

COUNTRY  
REVIEWS

# OECD Reviews of Foreign Direct Investment

## Hungary

FINANCE AND INVESTMENT

OECD



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# **OECD Reviews of Foreign Direct Investment**

**HUNGARY**



ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

## ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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*Publié en français sous le titre :*  
EXAMENS DE L'OCDE SUR L'INVESTISSEMENT DIRECT ÉTRANGER  
HONGRIE

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## Foreword

This report examines Hungary's foreign direct investment policies. It is based on the results of the first examination since Hungary's accession to the OECD in 1996 of the country's position under the OECD Codes of Liberalisation and the Declaration and Decisions on International Investment and Multinational Enterprises. This examination was carried out in June 1998 by the Committee on Capital Movements and Invisible Transactions and the Committee on International Investment and Multinational Enterprises. These committees, whose members are officials from ministries of finance, foreign affairs, commerce and industry, and central banks, promote liberal, non-discriminatory investment policies through the OECD Code of Liberalisation of Capital Movements and the National Treatment Instrument.

This publication has been prepared by Ms. Eudes Brophy and Ms. Magdolna Sass under the supervision of Mr. Stephen Thomsen and Ms. Marie-France Houde at the Directorate for Financial, Fiscal and Enterprise Affairs of the OECD Secretariat. It is published on the responsibility of the Secretary-General of the OECD.

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## Overview

Increasing both foreign and domestic private investment has been an important element of Hungary's successful transformation to a market economy since the late eighties, although its openness to investment and trade dates back to the COMECON era.

One of the first laws in the region permitting foreign participation was enacted in Hungary in 1972 and further significant legislation followed in 1988 ensuring national treatment for foreign investors. As a result, Hungary quickly gained a head start among the transition economies as an investment location from the late eighties onwards due to its early market reforms and privatisation initiatives, increasingly liberal investment conditions and legislative framework. Hungary offers a stable multi-party political system and economy, a favourable geographic position as a gateway to the European Union and other central and eastern European markets, growing domestic market potential and competitive labour resources in terms of productivity, skills and costs. The Hungarian authorities have succeeded in both attracting and effectively absorbing investment from the beginning of its reform process and since its accession to the OECD in 1996, constantly maintaining the highest per capita levels of foreign direct investment (FDI) in Central and Eastern Europe throughout this period.

Inward investment amounted to about US\$2 billion on average annually over the period 1990 to 1999 and foreign-owned companies now account for more than one-third of GDP and 30 per cent of private-sector employment. Exports account for around 50 per cent of the country's GDP at present and the Hungarian government attributes much of its competitiveness as an exporting country directly to foreign investment. Foreign-owned companies generate around 80 per cent of Hungary's industrial exports. Mechanical engineering products represented over half of Hungarian exports in 1998 and the share of high- and medium-high-tech goods has also been growing rapidly. Overall the strongly export-oriented character of economic growth in the second half of the nineties is reflected in the high value-added of the goods produced and exported by companies with foreign participation. Hungarian affiliates of multinational corporations now account for eight of the country's top ten exporters. In the first half of the nineties, FDI also acted as one of

the catalysts in the process of geographic reorientation of trade from former COMECON to OECD and, in particular, to EU countries.

In addition to its impact on exports, FDI has helped to narrow the investment gap arising between the level of domestic saving and investment, which is especially acute in the case of an economy in transition with enormous modernisation needs. FDI has also provided a source of finance for the balance of payments deficit. The restructuring of those sectors open to foreign investment was more rapid and effective and accompanied by above-average growth rates in productivity and competitiveness in regional comparison. Similarly, inflows of FDI have played a vital role in the restructuring of the financial sector, which is crucial for the efficient operation of a market economy.

In the late eighties and early nineties as legislation affecting FDI was still evolving in Hungary, many of the foreign investors embarked upon small-scale joint ventures frequently based on existing trading links with a Hungarian partner. The pattern of investment inflows was characterised by a large proportion of joint ventures involving minority foreign shareholdings in Hungarian private and state-owned companies and a predominance of small and medium-sized investor companies from neighbouring countries. At the end of 1990, German companies accounted for 28 per cent and Austrian for 18 per cent of a total of 3 684 foreign affiliates in Hungary.

