

# JAPANESE FOREIGN DIRECT INVESTMENT IN THE VISEGRÁD FOUR: TRENDS, CHARACTERISTIC AND DRIVING FORCES

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**Abstract:** Japan continues to be the most important Asian investor in Poland and Czechia, and the second most important player in Hungary and Slovakia (after South Korea). Japanese multinationals, operating in the automotive, electronics and other industries, as well as in certain services, play an important role in the Central and Eastern European economies, enhancing the performance of the respective V4 economies. Although compared to, for instance, German MNCs' investment, Japanese MNCs represent a rather minor share in the total FDI stock of these countries, the number of companies increase year-on-year. The paper briefly presents the history and main trends of Japanese investment in the V4 region, maps out the main characteristics of Japanese investment flows, and identifies the driving forces of Japanese FDI within the V4 region. The last section of the paper also sheds light on a new opportunity for the V4 countries to attract more investment from Japanese companies, that is the Japanese companies' possible relocation to the V4 region from the United Kingdom, as a result of Brexit.

**Keywords:** foreign direct investment, Japanese MNCs, Visegrad Four, driving forces of FDI, location decisions, relocation

## Introduction

The change of the Visegrád Four (V4) countries from centrally-planned to market economies resulted in increasing inflows of foreign direct investment (FDI) to these transition countries. During the transition, the region went through radical economic changes which had been largely induced by foreign capital. Foreign multinationals realized significant investment projects in the V4 and established their own production networks. Investors - mainly from core European Union countries - were attracted by macroeconomic factors such as relatively low unit labour costs, market size, openness to trade, and proximity. When it comes to institutional factors that influence inward FDI, the prospects of V4 countries' economic integration with the EU have already increased FDI inflows into the region.

Although the majority of investors arrived from Western Europe, the first phase of inward Asian FDI came also right after the transition. Japanese as well as Korean companies indicated their willingness to invest in the V4 region already before the fall of the Iron Curtain. The majority of their investments took place during the first years of the democratic transition. The second impetus was given by the V4 countries' accession process to the European Union. EU membership of the V4 countries allowed Asian investors to avoid trade barriers and the countries could also serve as assembly bases for them. Not only membership but the prospect of EU accession attracted new Asian investors to V4 countries. New investments arrived in the year of accession, too. The third phase dates back to the global economic and financial crisis, when financially-distressed companies all over Europe had often been acquired by non-European companies.

In line with the above, the aim of this paper is to briefly present the history and main trends of Japanese investment in the V4 region, map out the main characteristics of Japanese investment flows, and to identify the driving forces of Japanese FDI within the V4 region. The final section of this paper sheds light on a new opportunity for V4 countries to attract more investment from Japanese companies, that is, the Japanese companies' possible relocation to the V4 region from the United Kingdom as a result of Brexit.

## Japanese investment in the V4 region in retrospect

Japanese companies started to expand overseas by the early 1960s with modest growth in the beginning. The Foreign Exchange and Foreign Trade Control Law and the Foreign Capital Law were the two main laws which regulated - and somewhat restricted - Japanese firms' international activities during the 1950s, 60s and 70s. However, the revision of the Foreign Exchange and Foreign Trade Control Law in 1979 accelerated the overseas activities of Japanese companies as this revision created the opportunity for free outward investment (Yang et al, 2009).

Japan led the way in government-subsidized outward FDI in the 1950s, well before the liberalization through offering subsidized loans to companies investing abroad. Irwin and Gallagher (2014) highlight that the Export-Import Bank of Japan created a branch focusing on OFDI in 1953 which gave almost 70 billion USD by 1999 to finance its companies' foreign investments. Likewise, the Japan Bank of International Cooperation (as well as its predecessor, the Japanese Development Bank) began operations mainly with export loans in the 1950s but later evolved as an outward investment creditor (Irwin-Gallagher, 2014).

When it comes to Japanese companies' investments in the V4, the three waves of FDI, mentioned in the introduction above, can be observed. The first investments by Japanese firms were made in the service sector in the late 1970s and 1980s. General trading companies opened their local representative offices to develop and strengthen trade relations with Japan. At that time, Japanese companies, such as Itochu, were mainly acting as distributors, representing certain goods in their line of products (Grill et al. 2016). The real impetus was given by the democratic transition of Visegrád countries in 1989, followed by notable investment inflows from the 1990s. In Hungary, the largest of these was the establishment in 1991 of a Suzuki plant in Esztergom, Hungary. Suzuki's experience became a model for other Japanese companies wanting to invest in the region (Grill et al. 2016), followed by companies such as Sony, Alpine, Aikawa, Clarion, TDK, Denso - just to mention a few companies hailing from the electronic

industry as well as those from within the car part manufacturing industry. Toyota arrived in Poland in 1999 and initiated production in the early 2000s (McCaleb-Szunomar 2016).

