.

The selection was based on the 'top 500' list of Hungarian companies (ranked by sales in 2005) published by the leading Hungarian weekly (HVG, 2007). The questionnaires were sent by post and/or e-mail, addressed to the managers responsible for strategy of the firms. The responding rate was 11 per cent, so our sample consists of 55 companies. Comparing the sales data published in HVG (2007) with statistics provided by the tax authority (APEH), the responding companies account for 10 per cent of total sales revenues and 21 per cent of total export revenues of all Hungarian non-financial enterprises in 2005. Consequently, in spite of the relatively small sample size, one can draw reliable conclusions on the main characteristics of OFDI from Hungary to SEE countries.

40 per cent of answering companies declared that they had foreign subsidiaries. A majority of them are 'traditional firms', i.e. they have predecessors established before 1990. Among companies having foreign investment, firms fully owned by domestic investors are over-represented (with 40 per cent share), one third of them are foreign controlled, while proportion of 'multinationals controlled by domestic management' (27 per cent) is also higher than their share in the sample.

Some one-third of companies in the sample (17 firms) said that they had subsidiaries in South East Europe. Romania is the most popular investment destination. Romania was the first or the only one country of international expansion for half of the responding companies investing abroad. Furthermore, almost half of the SEE firms owned by the responding companies are located in Romania (see Figure 2).

Figure 2
Distribution of SEE firms owned by Hungarian companies surveyed, by countries

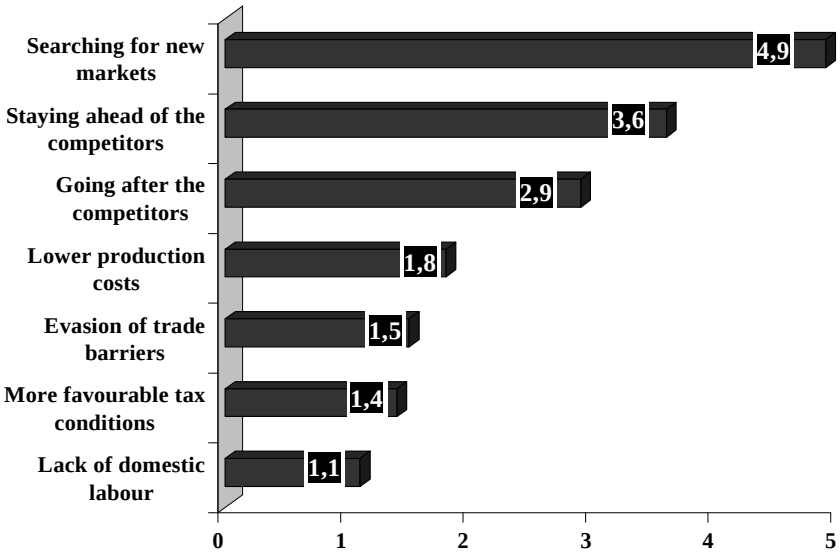


Notes: 17 of 55 responding companies had subsidiaries in SEE at the end of 2007; the figure shows the distribution of 32 firms owned by them, by host countries.
Source: PFECMR-survey

Considering the timing of establishment of firms, Romania is clearly separated from the other SEE countries. Two-thirds of Romanian investments were carried out already in the second half of the 1990s, while Serbian, Bulgarian and Croatian firms (with few exceptions) were typically established after 2000.

The representative results for the main factors driving OFDI show that market expansion is the primary motive behind SEE expansion of Hungarian companies. All companies in the sample, with the exception of two firms engaged in machinery production, stated that 'searching for new markets' had been the most relevant factor influencing their investment decisions. As Figure 3 shows, 'staying ahead of rivals' was the second most significant motive, which indicates that most of the companies followed a 'proactive' strategy. Nevertheless, the weight of 'going after the competitors' was also above the average. Surprisingly, the lower costs and taxes did not significantly motivate the companies surveyed. The responses categorized by industries, however, show remarkable differences. Savings available through lower production costs was highly important for firms belonging to the machinery sector. The 'evasion trade barriers' (still existing at the time of establishment of subsidiaries) was a significant factor for Hungarian companies of the food as well as the chemical industries. The 'more favourable tax conditions' were attractive especially for enterprises representing construction services.

