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Author:

Marta Götz

Editorial Board:

Marta Götz

Radosław Grodzki

Krzysztof Malinowski

Polish Foreign Investment – State Aid?

Highly desirable in view of the very limited extent of Poland's foreign direct investment and justified by the fact that other countries engage in similar support practices, state aid for the foreign expansion of Polish enterprises could help intensify industrial policy on the one hand and enhance the so called public diplomacy on the other. Such state aid might, as its consequence, offer an unintended added value of "reverse economic diplomacy" promoting the country of Poland abroad through businesses which succeed in conquering foreign markets.

Support for internationalization and industrial policy

In principle, goods and production factors should be allocated by market forces while the state should only resort to regulation when necessary to streamline market mechanisms so as to compensate for imperfect competition in real-life markets. The market and the state are therefore complementary cooperation mechanisms which suffer from certain faults (and are susceptible to failure). Industrial policy may be defined as governments undertaking measures to produce economic effects that differ from those expected in a scenario devoid of interference into the operation of market mechanisms. Such tools do not have to and, as a matter of principle, should not be limited to a specific sector. Rather, they should horizontally extend across multiple industries to prevent any discrimination. Defined in such a way, industrial policy may also be seen in a broader sense which includes measures taken to promote domestic enterprises abroad and thus support domestic businesses in their international expansion.

At a time of crisis and in the face of intense efforts undertaken in many economies, mainly emerging markets such as China, to support local business, opposition to a “wise” industrial policy of the European Union (EU) continues to dwindle. Poland too grows increasingly more aware of the need for a new industrial policy which would be “strategically-oriented (...) and designed to support the competitiveness of companies rather than focusing on the protection of the domestic economy (...) with emphasis on sectors whose exports provide a high added value” (J. Hausner Report). Such a new policy should support entrepreneurship and competitiveness. Meanwhile, a strong comeback is seen of economic diplomacy defined as the use of the political influence of individual states to promote domestic business interests internationally. “In an environment characterized by tight competition for market share and the central role of the state in promoting the businesses of emerging economies, there is an unquestionable need for support by the Polish government in many areas extending well beyond the current promotional and advisory efforts” (DemosEuropa).

Aid for enterprises seeking to expand abroad, i.e. support for international expansion of domestic businesses, appears to be an excellent example of industrial policy improvement. While industrial policy in the past was aimed at providing special care to foreign capital and offer an array of incentives to attract incoming investors expected to further the country’s modernization, Poland’s interest today is to back firms which seek to expand abroad (i.e. support foreign direct investment). It is essential to ensure that such a policy does not express nationalist sentiments or distorted economic patriotism or become a way to resolve day-to-day problems but rather paves the way for the country’s long-term growth.

The issue of state aid for foreign expansion has been raised in literature in connection with the so called national champions. Their emergence and support for their development seem to be part of a consolidation trend which results naturally from continued globalization and tightening competition and is consistent with a business model pursued by the EU. Three arguments can be named in favor of interventions by public authorities in the active pursuance of industrial policy and in support of such national champions. These include security and, specifically, an effort to reduce dependence on foreign supplies, the existence of industries of strategic importance for the economy which create jobs and add substantial value and the so called strategic trade policy calling for interference in sectors with considerable barriers to entry and strong externalities, including economies of scale.

Prior experience, as described in the literature, is insufficient to unambiguously assess the outcomes of an industrial policy designed to establish such national champions and indirectly further foreign expansion. The available scholarly literature still needs to fully



recognize all detailed workings of policies for promoting the foreign investment of domestic companies, i.e. their instruments, the adopted methods of enterprise selection and effectiveness assessment. Research findings so far have focused on differences between industry sectors as a key factor for determining whether investments abroad are complimentary or substitutive to national projects. Even studies on emerging economies emphasize marked differences across such economies which require individual countries to become highly specialized and modify their foreign promotional measures to the capacities of the national economy. It is difficult, therefore, to identify a single model policy for supporting outgoing FDI and find the most optimal solution for promoting domestic firms abroad through tax incentives and by backing national champions.

