National Specifics and International Experience in Foreign Direct Investment Attraction[1].

Anastasiya Luzgina[2], 2016

BEROC Policy Paper Series, PP no.36

Keywords: foreign direct investments, the Visegrad Group countries, a free economic zone, tax relief, privatization

Summary

The uncontrolled inflow of foreign investment in the country can have both positive and negative effects. In this regard, national governments develop and implement measures to attract foreign capital, taking into account the characteristics and interests of a particular state. With a view to better understanding the logic of the FDIs movement, the paper gives a brief description of the FDIs dynamics in the Republic of Belarus, as well as the study of the international experience based on the analysis of the FDIs attraction policies of the Visegrad Group countries (Hungary, Czech Republic, Poland) and Georgia.

[1] The article first appeared in Russian in the journal Bankovski Vestnik, June 2016.

[2] Anastasiya Luzgina Belarusian Economic Research and Outreach Center (BEROC), Minsk, Belarus, luzgina@beroc.by.

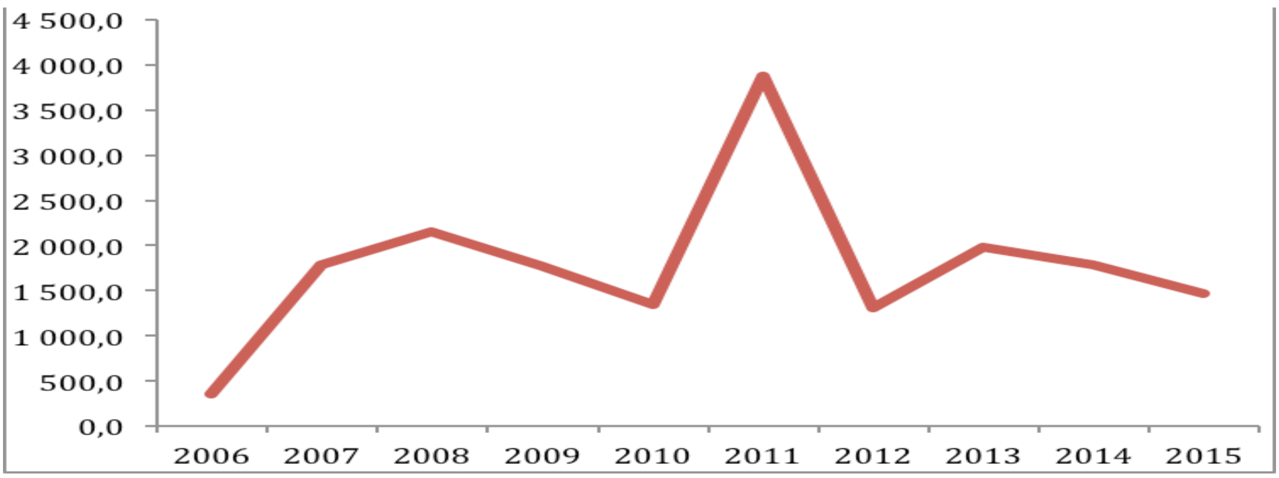
1. Introduction

Foreign direct investments (hereinafter referred to as the FDIs) is an important component of the successful economic development of some countries. The inflow of foreign capital in the form of direct investment contributes to the development of economic sectors, promotes the introduction of high technologies, creates new jobs and increases the level of skills of the workforce. The world practice has a number of developed mechanisms that contribute to the inflow of foreign capital. However, the uncontrolled inflow of foreign investment to the country can have both positive and negative effects. In this regard, national governments develop and implement measures to attract foreign capital, including foreign direct investment, taking into account the characteristics and interests of a particular state.

The Republic of Belarus

In Belarus, foreign direct investments attraction is one of the important objectives of the state economic policy. At the same time, over the years, the inflow of foreign investment resources was not well developed. If we analyze the FDIs inflow in annual terms, their maximum amount was recorded in 2011 of 3.9 bln US dollars. (*Figure 1*). The sharp increase in foreign direct investments in this period was due to the sale of 50% of Beltransgaz's shares. In other years, the increase of the foreign capital in the form of FDIs was up to 2.2 bln US dollars.

Figure 1. ***The inflow of foreign direct investments to the Republic of Belarus, mln US dollars***[3]



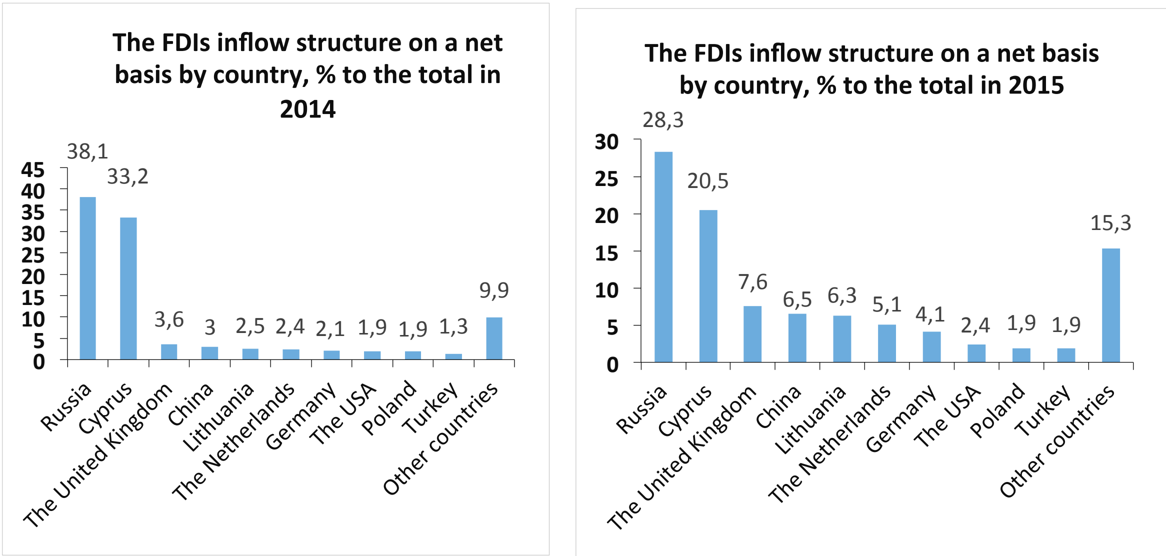
***Source**: the data of the National Bank of the Republic of Belarus [7].*