Figure 3
Significance of factors affecting the decisions of Hungarian companies to invest in SEE



Notes:

- Companies answered the question 'What has motivated You to establish firm(s) in South Eastern Europe' and evaluated the possible factors affecting their decisions on a scale where 1 means 'it was not important at all' and 5 means 'it was the most important'
- In order to make the results representative, answers were weighted according to the industrial breakdown of Hungary's total OFDI

Source: PFECMR-survey

The survey examined the effects of Balkan investments on domestic activity of firms as well. The results (see Table 5) obviously show that exports to SEE countries of investor companies have increased, while the volume of imports from there has been not changed. The latter indicates that most of the SEE manufacturing subsidiaries do not sell to its Hungarian parent companies but to the local and/or other export markets. The impacts on domestic employment and investments, which are usually assumed to be negative, proved to be neutral. Even, some 20 per cent of the companies said that employment and investments in Hungary had also increased in parallel with their expansions in SEE.

Table 5
Effects of SEE direct investments on domestic activity of Hungarian companies

	Positive	Negative	Neutral
Exports to SEE	94	0	6
Imports to SEE	3	2	95
Employment in Hungary	19	1	80
Investments in Hungary	19	1	80

Notes: in order to make the results representative, answers were weighted according to the industrial breakdown of Hungary's total OFDI
Source: PFECMR-survey

Considering the barriers to Balkan investments of the other part of companies surveyed, mainly the ownership structure of firms explains the lack of the Balkan (and generally the foreign) subsidiaries. More precisely, Hungarian managements of the majority of foreign-controlled enterprises usually do not have decision-making authority to invest abroad. Most of companies whose activities are related only to the domestic market can also be classified into this category. Some one-fifth of respondents, however, emphasized that the risks of Balkan investments were too high. Companies that prefer other investment destinations than the Balkan countries have the same share. The shortage of capital and market information does not explain significantly the lack of investments in SEE.[11]

In order to refine the conclusions of the questionnaire survey, qualitative interviews were made with managers responsible for international expansion strategy of companies known as the most important Hungary-based investors in SEE.[12] These 9 companies now present in the Balkan countries with 25 subsidiaries and they share in common that they are typically market leaders in their sectors in the Hungarian market.

The main driving force of foreign investments of the firms interviewed was the intention to increase their markets. They realized at the end of the 1990s that the potential development of the home market was too low to exploit their capacities and abilities. Growth through internalisation was especially vital for companies listed on the stock exchange (four firms asked), however, in order to maximize the shareholders' value added, relatively short-run returns on investments were also important for them. Nevertheless, one of the manufacturers

[11] Survey results of barriers to SEE investments of Hungarian companies are not representative
[12] Managers of the following companies were interviewed (in the period of October 2007 to February 2008): Dunapack Paper and Packaging Ltd., Hungarian Foreign Trade Bank (MKB) Ltd., Hungarian Telekom Plc., MAL Hungarian Aluminium Ltd., MOL Hungarian Oil and Gas Plc., National Savings and Commercial Bank (OTP) Plc., Gedeon Richter Pharmaceuticals Plc., Trigranit Development Ltd., Videoton Holding Ltd.

was mainly 'pushed' by increasing labour costs in Hungary to invest in SEE (in Bulgaria). Exhaustion and lower quality of natural resources needed for its production in Hungary forced another manufacturing company to maintain its competitiveness through foreign acquisition. For most of the vertically integrated companies, it was also an important motive that they could get closer geographically to their regional markets (served through exports earlier) and could optimise their transportation routes. It is interesting that most of the investor companies engaged in manufacturing had traditional commercial relations with the firms acquired. Companies of the tertiary sector (telecommunication, commercial banking, real estate development) was motivated mainly by the expectation that, in parallel with the increase in purchasing power, demand for their services would be considerably higher.

Within the SEE region, choices of investment locations were determined mainly by the market size (measured by population), development of transportation infrastructure as well as political and cultural factors. The (potential) market size explains why the majority of interviewed firms started their regional expansion in Romania.[13] Furthermore, especially in the last decade, investors perceived political risks to be higher in the Western Balkan countries than in Romania.