In the past, as markets worldwide performed excellently, Western European and US enterprises pursued their FDI in a whole different manner. Host countries, such as Poland, sought to attract them as a source of knowledge or capital or an opportunity to modernize the country and create jobs. Today, early in the second decade of the 21st century, Polish companies are faced with a very different environment. Their FDI in Western Europe needs to live up to a whole new set of challenges. Such companies rarely receive subsidies, requirement waivers, tax exemptions and incentives to invest. No wonder that many of them call upon their home country to extend more aid and actively support their expansion efforts. Theoretically, they are free to operate in the open European Union with no internal national borders which is regulated but non-discriminating and offers unrestricted access to nearly all markets. However, support from Polish administration is often crucial to enable the companies to take practical advantage of opportunities afforded to them by the common EU market. According to investors: “the promotion of (but not ‘support for’) domestic enterprises is as old as economy itself and is set to stay around for as long as national governments exist”.

The EU legislation (adopted partly within the framework of the four freedoms) has opened up a host of new opportunities for Polish businesses. The existing Community policies have altered the expansion environment (perhaps becoming an impediment). This has forced domestic companies to adjust quickly to new conditions and requirements and catch up with more developed economies. It seems legitimate therefore that state aid be extended to the businesses of less developed countries. Traditionally, investing states experiencing favorable economic cycles and many transitional economies of Central and Eastern Europe (as well as some other states receiving FDI) have used elaborate incentives to channel investment into their most attractive locations. Host countries vied for foreign capital by offering a number of benefits.



Today's unstable economies of the crisis or post-crisis era make foreign expansion into any place in the world very difficult for our region's businesses. The EU market, the access to which should theoretically be unrestricted, is only open to those who satisfy numerous criteria. Troubled West European economies resort ever more shamelessly to economic patriotism or downright protectionism. Industrial policy has become a frequent weapon of war used to overcome (post)crisis challenges. Faced with such an environment, Poland too should seek to make the lives of its firms easier by, among other things, fostering their foreign expansion. Particularly at this time of poor economic performance, interference by public authorities seems to have become an integral part of the game. The global environment appears to have fashioned an exceptional framework for the pursuit of FDI by Polish enterprises.

The available publications on investment coming from Central and Eastern Europe, including Poland, and the option of state aid, focus on the state-ownership of expanding companies. Most investment coming from the Czech Republic and Hungary is made by foreign investors who already operate in those countries. In Slovenia, decisions to expand abroad are made by domestic companies aspiring to turn multinational. Investments originating in Poland, on the other hand, typically come from large operations which are partially state-owned and stem from such strategic sectors as the fuel industry. Meanwhile, Poland is listed next to Estonia, Croatia, Hungary, the Czech Republic, Slovakia and Slovenia, as one of the "seven dwarves" whose investments are distinguished from those of the Russian Federation by the limited state involvement in persuading local businesses to pursue FDI.

Support for internationalization – the Polish experience

The need for quick and targeted economic policy action to promote FDI has been noted for years. Due to the rapid pace of globalization and the extent of economic transformations taking place all around the world, businesses in long-neglected transitional economies cannot afford to restore their potential and develop competitive advantages in a slow and gradual manner. Hence it is only natural that a certain degree of state aid is in order. It is essential, however, that states intervene in an "enlightened" fashion and refrain from manually controlling their economies. Such interference in the case of Poland is justified by the fact that, upon its accession to the European Union, the country abandoned a number of instruments previously available to other states which had allowed them to create national champions capable of competing abroad. The companies which succeed in entering and growing in new markets will be vital for Poland's standing on the economic map of the



world in the 21st century. However, as chances of Polish businesses growing globally without proper support are fairly slim, Poland remains at risk of being marginalized. On the other hand, the recession experienced in many foreign markets offers unique opportunities to expand, mainly by acquiring other operations. At times of good market performance, companies would be too expensive to be bought by Polish businesses which are usually limited in their means.

