The Endeavour to Maintain Full Employment

Do FDI Inflows Stimulate Labor Market Developments in Central Europe?

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ABSTRACT

The present study intends to create a better understanding of the relationship between foreign direct investment inflows into Central Europe and their effects on labor markets. All countries of the region have attracted huge amounts of FDI during their transition in the hope for economic development. During the last 20 years not only the amount of FDI inflows but also its structure has significantly changed. While several studies investigate single effects of FDI on labor in the region, there is a lack of analysis of effects throughout the development of FDI attraction patterns. This thesis therefore analyses the development of FDI attraction in Central Europe over time. Subsequently, its focus turns towards FDI effects on the labor market, concentrating on the three variables of employment, labor productivity and trade union power. These two sets of research are brought together in order to infer policy implications from it. During the analysis a special focus is taken on the cases of Hungary, as a first mover and Slovakia, as a late mover in FDI attraction. As a result the thesis finds that at the first stage of transition foreign owned affiliates work more efficiently and show thus better conditions for job maintenance and spillovers, usually achieved through training. Working conditions at this stage are improved by foreign investors and cooperation with trade unions seems to take place. This study, however, observes a transformation over time, due to a changing structure of inward FDI patterns. At a later stage, FDI, especially focused on export-oriented activities, may still contribute to employment, but spillover effects into the local economy require the presence of absorptive capacities, while trade unions experience increased rejection by foreign investors. For policy makers this means, that they need to adapt to these changes in order to gain benefits on the labor market.

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Introduction

With the fall of the Iron Curtain, the region of Central and Eastern Europe entered a long process of transition. Markets were liberated and thus borders not only opened for people, but also for capital flows and business ideas. As a result, numerous foreign companies perceived promising chances for expansion on the newly liberalized markets during their period of construction. These foreign direct investments are often seen as a core factor to development (United Nations 2002). Political leaders are even evaluated on their ability to attract foreign investments (Woolfson and Beck 2002, 754). With the fall of communism a number of countries opened their markets at the same time, all with similar advantages and disadvantages for investment, as all countries are located closely to European sales markets, have large amounts of educated labor force and struggled with similar problems of political instability and lacking infrastructure. In other categories of importance for the attraction of FDI, however, politicians started to compete for the highest amounts. A race to the bottom began, in the hope that FDI would conduct the transition process to a market economy (Woolfson and Beck 2002, 754; Jensen 2006, 889). Politicians perceived FDI as a panacea for economic development and transformation (Jensen 2006, 881). One of the strongest hopes was and still is that large multinationals would be able to maintain high levels of employment. Moreover, skills were anticipated to spill over to domestic industries.

Significant changes on the labor market, however, are contested, especially throughout the progressing of transition. Konings, for example, sees clear limits for the benefits from spillover effects (2001). Woolfson and Beck even argue that FDI

have very negative effects on labor protection (2002). Moreover, few articles explicitly study the effects of FDI on the labor market, despite the assumption of policy makers that causation is strong. The debate rather focuses on effects of FDI on economic growth and thus, whether the attraction of FDI should generally be promoted or not (Neuhaus 2006; Lansbury et al. 1996). Other studies investigate the factors that attract FDI, but even here labor incentives are rarely at the focus of analysis (Janicki and Wunnava 2004; Blomstroem and Kokko 2003). Effects of FDI on employment are almost exclusively analysed in the home country (Baldwin, 1995; Feinberg et al., 1998). On the main target countries of FDI flows, namely Central Europe encompassing the Visegrád countries and Slovenia, little research is done so far. The present study will therefore focus on Hungary and the Slovak Republic as these two cases are highly representative for the region.

Both countries show great similarities in all generally relevant factors for the attraction of FDI such as country size, competitiveness of wages, level of income, geographical proximity to Western European sales markets and endowments, but also political stability, infrastructure and education level (Jensen 2006, 884). Moreover, they stand in direct competition and attracted huge amounts of FDI during the last twenty years, as all countries in the region. What distinguishes them, however, is that Slovakia is only recently considered as highly successful in terms of economic development and thus in the enhancement of national welfare, while Hungary faces severe problems of economic decline and political instability despite its very positive development in the initial phase (Jaklicand and Svetlicic 2001, 73). Hungary belongs to one of the first movers in the attraction of FDI, while Slovakia is rather a late mover in terms of policy making but might thus face similar challenges at

a later point in time (Jensen 2006, 889). As these two countries developed similarly but in different time sequences, they are expected to reveal new insights on development over time. On this background, the present study will investigate the effects of FDI on labor markets in Central Europe and deduce policy implications from this.

The question I will thus pose in this thesis is: what are the effects of inward FDI flows on the labor markets in Central Europe? The evaluation of effects will concentrate on the three variables of employment effects (1), labor productivity effects (2) in the sense of skill spillovers, and the power of trade unions in the region (3). In these areas of research the following hypotheses are formulated for investigation:

1. FDI inflows increase a country's employment. Greenfield investments in the region of Central Europe allow new industries to enter the markets and thus to create numerous jobs in the region. Moreover, foreign investors who were involved in the process of privatization are assumed to be more efficient in leading the acquired company through transition and hence could maintain higher numbers of jobs.
2. FDI inflows increase overall labor productivity. Through the inflow of FDI skills are transmitted into the new market. First of all, employees of multinational companies receive training, but their knowledge might also spill over to domestic companies through job changes. Thus, labor productivity is expected to rise in multinational as well as domestic firms.

3. FDI inflows have negative effects on the establishment of trade unions. Foreign investors often take an anti-union position and prevent their strengthening by the exertion of financial power.
4. The positive effects on the labor market were stronger in the initial phase of transition and even the negative effects become reinforced over time. Because competition increases, foreign affiliates are less likely to employ workers above their actual level of efficiency. Training of staff for knowledge intensive activities becomes less efficient over time. The attitude of multinationals towards trade unions becomes more aggressive in the need for higher competitiveness.

The methodology relies on the analysis of two different sets of studies. The first part concerns the structural aspects of FDI flows into Central Europe and their transformation over time. The second part will be an analysis of several quantitative and qualitative studies of FDI effects on the labor market in Central Europe. These research results will allow me to evaluate the causal relationship between FDI, as my independent variable and its effects on the labor market, concentration on employment, labor productivity and power of trade unions which represent the dependant variables. My assessment will mainly be based on the works of Radosevic, Mickiewicz, and Varblane. Combining the results of these two sets of research will allow me to evaluate effects of FDI on the labor market throughout different stages of FDI attraction. In a second step, I will draw some conclusions on governmental policies needed to ensure desirable effects on the labor market. Several governmental incentive packages which were designed in the region will back up the conclusion.

