

# Determinants of Effects of Foreign Direct Investment in Terms of Slovak Republic and Wood-Processing Industry of Slovakia

## Odrednice učinkovitosti izravnih stranih ulaganja u uvjetima poslovanja Republike Slovačke i slovačke drvoprerađivačke industrije

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**ABSTRACT** • *The presence of foreign direct investment in certain sectors or country determines several factors - the determinants of foreign direct investment. The article analyzes the selected factors of FDI inflows to the Slovak Republic and to the wood-processing industry in SR; it focuses primarily on assessing the contemporary situation of the business environment in Slovakia and investment incentives provided to foreign investors. The article also presents the development of foreign direct investment in Slovakia, in the branch of wood processing, analyzing the effects of FDI in specific conditions of the Slovak Republic and wood-processing industry.*

**Key words:** *foreign direct investment (FDI), effects of FDI, business environment, investment incentives, wood-processing branch*

**SAŽETAK** • *Zastupljenost izravnih stranih ulaganja (FDI) u pojedinim sektorima ili državi određen je s nekoliko čimbenika – čimbenika izravnih stranih ulaganja. U članku se analiziraju određeni čimbenici FDI-a u Slovačkoj Republici i u drvoprerađivačkoj industriji Slovačke, pri čemu se autori primarno fokusiraju na pristup trenutačnoj situaciji u poslovnom okruženju u Slovačkoj i na ulagačke poticaje koje strani ulagači imaju. Članak također predočuje razvoj izravnih stranih ulaganja u Slovačku, u drvoprerađivačku djelatnost, analizirajući učinke FDI-a u specifičnim uvjetima u kojima se prerada drva u Slovačkoj nalazi.*

**Ključne riječi:** *izravna strana ulaganja (FDI), učinci FDI, poslovno okruženje, ulagački poticaji, drvoprerađivačka djelatnost*

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## 1 INTRODUCTION

### 1. UVOD

The inflow of foreign direct investments (FDI) into the country affects a number of factors described in literature or published annually for example in UNCTAD surveys. Major factors in terms of savings are low labor costs, availability of resources (material, energy, financial). On the other hand, factors that influence revenues are usually market size and market growth (*World Investment Prospect Survey, 2009*). However, it is also important to evaluate factors that affect the business environment and the presence of foreign investors in the country. These factors are condition and quality of business environment, the level of corruption, but also the rate of assistance from the state - investment incentives (Ferenčíková *et al*, 2010).

The results of analysis of rating institutions show that the attractiveness of some country for foreign direct investment is crucially dependent on favorable business environment, the quality of institutional environment, as well as the relative price and cost competitiveness (Drábek and Polách, 2008). However, the dynamics of FDI flow is significantly influenced by the targeted state policy to promote foreign investments (Drábek and Jelačić, 2007). Results of the global economic crisis, as well as the acceptance of a comprehensive system of measures to reduce them, may affect not only the long-term macroeconomic stability, but also the policy towards FDI, and hence foreign direct investment inflows to Slovakia both in the short and long term.

It can be concluded that maintaining long-term political stability in Slovakia is also reflected positively on the real economy, which is impacted in the continuity of macroeconomic stability and keeping up the suitable business environment. The evaluation of the International Monetary Fund (*IMF, 2009*) shows that long term positive economic development in the SR is manifested in the rapid GDP growth, which was based on health macroeconomic and structural policies and helped to speed up the convergence process of the Slovak economy. Since the Slovak economy is an open and export-oriented economy, its development is significantly influenced by development in the external economic environment. This is confirmed by time-coordinated course of the economic crisis in the external environment and in Slovakia, which also shows that the Slovak economy is tightly integrated into European and world economy (Okáli *et al*, 2009). Simultaneously, the imported recession also causes many negative consequences on the domestic economy. Such close connection with the external environment is also reflected in forecasts of economic development for the years 2012-2015, which can be evaluated as positive in comparison with other EU countries.

The government deficit exceeding 3 % of GDP is not the cause for investors concerns in the current situation. However, the expected economic recovery will be reflected in the re-tightening of the fiscal policy, and it will be a positive signal to encourage the investor confidence, underlining the government's responsible approach to meeting the commitments under the Stability and Growth Pact (SGP).

The main objective of each company is an efficient and successful business. There is a general economic principle: to achieve the maximum result with the minimum of means (Oblak *et al*, 2008, Stasiak-Betlejewska *et al*, 2007). The objective of this research was to evaluate the impact of investment and foreign direct investment in the Slovak Republic with the focus on the wood-processing industry in SR all based on the analysis of time series of selected economic indicators, business and investment environment and investment incentives.

To achieve this objective partial objectives were formulated:

- the analysis of foreign direct investment in the Slovak Republic as well as in individual sectors of the wood-processing industry, analysis of the business and investment environment, investment incentives in Slovakia,
- the evaluation of selected economic indicators in SR and wood-processing industry of SR with the application of selected statistical methods (correlation and regression analysis), the interpretation of the solution and obtained results.

## 2 METHODOLOGY OF RESEARCH

### 2. METODA ISTRAŽIVANJA

Statistical methods were used to analyze and evaluate the effects of investment in SR and in wood-processing industry of SR. Correlation analysis describes the relationship between two quantitative variables. This analysis does not imply cause and effect relationship between two variables. Linear regression allows to examine the cause and the subsequent relationship between two variables  $x$  and  $y$ . The regression line determines the dependence. The chart of correlation and linear regression analysis shows the values of independent and dependent variables in each year and the regression line. Values closer to the regression line mean stronger impact on the examined variable.

Correlation and regression analysis of research focuses on foreign direct investment in Slovakia, the GDP growth of Slovakia, investment and selected variables in the wood-processing branch. These are indicators that characterize the economic situation in the mentioned sector, focusing on indicators that have a positive impact on the economic development of the wood-processing industry.

The selected economic indicators are evaluated over a period of 10 years in the 1999-2008 time series. Software products STATISTICA 9 of the company StatSoft and the application Excel from Microsoft Office 2003 from Microsoft, as well as spreadsheet and graphics tools of applications were used for data processing.

## 3 RESULTS AND DISCUSSION

### 3. REZULTATI I RASPRAVA

#### 3.1 Business environment in Slovakia

##### 3.1. Poslovno okruženje u Slovačkoj

Generally, it can be stated that the business environment in Slovakia is not quite good. According to the

**Table 1** Index of Economic Freedom worldwide in 2010

**Tablica 1.** Indeks ekonomske slobode u svijetu u 2010. godini

World Rank <i>Mjesto u svijetu</i>	Overall Index <i>Ukupni indeks</i>	Country <i>Država</i>	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]	[9]	[10]
1.	89,7	Hong Kong	98.7	90.0	93.0	93.7	83.1	90.0	90.0	90.0	81.0	87.4
2.	86,1	Singapore	98.2	90.0	90.7	95.3	80.9	75.0	50.0	90.0	92.0	98.9
3.	82,6	Australia	90.3	85.1	61.4	64.9	82.7	80.0	90.0	90.0	87.0	94.0
4.	82,1	New Zealand	99.9	86.0	63.6	51.3	83.1	80.0	80.0	95.0	93.0	88.8
5.	81,3	Ireland	92.8	87.5	71.1	61.8	79.0	95.0	80.0	90.0	77.0	79.0
6.	81,1	Switzerland	81.2	90.0	68.2	68.9	81.3	80.0	80.0	90.0	90.0	81.8
7.	80,4	Canada	96.5	88.1	76.7	54.1	75.4	75.0	80.0	90.0	87.0	81.5
8.	78,0	United States	91.3	86.9	67.5	58.0	78.0	75.0	70.0	85.0	73.0	94.8
9.	77,9	Denmark	97.9	87.5	35.9	22.0	79.3	90.0	90.0	90.0	96.0	93.7
10.	77,2	Chile	64.8	88.0	77.5	89.6	73.0	80.0	70.0	85.0	69.0	75.4
34.	69,8	Czech Republic	65.5	87.5	80.1	45.6	75.6	70.0	80.0	65.0	52.0	76.4
35.	69,7	Slovak Republic	72.6	87.5	84.0	64.5	78.2	70.0	70.0	55.0	50.0	65.0
51.	66,1	Hungary	76.8	87.5	68.6	25.9	74.1	75.0	70.0	65.0	51.0	67.6
71.	63,2	Poland	62.2	87.5	74.9	46.8	78.1	60.0	60.0	55.0	46.0	61.5
177.	26,7	Cuba										
178.	21,4	Zimbabwe										
179.	1,0	North Korea										

