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Ioanna Bella

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**Greek corporate strategies in the Balkans: The consequences of post-  
1989 reforms for investment and trade**

**Submitted for the degree of M.A by research**

**By Ioanna Bella**

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**Department of Geography  
University of Durham, June 2003**



**13 JUL 2004**

## **Abstract**

The thesis deals with the Greek business activity in response to the reforms that were initiated in Eastern Europe in 1989. The focus is on Foreign Direct Investment (FDI) as a major corporate strategy of Greek firms. The thesis attempts to explain the novel phenomenon Greek FDI. The aim of the thesis is to contribute in the understanding of the Greek FDI phenomenon, examine the nature and the process of Greek FDI, and evaluate the consequences for the Greek economy.

## **Declaration**

**I declare that this thesis results entirely from my own work, and that I have not previously submitted any material of this thesis for a degree in this or in any other University.**

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## **Dedication**

To my Father

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## 1. INTRODUCTION

The following thesis addresses the issue of the reforms in the Central Eastern European Countries (CEECs) in respect to Greece. The main aim of the thesis is to assess the impact of the reforms on the Greek economy. The thesis describes the Greek business activity in response to the reforms that were initiated in Eastern Europe in 1989. The focus is on Foreign Direct Investment (FDI) as a major economic response of Greek companies.

The political and economic reforms in the Central and Eastern European countries (CEECs) initiated in 1989, generated a new geography of economic relations in Europe. The removal of barriers that restricted economic relations for years created new opportunities and challenges for economic interaction between East and West. The consequences were expected to be significant not only for the CEECs themselves but also for Western European countries (CEC 1993, Hudson 1994, Hughes 1996). For Greece, the impact of the reforms in the CEECs is of great importance involving many opportunities but also some threats.

The case of Greece is of interest due to special geographical, economic and historical factors that operate in the area. Greece is a relatively poor, peripheral country of the EU that still appears to have problems in integrating economically within the Community. The geographical position of Greece in the periphery of Europe has always been an impediment in the economic relations of the country with the EU, and it has been considered as one of the main reasons for its poor economic performance. Specifically, Greece is the only EU country that is located at the South East of Europe, a backward region comprised of former communist countries (except Greece) with a long history of disputes over national minorities and ethnic borders.

The economic relations of Greece with these countries were limited for many years, being affected negatively by the post-1945 cold war climate. Therefore, Greece was

not only geographically isolated from other EU member states but also was missing benefits that might have arisen from economic interaction with neighbouring countries.

The reforms of 1989 have been seen as an opportunity for the country to come out of its peripherality, to restore economic relations with neighbouring countries and to deal with its regional problems as well as with the difficulties it faces in the process of the EU integration (Petraikos 1997). The opening up of the CEECs represents a new market for the Greek products and new opportunities for Greek entrepreneurs to co-operate and expand their economic activities (Dimelis & Gatsios 1995). Benefits arriving from specialisation, a more efficient division of labour and economies of scale were predicted for Greece during the early years of transition (CEC 1993).

Of specific importance for Greece has been the economic transition of the Balkan countries into market led economies. The opening up of the Balkan region represents for Greece a new regional market, where Greek producers can more easily sell their products. Greece's geographical isolation and its small domestic market were resulting in specialisation of the economy in sectors with small international potential. Now the opening of a new regional market of more than 50 million people in the Balkans offers to Greek producers the opportunity to invest and expand their economic operation. In general the Balkans have been seen as "a region of hope" (Hellenic MFA 1999). Moreover, the new conditions bring opportunities for Greek companies to co-operate with low-cost Balkan producers, to develop specialised products that could compete internationally or at least to take advantage of the cheap labour force in the neighbouring countries in order to survive in a highly competitive environment.

The opening up of the CEECs can be considered as a great opportunity for Greek exporters. Greek firms that find it either unprofitable or difficult to place their products in the EU markets could find a relatively easy outlet for their products in the CEE countries. These countries have been through a process of restructuring of their economic relations and are looking for new economic partners. Furthermore, the relative shortage of, and conversely high demand for, consumer products in the eastern countries gives the potential for access to Greek consumer good industries in these markets.

Indeed, the results of the reforms have become immediately obvious in the pattern of trade between Greece and the CEECs. This has changed remarkably since 1989, particularly the exports. The share of Greek exports to the CEECs accounted in 1989 for 3% of the total exports of the country. In 1997, the share reached 15%. Even more impressive is the evolution of Greece with the Balkan countries. On the other hand the volume of Greek exports to the EU is in gradual decline. Thus, trade with the CEECs is gaining significance in the Greek economy and many Greek producers seem to be re-orientating their trade operations towards the East (table 5-12 and 5-13)

Concerning FDI the opening of the CEECs economies signalled a new era for Greek firms contacting outward investment. Since the early 1990s an impressive number of Greek firms started undertaking FDI in the CEECs. The phenomenon was unprecedented. It is estimated that approximately 2000-3000 companies with Greek interest have set up their operations throughout the CEECs during the last 10 years. The reforms in those countries seem to have been the driving force that urged the Greek firms to follow strategies that leads to their internationalisation. Furthermore, the Greek government is adopting various measures in order to help and promote outward investment, believing that Greece can become a multinational power (at least in the area of Balkans).

However, questions arise about the alleged internationalisation of Greek firms and its potential effects on Greece. Concerns are raised regarding the nature of the firms investing, the strategies followed, their viability and the potential benefits for the Greek economy. The phenomenon of Greek FDI and its impact often has been exaggerated by the Greek media and the politicians and its real dimension is under question. It is therefore necessary to look further into the issue of Greek FDI in order to gain better understanding and avoid the myths surrounding it.

Furthermore, the prospects for economic co-operation and development should not be exaggerated, since a number of factors act in the opposite direction. First, in the Balkan countries (where the main economic interest exist) the markets are unstable and involve a high degree of risk. Political instability, uncertainty and constrained purchasing power are all impediments to Greek investment, and co-operation. Furthermore, in the Visegrad countries the economic activity of Greek entrepreneurs is, comparing to the Balkan countries, rather limited.

Overall, it can be argued that the reforms of the CEECs represent a significant challenge for Greece, raising many questions open for investigation. This thesis will focus on the Greek firms and FDI as a competitive strategy. In order to address the above issues, the chapters of the thesis have the following structure.

The second chapter is looking into the historical and political factors that influenced the economic relations of Greece with the CEECs during the cold war period and assesses the effect of the reforms. Specifically, it attempts to describe and assess the forces that determined the economic policy that was implemented during the turbulent years of the post-war world and how this was reflected in the economic relation of Greece with the countries of the Eastern Europe. Furthermore, the chapter stresses the changes that occurred in regional economic and political power in south East Europe and its implications for the Greek economic and political relations with other Balkan countries.

The third chapter focuses on FDI. The aim of the chapter is to examine the nature of foreign direct activity of Greek firms into CEECs and to evaluate the consequences for the Greek economy. The first part of the chapter reviews the theories of FDI while the second explores the question of the effects of FDI on the home and host country. Finally, the last section of the chapter, drawing from the previous theory, attempts to explain in short why Greek firms have undertaken FDI in the CEECs and what might be the possible effect for Greece as a home country.

The fourth chapter attempts to analyse the economic behaviour of Greek firms drawing from the theories of the firm literature. By using the firm as the focus of analysis, the chapter attempts to provide a deeper understanding of the process of FDI and the behaviour and strategies followed by the Greek firms. The chapter provides a thorough literature review of the theory of the firm and how the firm is related to society and place. Specifically, the chapter is looking into the economic behaviour of the firm and how this is affected by the environment where it is located.

The fifth chapter presents the secondary data available on the FDI and Trade flows between Greece and CEECs. The amount of FDI, the type of investment and the sectors are presented as well as the spatial pattern of both FDI and Trade. The chapter also attempts to make a qualitative analysis of FDI in order to explain process of investment and to evaluate its significance.

Finally, drawing from the above chapters and the empirical evidence available, the final chapter makes an overall assessment of Greek FDI in the Balkans, the behaviour of Greek firms and the the potential impact on the Greek economy.

## 2. THE IMPLICATION OF THE POLITICAL REFORMS ON THE ECONOMIC RELATIONS OF GREECE WITH THE CEECs: A GEO-POLITICAL ASPECT

### *I. Introduction*

A geopolitical analysis of South Eastern Europe would be beyond the scope and objectives of this thesis. Nevertheless, in order to achieve a broader perspective of the overall changes that took place in the region as well as a greater understanding of how those were reflected in economic relations, certain analyses are deemed to be important. Specifically, this chapter attempts to demonstrate how geopolitics affected economic relations between Greece and former communist countries before and after the reforms of 1989. The Greek FDI in the Balkans that followed the reforms could not be simply explained in economic terms. The political background that effected those economic relations is presented in this chapter.

This introductory chapter is employed to demonstrate the geo-political context within which the economic relations between Greece and the Balkan countries were shaped and to observe the underlying political considerations that influenced those relations before 1989. Through this chapter it is argued that the geopolitical position of Greece, a western ally surrounded by former communist countries, deprived the country from the expected economic relations with neighbouring countries. International politics, Cold War climate and divisions of East and West, together with internal politics, consecutive wars and disputes over borders and ethnic minorities in south east Europe, were negatively influential with respect to the economic relation of Greece and the CEECs.

If not for any other reason, due to its geographic proximity, Greece should have been expected to develop strong economic relations with its Balkan neighbouring countries (see chapter 5 gravity model). From the perspective of regional theories, there were

several factors conducive to cooperation in South East Europe. Yet, political obstacles were offsetting those potentials. It was not until 1989, a sudden break with the past, that the political barriers preventing close economic relations would fall. The reforms that initiated in 1989 in the CEECs significantly improved the relations between Greece and Balkan countries and set the ground for economic activity to take place.

An attempt will be made to describe and assess the forces that determined the economic policy that was implemented during the turbulent years of the post-war world and how this was reflected in the economic relations of Greece with the countries of Eastern Europe. This task is complicated by the fact that economics and politics became very closely interwoven. Political considerations and external influences were important factors determining the economic relations of Greece with the rest of the countries.

The chapter follows the following structure. In the first section of the chapter the focus is on the geopolitical position of Greece after the end of the Second World War and the struggle of the so-called great powers to incorporate her into their respective spheres of influence. The important element of this section is the attempt it makes to examine the economic consequences that this had for the country - especially with respect to its relations with the CEECs. The basic argument is that the incorporation of Greece under the western sphere of influence determined to a great extent the economic process of the Greek economy and deprived her for developing close economic relation with its natural hinterland; the Balkans.

The second part of the chapter describes in greater detail the economic relations of Greece with the Eastern European countries during the period 1950-1989. The above period will be subdivided into smaller ones, with greater political cohesion, in order to enhance understanding. The early years immediately after the end of World War II are not analysed because of a lack of reliable sources. Emphasis is placed on the trade relations of the country with Eastern Europe and how they evolved during the Post War period.

Finally, in the third part an assessment of the present situation is made in view of the reforms in the CEECs. This section describes the new conditions, assesses the Greek response and comments on current possibilities and/or opportunities open to Greece. A significant aspect that is stressed in this section is the significant changes that occurred in

the economic and geopolitical sphere of influence in the Balkans during the post war period (Constas and Papisotirou, 1999). Greece, during the last decades has followed a very different developmental path compared to its Balkan neighbouring countries. Today, she is considered among the most developed countries of the world. Greece, after some turbulent years, succeeded in establishing a stable democracy and eventually in joining the EU while the other Balkan countries established different types of communist regimes. Through this trajectory Greece developed economically much more rapidly than any of her Balkan neighbours. Notably, while Greece's GDP in the 40s was less than that of Bulgaria, today it is higher than the sum of all Balkan GDPs combined. Furthermore, Greece, being a member of the EU and having established a long-standing democracy, is considered a significant actor in international relations, promoting democracy, human rights and stability in the entire region. This economic and political advancement of Greece over the other Balkan countries enables it to play a significant economic and political role in the South East Europe. Furthermore, this upgraded economic and political role of Greece created new conditions under which Greek firms could operate, invest and trade with CEECs from comparatively advantageous positions.

## ***II. Post-war Greece: internal conflict and external intervention***

### ***II.1 Greece and the Division of Europe***

After the end of World War II the whole map of Europe was redrawn. The European continent came to be divided into two political and economic zones; the Eastern and Western. Greece was caught in a peculiar position. In a time when East and West were distinctively and clearly separated into two political and economic blocks, Greece found itself somewhere at the crossroad. Although geographically located in the South-East of Europe, in the Balkan Peninsula, it was at the same time a political and military ally and economic partner of the West. Within this segregated Europe, Greece after some turbulent years of struggle and ethnic division was finally assimilated by the Western block. Unlike Greece, the rest of the south-eastern European countries like Albania, Bulgaria, Romania and Yugoslavia fell under the eastern block and adopted a Soviet type

of command economic system. Therefore, Greece during the years of the cold war period was considered a strategic part on the anti-Communist fight of the U.S. against the expansion of the USSR. . The economic policy and the relations of the country were strongly influenced by this factor. Therefore, Greece limited its relations with the east and was more closely related to the Western Europe.

The fact that Greece came to be considered under the Western sphere of influence was of extreme importance for the future of the country. Greece during the war had been a Western ally, and it was meant to remain after the end of the war. Britain, having a long legacy of influence over Greece and a strong interest in the area, was determined to keep Greece under its influence and control. The problem for her plans strangely enough came not that much from Stalin, who agreed with Britain taking other countries under its influence as a reward, but from a strong internal leftist partisan movement that was created for resistance purposes in Greece during the occupation. Thus, while the war ended in the 1944 Greece did not find a peaceful solution to its various political economic and social problems. Political order and economic stability did not arrive immediately. On the contrary, the country entered a turbulent period that was soon escalated and ended up into a devastating Civil War. The Great powers played a very important part in this. No doubt the role of the great powers was magnified by a very old Greek political habit of seeking patrons in the struggles for power at home.

## ***II.2 The British influence***

Greece, since the movement of independence, in 1821, has been under the sphere of British influence. Britain played an important role in the country's fight of independence and ever since was exercising a significant degree of influence over the country's issues. Under those conditions Greece was one of the countries that it looked very natural to come after the war under the western block and under Britain's hegemony.

However, by the end of the war the control of most the country was under armed communist led partisans that had fought against the Germans during the war and they were enjoying much popularity among the Greek people. The Peoples Liberation Army

(ELAS), the strongest resistance movement, was controlled by communists and therefore it was a potential threat to British plans. Thus, this movement had to be stopped. Stalin after an agreement he had with the British government did not intervene and on December 1944 did nothing to help them from the British gunfire.

Specifically, after the end of the war the great powers made a crude divide of Europe into two separate spheres of influence. Churchill had a strong interest in Greece and he wanted by all means to keep it under his control. Churchill and Stalin reached an agreement in May 1944, that Greece would become a British "sphere of operation". Britain, gained 90 percent of influence over Greece while the soviets gained 80 percent in Hungary and Bulgaria, 90 percent in Romania and 60 percent in Yugoslavia.

However, by the summer of 1944 the Greek Communist partisans were close to the point of forming a (Yugoslav style) national Liberation government. They had the military power and the popular support that would allowed them to attempt it with good chances of success. The reason for their final decision to co-operate with the government in exile it is argued came from their compliance to followed Moscow's commands (Swain, McNeil). Stalin ordered that they should come to terms with the British-supported exile government in Cairo.

On 1944 British troops arrived in Greece. However, a clash did not take long to come and indeed a bloodshed confrontation with the communists started on December 1944 (Dekembriana) when Papandreou ordered their disarmament. Great Britain assisted the anti-communist forces and successfully defeated the National Liberation front, EAM, the political arm of the communist-guerrilla resistance movement. Stalin did nothing to prevent it. Churchill was the first to admit, "Stalin did fulfil his pledges with respect Greece...without lifting his finger he allowed the British to massacre the ELAS partisans who were led by Greek communists". Stalin probably expected the same generous response from his allies concerning his sphere of interests.

After the Athens revolt, "Dekembriana", the British government assisted in the formation of "Service governments" in Athens. These transitory governments were designed to quell the communist threat while giving the royalist forces time to consolidate and prepare for restoring the King (George II). The governments, however, tolerated

violence against the leftists. A certain group of right-wing gangs and paramilitary organisations launched a wave of “white terror” tactics that was directed against the leftists. That was taking place with the encouragement of the British authorities in Greece, which were partly responsible for provoking the Civil war in 1946-1949. British and soviet geopolitical interest were thus realised by exporting civil were to Greece. (Berend,1996)

While the Greek Communist party’s policies were also to blame for the fateful conflict, there is no doubt that most of the republican and monarchists parties did not have a propensity towards compromise and deliberately sought confrontation. Finally, the cold war policies in the Greek political arena exacerbated the tensions and contributed to the polarisation of the country during the three decades after the liberation (Stavrianos,1989).

Under the above situation, lawlessness and intimidation of communist, on March 1946 held election which turned out to be a victory of royalist and conservative politicians. In Spring 1946 Stalin became convinced that the era of war-time co-operation with Britain and the United States was over and that newly formed United Nations would become a forum for confrontation rather than co-operation. His response, with respect to Greece was to ask on September 1946, the Yugoslavs to step up support for the Greek communists in their nascent civil war against the British supported Greek government. However, he was still unwilling to commit himself fully to such confrontation, and by December of 1946 Soviet aid to the Greek communists, though promised, had still not come (Swain Geoffrey and Nigel Swain).

On the other hand, the Balkan communist states were offering military aid to the Greek partisans. Yugoslavia, under Tito’s government, had started an active campaign to establish an international aid network for Greek communists. Tito however was acting under his own initiative and without consulting Stalin. One of the main plans that Tito had in mind was to create an independent state of Macedonia that would include part of the Greek as well the Bulgarian Macedonian. However, Stalin, who made clear that he would not accept an independent foreign policy formulated by Yugoslavia, did not like this act on behalf of Tito. Stalin, first of all had promised Greece to the British and

furthermore he could see the Americans being increasingly involved into the Greek dispute. Therefore he was not willing to go into a serious confrontation over this issue.

Thus, Stalin's limited support for the Greek communists ended without result. At this time due to the weight of the primarily economic problems they were facing in their colonies, the British decided to withdraw, and the Americans took over.

### ***II.3 The American intervention***

After 1947, when the British were unable any longer to sustain the financial burden of control over Greece, the Americans undertook the above task with significant implication for the political and economic developments of the country.

Undeniably, after the end of the disastrous World War II, Greece needed urgently some source of financial aid in order to meet its basic needs. The economy was threatened collapse and the Greek government, royalists, (1946) was seeking for assistance from outside. Greece had been a wartime ally and much of the problems of the country were the immediate cause of the war. So naturally, it was seeking assistance from its western allies. The Greek government in order to achieve its target was using the communist threat as a useful device in order to extract foreign aid. Characteristically, Tsaldaris warned Greece's (western) allies in an interview in Paris "Greece is surrounded by the occupying armies of communism and her internal economic and social structure cannot continue to exist without outside aid...." (Kofas, 1989, p.55)

At the same time United States preoccupation with Greece was very much related to its anti-Soviet campaign. Greece constituted the western part of the "Northern Tier", which was a strategic belt that included Turkey and Iran and was preventing USSR from expanding<sup>1</sup>. The country was useful as an outpost of the anti-Soviet camp. It was the only Balkan country that was not assimilated in the Soviet block. Therefore, the country was considered of strategic importance for the strategic plans of the U.S.

The United States were determined to prevent the expansion of the USSR's influence in Europe by whatever means were required. At that time the means that were envisaged

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<sup>1</sup> This was based on the Domino theory of the U.S foreign policy. Greece and Turkey were considered front-line states; if they fell, then Europe would also fall (Short R J, 1993).

were more political and economic rather than military. The United States were willing to launch a new era of close commercial and financial relations in exchange of establishing close diplomatic and strategic ties with Greece. Under those circumstances on 11<sup>th</sup> of March of the 1947 Truman declared to the congress that the U.S. had to “support free peoples who are resisting attempted subjugation by armed minorities or by outside pressures” He suggested economic assistance to assure “economic stability and orderly political process...”.

However, it is argued that although the American involvement in Greece initially was conceived as a program of financial support its emphasis shifted its emphasis on military and security issues (Iatrides, 1999).

#### ***II.4 The economic dimension***

Ever since the war of independence, there was a large degree of British involvement in Greece's economic affairs. The immediate result was a lender-borrower relationship. Consequently, Britain had developed many economic interests in Greece that she was not willing to lose.

Greece also became an aid recipient and a client country of the U.S. after 1947 (Kofas, 1989). The American mission for aid in Greece wielded considerable degree of influence in a wide range of economic matters of the country.

A program of reconstruction started to take place in 1948, four years after the liberation, with the influx of economic aid from the US. However, it is argued that the broader lines of this developmental plan was very much affected by the main idea of the Marsall Plan which looked Western Europe and the United States as an economic block separate from Central and Eastern Europe and the Soviet sphere of influence. Therefore, the development program that was formulated in 1948 was aiming to direct Greece's trade with Western Europe and the United States (Thomadakis, 1995).

On the other hand, the USSR undertook the formation of an economic block by linking the Eastern European economies to it through a network of bilateral trade agreements. The Council for mutual economic assistance (CMEA, or known as Comecon) was the

organ that was formally established in 1949. On the side of the Soviet-type socialist economies the foreign trade behaviour was determined by the policy of 'Block' autarky<sup>2</sup>.

This separatist behaviour from both blocks however, would deprive Greece for many years from developing economic relations with its natural hinterland; the Balkans.

### *III. Economic Relations of Greece with Balkan countries before 1989*

Due to its geographical proximity, if not for anything else, Greece was always a potential trade partner for the countries of the CEECs and especially South Eastern Europe. However, as long as cold war politics determined their external relations this potential could not be fully explored. This section demonstrates how the political climate was affecting the economic relation of Greece with the East during the post-war period. In order to achieve a better understanding the above period is divided into five smaller ones that each one represents relative homogeneity in terms of the political and economic conditions of Greece. The period immediately after the World 40s is not analysed due to lack of sufficient and reliable data.

In general, trade with Eastern Europe has always been of great importance for the Greek economy. Greece ranks among the first EU countries as to the weight of Eastern Europe in its total foreign trade. However, its economic relations fluctuated during the post war period according to the political climate. The share of Greek exports to Eastern Europe reached its peak in 1966, under the political détente climate, they accounted for 29% of the total foreign exports of the country and 10% of the imports. During the military, anti-communist regime in Greece (1967-1974) the proportion decreased considerably (1974:16% exports and 6% imports), while during the period 1975-1980, with the restoration of democracy, there was a stabilisation in trade relations between Greece and the Eastern countries. In 1980, on the eve of Greece's accession to the EC the Eastern countries accounted for 11.3% of the country's exports and 9.5% of the imports (both the percentages were the highest among the EU) (Table. 1, Wallden, 1988). However,

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<sup>2</sup> According to the 'bloc' autarky policy the Comecon members were supposed to seek suppliers within the block first.

Greece's accession in the EC (1981) and the economic crisis in Eastern Europe had as a result a considerable deterioration of economic relations.

It was only after the removal of the Iron Curtain and the introduction of measures for political and economic liberalisation when major changes were initiated in the economic relations of Greece and the CEECs.

### ***1950-1967***

During the period of 1950s and 1960s the trade relations between Greece and the CEECs were of significant importance in the economic and political situation of the country. The CEECs were important export markets for the Greek products. That was happening because of the structure of Greek exports. Exports consisted almost exclusively of agricultural products and raw materials, tobacco and raisins constituting almost half the total value. The East European countries proved to be easier export markets for the Greek products comparing to the Western markets where the demand for those products was limited and that was accompanied by strong competition. Therefore, the Eastern countries were of vital importance for the trade balance of the country.