The expectations of politicians towards FDI to cure national employment problems are usually very high (Mickiewicz et al. 2000, 9). Despite this fact, only little research has been done on the actual effects in this field. This study will contribute to a better understanding of how valuable expectations towards FDI to positively affect the labor market are. Very often policy makers are willing to accept very high cost for the attraction of FDI. This thesis will analyse to what extent costs for the attraction of FDI are justified and what this means for policies that attract and condition FDI inflows.

This thesis will, however, neither make a full evaluation of costs and benefits of inward FDI, nor take into account all relevant factors on the labor market. The level of income or regional distribution of employment and income are further important dependant variables of inward FDI for the assessment of the labor market, but will not be discussed in this paper. Moreover, no complete evaluation of policies towards FDI will be presented but a limited case selection will support the understanding of policy trends in the region.

The first chapter will provide an overview on the development of FDI in Central Europe based on the empirical model of Lankes and Venables. In the second chapter the three variables of the labor market will be analyzed accordingly and put into relation of their development over time. From this, some policy implications will be deduced, taking also existing policies into account. Finally the thesis will conclude on the hypothesis made.

1. Patterns of Foreign Direct Investment in Central Europe

The political, societal and economic situation in the region of Central Europe changed significantly during the process of transition, which also implies important developments for the region as an investment environment. Conditions for investment as well as effects of investments for societies were and still are under constant transformation. For the labor market, this means that effects of the attraction of FDI might have been different throughout the transformation process. This chapter will therefore focus on quantitative and qualitative aspects of FDI and their transformation over time in Central Europe.

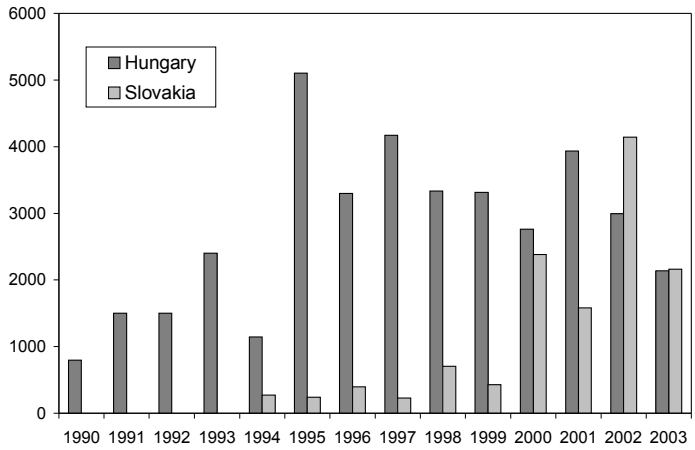
The amounts of FDI allocated to Central Europe were enormous. In the 1990s the share of worldwide FDI flows in the region of Central and Eastern Europe rose from 0.1 to 3.7 percent (Protsenko 2003, 3). In absolute numbers this means an enhancement of FDI flows from $476 million in 1990 to $28.7 billion in 2001 (Protsenko 2003, 3). Moreover, Central Europe was clearly preferred by investors over countries located further to the East. Despite trends of allocating investments further eastwards, even in 2001 69% of all inward FDI of Central and Eastern Europe flowed into Central Europe (Radosevic et al. 2003, 54). In 2000 around 25% of companies in the region were owned by foreign investors and in the more advanced countries, employment among foreign companies counted for more than 50% (Protsenko 2003, 7).

In Hungary FDI inflow increased to its peak in 1995. In this period FDI stocks grew to approximately ten times of their original volume (UNCTAD Hungary 2001). By 2001

the country held the third highest stock of FDI in the region (UNCTAD Hungary 2001). Typically for investments in the region, capital comes mostly from Western Europe, at a rate of more than 90 percent (UNCTAD Hungary 2001). Investments are mainly directed towards the tertiary sector, especially in the areas of trade and finance (UNCTAD Hungary 2001). These represent typical targets for investment which strive to gain local market power.

After ten years of attracting little FDI, Slovakia experienced a strong and sudden development in the years 2000 and 2001. Suddenly it became one of the six largest recipients of FDI in the region (UNCTAD Slovakia 2001). By 2001 FDI stocks thus grew to around ten times of its volume in 1994 (UNCTAD Slovakia 2001). While Hungary was one of the first-mover countries in the attraction of FDI, Slovakia only started to advertise itself at a much later stage with much more sudden developments. Comparing the development of FDI inflows, Slovakia has gone through a similar process of FDI attraction as Hungary, but with a five to ten years delay. The huge quantities of FDI attracted in the whole of Central Europe are generally assumed to have significant effects on local economies and employment.

Figure 1: FDI inflows in Hungary and Slovakia



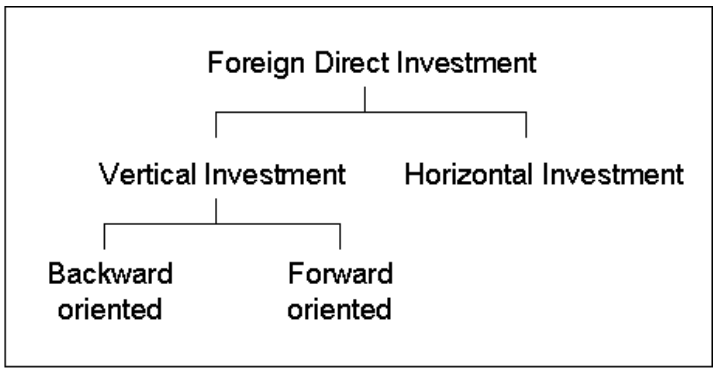
Source: OECD Country Statistics

In qualitative terms, foreign direct investment can have two functions. Either it seeks market access or aims to profit from lower input costs (Protsenko 2003, 5). Despite their function, FDI appears in two different structures, horizontal or vertical (Protsenko 2003, 5). By horizontal, the literature refers to the establishment of similar production processes abroad as in the home country. The benefit of such investments lies in the local cost advantage of production instead of exporting products or services. Thus, horizontal investments refer to a duplication of activities abroad. Vertical FDI, in contrast, describe the outsourcing of specific stages of the value creation chain to a foreign country. In this case, single production or assembly processes are integrated into an international production network because of specific input cost advantages. These advantages are most likely to refer to lower costs for labor through regional wage differences. Thus, it might become profitable for companies to split production chains.