Scale 0-100, 100 – maximum freedom, Source: data from heritage.org/Index  
Skala 0-100, 100 – maksimalna sloboda; Izvor: podaci s heritage.org/Index

Slovak Chamber of Commerce and Industry (SCCI), it is getting gradually worse. The survey of SCCI shows that 71 % of the 170 surveyed companies consider the business environment as adverse. Only 2 % of surveyed companies identified the Slovak business environment as favorable. Based on the survey, it follows that 59 % of surveyed companies expect no change in the business environment. Only 6 % of respondents expect improving of the business environment and 35 % its further deterioration.

Slovakia had its economic growth based on the quality of business environment, of course using the comparative advantages which the country still has, but their strength in relation to other countries gradually weakens (Merková and Drábek, 2010). Justice and legislation are among the worst areas of business environment in Slovakia. Worse legislative environment according to the SCCI survey is particularly evident in the rapid adoption of amendments and laws (Merková, 2010).

The situation of the business environment in Slovakia and other countries was analyzed on the basis of five ratings - indexes and rankings compiled by various world expert organizations and institutions. Ratings are not only supported by statistical data of the economic development of countries; they are the result of experts' opinions and independent assessors' perceptions of the development of each country in comparison with the development in other economies. Although rankings are not scientific facts, the mentioned institutions that compiled the rankings are considered as independent, objective and credible. The ratings reflect the perceptions of the situation in the country from the perspective of the business sector.

### 3.1.1 Index of Economic Freedom

#### 3.1.1. Indeks ekonomske slobode

According to the *Index of Economic Freedom*<sup>1</sup> in 2010, Slovakia improved by 0.3 points and was ranked 35<sup>th</sup> with the overall assessment of 69.7 points (in 2009 it was 69.4 points, 36<sup>th</sup> place). The overall score is higher than the world average. The Czech Republic took the highest position among V4 countries after five years, and was ranked 34<sup>th</sup> (37<sup>th</sup> in 2009). Hungary was ranked 51<sup>st</sup> (44<sup>th</sup> in 2009) and Poland 71<sup>st</sup> (82<sup>nd</sup> step in 2009). However, Poland is included among top ten countries with the best annual improvement in the ranking. According to the European region, Slovakia ranked 18<sup>th</sup> out of 43 countries (in 2009 it was ranked 20<sup>th</sup>). The former British colony of Hong Kong has been declared the freest economy in the world for 16 times.

The Index of Economic Freedom contains ten subcriteria:

- |                         |                             |
|-------------------------|-----------------------------|
| [1] Business Freedom    | [6] Investment Freedom      |
| [2] Trade Freedom       | [7] Financial Freedom       |
| [3] Fiscal Freedom      | [8] Property Rights         |
| [4] Government Spending | [9] Freedom from Corruption |
| [5] Monetary Freedom    | [10] Labor Freedom          |

Experts in evaluation of Slovakia show a significant deterioration in the category of freedom in the labor market, but offset by improvements in other areas. Slovakia is still limited by two institutional weaknesses - the judicial system is inefficient and slow, and in recent years efforts to eliminate the corruption have

<sup>1</sup> *Economic Freedom Score* is compiled and published by the Heritage Foundation, Washington No.1 think tank and the Wall Street Journal, the index covers 183 countries.

**Table 2** Index of Economic Freedom in V4 countries in the period 2008-2010**Tablica 2.** Indeks ekonomske slobode za zemlje Višegradske skupine V4 u razdoblju 2008 -2010.

Country <i>Država</i>	Rank in 2010 <i>Mjesto u svijetu u 2010.</i>	Rank in 2009 <i>Mjesto u svijetu u 2009.</i>	Rank in 2008 <i>Mjesto u svijetu u 2008.</i>
Czech Republic	34.	37.	37.
<b>Slovak Republic</b>	<b>35.</b>	<b>36.</b>	<b>35.</b>
Hungary	51.	44.	43.
Poland	71.	82.	83.

Source: data from heritage.org/Index / Izvor: podaci s heritage.org/ Index

shown only limited progress; in the long-term perspective, investors consider these weaknesses to be a serious factor in locating the foreign enterprises.

### 3.1.2 Ease of Doing Business

#### 3.1.2. Lakoća poslovanja

In the *Ease of Doing Business*<sup>2</sup> Slovakia was ranked worse in 2010 than in previous years. Among all countries, Slovakia fell from 32<sup>nd</sup> place in 2008 to 35<sup>th</sup> in 2009 and 42<sup>nd</sup> in 2010. Although Slovakia has maintained its leading position among the V4 countries (Czech Republic is 74<sup>th</sup>, Hungary 47<sup>th</sup> and Poland 72<sup>nd</sup>), Slovakia is lagging behind faster reformers of Eastern Europe such as Georgia, Estonia, Latvia and Lithuania. Despite this, however, Slovakia overtook five industrially more developed economies of Europe (Portugal 48<sup>th</sup>, Spain 62<sup>nd</sup>, Luxembourg 64<sup>th</sup>, Italy 78<sup>th</sup>, Greece 109<sup>th</sup>). Unexpectedly, Slovakia as the largest manufacturer of automobiles per capita in the world, belongs to the countries in the EU with the lowest “trading across borders”. The Slovak government needs to reduce requirements and shorten the time required for exports and imports, and to optimize this process through competitiveness and transparency.

Slovakia can support the entrepreneurial spirit by simplifying the procedures for starting business and by providing steps aimed at simplifying business registration and making it more acceptable for enterprises. In

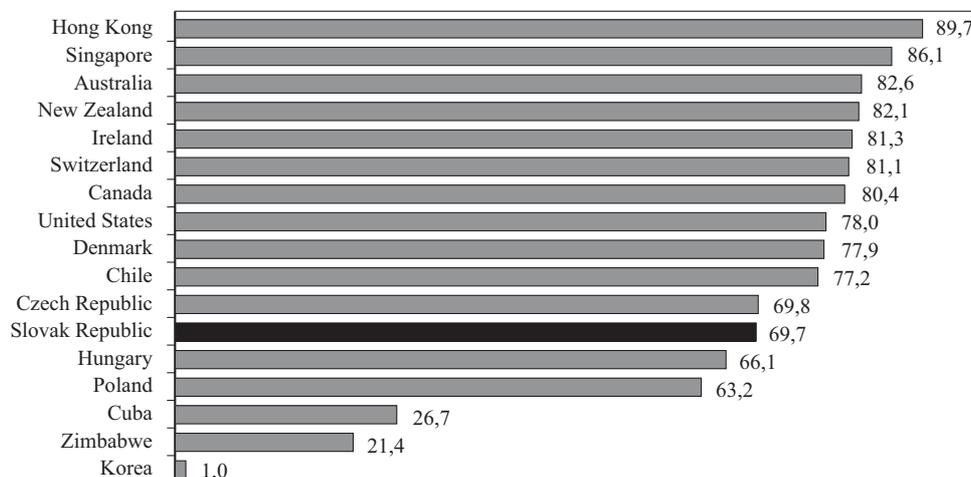
addition, the report of Doing Business indicates that Slovakia needs to shorten the time needed for the enforcement of contracts and decrease costs associated with enforcement. Slovakia has one of the longest waiting times among European countries for obtaining a building permit (287 days), followed only by Poland (308 days) and Cyprus (677 days). This is especially troubling when compared with countries such as Finland or Denmark, where the same may be carried out in 38 or 69 days according to the World Bank.