The dependence of Greece by those countries for its agricultural surpluses urged the re-establishment of economic relations between them. That happened in spite of the strong anti-communistic atmosphere that prevailed in Greece after the Civil war. In fact it was Greece and Poland were the countries that first signed the East-west trade agreement within the framework of the ECE consultations in 1952 (Wallden, 1993).

The economic relation of Greece and the East was very much a political issue and it was dominated by political and security considerations. However, although the government in power was conservative and hence strongly anti-communist, with respect to trade policies they dealt with a "business" attitude. At the same time the left parties were trying to take advantage of the situation by arguing that trade with the east was the solution to the country's economic problem.

The economic cooperation with neighbouring Balkan countries was more complicated. Deeprooted historical issues and classic Balkan conflicts proved a quagmire in relations. Specifically, the economic relations between Greece and Yugoslavia were very much

influenced by the Macedonian<sup>3</sup> issue. Thus, although re-approchement between Greece and Yugoslavia was very much supported by the Allies, Athens was reluctant to deepen economic relation because of political issues. As far as Albania was concerned, economic co-operation and trade were almost not existent. Albania, after moving to China sphere of influence adopted a very strict isolationist policy. Furthermore, the presence of Greek minority in the south was an issue which was creating a further tension between the relation of the two countries. Relations with Bulgaria and Romania were normalised evidently in response to Western “bridge-building” tactics. Overall, Cold War tension and pending bilateral issues were preventing economic relations and co-operation from flourishing in the Balkan Peninsula. It was only in mid-1960s after the change that occurred in Great Powers policies that relations start to improve.

#### ***1967-1974***

During the period 1967-1974 Greece entered a ‘black’ period, being under a military regime. The policy followed was in line with the previous one: anti-communist alliance with the west and economic and political integration with Western Europe. The situation however was more complicated due to the nature of military regime that was ruling the country.

Europe did not approve the military regime since the beginning and its disapproval and the reactions got stronger in the course of time. On the 12 December 1969, Greece was indicted before the council of Europe and was expelled from the council. In the meantime, the European Economic Community executive had decided to withhold the balance of a development loan. Overall, military junta did not enjoy full approval in the Western Europe and in the United States a large body of public opinion was morally and

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<sup>3</sup> The end of the World war followed a devastating Civil War. The war ended in 1949 with the defeat of the communist supported democratic army. After the end of the Civil war many of the communist, both civilians and partisans, fled to Yugoslavia and Bulgaria and the borders with those countries were sealed. Furthermore, Yugoslavia, which was actively supporting the communist partisans during the whole Civil war had territorial claims over Greek Macedonia because of an alleged Macedonian minority that was leaving in the area.

politically against the military regime. Under those conditions Greece seemed that was losing its 'natural' friends and allies: the Western Europeans.

Paradoxically, the Eastern European countries recognised and did business with the regime since the beginning of the establishment of the regime. Good relations between Greece and the Eastern countries were soon established and visits of the foreign ministers of Bulgaria and Yugoslavia foreign minister and the Romanian prime minister were made to Athens. In June 1971 the Greek minister of commerce visited Bucharest. The Eastern countries and mainly the Soviet Union saw an interesting possibility developing by the regime: to increase their influence in an important strategic area. Therefore, the relations between Greece and Eastern countries seemed to be based on a non-ideological, pragmatic type of international economic relations.

Two explanations are given for this attitude of the Greek Junta by Xydis AG(1972). The first was related to the disapproval that the regime was facing by the West. The regime needed both domestic and international approval and since it could not have this from the West it was seeking it from Eastern Europe. By the same line of thought Junta was using these relations from the communist countries in order to counteract the pressure it was facing by the West for restoration of democracy. Furthermore it could be used as a hint of blackmail towards the Americans that Greece might move away from NATO and closer to political co-operation with the Soviets. At the same time, in this way the regime managed to maintain commercial exchange at a satisfactory level, which was reached before the coup, and to obtain important investments from the Soviet Union and the German Democratic Republic.

In the Balkans too, some progress was made. Greece strengthened her ties with Yugoslavia and paved the way for a settlement of all differences outstanding since the World War II with Rumania and Bulgaria<sup>4</sup>. Economic co-operation was developed and institutionalised in sectors such as tourism, water management, transport, etc. With Albania relations were normalised in 1971, although the Greek minority that was leaving in the southern Albania remained to be a source of tension.

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<sup>4</sup> Those developments must be seen in the wider context of a period of détente (1964-late 1970) between the great powers that allowed improvement of the international relations.

However, a closer look into the relation of Greece both with West and the East reveals another picture. First of all it appears that there was a gap between the rhetoric and the action of the Western countries regarding their disapproval of the Hunta. This is reflected in the trade and the investment flows between the two partners. Indicative, while in 1966 the exports of the EEC countries to Greece worth 485 million dollars, by 1969 the amount of exports reached the 610 million dollars, comprising 43% of Greece's total imports. The other western countries increased their exports to Greece at a rate of 49% during the same three-year period. Furthermore, the exports of the United States increased substantially since the military took over. (Treholt A, 1972). On the other hand the proportion of the trade with the Eastern countries dropped significantly: in exports from 28% in 1966 to 16% in 1974 (table 1). It has to be stressed however that the above figures was not just the results of the economic policy followed by the regime but also the results of the structural changes initiated in the early 1960s in the Greek economy and its exports. Indeed, after 1966, several new export-oriented industrial units started operating, thus boosting Greek industrial exports to the West and reducing the relative importance of agricultural exports.

### ***1974-1980***

The restoration of the democracy in 1974 and East-West detente contributed to an amelioration of the political and economic climate in Greek-East European relations. Although Greece's main objective during that period was to enter the European Community it also pursued an active 'ostpolitic'<sup>5</sup> both in the Balkan region (particularly during 1975-76) and in the other eastern countries (mainly during 1977-78).

In terms of trade, the economic relations with Eastern Europe expanded. During 1977-1978, anticipating EC accession but also responding to pressure by Eastern partners, Greece agreed to abolish the clearing agreements with Yugoslavia and the USSR. On the whole, the downward trend of eastern Europe's share in total Greek trade started, but this

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<sup>5</sup> The term was used to describe the policy that was followed by west Germany during 1969-1974 and which was aiming in the termination of the cold war climate and the establishment of good relation between East and West.

was due to rising imports (mainly because of oil crisis); eastern Europe's share in exports further dropped from 16% in 1974 to 11 percent in 1978".

In mid 1970s there was an increased desire on the part of Greece to improve and expand its economic relation with its Balkan neighbours. That was driven by an ambitious image of Greece as a "bridge" from east and Southeast Europe to the Middle East and Africa. "However, deterioration of the economic conditions, both in Greece and the Eastern countries, doubts as to the economic feasibility, and political second thoughts related to underlying potential conflicts particularly with Yugoslavia, resulted in a gradual change of mood, and most of the projects were abandoned in practice"(Wallden, 1993)

### ***1980-1989***

In the 1980s many important events altered the economic relations of Greece with Eastern Europe. The most important factor may have been the accession of Greece in the European Community. That had as a result an alteration of the economic policy of Greece. The second factor was the economic deterioration of the economic situation on in Eastern Europe during the same period.

The accession of Greece in the EC had as a consequence the abolishment of all the bilateral and clearing agreements that had established during the previous years with the eastern countries. That had as a result the economic relation with those countries to become more difficult. As far as imports with CEECs were concerned, those became more difficult to implement and Community rules and pressures imposed their replacement with EC ones. For example, the inclusion of Greece in the common agricultural policy entailed a costly diversion of meat imports from Yugoslavia and other European suppliers to community suppliers. That had some negative consequences to the country's bilateral balances<sup>6</sup>.

As far as exports with CEECs were concerned, those were also hampered by the economic crisis that hit those countries in the 1980s. This proved to be a serious impediment and constrained the Greek exports towards those countries since the Greek export products were not of first priority. Overall, Greek trade with Eastern Europe

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<sup>6</sup> Although some Greek agricultural exports to eastern countries profited from CAP subsidies.

declined considerable during the 1980s. Eastern Europe's share in Greek foreign trade fell from 8.6 percent in 1979 to 6.4 percent in 1989.

Another determining factor for the Greek relation with East during the above period was the accession of PASOK (socialist party) in power in 1981. The PASOK government diverged its policy form that of the rest of the community and NATO: it opposed economic sanction and on the contrary pursued close relations with The Eastern European Countries. In general PASOK's philoshophy in economic policies were not in line with that of the European Community. However, despite the political will the attempt did not bear great results in purely economic terms. Nevertheless, its economic policies that implemented, particularly before 1989, had important consequences for the country's relations with Eastern Europe.

However, it is only after the collapse of the communist regimes and the fall of the "iron curtain" when Greece emerges as a major economic partner. Greece indeed after 1989 emerged very dynamically as an important economic partner of the CEECs offering very good potential for economic relation and co-operation.

**Table 1-** Eastern Europe's share in total Greek trade

<i>Year</i>	<i>% Exports</i>	<i>% Imports</i>
1950-1954	6.1	1.8
1955-1959	15.8	8.2
1960-1964	25.8	10.2
1965-1969	24.0	10.0
1970-1974	17.2	6.6
1975-1979	13.5	8.1
1980-1984	10.3	7.2
1985-1989	6.5	6.7

Source: Wallden (1993), National Statistical Service of Greece (NSSG)

#### *IV The present state: Greece in a changing geopolitical scenery*

##### *IV.1 The Reforms and the Opportunities*

Since autumn 1989 the former socialist countries initiated a number of political and economic reforms in their effort to be transformed into a western type, market led economies. The “Iron curtain” fell, the Cold War was over and the obstacles for economic co-operation between the Western and Eastern countries seemed to have been gone for good. Thus, the transition of the former socialist countries opened up a new era of potential collaboration and mutually beneficial economic relations between the countries of the East and the West.

For Greece, the demise of the communist regimes and the reforms that initiated in 1989 in Eastern European countries has significantly altered the picture. It offered an opportunity to re-establish historical, economic and trade relations that during the post-war period experienced significant shrinkage. Furthermore, Greece emerged as a state that could play an important political role in the remote corner of South-East Europe. Greece was ideally placed within the Balkan region. Its position in the international community, member of the EU and NATO, and its long established democratic institutions constituted an important advantage over the rest of the South-eastern neighbours. Greece could become the “bridge” between the Balkan countries and the EU as the only EU member in the region. Also it could be a stabilising agent in the volatile area of the Balkans. Therefore, Greece since the early beginning of the reforms, envisaged playing a very strong political role in the area of South-Eastern Europe. According to the Minister of Foreign Affairs of Greece Mr. Papandreu Greece, being at the same time a Balkan and an EU member deserved a leading role in the political and economic reconstruction of the Balkans.

Another important factor is the upgraded position of Greece in the area of Southeast Europe. It is striking the change that occurred in the regional balance of power in the Balkans during the cold war (Constas D and Papatotiriou, 1999). Greece, appears to be in a superior position comparing to those countries that fallen under communist regimes in both economic, political and military terms. The magnitude of the structural changes that

occurred becomes evident by comparison to the Balkan balance of power before and after the cold war. In the 1930s Greece's economic development was very similar to those of Bulgaria, Romania and Yugoslavia. In the 1990s, by way of contrast, Greece exceeds by far all other Balkan countries added. Notably, Greece's GDP alone is greater than the GDP of all the Balkan countries. Thus, Conostas and Papasotiriou (1999) maintain that those changes in the structural conditions presented major opportunities for Greece to predominate in the Balkans (Conostas and Papasotiriou, 1999).

However, it should be mentioned that together with the opportunities that appeared with the reforms, Greece was also confronted by many serious political problems. The proliferation of new states, the reappearance of claims of numerous national minorities and disputes over national borders were all issues the Greece had to deal with. Some of the reactions and measures that were implemented, especially the first years after the reforms, have gone under scrutiny and they have been criticised for isolating the country instead of allowing her to play the role that was envisaged<sup>7</sup>. Nevertheless, the relations of Greece with the other Balkan countries are improving and a framework of good neighbourhood has been established.

#### ***IV.2 The Greek policy in the Balkans***

The recent Greek policy in the Balkans moves along two main lines: a) towards integration of the Balkans into EU and NATO b) towards promotion of interregional cooperation in the area (Ioakimidis, 1999).

The Greek government has recognised that the country has significant interest from the integration of Balkan states into the European Union. The successful integration of the Balkan area into the European structures is of strategic importance to Greece, since it will provide its northern neighbours with the possibility of finding themselves in the same

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<sup>7</sup> The most controversial issue is that of "Macedonia". The Greek government did not recognize the newly formed state now recognized as "Former Republic of Macedonia" under the name "Macedonian" and imposed an embargo towards the new established state despite the disagreement of the European Union. Furthermore, Greece's stance towards Serbia's reaction over the autonomist attempts of other nationalities during the turbulent years of the split of the former Yugoslavia has been criticised by the international community.

geopolitical area for the first time since the second World War. Furthermore, the economic integration of the countries of South East Europe will greatly contribute to the well-being and prosperity of the area and of Europe as a whole. If the Balkans remain at the margins of European developments, then the prospects of further destabilisation in the region is increased (Ministry of foreign Affairs, <http://www.mfa.gr/foreign/year99/southeur110399.htm>)

Integration into the EU is seen as a powerful factor capable of contributing decisively to consolidating stability, democracy, and prosperity in the region. Greece as a member of the European Union in the Balkans has the opportunity to bring the countries of the region into trans-European networks and projects facilitating economic change and development. Wallden (1999) argues that a marginalised Balkans will contribute in the marginalisation of Greece on the fringes of Europe.

Inter-Balkan co-operation is the second major objective of the Greek government. Greece has realised that its future in the Balkans lies in regional co-operation schemes. Efforts are being made in order to facilitate the process of “physical integration” between Greece and East and particularly its Eastern neighbouring countries. Joint ventures, infrastructure improvements and expanding trade finance and services are tools that are used towards this aim. Overall economic relations with the east are thought to bring prosperity and also to contribute in the stabilisation and peaceful coexistence of the area of the Balkans.

In 1997, in a meeting in Thessaloniki the Balkan countries set out very clearly the principals and the objectives of international co-operation: a) enhanced political co-operation b) Reinforced economic co-operation c) Promotion humanitarian, social and cultural co-operation and finally co-operating in the field of criminal justice.

The Greek government, in order to enhance prospects of economic development and co-operation with the Balkans initiated a number of supporting policies to support trade and investment, implementation of co-operative schemes in the fields of transport, telecommunications, energy, infrastructure, small-and medium size enterprises, technology and cross-border Cupertino.

Greece at the same time is actively promoting all initiatives for multilateral co-operation in the region. These include the European Union’s PHARE and INTEREG programmes,

the US inspired South east cooperative initiative and the Black sea Economic cooperation.

In this context, Greece has also drawn up the Second 5- Year Program of Hellenic Development Aid for the period 2002-2006; an important part of this program, is the Hellenic Plan for the Economic Reconstruction of the Balkans (HiPERB).

The HiPERB, which was adopted by the Hellenic Parliament in March 2002, is the first effort made by Greece as a donor country to incorporate various separate development aid initiatives into a single comprehensive plan so as to promote an integrated development policy. The HiPERB is a five-year development aid programme in the total amount of 550 million Euros (Table 1-2), that undertakes the financing of projects, investments and activities in 6 Balkan countries, namely Albania, Bosnia and Herzegovina, Bulgaria, the Federal Republic of Yugoslavia (Serbia and Montenegro), the Former Yugoslav Republic of Macedonia (FYROM), and Romania. ([http://www.mfa.gr/english/foreign\\_policy/hiperb](http://www.mfa.gr/english/foreign_policy/hiperb))

**Table 1-2** Financial aid according to the HiPERB, million Euro per country

<i>Countries</i>	<i>2001</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>Total</i>
Albania	5.99	9.97	12.47	11.48	9.97	49.89
Bulgaria	6.51	10.85	13.57	12.49	10.85	54.29
FYROM	8.98	14.96	18.71	17.22	14.96	74.84
Romania	8.45	14.08	17.61	16.20	14.08	70.43
FRYugoslavia	51.35	47.24	45.19	30.82	30.82	205.43
Bosnia-herzegovina	18.34	16.87	16.14	11.1	11.1	73.37
Total	99.62	113.97	123.69	99.31	91.78	528.25
Extra						21.75
<b>Total</b>						<b>550</b>

Source: Economic review, June 1998

## *V Conclusion*

This chapter adopted a geopolitical approach in order to demonstrate the magnitude of changes and the opportunities that were initiated in 1989 for the Greek economy. Through the chapter it is shown how Greece's geopolitical position, somewhere in the crossroad between East and West, affected its economic relation with the CEECs. The incorporation of Greece within the western block inevitably oriented its economy towards the Western countries and separated her from the Eastern Block. Thus, despite that Greece was expected and was on her benefit to develop close economic relation with its neighbouring Balkan countries, this was restricted by the separatist behaviour that was prevailing in both blocks during the years of cold war. Therefore Greece, for many years was deprived from benefits that accrue from regional economic co-operation and trade.

1989, brought a new era were those barriers fall and opportunities were created. Those changes took place in a time where the political and economic power in the region had change significantly. Greece, appears to be in a superior position comparing to the countries that fallen under communist regimes in both economic, political and military terms. This economic and political advancement of Greece over the other Balkan countries gives her the opportunity to play a significant economic and political role in the South East Europe. Furthermore, under those conditions, Greek firms could operate, invest and trade with Balkan countries from a comparatively advantageous positions.

Overall, it could be argued that the political changes that were initiated in 1989 had a great impact on the economic relations of Greece and Eastern Europe. The above year has been a breaking point with the cold war climate that was preventing close economic relations from developing between a 'western' ally and communist countries. Since, 1989 a new era of economic relations has been initiated between Greece and East Europe with great expectations especially on the part of Greece.

The following chapters will attempt to demonstrate how the wide opportunities that opened for Greece with the momentous events of 1989 are underscored by the economic performance of the Greek entrepreneurs. In the following chapter the focus is on FDI.

### **3. THEORIES OF FOREIGN DIRECT INVESTMENT: THE MOTIVES OF FIRMS ENGAGING IN FDI ACTIVITIES AND CONSEQUENCES FOR THE HOME COUNTRY.**

#### ***I. Introduction***

The aim of this chapter is to examine the nature of foreign direct activity of Greek firms into CEECs and to evaluate the consequences for the Greek economy. In order to do that it is necessary to determine the criteria under which foreign direct investment (FDI) decisions are taken and the conditions under which home countries are benefited by FDI. Therefore, the chapter will focus on established theories on FDI.

The chapter is divided into three main parts. In the first one a short review of the theories of FDI is presented. The second part explores the question of the effects of FDI on the home and host countries and the different theories and opinions are discussed. Finally, the third part of this chapter attempts to apply the above theories in the case of Greece. Drawing from the first two theoretical sections the third will attempt to shed some light onto the question of why Greek firms have undertaken FDI in the CEECs and what might be the possible effect for Greece as a home country.

#### ***II. Review of theories of FDI***

One main issue that has to be explored is the reason why firms undertake FDI. There are several strands of theories that attempt to explain the phenomenon. However, the task to present analytically those theories would be well beyond the aim and limits of this chapter. Nevertheless, a brief consideration and presentation of some of the most significant theoretical efforts is necessary for our understanding and it will follow in this section.

The concept of FDI, as we understand it today<sup>8</sup>, did not emerge suddenly, rather it developed as a result of a long process. It took a substantial time until a specific theory was built to explain explicitly FDI. Originally FDI was simply reduced to a variant of international capital and was explained by capital movement and trade theories. Specifically, it was not until the 1960s when a substantial body of theory emerged attempting to explain FDI at a time when FDI experienced an unprecedented increase.

Capital movement explanations accounted for foreign investment simply on the basis of higher rates of return abroad. Classical theory suggests that international capital movements are due to the differences in interest rates among countries. Therefore funds will flow from one area where there is abundance of capital and low interest rates to areas of capital scarcity where interest rates are higher. However, the above theory, while adequate to explain portfolio investment, was not appropriate for direct investment. At the same time traditional trade theory had little to contribute to the subject (Gilpin, 1987).

Hymer (1976) argued that the orthodox international trade and capital movement theories do not explain FDI. In particular they are insufficient to explain two-way FDI flows through countries and even more between countries with similar product factors. More than that, Hymer brought the firm in the central focus of his theory. His explanation of why firms undertake FDI was based on the theory of the firm and industrial organisation. Hymer argued that firms that undertake FDI should possess some kind of firm-specific advantages (which could offset the advantages held by indigenous firms) (Hymer, 1976). Such advantages were essentially those of firm size and economies of scale, market power and marketing skill (for example, brand names, advertising strength), technological expertise (product, process or both), or access to cheaper sources of finance. Since then many different theoretical frameworks emerged in the search for an appropriate explanation of FDI. Some of the most important are reviewed below.

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<sup>8</sup> “ ‘Direct investment’ is defined as the investment by one firm in another with the intention of gaining a degree of control of the firm’s operations. ‘International’ or ‘foreign’ direct investment is simply direct investment which occurs across national boundaries”. The distinction with the ‘Portfolio investment’ lies in the control of the investment. In that case the firm purchases stock/shares in other companies purely for financial purposes; but it does not gain the control of the foreign enterprise (Dickens 1992, Hymer, 1976).

## ***II.1 Product life cycle***

Product life cycle theory was developed by Raymond Vernon in 1966 and it was successful in explaining the early overseas investment of (mainly) American corporations. Vernon's contribution was to introduce a locational aspect into the product cycle that in the original form had no spatial connotation at all.

The product life cycle theory suggests a model to explain the evolution of international production. According to this theory the pattern of international trade and investment are very much influenced by the life cycle stage of a firm's products or processes. The life cycle of a new product progresses through three stages: a) the introductory or innovative phase, b) the maturing or process-development phase and c) the mature or standardised phase (Giplin, 1987). According to the theory different types of economies are better equipped to stage a specific phase of the production and therefore the firm decides to produce in the home or host country or export accordingly.

Specifically, during the first stage of the product firms choose to innovate in their home country, which is most likely to be an industrialised country. That can be explained both by the rich technological research capabilities acquired by those countries as well as from the greater demand for innovative products. Furthermore, at this early stage of production there is no price competition that could urge the company in search of low cost location. Production can therefore take place near the site of product development and research, where the production process can be monitored and adjusted (Czinkota, 1992).

During the maturing stage exports to other countries expand rapidly. At the same time attempts to break the monopolistic position of the innovator firm erupt from home firms and other industrialised countries (Taoka, 1991). The innovator firm might face strong competition as it becomes subject to quotas or tariffs and supply increases by local producers. As a result of this competition, prices are falling and an effort to reduce cost is made by further improvements in the method of production.

Eventually in the final, mature phase, firms begin to replace their exports with local production to avoid import barriers imposed by the host governments, transportation cost and in order to protect the foreign market. This will lead to licensing agreements or joint

ventures with firms in the foreign country, or to wholly owned investments (Taoka, 1991).

The product cycle theory applied best to FDI in manufacturing, the early overseas expansion of American corporations, and what is called 'horizontally integrated' investment, that is, the establishment of plants to make the same or similar goods everywhere. However, since the end of the Second World War several important changes have taken place that the theory could not explain (Gilpin, 1987).

### ***II.2 Oligopolistic-Monopolistic advantage***

Other theories emphasised on the oligopolistic or monopolistic advantages of the multinational corporations. Those advantages were assumed to overcome the disadvantages faced by MNCs when they go to an unfamiliar foreign market. However, as far as the monopolistic factor is concerned, Kickerbocker (1973) pointed out that it plays a role in motivating firms to invest abroad only when another rival company preceded it in establishing production abroad. He considered the second firm's behaviour as an oligopolistic reaction. To understand the first move of FDI he depended on the product life cycle theory.