As for FDI into Central Europe, the first wave of investment was motivated by the aim of accessing large numbers of potential consumers and thus of seeking for new markets. These investments were moreover characterized by horizontal structures. Once the first attempt of occupying market shares was fulfilled, multinationals changed their strategies towards more vertical integration (Brenton et al. 1998, 21). Horizontal investment has been mainly motivated through first-mover advantages while later horizontal investment aimed to benefit from location factors, such as low taxation and low labor costs for increased competitiveness in the export of products (Radosevic et al. 2003, 61-62). Nevertheless, it is observable that FDI was only attracted by growing domestic markets (Radosevic et al. 2003, 62). This is a dominant factor for the attractiveness of Central Europe in comparison to Eastern

Europe. Only over time, did investors move further eastwards. Moreover, there is a trend that vertical investments were initially concentrated in the final steps of the production process but increased in the first stages of the value creation chain over time. In the theory, these tendencies are described as a change from vertical forward to vertical backward investments (Protsenko 2003, 7). An investment which is meant to set up a supplier of input products abroad for the assembling in the parent company is considered as a backward investment. Thus, this kind of investment describes activities which are rather at the beginning of the value creation chain. Forward investments accordingly describe the establishment of production processes at the end of the value creation chain. The affiliate abroad receives input factors from the parent company for further assembling. In Central Europe vertical forward investment previously dominated for the retail of products on local markets, as market seeking was the main priority. Over time, however, plants which were built up in the region became integrated into global production networks for export purposes.

Figure 2: Types of FDI



Source: Protsenko, 2003

In their study, Lankes and Venables (in Radosevic et al. 2003, 60-61) analyse these structural trends in Central Europe and deduce from their results a model of three stages of transitional development in regard of the attraction of FDI. They show that

there is a correlation between the level of transition and the type of FDI which is attracted. The first phase of transition, in which society and economy undergo deep institutional transformation, is characterized by the attraction of distributors, local market seekers and the establishment of joint ventures (Bevan and Estrin 2002, 7). In other words, investments flow into activities of vertical forward type. Because institutional instability as well as market uncertainty are actually inhibitive factors for multinationals, Radosevic et al. explain huge amounts of investments by the seeking for competitive advantages through a first-mover strategy (2003, 62). At this stage of development, investors are mainly concerned about taking over domestic market shares for future expansion. Moreover, the employment of cheap labor in offshore locations incentivizes investment for an increase of competitiveness (Mickiewicz et al. 2003, 12). Equity investment is made in combination with the subcontracting of other companies (Radosevic et al. 2003, 62). Thus, investment is rather concentrated in the last parts of the value chain, namely in the assembly activities of the production process or distributive division (Mickievicz et al. 2000, 12). Investments primarily target consumer goods distribution on local markets and are therefore accumulated in trading (Radosevic et al. 2003, 62).

Table 1: Phases of FDI inflows in Central Europe

Item	Phase I Market Seeking	Phase II Market/Efficiency Seeking	Phase III Efficiency seeking
Motives for FDI	•First-mover advantages •Cheap labor •Domestic Market acquisition	•Factor cost advantages •Skill improvement •Local market	•Export-oriented FDI •Local suppliers •International value chain integration
Dominant FDI types	•Distributors •Low value-added activities	•Phase I type + offshore plants	•Phase II types + focused production activities

Source: Radosevic et al., 2003

The second phase of transition is characterized through improvements of the institutional framework and skills, as practises of liberal market behaviour reached the labor force. Thus, the environment for investments changes and investors increasingly build up supplier networks with local firms which makes them independent of the import of components (Mickiewicz et al. 2003, 13). Offshore plants are included in such networks which thus become part of international value chains, providing an advantage in terms of low input costs (Radosevic et al. 2003, 64). Multinational firms, consequently, strive for profit from low factor-costs and increasing benefits from growing purchasing power in the domestic market.

In their third phase of transition, countries increasingly attract investors for export purposes which profit from specific location factors. Thus, especially labor intensive activities of the value chain are located abroad (Radosevic et al. 2003, 63). At this stage, investors, moreover, tend to acquire wholly owned affiliates instead of equity investments and subcontracting. Thus, at this level, investments become a lot more focused. The decrease of risks and the growth of domestic markets function as strong incentives which provide investors with more certainty for long-time investments.

Unfortunately there is no analysis of when countries of Central Europe entered such three stages of transition. Some countries, like Hungary or Poland sought FDI more aggressively right after the fall of the Iron Curtain and are thus considered as first-movers, while other countries like Slovakia or the Baltic States, as part of Eastern Europe, only recently increased incentives for FDI attraction. Countries within the

region developed at different time intervals and at different speeds. On the one hand this raises the assumption that employment developed with great variation in the region and on the other this fact could reveal important causality between the level of FDI development and the labor market. Both quantitative as well as qualitative aspects of FDI are assumed to have effects on employment developments. As both factors strongly changed during the transition process, effects on employment, labor productivity and trade union power are likely to have changed over time.

2. Effects of FDI on the Labor Market

As FDI was channelled into Central Europe in huge quantities, it has great influence on local employment in terms of structure, regional and income distribution, wage levels and development of skills (Mickiewicz et al, 2000, 8). While an analysis of all these factors would provide a comprehensive picture of labor market developments, this chapter will focus on the study of the effects on employment, labor productivity and power of trade unions one by one. While doing so, the described FDI developments over time will be taken into consideration and show to what extent they differently affect labor markets.

2.1 Effects of FDI on Employment

During communism and under planned economies, the problem of unemployment was entirely unknown to all governments of Central Europe. Companies did not produce according to efficiency but output (Mickiewicz et al. 2000, 9). Instead “labour hoarding” (Mickiewicz et al. 2000, 9) was a widespread practice of companies. Unemployment was nonexistent. The transition to a market economy was certain to require deep cuts in employment throughout the process of privatization in order to make companies run efficiently and to adapt them to the competitive needs of a market economy. Nevertheless, governments hoped to maintain levels of employment through the attraction of FDI (Radosevic et al. 2003, 54). This was an attempt that clearly was doomed to failure.

Investments made can be differentiated into greenfield investment, meaning the building of entirely new plants, and brownfield investment which usually implies a

transfer of ownership of an existing production unit. Brownfield investment occurred mainly as part of the privatization process. Greenfield investment clearly contributes an additional unit to national GDP and is thus likely to create employment. Brownfield investment, however, dominating in privatization processes, faced the challenge of transforming companies of the former system of planned economies into competitive players in a market economy. It is thus not entirely clear whether the attraction of FDI could support the maintenance of jobs in brownfield investments. The aggregated data suggests that there was a great loss in jobs and that industries declined. De Loecker and Konings, however, suggest in their study on Slovenia, that this was a process of “creative destruction” (2003, 6) of jobs. By this, they mean that job destruction is a necessary process for the elimination of unproductive jobs which is then followed by the creation of new and more productive jobs. The net result of jobs created would thus still be positive. Moreover, this would also include an increase of labor productivity. For Slovenia, De Loecker and Konings found that in the Slovenian manufacturing industry, job destruction is accompanied by a simultaneous and much more extensive job creation process (2003, 22). While firm exit rates are similar to many countries of Western Europe, they find that firm entry rates are much higher with an average of 5.56% per year in the period of 1994 till 2000 (2003, 5). Moreover, they identify a positive net employment growth rates to which export companies contribute the most with highest rates of job maintenance and creation (2003, 7). Thus, transformation includes a significant process of job reallocation. It can be assumed that similar processes took place in other countries of Central Europe with similar challenges of transition.