At the same time, if we consider the net FDIs inflow by country, main investing countries are Russia and Cyprus. It should also be noted that most of the

[3] In accordance with the sixth edition of the Balance of Payments and International Investment Position Manual (IMF, 2009), the standard representation.

foreign investment resources is concentrated in Minsk. This trend indicates that even with the creation of more favorable conditions for doing business in small towns, other regions of Belarus are still weakly attractive to foreign capital.

Figure 2. The structure of FDIs in the Republic of Belarus by country, % to the total in 2014 and 2015



***Source**: the data of the Ministry of Economy of the Republic of Belarus [4].*

In general, if we consider the FDIs dynamics, it may be noted that the country has created the basic conditions necessary formally to attract foreign capital. In particular, there are six free economic zones, within which produces about 11% of total industrial production. The residents of these zones ensured 12% of the total exports of Belarus in 2014. At the same time, the share of the foreign sources of the total investments in the free economic zones amounted to 45% in the reporting period. This figure rose to 55% in 2015.

In addition, foreign investors can minimize their costs when placing their business in small and medium towns. In this case, the investor is exempt from paying income tax for 7 years.

The qualified and relatively low cost labor is attractive for investors. Belarus has a high percentage of people with higher education. At the same time, many large industrial complexes in the country formed the necessary level of training of specialists of the corresponding profile.

A positive signal for investors is also a gradual improvement of Belarus's position in the *Doing business* ranking compiled annually by the World Bank. For example, under the 2015 results, Belarus was ranked as 44th out of 189 countries. The Investment and Privatization National Agency Active is active in raising the country's attractiveness for foreign capital. The main tasks of this body are the creation of a positive investment image of the country, improving the conditions of the privatization processes, and the establishment of dialogue and promoting linkages between foreign investors, government bodies and local businesses.

Finally, Belarus has a developed transport infrastructure, including a fairly good quality of highways, as well as an acceptable level of rail and air links. The geographical location of Belarus predetermines its bridging role between the countries of the Eurasian and European Union.

Despite a number of attractive components of the investment climate of the country, foreign investors are still not interested enough in Belarus. The main factors that hinder the inflow of foreign capital in the domestic market of the country are as follows:

- Lack of a stable macroeconomic environment, including relatively high inflation and unstable dynamics of the national currency;
- Low availability of credit resources, which is associated with high cost of loans, while maintaining preferential loans for certain categories of economic operators;
- The slow pace of the privatization process;
- The complexity of the tax laws;
- Inflexibility of the state policy in the labor market;
- Rather a complex public administration system.

It should be noted that there are a limited number of states, which would perfectly meet foreign investors' interests. In most countries, there are both attractive sides to foreign capital and disadvantages. It is necessary to consider the experience of countries with a level of economic development similar to that of Belarus, but which could form an attractive environment for foreign investment for a relatively short time.

Georgia

The feature of Georgia's development is that the country was able to rebuild its economy for a relatively short time. The FDIs were due in no small part to this transformation.

If we look at the 2002 data, in this period the GDP per capita amounted to only 0.8 thousand US dollars at current prices. At the same time there was a recession, the lack of financial income remained, the high level of corruption and bureaucracy limited the possibilities of attracting foreign capital in the economy. The military actions also adversely affected the situation in the economy.

However, the implementation of new reforms radically changed the situation in the country. Already in 2012, the GDP per capita at current prices amounted to 4.1 thousand US dollars. The increase of the attractiveness and efficiency of the national economy in terms of attracting FDIs was carried out by conducting the following reforms:

- Anticorruption reform;
- Law enforcement system reform, which included the criminal laws reform and judicial reform;

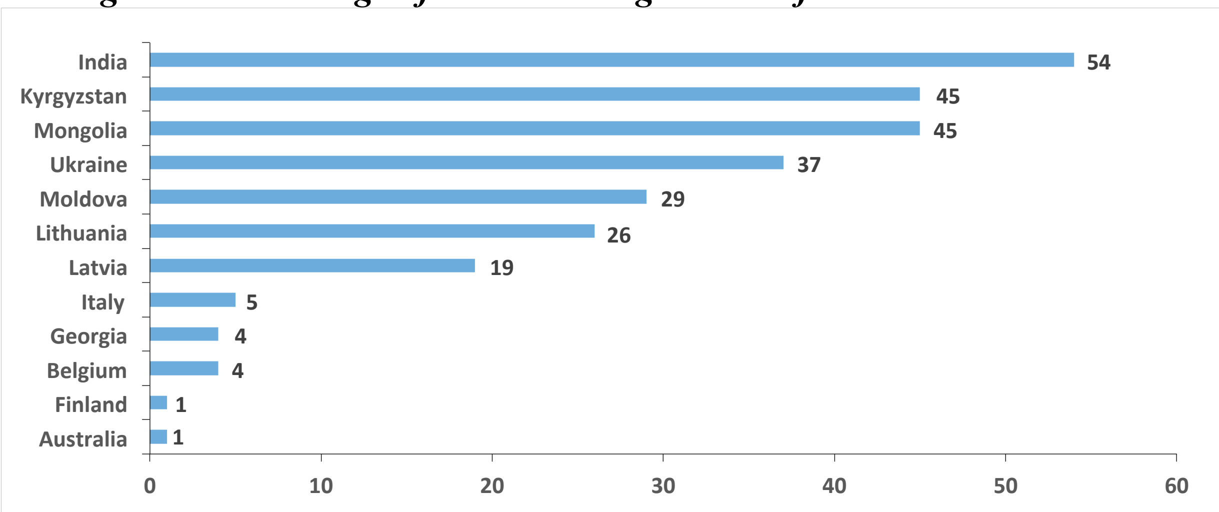
- Public sector reform, which included an e-government project, the public services reform and the introduction of the open governance principle and nepotism elimination;
- Customs reform, under which the tariffs were drastically reduced;
- Reform of licensing and issuance of business setting-up permits.