Investment opportunities came more gradually for larger multinational companies, initially through exports, then progressively through the privatisation of state-owned enterprises and, in time, greenfield investments. The early stages of the privatisation process were strongly driven by western multinationals' interest in consumer goods businesses with established markets and brands. Investments by Proctor and Gamble, Electrolux and General Electric are characteristic of this early era and throughout the nineties Hungary privatised a bigger share of its economy than any other OECD country.<sup>1</sup>

After a successful start in the early nineties with two major projects by Opel/GM and Suzuki, greenfield investments gathered pace from 1995, reflecting the increasingly stable investment climate, bringing new life to existing sectors and creating entirely new industries such as car assembly and automotive components. Audi and Ford joined Suzuki and General Motors/Opel and are the leading players in this sector at present in Hungary, their greenfield investment projects having benefited considerably from the support of both the EBRD and the International Finance Corporation and special incentive packages. These and other multinational greenfield investors (IBM, Philips, Sony, TDK) are now among Hungary's leading exporters and, in a new recent trend, are upgrading existing assembly and production plants with higher value added and research and development activities.

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<sup>10</sup>

Joint venture and privatisation investments covered virtually all sectors, green-field investments to date have been concentrated particularly in the engineering sector followed by the food and chemical industries and increasingly the retail sector. The most recent privatisation initiatives have resulted in a strong increase of foreign capital in the telecommunications, energy and financial services sectors.

The main sources of foreign investment are Germany, the United States, the Netherlands, Austria, United Kingdom and France with companies present in a wide variety of sectors and with different forms of investment. Japanese investors (mainly multinationals) have entered the Hungarian market more gradually and almost exclusively (90 per cent) opted for greenfield projects. Multinationals (originating mainly in the United States, Germany and France) account for over two-thirds of the total investment volume. Small and medium-sized German and Austrian companies also have a strong presence as investors. French investors have tended to concentrate on opportunities generated through privatisation projects.

Decisive factors common to all investment decisions in favour of Hungary are its political and economic stability, liberal trade and investment climate and generally well-developed infrastructure together with good productivity levels, a well-educated and skilled workforce and competitive labour and production costs. Generous tax treatment and other incentives were among the elements which proved attractive to some investors in earlier years and, in recent years, investors have responded favourably to regional, export and technology-oriented incentives and schemes.

At the same time, investors' motivations have varied over the years as a function of the timing, size and even origin of the project and company in question. Investment projects have been either export-oriented or focussed on the domestic market and sources of supply. Many of the early investors from neighbouring countries had maintained previous business relationships in Hungary through exports, licensing or service transactions and tended to regard the country as an extension of their home market in terms of both sales and sources of supplies. Their previous experience of business in Hungary and their proximity to the market facilitated their early entry and enabled them to take advantage - frequently through small joint ventures - of gaps and opportunities as they presented themselves on the rapidly changing market at the time.

Although foreign-owned companies occupy a dominant position in the export sector, many larger companies and multinationals were attracted by Hungary's above-average domestic market growth rates and potential as a gateway to other markets of central and eastern Europe, increasingly viewing the country as a part of their global sourcing network. For some the rapid and open privatisation programme created opportunities to gain a foothold in the market by acquiring established local brands and production facilities at favourable conditions, whilst others,

encouraged by tax allowances and access to industrial duty-free zones sought to quickly establish a strong local presence through greenfield investments in new industrial sectors for Hungary or retail and wholesale trading networks. The increased presence of production facilities of larger and multinational companies in Hungary has also encouraged a further category of investors as suppliers followed their customers to serve them in the Hungarian market.

Although outward flows of FDI have been relatively low and mainly targeted countries with favourable tax regimes up to 1998, there was a marked increase in productive investments in neighbouring countries more recently. Some of the outward investment flows are attributable to Hungarian-based affiliates of multinationals.

Privatisation was accomplished in Hungary in a relatively short period of time and with substantial foreign participation, particularly since 1995 when a new privatisation law accelerated the process with increased offers of state assets in cash sales to strategic investors. At the time Hungary was unique in central and eastern Europe in offering foreign buyers generous stakes in key sectors, including utilities, telecommunications and financial services. In addition to improving public finances, the successive privatisation of state-owned companies between 1989 and 1999 brought in modern management capacities, facilitated access to new markets and technology and the upgrading of key energy, water and sewerage sectors which the government would otherwise have been unable to fund. With 85 per cent of the economy now privatised, the role of the Hungarian Privatisation and State Holding Company, ÁPV Rt., will have to be redefined and new sources of foreign direct investment identified to maintain the desired flows on which the economy still depends. The December 1999 amendment of the Privatisation Act foresees a more active asset management role for the institution which may, however, reduce transparency in the management of the affairs of state-owned companies.