### ***II.3 Market Imperfection***

Also another strand developed based on the assumption of market imperfection. Hymer (1976) was the first to talk about the relation between market imperfection and FDI. In the core of this theory is the assumption that a decision by a firm to undertake FDI is in order to take advantage of certain capabilities not shared by local competitors. Robock (1989) argued that the competitive advantage of firms is explained by imperfections in markets of goods or factors of production. "In the theoretical world of perfect competition, firms produce homogeneous products and have equal access to all productive factors. In the more realistic world of imperfect competition, as explained by the industrial organisation theory, firms acquire competitive advantages through product differentiation, brand names, special marketing skills, and restrictions to entry"(Robock, 1989 p.43). Finally although he recognises the contribution of the theory he claims that the model leaves many questions unanswered.

“Given the special advantages that permit the firms to invest abroad...the model stops short of explaining why foreign production is the preferred means of exploiting the advantage (i.e., the sufficient condition). The firms advantage can also be exploited through exporting or licensing” (Robock, p.44).

#### ***II.4 Eclectic paradigm***

However, most of the theories suffered from limitations and a more inclusive theory of the multinational corporation and FDI was needed. John Dunning’s eclectic paradigm offered this alternative. The eclectic paradigm is considered as one of the most widely accepted frameworks to explain the internationalisation of business. Dunning’s major contribution was to propose a framework that attempted to integrate various strands of explanation of international production. Dunning proposed a set of three general and interrelated principles which, he suggests, are fundamental to an understanding of international production. The three principles themselves have derived from a variety of theoretical approaches- the theory of the firm, organisation theory, trade theory and location theory. Therefore, Dunning labels his approach eclectic.

Dunning’s model states that a firm’s decision to engage in international production requires three conditions or advantages: the firm’s possession of certain ownership-specific advantages (O) not possessed by firms of other nationalities. Also, there must be location-specific factors (L) which make it more profitable for the firm to exploit its assets overseas, rather than in the domestic locations. Finally, the third set of advantages are associated with internalisation (I). That is when it is more profitable to internalise these advantages within the firm rather than sell them to independent parties.

In the eclectic paradigm it is contended that multinationals have competitive or ownership advantages vis-à-vis their major rivals. Such advantages are most suitably exploited by the firm itself rather than by selling or leasing them to other firms. In other words, the firm internalises the use of its ownership-specific advantages.

#### ***II.5 Investment Development Path (IDP)***

Dunning has also developed an Investment Development Path (IDP) model in order to illustrate the relevance of the eclectic paradigm in explaining the Net Outward

Investment (NOI) position of countries. The IDP model systematically relates the outward and inward direct investment of a country with the stage of its economic development. It supposes that there are consistent patterns of structural change with development; and second that these changes are systematically related to patterns of FDI (Dunning and Narula, 1996)

Specifically, the IDP model identifies five different development stages according to the propensity of the country concerned to be outward and/or inward investor. This propensity rests on the extent and pattern of the ownership specific (O) advantage of the indigenous firms, on the location-bound resources and capabilities of that country (L) related to the others, and last, on the choice of the firms to internalise these advantages (I). Dunning and Narula (1996) argue that the relationship between FDI, on the one hand, and the ownership, locational and internalisation (OLI) advantages of the countries and firms, on the other, change according to the country's stage of economic development. In other words, "the relative weights and roles of the three elements of OLI or eclectic approach to international production vary as countries and their firms become richer, shift from natural to created assets, and become more embedded in the world economy" (Campa, p.207).

Finally, according to Dunning (1996) the impact of both outbound and inbound MNCs activity on the development and economic restructuring of the countries in which they operate depends on three main variables: a) the type of FDI undertaken, b) the structure of the indigenous capabilities of the countries concerned, and c) the macro-economic and organisational policies pursued by governments. For instance, according to the IDP model, the level of development of the host country is a major predictor of the type of inward investment. A less developed country does not have a high level of created assets and its comparative advantage lies in its natural endowments. Therefore it is argued that a country's per capita income is inversely related to the percentage of factor-seeking FDI into the country and positively related to the percentage of asset-seeking investment. Existing trade flows will also determine the purpose of FDI activity.

## ***II. 6 Third World Multinationals (TWMCs)***

Over the period 1977 to 1985 there was a growing interest in the rise of FDI firms based in developing countries. Therefore, a new theoretical strand developed concerning FDI from Third world countries (TWCs), since this was not predicted to a great extent by the normal postulates of international or development economics. The main proponent of this theoretical strand was Sanjaya Lall (1985).

The previous theoretical analysis of FDI was mainly based on studies done on MNCs from the USA and therefore the literature had barely taken note of the different nature of monopolistic advantages that firms from other countries might have (Lall, 1985). Lall argues that there can be several conditions under which a firm from a less industrialised country can develop a proprietary advantage vis-à-vis competitors from more advanced countries. Wells (in Lall, 1985) based on an empirical work claims that the advantages of the MNCs from TWCs are not based on 'high technology' or advertising; rather many firms possess a know-how that enables them to produce at a low cost with small production runs and inexpensive labour. Furthermore, in many cases, they meet little challenge from firms of rich countries as long as they stay on this turf. However, although their experience at home gives them advantages over local firms, in most cases it would be only a matter of a few years until local firms could copy their skills and develop similar skills themselves. Furthermore, he argues that only a few firms continue development activities at home that would lead them to innovations to replace old ones. Wells also comes to the conclusion that Third World MNCs become active mainly in sectors marked by price competition rather than product differentiation and their scale of investment is relatively small.

Lecraw (1992) offers a brief summary of the conclusions about Third World MCs (TWMCs). Some of the most important points he makes are the following. First of all, TWMCs investment are based on firm-specific advantages in the generation of product and process technology that are appropriate to the factor cost, input characteristics and demand conditions in the host countries where they invest. Second, usually TWMCs utilise smaller scale, more labour-intensive, more flexible technology compared to the "true" multinationals. Furthermore, their output is again of lower quality and they

compete more on price rather than on product differentiation. Finally, TWMCs usually export less of their output compared to 'true' MNCs and their exports are directed to other countries than their home country. At the same time, they tend to import a lower proportion of their input in comparison with other firms.

Overall, it could be argued that the TWMCs "are more adapted and more adaptable to the economic, social, cultural and climatic conditions of the host countries: that their technologies save capital and foreign exchange and generate more jobs; that the firms are on a smaller scale, more flexible and readier to enter into joint ventures, use more local materials and generally are more adapted to the host's environment" (Hamilton, 1985). However, looking from the point of view of the home country they have some drawbacks; as for instance they might remit of a smaller proportion of their profits back home since they are usually more independent from their parent firms.

The above discussion about theories of FDI is indicative of the importance that is placed on FDI and the internationalisation of economic activity. The operation of multinational corporations to the international arena has undoubtedly significant economic as well as political consequences. These have been investigated both on the side of the country where the MNCs begins (home country) as well as from the country where the MNCs invest (host country). The opinions about the role of the MNCs and the effect their operations have both in the host as well as in the home country differ considerably. "Some consider MNCs to be an advantage to mankind, superseding the nation-state, diffusing technology and economic growth to developing countries and interlocking national economies into an expanding and beneficial interdependence...while others view them as imperialistic predators, exploiting all for the sake of the corporate few while creating a web of political dependence and economic underdevelopment" (Gilpin, p.231, 1987). This topic will be discussed in detail in the following section.

### *III. The MNC and Home and Host Countries*

During the 1960s and the 1970s the literature on multinationals (MNCs) gave a lot of attention to the arguments for and against FDI. The literature focused on the impact of

FDI from various angles, including the so-called 'source' and 'host' country concerns. The issue was about the alleged benefits and/or costs that the operation of MNCs entail on the host as well as on the home country.

Most of the arguments over the possible costs and benefits of MNCs have been concerned with their effects on the host economies (Dickens 1998). This is not surprising since the majority of the multinational firms were coming (especially in the first years) from a small number of developed countries, while the host countries were relatively underdeveloped countries that many times were counting on foreign capital for their economic development. However, this thesis is looking at FDI from a different angle, from the point of view of Greece, a western, EU country that is conducting outward investment in the CEECs. Therefore the main interest is on home country effects. Nevertheless, a short literature review follows from both perspectives to provide a more complete picture of the issue.

### *III.1 Host country effects*

Multinationals were widely believed to have the potential to benefit the country and region where they were investing. According to this assumption FDI (FDI) from the 1960s onwards has been used as a possible solution to the problems of regions with low levels of regional development. In this context, the attraction of FDI was used as a tool for regional regeneration by central and regional authorities. This strategy, however, fall into considerable criticism in the early 1980s. FDI was criticised as leading to little more than 'cathedrals in the desert'. Therefore, some alternative policies of regional development, focusing on small firms and endogenous development were pursued as being more suitable. However, in the 1990's, attention once again turned to multinationals. This was due to two different but parallel processes. Firstly, it was due to the problems that appeared with the endogenous growth strategies. Policies focusing on indigenous development and small firms were proved fragile and inadequate to generate self-sustained growth. Secondly, the policy shift was also due to the alleged changes that are taking place in the organisation and management of multinationals. These changes imply that the use of territory by multinational firms may well be changing and that the

potential benefits for the host economies are greater than ever (Amin et al 1995, Dicken et al 1994).

During the 1960s and the 1970s the attraction of inward investment was used extensively as a measure for regional economic development. Within Europe, many less favoured regions were offering incentives in order to attract FDI. The multinationals were expected to act as growth poles in the host area by offering, apart from the direct benefits (like employment), dynamic benefits through spillover effects. In other words, inward investment was expected to contribute the host area by facilitating self-sustained and innovative economic development. However, the reality was rather different. Many multinationals were establishing their plants in certain areas in order to take advantage of the incentives offered by the governments and/or to exploit the cheap labour force in the area. The plants were used mainly for assembly and they were employing low skilled personnel, establishing hardly any linkages within the area. This type of plant, though, did not become embedded in the host area, and did not contribute much in the host area. Therefore they were characterised as 'cathedrals in the desert'. In particular, they were criticised for offering in the host economy little in the way of skill formation, technology transfer, linkage opportunities, transmission of managerial and entrepreneurial know-how or reinvestment of profits (Amin et al 1995). Therefore, multinationals, apart from offering some static, short-term benefits, failed to serve the aims of the host area; to facilitate self-sustained economic development (Netherlands Economic Institute 1992 in Young et al 1994).

However, in the 1990s the perception about multinationals and their potential impact on host economies changed. Recent developments in the organisation and technology of production processes suggest that there have been changes that might significantly affect the relationship of MNCs and host areas (Dicken et al 1994). Furthermore, changes have been occurring in the organisation and management of the firm that might mean different use of territory by multinational firms (Amin 1995). For example, the introduction of just in time (JIT) production systems have meant that the firms themselves may try to establish greater links with firms of the locality. Furthermore, the emergence of the so-called 'entrepreneurial firm' or 'performance company' have led to an emerging re-evaluation of the relationship between MNCs and local areas. Therefore, it has been

argued that there is a tendency of multinational firms to engage more with the local environment.

From the economic perspective, it can be argued that the most important single indicator of local embeddedness relates to the linkages that are developing between the multinational firm and local suppliers. Turok (1993) gives emphasis to the 'quality' and the dynamic nature of linkages, together with the long term implications for local economic development and he distinguishes between two different scenarios; namely developmental and dependency. In the developmental scenario the pressures for greater flexibility lead to vertical disintegration of production and collaborative partnership between suppliers and distributors, encouraging geographical clustering. The clusters act as an internally generated growth pole, transfer technology and expertise to local firms. Finally the multinational firm gets deeply embedded in the local economy through the creation of a network of sophisticated, interdependent linkages which support the expectation of local firms and generate self-sustained growth of the cluster as a whole. Conversely, in the dependency case, the linkages with suppliers are hierarchical, governed by price considerations or other short-term objectives. The suppliers do not participate in the technological development and their capacity to upgrade is undermined. The MNCs ties to the locality are very weak and, hence, the local subsidiary is vulnerable to external decisions and corporate decisions.

Similar to the above developmental scenario is the notion of the performance plant. Amin et al (1995) argues that the performance plant has developed as a result of the acute pressures of the economy for high quality products and continual ability for change and innovation. The performance plant possesses a set of distinctive attributes which makes it an attractive opportunity for stimulating endogenous development. In particular, he groups the attributes that justify the re-examination of the role of inward investment as a stimulus to self-sustained local economic development under four categories. First, quality plants exhibit a wide range of functions and competencies, including high-skill functions such as research and development. Thus they can promote the skill base and entrepreneurial qualities of the host region. Second, the performance plant has a degree of autonomy and decision-making authority that serves to the involvement of local managers, committed to the long-term survival of the plant. Third, it has a great

propensity to stimulate closer and more collaborative supplier linkages. Finally, the strategic position that the company possesses within the corporation reduces threats for closure or rationalization.

### ***III.2 Home country effects***

As far as the home country is concerned the beliefs have been mixed. The main worries lay around the belief that FDI may take away domestic investment, displace exports and consequently have a negative impact on employment (Dicken 1998). On the other hand, the most common argument in favour of outward investment is that it is necessary for firms to invest abroad in order to stay competitive in a highly international environment.

#### ***Balance of payments***

The first worries, expressed by the 'home' countries, were centred around the impact of outward investment on the balance of payments of the country. Considering first of all balance of payments issues, a number of possible effects may result. This depends mainly, as Young and Hood (1979) argue, on what multinationals would or could have done if they have not established affiliates overseas. In other words, does the direct investment abroad substitute for domestic investment, does it substitute for domestic consumption, or does it supplement both?

One of the negative aspects is the possibility that outward investment may replace exports, or stimulate imports with an adverse effect on the balance of payments. Pitelis (1996) argues that the full impact of this would depend on the extent to which the overseas operations take exports from the home country, and the extent to which there are lower order effects as a result of the overseas investment increasing economic activity overseas, hence causing a general rise in the exports from the home country. Furthermore, that might depend also partly on whether foreign investment contributes in the increase of the income of the host country and hence stimulates import demand. Finally, the general impact on the balance of payment might be affected by the degree to which the profits of the foreign investment are repatriated in the home country.

### ***Empirical assessment***

A number of studies have sought to determine the effect on home country exports and balance of payments of outward investment<sup>9</sup>. The crucial question that occupied those studies was what might have happened if the FDI had not taken place. Three extreme cases had been identified as possible (Hood and Young 1979, Buckley and Artisien 1988):

a) The classical assumption

This postulates that FDI produces a net addition to capital formation in the host country but produces a similar decline in capital formation in the home country. This implies that direct investment abroad is a perfect substitute for investment at home and that the output of foreign investment substitutes for exports.

b) Reverse classical assumption

In this case FDI substitutes for investment in the host country to some degree but does not diminish capital formation, in the investing country. This is essentially the defensive argument, which states that foreign investment is required to maintain markets, as exports are likely to be excluded by host country policies designed to promote self-sufficiency. In other words, this type of 'defensive' investment can occur where tariffs, quotas or other restrictions prevent imports to the market.

c) Anti-classical assumption

This case applies where FDI does not substitute for capital investment in the home country, but it does increase capital formation in the host country. Consequently, world capital formation is increased by FDI. This situation could occur when MNCs establish projects in the host country that local firms were incapable of undertaking.

Several important studies were based on those assumptions. One of these was the major initial study, over the impact of FDI on USA's balance of trade, which was undertaken by Hufbauer & Adler in 1968. The Hufbauer-Adler study investigated all three hypotheses and shows outward investment to have a negative impact on the home country's balance

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<sup>9</sup> Reddaway *et al* (1968), Hufbauer and Adler (1968), Dunning (ed) (1985)

of payments when it is assumed that exporting from home is an alternative to overseas production. Immediately preceding this, somewhat similar research has been undertaken for the UK by Reddaway and others (1967 and 1968). Reddaway's study was limited to the reverse classical hypothesis and it concluded that the UK's balance of payment benefited from UK outward investment. However, Reddaway's assumption, that in the absence of overseas production the market would have been totally lost, is open to criticism.

From the above empirical cases it becomes clear that it is not easy to give definite answers on the effects on the balance of payments of the home country that arise as a consequence of outward investment. Different assumptions can lead to different results. Furthermore, the above assumptions have been criticised as rigid and static (Buckley and Artisien 1988). In addition, Hood and Young (1979) pointed that there are several weaknesses with such investigation. The models do not give sufficient weight to the existence of 'anticipatory exports' (i.e. goods exported by the home country in anticipation of building the plant abroad) nor to 'associated exports' (i.e. complementary products exported by the home country after the establishment of the subsidiary). Furthermore, they do not take into account 'balancing exports' that result after the first plant build upon is operating at full capacity. Finally these models do not reveal the dynamic effects of overseas direct investment in terms of maintaining the competitive position of home country firms. Therefore Buckley and Artisien suggest that the impact of outward investment must be investigated on a case by case basis, taking account of the feasible changes open to the firm, and the changing supply and demand conditions and other environmental circumstances.

### ***The employment effect***

As shown before, the act of establishing an overseas operation has implications for the home country's balance of payments, through its influence on capital and financial flows and its effect on trade. However, the most obvious implication for the average citizen is the effect on employment (Dicken 1998).

The possible effects might vary significantly, depending on whether the foreign investment will displace local jobs or will give a further stimulus to local economy. In the

first case there might be a loss of domestic employment through overseas production both directly (relocation or job exports if foreign affiliates substitute for production at home) and indirectly (loss of jobs in firms/industries linked to production/ activities that are relocated). While, in the second case there might be a creation of new jobs both in the parent company and/or in supplier/service industries at home that cater to foreign affiliates.

More detailed, Hawkins (1972) distinguished four possible employment effects:

- a) Production displacement effect: In this case, there are job losses arising from the transfer of production from home to host country and also from servicing foreign markets by those overseas affiliates.
- b) Export stimulus effect: This occurs when home country exports increase as a result of affiliate's demands for capital equipment, intermediate goods, and complementary products. Thus, domestic employment rises through the production of goods which would not have taken place in the absence of the foreign investment.
- c) Home office: employment gains in non-production categories at the company's headquarters made necessary by the expansion of overseas activities.
- d) The supporting-firm effect: employment gains in other domestic firms supplying goods and services to the investing firms in connection with its overseas activities.

As a result of outward investment labour at home may be released from marginally productive jobs and transferred to jobs where productivity is higher. Therefore, the employment effect on home countries must be viewed not only in terms of impact on the level of employment but also on the mix in employment.

### ***Spillover effects***

Although the issue of 'spillover effects' has rarely been used in the home country debate, Blomstrom & Kokko (1995) argue that spillover effects similar to those that occur in the host country can take place in the home country as well. In particular, they argue that it is likely that the linkages between MNCs and their suppliers in the home country yield similar effects as linkages in the host countries. The only problem according to the

authors is the difficulty of defining what is a spillover effect in the home country context. Nevertheless, the authors bring a number of examples of potential positive effects that might occur to home country firms as a consequence of the outward investment of home multinationals.

Firstly, FDI opens up opportunities to benefit from economies of scale, since it allows the MNC to grow larger than what would be possible if its production was restricted to a single country. When that results in reduction of the average cost then it may generate productivity spillovers. For instance, there are spillovers if the MNC produces intermediate goods that become available at a lower cost to all home country firms as a result of FDI, and if this cost reduction raises the international competitiveness of home country firms. Moreover, there may be market access spillovers on the non-multinational home country firms from the distribution networks and the knowledge of foreign markets that is built up through FDI. For example, there might be positive effects on the home country's exports only by the establishment of a good name, and the familiarity with the products of the home country in a foreign country<sup>10</sup>. There are also more obvious spillover effects, for example the increasing R&D operations at home that usually follow a firms's investment abroad can be expected to result in positive spillovers in the home country. Other possible spillover effects in the home countries stem from the structural changes that take place as domestic firms become (more) multinational. As MNCs expand their foreign operations, it is common for a shift in the structure of their production in the home country to occur. The structural effects can be both positive or negative, depending significantly on the level of development of the home compared to host country<sup>11</sup>.

Overall, the effect of the outward investment on the home country depends, as was shown above, mainly on the impact on the trade balance of the country, the employment effect

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<sup>10</sup> For example, Swedish products are highly regarded for their quality in Latin America, partly because Swedish MNCs have been producing there for decades.

<sup>11</sup> For, instance, if the home country's labour force is well educated and the wages higher in relation of that of the host country, then the structural shift is likely to bring an increasing emphasis on the home country production in advanced industries with labor productivity-simple production processes requiring lots of unskilled labor may be moved to foreign affiliates.

and the possible spillover effects. The effects are in general believed to be positive, but nevertheless there are also some negative aspects involved with outward investment. In the case of Greece there is a widespread optimism about the effects of the internationalisation of firms, but this is merely an assumption and it has not been based on solid research and investigation. Therefore, all the above issues must be thoroughly examined and a serious evaluation has to be done on the impact of outward investment on Greece. The following section will present the first findings of research done on the above issue.

#### *IV. Greek outward investment: Application of theories of FDI in the case of Greek investment in the CEECs*

The first two sections of the chapter provided a brief overview of the theories of FDI. The first one is focused on the theories that explain the reason why firms undertake FDI while the second refers to the theories that have been designed to evaluate the consequences of FDI in the home and/or host country. In this section the aim is to examine how the above theories apply in the specific case of Greece. There are two main tasks: one is to explain the phenomenon, defining the mechanisms that underlie FDI. Second, is to evaluate the consequences for the Greek economy

The plan of the section is as follows: the first part sets, in brief, the general picture of FDI in the CEEC and places Greece in this wider context. The second, and main part, attempts to address some of the most significant questions related to Greek outward investment in the CEECs based on the existing literature about the topic.

At this point it should be mentioned that the task of analysis of the Greek case is confronted with certain obstacles. Firstly, one problematic issue is that both Greece and its firms are difficult to place in fixed categories (i.e. Greece is not a developing country but neither a typical developed industrialised one). This is also related to the fact that the theories of FDI have been developed mainly in order to explain certain types of economies and firms (i.e. American) that are not similar with the Greek ones. Therefore there is a difficulty in choosing an appropriate set of theory where the Greek case falls in

(i.e. is the theory about TWMCs relevant to the case of Greece)? Finally, there is a considerable problem with the availability of data on Greek FDI. There are limited sources of data and those are not always reliable. Therefore, most of the studies on Greek FDI end up with tentative suggestions rather than concluding with fixed results.

#### *IV.1 FDI in the CEECs*

The reforms in the CEECs have been a major political and economic event that has given rise to a lot of discussion. One of the major issues that has attracted a lot of attention is that of FDI in those countries. FDI has been seen as both an opportunity for foreign firms as well as a major contributing factor in the restructuring efforts of these economies. Therefore, a new theoretical interest developed around the benefits and opportunities that appear for western firms through FDI to the CEECs (see Buckle & Ghauri, 1994). "Closely allied to this corporate interest in Eastern Europe are the forces shaping EC integration and enlargement...in the EC context, moreover, there has been some debate on the ways in which corporate integration might be encouraged to promote the objectives of regional integration" (Hood & Young, 1994). Related to the second concern, an optimistic climate about the role of FDI and its developmental potential in less favoured areas raised great expectations on FDI in the CEECs.

One segment of literature has been focusing on the effects of FDI on central and eastern European countries (CEECs) and their transformation process on the national level. There was a widespread optimism that FDI in the CEECs would facilitate their economic development. Much commentary has stressed the importance of integrating the countries of Central and Eastern Europe into the global economy, emphasising the view that investment by transnationals could play a significant role in assisting these countries to develop. Dunning (1994) argues that judging from previous experience it should be reasonably expected that the opening of Central and Eastern Europe to market forces will markedly improve the economic lot of its citizens. Finally he concludes that "foreign technology, management expertise and the access to foreign markets can...play a critical role in Central and Eastern European economic development". Similarly, reports by the World Bank, UNCTAD and the EBRD are in favour of FDI. For example the EBRD in its 1995 transition report states, "FDI and partnership can carry great benefits in

providing market skills, management, technology and finance as well as effective corporate governance”.