Slovakia has a poor rating in the category of closing the business, particularly in two areas: the duration of the bankruptcy settlement - about 4 years (followed only by the Czech Republic with a period of 6.5 years) and bankruptcy costs as a percentage of assets, which is 18 % in Slovakia as well as in Austria (followed by Poland with only 20 % and Italy with 22 %). Slovakia has a better score than most EU countries in the cost of obtaining a building permit (the second lowest in the EU, 13.8 multiple of the average wage). Building permits in Hungary is 9.8 times higher than the average wage, while in Bulgaria it is an overwhelming factor - 436.5 times more than the average wage. Investors may obtain a building permit in Slovakia completing 13 treatments, which is less than most other EU countries require (*Report on the state of business environment in SR, Ministry of Economy, 2010*).

What makes Slovakia particularly attractive is the process of acquiring ownership. Slovakia is the country with the lowest costs for this process, which is very fast and efficient. Slovakia is among the top six countries in the strength of their legal rights in obtaining the loan. This index measures the protection rules in relation to

<sup>2</sup> *Ease of Doing Business* – data compiled by the World Bank and International Finance Corporation in the report Doing Business, giving analysis of 183 countries. Annual report 2010 covers data in the period June 2008 to May 2009.

Source of data: <http://www.doingbusiness.org>

**Figure 1** Index of Economic Freedom in 2010 (Source: data from heritage.org/Index)**Slika 1.** Indeks ekonomske slobode u 2010. godini (izvor: podaci s heritage.org/Index)

**Table 3** Ease of Doing Business worldwide in 2010

**Tablica 3.** Lakoća poslovanja u svijetu za 2010. godinu

World Rank <i>Mjesto u svijetu</i>	Country <i>Država</i>	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]	[9]	[10]
1.	Singapore	4	2	1	16	4	2	5	1	13	2
2.	New Zealand	1	5	15	3	4	1	9	26	10	17
3.	Hong Kong, China	18	1	6	75	4	3	3	2	3	13
4.	United States	8	25	1	12	4	5	61	18	8	15
5.	United Kingdom	16	16	35	23	2	10	16	16	23	9
6.	Denmark	28	10	9	47	15	27	13	6	28	7
7.	Ireland	9	30	27	79	15	5	6	21	37	6
8.	Canada	2	29	17	35	30	5	28	38	58	4
9.	Australia	3	62	1	34	4	57	47	27	16	14
10.	Norway	35	65	114	8	43	20	17	9	4	3
42.	Slovak Republic	66	56	81	11	15	109	119	113	61	39
47.	Hungary	39	87	77	61	30	119	122	70	14	58
72.	Poland	117	163	76	88	15	41	151	42	75	85
74.	Czech Republic	113	76	25	62	43	93	121	53	82	116
181.	Guinea-Bissau										
182.	Congo, Dem. Rep.										
183.	Central African Republic										

Source: data of Doing Business / Izvor: podaci s Doing Businessa

**Table 4** Ranking of V4 countries in global ranking of Doing Business in the period 2006-2010

**Tablica 4.** Mjesto zemalja V4 u globalnom redosljedu Doing businessa za razdoblje 2006 – 2010.

Country <i>Država</i>	Report 2010 <i>Izvešće za 2010.</i>	Report 2009 <i>Izvešće za 2009.</i>	Report 2008 <i>Izvešće za 2008.</i>	Report 2007 <i>Izvešće za 2007.</i>	Report 2006 <i>Izvešće za 2006.</i>
Slovak Republic	42.	35.	32.	36.	34.
Czech Republic	74.	66.	56.	52.	50.
Hungary	47.	41.	45.	66.	60.
Poland	72.	72.	74.	75.	74.

Source: data from Doing Business / Izvor: podaci s Doing Businessa

the possession of movable property. However, Slovakia was ranked between 18<sup>th</sup> and 23<sup>rd</sup> place in terms of quality and availability of debt information obtained from public and private debt registries (*rokovania.sk*). In EU Slovakia is ranked between the 7<sup>th</sup> and 10<sup>th</sup> place according to the employment index, which evaluates the rules for hiring people, working time, number of leave days and statutory requirements for dismissal of employees for economic reasons (*spectator.sk*).

The Ease of Doing Business consists of ten indicators:

- [1] Starting a Business
- [2] Dealing with Construction Permits
- [3] Employing Workers
- [4] Registering Property
- [5] Getting Credit
- [6] Protecting Investors
- [7] Paying Taxes
- [8] Trading Across Borders
- [9] Enforcing Contracts
- [10] Closing a Business

### 3.1.3 Global Competitiveness Index

#### 3.1.3. Indeks globalne kompetitivnosti

According to the *Global Competitiveness Index*<sup>3</sup> Slovakia was ranked in the group of developed countries

in 2009 for the first time (based on last year's GDP level); the economic development of these countries is mainly based on the ability to innovate.

The Index consists of 12 pillars of competitiveness:

- [1] Institutions
- [2] Infrastructure
- [3] Macroeconomic environment
- [4] Health and primary education
- [5] Higher education and training
- [6] Goods market efficiency
- [7] Labor market efficiency
- [8] Financial market development
- [9] Technological readiness
- [10] Market size
- [11] Business sophistication
- [12] Innovation

Slovakia was gradually decreasing from the 36<sup>th</sup> place in 2006 to 37<sup>th</sup>, 41<sup>st</sup>, 46<sup>th</sup> and finally 47<sup>th</sup> place in 2010. The Czech Republic annually rose by 2 positions, Poland's position improved by 7 places and Hungary also moved upward. Slovakia is, thus, the only country from the V4 group, rating decreases.

According to the Executive Director of the Business Alliance of Slovakia, which is a partner institution of the World Economic Forum, the global economic crisis means that most countries assessed lower competitiveness index score this year. However, due to the strong

<sup>3</sup> *Global Competitiveness Index* compiled by the World Economic Forum annually in the Global Competitiveness Report, covers 133 countries. Source of data: <http://www.weforum.org/documents/GCR09/index.html>

**Table 5** Global Competitiveness Index worldwide in 2010**Tablica 5.** Indeks globalne kompetitivnosti u svijetu za 2010. godinu

Rank Mjesto u svijetu	Country / Država	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]	[9]	[10]	[11]	[12]
1.	Switzerland	8	5	17	21	6	5	2	14	3	36	3	2
2.	United States	34	8	93	36	7	12	3	20	13	1	5	1
3.	Singapore	1	4	35	13	5	1	1	2	6	39	14	8
4.	Sweden	2	14	15	12	3	4	19	12	1	32	4	5
5.	Denmark	3	12	14	6	2	7	5	8	4	49	8	10
6.	Finland	4	10	12	1	1	19	23	7	10	53	9	3
7.	Germany	16	1	30	24	22	18	70	36	12	5	2	7
8.	Japan	28	13	97	19	23	17	12	40	255	3	1	4
9.	Canada	17	7	31	7	9	16	7	11	11	14	17	12
10.	Netherlands	10	15	38	14	10	6	27	23	2	18	6	13
31.	Czech Republic	62	48	43	33	24	27	20	42	30	40	25	25
46.	Poland	66	103	74	35	27	53	50	44	48	20	44	52
47.	Slovak Republic	78	63	40	48	47	32	29	28	33	57	51	68
58.	Hungary	76	57	83	53	35	64	63	69	40	45	76	45
131.	Chad												
132.	Zimbabwe												
133.	Burundi												

Source: data of Global Competitiveness Report / Izvor: podaci s Global Competitiveness Reporta

**Table 6** Global Competitiveness Index in V4 countries in the period 2006-2010**Tablica 6.** Indeks globalne kompetitivnosti za zemlje V4 za razdoblje 2006 - 2010.