In addition to the above changes, a number of international treaties was signed, which also had a positive impact on the FDIs dynamics. The following can be identified among them: the free trade agreement, agreement on the avoidance of double taxation, investment protection agreement, etc.

Due to a fundamental restructuring, Georgia was able to carry out the transformation of public administration principles, together with changes in the economic sphere within a short time. The corruption efforts and registration procedure simplification were of particular importance for attracting FDIs.

If we look at the results of *Global Corruption Barometer* report, it may be noted that according to indicator such as the percentage of users bribing in education, health, taxation and customs clearance as well as the judicial system, Georgia's figures represent less than 5 %. This level allows the country to be among the leading countries characterized by a minimum level of bribery.

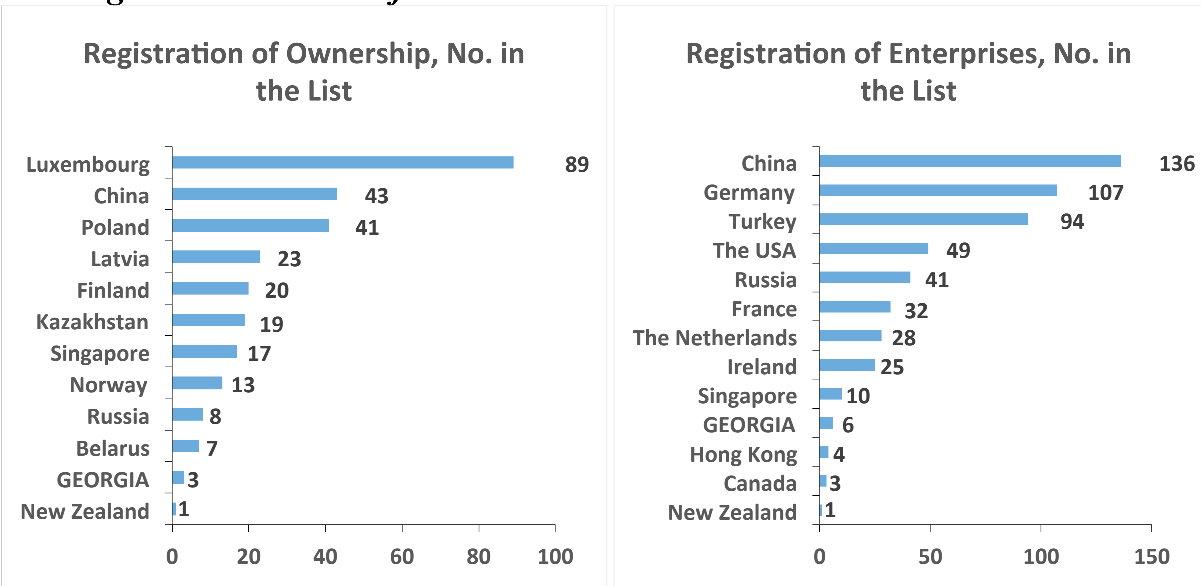
Figure 3. Percentage of Users Bribing in One of the Economic Sectors



***Source**: the data of the "Global Corruption Barometer, 2013" report [16].*

Georgia is on the 29th place out of 102 countries in the calculation of the supremacy of the statute law index and is on 23th place out of 178 countries in the calculation of the economic freedom index. At the same time, according to the World Bank's analysis, Georgia is one of the five leading countries by the property and businesses registration simplicity. All the above figures are indicators for potential investors.

Figure 4. Indicators for Potential Investors



***Source**: the data of the "Doing Business, 2016" report [12].*

Another factor in the investment attractiveness of the country is the tax burden level. Changes in the tax system in 2005-2009 led to the fact that today Georgia is characterized with one of the lowest tax burden levels. The number of main taxes was reduced from 21 to 6, which greatly simplified the procedure for their collection. In addition, rates of some taxes, such as VAT and income tax were reduced.

Table. The Tax Rate Level in Georgia

Tax	The rate prior to the reform	Current rate
VAT	20%	18%
Income tax	12–20%	20%
Social tax	33%	–
Profit tax	20%	15%
Import tax	0%, 5% or 12%	0%, 5% or 12%
Excise tax	It depends on the product	It depends on the product
Property tax	Up to 1%	Up to 1%