Acquisition is the most frequently used method among investment projects examined, but the share of greenfield investments (40 per cent) is also significant. About half of the takeovers were privatisation deals, meaning that the growing privatisation opportunities in the Balkan countries also explain for the firms' expansion. By contrast, only a few Hungarian companies could buy significant state assets. They experienced only in the case of Romania that, as investors coming from Hungary, they did not have real chance to win the privatisation tenders. Political elites usually preferred Western investors in privatisation of 'national jewels' in the other countries too, but there Hungarian companies could compensate their political disadvantage with higher bid prices.

Political obstacles, however, were important in the 1990s, nowadays none of the managers interviewed feel that they are negatively discriminated as 'Hungarian' companies. The importance of political factors is higher in those countries (regions) where Hungary-based companies are among the largest foreign investors, so they are in the focus of local media's attention. Slow bureaucracy is a more serious problem for the firms, they experience that it is more time-consuming to obtain the licences required for their business than now in Hungary. Most of the managers, however, think that this is 'natural', they faced similar problems in Hungary in the 1990s.

The companies try to 'export' their business models proved to be successful in the Hungarian market, but they have to adapt them to the local economic, political and cultural environment. Their main competitive advantage rests on managers' experience gained in the period of transition, which are useful in solving similar problems related to recent economic changes in the Balkan countries. The leading foreign investors of Hungary underwent the process of restructuring in the 1990s, so they could learn how to become flexible, market-oriented companies. Moreover, 'indirect' investors (3 firms interviewed) enjoy the financial support and brand name of their parent companies as well.

It gives an additional, 'implicit' competitive advantage for Hungary-based companies against their Western competitors that a considerable number of Hungarian minorities live in the SEE region.[14] The presence of ethnic Hungarians also influenced the first-wave of investments made in Romania. Companies of service sectors initially concentrated their activities on Romanian regions inhabited mostly by Hungarians, and most of manufacturing

[13] With one exception, all of the companies interviewed have got subsidiary in Romania.

[14] The latest population censuses indicate that some 1.4 million ethnic Hungarians live in Romania (representing the largest Hungarian community living outside Hungary), 295 thousand Hungarians live in Serbia and 17 thousands of them in Croatia.

firms interviewed chose Transylvanian towns as headquarters. Many of the companies benefit from the common Hungarian language, however, they said that their investment decisions had been not 'emotional'. On the other hand, there is a company that, learning from the negative experience of some other firms, decided not to emphasize its 'Hungarian nationality' in Romania.

5. Conclusions

South Eastern European economies showing dynamic growth in recent years, play a greater and greater role in foreign economic relations of Hungary. Besides the development of bilateral trade, the SEE region has become one of the most important destinations for outward foreign direct investments of Hungary-based companies.

Political and macroeconomic stabilization, high potential growth of markets and significant improvement of business environment make Balkan countries attractive for direct investments of Hungarian firms facing challenges of limited potential of domestic markets as well as competitiveness pressures. The results of a company survey presented in the paper have confirmed that seeking new markets is the main motive behind companies' regional expansion. The investments examined have overall positive effects on Hungary's economic development. OFDI to Balkan countries has resulted in higher export performance of investors, consequently has improved Hungary's trade balance. Exploitation of cost differentials does not have been relevant motive so far, so Hungarian government should not be afraid of relocation of significant production capacities and 'export of jobs' from Hungary to SEE. Investments made in Hungary and in the Balkan countries rather complement than substitute each other. Tax conditions offered in SEE are also attractive, but have not influenced the decisions of the largest investors considerably.

The EU accession of Bulgaria and Romania as well as the EU's commitment to further enlargement to the Western Balkan countries will likely promote political and economic stability in the whole SEE region. The changing geopolitical situation of the Balkans implies new challenges and opportunities for Hungary. On the one hand, competition for inward FDI has become more intense. On the other hand, domestic companies have more possibilities to increase their competitiveness through outward investments contributing to the economic upgrading of Hungary. In order to utilize the competitive advantages of Hungarian companies in SEE, provided by geographical and cultural proximity as well as experience related to market economy transition, it is also required that promotion of OFDI should be a more pronounced part of Hungary's foreign economic policy.

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