Country / Država	2009-2010	2008-2009	2007-2008	2006-2007	2005-2006
Czech Republic	31.	33.	33.	29.	29.
Poland	46.	53.	51.	48.	43.
Slovak Republic	47.	46.	41.	37.	36.
Hungary	58.	62.	47.	41.	35.

Source: data of Global Competitiveness Report / Izvor: podaci s Global Competitiveness Reporta

interdependence of economies, there was no pronounced movement in the ranking. Regarding the ranking of Slovakia he says: "Poor government's ability to improve the business environment, reform and eliminate the major barriers of business were the cause for Slovakia to fall in the ranking for the third time in a row." (*alianciapas.sk*). The basic disadvantage of Slovakia is that most foreign companies have their innovative potential organized in the home country, so the share of R&D capacities is gradually reduced, and thus it fails to engage the capacities into innovative projects.

### 3.1.4 Global Competitiveness Breakdown

#### 3.1.4. Smanjenje globalne kompetitivnosti

According to *Global Competitiveness Breakdown*<sup>4</sup> Slovakia results in 33rd position in year 2010, occupies second position among V4 countries in long-term situation. The *Global Competitiveness Breakdown* is compiled on the base of four indicators as economic performance, government efficiency, business efficiency and infrastructure. Each one consists from next five subcriteria.

<sup>4</sup> *Global Competitiveness Breakdown* compiled by the Swiss Institute of the International Institute for Management Development in the annual report the World Competitiveness Yearbook, covers 57 countries worldwide. Source of data: <http://www.worldcompetitiveness.com>

### 3.1.5 Corruption Perceptions Index

#### 3.1.5. Indeks percepcije koruptivnosti

In 2009 Slovakia became one of the 9 countries with the worst decline in scores. According to the Corruption Perceptions Index, Slovakia set back four years ago. According to the *Corruption Perceptions Index*<sup>5</sup> in 2009, the score of Slovakia dropped the most in the history of measurements since 1998, from the level of 5.0 to 4.5. Slovakia also worsened annually in the countries ranking: it dropped from the 52<sup>nd</sup>-53<sup>rd</sup> to the 56<sup>th</sup>-60<sup>th</sup> place. For the first time since 2001 Slovakia is ranked worst of the V4 countries (*Transparency International*).

Finally, in connection with the presented ratings, it should be noted that the evaluation does not always reflect the real and actual situation of the country's economy. Can the Index of Economic Freedom be considered as objective, if in 2010 Ireland was ranked 5th, and in

<sup>5</sup> *Corruption Perceptions Index* is compiled by the Transparency International, covers 180 countries worldwide. A composite index, the CPI is based on 13 different expert and business surveys. Eight surveys are made for Slovakia every year. Transparency International makes neither of them, and they are made by different institutions. For Slovakia, the last time they were as follows: the World Economic Forum, Freedom House, The Economist Intelligence Unit, International Institute for Management Development, IHS Global Insight and Bertelsmann Foundation. Source of data: <http://www.transparency.sk/vystupy/rebrick/>

**Table 7** Global Competitiveness Breakdown worldwide in 2010

**Tablica 7.** Smanjenje globalne kompetitivnosti u svijetu za 2010. godinu

Rank Mjesto	Country Država	Economic Performance <i>Ekonomski rezultati</i>	Government Efficiency <i>Učinkovitost vlade</i>	Business Efficiency <i>Učinkovitost poslovanja</i>	Infrastructure <i>Infrastruktura</i>
1.	United Nations	1	20	16	1
2.	Hong Kong	3	2	1	19
3.	Singapore	8	1	4	8
4.	Switzerland	13	3	3	4
5.	Denmark	23	4	2	6
6.	Sweden	20	10	6	2
7.	Australia	15	8	7	12
8.	Canada	16	9	9	7
9.	Finland	40	6	5	3
10.	Netherland	7	14	8	11
29.	Czech Republic	25	31	36	25
33.	Slovak Republic	34	34	26	37
44.	Poland	39	44	50	39
45.	Hungary	33	50	52	33
57.	Venezuela				

Source: data of the World Competitiveness Yearbook / Izvor: podaci iz World Competitiveness Yearbooka

**Table 8** Global Competitiveness Breakdown in V4 countries in the period 2006-2010

**Tablica 8.** Smanjenje globalne kompetitivnosti za zemlje V4 u razdoblju 2006 - 2010.

Country / Država	2009-2010	2008-2009	2007-2008	2006-2007	2005-2006
Czech Republic	29.	28.	32.	28.	30.
Slovak Republic	33.	30.	34.	33.	34.
Poland	44.	44.	52.	50.	48.
Hungary	45.	38.	35.	35.	31.

Source: data of the World Competitiveness Yearbook / Izvor: podaci iz World Competitiveness Yearbooka

**Table 9** Corruption Perceptions Index worldwide in 2009

**Tablica 9.** Indeks percepcije koruptivnosti u svijetu za 2009

Rank Mjesto	Country Država	Corruption Perceptions Index 2009 <i>Indeks percepcije koruptivnosti za 2009.</i>
1.	New Zealand	9.4
2.	Denmark	9.3
3.	Singapore	9.2
3.	Sweden	9.2
5.	Switzerland	9.0
6. – 7.	Finland	8.9
6. – 7.	Nederland	8.9
8. – 10.	Australia	8.7
8. – 10.	Canada	8.7
8. – 10.	Iceland	8.7
46.	Hungary	5.1
49.	Poland	5.0
52.	Czech Republic	4.9
56.	Slovak Republic	4.5
178.	Myanmar	1.4
179.	Afghanistan	1.3
180.	Somalia	1.1

Scale: 0-10, 10 being the best, Source: Transparency International data

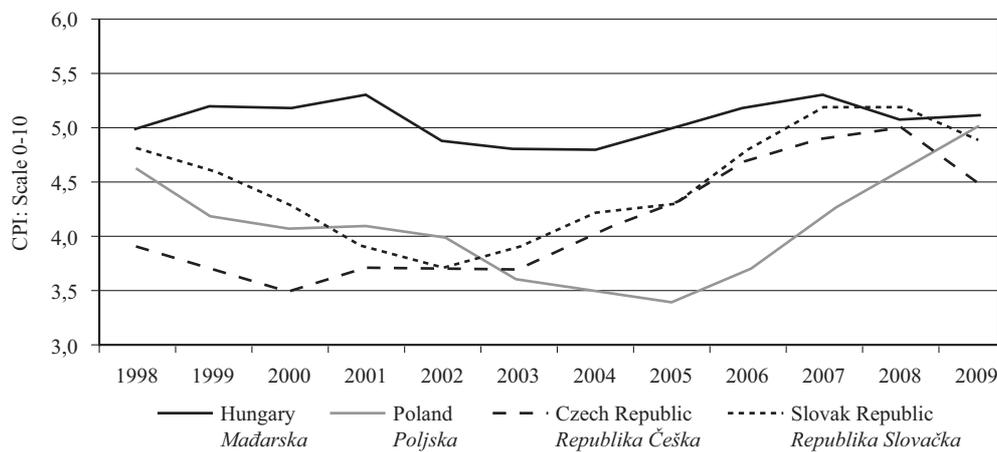
Skala: 0-10; 10 je najbolji; izvor: podaci Transparency Internationala

2009 it nearly declared the state bankruptcy due to extreme indebtedness? Can this country be considered economically free in these conditions? The same applies to the USA (8<sup>th</sup> place). Can its Quality of Business Environment be assessed as reliable, if the best ranked countries are those most indebted in the world such as the USA (4<sup>th</sup> place), Great Britain (5<sup>th</sup> place) and the above-mentioned Ireland (7<sup>th</sup> place)? Even less credible are the results of the Global Competitiveness Index. According to this indicator the USA are excellent (2<sup>nd</sup> place), and the objectively the most competitive China is ranked 29<sup>th</sup> place. However, experts' rankings are accepted by investors, of course in terms of their insights into this issue (Drábek and Merková, 2010).