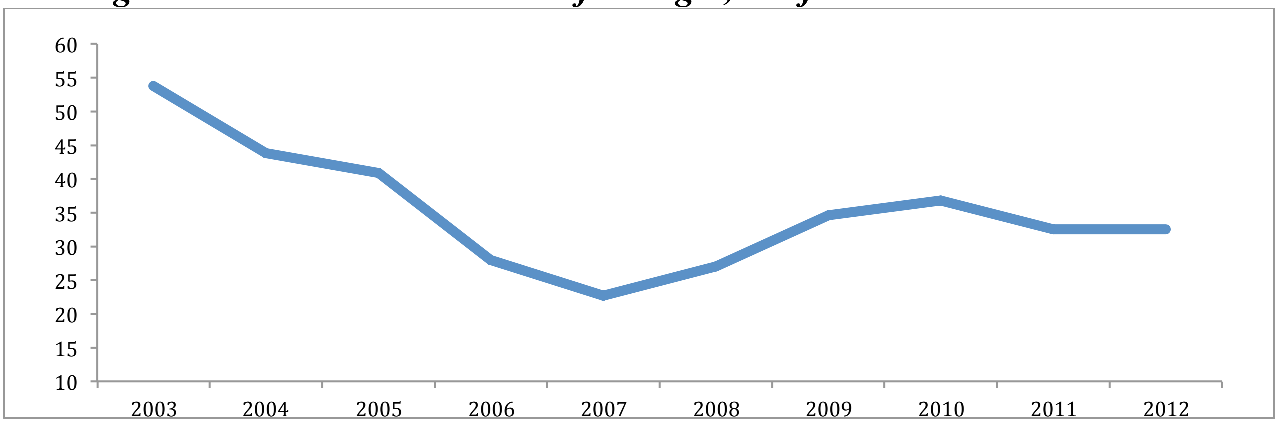
***Note**. The materials of the seminar "Learning from the Visegrad Group countries and Georgia in the field of administrative reforms to accelerate the economic development of the Republic of Belarus" [10].*

As part of the tax reform, all currency conversion restrictions and capital and profits repatriation restrictions were let down. Georgia has also signed agreements with 47 countries on avoidance of double taxation.

In addition, the country has abolished the trade regimes, which was reflected in the customs policy simplification. Since 2000, Georgia is a WTO's member. Currently, almost 80% of goods are exempt from import tariffs, while customs inspection takes on average 15 minutes. Georgia has established simplified trade regimes with a number of countries, and as a result, a market with more than 900 million people was formed for Georgian exporters, where there are preferential trade regimes. Among the major agreements that helped to facilitate the Georgian goods access to foreign markets, we can distinguish the following: Free Trade Agreement with Turkey and the CIS countries, Comprehensive Free Trade Agreement (DCFTA) with the EU, as well as the Preferences System with the US, Norway, Switzerland, Canada and Japan.

A favorable economic environment has also a positive impact on foreign investment. For 10 years (from 2005 to 2014), the Georgia's GDP in US dollars per capita increased almost by 3 times and at the end of 2014 was 4.4 thousand US dollars in nominal terms. Thus, from 2004 to 2013, the Georgia's GDP showed a steady growth in real terms. The year of 2009 was the only exception. It was a year of global economic crisis development. Despite the military conflicts and less-then-firmed-up economy, the country was able to maintain the total and external public debt at a low level.

Figure 5. The Total State Debt of Georgia, % of GDP

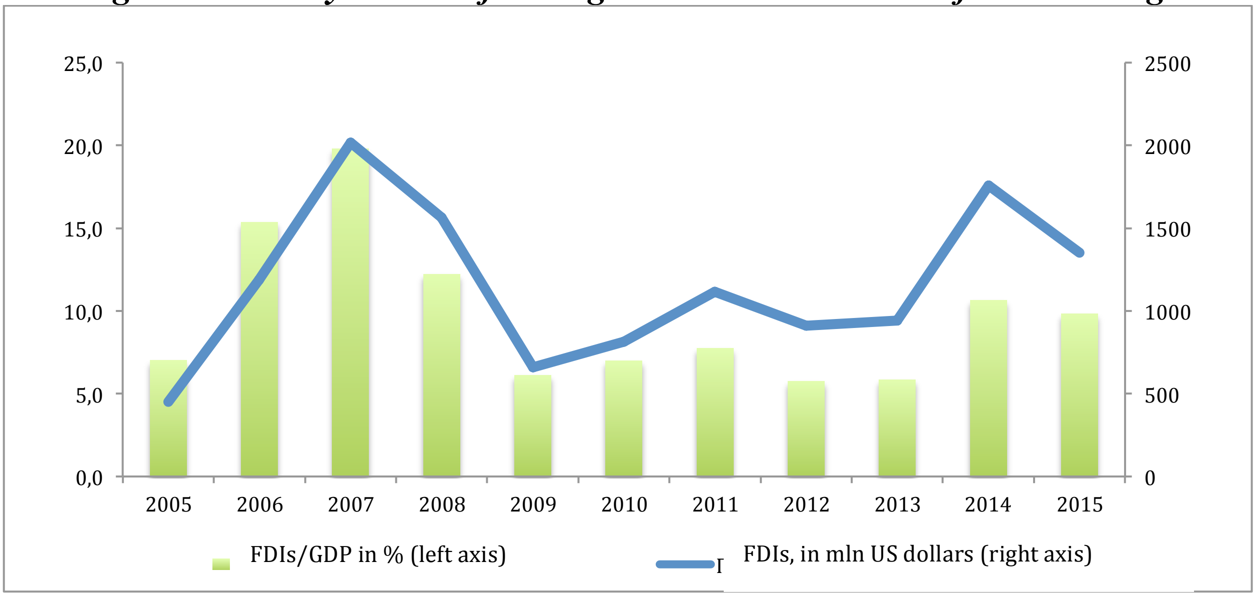


***Source**: the World Bank data [2].*

In addition to all these factors, the country has signed investment agreements with 32 countries. The Georgian National Investment Agency vigorous activity also promotes attracting foreign investments, which acts as a link between government, investors and national companies.