The study unfortunately draws no conclusion on the role of foreign investors in the process of creative destruction. Hunya and Geishecker, however, describe the same process in the whole of Central Europe when they write about simultaneous job losses and creation (2005, 6). They further add, that transnational corporations were "the major investors in the competitive sectors and thus had a primary influence on job creation and job destruction" (2005, 7). According to them, foreign investors only moved faster in the restructuring process and thus laid off workers at an earlier stage than domestic owners (2005, 7). Moreover, in Slovenia, as in other countries, participation of foreign investors in the production of export products is very high (Radosevic et al. 2003, 66). In Hungary for example, 70% of all exports are produced by partly or fully foreign owned companies (ITDH, Foreign Trade). On average the level in the region is even at 80% (United Nations 2002, 288). As exporters in Slovenia show the highest level of job creation, FDI seems to have positive effects on employment in this region. As exporters do not rely on local market purchasing capacities, they may occupy further shares of labor without reaching any limits in local selling. This causation is also supported by Radosevic et al., stating that in the third stage of transition, foreign investors increasingly invest for export purposes into labor intensive activities (2003, 63). As these investments occur in addition to market-seeking activities, usually during the second stage of transition, according to Radoseciv et al. they support a change from substitutive investments towards complementary investments in terms of employment (2003, 73). Moreover, the time horizon for investments increases at this stage which raises employment and employment stability. As foreign investors furthermore increasingly build up networks with local suppliers, as reported in their study, domestic linkages contribute to employment developments in local firms as well (2003, 73). Exporters, however,

become only more frequently involved into investments in later stages of the transition period. Therefore, the strongest effects are observable in the end of the second and in the third phase.

For most transition countries of the region, the role of FDI for employment has only become more important since the mid-1990s (Radosevic et al. 2003, 54). Large scale layoffs during the first period of change surely contributed to this fact. Privatization required huge cut backs in many firms which were overcome by the mid-1990s. In Poland for example 40,000 workers lost their jobs in the privatization of the national fixed-line provider TPSA, being bought by France Telecom (Lewis 2005, 52). For a number of years the communist job level was often maintained, due to arrangements with governments. This was only possible as wage levels in Central Europe were very low, like 16,766 Forint in Hungary in 1992 (Becskeházi and McDonald 1992, 105). Even now, in 2009, Hungarian average gross income of €712 competes with a German equivalent of €3176 (AHK 2010, 86). But despite this huge difference in labor costs and even after some years of restructuring and increasing productivity, many companies could not maintain the original number of employees. As Jurajda and Terrell explain, the initial phase of transition simply underwent such a deep transitional recession as well as huge reallocation processes of capital and labor, that employment numbers could not be maintained during a certain period (2006,2). The United Nations, however, state in their world investment report from 1999, that a short term loss of employment may be more than offset by long term gains, if FDI raises the competitiveness, efficiency and export-orientation of domestic firms (United Nations 1999). With this statement, it supports the theory of creative

destruction. Many losses of jobs were thus a necessary means for future economic development and competitiveness.

An analysis of the employment structures in several Central European countries provides further information on the impact of FDI on employment. From 1993 till 1999 employment in manufacturing in Poland and the Czech Republic declined, while employment in foreign affiliates increased during the same period (Radosevic et al. 2003, 77). Slovakia also, in the period from 1993-1996 showed a very strong domination of overall employment decline and foreign company employment rise in almost all industries (Radosevic et al. 2003, 78). This kind of data is a sign for significant restructuring processes after privatization. The job creation of foreign investors, however, is not strong enough to outweigh the losses. The majority of jobs created by foreign investors are likely to result from the acquisition of domestic companies. Thus, job structures do not actually change. In Hungary in contrast, net employment as well as employment in foreign affiliates increased during this period (Radosevic et al. 2003, 76). The prospects of employment development are thus very good. The different development of Hungary might be due to its advanced development in the transition process. Hungary, in 2001 had reached a share of 45.2% of employment in foreign affiliates, but seems to be stagnating on this level (Hunya and Geishecker 2005, 8). While Slovakia with 36.4% of employment share in foreign affiliates lies clearly below the Hungarian level, its numbers are still rising year by year (Hunya and Geishecker 2005, 8). Slovakia accordingly, as one of the late movers in the attraction of FDI might increase employment in foreign affiliates in the years to come and thus catch up with the Hungarian development at a far later stage.

As several studies on the region show, a first stage of transition and FDI attraction undergoes significant restructuring processes and is thus characterized by creative destruction. The outcome is thus difficult to assess especially as aggregated data might only show negative effects. Labor intensive investments at later stages of transition promote employment much stronger and turn creative destruction into a positive outcome, as it becomes visible through the examination of the different developments over time of Hungary and Slovakia.

2.2 FDI Effects on Human Capital

While the immediate benefit of FDI attraction was expected to be a rise in employment, in the long-term perspective, governments justified their policies for the attraction of FDI with the expectation of positive spillover effects into the local economy and thus increased productivity. During the first stage of FDI attraction, politicians believed that multinationals investing in the region would raise productivity in newly established or acquired plants, namely in their own greenfield or brownfield investments. In the second stage, their investment was additionally regarded as a vehicle for knowledge transfer into the domestic market and thus supposed to also increase productivity of domestic firms. While technology, as a capital input with capacities for increasing productivity is an important aspect of overall enhancement of productivity, the spillover of skills is at the focus of expectations as human resources are a core long-term factor for productivity improvements.

In the initial phase of transition, former communist companies had little expertise in running an enterprise in an open market economy. The participation of multinationals

in the privatization process might thus have contributed significantly to knowledge and skill transfer into post-communist countries. In the privatization of firms, foreign investors had to conduct extensive restructuring in order to make companies competitive. Their imported management skills were of major importance for a fast adjustment of the company to the needs of the market (Radosevic 2003, 63). The local labor force could thus profit from the management expertise of their investors. Many companies, moreover, sent their leading staff members for several months to their headquarters in Western Europe for training purposes. McDonalds took its staff to Illinois, Kraft brought people to Switzerland and IBM and Johnson&Johnson provided their workers with trainings abroad (Lewis 2005, 62). In other cases trainers came to the region to train personnel at sight. With the intention of breaking with old structures and transforming acquired affiliates into efficient production units as fast as possible, investors were ready to devote huge amounts of resources to the development of human capital. As a result, productivity improvements through the involvement of FDI led foreign affiliates to higher levels of productivity in comparison to domestic firms as Radosevic et al. conclude (2003, 58). Greenfield investments operated similarly, though without the struggle of restructuring. Nevertheless, these investments too implied extensive training and commitment to human capital development.