### 3.2 Investment incentives for the development of investing

#### 3.2. Ulađacki poticaji za razvoj investiranja

The analyzed data show that Slovakia still has significant comparative advantages (high correlation between wage and labor productivity, low cost of release, index of rights of creditors and debtors, a healthy banking sector, relatively good availability of financing by loans, low duty barriers, support of the FDI, good conditions for technology transfer and FDI), which should be used, while the negative factors that foreign investors analyze with the location of their business activities should be removed (Merková and



**Figure 2** Corruption Perceptions Index in V4 countries in the period 1998-2009 (Scale: 0-10, 10 being the best, Source: Transparency International data)

**Slika 2.** Indeks percepcije koruptivnosti u zemljama V4 za razdoblje 1998 - 2009. (Skala: 0-10; 10 je najbolje; izvor: podaci Transparency Internationala)

**Table 10** Corruption Perceptions Index in V4 countries in the period 1998-2009

**Tablica 10.** Indeks percepcije koruptivnosti u zemljama V4 za razdoblje 1998 - 2009.

Country / Država	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Hungary	5.0	5.2	5.2	5.3	4.9	4.8	4.8	5.0	5.2	5.3	5.1	5.1
Poland	4.6	4.2	4.1	4.1	4.0	3.6	3.5	3.4	3.7	4.2	4.6	5.0
Czech Republic	4.8	4.6	4.3	3.9	3.7	3.9	4.2	4.3	4.8	5.2	5.2	4.9
Slovak Republic	3.9	3.7	3.5	3.7	3.7	3.7	4.0	4.3	4.7	4.9	5.0	4.5

Drábek, 2011). In connection with the FDI inflow and encouragement of foreign companies to invest, it is necessary to present the investment incentives - all the measurable economic benefits provided by the host government to foreign investors for the purpose of motivation in business activities. The primary role of the investment incentives should be to motivate the investors to place their new projects in the so called disadvantages areas, which means in the regions with higher unemployment, lower infrastructure quality, etc. The positive impact of a new investment shall be proved by job creation, by chances for the graduates to be used as well as by creation of new entrepreneurial opportunities for local companies (*Ministry of Economy, 2010*).

Investment aid is a form of state aid targeted at promoting economic development of the most disadvantaged regions and at mitigating regional disparities. Granting of investment should stimulate the creation of new jobs.

Investment aid beneficiary can be a legal person or a natural person-entrepreneur with a registered office in the Slovak Republic, incorporated in the Commercial Register or the Trade License Register, ready to implement an investment plan in the Slovak Republic; the beneficiary must be 100 % owned by the applicant, or the applicant must be a controlling person of the beneficiary. The beneficiaries' investment activities and projects have to be in compliance with the Act 565/2007 Coll. the "Act on Investment Aid".

One of the factors affecting the investor's decision on its investment placement is also the amount and the structure of the investment incentives that may be obtained. The so-called intensity of the aid means the maxi-

mum proportion of the eligible costs that may be approved for the investor in the form of particular investment incentives. The maximum intensity differs depending on the district. The limit in Bratislava region is 0 %, Western Slovakia 20-40 %, Central Slovakia 25-50 % and Eastern Slovakia 25-50 % (*Ministry of Economy, 2010*).

The Act on Investment Aid 565/2007 Coll. divides the projects that may be supported into four categories:

- Industrial production
- Technological centers
- Shared services centers
- Tourism

The main factors affecting the acquisition of investment aid are (*Ministry of Foreign Affairs, 2009*):

- Amount of investment
- Region in which the project will be implemented
- Unemployment rate in the region
- Number of direct and indirect jobs created
- Intensity of state aid in the region
- Technological standard, innovation
- Amount of training costs
- Share of highly qualified staff
- Environmental impact
- Quality of the investment plan and application completeness.

If the investor meets all the requirements of the investment aid in individual areas, it can apply for the following forms of investment incentives (*Slovak Investment and Trade Development Agency, SARIO*):

- a) subsidy for the acquisition of material assets and immaterial assets,
- b) an income tax relief,

**Table 11** Forms of investment incentives

**Tablica 11.** Oblici poticaja investicijama

<b>Forms of investment incentives in the Slovak Republic</b> <i>Oblici poticaja investicijama u Slovačkoj Republici</i>	
<b>Direct support for:</b> <i>Izravna potpora za:</i>	<b>Indirect support for:</b> <i>Neizravna potpora za:</i>
construction / <i>izgradnju</i> technology / <i>tehnologije</i> research and development / <i>istraživanje i razvoj</i> job creation, retraining of the workforce / <i>nova radna mjesta, izobrazbu kadrova</i> allowance for staff training / <i>pozajmice za obuku kadrova</i> land acquisition and implementation of infrastructure / <i>kupnju zemljišta i uvođenje infrastrukture</i> loan policy, lower interest, longer repayment period, the state guarantee / <i>zajmove s nižom kamatom, duljim rokovima povrata, državna jamstva</i>	income tax relief / <i>oslobađanje od poreza na dohodak</i> transfer of real estate or exchange of real estate for the price lower than the general value / <i>prijenos nekretnina ili za iznajmljivanje nekretnina za manji iznos od uobičajenoga</i> providing advisory services free of charge or for a partial payment or deferred tax payment / <i>davanje savjetodavnih usluga bez naknade, za djelomično plaćanje ili za plaćanje pojedinih poreznih davanja</i>

Source: data of the Ministry of Economy in SR / *Izvor: podaci Ministarstva gospodarstva Slovačke*

**Table 12** Overview of investment aid in Slovakia in the period 2002-2010 (mill. EUR)

**Tablica 12.** Pregled potpora investicijama u Slovačkoj u razdoblju 2002 - 2010. (mil. EUR)

<b>Forms of investment aid in Slovakia in the period 2002-2010</b> <i>Oblici potpore investicijama u Slovačkoj u razdoblju 2002 - 2010.</i>	<b>Approved</b> <i>Odobreno</i>	<b>Used</b> <i>Iskorišteno</i>
Subsidy for the acquisition of longterm assets / <i>Potpora za stjecanje dugotrajne imovine</i>	547.50	393.60
Contribution for new job creation / <i>Potpora za kreiranje novih radnih mjesta</i>	92.70	48.11
Contribution for staff retraining / <i>Potpora za obuku kadrova</i>	52.51	42.68
Income tax relief / <i>Oslobođenje od poreza na dohodak</i>	439.39	90.06
Transfer or exchange of real estate / <i>Prijenos ili promjena nekretnina</i>	46.69	46.69
<b>Overall / <i>Ukupno</i></b>	<b>1178.79</b>	<b>621.16</b>

Source: data of the Ministry of Economy in SR / *Izvor: podaci Ministarstva gospodarstva Slovačke*

- c) contribution for new jobs created,
- d) transfer of immovable property or exchange of immovable property at a price lower than a general asset value.

Investment incentives mean the price or cost that the country must cover to some extent in connection with the inflow of foreign capital (in periods of deficit in domestic financial resources) considering the positive effects that FDI will bring (in the past it was the solution of two serious problems in the SR - employment growth, improved trade balance) (Drábek and Merková, 2010).