For the past ten years, Georgia is still characterized with the excess of imports over exports in the foreign trade. It should be noted that this problem is also a characteristic of the Republic of Belarus. At the same time, taking into account receipt of remittances and income from tourism, it is foreign direct investments, which have a positive effect on the foreign trade flow balance. The heterogeneity of the investment dynamics in time should be noted. Years of strong investments growth were followed by decline, which was largely due to the development of the global economic crisis. However, in recent years, despite the difficulty of attracting capital in foreign markets, Georgia managed to achieve quite a stable inflow of foreign direct investments.

Figure 6. The Dynamics of Foreign Direct Investment Inflow to Georgia



***Source**: the data of the Georgia National Statistics Committee, the International Monetary Fund [6; 8].*

Thus, Georgia's attractiveness for foreign investors is determined by the following factors:

- The ease of starting and running a business;
- A low taxation level;
- Openness and transparency of the administrative bodies' actions, a low corruption level;
- The simplified customs clearance system;
- The stable banking sector;
- Free trade agreements with several countries;
- Sufficiently high economy differentiation and growth of Georgia's attractiveness as a tourist destination.

In conclusion, it should be emphasized that Georgia is one of the few countries, which has transformed its economy and has managed to become attractive to foreign investors even in conditions of not a quite calm political situation. As a result, this has led to an increase in living standards.

Visegrad Countries

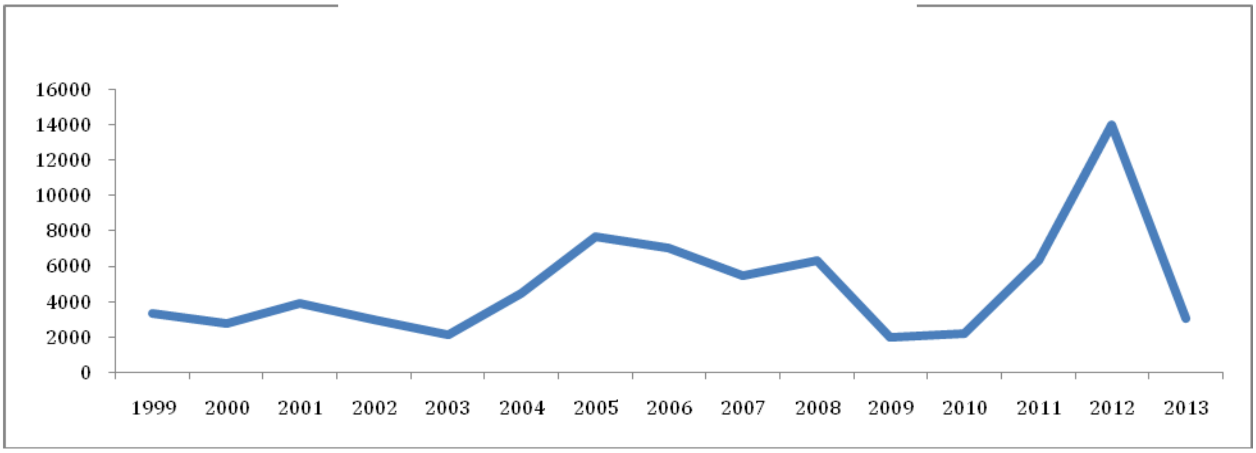
The FDIs dynamics of the Visegrad Group countries (among them Hungary, Poland, Czech Republic and Slovakia) has common features. This is due to several factors. First, these states were attractive to foreign investors in terms of the privatization processes and had a relatively low cost and skilled labor force. In addition, the countries' openness for foreign trade had a positive impact on FDIs. It should be noted that the Visegrad Group countries are strongly dependent on foreign capital, as it was associated with the access of the high technology and distribution networks to the markets. Slowing down of the privatization processes in the first half of the 2000s, as well as the global economic crisis have had the negative impact on the investment activity in the region.

Hungary. Hungary's FDIs dynamics can be divided into the following steps, namely:

- A transitional period (1989-1997);
- A period up to the accession to the European Union (1998-2004);
- A period after the accession to the European Union (2004-2008);
- The global economic crisis;
- A modern period.

In the transitional period, the FDIs growth rates were very high, which was due to the low comparison base, the introduction of market economic management principles, as well as the privatization processes intensification. During this period, Hungary was the first among the Eastern European countries by FDIs attraction. The FDIs inflow formed the potential investors' confidence and had a positive effect on foreign investment flows in subsequent periods. Since the beginning of the 1990s, more than 1,300 state enterprises were privatized in the country. By 2004, the privatization process was almost completed.