The first wave of investment took place under high levels of insecurity due to political instability and uncertainty in terms of market developments, which might have negatively affected investors' willingness for investment in a long-term perspective. Only in the third phase, did investment become more long-term oriented and is thus likely to have put more emphasis on developing human capital. Moreover, investment

at a later stage was much more focused on labor intensive activities, for which special training of staff can significantly improve productivity. This view is supported by Tytell and Yudayeva who find that export-oriented firms, for which investments are usually made at a later stage only, are more likely to create positive spillovers for the domestic market (2005,4). They explain that export-oriented firms have better technological equipment than market seeking firms (2005,4). Another field of high spillovers is R&D which was also only invested in at later stages of FDI attraction (Konings 2001, 621). In general specialized, vertical investments are likely to be more knowledge intensive and therefore have a higher probability for spillovers. Moreover, the knowledge gap at the beginning of transition was much bigger, which made returns to investment into human capital more profitable. Therefore, few days of training contributed already significantly to increased productivity (Lewis 2005). With the changes of FDI structure, therefore also the structure of skills changed significantly and thus the kind and extent of training.

The measurements of spillovers of skills are very hard to make. According to Radosevic et al. a rise of national productivity might solely refer to increased productivity in foreign owned firms, but does not prove any spillover effects to domestic companies (2003, 58). In his study, Konings therefore used a firm-based panel to analyse spillover effects in Romania and Bulgaria, as two of the less advanced countries in terms of FDI attraction and Poland as one of the more advanced countries in the period between 1993 and 1997 (2001). In Bulgaria and Romania Konings did not find foreign owned companies ahead of domestic companies in terms of productivity which he explains by ongoing restructuring efforts (2001, 627). Moreover, many foreign investors agreed with the government to

maintain jobs for a number of years below their actual maximum level of productivity. These restrictions might well have effects on such a comparison. This, however, does not mean that there are no spillover effects. For Poland, Konings simultaneously finds that foreign owned companies are significantly more productive than domestic firms (2001, 630). This means that knowledge spillovers may show their effects only once the initial phase of restructuring is lived through.

Concerning spillover effects between foreign owned and domestic firms, Konings finds significant negative effects in Romania and Bulgaria (2001, 628). Thus, a competition effect seems to be dominating positive spillover effects. Konings explains that this means, that domestic firms face decreasing market power for selling their products and while producing less, are pushed up their average cost curve (2001, 628). This interpretation, however, assumes increasing returns to scale. However, he also found, that in Poland which is at a much further stage of transition, foreign companies show higher productivity than domestic firms (2001, 630). From this he concludes that foreign firms in Poland have superior knowledge for higher efficiency (2001, 631). But for successful spillover, the technology gap between companies may not be too large and a certain threshold of human capital needs to be present (Konings 2001, 622). Moreover, Konings adds, that the degree of transfer of knowledge and skills also depends on the absorptive capacities of domestic firms (2001, 621). As education in most of the transition countries was already initially at a high level, according to Tytell and Yudayeva, sufficient capacities for the absorption of skills and knowledge could be expected by foreign investors (2005, 3). According to their study, corruption is a further factor to diminish capacities for absorption (2005, 4). In the initial phase of FDI attraction, like in Bulgaria and Romania,

domestic firms can thus hardly benefit in terms of spillovers, while Poland had a much more advantageous institutional background. Only over time, is knowledge transmitted through job migration or the increased build up of supplier networks.

Even though spillovers of knowledge within a firm are not perceivable in the beginning of FDI attraction, they might have contributed significantly to the restructuring process of privatized firms. Due to a huge knowledge gap, despite the presence of a well trained labor force, returns to investment were very high and little training could produce considerable spillover effects. At a later stage of foreign investment, incentives for investment into human capital might rise with specialization on knowledge and labor intensive activities. Moreover, investment structures might support spillover effects to domestic companies. But these tendencies will only be possible to be analyzed in future research, once the process of FDI attraction developed further. Nevertheless, training on knowledge intensive activities, the rise of networks and job changes are likely to promote spillover effects into domestic firms.

2.3 Trade Union Development

Trade unions in Central Europe are still far weaker than in Western Europe and could not gain any institutional strength during the last years, despite their integration into global markets (Neumann 2005, 63). Even though labor protection during communism was very strong, independent labor organizations as part of civil society grew only slowly in post-communist countries. Density is low and industrial action unusual (Keune 2004, 670). As foreign investors entered the market, some institutional spillovers might be expected. At the same time, some authors, like Woolfson and Beck, claim that governments significantly reduce the power of trade

unions for reasons of competitive advantages in the attraction of FDI (2002). The path of development of trade union power in the region is in deed a very distinct one of which the role of FDI will be analysed in the following section.

Working conditions in Central Europe were very dissimilar to Western Europe after the decline of communism. Circumstances which multinational companies found while expanding eastwards required both improvement by investors and adaptation from workers and governments. Often health and safety conditions were not very high and wages were not paid at the end of the month (Lewis 2005, 45). Some companies even continued paying salaries in the product produced by the company (Aslund 2007, 93). In these aspects, foreign investors themselves brought about quick improvements, while former working practices remained much longer in domestically owned companies (Lewis 2005). Moreover, workers in the early transition period, and often even still now, associate multinationals with higher wages, better working conditions and trainings (Kubicek 2004, 61). Many multinationals like in Hungary even voluntarily paid 10%-75% more than the usual salary, as Becskeházi and McDonald report (1992, 105). This payment, however, was often linked to the request that workers would not have any other jobs beside. Even though multinational companies brought manifold working improvements into the region these benefits did not have any effects on the institutional development of trade unions (Kubicek 2004, 61). While these informal practices brought benefits for some individuals, they did not strengthen labor organizations as part of civil society.

Despite these benefits, workers also had to adapt to unpleasant changes, like the reduction of job security. Large scale layoffs in privatized companies made workers

worry. At the same time, multinational companies had to fight other remaining practices from communist times. Rates of absence for example were extremely high. Lewis reports that in the region around 5% of workers could constantly be expected to be absent because of illness (2005, 59). He points out that in the Czech Republic a worker in the mid-1990 would take off 25 days a year on average because of sickness (2005, 59). As doctors were receptive for bribes, according to Lewis foreign investors responded by introducing positive incentives as the only solution to achieve behavioural change (2005). Similarly, he adds, alcoholism, theft and sexual harassment were common problems for which multinational companies even found little support in the legal system (2005).