Another strand of literature focuses specifically on the effects of FDI on the regional level (Michalak 1993, Hardy 1998, Pavlinek P 1998, Sadler & Swain 1994, Smith & Ferencicova 1998). They examine the locally specific impacts of inward investment in relation to mode of entry, institutional engagement, different corporate strategies, technology transfer and linkages created in the local region. In this case the results are not that optimistic. After examination of several case-studies in various countries of CEE most of the authors are arguing that inward investment has not provided the solutions to sustainable restructuring that many hoped. The authors suggest that the FDI, although it had significant transforming impacts on the individual firms, had rather limited impact on the regional economies. They find limited the role of FDI in establishing a deep network of ‘embedded’ linkages. On the contrary some argue that FDI has created ‘cathedrals in the desert’ (Hardy 1998). MNC’s strategies are said to impel private but not necessarily social efficiency. There may be a substantial gap between the corporate optimum and the regional optimum.

Greece finds itself in the middle of this interplay between different (and often contradicting) interests among firms, countries and regions. Greece’s geographical position (in the Southeast of Europe) and its economic condition (the poorest country of the EU) put her among the countries most immediately involved in and affected by the reforms in the CEECs. Despite its small size and its limited economic power, the country desired to play a significant role in the restructuring process of the CEECs. The government immediately saw many opportunities arising from the opening up of the CEECs for Greek firms and also its (acclaimed) ability to play a significant regional role in the area of Balkans. Therefore, the reforms of the CEECs have triggered strong reaction from the part of Greek firms, mainly in the form of outward investment towards these countries.

#### ***IV.2 Greek FDI in the CEECs***

The demise of the communist regimes in the CEECs has triggered a remarkable new phenomenon in the Greek economic business world. A significant number of firms of

Greek ownership have started an active investment into those countries. The phenomenon itself and its magnitude were unprecedented by Greek standards. Greece, for many years has been mainly, if not solely, a recipient country of FDI flow (table 3-1 and 3-2), but that has altered significantly since 1989. This novel phenomenon attracted much attention and became the topic of extended presentation in the media. However, the actual picture is not yet very clear. There are many questions to be answered related to the nature of the investment and its implications for the Greek economy. A certain number of academics have been dealing with those questions, attempting to explain the phenomenon, and evaluate the possible effects in the Greek economy ( Labrianidis 1999, Kamaras 2001, Pitelis & Iammarino, Pitelis, Tsipouri and Sudgen 1996, Louri et al 2000, Dimelis and Gatsios 1995). Drawing from their work, the section will attempt firstly to explain this phenomenon, defining the mechanism that underlies FDI, and second, evaluate the consequences for the Greek economy.

The Greek FDI rises many questions. How can it be explained? Under which theoretical framework does it fall? What type of companies are those investing abroad? What are the implications for Greece's development and international competitiveness?

Firstly, the Greek outward investment could be explained as a country-specific phenomenon. This explanation would come in accordance with the theory of the investment development path (IDP) (that was developed in the first section). According to the theory the propensity of a country to engage in outward investment goes through various stages as the country develops, with outward FDI becoming a means of industrial restructuring only in the final stages of development (Iammarino & Pitelis).

According to Louri et al (2000) Greece could be classified as a stage three country. At this stage the comparative advantages in labour-intensive activities deteriorate, domestic wages rise, and outward investment is directed more to countries at lower stages in their IDP. Specifically, outward investment increases and is directed to stage 1 and 2 countries, both as a market seeking investment and as export platforms as prior domestic location (L) advantages in resource-intensive production are eroded. Efficiency or asset-seeking do not seem to influence Greek FDI decisions at the initial phase (of the Balkan expansion) according to the model (Louri et al 2000).

Outward direct investment also might occur in stage 3 and 4 countries, partly as a market seeking strategy, but also to acquire strategic assets to protect or upgrade O advantage of the investing firms. Finally, it is predicted that the government will seek to encourage the country's companies to invest abroad in those sectors in which they have strong ownership (O) advantages and the comparative locational (L) advantages are weakest.

The same question about the mechanisms underlying FDI can be examined from the point of view of the firms. Many theories are focusing on firm-level characteristics in order to investigate the determinants of FDI (Hymer, Dunning's OLI paradigm, Caves 1996, Grubaugh 1987). Louri, Papanastasiou and Lantouris (2000), using the above conceptual framework are attempting to explain the phenomenon of Greek outward direct investment. They are looking into the decision-making process of Greek firms before undertaking any type of internationalisation strategy. They seek to investigate the determinants of alternative expansion strategies (i.e. exports versus FDI) by focusing on the importance of firm-specific characteristics. The novelty of their research, they argue, is that they use firm specific characteristic in order to determine the probabilities of each alternative strategy.

The paper uses an econometric model trying to calculate the returns of each strategy using financial-asset characteristics of each firm i.e. borrowing capacity, liquidity and profitability and size advantages. The location and sectoral factors are not examined since there is homogeneity in their research.

The empirical findings seem to support the theory. The Greek firms undertook FDI taking into consideration their financial and market structures. It was found that there is a significant positive effect on the long and medium term borrowing capacity of firms engaged in FDI in contrast to the negative effect of short-term borrowing. Furthermore, on the market basis it was noticed that there is a positive effect of relative firm size as well as the growth rate of sales. Moreover, it appears that the more intense the acquired familiarity with the foreign market through exports, the more likely it is for a firm to undertake FDI. In addition, labour intensity and old local comparative advantages were found to affect positively the choice of FDI as opposed to exports.

Overall, the model predicted a different strategic reaction between domestic catering and export oriented firms (the two subgroups examined) with the former appearing more keen to engage more intensely in FDI, while the latter being more indifferent between exporting or investing, possibly preferring a home production based expansion strategy.

Another issue that needs investigation is what kind of firms are those investing abroad; are they similar with the typical multinational firms; or could they fall under the category of New Multinationals? This question is addressed by Labrianidis (1999). He has written extensively on Greek FDI. His interest is to examine the novel phenomenon of Greek outward investment and to evaluate its effect on the Greek economy. In order to do that he attempts to identify the type of firms that have invested in the CEECs.

Labrianidis (1999) initiates a theoretical debate on whether the Greek firms that have invested in the CEECs are meeting the criteria of the conventional types of Multinational Companies ("true companies") or MNCs from Developing countries (new multinationals). According to the author the aim is not just to come to a simple classification of Greek investment projects but to understand the mechanisms causing this internationalisation.

Labrianidis offers a systematic work on the character of Greek FDI. He is looking into the push factors (saturation of the Greek market and the intensification of competition) as well as the pull factors (cheap labour cost, exploitation of natural resources) that urged Greek firms to invest in the CEECs. Furthermore, he is looking into the monopolistic advantages that the Greek MNCs have over the other local and foreign firms. According to Labrianidis the main advantages that the Greek firms have over the firms of the host country are that they have substantial capital and that they also have established relations with the Western market. However he comments that these "monopolistic advantages" will not last for too long, it will be a matter of a few years only until local firms manage to develop similar skills themselves.

As far as the advantages over the other foreign firms are concerned, those seem to be based on the following factors: first they are more experienced and familiar in working in an unstable environment (as the Balkans). Furthermore, they are favoured by the geographical proximity to the host countries. Moreover, they have access to cheap labour

in their home country and finally the structure of the Greek firms, being relatively small and owned by one family, gives them the flexibility of taking decisions faster and being able to take risks more easily and hence grab the opportunities available.

Judging from the empirical evidence provided by Labrianidis it could be argued that Greek firms investing in the CEECs resemble in many respects MNCs from the Third world. The firms lack strategy and they give priority to labour cost reduction considerations in their decision, also they operate in labour-intensive industries and their size and the investment volume are small.

Therefore, Labrianidis expresses worries about the position of those firms in the CEECs. He believes that many of them are characterised by an opportunistic attitude and furthermore he suggests that to a great extent this type of investment could be described more accurately as immigration rather than as FDI.

Iammarino & Pitelis are looking into Greek FDI towards two Balkan countries as FDI from and towards Less Favoured Regions (LFRs). They attempt to analyse the key criteria that underlie the investment choices of Greek firms. The aim is to help identify their role in the restructuring process and the impact that outward flows may have on the Greek economy. By investigating the strategies that have been followed by the Greek MNCs in CEECs are trying to shed light on the implications that outward flows have for a peripheral EU economy such as Greece.

Their empirical analysis is based on the results of a survey carried out in 1995-96 as part of an ACE project supported by the European Commission on the economic integration through FDI in the less favoured CEECs and the impact on the LFRs of the European Union. They classify the FDI, according to the main objective of the investment itself, (into Exporters, Local suppliers, and Distributors,) and also by the control mode chosen by the parent company to establish an affiliate abroad (Wholly owned, joint venture;-licensing-franchising). By investigating on the strategies that have been followed by the Greek MNCs in CEECs they are trying to shed light on the implications that outward flows have for a peripheral EU economy such as Greece. They are using a probabilistic econometric model.

Iammarino and Pitelis argue that the result of outward FDI on the home country depends crucially upon the characteristics of the economies involved and upon the strategies followed by multinational enterprises (MNCs). In other words it depends on the type and pattern of FDI and upon the comparative points of strength and weakness of the national economy. Their empirical findings express some caution about the implications of FDI on the home country, especially when the FDI comes from a LFR. That is because some FDI might be negative for its possible substituting effects on similar exports, reducing effects on domestic capital investment and negative impact on jobs creation. Thus, they conclude that the “Competitiveness of Greek firms need not imply competitiveness of Greece as a nation” and they suggest some caution, and a pragmatic stance on the part of the Greek policy makers.

Finally, Pitelis, Sugden and Tsipouri (1996) are looking into Greek outward investment, competitiveness and development. They investigate the case of Greek outward investment in the Balkans. The paper examines the extent of the investment and the potential impact on Greek international competitiveness and industrial development. It addresses fundamental questions about the meaning of the term competitiveness and how it is related to social objectives. The authors question whether there is a relationship between outward investment by Greek firms and Greek competitiveness (as a nation), and if so what kind this is. Specifically they wonder “If and how outward investment will serve (the wishes of communities in) Greece”(Pitelis et al, 1996, p169).

The authors make a distinction between private and community costs and benefits. They claim that there is likely to be a divergence between the private and social community costs and benefits of overseas investment. Thus the Greek firm’s investment in (say) the Balkans may bear profits for the firms and the Greek capitalists but not necessarily for the people of Greece. This can be the case for firms that either do not repatriate profits or paying taxes in their home base and/or export from their host nation to their home.

Drawing from a wide literature on the implications of FDI (that has already developed in the second section) and taking into consideration the case of Greece, they conclude that outward investment per se is not unambiguously good or bad. Therefore they conclude by arguing that “it is inappropriate for the Greek Government to presume outward

investment as unconditionally desirable". Finally, they conclude by suggesting that the Greek government should attempt to design an industrial strategy which only facilitates outward investment beneficial to Greece.

### V. Conclusions

Attempting to apply the theories on FDI in the case of Greece we come up immediately with the following observation: no single theory seems to be sufficient on its own to explain the phenomenon of Greek outward investment to the CEECs. An analysis of FDI theories shows that most of them are useful and partly applicable in explaining the phenomenon of Greek outward investment, but none would be adequate by its own to explain the motives that underlie Greek outward investment. Further research is required in order to establish a better understanding over the issue.

**Table 3-1.** Inflows and Outflows of FDI per \$1000 GDP per country, 1970-2000

YEAR	1990-1996							
	1970	1980	1989	average	1997	1998	1999	2000
COUNTRY_GROUP								
Inflows per \$1 000 GDP								
World	4,84	5,24	10,27	9,60	16,10	23,55	35,65	47,69
Developed countries	4,36	5,86	10,70	7,73	11,92	21,28	35,09	50,94
European Union	6,47	5,99	13,76	11,39	15,49	30,69	57,11	102,92
Greece	4,41	13,76	11,06	10,53	8,12	0,70	4,58	9,67
Outflows per \$1 000 GDP								
World	6,17	5,60	12,45	10,77	16,07	23,34	34,34	44,37
Developed countries	6,56	6,40	13,90	11,74	17,59	27,74	40,46	52,76
European Union	6,59	6,83	19,77	16,33	26,76	48,62	83,78	123,22
Greece			-0,19	0,05	1,28	2,16	4,32	18,66

Source: UNCTAD/DITE (<http://stats.unctad.org/fdi>)

**Table 3-2.** Inflows and outflows of FDI as percentage of gross fixed capital formation by country (GFCF) 1970-2000

YEAR	1990-1996							
	1970	1980	1989	average	1997	1998	1999	2000
COUNTRY-GROUP								

<b>Inflows</b>									
World	2,41	2,28	4,67	4,40	7,44	10,96	16,50	22,03	
Developed countries	2,17	2,72	5,04	3,81	6,01	10,70	17,40	25,01	
European Union	2,86	2,80	6,57	5,65	8,10	15,68	28,51	50,08	
<i>Greece</i>	2,12	6,92	4,99	5,17	4,10	0,33	2,09	4,24	
<b>Outflows</b>									
World	3,07	2,49	5,74	5,00	7,42	11,03	15,91	20,61	
Developed countries	3,26	2,97	6,55	5,78	8,86	13,95	20,07	25,90	
European Union	2,90	3,19	9,44	8,12	13,99	24,85	41,82	59,96	
<i>Greece</i>	-	-	-0,09	0,03	0,65	1,02	1,97	8,19	

Source: UNCTAD/DITE (<http://stats.unctad.org/fdi>)

#### **4. THE RECONCEPTUALISATION OF THE FIRM IN ECONOMIC GEOGRAPHY: KNOWLEDGE CREATION AND COMPETITIVENESS**

##### ***I. Introduction***

The previous chapter focused mainly at the national/regional level, looking into the consequences of Greek business activity on the home country (Greece) and on the host countries. This chapter will focus on the firm as the unit of analysis. This allows us to increase our understanding of the process that underlies the Greek FDI phenomenon. The aim of the chapter is to add further to our understanding on the behaviour and response of Greek firms, the process of decision making, and the importance of the place where firms are located in this process.

The chapter provides a thorough presentation of the theories of the firm and the latest debates over the firm in economic geography. The relation of the firm's home environment and its competitiveness is also discussed. Emphasis is put on the recent literature on knowledge and learning as competitive assets of the firm. The chapter further discuss the importance of knowledge in the internationalisation process of the firms and theoretical insights together with empirical evidence of Small and Medium Enterprises (SME) contacting FDI in the CEECs are presented.

##### ***II. Review of theories of the Firm***

The nature of the firm has been an issue of increasing interest in recent years in economic geography, largely because a clarification and re-conceptualisation of the object was

needed. According to Taylor, Yeung and Maskell respectively, the firm in economic geography has been criticised for being indefinite grouping, an unclear and ambivalent analytical category, and a grey area unable to be clearly defined with respect to form and function. Maskell goes on to state that the reason for this perhaps lies in the fact that the majority of economic geographers perceived (for many years) the internal analysis of the firm as being beyond their rightful agenda, or even, in some cases, derogatory with respect to the competence of economic geography as a discipline. However, recent years have witnessed a growing number of attempts to re-conceptualise the role of the firm in economic geography.

This attempt at re-conceptualisation occurs in the context of a broader 'cultural turn' that takes place in 'new economic geography' and reshapes both the topics, concepts and approaches of economic geography (Crang, 1997). Previously leading schools of thought are today on the defensive and, together with the reshaping of the old topics, new questions are appearing in the research agenda (Lee and Wills, 1997). Under this broader 'reconstruction' that occurs in economic geography the old conceptions of the firm have been challenged severely. Yueng (2000) characteristically argues that only recently have the "new economic geographers" developed and reshaped the notion of the firm and its social-spatial constitution.

However, until very recently economic geography was mainly adopting classical or neo-classical theories of the firm, where the enterprise was hardly seen as something more than a 'black box' that responded in the pressures of the market. The firm was represented more as a set of cost and revenue curves and less as an organisation (Hodgson, 1998). The mainstream neo-classical world did not deem theoretically significant phenomena including firm's strategies, managerial forms, entrepreneurial efforts and competitive alliances. (Maskell, 2000).

Nevertheless, a new literature has started to develop around the firm in economic geography that is concerned more with linkages and relations: opening up the 'black-box' conception of the firm dominant in mainstream economics and focusing upon the internal organisational make-up of firms (Lawson, 1999). Many of the academics that are interested in the redefinition and broadening of the concept of the firm are drawing

insights from other 'neighbouring' disciplines (i.e. network theories, management theory, economics). Dicken (1990) makes a plea for a much greater cross fertilisation between researchers in different traditions (within economic geography). Maskell (2000) goes further talking about the developments that "cousins in economics" have made on theories of the firm and how these can be useful and applicable within economic geography. Therefore, it is apparent that a broader investigation on theories of the firm on different disciplines can be of great use in our effort to better understand the nature of the firm.

Among the different theories of the firm, in mainstream economics, the evolutionary, competence theory of the firm appears to gain ground among the economic geographers. Foss, for example, argues that the dominant standpoint with respect to the conduct of firms is the competence perspective (Foss, 1996, p.1 ). This opinion seems to be supported by many others. Amin (2000) maintains that the competence based approach has led to promising new avenues of research for both economics and sociology of organisation. Furthermore, Hodgson (1998) argues that recent research conducted in the fields of organisational learning and cultural transmission seems to reinforce a competence-based explanation of the persistence and relative efficiencies of firms. Maskell (2000) also claims that the competence approach to the firm is the most suitable theory to be applied in economic geography. Finally, Lawson (1999) argues that the competence theory can be applied both in the micro and macro level since it can be used in the analysis of regions.

### ***II.1 The firm in economic theory***

Although the firm has been the topic of many and long-term studies there is not yet a general consensus (among economists) over the subject matter designated by the title 'theory of the firm'. The study of the firm is a wide and complex subject and can be examined from several perspectives. Many strands of theories have developed over the years, focusing in different issues of the firm, making different assumptions and following different approaches. This section will present some of the most important theoretical schools in economics that also had a great influence on the conceptualisation of the firm in economic geography.

Economic thought changed throughout time and a continuous reconstruction of the theory of the firm took place. Gustafsson (1990) argues that “Looking at the theory of the firm from the point of view of economic history, it is manifest that theories of the firm are born, flower and give way to new theories not only because existing theories are destroyed by new and superior ones but because historical reality, in this case the institutional settings, structure and behaviour of firms, is changing, making old theories outmoded and creating a demand for new ones”.

### ***II.2 The neo-classical school***

Accordingly, the original classical and neo-classical theories of the firm have received substantial criticism and have become outmoded. Standard neo-classical theory takes the firm as given; no attention is paid to how it comes into existence, the nature of its internal organisation, competitive strategy or the dynamics of the capitalist system (Best, 1990; Taylor, 2000; Hart). The firm is described as a production function; it is simply the place where inputs are transformed into outputs. Furthermore, the economic agents are considered to be rational, perfectly informed, homogeneous and display non-opportunistic behaviour. In short, in a world of pure and perfect competition, market price mechanisms are what drive the firm’s decisions and activities (Cooke, 1998). Neo-classical theory, based on several simplistic assumptions, is incapable of explaining complex real-world occurrences and policy instruments implemented by firms including partnership, networking, oligopolistic situations, choice of satisfying rather than optimal decisions. Furthermore, it is unable to assess and explain the impact of phenomena such as history, routines, location of research and production centres, or the advantages of technologic superiority and human capital (Cooke, 1998). Therefore, new theories, like the ‘contractual’ and the recent ‘competence’ view of the firm came to be considered as the ones that can explain better the nature of the firm (Hodgson, 1998).

### ***II.3 Contractarian approaches***

Contractarian perspectives originate from the work of R.H.Coase (1937), who wrote a seminal article that opened up the research agenda of the theory of the firm. Coase’s began to deal with questions that neo-classical theory had ignored. He claimed that the

firm and market were alternative modes for organising the very same transactions. Specifically, he claimed that the economic activities of individuals in a capitalist economy are co-ordinated in one of two ways: spontaneously, by the price mechanism in the market, or planned via an authority relationship within the firm (Best, 1990).

Williamson (1975, 1985) made a significant contribution in the contractarian strand of literature. Williamson's work is critical in the respect that he tried to replace the conventional conceptualisation of the firm as a production function with that of governance structure. He attempted to explain why firms decide to make (internalise) or buy (purchase in the market) economic activities. His answer, concurring with the basic argument of the new institutional economics, was that the organisational forms that prevail are those that deal most efficiently with the cost of economic transaction (Grabher). The firm and the market are seen as alternative modes of governance, and the choice between the two is principally decided by transaction cost differences. In other words transaction cost approaches describe the firm as a response to market failure. Profit-seeking firms internalise operations when by so doing the cost of organising and transaction business will thereby be lowered (Teece, 1998).

However, this approach may not be without criticism. Contractarian approaches are criticised for their neglect not only of the production but of the dynamic features of firm behaviour more generally, and also for the treatment of individual agents as atomistic and as given (Hodgson, 1998). Also, they have been accused of describing the behaviour of the firm in terms of optimal reaction to the environmental signals detected by the firm (Amin, 1999). Dicken and Thrift (1992) reject transaction cost theory as, in effect, merely a reaffirmation of neo-classical economics. According to them, efficiency is the basic calculus. It allows for the minimisation of costs by rational actors embedded in a matrix of exchange. With the same rationale, Yeung (1994) criticises transaction cost theory because socio-spatial factors are easily overshadowed by sensible economic reasoning. Specifically, he argues that the firm is regulated to the status of only a puppet in the crowd of treaties and contracts. Its causal powers, as expressed in the mode of rationality, are overlooked. Furthermore, important social (network) relations are discarded and replaced by the economising of transaction costs. In this way, economic reasoning eclipses less important social-spatial considerations. Finally, the notions of 'treaties' and

'contracts' are deemed by Yueng to be too descriptive in explaining anything causally within, and outside of, the firm" (Yueng, 2000).

Therefore, a number of researchers are looking into the 'competence' theory of the firm for explanations (Amin, 2000; Hodgson, 1998; Lawson, 1999, Maskell, 2000). Hodgson (1998) makes a thorough comparison between competence and contractual theories of the firm. Although, he does not discard the contractual theory of the firm he is argues that key questions can be answered using the competence-based approach that concern the nature of the firm accordingly to the transaction cost and other contractarian theories. He is emphases more the limitations of the contractarian approaches: treating individuals as given, overlooking the dynamic aspects of the firm and neglecting production and technology and downplaying the distinctive kind and rate of human learning that takes place within firms. Therefore he claims that competence theory is more appropriate for work on organisational learning and cultural transmission. Amin (2000) also, observes that the new 'competence' based view of the firm as 'a process of knowledge' opens up promising avenues for the economics and sociology of organisation.

#### ***II.4 Evolutionary theories of the firm***

Economic agents, firms and markets can be conceived differently using evolutionary economics, which gives emphasis to history, routines, and influences of given environments and institutions (Cooke, 1998). Firms are not homogeneous, atomistic units who act with the primarily aim to maximise profit. According to evolutionary economics, firms differ from one another and inputs in their production vary accordingly. One of these inputs is knowledge. (Dosi, 1988). Knowledge and learning plays a fundamental role.

Furthermore, Cooke argues that firms have their own developmental histories which they learn from and which ultimately shapes their actions. They are founded, they travel differentiated routes of growth, develop technological prowess, engage in various opportunities and adapt to ever-changing constraints and competition. Indeed, several cannot respond to these challenges and inevitably slowly exit markets. (Cooke, 1998). Furthermore, firms do not operate in a vacuum. Evolutionary economics, and even more

modern economic geography, emphasise the importance of the socio-cultural milieu within which network forms of interfirm organisation are embedded.

Recently, an evolutionary, 'competence' theory of the firm has gained ground becoming a leading approach (Maskell, 2000). Being influenced by the notion of 'competences' (Prahalad and Hamel, 1990) and 'capabilities' (Teece and Pisano, 1994), there is a growing number of researchers whose work upon (dynamic) 'capabilities' and/or 'competence' of firms is gaining importance and influence into the study of firm's behaviour.