ÁPV Rt. maintains golden shares in certain companies in sectors deemed to be of strategic importance in the context of the national economy and state interests. The sectors concerned are mainly energy services and manufacturing of certain consumer products with local brands of largely historic significance. Within the context of OECD-membership, the Hungarian authorities accept the need to limit this practice, although the recent legislative amendment led to only a slight reduction in the number of companies affected. While the existence of golden shares is acknowledged as a potential deterrent to investment, in practice there has been no evidence to date of actual difficulties encountered by the investors.

Hungarian legislation on monopolies and concessions and on privatisation provides for the retention of specific activities to remain under state control. Designated public monopolies concern mainly transportation, postal and certain telecommunication services, utilities and nuclear energy. The 1991 Concession Act however allows foreign investors access to these activities and to the exploitation

of natural resources in Hungary on a national treatment basis through concession contracts awarded by public tender.

In terms of geographic spread, Budapest and north-western Hungary have proved the most attractive regions for foreign investment. In recent years labour shortages have occurred in the more developed western and north-western regions which have shifted investors' attention to nearby centres, now more easily accessible as a result of motorway expansions. The gap in prosperity within the country is reflected in unemployment rates running over 16 per cent in some eastern regions compared to between 4 and 5 per cent on average in the west and a national average of 9 per cent. The government and municipalities are now offering special regional incentives to investors and providing for further infrastructural development within these regions which will be essential as investments follow the line of existing and planned highways.

A comprehensive programme of investment incentives is deployed in Hungary, both to attract foreign investment and to channel flows to priority sectors, activities and regions. Up to 1993, the incentive regime discriminated in favour of foreign investors. Currently, incentive schemes are non-discriminatory and focus on national and local incentives linked to areas such as research and development, regional development, job creation, environmental protection, small and medium-sized enterprises and agriculture. Financial and fiscal incentives are accompanied by an industrial park network and industrial free trade zone scheme that is particularly attractive to companies largely importing inputs and exporting outputs.

Hungary has continued to liberalise its foreign direct investment regime throughout the nineties, consistent with its undertakings as an OECD member country and its objective to obtain membership in the European Union. In 1996 one of the last major discriminatory barriers to FDI was removed with the abolition of prior government approval to obtain shareholdings of over 10 per cent in financial institutions. The Branches Act in 1998 permitted the establishment of branches by non-resident enterprises. Only a few restrictions remain in certain transportation sub-sectors and with respect to asset management services provided by branches of foreign financial institutions and the provision of preferential credit facilities, guarantees and subsidies to small and medium-sized enterprises. The Hungarian government has committed itself to reviewing these. Hungary has concluded bilateral investment protection and double taxation agreements with most other OECD member countries and also ratified the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.<sup>2</sup>

Although the liberal and investor-friendly policies have drawn more foreign investment per capita to Hungary than any other Eastern Central and Eastern European country, there is concern on the part of policy-makers that backward linkages and technology transfers to local, as yet underdeveloped, industries have

remained below expectations. Further efforts are necessary to prevent the emergence of a dual economy with struggling local enterprises and thriving foreign companies and over-dependence on these latter for future industrial development. Recently there have, however, been signs of increased local value-added in some foreign owned companies in Hungary and better integration into the local economy.

Investors, for their part, are generally complimentary about Hungary's investment climate. Some nonetheless have certain concerns regarding the stability and transparency of the legislative framework, the consistency of government policy and commitments and cumbersome bureaucratic procedures that they feel are in need of improvement in order to maintain and improve the favourable business and investment climate. A recent law simplifying the permit application procedure for the employment of foreigners in Hungary constitutes a significant accommodation of investors' needs in one particularly bureaucratic area to date.

Without the same level of investment inflows from privatisation, the emphasis of future investment policy will shift to further greenfield projects, capacity expansions, reinvestments and small and medium-sized enterprises. Other challenges lie in closing the development gap between western and eastern Hungary, fostering better backward linkages between foreign investors and local industry and suppliers and encouraging technology transfers and research and development activities. Recent measures by the Hungarian government reflect an acknowledgement of the need for some reorientation of policy. The government is particularly committed to assisting domestic small and medium-sized companies to integrate better into the competitive environment created by enterprises with foreign participation and to encouraging local entrepreneurs to avail of investment opportunities in neighbouring countries.