A report by the Institute for Market, Consumption and Business Cycles Research (IBRKK) and by Vale Columbia Center on Sustainable International Investment (VCC) distinguishes between three phases in the development of Poland's policy on outbound FDI. Phase One, which ended in 1989, was characterized by hostility towards capital movements and the use of barriers which would impede or block them. Phase Two, which continued for the two decades that followed, can be described as neutral. Subsequently, 2010 ushered in a period of active involvement by ministries and governmental agencies seeking to promote the international expansion of Polish companies.

The aid available to Polish companies which consider foreign expansion comprises four types of instruments: direct (subsidies towards the price of licenses, publications by the Ministry of Economy, export passports from the Polish Agency for Enterprise Development, etc.), indirect (international promotion of the Polish economy financed by EU funds), institutional support for the business environment (pursued through departments for promotion and trade at embassies as well as Investor and Exporter Support Centers) and financial instruments (guarantees, insurance, endorsements). The Polish government is still to formulate a comprehensive strategy for "going global". The Ministry of Economy and governmental agencies have launched programs aimed at supporting Polish investment abroad. What also deserves a mention is the "Go China" initiative unfolding on the heels of President Bronisław Komorowski's visit in that country (as well as the planned "Go Africa" initiative), a network of exporter and investor support centers set up in Poland's administrative regions and a systemic program covering 16 field branches placed in each region. The program, which envisions support for exporters and potential investors, complements prior direct assistance offered in the form of grants and loans.

The National Center for Research and Development has announced a competition as part of its pilot project Go_global.pl. Within this framework, support was offered for innovative companies which commercialize research findings and outcomes of development work in world markets. Examples of efforts eligible for such support include the development of a strategy for international expansion, formulation of business plans or development programs for innovative companies, analysis of international markets, including purchases of specialized market research reports, training and coaching in how to adjust to the legislative



and cultural demands of a given market, intellectual property management, preparation of bids for negotiation, identification of key customers and business partners, cooperation with foreign business advisors in developing innovative markets to establish business relations, fine-tuning of market strategies and preparation of market entry tactics, workshops for prospective financial investors, professional valuation of offerings by venture capital, and launches of cooperation in R&D or production.

An appealing form of support are initiatives by business and media organizations offered commonly in the form of dedicated programs and contests. Companies which successfully invest and increase their sales in foreign markets have been allowed to enter a prestigious contest “Polish Company – International Champion” organized by PricewaterhouseCoopers under the auspices of the *Rzeczpospolita* daily. The contest was open to businesses which had made foreign investments in the preceding five years (i.e. had established a service point or another business location or acquired a company), as well as those which successfully developed international sales. On the initiative of the ICAN Institute (the publisher of *Harvard Business Review Polska*) and KGHM, a Poland Go Global think tank was set up which commenced its activities with a conference in 2012. Its main purpose was to support the internationalization of Polish businesses by exchanging good practices and carrying out joint commercial projects. In more remote future, the think tank is to examine the international activities of Polish businesses, establish collaboration with organizations dealing with economic issues in Europe (associated in the Stockholm Network), hold regular conferences and maintain joint scholarly-business fora. Support for the international expansion of Polish enterprises comes also from Citi Bank Handlowy which, together with the *Puls Biznesu* daily, acts as partner in the “Time for Economic Patriots” program.

Experts in various fields point to the need for state support for the foreign expansion of Polish companies. Prior studies suggest that the majority of prospective investors have indeed expected such support from Polish state institutions. The assistance would mainly involve “establishing an investment-conducive environment by maintaining good political relations”, “offering state aid, i.e. direct financial support”, and “providing information on rules and requirements for investing in specific countries”. An interesting approach was adopted by the US-Poland innovation hub of Paulo Alto formed in the Silicon Valley which supports smaller but innovative and promising companies in networking and establishing partnerships with local businesses and ultimately moving into local markets. Envisioned as a contest, the project is to provide participating companies with hands-on instruction on how to act flexibly in pursuance with long-term strategies. Wrocław, in its turn, has set up a hall of fame to recognize internationally successful companies. The project is to provide enterprises which



have not yet accomplished such goals with the know-how they need to succeed. Its purpose is to help bring companies and research and development institutes together and modify local government training programs to meet their needs. Cities, which in the past focused on procuring foreign investment, have now gone a step further to promote internationally any local businesses that are critical for their region's long-term development. Time will show to what extent such efforts prove successful.