### ***II.5 Competence theory of the firm***

Both competence theory and the knowledge based views of the firm are seen as distinct alternatives to both neo-classical and transaction-cost economics (Malecki, 2000). The competence perspective rejects the idea of the firm as a production function and emphasises management and organisation features instead (Williamson, 1999). The firm is a database, storing skills, experience and knowledge, not simply a set of mechanical responses to information or transaction costs (Malecki, 2000, Lawson, 2000). Hodgson (1998), more explicitly, argues that in contrast to the 'contractual' theories, that emphasise the cost of making and monitoring transactions, the competence perspective does not simply respond to individual and organisational responses, it is essentially a repository of knowledge.

Furthermore, competence-based research ascribes great importance to learning. In contrast to transaction cost, that downplays the distinctive kind and rate of human learning that takes place in the firm, for the competence theories of the firm, learning and relationships (of trust, etc.) that facilitate learning are of central importance.

In short, the competence perspective has to do with understanding the firm and its actions through a realistic, multifaceted approach. a (Lawson, 1999).

A critique of this school has been done by Williamson (1999), which according to his words, has been curiously exempted from sustained critique. He criticises the theory for being "obscure and often tautological definition of key terms". Furthermore he criticises the concept of core competences for "relying on ex post rationalisation: show me a

success story and I will show you (uncover) a core competence (or show me a failure and I will show you (uncover a missing competence)". Nevertheless, on his conclusions he claims that the relation between the two sets of theories are more complementary than rival since the differences are more apparent than real.

### ***II.6 Which theories of the firm apply better in economic geography?***

Maskell (2000) expresses a very interesting criterion in order to identify the theories of the firm that are the most appropriate for economic geography. The main criterion that he uses is how far the theory of the firm is applicable in the local and regional level of analysis. Specifically, he questions the fact that the theory of the firm gives theoretical significance to the spatial context in which the firm is placed.

Maskell comes to the conclusion that the 'competence' theory of the firm is the most suitable for economic geography since it fulfils better than all the other theories the spatial requirements that can be useful for economic geography. On both the micro and aggregate level, the competence based view of the firm can provide coherent theoretical framework. It can explain the behaviour of competing firms with respect to the former, and territorial competitiveness (between regions and countries) with respect to the latter. The theories of competence take into consideration the external environment where firms are located. Teece and Pisano (1994) argue that "Geography matters". Non tradable location assets can lead to uniqueness in certain business. Both learning processes and location with respect to business assets guide the strategies and tactics taken by a firm. The above theories take into consideration the local and/or regional forces that affect the competencies of the firm mainly through the facilitation of learning and knowledge.

Lawson (1999) develops the idea of expanding the competence theory of the firm to the analysis of the region. He argues that the competence perspective is equally relevant to the study of the firm and to the study of the regional productive system. In his analysis he presents firms and regions as ensembles of competencies that emerge from, but are not reducible to, social interaction. Furthermore, he tries to match the competence theory of the region with recent regional literature (local milieu, industrial districts, untraded interdependencies) arguing that they are based on the same rationale. Finally he

concludes by saying that there is a need to understand and assess the regional set of competencies within which the firms act.

### *III. The debate over the firm in economic geography*

Two main issues have to be addressed about the role of firm in economic geography. The first one is about the relevance of business enterprise in economic geography and the second is concerned with the choice of a precise theory of the firm that can be adopted by economic geographers. The two topics are highly interlinked, since the proper theory of the firm might give more credit and relevance of the firm in economic geography.

Therefore, the first of the issues is highly dependent on the ability to build a robust theoretical, as well as empirical base, of the theory of the firm (Dicken 1990). Or as Crang (1997) puts it a theorisation and methodology is needed to make sense of whatever empirical and conceptual concerns economic geographers decide they are interested in. Or more precisely, in the words of McNee “the geography of enterprise requires a theory of enterprise”.

The theory of the firm in economic geography has developed initially within the broader context of industrial geography and specifically industrial location theory. However, the concept of industrial (location) geography itself has changed considerably over time and within it the concept of the firm. A broad classification into three main schools is possible in order to follow the progress of the firm. The first school, and arguably the one with the greatest/longest influence, was the so-called classical location theory school. Two other schools followed as a response to the first one, the ‘geography of enterprise’ firstly and secondly a more radical political-economic school of thought. The contribution of the above schools into our understanding of the nature and organisation of the firm has been valuable. However, nowadays they meet criticism for being, at the least, limited in the way they conceptualised and used the firm in their analysis.

### ***III.1 The classical location theory***

The 'classical location theory' school is rooted in the neo-classical economic tradition and is mainly concerned with the interpretation of the location patterns of individual plans or industries. The main subject of study is the individual firm and the aim is to define the variables which determine the location choice of those firms. This approach treats space as distance and as land that each productive unit occupies (Labrianidis 1990).

Within this school the firm is perceived as a black box that converts market price signals into outputs of commodities or intangibles. No specifications of any particular processes are involved in this transformation (Maskell, 2000). The basic building block in neo-classical location theory is "an idealistic, abstract model of the individual firm, a model constructed to represent either all, or a specified, subset, of actual firms" ( Massey, 1979 in Yeung 2000)". The firm is separated from the rest of the society and it becomes a highly atomistic entity- a 'representative firm'. Furthermore, this approach is not interested about the organisational structure of the firm, this is reduced to an oversimplified dichotomization between single or multiple plant. Finally, central to the classical approach is the idea of the 'economic man' which posses perfect knowledge and makes the best, rational decisions.

The 'world' of the classical school is an abstract society in a permanent equilibrium state. It disregards the complicated and often contrasting social relations and moves within society and ends up in mistaken conclusions about society and human behaviour.

In the 1960s the classical school started to lose credit and to be under scrutiny. The first to challenge this approach were urban and regional geographers that were trying to explain uneven spatial development. There was a consensus that the equilibrium analysis of classical location theory could not cope with the realities of strongly disequilibrium forces in the space economy (Walker, 1989). Furthermore, the School has been criticised for its deductive and normative character (Labrianidis 1990, Chapman 1987).

The 1960s were characterised by a rapid economic growth that was accompanied by a high volume of investment by large multinational corporations. Those large corporations attracted the attention of economic geographers. On the centre of their academic interest

was the power of those large corporations on the creation of space–economy: the way they could influence the spatial distribution of economic activity.

### ***III.2 Behaviourist school***

At the same period emerged the so-called behaviourist school of industrial location. This school was emphasising the behaviour of the people (and the companies) in the location-decision-making. Behaviourists utterly reject the world of perfect competition and information in which the Marshallian single-plant family firm operates. (Walker, 1989). According to the behaviourist view, large firms have, to some extent, control over their environment. Furthermore, central to this approach is the concept that the firms are acting on the basis of ‘bounded rationality’.

### ***III.3 The geography of enterprise***

Under the above influences appeared the school of ‘geography of enterprise’ that became the dominant theory of industrial geography since the late 1960s and up to the 1970s. The theory of ‘geography of enterprise’ is widely attributed to the work of McNee in 1960 and it is preoccupied with the locational and behavioural patterns of large firm in the space. The Geography of enterprise tried to set more realistic behavioural assumptions into the location decisions of the firm. The location-decision making is not as central in the ‘geography of enterprise’ as in the classical school. During the 1970s the focus was directed on the organisational structure of the firms and their strategies. Some writers emphasised, in particular, the need to explore the environment within which firms operate (Walker, 1989).

A major shift in emphasis has occurred due to the geography of enterprise approach. This has been exemplified by normative location theory, and has to do with the concern for the influence of the spatial dimension of the economic environment upon industrial location (i.e. proximity to raw materials, markets, etc.). Concern is now placed more on an interest in the impact of the activities of industrial enterprises upon the environment (Chapman, 1987).

The school however did not escape criticism. Yeung (2000) argues that the geography of enterprise approach gave economic geography a new focus, but did not go far enough.

But, it was Walker (1989), and Storper and Walker (1989) who were most critical of geography of enterprise or 'corporate geography'. Walker sings the requiem of 'corporate geography' focusing on the failures/limitations of corporate geography. He claims that it could be possible to put corporate studies to a subordinate place in the geography of industrial organisation. That statement initiated a debate about corporate geography and the relevance of business enterprises in the study of geographical industrialisation. Dicken and Thrift (1992), taking part in the debate, are arguing in favour of the centrality of business enterprises in our understanding of the organisation of the production which, on its turn, is a prerequisite to our understanding of the dynamics of space economy. Furthermore, they are calling for a need to adopt "a broader socio-organisational view of the business enterprise".

#### ***III.4 Political-economy approach***

The early 1970s was the beginning of the rise of an intellectual hegemony of marxian political-economy approaches (Crang 1997). A number of radical geographers were not satisfied by the explanatory framework offered by both classical and behavioural approaches to the geography of business organisations and geographical industrialisation: (e.g. Massey 1977, 1984; Harvey 1975, Walker and Storper 1981)

Major theoretical and empirical reorientations with respect to research industrial (economic) geography came out of a radical approach in the 1970s and 80s. In the late 1970s there was a turn in the focus of industrial geography (from corporations) towards industrial restructuring (Yeung 2000, walker R). Emphasis was placed on industry studies rather than enterprise research, on change in the space economy rather than management of corporate systems. That was associated with the recession of the economy and the de-industrialisation process that was taking place in England, Western Europe and U.S.

Subsequently, because of this radical literature, the firm was subsumed under dominant capitalist class relations such that the spatial behaviour of the firm was explained by capital's logic . While the 'geography of enterprise concentrated on the individual firm and on particular aspects on management behaviour, the Marxist school focussed on the economic system as a whole and, especially, on the conflict between capital and labour (Dicken, 1990).

Despite the useful contributions of the radical school, Yueng (2000) criticises the way it conceptualised and used the firm. He refers to two main strands of radical literature: firstly, the spatial division of labour thesis and second the flexible specialisation and Post-Fordism debate. In the first theory he identifies the problem in the fact that it was given very little consideration in the specific strategies followed by the firms and the way that might influence the spatial division of labour. In the second strand he comments that virtually no analytical attention was given to the firm since the key analytical unit in this approach was the production systems.

That comes to verify Maskell (2000) who claims that the economic geography lacks any real micro-theoretical foundation, which gives clear explanations of how and why 'the firm' behaves and performs the way it does. In overall, it can be claimed that "the firm has not been adequately theorised in economic geography" (Yeung, 2000).

#### *IV. Competitiveness of firms and the local and regional environment*

Nowadays, it is widely accepted that the firm's competitiveness is highly related to its ability to continuously learn, innovate and upgrade its knowledge. Having accepted the above statement, then, what remains, for researchers, is to identify the factors that facilitate and promote these processes of knowledge and learning to take place. Whether these factors can be found within or outside the borders of the firm has been a topic of an on-going debate. However, the recent years, it has become increasingly common for scientists, even outside the discipline of economic geography (economists, sociologists), to try to analyse the effect of the 'environment' of the firm on firms' innovation and learning capabilities. Some of them emphasise the national level (Lundvall 1992, Nelson 1993), while others favour the regional level as the most influential on the firm's innovative and learning performance (Lawson, Storper, 1997). But, the most significant break with the past is that a significant number are now focusing on the so-called 'soft' (non-economic) factors of firm's environment. Concepts such as 'institutions'<sup>12</sup>, 'social

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<sup>12</sup> By institutions here we don't refer as much to the formal institutions (public or private bodies) as to sets of habits, routines, rules, norms and laws (Johnson, 1992)

capital'<sup>13</sup> 'culture'<sup>14</sup>, 'untraded interdependencies' are being used extensively in the literature of economic geographers. Amin (1999) distinguishes this new strand of literature from a previous one drew more on economic concepts (external economies, economies of scale) in order to explain the dynamism of regions and firms. This new strand of literature that Amin calls the 'relational strand' is concerned very much with the role of proximity and local ties of association as a source of knowledge and learning (Amin, 1999). Furthermore, this new strand of literature challenges the old conceptualisation of the firm. "The theory of the firm is being pushed well beyond its early disciplinary concerns by new insights developed in organisation theory, sociology of science, communications theory, evolutionary economics and linguistics, cybernetics and cognitive theory" (Amin, 1999).

In the following section I briefly discuss the 'new' theoretical conceptualisation of the region and the relationship between the firm's competitiveness and its regional/local environment.

#### ***IV.1 The rediscovery of the region and the firm in 'new economic geography'***

During the last decade the region has been rediscovered, not only, by economic geographers but also researchers of other social science disciplines. A growing number of social scientists—often inspired by new sets of ideas labelled 'flexible specialisation', 'networking' and 'post Fordism'- have argued that regional production systems, industrial districts and technological districts are becoming important. The attention was attracted by the observation that in a world of intensified globalisation the region seemed to gain/retain power as a source of competitive advantage and success. The examples of

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<sup>13</sup> The 'Social capital', similar to the above notion of 'institutions' refers to 'features of social organisation, such as networks, norms and trust, that facilitate co-ordination and co-operation for mutual benefit' (Putman, 1993) and comes to challenge the previous notions of 'physical capital' and 'human capital' that prevailed in classical and neo-classical economics respectively (Asheim, 2000)

<sup>14</sup> Two broad categories can be made of culture as a) ideas (understood as beliefs, attitudes, understanding, myths, values, norms, etc.) and b) as social practices (traditions, established way of behaving, etc) (Oinas, 1998). Saxenian, distinguishes between three different types of culture: 1) Regional culture: shared ideas and social practices that remain relative persistent over time in a (typically subnational) spatial entity 2) A regions Industrial culture and 3) organisational culture.

successful regional economies and industrial districts were not limited (Some of the most well known are: Emilia Romagna, Baden Wurttemberg, Silicon Valley). Under this observation an interesting research started taking place around the region and its importance as a source of dynamism and competitive advantage of production systems and capitalism.

A broad distinction can be made between two different conceptual strands that have developed in economic geography working with the above idea. The first one, that we will call NEG<sup>15</sup> I, is associated with the work of Krugman. The main characteristic of this strand is that it is closer to 'mainstream' economics, using mathematics and formal modelling. This strand has become quite popular due to its purely economic reasoning.

On the other hand there is the NEG II that is highly associated with the 'cultural turn' that takes place in economic geography. As Perrons (2000) comments, the issues considered intangible or 'messy' by the NEG I form the substance of NEG II. Specifically, in NEGII it is the 'soft' factors – that is, relational, social and contextual aspects of economic behaviour, which are mostly emphasised. These are referred to as 'untraded interdependencies' (Storper, 1995) or 'institutional thickness' (Amin and Thrift 1994).

Martin (1999) makes a very interesting critique of Krugman's 'economistic' approach and argues that it suffers from epistemological and ontological limitations. Specifically, Martin criticises the reluctance of Krugman to involve 'messy' social, cultural and institutional factors in his analysis. On the contrary, Martin argues that the embedded nature of social, institutional, cultural and political aspects of local and regional economies play a key role in determining the possibilities and/or constraints on development, and therefore spatial agglomeration occurs in particular places and not in others. In the first theoretical strand, a fundamental problem with previous schools is their reliance on neo-classical economics to explain firm behaviour. It draws from endogenous growth theory to support its arguments on theories of economies of scale, reduction of transaction cost and economic externalities. The focus of the school is predominately on 'traded' relations, typically conceptualised on input-output relations.

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<sup>15</sup>NEG stands for new economic geography according to the categorisation that Perrons makes (2000)

More recently however, the rediscovery of the region has begun to draw on insights offered by institutional and evolutionary economics where emphasis is put more on the 'untraded interdependencies' of the region (Amin, 1999). Storper (1995, 1997) accentuates the role of 'untraded interdependencies' (labour markets, local conventions, norms and values, public or semi-public institutions) in order to explain the observed spatial patterns. Transaction based approaches cannot be figured into the field of untraded interdependencies opened up by evolutionary economics.

Although untraded interdependencies seem to be rooted in transactions and market contract exchanges- the analysis of such cannot easily be accommodated within transactions-cost based theories" (Storper, 1995, p 207).

Storper argues (1997) that these untraded interdependencies have become the most general, and necessary, role of the region. It seems that they take the form of conventions, informal rules, and habits that co-ordinate economic actors under conditions of uncertainty. These relations constitute region-specific assets in production. He suggested that distinctive insights into why the local continues to matter as a sphere of economic organisation in which globalisation is consistent with the localisation of economic activity is the strength of their 'relational assets' or untraded interdependencies'. Furthermore those assets are claimed to be scarce in contemporary capitalism and therefore they constitute a distinctive characteristic that can be used for the growth of the region.

These relational assets are claimed to have an impact on the competitive advantage of firms through the effect they have on the learning ability of firms and consequently on the region's competitive potential. The relational assets or untraded interdependencies constitute the learning environment of the firms.

#### ***IV.2 The firm's environment and its competitiveness***

A major question for economic geographers is how much the place<sup>16</sup> where the firm is located affects its performance and its competitive strategies. It is a subject of questioning

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<sup>16</sup> I adopt Ettlingers (2000) definition of the 'place' as the variety of social, economic, political ecological and cultural processes occurring in a locality

whether it is the firm or the environment of the firm that is the main actor of competitiveness. Is the competitiveness of the firm constituted on the level of the firm, industrial system, or network? How does the place and space where firms are located affect its competitive strategy?

A significant number of studies have tried to examine the relations of firms with their local and regional environment in order to understand how they are affected by their environment and vice versa. Many economic geographers, trying to identify the reasons for the success of certain firms, are looking into the productive system and networks within which firms operate. Yeung (2000), making an evaluation of 'the firm' in industrial geography, is looking into the relationship of the firm with networks, institutions and regional development. Others are looking into the economics of sunk cost on firms' competitive strategies (Clark). Furthermore, more recently they are focusing on cultural bases of industrial organisation and corporate behaviour (Schoenberger, 1997; Saxenian, 1994). Finally the last, and perhaps most popular, theory that develops around the firms' competitiveness and its local/regional environment is related with the notion of knowledge learning and learning economies.

Saxenian (1994) emphasises the culture of the region in her explanation of firm's failure or competitiveness. She develops her argument by comparing Silicon Valley and Route 128 and arguing that the successful story of the latter and the less successful story of the former are based on their cultural and institutional legacy. Firms, to Saxenian, "are embedded in a social and institutional setting that shapes, and it is shaped by, their strategies and structures". In Saxenian's analysis firms are entrenched in their regional environments, providing a basis for their success (or lack of it) in competition" (Oinas, 1998). In other words, firms are embedded in their regional environments and their competitiveness is not only a result of firm characteristics alone but a result of its embeddedness in an industrial system, characterised by a practical kind of regional industrial culture and supported by the wider regional culture. Saxenian tries to prove that the competitiveness is created in the level of the region, not that of the firm; firms are not key actors, regional networks are.

Similar ideas have been expressed by Amin and Tomaney (1998). They argued that companies or nations do not compete in global markets, but productive systems including individual districts, clusters and value chains do. Using similar reasoning, Ettlinger (1996) examines firms performance in the US, in the context of an industrial system. Firms and their performance are part of a system; one firm's performance is tied to the performance of others.

Oinas (1997) also attempts to examine the nature of firm-environment relation. He claims that it is not possible to understand regional development without understanding the key economic actors who affect the development of the regions (i.e. the firm). Although he mentions that it is a rare phenomenon in economic geography to study economic phenomena at the level of the firm. Furthermore he argues that this tradition of neglecting the nature and variety of the firm has also hindered the analysis of the spatial change in relation to theories of organisation and operation of the firm. Oinas, names the resources that firms derive from their institutional environments '*institutional resources*'. (This concept is similar to the one of 'untraded interdependencies'). According to Oinas 'embeddedness' is one term that captures the firm's relations to environments which provide them with such resources or 'interdependencies'.

A comparable idea is that of '*localised capabilities*,' developed by Maskell et al (p.51). Maskell calls 'localised capabilities' all the regional properties that influence the competitiveness of the firms. According to him, firms become competitive, and retain their competitiveness, by envisioning, developing and implementing strategies which utilise several valuable traits and properties specific to their place of location. He also argues that the strategies that the firms pursue can not be completely different to the quality and capabilities of the region (and country) where they are located. By backing and subsidising certain types of activities, while at the same time hampering or blocking others, the potential of a region or country do have a directional effect of efforts of the firms located there. Dicken and Thrift (1992) state that business organisations are 'produced' through a complex historical process involving interactions between specific cognitive, cultural, social, political and economic characteristics of a firm's 'home territory' which ultimately leads to entrenchment or some sort of embedded nature (Porter, 1990). Oinas (1997) interprets that as if "the authors want to point out that

firms operate under influences originated from various societal spheres and competitive situations in certain environments in which they are active in different countries and regions”.

But the subject that seems to attract the most attention, for economic geography, related to firms competitiveness is related to issues of learning and knowledge( Amin and Willkinson 1999, Maskell and Malberg). At the same time the transfer of knowledge and learning is said be easier and/or more efficient at the regional/local level. Regions are therefore said to represent the effective spatial scale for contemporary dynamic development (Perrons, 2000).

#### *V. The firm in a knowledge-based economy*

The turn of the last century proclaimed an entrance to a new era of “Knowledge-based economy”. Drucker in 1993 argued that in the new economy, knowledge is not just another resource alongside the traditional factors of production. He states that it is the only meaningful resource today. The fact that knowledge has become *the* resource rather than *a* resource, is what makes the new society a *knowledge society*, he contends (Nonaka, 1995). Similar ideas have been expressed by highly regarded academics claiming that “knowledge is the source of the highest-quality power and the key to the power shift that lies ahead”(Toffler 1990). This widely projected view that “*knowledge is power*” and hence *a/the* competitive asset for an economy has become an issue of highest interest. Thus, although the notion of knowledge (and its importance in the economy) has a very long history, it is only recently that the interest has become ever so great. Academics from different disciplines expressed a vivid interest to define and explain the new phenomenon and the consequences arising this new “*Knowledge era*”.

Economic geographer’s interest on the above issue seems to have reached a point close to obsession (Hudson, 1999). Some of the themes that appear most frequently in economic geography, recently, are concerned with notions of knowledge and learning since it has been widely accepted that knowledge has become the most strategic resource and learning the most important process (Lundvall, 1999). Hence, a great interest is focused

on the importance of Knowledge and learning in economic performance (of regions and firms).

### ***VI.1 Knowledge creation, local capabilities and competitiveness.***

The learning process is collective activity and its effectiveness depends to a great extent on social interaction and the cultural environment (Amin, 2000). This interactive nature of learning makes geography an important factor to be taken into consideration (Maskell et al 1999). Sharing knowledge, like many other transactions, is “highly sensitive to geographical distance by virtue of the sensitive complexity, uncertainty and recurrence over time” (Storper and Scott 1995, pp 507-508 in Malecki 2000). Therefore, many academics are concerned with the exploration of the role of the region/territory in this learning process. They question how far does the local environment affect firm learning and how far is this learning process space-specific?

In other words, the topics of knowledge and learning, industrial and regional competitiveness and socio-spatial issues (local capabilities, institutional thickness, local and culture) have come to the front of an academic debate in economic geography. One of the main issues that is discussed concerns the importance of geographical proximity as generator of corporate competitiveness through facilitation of learning and innovation.

Maskell et al (1998, 1999, 2000) are arguing that proximity within firms plays an important role in the promotion of competitiveness. First, they presume that the ability of a firm to learn and upgrade its knowledge is one of the most important assets of firm's competitiveness. Proximity between firms promotes interactive learning and consequently helps their competitiveness. Therefore, the proximity of the firms plays an important role since it facilitates exchange of information and collective learning. The advantage of being local and of benefiting from face-to-face contacts, social relations, and embedded institutions and structures is widely known (Malecki 2000). The factor of proximity, according to Maskell, operates in two levels. First, it is the physical/natural geographical proximity that facilitates collaboration (especially when the knowledge is tacit) making its exchange cheaper, easier, faster. The second level is related to a social and cultural dimension (trust, understanding).