Figure 7. The Inflow of Foreign Direct Investments to Hungary, mln US dollars



Source*: the OECD data [9].*

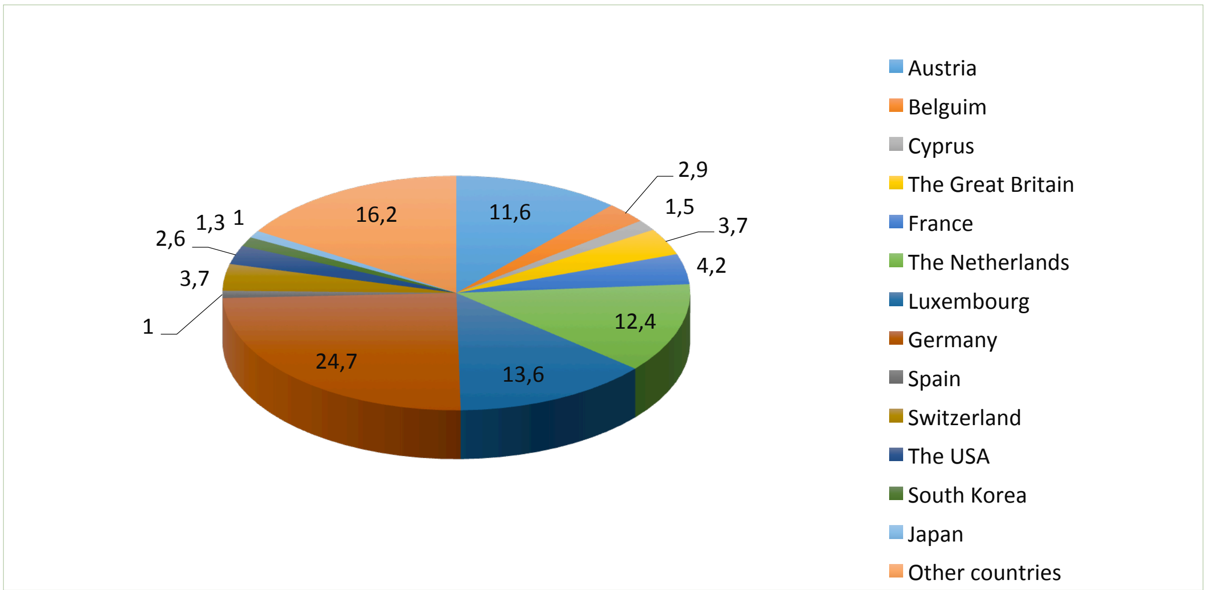
Prior to joining the European Union, the FDIs dynamics had its own peculiarities. If in 1998, investments in new projects were within 1-2 billion US dollars, then their gradual decline was observed in the subsequent years. Although the profits repatriation retained during this period at a constant level and the reinvestment volumes rose, Hungary lost its leading position in attracting FDIs among the Visegrad Group countries. Slovakia became a leader in the investments inflow.

At the beginning of the 2000s, Hungary's attractiveness decreased as a result of slowing down privatization processes, as well as of rising labor costs. After the country's accession to the EU, Hungary received an opportunity to attract external funding from the European Union structural funds, through which education projects and the national infrastructure development were implemented. Besides, for five years (from 2004 to 2008), Hungary managed to double the external financing of the services sector on account of external resources.

As a result of the global economic crisis in 2009, there was a sharp decline in the FDIs inflow in Hungary, however, already in 2010 the level of investment flows recovered. Despite the positive dynamics of the investment processes, the share of investments in high-tech production remained at a low level, since the main attractive feature of the Hungarian economy to foreign investors remained relatively low cost labor.

It should be noted that Hungary is actively participating in the Global Supply Chain. For example, German companies is constantly attracting Hungarian companies to their production and manufacturing processes. At the same time, if we consider Hungary's FDIs inflow structure by country, we can note their relatively high differentiation. The main investing countries in the Hungarian national economy are naturally the EU countries, namely Germany, Luxembourg, the Netherlands and Austria.

Figure 8. The Structure of Foreign Direct Investments to Hungary by Country at the End of 2012, %

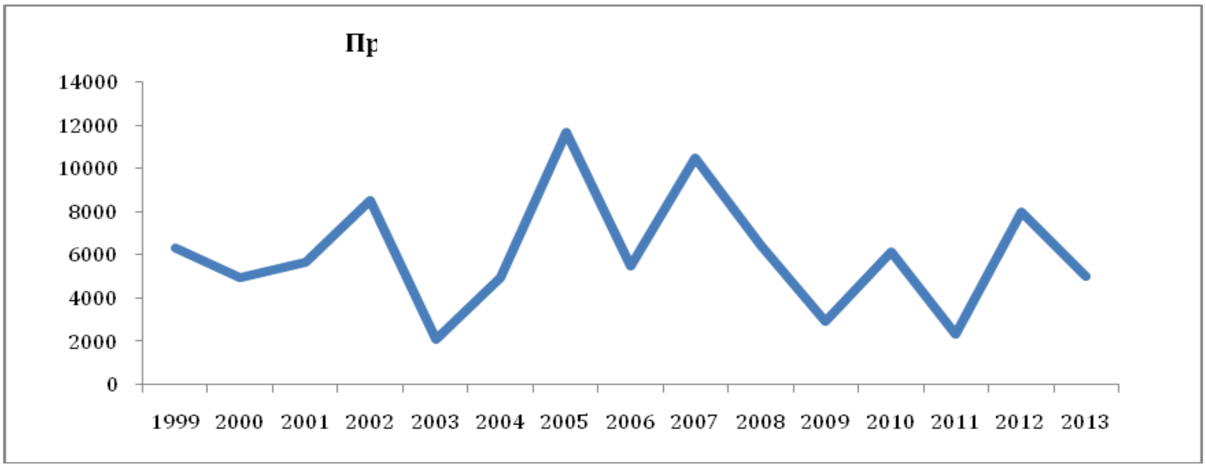


Note*. The materials of the seminar "Learning from the Visegrad Group countries and Georgia in the field of administrative reforms to accelerate the economic development of the Republic of Belarus". [10]*

Thus, FDIs attraction had a significant positive impact on the development and reconstruction of the country's economy. FDIs resulted in labor productivity stimulation, technological modernization acceleration and export activity increase. In addition, the foreign capital inflow helped the creation of new jobs.

Czech Republic. The processes associated with the foreign capital inflow to the Czech Republic had much in common with similar processes in other Visegrad Group countries, but had its own characteristics.