## Inward FDI

Over the 1989-99 period, US\$20.7 billion (including contributions in kind) was invested in Hungary and the stock of FDI rose to over US\$19 billion (paid in cash through the banking sector) by end-1999. On a per capita basis, the cumulative amount invested in Hungary in the period 1989-1999 exceeded US\$1 900, by far the highest in the region (Table 1).<sup>3</sup>

A substantial amount of FDI was centred around strategic privatisation projects (see Chapter 4 on Privatisation). In the late 1990s, greenfield and capacity expansion projects assumed a more important role with the increased availability of incentives for investors, including the creation of industrial free trade zones. The total value of greenfield FDI in Hungary was US\$3.8 billion at the end of 1997, representing 296 projects and 22 per cent of total FDI. In 1998 greenfield projects accounted for investments of over US\$450 million with Japanese accounting for US\$200 million alone that year. This trend continued in 1999 with investments by

**Table 1. FDI in Hungary**  
(in US\$ million)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
<b>Contribution in cash</b>										
<i>(i.e. capital transfer through the banking sector)</i>										
Inflow	311	1 459	1 471	2 339	1 147	4 453	2 275	2 173	2 037	1 944
Stock	569	2 107	3 424	5 576	7 087	12 829	14 961	16 086	18 517	19 276
<b>Contribution in kind</b>										
Inflow	589	155	170	142	173	117	57	22	11	6

*Note:* In December 1999, the National Bank of Hungary revised certain earlier figures published with the monthly balances and stocks of foreign assets and liabilities for the period 1995-99. This included the reconciliation of direct corporate borrowing/repayment figures with information reported at later dates. These very recent changes affected existing data on the total inflow of FDI for the years 1996, 1997, 1998 and 1999. For this reason also the data above does not correspond in its entirety with the data in Tables 3 and 4 in Annex 4.

*Source:* National Bank of Hungary (cash), Ministry of Economic Affairs (in kind) – (19th February 2000).

Nokia, Temic and Shinwa, among others, and greenfield projects now account for well over one-quarter of the total investment volume in Hungary.

Developments in the registered value of contribution in kind can be explained by changes in the domestic regulatory environment. Until the end of 1993, contribution in kind could enter the country duty-free and it included items such as computers or cars. Thus, many small companies frequently availed of the opportunity to import these products under these favourable conditions for personal use.

After 1995, many companies transferred their activities to or established them in industrial free trade zones. They were partly induced to do so initially by the fact that companies operating in such zones do not have to pay duties and value-added tax on contribution in kind. After that, many newly established companies with high-value machinery and equipment preferred to operate in an industrial free trade zone. Their contribution in kind is not covered by the customs statistics.

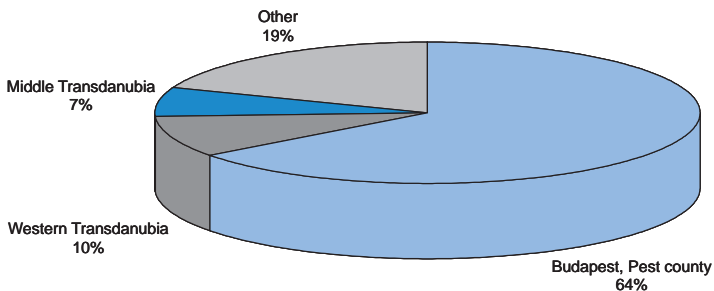
In 1995, the volume of FDI inflows in Hungary was exceptionally high, almost four times as much as in 1994 – US\$4.6 billion in comparison to US\$1.3 billion. This was due in particular to investments in the energy sector where the majority stakes of the gas and electricity suppliers and the two largest power plants were privatised.<sup>4</sup> In 1996, foreign direct investment inflows into Hungary amounted to almost US\$2 billion. The major investments resulted from the privatisation of the power plant Tiszai Eromu, the chemical companies, TVK and Borsodchem, the Hungarian Aluminium Co. (Hungalu), as well as the ball bearing manufacturer MGM, and greenfield investments by AUDI and General Motors. In 1996 and 1997, FDI inflows were almost similar and amounted to over US\$2 billion. In 1997 the process continued with the privatisation of the minority stake in MOL (Hungarian Oil Company) and MATÁV (Hungarian Telecommunications Company), while the K&H Bank was privatised on the basis of a capital increase. The largest privatisation transaction in 1998 was the sale of DAM (Diósgyőr Steel Works) followed by the disposal of a further tranche of MOL shares and Budapesti Eromu (Budapest Power Plant). The privatisation process continued in 1999 reflected in the significant success of the largest capital market transactions of the year: the secondary offering of shares in MATÁV and OTP Bank, Hungary's largest retail bank and the sale of the electricity supply companies TITÁSZ, ELMU, DÉDÁSZ, ÉDÁSZ.