Trade unions recently started to interact on a much more global scale, with social movements based on reciprocal support (Keune 2004, 671). Many organizations like the European Trade Union Confederation or the European Works Council reached the region, from which positive effects were expected. The establishment of a European Social Model, however, suffers from conflicting interests among different countries. Moreover, social regimes as well as institutional arrangements vary substantially (Keune 2004, 668). Western European trade unions are highly concerned about the delocalisation of jobs to Central and Eastern Europe (Keune 2004, 669). In Central Europe in contrast, the maintenance of labor protection as a priority over the attraction of capital is of major concern. Weak trade unions in addition to low wages and high levels of productivity are major factors of attraction for foreign capital (Keune 2004, 669). As countries of Central Europe are equipped with strong incentives for FDI, Western European countries fear not to be competitive any longer. Meanwhile Central European countries struggle for higher social standards

and wages (Keune 2004, 669). This produces a significant divide of interests throughout Europe which has strong inhibitive effects for reciprocal support. Support from Western European civil society through the networks of multinational companies for the development of trade unions in Central Europe is therefore unlikely.

While labor protection, as part of the communist heritage, was very high at the beginning of FDI attraction, market liberalization required also adaptation of labor rights. Governments in countries like Hungary introduced liberalizing labor reforms early after the fall of communism in 1992 (Illessy et al. 2007, 102). Slovakia, however, only recently, in 2000, reformed its labor market towards more liberalization (Hunya and Geishecker 2005, 2). Trade unions of the former communist system meanwhile transformed into new institutions, like the MSZOSZ in Hungary and maintained their high numbers of membership (Illessy et al. 2007, 100-101). Additionally, even some new trade unions were established. But this level of labor protection was not maintained for long. In all Central European countries trade union density dramatically declined. In Hungary density decreased from 63.4% in 1995 to 19.9% in 2002 and in Slovakia from 78.7% in 1990 to 35.4% in 2002 (Illessy et al. 2007, 101). Only Slovenia represents an exception with a considerably high level of 41% in 2002 (Illessy et al. 2007, 101). Moreover, Illessy et al. state, that membership in Hungary, Poland and Slovakia is mainly accumulated in the public sector because of institutional heritage (2007, 101). This means that among private companies the level of membership must be expected even far lower. In fact, as Dimitrova and Petkov report, trade unions in Hungary have no strong presence in private and multinational enterprises (2005, 42). Thus, even though Central Europe became part of the global market when multinational companies directed investments into the

region, the region's global participation in civil society labor protection could not be achieved.

Weakening policies towards trade unions are often claimed to purely feed the interests of foreign investors (Keune 2004; Woolfson and Beck 2002). In the beginning of FDI attraction, foreign investors, however, held a very positive attitude towards trade unions (Lewis 2005, 51). Yet, over time, this attitude significantly changed. Indeed, some multinational companies which reached the region at a later stage, tried to put special pressure on their employees. According to Lewis, a German company in the Czech Republic for example paid its employees an extra $16 a month if they agreed on leaving the trade union (2005, 55). Through such incentives, trade unions were often systematically excluded from the organization. As this was rather a phenomenon at later stages of FDI attraction, it might be a reaction to increased competition. At the third stage of FDI attraction, increasing investments into export-oriented activities faced strong needs for specialization and competitiveness. As Kubicek states, these activities go along with cuts in wages, benefits and subsidies for labor in order to reach enhanced market flexibility for competitiveness (2004, 60). He adds, that also on a global scale, trends of globalization expose companies to a stronger need of productivity and efficiency which adds to a decline of the former role of trade unions (2004, 60). Nevertheless, other companies like Skoda still provide one of the best salaries and working conditions in the region, proving that fair business has not become impossible (Lewis 2005). As a result of both, diverging interests of trade unions within Europe as well as increased pressure through trends of globalization, the institutional weakness of trade unions in the region could not be cured until now.

Whether it concerns the development of employment, human capital or trade union power, the first stage of transition and FDI attraction was strongly influenced by fundamental restructuring processes. While full employment of communist times was followed by large scale layoffs, knowledge was quickly transferred through the channel of foreign investors and working conditions strongly improved, even without the support of trade unions. Thus, investments at the beginning made significant qualitative improvements but had negative effects on quantitative factors of employment. These effects, however, undergo deep changes throughout the process of FDI attraction which is especially visible in the comparison of Hungary and Slovakia, as they developed at different times in terms of FDI attraction but show similar tendencies. While foreign investment becomes progressively more beneficial for employment and spillover effects increasingly spread into local economy through the building of supplier networks and job migration, trade unions could only find little support for strengthening their position through their integration into international networks because of diverging interests. Increased competition, as well as large lobbying power of multinational companies pushes governments towards labor market liberalization and limiting the power of trade unions. Striving for qualitative benefits is thus replaced by an emphasis on competitiveness and efficiency for the aim to regain full employment.

3. Policy Implications for Labor Market Development

The hope of politicians for accelerated development in Central European countries through the attraction of FDI was and still is high. What is described as a “race to the bottom” (Woolfson and Beck 2002, 754; Jensen 2006, 889) by several scholars, is the governmental policy reaction to compete with other countries’ incentives for the attraction of FDI. Numerous studies analyse the incentive priorities of multinationals’ investment decisions and find that besides tax incentives labor market aspects are of great importance. Several scholars find, that unit labor costs, as an indicator for both, wage level and labor productivity, are negatively correlated to location decisions of foreign investors (Bevan and Estrin 2004, 783; Disdier and Mayer 2004; Janicki and Wunnava 2004). Bevan and Estrin further explain that investors are strongly concerned about their operation costs for which labor is a central factor, especially at later stages of the FDI attraction due to concentration in labor intensive activities (2004, 738). Thus, labor costs as well as labor productivity are primarily important for companies seeking for the establishment of production sites abroad (Bevan et al. 2004, 55).

The reaction of governments, however, is difficult to analyse, as only few policies respond directly to these needs of multinationals and only are rarely explicitly related to the attraction of FDI. Nevertheless, governments are well aware of the main incentives for FDI attraction as agencies like the Slovak Investment and Trade Development Agency SARIO or the Hungarian equivalent ITDH offers information on their country with extensive data on labor market benefits. Slovakia for example presents its labor costs as well as labor productivity in comparison to other countries

of the region in a special booklet (SARIO Labor Market, 5; 7). Moreover, SARIO gives detailed information on the education level of its population (SARIO Labor Market, 9). ITDH similarly publishes information on its human capital and labor market with precise information on the costs that foreign investors have to expect for employment (ITDH Business Environment). Even though some authors, like Woolfson and Beck argue that many reforms of market liberation were made in regard to the attraction of foreign investments, it is not possible to deduce any causation (2002). However, the fact that governments advertise themselves with such incentives means that they are well aware of their impact.