### 3.3 Foreign direct investment flows in the SR and WPI SR

#### 3.3. Izravna strana ulaganja u Slovačku i u slovačku preradu drva

Data of the United Nation Conference for Trade and Development (UNCTAD) held in 2008 show that Slovakia was most highly ranked among 27 EU countries according to the indicator of FDI inflows per capita – 16<sup>th</sup> place with the value of 632 USD/capita. The evaluation of the total FDI inflows in millions of USD, as well as the percentage of FDI in GDP of the country (17<sup>th</sup> place) show similar results.

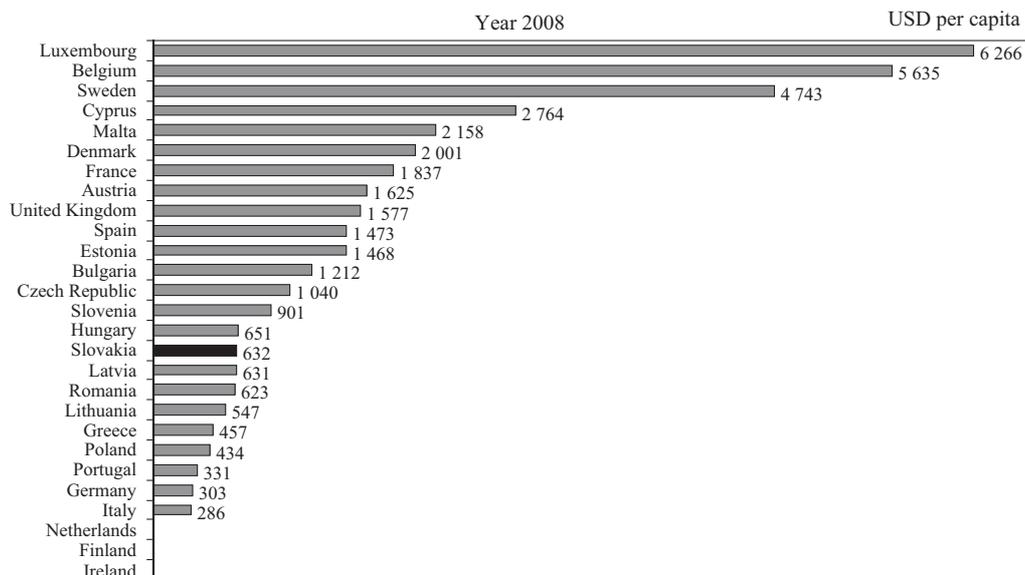
At the beginning of transformation, Slovakia had similar comparative advantages as other countries in Central and Eastern Europe, particularly qualified and cheap labor, cheap raw material and energy inputs, good location and close relations with the EU. Until

2000, FDI inflows had risen, but its volume lagged behind the volume of FDI inflows in the other V4 countries (*The concept of management of FDI, Ministry of Economy, 2009*).

FDI inflows into the wood-processing industry (WPI) in the presented period of 5 years reached the largest volume in 2005, amounting to 1.557 billion SKK, and however 90 % of these resources was absorbed by the furniture industry. In other years, less than half of this value was achieved. The second largest inflow was in 2006, when 835 million SKK were invested into WPI. Pulp and paper industry dominated in 2006 and 2007 with the inflows of 608 million SKK and 606 million SKK of FDI, respectively.

The smallest amount of foreign investment flowed into the sector of wood industry (annually and totally) with the exception of 2004, when the wood industry recorded FDI inflows of 556 million EUR. The opposite trend was recorded in the industrial production of the Slovak Republic, with the lowest FDI inflows, amounting to 10.901 billion EUR, in 2005.

Stagnation of investment in sawmilling, construction and carpentry was reported in the period 1999-2002, and in the period 2003-2006 an increase was recorded amounting to nearly 1.7 to 2.6 billion Slovak crowns (SKK) per year (*NLC, 2009*). A significant increase of investment to the level of 6.07 billion SKK occurred in 2007, but this growth was followed by a drop to the level of 2.25 billion SKK.



**Figure 3** Foreign direct investment inflows per capita in the EU countries, USD per capita. (Source: Eurostat data, <http://epp.eurostat.ec.europa.eu>).

**Slika 3.** Izravna strana ulaganja po stanovniku zemalja EU, USD po stanovniku. (Izvor: podaci Eurostata, <http://epp.eurostat.ec.europa.eu>).

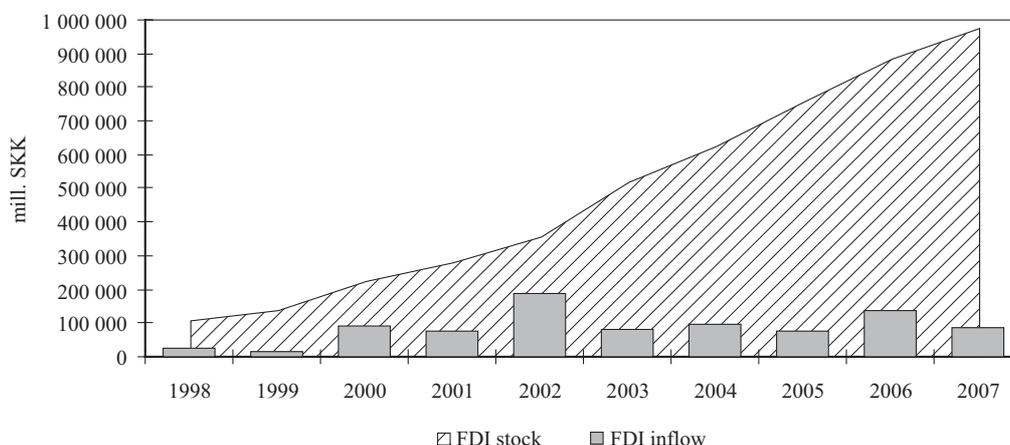
**Table 13** Investment in the WPI and industrial production of the Slovak Republic (mill. SKK)

**Tablica 13.** Investicije u WPI i industrijsku proizvodnju Slovačke Republike (u mil. SKK)

Indicator / Pokazatelj	Sector / Sektor	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Investment (millions SKK) / Investicije (u mil. SKK)	Wood Industry (WI) / Prerada drva (WI)	506	881	766	734	1 788	1 710	2 564	2 573	6 068	2 249
	Furniture Industry (FI) / Proizvodnja namještaja (FI)	580	1 572	1 645	701	794	1 687	2 024	2 787	4 512	1 644
	Pulp and paper Industry (PPI) / Proizvodnja pulpe i papira (PPI)	4 785	1 594	2 205	3 083	6 634	5 161	4 744	3 185	2 796	3 300
	Wood Processing Industry (WPI) / Drvoprerađivačka industrija (WPI)	5 871	4 048	4 616	4 519	9 216	8 558	9 331	8 545	13 375	7 194
	Industrial production / Industrijska proizvodnja	44 489	42 328	71 077	56 466	59 152	71 897	104 046	105 101	102 993	98 627

Source: data from Ministry of Economy SR and Statistical Office of SR

Izvor: podaci Ministarstva gospodarstva Slovačke i Statističkog ureda Slovačke



**Figure 4** Foreign direct investments in the Slovak Republic, mill. SKK. (Source: NBS data, National Bank of Slovakia.)