The years before and immediately after the EU accession of V4 countries attracted many Japanese companies and brought major investments, mainly in the automotive and electronic sectors, but Japanese companies also became involved in other sectors such as the chemical industry. In Hungary, for instance, Asahi Glass, Ibiden, and Bridgestone were the three major automotive companies that arrived that time with further companies arriving in other sectors such as in chemicals (Zoltek), food (Nissin) and beverages (when Asahi Group acquired Dreher, the famous Hungarian brewing company).

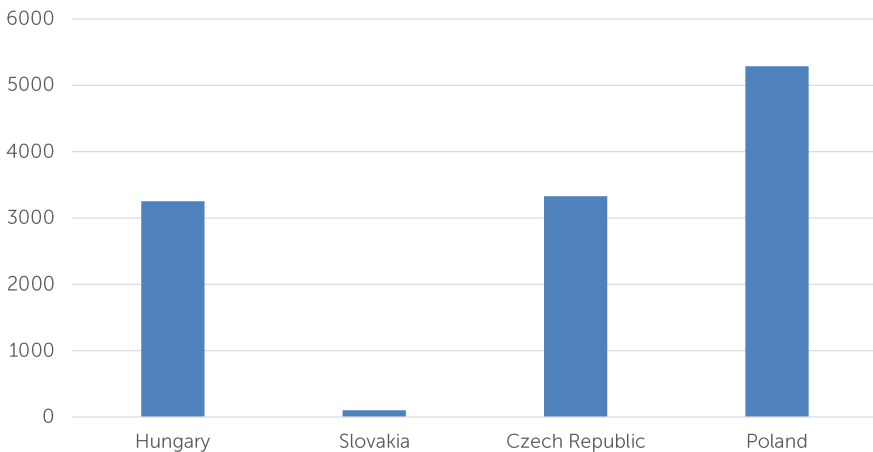
Although the global economic and financial crisis did not bode well for attracting many new companies, those that invested in V4 countries are continuously expanding, introducing new production technologies and increasing available supplier capacities. In 2020 in Hungary, for instance, Japanese companies invested around 68 million EUR<sup>1</sup>. In 2021, three major companies in the automotive sector - Alpine European Electronics Industry Ltd. in Biatorbágy, DENSO Manufacturing Hungary in Székesfehérvár and Diamond Electric Hungary Kft. in Esztergom - have recently announced investments of 18 million EUR, while developments are also planned at the Suzuki plant in Esztergom.

## Characteristics of Japanese investments in the V4

According to the Amadeus Database, there are 132 Japanese companies operating in Hungary, 82 in Slovakia, 260 in Poland and 229 in the Czech Republic. It varies country to country but 40-50% of these are manufacturers. Their geographical location is diverse; some of these companies are located in more developed regions of V4 countries (in the case of Hungary, for instance in the north-western part of the country with a larger cluster in and around the capital city of Budapest), but there are cases of companies located in less prosperous sub-regions (such as

Eastern Hungary). Japan is one of the most important non-European investors in the V4 region, especially in Poland, Hungary and the Czech Republic (see Figure 1).

*Figure 1.*  
*Japanese FDI stock in the V4, 2018, million USD*



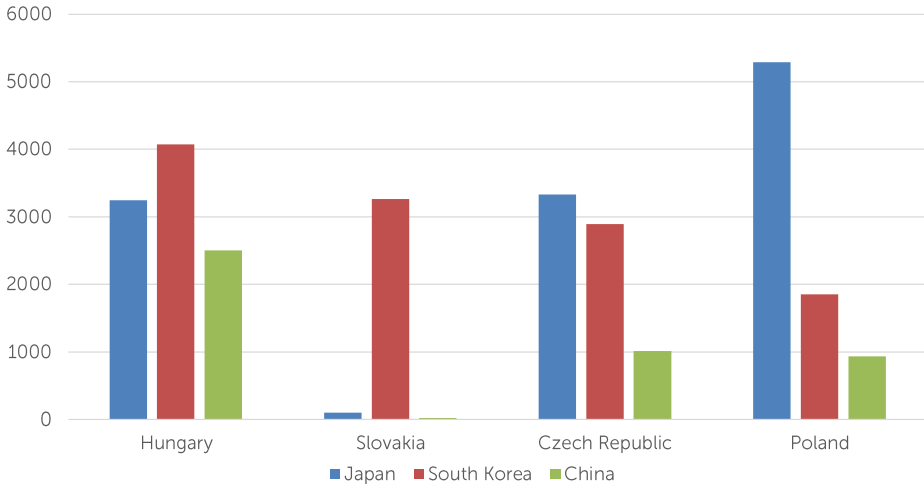
*Source: OECD Stat*

If we compare Japanese FDI stock with other East Asian countries' (South Korea and Japan) FDI positions (see Figure 2.), Japan seems to be the most important East Asian investor in Poland and the Czech Republic, while being the second most important player in Hungary and Slovakia (after South Korea).