Clearly, however, conclusions can be drawn on government intensions from policies made explicitly for the attraction of FDI. These usually encompass incentive packages for large scale investments which also imply certain conditions on location, employment and time perspectives. Governments often sign contracts with large multinationals which include agreements on the maintenance of employment numbers over a specified period of time in return of numerous tax incentives (Radosevic et al. 2003, 55). In Hungary the ITDH provides information on such incentive packages (ITDH, Investment Incentives). Greenfield investments over €10 million may obtain direct subsidies, job creation subsidies, training subsidies as well as tax allowances (ITDH, Investment Incentives). An 80% tax exemption is available for ten years (ITDH, Investment Incentives). Further incentives are available for the creation of large scale research and development facilities (ITDH, Investment Incentives). In Slovakia, SARIO offers similar incentives like grands, tax reliefs, sub subsidies and discounts on the acquisition of property of land (SARIO, Invest in Slovakia). While these benefits are not specified, conditions are clearly formulated.

Investors in industry must spend 40% of their investment on new machinery and have a certain education structure in their affiliates (SARIO, Invest in Slovakia). In comparison to Hungary, Slovakia makes a more detailed regional differentiation for investment incentives based on three categories, ranging from a minimum investment volume of €3.31 million to a minimum of €13.27 million (SARIO, Invest in Slovakia). Slovakia thus has a much lower threshold for investment incentives than Hungary. Moreover, Slovakia as a result puts more emphasis on support for the initial setup of investments while Hungary focuses on establishing agreements over a certain period of time. In addition to its fiscal incentives, SARIO offers assistance on the establishment of contacts to local suppliers, the handling of foreign citizens' issues, investment consultancy and supports co-operations with schools (SARIO, Why Invest in Slovakia). With these incentives, Hungary as well as Slovakia feed a number of needs of foreign investors. In the following the three core factors of the labor market will be analysed in relation to these policies. Moreover, policy options for countries of Central Europe will be discussed.

3.1 Policies for Employment

With the implementation of incentive packages governments practically subsidize large scale job maintenance. Moreover, these kinds of agreements support single firms to gain market power, first because such incentive packages are usually exclusively for large scale investments and do not promote entrepreneurship and second, because they provide a competitive advantage through cost reduction in terms of fiscal incentives. However, Bruckner (in Mickievicz et al. 2000, 10) in his research on investments in Eastern Germany showed that these kinds of arrangements are largely insufficient.

One argument against incentive packages is that large scale layoffs in the privatization process were only postponed but not avoided. Through the indirect subvention of jobs in terms of tax holidays, companies can afford to maintain and create jobs above their actual level of efficiency. But as soon as the agreement comes to its end, large numbers of employees are laid off. Such contracts thus only shift unemployment into the future. In the case of privatization, such contracts, however, might reduce fluctuation on the labor market as those employees who are employed over capacities in the initial phase of company transformation are not laid off and reemployed at a later stage, when the company runs more efficiently. In the case of Greenfield investment, companies might start to employ earlier the number of employees which they will employ after a certain period of growth. In both cases, such governmental agreements prevent unemployment for a certain period of time and thus prevent a shock of unemployment on the labor market in the initial phase of transition, which is a very important factor for political stability and societal cohesion. Thus, not for economic development but for social reasons such contracts in the initial phase might be of importance. While these labor market policies thus had some micro results, they, however, could not solve long-term problems (Mickevicz et al. 2000, 10). In the long run, such policies are even likely to be misused by politicians to artificially reduce unemployment during their legislation period and thus to increase chances for re-election.

Apart from subsidies it is difficult to take influence on labor costs. Only through the influence on exchange rates, governments could artificially keep labor costs low for foreign investors. But risks for inflation produce a considerable negative effect. Labor

productivity, however, is strongly dependant on the population's education level which lies among the responsibilities of governments. By investing into vocational training, and higher education, governments may increase labor productivity and thus raise the attractiveness of their country for foreign investment which would then have positive effects on employment.

Thus, in an initial phase of FDI attraction governments may create direct incentives for foreign investors to maintain high levels of employment and thus prevent social unrest. At a later stage of FDI attraction, when investments become more labor intensive and knowledge specific, only overall education improvements may have positive effects on employment through the attraction of FDI.

3.2 Policies for Human Capital Development

Even though agreements on job maintenance in foreign affiliates do not solve long-term unemployment problems, they might have positive effects on spillovers. Workers in foreign affiliates profit from trainings and knowledge transfer from abroad. Those who become victims of large scale layoffs might spread knowledge into domestic firms through new job acquisition. This channel of knowledge transfer worked especially well in the initial phase of FDI attraction, as at this time, returns to investment for trainings were particularly high. Thus, foreign investors did not hesitate to supply large scale investments. At a later stage of FDI attraction, when privatization is already completed, it is questionable, however, if a company would still invest into staff, of which it knows that it will not remain in the company for long.

As we have seen in the previous chapter, absorptive capacities are an important factor for successful spillovers into the host economy. One measure to increase absorptive capacities is by raising the level of education. According to Blomström et al., employees are then not only more capable to absorb new knowledge, but foreign companies are also more likely to invest into knowledge intensive activities and to import more technology (2000, 204-205). They explain that through such measures transfer costs are reduced for further import of technologies (2000, 214). All countries of Central Europe started into transition with a reasonably well educated labor force. While Slovakia, like most Central European countries is since constantly increasing the number of tertiary education graduates, Hungary seems to stagnate around a graduation rate of 30% of a year of age (OECD Country Statistics). While these numbers do not reveal any information on the quality of education, in quantitative terms, Slovakia seems to be better adapting to the needs for successful spillovers. Moreover, the offer of consultancy in regard to the search for local suppliers and joint-ventures, as well as co-operations with schools, might further contribute to the establishment of channels for the transfer of knowledge into the domestic economy.

Another factor for spillover effects, emphasized by Blomström et al. is competition (2000). As they state, only if foreign companies are exposed to competition, will they feel the need to import advanced technology from their parent company in order to maintain competitiveness (2000, 204). For market seeking investments this implies that governments should also encourage local investment according to Blomström et al., as well as entrepreneurship (2000, 217). Only if local economy has a certain strength foreign investors will have to bring in advanced knowledge or technology for increased competitiveness. For export purposes, governments, however, cannot

promote global competition. But by competing for large scale investments and therefore providing foreign investors with strong location incentives, governments tend to increase market power of single firms, and thus decrease competitiveness. Generous incentive packages, such as Hungary and Slovakia offer them, might thus inhibit spillover effects.

Spillover effects at an early stage of FDI attraction can thus be supported by subsidising jobs for several years of maintenance. As market seeking activities are prevailing at this stage, it might also raise benefits to increase competition by supporting local investments. At a later stage, however, job subsidies turn into a pure shift of unemployment into the future and generous incentive packages might even reduce multinationals' incentives for the import of high technology. Instead, governmental investment into education can reduce the technology gap and increase absorptive capacities for enhanced spillover effects.