**Slika 4.** Izravna strana ulaganja u Slovačku, u mil. SKK. (Izvor: podaci NBS-a, National Bank of Slovakia.)

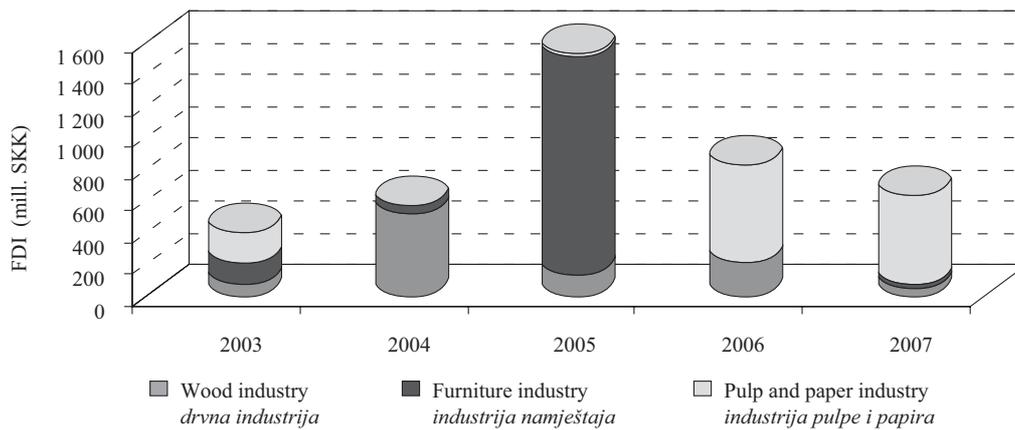


Figure 5 Inflow of FDI in sectors of wood-processing industry (mill. SKK)

Source: NBS data

Slika 5. FDI u sektor drvoprerađivačke industrije (u mil. SKK)

Izvor: podaci NBS-a

The sector of furniture production has seen better investment in the years 2000, 2001, 2004-2006 and this fact caused the growth of labor productivity. The investment was in the range of 1.5 to 2.8 billion SKK in the years mentioned above. Similarly as in the sector of wood industry (WI), in furniture industry (FI) an equally sharp increase was recorded in 2006-2008, from 2.8 billion SKK to 4.5 billion SKK in 2007 and then a fall to 1.6 billion SKK in 2008.

Rapid changes of investment in the pulp and paper industry (PPI) were reported following the realization of significant business actions during the whole period. Major modernizations in this sector were made in 1999 and 2003-2005, but the overall trends suggest that the highest volume of investment of all three sectors of wood processing industry were made into the pulp and paper sector ranging between 1.6 and 6.6 billion SKK per year (Merková *et al*, 2011).

### 3.4 Effects of investment and FDI in the SR and WPI SR

#### 3.4. Učinci investicija i FDI-a u Slovačku i slovačku prerađu drva

Effects of investment and FDI were analyzed through correlation and regression analysis, which was applied to detect dependencies between investment and other economic indicators. Selected analytical results, which demonstrate the positive impact, are presented in Table 15.

The first significant dependence is between foreign direct investment stock in the SR and GDP growth of SR with the correlation coefficient  $r = 0.94$ , which demonstrates that the growth of FDI causes GDP growth. Regression coefficient  $b = 0.000009$  means that the growth of FDI in 100 billion SKK causes the GDP growth of 0.9 % on average.

Subsequent correlation and regression analysis examined the correlation between variables in the wo-

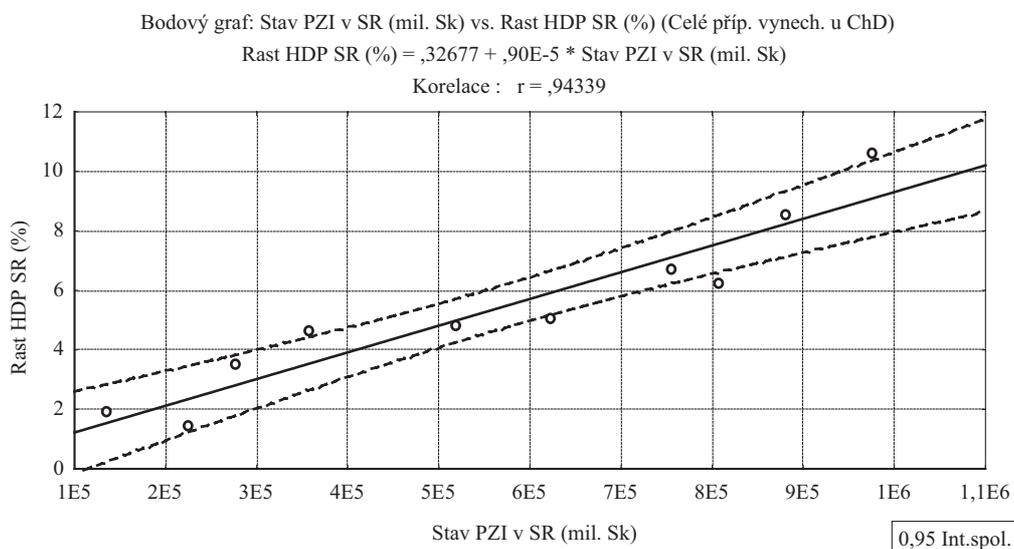


Figure 6 Correlation: FDI stock in SR ~ GDP growth in SR (period 1999-2008)

Slika 6. Korelacija zaliha FDI-a u Slovačkoj i rast BDP-a u Slovačkoj (za razdoblje 1999 - 2008)

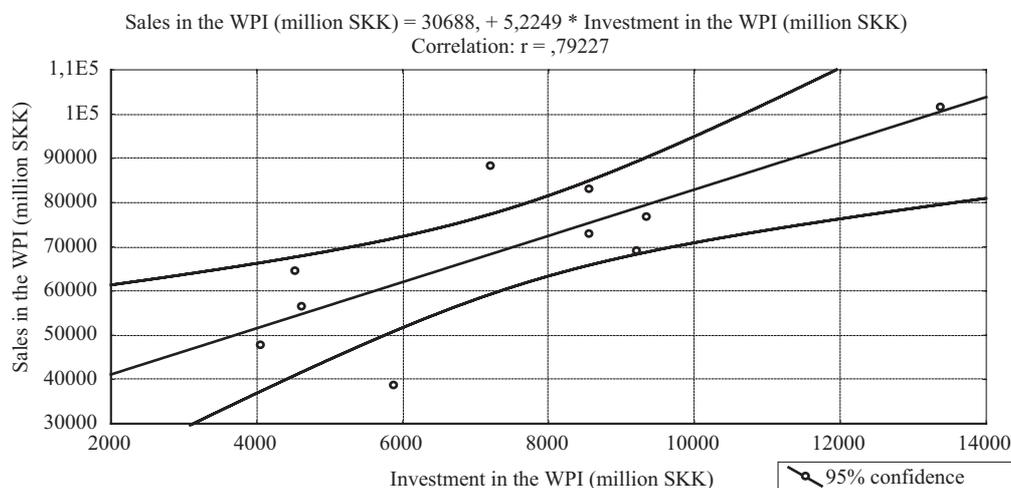
**Table 14** Selected results of correlation and regression analysis**Tablica 14.** Odabrani rezultati korelacijske i regresijske analize