The socio-cultural dimension of proximity is dealing with the aspect of knowledge creation as a localised activity, embedded in the cultural context of the area (Maskell, 1999). A shared social and cultural environment, from which develop common routines, norms and conventions which depend upon trust and the willingness to co-operate, enhance social interaction and communication (Amin, 1999). The local culture of some regions can operate as “internal” and facilitate knowledge creation and widespread learning (Malecki 2000). Social relations and corresponding institutions, at all levels of the state, help to promote knowledge creation in industrial networks between firms (Maskell, 1998).

Furthermore, the increased importance of embedded tacit knowledge gives more credit to the importance of geography in the learning process. The concept of tacit knowledge was made widely known by Nonaka, who made a distinction between explicit (or codified) and tacit knowledge. The nature of tacit knowledge “is often collective rather than simply individual, locally produced and often place specific” (Hudson, 1999). One important feature of tacit knowledge is that it is not easily transferable or replicable. Tacit knowledge is embedded in people (on skills, routines etc.) rather than in written form. Therefore, it cannot be transferred easily and it can not easily be replicated elsewhere. Lawson (1998) is arguing that tacit knowledge because of the difficulty to be transferred in the absence of labour mobility may constitute a basis for sustainable regional competitive advantage. Therefore, tacit knowledge can reasonably be argued to account for the sustained competitive advantage of regions and corporations.

This specific character of knowledge is used to explain the existence of agglomerations of related firms. The benefits of proximity can be seen in the ability of interchange of knowledge among firms that constitutes an important part of their competitive advantage. “ The path-dependency and interactive character of knowledge is a key to the understanding of the contemporary emergence and reproduction of spatial agglomerations of related firms” (Maskell, 1998). Proximity and tacit knowledge are also used to explain the competitiveness of industrial districts. Nooteboom is arguing that variety and proximity (owing to the importance of tacit knowledge) encourage learning, which explain the competitiveness of industrial districts under a regime of globalisation. Lawson and Lorenz (1999), also, are trying to incorporate the notions of knowledge

creation and innovation into the theory of industrial districts. They are attempting to develop a notion of 'collective learning' among regional clustered firms that can help account for the innovative capabilities of high tech clusters. They are arguing that an important feature that differentiates from the regional innovation system literature is that they turn for theoretical inspiration to micro level concepts developed in what can be broadly referred to as the capability or competence perspective of the firm.

So, there is a debate whether it is the macro or micro level where 'collective learning' takes place and hence how important is the geographical proximity of firms for their competitiveness. For instance, Sternberg and Arndt (2000) disagree with the recent literature that gives credit to regional and national level for the explanation of the innovative behaviour of (European) firms. They argue instead that firm specific determinants are more important to the firm's innovation ability than external factors (as regional and national characteristics).

Amin (2000a) does raise the question as to the degree to which innovation and learning are territorial properties. He emphasises communities of practice, which highlight the power of relational proximities and distances and defy the simple reduction of learning to geographies of place and space. He argues that codified and tacit knowledge become mobilised for competitive advantage through organisational spaces and their complex geographies, which blend action at a distance and local practices. Thus, he goes beyond the debate about geographical proximity as the source of (tacit) learning and he emphasises the importance of the relational assets of firms (Storper, 1997) in securing innovation and competitiveness. Whether these properties are geographically circumscribed or not may be a secondary issue, primarily due to the fact that effective learning and adaptation is the combined product of informal and formal knowledge, at both the local and global levels. Similarly, Hudson (2001) argues that instead of arguing over territorial and corporate knowledge production and learning we should rather explore the relationships between these two institutional bases of learning.

According to Hudson competitive success is dependant on how companies combine knowledge and learning strategy rather than the strength of ties among firms and their networks or tacit and codified knowledge. Knowledge and learning are important assets

for firms following “strong” competition (i.e. competition that lies on innovation and differentiated strategies) rather than “weak” competition (based on price competition).

### ***VI.2 knowledge and internationalisation process of SMEs***

Knowledge and learning development are also very important assets for firms engaging in foreign markets (Johanson, 1994). According to Meyers (2000) most of the resources crucial for international business are knowledge-based. They include both general knowledge on how to do international business, and country-specific knowledge, such as knowledge on local markets, business practices and institutional conditions.

Meyers (2000) studied the internationalisation process of SME in the CEECs and found out that firms draw extensively upon partners in their home environment for information, experience and support services. The knowledge that acquire through interaction with firms of their home environment is crucial especially in the first stage of the engagement into foreign markets. Indeed, most decisions on entry are based on knowledge and contacts. (Meyers 2000, p.19). Especially when the firms investing are SME then the exchange of information and experience is of great importance. Unlike large multinationals SME rely very much on shared knowledge for their decision making. Even more when the investment takes place in countries with different economic, political and cultural environment, such CEECs. The east European countries representing an unknown, volatile and risky environment and therefore any source of information and knowledge is crucial in firms decision making.

Several authors point to the special importance of network relations for firms doing business within Eastern Europe for creation and dissemination of knowledge (Pervez n Ghauri and Herniksen 1994, Meyers 2000, Johanson 1994). By network Meyers (2000, p.7) means “long-standing relationships between legally independent firms, that exploit mutual complementarities and exchange information”. These networks are generally based on mutual trust and/or common long-term interest and can work as a pool of information. Networks provide a knowledge-pool that grows with the experiences of the

partners and also can provide stimulus to pursue business opportunities. "Firms internationalisation co-evolves with the internationalisation of their networks, as they can draw upon resources in the network and react to opportunities arising with business partners"(Johansen 1994, p.8).

Knowledge can be either objective (codified), which can be taught, or experiential which can be learned by experience (Johansen and Vahlens, 1977). The results from research conducted on SME investing in the CEECs show that practical experience is considered more important than formal knowledge. "Experiential knowledge, such as the understanding of a foreign business culture can be transferred through active involvement, preferably in the host country itself, but not in codified form"(Meyers 2000, p.6). Furthermore, information barriers can be overcome easier by personal contacts. Therefore, personal and professional networks and socialising are essential because the practical knowledge is believed to be acquired by those actually engaged in business. Furthermore, codified information is provided by media, education and formal institutions such as chambers of commerce. But for SMEs undertaking FDI in eastern Europe exchange of view and information with people in the business seems to be the most decisive factor for knowledge creation and decision making.

Another important aspects in the internationalisation process of SME is related to the influence of firms home environment in this process. Meyer's argues that in the case of SME their internationalisation process is influenced by their domestic environment (i.e. cultural, institutional and economic environment). SMEs are embedded more than the large multinational in their domestic business environment. Therefore, decisions and practices of internationalisation are influenced directly and indirectly by the home environment.

Drawing from the above theories and empirical findings, the following chapter will attempt to shed some light on the Greek case of firms engaging in FDI activities in CEEC. The chapter will try to explain the process of how exchange of information and knowledge took place, what kind of networks developed, how decisions were made, what

type of competitive strategies followed and how the home environment of the firms influenced the above process.

## 5. SECONDARY DATA ON FDI AND TRADE FLOWS

### *I. Introduction*

The purpose of this chapter is to provide empirical evidence on Greek FDI and trade with the CEECs and also to analyse and deepen our understanding of this economic process. The chapter is organised in the following way. The first part provides a general picture of Greek FDI in the CEECs. The amount of FDI, the type of investment, the sectors, and the firms are presented. The second section proceeds with a more detailed analysis of the Greek FDI by country and the major recipient countries of FDI are examined. The third part attempts to describe the geographical pattern of Greek FDI and comments on the possible regional impact. The fourth section of the chapter focuses on the evolution of Greek trade with the CEECs. Finally the last part of the chapter employs a more qualitative approach and drawing from the previous theoretical chapters attempts to analyse the qualitative aspects of FDI, explain and evaluate the phenomenon.

At this stage is important to refer to the difficulties faced while collecting data on Greek FDI. The main problem is related to the fact that there is no official body in Greece that is responsible for collecting and processing data on FDI. In addition most of the host countries are also lacking these information centres, with the exception of Bulgaria. That creates serious obstacles in finding reliable sources on FDI flows coming from Greece towards CEECs. It is indicative that the official EU statistics, despite the provision of extensive data for all the rest of EU members, have no figures on FDI data emanating from Greece. Therefore, after extensive search this paper had to be based on a collection of data coming from various sources, mainly secondary. However, although the data that has been collected is quite rich the disadvantage is that it does not exhibit continuity. Furthermore, it should be mentioned that a substantial amount of investment from Greece towards CEECs has been directed through Cyprus and Luxembourg. These numbers do

not appear in the official statistics as Greek investment. Thus, if we take them into consideration the picture of Greek FDI might change considerably.

Specifically, the data has been collected from a number of Greek institutions and international bodies and also by the Greek daily press and specialised magazines. The most important sources are the following: Chambers of Commerce and Industry of Thessaloniki, Inter-Balkan business centre (DIPEK), Ministry of National Economics and Finance (YPETHO), Ministry of Foreign Affairs (MFA), EBRD, Eurostat, Bulgarian Foreign Direct Agency (BFDA), Ambassador reports, Euroinfocentre, limited number of Interviews and collection of articles from specialised Greek magazines and newspapers.

## *II. Greek FDI in the CEECs: the overall picture*

Since the demise of the Communist regimes in 1989, the CEECs have received a considerable amount of FDI. The transition of these countries into free market economies and the opening of their economies created many opportunities. The new conditions urged many Greek companies to take part in that process of investment. The phenomenon was unprecedented for the Greek business world. The Greek firms up to that moment used to restrict their activities within the borders of the country and not to undertake FDI. Most of them had neither the experience, know how or the economic assets for doing FDI. Therefore, the new phenomenon, the so-called "economic penetration" of the Greek firms to the CEECs attracted much attention and raised many hopes about the future of the Greek economy. However, the extent and the nature of Greek outward investment have not been explored thoroughly yet and many questions remain open about its impact on the Greek economy.

The total Greek investment in the region is currently estimated at about \$ 5bn according to Alpha Bank's economic research division. It is estimated that over the past seven years about 2000-3000<sup>17</sup> Greek companies have set-up their operations across Eastern Europe to promote cross-border trade, including retailing and distribution operations, as well as more substantial amounts spent on acquiring and modernising manufacturing plants. The

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<sup>17</sup> Not all the companies are active. The number of active firms probably does not exceed 1500.

number is impressive on its own, and even more when someone takes into account the very poor record of previous Greek FDI before '90. However, this figure reflects mainly small-size investments. Indicatively the total amount invested by OTE, Greece's public telecom operator accounts for almost 1/5 of the total amount invested in the region.

The majority of the investments are concentrated in the tertiary sector (47,2%) (with the exception of Albania), aiming more in the distribution and commercial activities and less in industrial ones (36%) (Labrianidis, 2000). Furthermore, the investments in manufacturing are concentrated in traditional sectors (food products, textiles, apparel and accessories) with most of them in the clothing industry.

The telecom sector accounts for more than a billion dollars of investment in Albania, Bulgaria, the FYROM, Romania and Federal republic of Yugoslavia, mainly by the state-controlled Greek state telecom (OTE) but also by private mobile operators (Panafon-Vodafone). The next biggest group of investors are the banks, where National Bank of Greece has been the most aggressive in terms of establishing branches. Total Greek banking investment in the region amounts to more than \$400 million (EFG Ergasias and commercial bank are active in Bulgaria and Alpha Bank in Romania). Just below banks and telecom in the ranking come the oil and energy sectors. Hellenic petroleum is the leader, with more than \$90 million already invested in FYROM, where it is building the Thessaloniki-Skopje oil pipeline, and in Albania (<http://www.greece.gr/business>).

Specifically, the ten leading Greek investors in the region are: 1. OTE 2. Hellenic Bottling Company (Coca-Cola's Greek franchise holder) 3. Hellenic Petroleum 4. National Bank of Greece 5. Alpha Credit bank 6. Titan Cement 7. Mytilineos (metal trading group) 8. Athenian Breweries (the Greek affiliate of Heineken) 9. Delta dairy (Greece's biggest dairy products and ice cream company) and 10. Chipita (snacks manufacturer).

However, along with these few large companies there is a great number of very small to medium size business that set up their operations in the CEECs during the last 10 years. Those were initiated by small retailers, distributors and/or manufacturers and they do not have much to exhibit in terms of size or invested capital. However, it was mainly those

small entrepreneurs who attempted to do business first in the CEECs, choosing mainly their close neighbourhood.

The first wave of Greek outward investment toward the Eastern European countries initiated in 1989, immediately after the collapse of the communist regimes. Specifically Greek firms were among the first ones that opened the doors of South Eastern European markets. During the first years of the transition it was mainly small (trading and manufacturing) firms that took the risk to invest in a very risky environment. In subsequent years, they have been followed by larger Greek companies that have become some of the leading foreign investors in the region. Therefore it is argued that the first years there was an element of opportunism and experimentation in many of the Greek investments while the second wave of FDI that followed was characterised by more maturity and included some very important investments by large Greek companies (Nautemporiki 1997).

The volume of the Greek investment has not been equally distributed throughout CEECs. A clear distinction of Greek FDI can be drawn between Balkan and non-Balkan countries. Specifically, the vast majority of the Greek investment has been concentrated in four Balkan countries (Bulgaria, Albania, FYROM and Romania) (Table 5-1). On the other hand the Greek FDI to the non-Balkan countries has been marginal (Dimelis & Gatsios 1995, Financial Times 1998).

The first country to receive Greek FDI was Bulgaria in 1989, afterwards Albania and Russia and since 1994 the wave of Greek outward investment expanded to the rest of the CEECs (Labrianidis 1999). At this stage Bulgaria remains the biggest host country concentrating 41.1% percent of the total invested amount followed by Albania and Romania (20.3 each). Russia, as well is a significant recipient of Greek investment and to a lesser extent Poland, FYROM, Ukraine and Yugoslavia (Labrianidis 2001).

The impressive concentration of the Greek FDI in the Balkan countries, at the same time when these countries receive little investment comparing to the rest of the CEECs renders Greece a very important economic actor in the area of south East Europe. Table 5-2 demonstrates the concentration of FDI in few CEECs. Precisely, it is the Visegrad

countries that have attracted most of the FDI. While, on the other hand Balkan's share in the total investment in the CEECs accounts only for 13% (Figure 1).

The relative small size, the poor economic conditions (table 5-3) and the unstable environment in the Balkan region discouraged many large multinational companies. Large multinational companies considered the risks too high and the markets too small. Thus, they choose to place their investments in more promising markets like those of Poland, Hungary and Chech Republic.

On the contrary the Greek companies have been attracted by the Balkan region. Greek companies limited resources and inexperience in FDI prohibited them from attempting big ventures beyond their neighbourhood. They were aware that their competitive advantages were limited outside the region of the Balkans. Therefore, they focused in an "easier" environment were they had more chances to compete successfully. Those two factors in combination; the relative indifference of the international investors in the Balkans in accordance with the active involvement of that same investors in Central Europe combined with the limitations of Greek management, lead into a Greek focus and a leading position in the Balkans (Kamaras, 2001).

Consequently, Balkans have become an area of great importance for the Greek investment activity. Therefore, the following section will provide a detailed analysis of the Greek investment activity in the Balkans by country.

**table 5-1** Cumulative Greek invested capital and number of firms in 4 Balkan countries

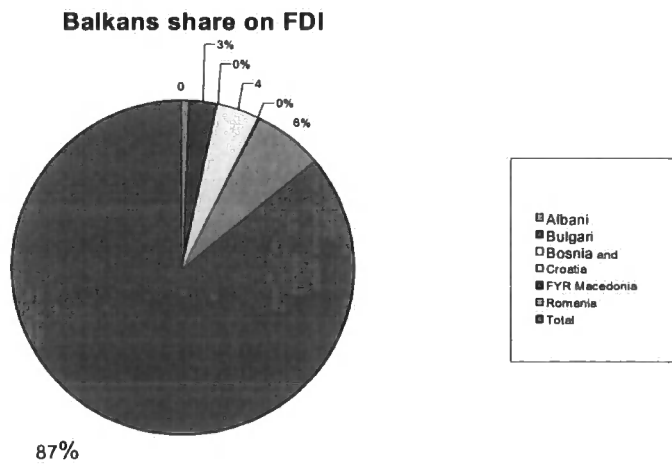
<i>Country</i>	<i>Value million \$</i>	<i>Number of firms registered</i>
Albania	100	300
Bulgaria	489	1700
FYROM	230	150
Romania	500	1679
<b>Total</b>	<b>1319</b>	<b>3829</b>

Source: Oikonomhkh kathimerinh, 04/08/99), YPETHO (Ministry of national Economy)

**Table 5-2** FDI to Central and Eastern Europe

<i>Central/Eastern Europe and the Baltic states</i>	<i>Cumulative FDI inflow 1989-2000 \$ m</i>	<i>Cumulative FDI inflow as per capita 1989-2000</i>	<i>FDI 1989-2000 as per cent of total to region</i>
Albania	546	161	0.005762
Bulgaria	3152	386	0.033265
Bosnia and Herzegovina	307	75	0.00324
Croatia	3984	885	0.042045
Czech Republic	19424	1884	0.204992
Estonia	1882	1307	0.019862
FYR Macedonia	368	184	0.003884
Hungary	19420	1935	0.20495
Latvia	2400	1016	0.025328
Lithuania	2307	626	0.024347
Poland	29052	751	0.306601
Romania	6768	303	0.071426
Slovakia	3611	669	0.038109
Slovenia	1534	768	0.016189
<b>Total</b>	<b>94755</b>	<b>782</b>	<b>1</b>

Source: European Bank for Reconstruction and Development



**Figure 1** Balkans Share on FDI, Source: EBRD

**Table 5-3** GDP in Central Eastern Europe and the Baltic states

<i>County</i>	<i>GDP per capita in 2000</i>
Albania	1195
Bulgaria	1484
Croatia	4245
Czech Republic	4909
Estonia	3409
FYR Macedonia	1689
Hungary	4721
Latvia	2935
Lithuania	3045
Poland	4108
Romania	1600
Slovakia	3736
Slovenia	9319
<b>Total</b>	<b>46395</b>

Source: European Bank for Reconstruction and Development

### *III. FDI by country*

#### *III.1 Bulgaria*

Bulgaria seems to be by far the most attractive country for Greek Investors. It is estimated that around 1700 companies are operating in Bulgaria according to Bulgarian ambassador in Greece (Kerdos, 17/02/2000). During the period 1991-1994 Greek investment in Bulgaria was very important, since Greece was the biggest investor there (70%). However things changed abruptly in 1994 when a huge German investment was realised, and Greece's share fell to 3.6% (Labrianidis, 1999). In 1996, Greece accounted for 6.2% of the total foreign investment (718.5 million dollars) in the country and ranked fourth after Germany (32.8%), Netherlands (9.7%) and Switzerland (7.9%) (OECD 1997, Foreign Investment Agency). In 1998, according to Naytemporiki 1998, the amount of FDI emanating from Greece accounted for 120 million dollars, 10% of the total foreign investment, and that made her the third most important FD investor of Bulgaria.

According to recent estimations the total Greek invested capital in Bulgaria accounts to 489 millions dollars and that renders Greece the second most important investor in the country after Germany (table 5.5). The picture of the Greek investment in Bulgaria has changed considerably during the last two years where large investments took place. That is demonstrated in the tables 5.4 and 5.5. Greece, in 1999 ranked 10<sup>th</sup> foreign investor in Bulgaria, representing only 3.3 percent of the total invested amount (table 5.4). While today officially is second and if we take into consideration the Greek interest investment that goes through Cyprus and/or Luxembourg, that is not included in the official statistics, then it is the most important investor in the country (Dipek, Bulgarian business guide 2001).

The majority of the investments are concentrated in the tertiary sector, aiming more in distribution and commercial activities and less in industrial ones. Furthermore, the investments in manufacturing are concentrated in traditional sectors (food products and beverages, textiles, apparel and accessories) with most of them in clothing industry. There are few large projects by Greek manufacturing companies. Most of the firms are of

very small size, are coming from Northern Greece and invest in the areas close to the borders (Labrianidis 1996, Naytemporiki 1998).

It is estimated that the firms with Greek capital invested employ around 22.000 people in Bulgaria, with the majority of them working in southern Bulgaria for Greek clothing manufacturing firms. The number of these firms is arguable: Naytemporiki (1998) mentions that around 80 Greek clothing firms have moved in southern Bulgaria in order to exploit the cheap labour force of the area, while a report by the Financial Times (1998) rises the number to 200.

The second most important sector of Greek investment is the sector of food and beverages. In this group belong the largest Greek enterprise in Bulgaria: Delta Dairy. Delta Dairy is the fourth largest investment in Bulgaria and has managed to dominate in the Bulgarian market of dairy products Other large Greek investment enterprises are 3E, Intracom, Tsipita and Latsis and Vardinogiannis group (Dimelis & Gatsios 1995, Naytemporiki 1998).

Finally, this activity by Greek firms in Bulgaria is supported and facilitated by the presence of several Greek banks: Xios Bank, Ionian bank, National Bank of Greece.

**Table 5-4 FDI by country 1992-1999 (until 31/06/1999)**

<i>Country</i>	<i>Millions USD</i>	<i>Companies number</i>	<i>% value</i>
Germany	409.8	420	17.5
Belgium	307.9	124	13.1
Cyprus	184.9	200	7.9
USA	150.9	285	6.7
United Kingdom	145.9	172	6.2
Holland	139.3	121	6
Austria	119.4	275	5.1
Spain	105.8	30	4.5
Switzerland	83.1	120	3.5
Greece	76.8	1.331	3.3
Luxembourg	72.4	38	3.1
Ireland	55.9	24	2.4
Russia	50.2	604	2.1
N. Korea	49.5	20	2.1
Turkey	48.7	1664	2.1
France	47.3	127	2
Other	.....	.....	.....