Japanese MNE's have also become important employers in the V4 region. Péter Szijjártó, Minister of Foreign Affairs and Trade, recently stated that Japanese companies employ some 34,000 Hungarians, 40,000 in Poland, and 47,000 in the Czech Republic. The management methods and practices of the Japanese V4 subsidiaries represent a unique mix due to (1) early collaboration in the Visegrád region's economic development, (2)

the U.S.-style influence on European affiliates of Japanese multinationals, (3) the European Union’s effect on V4 market practices, (4) and the fact that V4 markets are also unique in comparison to other European markets as a result of their transition process (Grill et al. 2016).

*Figure 2.  
East Asian FDI stock in the V4, 2018, million USD*



*Source: OECD Stat*

## Driving forces behind Japanese investments in the V4 region

Different types of investment motivations attract different types of FDI which Dunning (1992, Dunning and Lundan 2008) divided into four categories: market-seeking, resource-seeking, efficiency-seeking and strategic asset-seeking. The factors attracting market-seeking multinationals usually include market size, as reflected in GDP per capita and market growth (GDP growth). The main aim of a resource-seeking MNE is to acquire particular types of resources that are not available at home (such as natural resources or raw materials) or are available at a lower cost compared to the domestic market (such as unskilled labour).

Investments aimed at seeking improved efficiency are determined by factors such as low labour costs and tax incentives. Finally, the companies interested in acquiring foreign (strategic) assets may be seeking brands, new technologies or market niches that they can fill in.

Till the end of the 1970s, Japanese outward FDI was characterized by natural resource-seeking motives in order to supplement the countries' resource-poor economy (Park, 2003). Between 1979 and 1985, Japanese companies' overseas investments were motivated by market-seeking, as – according to Yoshida (1987) – market expansion was cited as the number one reason for Japanese firms' investment in the United States. Besides market-seeking investments over the last twenty years, efficiency-seeking became another important motive for Japanese companies for reasons of cost reduction (Yang et al., 2009).

Kawai (2006) analysed motivation and location determinants of Japanese MNEs in Central and Eastern Europe. The author found that by 2004, Japanese investment in CEE was low when compared with European counterparts and 90% of investment was located in the Czech Republic, Hungary and Poland. Japanese MNEs' investment in ECE was motivated by relatively low labour and land costs, well-educated labour forces deemed necessary in manufacturing sectors while access to rich EU markets also played a role. Thus, overall, Japanese FDI in CEECs is characterized by efficiency-seeking and market-seeking motives (Kawai 2006).

And, indeed, when searching for possible factors that made the V4 region a favourable investment destination for Japanese investors, the labour market is to be considered as one of the most important factors. A skilled labour force is available in sectors where Japanese companies are operating, while labour costs are lower in the Central and Eastern European (CEE) region than the EU average. However, there are differences within the CEE region as well. Unit labour costs are usually cheaper in Bulgaria and Romania than in Hungary, the Czech Republic, Slovakia and Poland. Corporate taxes or various tax incentives are among the further potential pull factors of the CEE region.

Nevertheless, these labour costs and tax differences are not the most important factors in attracting investments within the CEE region as there is more investment from Japan in Visegrád countries where labour costs and taxes are relatively higher when compared to Romania and Bulgaria. Since FDI in the V4 countries is generally the highest in the CEE region, an explanation for that can be the so-called ‘agglomeration effect’ - when multinational companies from the same country increase their efficiency by locating close to each other - and the ‘demonstration effect’ - whereby multinational companies that have already invested in V4 countries send signals to new potential investors on the reliability and attractiveness of the host country (McCaleb-Szunomar 2016, 2017 and Szunomar et al. 2020).