Figure 9. The Inflow of Foreign Direct Investment to the Czech Republic, mln US dollars



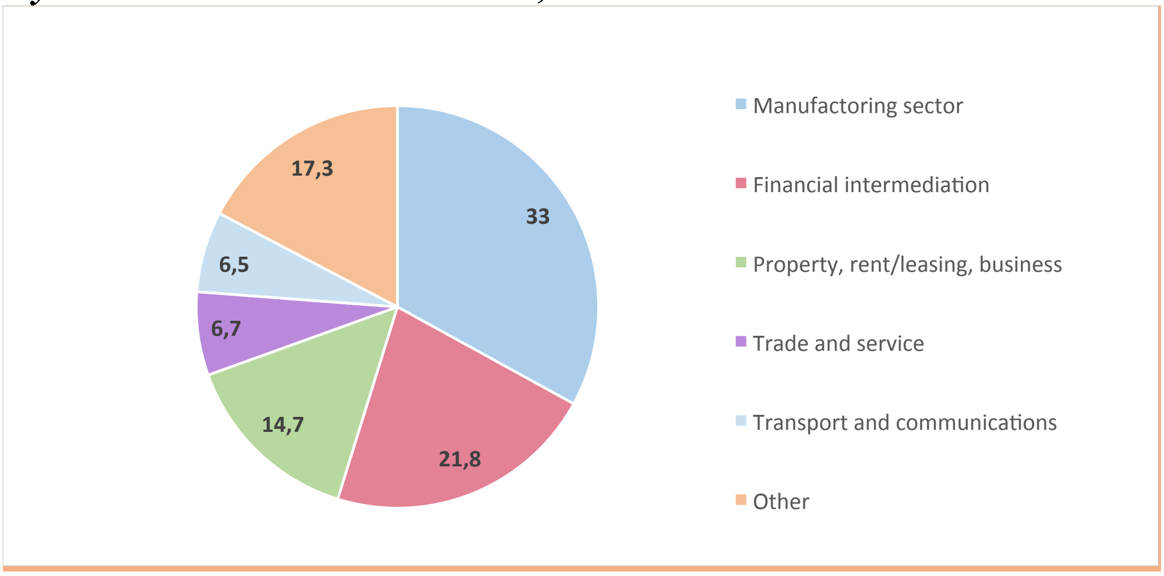
Source*: the OECD data [9].*

The situation with the involvement of FDIs to the Czech Republic can be divided into several phases. In the first phase (from 1989 to 1996), the foreign capital inflow was largely due to the direct sale of state enterprises to foreign investors, as well as due to the inflow of medium- and long-term loans. The Czech authorities' policy was aimed at preventing any advantages for foreign investors. The economic growth of the country in a given period was based on the competitiveness of Czech goods in foreign markets at the expense of low cost labor and the devaluation of the Czech crown. The FDIs inflow was at the level of 2% of the GDP.

However, the country's economy faced a recession in 1996. This was associated with a low level of enterprises modernization and the unreasonable increase in the money supply. The foreign capital inflow in conjunction with the excessive increase in wages led to the national economy overheating. The economic crisis has pushed the Czech authorities to understand the importance and necessity of FDIs. As a result, in 1998-1999, a number of measures that have contributed to the attraction of foreign capital into the economy was adopted. The country's telecommunications and transport infrastructure development, as well as a number of privatization deals in this period and the creation of new enterprises contributed to Improving the investment climate.

It should be noted that, since 1989 and up to the beginning of the 2000s, the country has received about 20 billion US dollars of foreign investments, half of which was attracted for 1999-2000. Thus, from 1998 to 2002, the country was characterized with a FDIs inflow, and in addition to the production sector, the banking sector and the public services sector were invested significantly. Then gradually, a foreign investment inflow vector began to shift to the telecommunications and real estate. In addition, due to foreign capital, business support services and technology centers began to develop.

Figure 10. The Inflow of Foreign Direct Investment to the Czech Republic by Main Economic Sector in 2012, %



Note. *The Author's Development Based on the Data [17].*

Currently, the attractiveness of the Czech Republic is also based on a high rating, which the country has received based on the results of the Global Competitiveness Report 2014 -2015. According to the document, the Czech Republic ranks the 37th among 144 countries in the world and 2nd among the European Union countries. Besides, the Czech Republic is the first among the countries that are new EU members by the quality of rail transport, air traffic, inner competition intensity, credit availability, manufacturing process complexity, innovation and expenditures on researches and innovation by private companies. Germany, Austria and the Netherlands remain main investors in the economy of the Czech Republic.

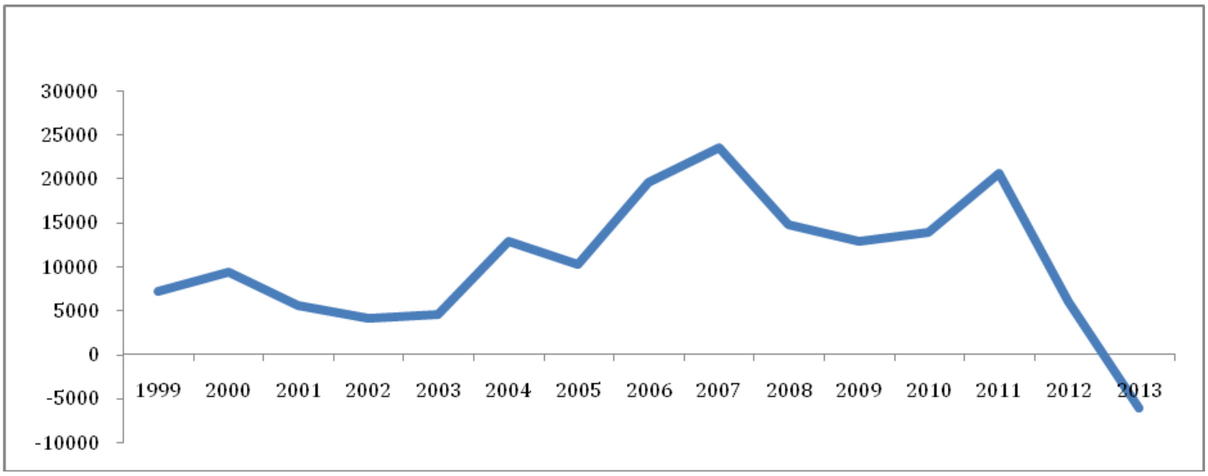
The Czech Republic Investment Agency plays an important role in attracting foreign investments. It provides information support to potential investors, has access to the EU structural funds, creates and develops infrastructure for business, considers investment initiatives, as well as provides support for investors, who are already operating in the Czech market.