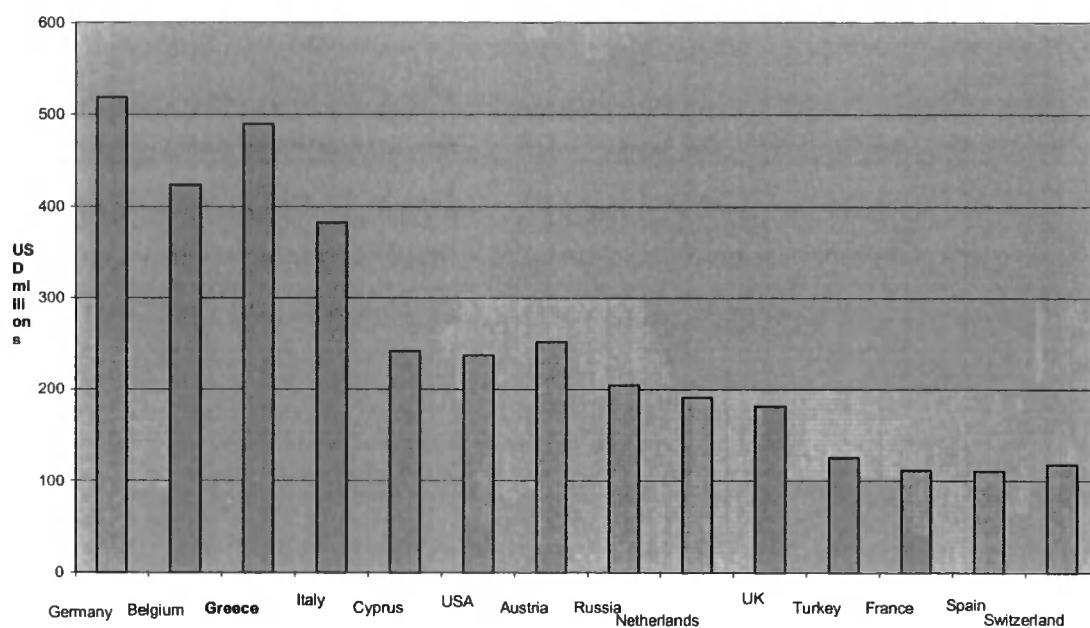
Total	2.343.6	11.000	100
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Source: Foreign Investment Agency in Bulgaria, DIPEK (Inter-Balkan business centre)

**Table 5-5 FDI in Bulgaria by countries and by year in millions of USD**

Country	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001*	Total by countries
GERMANY	0,11	56,63	111,43	16,16	53,10	31,44	55,7	101,3	72,3	20,32	518,5
BELGIUM	0,00	0,14	0,30	10,02	0,79	264,39	31,22	66,22	39,80	0,014	413,1
ITALY	0,01	0,22	5,17	2,27	1,19	0,42	2,06	23,02	339,70	8,02	382,1
GREECE	0,16	5,08	2,97	29,79	14,55	16,10	3,33	14,91	241,1	161,67	489,7
CYPRUS	0,33	1,19	0,39	1,40	7,51	20,55	109,09	108,91	-11,3	3,05	241,1
USA	0,00	10,49	16,15	16,10	20,66	46,61	38,6	49,8	37,1	1,59	237,1
AUSTRIA	13,03	1,02	14,66	1,39	12,07	12,46	46,91	23,39	88,8	37,75	251,5
RUSSIA	0,31	1,35	2,27	15,05	14,37	2,01	14,84	103,74	50,8	0,13	204,8
NETHERLANDS	0,07	0,52	37,94	0,85	46,27	10,80	41,28	27,96	17,4	7,71	190,7
UK	6,2	5,6	2,4	13,7	7,3	15,8	58,9	48,00	22,6	0,46	181
TURKEY	0,00	9,84	1,26	13,74	7,26	9,87	23,76	39,39	19,5	0,65	125,3
FRANCE	0,00	0,22	4,19	4,99	6,51	0,82	3,35	62,72	28,9	-0,49	111,2
SPAIN	0,04	0,06	0,01	0,00	0,00	49,55	56,8	3,21	0,7	0,13	110,43
SWITZERLAND	0,38	6,69	0,24	7,87	23,08	31,36	6,58	13,13	15,0	13,53	117,8
KOREA	0,00	0,00	0,26	0,20	22,31	22,90	1,78	2,81	6,6	0,22	57,1
BAHAMAS	0,00	0,00	0,00	0,00	0,00	0,00	22,76	10,36	14,2		47,3
LUXEMBOURG	0,40	0,58	0,58	0,36	0,23	11,75	22,71	3,81	0,0	7,72	48,1
IRELAND	0,00	0,00	0,02	17,40	0,18	5,21	0,97	3,72	1,0	143,02	171,5
HUNGARY	12,26	0,05	0,00	0,00	0,07	0,00	0,68	1,68	2,0	0,52	17,2
ISRAEL	0,00	0,03	0,93	0,02	1,45	0,01	0,03	13,84	0,00	0,14	18,2
CZECH	0,00	0,00	0,05	2,34	2,28	4,68	0,58	0,09	0,00	25,77	35,92
MALTA	0,00	0,00	0,01	0,12	0,09	0,09	8,9	0	0,5	0,02	9,72
LIECHTENSTEIN	0,00	1,11	0,13	0,01	0,00	2,53	0,79	1,28	3,0	0,2	9,1
SWEDEN	0,00	0,00	0,01	0,03	1,42	2,36	0,94	1,57	0,3	1,47	8,1
JAPAN	0,01	0,00	0,08	0,50	0,60	1,90	1,89	0	1,3	0,53	6,83
DENMARK	0,00	0,00	1,07	0,02	0,00	1,12	1,58	0,33	1,3	0,01	5,41
.....											
Total by years	34,42	102,37	210,86	162,63	256,36	636,16	619,96	806,10	1100,0	303,01	4231,917

\* As of 31 March 2001 Source: Foreign Investment Agency in Bulgaria



**Figure 2: FDI in Bulgaria by countries 1992-2001**

**Table 5-6 Greek Investment in Bulgaria by Sector During 1992-1998**

<i>Sector</i>	<i>Period</i>	<i>Value USD</i>	<i>%</i>
Industry	1992-1998	1.085.300.000	53.65
Agriculture	1992-1998	6.200.00	0.31
Trade	1992-1998	418.900.000	20.71
Construction	1992-1998	37.700.000	1.86
Other Sectors	1992-1998	62.000.000	3.07
Transfer	1992-1998	85.300.000	4.22
Telecommunications	1992-1998	20.000.000	0.99
Tourism	1992-1998	102.400.000	5.06
Finance/Market	1992-1998	205.000.000	10.13
<b>Total</b>		<b>2.022.800.000</b>	

Source: DIPEK (Inter-Balkan business centre)

### **III.2 Albania**

Greece is the second most important investor in Albania with 100 USD millions invested capital (27% of the total investment) and 300 established companies. The top investor in

Albania is Italy with USD 200mln and 600 companies (Investment guide for Southeast Europe, 2001).

The Greek investment activity has been supported actively by a) the 2601/98 development law, that applies in the whole of Albania b) the Phare programme and c) by the plan for the reconstruction of Balkans 2000-2004 according to which the Greek government will support Greek business initiatives in Albania.

Since 1992, the law 1890/92 (2601/98), which is supporting investments in Albania, has motivated a considerable number of Greek entrepreneurs to invest in the country. Most of them are located in the south and South-East part of the country where the Greek minority of Albania lives. Specifically 26.4% of the Greeks firms are located in Koritsa, 16.1% in Argirocastro, 4.6% in Delvina and 22.9% in Saranda (DIPEK, Business guide for Albania)

It is estimated the 300 Greek SMEs operating in Albania have created 7.400 jobs (DIPEK, 2001). However it should be mentioned that most of the investments are of small scale, and are directed to traditional sectors. The investments are mainly concentrated in the secondary sector (91,7%): 40% Clothing, 26% food industry, 10% tobacco processing, 8% building materials and 4% footwear (Labrianidid 1996, Naytemporiki 1998).

**Table 5-7** Greek investment activity in Albania

<i>Year</i>	<i>Value (million \$)</i>	<i>Number of firms</i>
1996	20.44	31
1997	6.45	30
1998	13.14	16
...	....	...
2001	100	300

Source: Greek Ministry of Economics, DIPEK (Inter-Balkan business centre)

### **III.3 FYROM**

Greece is the leading foreign investor in Former Yugoslav Republic of Macedonia, followed by Liechtenstein and Cyprus. (Investment guide for Southeast Europe, DIPEK).

In the case of FYROM the Greek investment belongs in the so-called second “mature” wave of investment. This delay of the investment activity occurred because of the embargo that was imposed to FYROM from Greece as a reaction to the political problems that were created over the name of the new established state. However, relations between Greece and the Former Yugoslav Republic of Macedonia have been steadily improving since the signing of the interim Accord between the two countries in September 1995.

It is estimated that Greek firms have already invested around 230 millions USD. The number of the active firms varies from 50 (DIPEK, 2001) to 150 (Express, 23/11/1999) depending on the source. Nevertheless, what is obvious is that the average Greek investment in FYROM is much higher than the average investment in the Balkans. The Greek investment in FYROM is characterised by relatively large, “mature”, investment projects.

The majority of the investment is directed to the industry (60 million) while the second most important sector is Services. Finally, according to Express (23/11/1999) the jobs created by Greek investment amounts to 4000 and they are expected to be increased to 5000 in the near future.

**table 5-8** Greek FDI in FYROM 1996-30/06/1999

<i>Year</i>	<i>Value USD</i>	<i>% value</i>
1996	1.547.000	1.03
1997	4.383.000	2.86
1998	36.274.306	23.67
1/1-30/06/1999	1.868.949	1.22
<b>Total (including other countries)</b>	<b>153.249.131</b>	

Source: Express 320 issue, results from the international Trade fair of Thessaloniki, ESYE, (National statistic service) DIPEK

### **III.4. Federal Republic of Yugoslavia**

Yugoslavia has been traditionally the closest economic partner of Greece among the Balkan countries. However, during the turbulent years that followed the split of Yugoslavia the economic relations deteriorated and Greece suffered an economic loss.

Today, although the crisis is not completely over, many prospects start to open up for the Greek business. Therefore, the Greek government that kept good relation with Yugoslavia during the conflict is aiming to re-establish and strengthen the economic relations between the two countries. At the moment it is estimated that 230 Greek firms are currently operating in Yugoslavia and the invested amount is approximately 1.4 billion USD. Furthermore, the Ministry of the National Economy foresees an increase in Greek investment in the region of up to ten times its current level in a short space of time. It is expected the number of Greek firms to reach the 2000 or more in the near future. That is even more impressive when compare it to the 150 Greek firms that were operating in Yugoslavia up to June 1992 with total capital invested amounting to 29.9 million DM (<http://www.acci.gr/trade/No20/63-68-pdf>)

Moreover, the Greek government has declared plans to provide 7.5 billion GRD (Greek Drahma) funding for the operation of the Stability Pact, which is based in Thessaloniki. At the same time, Greece has committed to fund Yugoslavia with 205 million EU over a five-year period in the context of the "Reconstruction of the Balkans" plan. The areas where investment will focus are infrastructure, energy, transport, communications, tourism and agriculture.

**Table 5-9: FDI in Yugoslavia by country for the period 1996-1998**

<i>Country</i>	<i>DEM millions 1996-1998</i>
Netherlands	933.4
<b>Greece</b>	653.9
Cyprus	135.9
Bahamas	23.0

Bulgaria	16.6
Italy	16.5
USA	12.9
Austria	12.9
Hungary	7.3

Source: Investment guide for Southeast Europe, 2001

### ***III.5 Romania***

According to a recent report from the Greek consulate in Romania, Greece accounts for 7% of the total invested capital and is considered the 6<sup>th</sup> most important investor in the country (table 5-10). However if in this number is added the investment of Greek interest that goes through Luxembourg, Cyprus and Ireland and also the large investment by OTE (which bought 35% of the Romanian 'RONTELECOM') as well as the investment by 3E then the total invested capital accounts for 1,2 billion USD and occupies one of the first three leading positions as an investor.

In Romania the number of firms with participation of Greek capital has reached 1.700, however, it is estimated that the number of the active firms comes down to 500. Most of the Greek firms are of small size and they operate in trade, retailing and services with a relative absence in the manufacturing sector. There is furthermore an additional amount of Greek FDI, directed to the shipping industry, pending a clearance by the Romanian authorities.

According to Romanian statistics the companies of Greek interests tend to concentrate mainly in Bucharest (77% of the total invested capital) while the second most important destination is the region of Timis (9.5%) followed by Konstanza 5.7%.

Greek-owned banks were prominent in Romania before the second world war, financing Greek ship owners who dominated sailing routes across the Black Sea. Now, we see again some Greek banks investing in Romania. Banca Bucuresti, controlled by Alpha Credit, has established a network of nine branches and is the largest Greek FDI.

The ten most important Greek investment enterprises are: Banka Bukuresti (Alpha Credit) \$7,6 million, Commercial Black sea bank (Emporiki) \$5,9 million, Intracom \$4,4 million, Best foods productions \$3,2 million, Croif Mister \$2,2 million, Frigorex Romania 2,1 million, Delrom (Delta Dairy) 2,1 million, Apemin 1,6 million, Butan Gaz Romania 1,3 million and Star Foods \$0,9 million (Naytemporiki 1998).

**Table 5-10** FDI in Romania by country up to November 2000

<i>Country</i>	<i>Millions USD</i>	<i>Percentage %</i>
France	818.4	11.5
Germany	748.9	10.5
Netherlands	706.5	9.9
USA	662.9	9.3
United Kindom	585.6	8.2
Greece	500.1	7.0
<b>Total</b>	<b>7119.4</b>	<b>100</b>

Source: Report of the Greek consulate in Bucurest, 3075/2/336, 7/03/2001

**Table 5-11** Cumulative Greek investment activity: Number of firms by sector up to 1997

<i>Country</i>	<i>Industry</i>	<i>Trade</i>
Bulgaria	1439	1009
Albania	735	660
Romania	680	431
F.R of Yugoslavia	238	345
FYROM	159	189
Slovenia	39	35
Croatia	46	41
Bosnia	20	21
<b>Total</b>	<b>3356</b>	<b>2731</b>

Source: Study "Investment in the Eastern Europe: Consequences for the Greek industry", Ministry of economic development, general secretary of industry (October 1997).

#### *IV. Geographical distribution of the investment*

It is difficult to formulate a specific spatial pattern of Greek FDI, mainly due to lack of information. Nevertheless, the following broad observations have been made regarding the origins and the destination of Greek investment.

First of all it is very obvious that, as was mentioned in the beginning of this chapter, there is a very strong concentration of Greek FDI in the Balkan countries. The Greek firms are represented very well in the Balkans but have a very poor record in the rest of CEECs. After all, "the role of geography (adjacency and proximity) seems to be a decisive factor affecting the allocation of Greek investment in the region"(Petraikos 2000).

The majority of the Greek firms that contacted FDI in the CEECs tend to concentrate in the capital cities of the host countries (Bucurest 91.2%, Moscow 83.3%, Skopja % Sofia 48.5% ) (Labrianidis 1998). The concentration in the cities is more common among the firms active in the tertiary sector.

Looking on the above figures it is obvious that the tendency for concentration in the capital cities of the host countries is less strong in the countries close to the Greek borders (i.e. Bulgaria, FYROM, Albania) than in the others. That can be explained by geographical proximity. Many firms are attracted in the southern part of those countries taking advantage of the short distance with Greece.

Thus in Bulgaria, a large number of Greek firms are concentrated in the cities of Petritchi and Blagoevrad in southern Bulgaria. This is the case mainly for Greek manufacturing firms in the clothing sector. As far as Albania is concerned there is also a strong concentration of Greek investment in the south of the country. This is mainly due to the close geographical and also cultural proximity. The south part of Albania is occupied by a Greek minority. Therefore, there is strong spatial concentration of Greek investment in the Greek –speaking regions of Argirkastro, Koritsa and Agioi Saranta.

As far as the origin of the Greek firms is concerned, the majority of them are coming from Northern Greece. The proximity of firms of Northern Greece with the Balkan countries has worked as a strong incentive to establish operations especially in the south part of their neighbouring countries.

Regarding the rest of Greece, there is a significant number of firms emanating from the greater area of Athens (where the majority of Greek productive activity is concentrated). According to Labrianidis the Greek firms based in Athens are not equally sensitive to the proximity factor. Therefore they do not invest as much in the immediately close countries (as in Bulgaria Albania and FYROM).

#### ***IV.1 The regional impact***

Northern Greece is the region where the impact of the reforms has been felt most strongly. Since the early years of the reforms there were great expectations about their consequences on the region. Due to its geographical proximity to the Balkans, Northern Greece, was accepted to be the region which would enjoy most of the benefits. The demise of cold war barriers would allow Northern Greece once again to look northwards to what is often called by analysts as its "natural hinterland" (Kostopoulou, 1996).

The benefits were expected to arrive first for the intensification of economic activity in the area. It was expected that the liberalization of previous "closed" economies of the Balkans would give a great boost for the local producers by enabling them to trade, cooperate, establish business and take advantage of the cheap labour force of the Balkans.

Furthermore, the whole region of Northern Greece and especially its capital, Thessaloniki, was expected to play a significant role as commercial center of the Balkans. Based on its geographical location, a glorious past and its economic strength, Thessaloniki was claimed to become a central trading point and a transit center. This argument is further supported by the choice of the city as a headquarters by several private and public organization related to the reconstruction of the Balkans.

However there is a great element of exaggeration in the statement that Thessaloniki is "bound to become" the metropolis of the Balkans. Thessaloniki has undisputable advantages as a major capital city in Northern Greece but nevertheless we should apply some scepticism about the alleged benefits and economic prospects for the city and the whole region.

Indicatively, there are signs of negative consequences on the regional level related with job loss in the region. Specifically, the region of Drama (which borders with Bulgaria)

suffered a serious job loss during 1988-1996. That was mainly due to local firms relocating their operation to Bulgaria and to a lesser extent to Albania. Similarly in the region of Thrace according to official estimation there was a loss of approximately 6000 jobs in the textile and clothing sector due to closures and relocation of firms in the Balkans (60% in Bulgaria, 20% in Rumania and 10% to Turkey) (interview 1)

Furthermore, another negative aspect from a regional perspective is that the Greek firms that invest abroad return only a small fraction of the value added back to Greece, either in the form of capital, profit, import of raw material etc. The links also of the Mother company and the subsidiary are very loose (Interview 1).

However, at the same time it is estimated that the policy of FDI of Local firms can prove beneficial for the region since can it save also a considerable number of jobs that could have been lost anyhow. The factory Falcon (based in Comotini, Thrace) saved 400 jobs while at the same time created 1000 outside Greece. "The 400 would get lost if the firm didn't relocate in FYROM and Bulgaria" (Interview 1).

Overall the prospects for the region of Northern Greece are optimistic, based either on real or "created" competitive advantages of Greece over its neighbouring Balkan countries.

#### ***V. Trade between Greece and the CEECs***

Along with the FDI flows it is very interesting to observe the trade flows between Greece and the CEECs since 1989. Although an in-depth analysis of trade relation would be beyond the limits and purposes of this chapter, it is considered useful to present the trend of trade flows between Greece and the CEECs. Observing the trade pattern between Greece and the CEECs can be very indicative of the scale of the changes that took place in the economic relations between Greece and CEECs since the initiation of the reforms. Lastly and the most important, is interesting to explain the impressive increase of trade flows between Greece and CEECs and maybe see the linkage between trade and FDI processes.

### *V.1 The evolution of Greek trade with the CEECs after 1989*

The evolution of Greek trade with the CEECs after 1989 is given in Table 5-12 and Figures 1, 2 and 3. We can clearly observe amazing changes in the trade pattern of Greece with CEECs. What really stands out is the reversal in the trend of Greek exports to the CEECs. Between 1989 and 2000 exports rose steadily at an annual growth rate of around 140%. Notably, in the same period, Greek exports to its European partners declined. Another very important observation is that the Balance of Trade (BOT) with the CEECs has been improved in Greece's favour, up from a deficit of 185 millions ECU in 1989 to a surplus of 629 million ECU in 2000.

**Table 5-12** Trade between Greece and CEECs (million ECU)

	<i>Exports</i>	<i>Index</i>	<i>Imports</i>	<i>Index</i>	<i>BOT</i>	<i>RX%</i>	<i>RM%</i>
1989	191	100	376	100	-185	2.78	2.5
1990	169	88.48	339	90.16	-170	2.7	2.18
1991	277	145.03	466	123.94	-189	3.95	2.68
1992	373	195.29	390	103.72	-17	4.89	2.05
1993	720	376.96	460	122.34	260		
1994	765	400.52	571	151.86	194	9.67	3.16
1995	887	464.40	721	191.76	166	10.49	3.64
1996	1,144	598.69	828	220.11	316	12.40	3.72
1997	1,414	740.16	1,065	283.11	349	14.16	4.48
1998	1,404	735.25	1,059	281.58	346	14.49	3.92
1999	1,551	812.23	1,010	268.54	542	15.77	3.84
2000	2,152	1,126.62	1,523	404.96	629	18.45	5.04

*Sources: Eurostat and my calculations*

By the examination of the data we can see that the value of Greek exports to the CEECs (in million ECU) has increased in the period 1989-2000 by 1,127%, accounting, in 2000, for 18.45 of total Greek exports. This change is extremely impressive, still we should mention here that after 1992 the following countries were added in the group of CEECs: Latvia, Lithuania, Estonia, Slovenia, Croatia and Bosnia-Herzegovina. Therefore, after 1992 the increase is partly due to the addition of these countries. This is reflected in the rapid expansion of trade between the years 1992-1993. The value of exports increased from 373 (million ECU) in 1992 to 720 in 1993, that means that between these years there was an increase of exports equal to 93%. This increase is important in the overall understanding of the evolution of trade but nevertheless does not change the main

argument that is since 1989 Greek exports to the CEECs exhibit a remarkable dynamism. This observation becomes even more important when we compare it with the performance of Greek exports to the EU.

**Table 5-13** Trade between Greece the EU and non EU (million ECU)

	<i>Intra EU</i>							<i>Extra EU</i>		
	Exports	Index	Imports	Index	RX%	RM%	BOT	Exports	Imports	BOT
1989	4,706	100	9,717	100	69.2	66.46	-5,011	2,095	4,903	-2,808
1990	4,242	90.14	10,547	108.54	68.01	67.69	-6,307	1,995	5,036	-3,041
1991	4,704	99.96	11,101	114.24	67.72	63.95	-6,397	2,242	6,257	-4,015
1992	5,212	110.76	12,221	125.77	68.70	66.47	-7,009	2,375	6,166	-3,792
1993	4,247	90.24	11,843	121.88	58.91	63.00	-7,596	2,962	6,956	-3,993
1994	4,516	95.96	12,276	126.33	57.13	67.90	-7,760	3,389	5,805	-2,415
1995	5,080	107.95	13,879	142.83	60.11	70.10	-8,799	3,371	5,921	-2,550
1996	4,975	105.73	14,328	147.45	53.95	64.42	-9,352	4,247	7,912	-3,664
1997	5,078	107.92	15,432	158.81	50.85	65.01	-10,354	4,908	8,306	-3,397
1998	5,216	110.83	17,732	182.48	53.81	65.62	-12,516	4,478	9,289	-4,812
1999	5,074	107.81	17,401	179.08	51.57	66.19	-12,328	4,764	8,887	-4,124
2000	5,061	107.55	17,744	182.61	43.40	58.73	-12,683	6,600	12,471	-5,871

Sources: Eurostat and my calculations

The high growth rate of Greek exports contrasts sharply with the quite smaller growth rate of Greek imports from the CEECs. Partly due to the difficulties of the transition process, Greece has increased its exports faster than its imports. As a result, its balance of trade (BOT) has turned from negative to positive in the period 1993-2000. This is a very important observation since, the permanent negative, Greek balance of trade is one of the main problems of the country. Now, in the last few years the asymmetry in the growth rate of exports and imports has led to a surplus in the Greek trade balance. In 1993 the Greek BOT was 260 ECU millions surplus and it reached the 629 ECU millions in 2000.

## ***V.2 Geographical distribution of trade***

Although the performance of Greek exports appears to have improved in extraordinary pace during the last few years with the CEECs, the picture is changing when we see it in a different perspective. The extraordinary performance that Greece exhibits in the above table is due to its very good performance mainly in the Balkan countries. In relative terms

Greece is still a minor trading partner for most of the CEECs. Greece's share in total EU trade with the CEECs is negligible comparing to other EU members.

Greek exports exhibit a significant dynamism in the Balkan countries comparing to the Visegrad, which happen to be the main players in the East-west trade. In overall we can claim that there is a dichotomy between Greece's trade performance with the Balkans and the rest of the CEECs in favour of the first.

The above observation might be an indication that geography is, after all, an important factor that affects the trade performance of a country. The explosive expansion of trade with the Balkan countries, comparing with the Visegrad, indicates that economic, geographical, historical, cultural and other factors in operation favour trade in the Balkan region (Petraikos 1996). Finally it should be mentioned that an interest research topic would be to examine the relation between trade and FDI flows.

**Table 5-14** Greek trade balances with Balkan countries (Prices in million USD)

<i>Country</i>	<i>1995</i>	<i>1996</i>	<i>1997</i>	<i>1998</i>	<i>1999</i>	<i>2000*</i>
Albania	223,7	228,0	214,9	157,1	183,1	12,8
Bulgaria	-36,5	-58,8	-97,5	57,4	61,4	5,2
Romania	46,2	30,2	-27,9	28,2	5,0	-2,6
Bosnia	-1,0	0,9	3,3	3,8	9,8	1,25
Croatia	-0,4	3,2	20,8	6,9	-4,8	0,65
Yugoslavia	20,7	91,2	68,7	93,1	53,3	5,0
FYROM	28,4	193,7	212,2	201	364,6	40,5
Slovenia	14,7	-14,1	-5,2	-4,9	-0,3	0,36
Total	295,8	431,8	389,3	542	672	63.2

Source Greek National statistics Service-Ministry of the national Economy (in <http://www.acci.gr/trade/No20/63-68.pdf>) (\* First quarter/provisional figures).