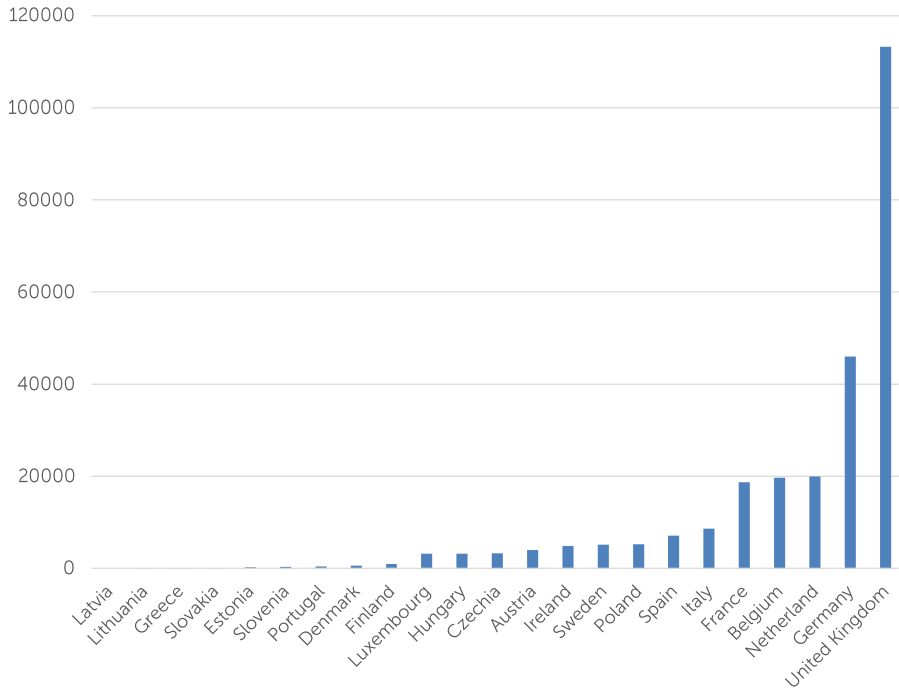
Although the above-mentioned efficiency-seeking motives play a role, the main type of Japanese FDI in the V4 region is market-seeking investment by entering V4 markets, Japanese companies have access not only to the whole of the EU market but also to the CIS, Mediterranean and EFTA markets. These companies’ operations in the V4 region can either be linked to their already-existing businesses in Western Europe or can help strengthen their presence on the wider European market. Another aspect of EU membership that has induced Japanese investment in the V4 region is institutional stability such as the protection of property rights (Morck et al. 2007).

## Conclusions and future prospects

When examining economic ties between East Asia and the Visegrád region, we can conclude that while Japan and South Korea have been investing in this region for more than three decades, China has recently been pushing forward. However, Japan continues to be the most important Asian investor in Poland and the Czech Republic, and the second most important player in Hungary and Slovakia (after South Korea). Japanese multinationals, operational in the automotive, electronics and other industries, as well as in certain services, play an important role in CEE economies, leaving their marks on the performance of the respective V4 economies. Although they represent a rather minor share in the total FDI stock of these countries, the number of companies increase year-on-year.



Figure 3.  
Japanese FDI stock in Europe, 2018, million USD



Source: OECD Stat

Moreover, when looking further ahead, the V4 region can possibly expect rising inflows of Japanese FDI as a result of the UK's decision to leave the European Union. At first reading, it may seem that Brexit might have nothing to do with Japanese companies' presence in the V4 region but in fact it has. As can be seen in Figure 3., the UK hosts the vast majority of Japanese FDI in Europe. They also have the highest number of Japanese companies (almost one thousand) as well as affiliated employees around 175,000 (Rudlin 2021).

The majority of these companies are exporting to the EU market which will be more difficult in the future as a result of post-Brexit rules. According to Rudlin's report (2021), as a reaction to Brexit, the Japanese presence in the UK is already declining while rising elsewhere

in Europe which most likely indicates that these companies are looking for new host countries. Since a significant share of Japanese companies located in the UK are manufacturers in sectors such as that of automotive, where V4 countries have strong traditions, their relocation could be an opportunity for V4 countries. There are more than 200 Japanese companies with manufacturing activities in the UK. Based on the long-established successful cooperation between Japanese companies and V4 countries, with the appropriate investment promotion activities, some of them could be convinced to relocate to the Visegrád region.

This could be the beginning of the next wave of Japanese FDI to the Visegrád region.

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## Endnotes

- 1 For more details, see □ <https://bbj.hu/economy/finance/trade/japanese-companies-plan-big-investments-in-hungary>
- 2 For more details see □ <https://hungarianinsider.com/japanese-companies-invest-billions-of-forints-in-hungary-6333/>
- 3 According to Foreign Minister Péter Szijjártó, this number is even higher in the Hungarian case with over 160 Japanese companies. For more details see □ <http://abouthungary.hu/news-in-brief/fm-japanese-companies-have-an-important-role-in-hungarys-economic-growth/>
- 4 For more details on the data, see □ <http://abouthungary.hu/news-in-brief/fm-japanese-companies-have-an-important-role-in-hungarys-economic-growth/> (Hungary) □ <https://www.thefirstnews.com/article/about-300-japanese-firms-in-poland-investments-total-eur-25-mln---pm-20238> (Poland) □ <https://www.nihonshokokai.cz/en/> (Czechia)