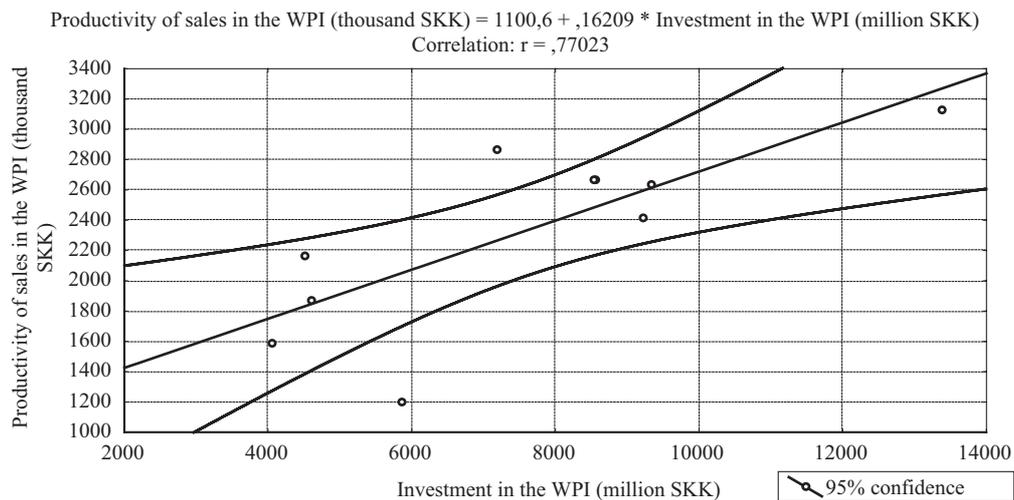
Variables Varijable	Indicator / Pokazatelj	Unit Mjerna veličina	Mean Srednja vrijed- nost	Standard Deviation stan- dardna devijacija	Correla- tion r Korelaci- ja r	Determi- nation r <sup>2</sup> Determi- nacija r <sup>2</sup>	Probabili- ty of error p Vjerojat- nost pogre- ške p	Constant a Konstanta a	Slope b) Nagib b
X	FDI stock in SR FDI zaliha u Slovačkoj	mill. SKK	556 169	297 078					
Y	GDP growth in SR rast BDP-a u Slovačkoj	%	5,32	2,83	0,943394	0,889993	0,000042	0,326772	0,000009
X	Investment in WPI investicije u WPI-u	mill. SKK	7 527	2 885					
Y	GDP growth in SR rast BDP-a u Slovačkoj	%	5,32	2,83	0,842908	0,710494	0,002194	-0,90	0,000826
X	Sales in WPI prodaja u WPI-u	mill. SKK	70 017	19 024					
Y	GDP growth in SR rast BDP-a u Slovačkoj	%	5,32	2,83	0,944034	0,891201	0,000040	-4,50275	0,00014
X	Value added in WPI dodana vrijednost u WPI-u	mill. SKK	15 715	2 587					
Y	GDP growth in SR rast BDP-a u Slovačkoj	%	5,32	2,83	0,779587	0,607756	0,007838	-8,06785	0,00085
X	Investment in WPI investicije u WPI	mill. SKK	7 527	2 885					
Y	Sales in WPI prodaja u WPI-u	mill. SKK	70 017	19 024	0,792267	0,627687	0,006287	30687,77	5,224946
X	Investment in WPI investicije u WPI	mill. SKK	7 527	2 885					
Y	Labour productivity of turnover in WPI produktivnost rada u obrtu WPI-a	thousands SKK	2 321	607	0,770233	0,593259	0,009143	1100,60	0,162090

od-processing industry of SR, with the focus on the positive impact of investment and the value of fixed assets. Dependence of investment and sales in the WPI showed a correlation coefficient of  $r = 0.79$ . Regression coefficient  $b = 5.22$  means that the growth in investment of 1 billion SKK causes sales growth amounting to 5.22 billion SKK. Dependence of in-

vestment and labor productivity in WPI has a similar correlation coefficient  $r = 0.77$ ; the regression coefficient  $b = 0.162$  shows that growth in investment of 1 billion SKK causes labor productivity growth of 0.162 million SKK (Figure 10).

Development of the WPI indicators in 2008 and 2009 is due to the financial and economic crisis as well

**Figure 7** Correlation in the WPI: Investment ~ Sales (period 1999-2008)**Slika 7.** Korelacija za investicije i prodaju WPI-a (razdoblje 1999 - 2008)



**Figure 8** Correlation in the WPI: Investment ~ Labor productivity (period 1999-2008)  
**Slika 8.** Korelacija investicija i produktivnosti rada WPI-a (razdoblje 1999 - 2008)

as to the negative trend caused by unsolved problems for a long time, as shown by the annual decline in sales, value added and profit. Development of selected indicators is shown in Tables 15 to 17.

The employment dropped in all sectors of the WPI and it can be assumed that a smaller number of employees has an impact on labor productivity growth, resulting in wage increases, as correlation and regression analysis showed a high dependence (correlation coefficient 0.95) between labor productivity growth and wage growth.

#### 4 CONCLUSION 4. ZAKLJUČAK

The global financial crisis also had a negative impact on the development of the foreign direct investment flows. Since the end of 2008, global FDI inflows have decreased in all three forms. Equity shares, reinvested earnings and other capital flows (especially inside-corporate loans) fell mainly in developed economies. Investments in equity shares have been reduced due to the weakening of foreign mergers and acquisitions. Lower profits of subsidiary units contributed

**Table 15** Selected indicators of wood industry  
**Tablica 15.** Odabrani pokazatelji za preradu drva

Indicator / Pokazatelj	2008	2009
Total revenues (mil €) / ukupni prihod (u mil €)	569	410
Value added (mil €) / dodana vrijednost (u mil €)	104	75
After-tax profit (mil €) / dobit nakon oporezivanja (u mil €)	-2	-41
Average number of employees / prosječni broj zaposlenih	8 590	6 360
Average monthly wage (€) / prosječna mjesečna plaća (€)	581	594

Source: Trend analysis / Izvor: analiza trendova

**Table 16** Selected indicators of furniture industry  
**Tablica 16.** Odabrani pokazatelji za proizvodnju namještaja

Indicator / Pokazatelj	2008	2009
Total revenues (mil €) / ukupni prihod (u mil €)	706	573
Value added (mil €) / dodana vrijednost (u mil €)	176	161
After-tax profit (mil €) / dobit nakon oporezivanja (u mil €)	19	16
Average number of employees / prosječni broj zaposlenih	11 960	10 470
Average monthly wage (€) / prosječna mjesečna plaća (€)	650	641

Source: Trend analysis / Izvor: Analiza trendova

**Table 17** Selected indicators of pulp and paper industry  
**Tablica 17.** Odabrani pokazatelji za proizvodnju pulpe i papira

Indicator / Pokazatelj	2008	2009
Total revenues (mil €) / ukupni prihod (u mil €)	1 403	1 227
Value added (mil €) / dodana vrijednost (u mil €)	270	262
After-tax profit (mil €) / dobit nakon oporezivanja (u mil €)	83	15
Average number of employees / prosječni broj zaposlenih	7 420	6 790
Average monthly wage (€) / prosječna mjesečna plaća (€)	904	959

Source: Trend analysis / Izvor: analiza trendova

to the decline in reinvested earnings (*World Investment Report, 2009*). In the period of restructuring of parent companies, foreign subsidiary units were often involved in balancing the outstanding debt.

All economies have been affected by the global crisis in terms of decrease in exports and industrial production, the slowdown of FDI inflows and rising unemployment.

FDI inflows into the region of the V4 countries affect various factors in crisis. In relation to individual V4 countries, however, expectations are primarily the highest average GDP growth over the long term (Slovakia), a large domestic market (Poland) and a relatively stable service sector (Czech Republic, Hungary). The V4 countries in crisis and uncertain investors have the advantage of a predictable and well known environment, in the case of Slovakia even strengthened by the membership in the monetary union.

There is a review of the perception of prices, as investors will certainly not decide for the lowest current price - meaning low production costs and cheap labor or low tax cost - but primarily for the lowest cost throughout the life cycle of the investment (Jelačić *et al*, 2010). Apart from the quality of infrastructure, size of the domestic market or access to regional and international markets, foreign investors will particularly take into account the factors such as energy costs, availability of suppliers and customers, sufficient qualified and skilled workforce, predictability of economic development, stability of legislative conditions, security of companies and others. One of the biggest challenges of the Slovak economy is the ambition to remain an attractive country for foreign direct investment.

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