3.3 Policies for Trade Union Strengthening

Trade unions seem to be in a trap. Aguilera and Dabu describe this situation by stating that on the one hand multinationals at a majority offer over average wages and benefits, high above what collective bargaining achieves in domestic industries (2005, 34). But on the other, they add that many multinationals seem to take a depreciative position towards trade unions (2005, 31). As many foreign investors exercise huge financial power, they can put governments under great pressure for keeping the influence of trade unions low (Kubicek 2004, 61). Governments, moreover show increasing tendencies to liberalize their labor markets which some authors like Woolfson and Beck interpret as an effort for competitive advantage

(2002). The result is that on the firm level, labor conditions might be significantly improved but no institutional power for the protection of labor rights is established.

Only Slovenia seems to be an exception in these region-wide trends. Meardi et al. note that especially in comparison to Hungary and Poland, Slovenia has a very strong institutionalised labor representation through trade unions (2009, 41). Its development, however, is not rooted in international linkages, but in the domestic industry. According to Meardi et al. trade unions show even lower activity in multinationals than the domestic industry (2009, 41). The government has thus achieved to set the conditions for the institutional strengthening of workers' rights but seems to face similar challenges in multinationals as other countries of the region.

While labor market liberalization and the prevention of trade union development might improve the country's attractiveness for FDI inflows, it might also inhibit a positive development of working conditions and workers' rights. Governments will have to take a clear position in how far they put their policy priority on quantitative or qualitative improvements on the labor market.

In policy making for the development of labor markets, governments face challenges to combine benefits for all aspects of the labor market. However, in the initial phase of FDI attraction, subsidising the maintenance of jobs for a number of years may have positive effects both on unemployment reduction for the prevention of an unemployment shock in society as well as for spillover effects through later job migration. But the support of local investments which may increase spillover effects might simultaneously inhibit the investment of foreign and probably more efficient

companies. Governments have to find a compromise in this respect between the promotion of spillovers or job creation and thus between short-term and long-term solutions for development. At a later stage of FDI attraction, competition rises and investments focus on more labor intensive activities. This means that spillovers have better conditions if a certain educational level is present. For trade unions, increased competition for multinationals, however, impairs the chances for achieving institutional strength. For long-term development and benefits on the labor market, nonetheless, it might be important to support the establishment of an institutionalized representation of labor and thus, to form a counterbalance to the financial power of multinationals.

Conclusion

Hungary and Slovakia, as all other countries of Central Europe have experienced significant societal and economic changes in response to their efforts of attracting FDI. These responses in regard to labor market developments changed significantly over time, as the present study shows. But further details must be revealed.

As assumed in the introduction, greenfield investments and participation of foreign investors in the privatization process bring benefits of higher efficiency and thus also of higher job maintenance. However, the process of creative destruction only after a while produces positive data, since company restructuring and market transformation exposes labor markets to turbulent reformation. With an increased governmental investment into education, a shift of investments into more labor intensive activities can be anticipated to contribute to an increase of employment. Export-orientation of foreign affiliates further expands possibilities for sale on the global market and does not limit retail on the purchasing power of domestic markets. Thus, governments have clear options for the promotion of FDI inflows for a healthy labor market development. Even though, incentive packages, including agreements on job maintenance, do not seem beneficial at later stages of FDI attraction, they might well contribute to the prevention of shocks on the labor market during intensive processes of company or market transformation.

For spillover effects trainings, job migration and supplier networks turn out to be the core channels of transfer. Trainings face the problem of decreasing returns to investment over time, as the knowledge gap within firms was a lot larger at the

beginning of transition and few efforts could significantly improve productivity. Even though trends show a turn of investment towards more knowledge intensive activities, risks for decreasing efforts on training exists because of increasing costs. Governments thus have to invest into education in order to make sure that absorptive capacities on the labor market are high. Spillovers into domestic industries are similarly dependant on the present degree of absorptive capacities, as they are transferred through supplier networks or job migration. As these two factors increasingly appear over time, economies have promising perspectives for spillovers into local firms.

Trade unions might not show any strong development over time. While numbers of membership were still high at the beginning of transition and decrease further and further, institutional protection of labor rights did not develop at any point. However, while the attitude of foreign investors towards trade unions was very positive in the beginning and working conditions were extremely good in comparison to the situation in domestic firms, these factors are in transformation. Foreign investors use their financial power on governments for the prevention of trade union's strengthening and benefits in foreign affiliates are no longer significantly higher than in domestic firms. For the protection of labor rights, governments thus have to make clear efforts.

According to the findings, governments have clearly changing challenges over time and moreover might need to adopt their policy priorities. While the prevention of sudden and high unemployment during privatization processes and economic transformation was a necessary policy goal in order to prevent a societal collapse,

long-term developments require a stronger focus on policies for the promotion of spillovers.

As Hungary is among the most advanced countries of the region in terms of FDI attraction, it should be mostly concerned about reducing dependencies, and encouraging spillovers into the local economy. Especially in the promotion of education, Hungary seems to have potential for improvement. Policy attempts for the increase of employment through FDI attraction at this stage only seem to feed politicians' purpose for popularity especially in regard to high unemployment. In real terms, subsidies for jobs in foreign affiliates over a certain period of time might only postpone unemployment, as deep transformation processes are already completed.

Even though Slovakia is by far not at the same point as Hungary, needs for the promotion of spillovers also apply for this country already. As Slovakia, though, only just started to actively attract FDI, a focus may lie on the promotion of spillovers within foreign affiliates. However, Slovakia seems to be prepared to benefit from some of the mechanisms explained in this study and thus to take a slightly different path of development than its neighbour Hungary.

Not only for Hungary and Slovakia it is important to understand relations between FDI inflows and labor market effects for policy making. As all other countries of the region undergo similar processes and experience similar trends in the structural development of FDI, similar conclusions on policy choices might be deduced for these countries. Moreover, countries of Eastern Europe become increasingly targeted by FDI and might therefore experience a similar path of development.

For Central Europe, however, this means that Eastern European countries are likely to become more and more competitive in the attraction of FDI, which could imply a relocation of investments further eastwards. In this regard, the promotion of spillover effects might become a policy priority, as this is the most crucial factor for sustainable economic and thus also labor market development. Even though tendencies of this development are already perceivable, further research on the reasons and consequences of these trends might contribute to the creation of best policy practices, based on conclusions drawn on Central European developments. Even though, it is impossible to predict the future, policy makers may learn from the analysis of developments in another place and time, such as Slovakia seems to have learned for the development of FDI attraction of its neighbours.

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