One possible form of institutional support for Polish businesses aspiring go global, which has been proposed by experts, could be to transform or expand the Polish Information and Foreign Investment Agency into e.g. an Agency for the Support of International Expansion. Thus far, policies, if any, to aid Polish companies in their international expansion, have been inconsistent and fairly ineffective. The ideas proposed by some ministries are decried by others. As coordination is lacking, programs promoted by certain ministries are likely to be duplicated by others while many crucial areas remain neglected and potential synergies wasted. Polish entrepreneurs, who expect the state to provide them with specific assistance in conquering foreign markets, note that:

- the Ministry of Foreign Affairs, the Ministry of Economy and the Polish Information and Foreign Investment Agency often duplicate their business promotional efforts;
- the authorities shy away from contacts with businesses – Polish businesses rarely take part in missions and foreign visits by Polish politicians;
- responsibilities are often ignored and neglected – the Poland Promotion Council only held three meetings in 2012;
- organizational neglect – Polish embassies do not provide translations of commercial codes from their countries of deployment, representation in African countries is insufficient.

A qualitative study of an unrepresentative sample of Polish companies operating in Western Europe shows that some of them speak clearly of the need for support by the Polish public authorities while others are either disinterested, neutral or even negative, seeing such help as being of little value, poorly matched to their needs or unnecessary.

We have no expectations of the state helping us in international expansion. While we do appreciate assistance in participating in international fairs, exhibitions and economic missions as well as the company matching effort, we do not anticipate practical support in any specific acquisitions due to the specific nature of our niche industry which requires specialized expertise.



Much remains to be done with respect to state aid. For one, the state should step up its efforts to promote Polish businesses abroad by, for instance, recognizing business interests during state visits, as practiced by other countries. This is of particular importance in view of certain hypocrisy seen among Western European countries which commonly succumb to economic patriotism.

Polish entrepreneurs have no single common universal model for cooperating with public administration to foster foreign expansion. While some businesses fear “excessive governmental interference”, others point to the need, which is particularly compelling in the (post-)crisis era of “interference and protectionism”, to create a competitive environment enabling Polish firms to expand abroad. Others yet expect top politicians to go as far as to follow the example of the authorities of many other European countries and proactively “lobby” for Polish investors. The negative assessments by some of the respondents in the state aid study may well have to do with the incompetence of the public administration and their own poor experience with state assistance. Such incompetence is likely to be the underlying reason for disapproval for state activities designed to support foreign ventures. While the findings are insufficient to formulate specific guidelines for decision-makers involved in furthering Polish FDI, they may well serve as a starting point for further work.

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Whereas many Polish companies have already established themselves on foreign markets, the scale of foreign investment falls short of Poland’s aspirations. Since, in the long run, internationalization is essential for the operation of businesses and foreign presence is a strategic necessity as it is crucial for long-term survival, the state cannot afford ignoring the needs of domestic companies which plan to go international. It is therefore difficult to overestimate the significance of properly designing and deploying a foreign investment policy. One might thus hypothesize that state aid for the international expansion of Polish businesses, which is desirable in view of the limited scale of FDI and justified by the fact that other countries engage in state aid practices, could become well aligned with industrial policy, which grows ever more popular, as well as public diplomacy efforts. It may, in effect, bear fruit in the form of a certain unintended “reverse economic diplomacy” by promoting Poland as a country through its businesses which succeed on international markets.



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Marta Götz – economist at the Institute for Western Affairs in Poznań; research interests: foreign direct investment, economic crisis, the economy of Germany.