### *V.3 Explaining trade flows*

Many of the studies about the direction of trade rely on the so-called “gravity” model. The fundamental point of this model is that the volume of trade flows is very much determined by the physical distance between areas. The gravity model is considered a useful tool in explaining the pattern of international trade flows and has been used to estimate the effects of economic reforms in central and eastern Europe. According to the model the increase of trade between Greece and the CEECs can be explained by the proximity between the areas.

A research done by Dimelis and Gatsios (1995) tried to estimate the potential trade flows between Greece and the eastern European countries, within the prospects of an integrated European market, based on a gravity model. According to the results the prospects for trade between Greece and the CEECs, within the prospects of a more integrated CEECs in the European market, appeared very promising. An EC gravity model has been used also by the Commission of European Communities (CEC, 1993) in order to estimate the impact on the EC regions of trade generated by economic reforms in Eastern countries. The gravity model made the assumption that the physical distance between the regions is the primary determinant of the volume of trade flows. Therefore Greece was predicted to be the main recipient of the gains, among the less developed regions of EU. Similarly, more recent researches (Egger, 2001) are also predicting economic profits and increase on trade flows for Greece mainly due to its close geographical proximity with eastern European countries. Overall, it can be argued the impressive performance of Greek trade with the CEECs can be explained quite satisfactory by the gravity-model predictions.

However, a further explanation can be added to this one, looking more at the real processes and connecting the FDI process with that of trade. Kamaras (2001) has been arguing that the impressive increase of Greek exports to CEECs lies on the economic activity of those Greek entrepreneurs that build distribution networks and created linkages between Greece and CEECs. Behind the extraordinary performance of Greek exports lies the activity of those Greek entrepreneurs (primarily small to medium sized merchants-distributors), businessmen that had been marginalised in Greece, who established a presence in the countries of the region in the very early years. “In the



absence of the population of merchants-distributors the average Greek exporting company would have stayed inactive” (Kamaras, 2001, p.11).

According to kamaras the average Greek exporting firm would not have been able to materialise exports because it lacked the managerial and financial resources to establish distributorship. Furthermore it was also unable to evaluate, take risks and approach the local private sector and finally was unwilling to deal with the illegal environment that characterised the early years of the reforms.

Therefore, according to Kamaras approach the trade activity is part of broader network of economic activity of Greek entrepreneur and very closely interrelated to the foreign investment activity. The following section is trying shed some light in the process of FDI, locate whom where those entrepreneurs that engaged in FDI, what type of strategies they followed, the channels through knowledge was disseminated and how the process of FDI has developed over time.

## ***VI. Qualitative aspects of FDI***

The purpose of this section is to provide a more in-depth analysis of the phenomenon of Greek FDI. It will attempt to explain why and how it started and to provide explanations as well as an evaluation of the phenomenon. Several qualitative aspects of the Greek FDI are discussed. Specifically, the issues that are raised in this section concern the process of FDI, the reasons that urged Greek firms to invest (pull and push factors), the factors that enable them to invest, the nature of investment, contributed in the success/failure, the type of the firms invested, their sustainability and the possible consequences for the Greek economy.

### ***VI.1 Why do Greek companies invest in the CEECs: the pull and push factors***

It is justifiable to initiate this discussion by asking why Greek firms wanted to invest in the CEECs in the first place. What urged them to contact FDI in those countries? According to a survey conducted by Labrianidis (1999) the reasons that urged the Greek firms to invest in the CEECs can be divided into two categories: push and pull factors.

The Push factors are those that push them outside the Greek market. Those are the saturation of the Greek market and intensification of competition mainly due to import penetration and the deteriorating competitive advantage that firms had over the labour cost (especially in the those labour intensive sectors i.e. clothing and footwear industry).

The Greek firms competitiveness has been deteriorating gradually for many years. The entrance of Greece in the EU and the gradual abandoning of the protective measures exposed Greek firms to an intense competition that they were not well prepared to face. Therefore, many Greek producers that were facing serious problems with selling their products in the EU could find a relatively easy outlet for their products in the CEE countries. Especially the Balkan region represented a new regional market where they could relatively easily sell their products since those markets were not mature yet and the Greek firms could compete successfully on the base of low-cost products. Furthermore, for many producers the Balkans represented the solution for their lost competitive advantage of low labour cost in the country.

On the other hand, several pull factors attracted the Greek firms to invest abroad, those are the following: a) the possibility of lowering the production cost by reducing the labour cost (which for many labour intensive industries is very important). b) The possibility of exploitation of raw material (such as mineral, agricultural or animal products) aiming either to produce there (for the local market or for exports) or to import them in Greece for the needs of the firm. c) The rush of some firms to invest first in order to get a good position in the market (especially for consumer goods such as ice-creams and beverages). d) In order to avoid problems with customs or any other problems in the importation. e) To take advantage of the good linkages with the other CEECs, and use them as platforms for their export activities to other CEECs f) the fact that the are still new, undefined markets, which means that the Greek firms would have the opportunity to compete on the cost basis rather than in quality. Finally the first flow of Greek firms was followed by other that followed their customers (such as banks, insurance companies, packaging firms).

## ***VI.2 Competitive advantages of Greek firm***

The question that follows is related to the factors that allowed the Greek firms to invest successfully in the CEECs. The Greek firms had to have some competitive advantages over the local companies as well as to the other foreign competitors in order to be able to establish successful investment projects.

One of the factors that facilitated the successful investment activity of the Greek firms was the relatively indifference of large foreign companies towards the Balkan Market during the early years of transition. As was mentioned in the beginning of this chapter and supported by table 5.1, the Balkan Market due to its small size, weak purchasing power and slim prospects for the future was unattractive for the large investing companies. The mass market was expected to remain poor beyond the planning horizons of most of the multinationals (Dawar N & Chattopaddhyay 2000). Therefore, the Greek firms faced a relatively reduced competition at least in the first years of transition in the whole area of the Balkans.

Secondly, it is claimed by Kamaras (2001) that the MNCs suffered from diseconomies of scale compared to the Greek firms. "For an MNC to...internalise essentially regional and local expertise and regional and local entrepreneurship on a global scale, it is often impossible. In that respect diseconomies of scale are an ever-present danger for ever the most well run MNC". A proof might be the fact that many MNCS have chosen to enter the Balkans through their Greek subsidiaries and partners.

Labrianidis (1999) also maintains that Greek firm's familiarity with the unstable environment of the Balkans was a great advantage over the large MNCs. Furthermore, the Greek firm's structure, small family-run type, paradoxically proved to be an advantage regarding the speed of response and decision making. Greek firms were more flexible, decisions could be taken faster and the involved risk was smaller. Another advantage of Greek firms was the fact that could combine host and home country assets. An excellent example of that was the use of a relatively cheap skilled labour force from Greece. Finally one factor that was of great significance was the close proximity of Greece with the Balkan countries.

As far as local firms are concerned, Greek firms were far superior in terms of available capital, know-how and linkages with the western markets (Labrianidis, 1999). However, it is significant to mention that the competitive advantages of Greek firms over the locals are weakening over time. Host firms are improving, learning and adapting to the free market conditions and might become significant competitors for the Greek companies in the near future.

### ***VI.3 Characteristics of FDI: type and control mode***

Another question that is raised is about the nature of the assets that Greek entrepreneurs have acquired in the region. Since most of the host countries companies are facing serious problems (organisation structure, obsolete machinery) it is justifiable to query about the worth of the asset attained by the Greek investors. This can be answered by looking into the type of investment done and the reason that lie behind it.

As far as the type of investment three main classification can be made according to the main objective of the investment itself: Exporters, Local suppliers and Distributors. while the three main control mode categories are: wholly owned, Joint venture and Licensing-franchising.

The majority of the Greek companies prefer to do joint ventures with local producers. That depends on several factors that are behind the general strategy of FDI. By choosing this type of investment firms “can reduce transaction cost as the local firm not only controls key assets but is embedded in local networks and labour markets” (Kamaras 2001). In other words they can use the existing network, enjoy a privilege position (the local labour pool/relations) and avoid problems that would have to face as foreigners (bureaucracy, foreign language, ignorance of the legal system). This type of strategy is mainly followed in the food, beverage and tobacco sectors where the above considerations are important.

Another category of firms is that seeking for resources, like the extraction sector. In this case an early entry can be of crucial importance. Therefore, “Greek companies have also been active acquisition-wise in the cement sector and in the metal extraction and

processing. Two classical examples of companies of this kind are Titan (cement) and Mytilinaios (metal processing and trading).

Finally, there are companies that follow their customers wherever they go. For example the banks followed a customer-follower tactic. "We followed companies we had backed in Greece into the Balkans...that turned out to be a wise policy, given the problems the neighbouring countries faced with economic transition" (Angelos Plakopittas, chief executive of Global Finance)

In the first two cases the replacement of the technological equipment is easy and it is a common tactic for firms to use old equipment of the parent companies in Greece (57.4%) or to purchase new equipment in Greece (35.3%). The consequences from both actions are positive for the Greek economy (Labrianidis). Greek firms invest in order to enjoy spillover benefits and use those countries as platforms for their expansion.

#### ***VI.4 Characteristics of the firms investing in the CEECs***

Finally, one more issue open for investigation is about the nature of the firms that have invested in the CEECs. What type of firms are those that took the risk and the initiative to invest in the CEECs? What were their strategies and what are the possible consequences of this?

At a first look a broad division can be made between two major groups of investors. On the one end of the scale, there are small trading companies, retailers and clothing manufacturing firms (almost exclusively from Northern Greece) that relocate part of their operation in countries such as Bulgaria and Albania in search of a cheap labour force. While on the other, there are some of the largest Greek banks, fast growing firms in food industry and big service companies that saw the opening up of CEECs as an opportunity to expand their business and become the multinationals of the Balkan region. It is mainly the latter group that creates many expectations about the future of the Greek economy and the role that can play in the Balkan Peninsula.

The latter group of companies has been strengthened in the last decade by a process of mergers and acquisitions. Furthermore, the comparative advantages that they have compared both with local producers (possession of capital and know-how) and foreign

investors (geographical proximity and better familiarity with the environment) gave them the potential of economic penetration in CEECs and especially in the area of Balkans. Those companies are presenting a very dynamic profile, investing widely in CEECs and arguing that the investment in those countries is not merely an opening to new markets but a strategic movement to become a “ regional power” in the area of Southeast Europe (To Bima, 8/11/1998).

On the other hand the majority of the Greek FDCs are characterised by small size, little invested capital, and lack of long run strategic plan. Furthermore most of those small companies have been relying on a cheap labour cost and the trade of low-price and relatively poor-quality products (Labrianidis 1997). Therefore, this type of investment has been criticised for not making a significant contribution into Greece’s economic development and competitiveness. On the contrary, it has been claimed they are focusing only on the temporary, short –term gain and that their life cycle can be very small since they do not have strategic plans (Express, Hellenews July 1998).

This type of firms were dominating especially during the early years after the reforms (1989-1993). During this period it was very common the phenomenon of “entrepreneurs” who sought short-term profits with no long-term investment perspectives, an “El Dorado” approach.

Another characteristic of the majority of Greek companies investing in the Balkans is its weak connections with Greece. According to a survey in Bulgaria, many small firms tend to have no affiliate with a company in Greece or to have very loose relations. The same survey reveals that many companies of Greek interests have no parent company in Greece. That is interpreted to very few links/connection with the Greek economy. Consequently, in this case the benefits for the Greek economy are expected to be minimal (Labrianidis et al 2001). Similar worries are shared by Iamarino and Pitelis according to whom the impact of FDI in Greece depends crucially on the strategies followed by the FDIIs.

That is a very common phenomenon in the clothing sector, where firms are relocating all or part of the operations to the Balkans in order to find a cheap labour force. This strategy however has lead, at least for the short-run, to significant unemployment in certain areas

(As in Drama -prefecture of N.Greece-). Furthermore, it should be noted that the perpetual search of cheap labour, and cutting down of cost might prove to be a problematic tactic in the future. Therefore Labrianidis questions whether the investment of those firms offer any benefit for Greece at all.

However, a different view is presented by Kamaras (2001). Although Kamaras does not deny the obvious difference between the two groups he disagrees with the “crude” dichotomy on short-termist, opportunistic action and the long-term sustainable business strategies. Particularly he claims that the dichotomy between short-termist, opportunistic action and long-term sustainable business strategies misses the mark.

Kamaras, stresses the positive aspects of small firm activity and its contribution in the overall economic activity of the Greek business community. He argues that both types of investment are part of the same process and he emphasises the importance of those small-scale investments especially in creating links/channels for trade and further investment. He argues that those investments should be examined in the context of “a social setting which makes available substantial resources and opportunities; a social setting in the absence of which resources and opportunities would simply not exist” (Kamaras, 2001, p.11). This kind of network developed between Greek entrepreneurs is evident in the process of knowledge and decision making that took place in the first stage of investment.

#### ***VI.5 Learning process and decision making***

As explained in the fourth chapter, knowledge is a very significant asset for firms engaging in FDI activities. Especially when the foreign investment is directed to a country like the CEECs where the environment is unknown, volatile and involves high degree of risk then knowledge plays a crucial role.

Therefore, the Greek entrepreneurs investing in the CEECs for first time had a strong desire to apprehend the changes that there were taking place in those countries and to acquire knowledge on the local circumstances. It was due to this eagerness to gain understanding of the new conditions, evaluate the new environment, and identify opportunities that lead to the learning process to take place. In the case of the Greek

firms, characterized by small size and limited financial and managerial capabilities, this knowledge could not be an outcome of a single firm's research. Sharing and exchange of information was of great importance. Therefore, a significant exchange of knowledge and experience was shared between Greek entrepreneurs.

Kamaras (2000) is arguing that significant knowledge was acquired by the first wave of FDI contacted by small Greek traders. The experience gained by those first investors allowed know-how to be built and to be transferred throughout the Greek community. Specifically he claims that "extensive knowledge was accumulated on the purchasing power and evolving consumer preferences of the market in question as well as on regional variations" (kamaras 2000, p.10). Familiarity was also gained. This knowledge and experience played an important role in the decision-making of Greek firms especially during the first years of investment activity.

The learning process followed mainly informal channels. Linkages were established between the first investors and their co-nationals both on a personal and on a corporate level. However, knowledge was mainly acquired through face to face contacts and an informal way of socialising. Despite the formal learning through chambers of commerce, public and private institution and education the learning process took place through socialising and exchange of views and experiences between people in the business. Airports, border crossing, restaurants and bars acted as meeting points where this place type of knowledge-generating socialising took place.

Gradually, since the mid-1990s onwards the investment opportunities changed and the learning process often took more advanced/mature form. One of the most important ways of sharing knowledge was through corporate partnership. Kamaras mentions the example of three corporate alliances, 3E and Athinaiki Zythopiia, Delta and Chipita, Kavex and North Greece Canneries, in order to exhibit how corporate alliances reinforce internal learning process for a company.

Geographical proximity played a very significant role in this process of learning. It made easier cheaper and faster the interaction and exchange of information to take place. Geographical proximity made possible for investors, which often had their base in cities of Northern Greece, just few hours drive from several Balkan capitals, to establish a

rapport and operationalise a partnership with Greek-based companies and Greek executives. Together with the physical proximity social and cultural closeness with the Balkan attitudes and norms facilitated the exchange of information.

### *VII. FDI and the Greek institutional and corporate environment*

The decisions and corporate strategies adopted by Greek firms and their competitiveness could be explained partly from the existing socio-economic environment and the Greek corporate culture.

As it was demonstrated in the firm's theory chapter the socio-cultural and institutional structures are considered to play a significant role in the competitiveness of the firm. The importance of the firm's environment on its competitiveness and behaviour has been stressed also in the previous chapter by several authors (Saxenian, Amin, Oinas etc.).

Especially, when we are dealing with SME contacting FDI, like the majority of Greek firms, then they tend to be embedded more than large multinationals in their domestic business environment and their practices and decisions are influenced by the home environment (Meyers, 2000).

Overall, the Greek economic environment is very demanding and uncertain. The Greek economy is marked by low 'structural competitiveness' in the sense of losing its competitiveness in the advanced international markets. Many firms base their operation on state support (i.e. public procurements, public grants, etc) while innovative sectors are underrepresented in the economy. Furthermore Greece lacks a developed network of company support schemes and the services provided by those schemes that exist leave much to be desired (i.e research institute, Public/local authorities schemes, consulting companies etc).

Furthermore, the Greek state is characterised by weak civil society. As Tsoukalas (1993) argues, the everyday Greek experience of work systematically cultivates "anti-reformist" values and attitudes, while reinforcing corruption, clientelism and personalised reciprocities. This value mix hinders severely the implementation of modernizing

reforms while the solid networks of personalised relationships that fosters are of low restricted trust in nature.

There is lack of community spirit and low trust between the public and private sector. Furthermore, the industrial culture is mainly characterised by individualism and mistrust. The majority of Greek firms are characterised as Street smart, they lack of formal education, they put emphasis on personal contacts and family ownership ethos, have very limited research knowledge and no-understanding of long term needs.

These conditions have encouraged for years attitudes and norms that contributed towards short-term ventures and encourage self centred and undisciplined behaviour (Tsipouri, 1998).

## 6. CONCLUSION

The Greek investment in the Balkans is a novel phenomenon that attracted the attention of Greek academic world and raised many issues. Some of the most important questions raised were related to the nature of the firms that contacted FDI and the impact of FDI in the Greek economy. Therefore, this thesis attempted to shed some light in several aspects related to Greek FDI in the Balkans and to contribute in the understanding of this novel phenomenon. The task has proved very difficult due to its extent and also the difficulty on collecting data concerning FDI in the Balkans. The research did not include primary research as it was originally planned. Therefore, the information is mainly drawn from academic literature, secondary sources, a couple of interviews and closely examination of the press.

The aim of this thesis was to look into the process of FDI taking into consideration the broader changes that were taking place in the area of south East Europe. Therefore, the first chapter attempts to examine the phenomenon adopting a historical and geopolitical view. Although, it is to my knowledge that a single chapter wouldn't be sufficient to cover such a broad and complex issue I believed that it important to delve into it in order to understand the overall context under which those economic development took place. The chapter stresses the importance of the geopolitical position of Greece on its economic relations with the Balkan countries and the impact of the momentous events of 1989 for the Greek economy related to neighbouring countries.

Greece was in geographical isolation from the rest of western countries (its official allies) and in economic "isolation" for its neighbouring Balkan countries due to the fact that belonged in different economic-political blocks, missing benefits that might have arisen from economic interaction with neighbouring countries.

However, the political reforms of 1989 gave the country the opportunity to restore economic relation with former communist countries. Also its upgraded regional position

in the Balkans rendered Greece a significant economic and political player in the area. Its position in the international community (member of the EU and NATO) and its economic supremacy constituted an important advantage over the rest of South-eastern neighbours. The economic opportunities became evident by the performance of the Greek entrepreneurs in both trade and FDI activities. The most striking change was an unprecedented wave of Greek firms investing throughout the Balkans. Therefore, the thesis is focusing on this phenomenon of Greek FDI.

The third chapter focuses on FDI from a national/regional point of view. A wide review on FDI theories are presented and an evaluation of the Greek FDI is attempted. However, Greek FDI does not seem to fit in any single theory which would be sufficient to explain the phenomenon of Greek FDI (i.e. TWMNCs, typical MNCs etc)..

According to the academic literature there are no clear benefits for the Greek economy coming from the investing activity in the CEECs. The results of outward FDI on the home country depends crucially upon the characteristics of the economies involved, strengths and weakness of the national economy, and the strategies followed by MNCs (type and pattern of FDI relations of mother company short-term opportunistic/ long term strategies etc).

Furthermore, there are questions on whether there is a link between Greek outward investment and Greek competitiveness. A distinction is made between private and public profit since competitiveness of Greek firms does not imply competitiveness of Greece. Also the links between the firms and their subsidiaries are proved to be rather weak if any. Therefore, doubts are expressed about the possible benefits that could be generated from Greek FDI activity. The chapter suggests that the Greek government should not consider outward investment as unconditionally desirable. Instead some caution is suggested to policy makers related to supporting of FDI and the design of an industrial strategy which will facilitate outward investment beneficial to Greece.

The fourth Chapter focuses on the firm as a level of analysis. Unlike the previous chapter that looked into FDI from a national point of view, looking at the consequences of the host and home countries, the centre of this chapter is the firm. The theoretical background of the firm is presented and how it is related to society and space. The chapter attempts to

place the firm in its socio-economic environment and examine how that affects firm's strategies and competitiveness. The aim of the chapter is to add theoretical knowledge in order to understand the process of Greek FDI, the learning process and the decision making of Greek firms investing in the CEECs.

The fifth chapter finally comes with the empirical findings which is a collection of data on FDI and trade with the CEECs coming mainly for secondary sources. The chapter is a manifestation of the economic impact that the reforms had on the Greek economy. It is estimated that more than 2000-3000 Greek companies have set-up their operations across Eastern Europe since 1989. The number is impressive on its own and even more when someone takes into consideration the poor records of FDI of the country the years before. The trade numbers are equally impressive. We can clearly observe amazing changes in the trade pattern of Greece with CEECs. What really stands out is the reversal in the trend of Greek exports to the CEECs. Between 1989 and 2000 exports rose steadily at an annual growth rate of around 140%. Notably, in the same period, Greek exports to its European partners declined.

The importance of geographical proximity is demonstrated clearly in both FDI and trade by looking at the geographical pattern of the two. Regarding FDI one can understand the importance of geographical proximity on the one hand by the fact that the great majority of FDIs have been materialised in the neighbouring countries. Moreover, within each country the majority of the Greek FDI is concentrated in the areas along the Greek borders. However, the proximity argument is valid mainly for the smallest firms.

Finally the chapter examines the qualitative aspects of FDI. The characteristics of Greek FDI, the nature of Greek firms, the factors that allowed the investment to take place, the process of learning and decision making, the strategies that followed and the viability of the firms are discussed and tried to be understood under the prism of the existing socio-economic environment and culture of Greece. Greek firms were pushed by the intensification of competition and the deteriorating competitive advantage that firms had over the labour cost (especially in the labour intensive sectors). The advantage of the Greek firms were based on the geographical proximity relatively familiarity with the

unstable environment of the Balkans and the relatively indifference of large MNCs for the Balkans especially during the first years after the reforms.

A broad division is made on the nature of the investors. On the one hand are some large Greek investors (banks, food companies etc) that expand their business and become MNCs. On the other hand a significant number of Greek firms have adopted an opportunistic behaviour towards the reforms in the CEECs. They followed weak strategies focusing simply on cost-reduction and had no strategic plans. Consequently, the future and the viability of those firms are dim and the contribution in the Greek economy rather weak. This attitude could be understood by the general corporate culture of Greece that encourages individualism and short-term ventures. However there is an obvious improvement in the recent years and significant number of firms are following more mature and long-term strategies. Therefore, the strategies that Greek firms are following now are of crucial importance for their future survivor. The firms should stop relying in cheap-cost policies and should invest in quality production.

Furthermore, as far as the regional consequences are concerned, the fifth chapter demonstrated that although there are expectation for great benefits there are also some threats related to the opening of the CEECs. There is some job loss in labour-intensive industries in Northern Greece, which has resulted from the relocation of firms in the CEECs. A further intensification of the competition is expected in the following years specially after the local firms (in the CEECs) acquire skills.

Without wanting to diminish the importance of Greek FDI, the case remains that many Greek firms responded towards the 1989 reforms and the opening of economies of neighbouring countries by adopting short-term ventures, having no strategic plan and following mainly cost-cutting strategies. Although their positive contribution should not be ignored (i.e. establishing linkages and providing useful knowledge information about the economic environment of the CEECs) their overall contribution in the Greek economy is rather poor and their future uncertain.

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