The State has developed a special scheme to attract new investments. Incentives for potential investors are the exemption from corporate income tax for 10 years and from property tax for 5 years for newly established companies, providing financial support for job creation, funding allocation for training and retraining new workers. The State also provides financial support in the event of a strategic investment in manufacturing or processing centers.

In addition to the above, the inflow of FDIs to the Czech Republic is contribute to by factors such as political and economic stability, the rule of law, investment protection, protection of private property rights, the availability of relatively skilled and low cost labor, good infrastructure and low investment risks.

Poland. In Poland, as well as in several countries of Central and Eastern Europe, FDIs were one of the sources of economic modernization. Active growth of foreign investments in the economy began in the early 1990s, when the country's economy began transferring to a market and accelerated economic development. FDIs were characterized with active growth until the early 2000s followed by a recession, which was mainly due to the slowdown in the privatization processes, as well as external facts, including the bankruptcy of a number of major corporations and international conflicts. Gradually, FDIs growth has been restored in Poland and it reached its peak in 2007. A number of authors associate it with the country's accession to the European Union. However, this inflow had no long-term nature, and was followed by a decline in 2008 that was due to the global economic crisis. In 2010-2011, the investment flow gradually recovered, that was again followed by a sharp decline in 2012.

Figure 11. The Foreign Direct Investments Inflow to Poland, mln US dollars



Source*: the OECD data [9].*

In general, Poland can be characterized with a quite heterogeneous dynamics of foreign investment inflow by year. Moreover, while Poland is in the lead by FDIs inflow in absolute terms among the CEE countries, this does not mean that the size corresponds to the economic potential. If we compare the FDIs sufficiency based on the ratio of FDIs to GDP or FDIs to the population, the country ranks one of the last places among the countries of Central and Eastern Europe by these indicators. This indicates the need to further encourage foreign investment in the country.

In this respect, the Government has developed a number of additional measures. For example, according to some investment projects, the State provides a direct financial support. This applies mainly to the projects that help create jobs, improve the situation on the domestic labor market, stimulate exports and promote the high technologies development. The state support is defined in accordance with the principles specified in the document *The Support of the System of Investments Important for the Polish economy*. The State provides assistance in the form of grants based on the signing of a bilateral agreement between the investor and the

Ministry of Economy, which is then approved by the Council of Ministers of Poland.

In addition to the direct State's support, the establishment of a number of tax preferences for investors contributes to the FDIs inflow. There are 14 free trade zones in Poland, within which a preferential tax system is used. For example, some companies are provided with "tax holiday" for income tax or property tax.

Given the fact that Poland is a member of the European Union, it is quite natural that European investors provide the bulk of investment resources. For example, in 2011, about 85% of FDIs came from EU member states. The main investing countries were Luxembourg, Spain, Germany and Sweden. The concentration of foreign capital is observed in areas such as industry, construction, telecommunications, and the financial sector. It should be noted that the investment priorities of some sectors in comparison with others determine the growth of the income gap.

If we review Poland in terms of its attractiveness for foreign investors, we can define the following positive features:

- The location of the country;
- A large domestic market;
- Cancellation of various barriers between the European countries and Poland in connection with the country's accession to the European Union;
- Relatively low cost and skilled labor force;
- A high proportion of the labor force at a relatively young age;
- Macroeconomic stability, including the GDP steady growth, financial sector stability and relatively low inflation.

At the same time, certain weak points of the investment climate in Poland explain insufficient and uneven FDIs inflow by year, which include:

- Poor quality of highways and railways;
- Excessive tax burden;
- Bureaucratic and inconsistent legislation;
- Weak interaction between science and business;
- Trade unions' strong positions;
- A foreign exchange risk due to the presence of its own currency (Polish zloty).

Thus, it should be noted the important role played by FDIs in the country's economy. A sustainable economic growth began from the active inflow of foreign capital to Poland. FDIs also influenced the dynamics of the country's exports. The share of companies with foreign capital in the total volume of exporters increased for 1995 – 1998 from 38 to 48%. It is an indisputable fact that FDIs contributed much to the dynamics of the total investment activity. In particular, the share of foreign investments in the total volume of investment resources has risen from 20 to 40% in 1994-1997. At the same time, the inflow of foreign capital would be considerably less if the Polish Government did not developed a series of measures to support foreign investors.

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Belarus are created the basic conditions for attracting foreign capital, but the inflow of FDIs to the country is relatively low as a result of both macroeconomic factors and some of the constraining economic policy instruments. If we turn to the experience of the Visegrad Group countries and Georgia, it is possible to state that the active attraction of FDIs had a positive impact on the economic development of the States. Sufficiently active foreign capital is observed in these countries.

The arrival of foreign investors was due more due to external factors then internal factors. It was possible to attract significant foreign investment in large part because of the active work of national governments, which created favorable conditions for attracting FDIs. As part of the investment program, they simplified the tax base, reduced interest rates by certain types of taxes, established tax incentives, formed a stable national legislation, reduced the level of corruption, set up free economic zones, etc. The relatively low cost and skilled labor force, the privatization process development, the creation of comfortable and well-developed infrastructure and macroeconomic stability also supported the attractiveness of the country to foreign capital. A successful experience of foreign investors in the market of the country was also an additional incentive for the inflow of foreign capital.

In conclusion it should be noted that only the implementation of the above factors in their immediate relationship would form a favorable environment for active FDIs inflow to the Republic of Belarus.

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