#### **a) Geographic distribution**

FDI is concentrated in Budapest, its surrounding area (Pest County), western Hungary along the Austrian border and in the north west of the country in the town of Székesfehérvár<sup>5</sup> in particular (Graph 1). This pattern largely follows the industrialisation structure of Hungary at the turn of the last century. During the COMECON era most of the heavy industries were concentrated in the eastern part of the country which was most severely affected by their decline throughout the nineties. It



Graph 1. Geographical distribution of the stock of FDI, 1998



Source: Hungarian Central Statistical Office.

should be noted, that many foreign companies maintain their registered headquarters in Budapest whilst conducting operations in different regions of Hungary.

Some of the less developed regions of the country have now started attracting the attention of foreign investors. A recent example of this trend is the “United States – Eastern Hungary Partnership”, a pilot project involving the opening of regional offices by the American Chamber of Commerce in the three main towns of the region, Miskolc, Debrecen and Nyíregyháza. These offices aim to bring together Hungarian and American companies with a view to jointly exploiting local investment opportunities and already claim some early successes in the steel and telecommunications sectors.

Special regional incentives for FDI have also been put into place (see p.34 Investment Incentives) and infrastructural developments are progressing to encourage a wider geographic distribution of FDI, fuelled also by labour shortages in some more industrialised towns and areas targeted by investors to date. Furthermore, a network of some 75 industrial parks - mostly in the traditional industrial regions of the country – provide an attractive starting base for foreign investors in Hungary. 80 per cent of the firms based in these parks are SMEs.

The trend towards a wider geographical spread of FDI has been progressing steadily since 1998, when a significant part of foreign capital targeted the less developed eastern parts of Hungary. This pattern continued in the first half of 1999 and important greenfield investments took place in those regions. The recently extended M5 motorway (between Budapest and the south-eastern town of Kiskunfélegyháza) seems to be becoming the new axis for mechanical engineering investments, thus boosting economic activities in the region. Other major new greenfield

investments were implemented by Elcoteq (Finland), Denso (Japan), Clarion (Japan), Veba Electronics (Netherlands), and Alpine (Japan).

Incentives and tax holidays offered by local governments play an important role in determining the geographical distribution of foreign direct investment. Since 1990, an active local investment promotion policy has resulted in an estimated US\$1.4 billion investment in Székesfehérvár and its surroundings and this area now ranks as one of the 10 fastest growing industrial zones world-wide. The town is located relatively close to Budapest and is easily accessible by motorway. Prominent examples of foreign investment projects here are Philips' VCR greenfield assembly plant, IBM's hard disc production facility and Nokia's car speaker manufacturing plant. Between 1990 and 1995 investing companies were exempt from all local taxes in Székesfehérvár.

### b) Sectoral distribution

The sectoral breakdown of FDI shows a remarkable change in investment inflows (Table 2). During the period of 1990-1994, some 50 per cent of FDI occurred in the manufacturing sector, especially in the automobile and electronics industries and in the traditional mainstays of the Hungarian economy: the pharmaceutical, food and beverage industries. About two-thirds of all greenfield investments were carried out in the engineering sector.

Foreign companies are shifting more and more to high-tech and high value-added products, deciding in some cases to establish research and development facilities in Hungary (*e.g.* Audi, Nokia, General Electric, Knorr-Bremse, ABB, Ericsson, and Sanofi).

Table 2. Sectoral breakdown of FDI<sup>1</sup>  
(as a percentage of total)

	Manufacturing	Construction	Trade	Transport, storage and communication	Financial activities and related services	Real estate and business activities	Other	Total
1995	36.3	12.7	16.4	5.0	9.1	15.6	4.9	100.0
1996	19.3	6.5	17.3	1.1	23.0	26.1	6.6	100.0
1997	19.6	0.7	7.6	0.7	7.2	28.2	36.1	100.0
1998 Jan.-June	30.4	1.9	14.2	1.0	33.6	16.3	2.6	100.0

1. These figures refer to the investment of newly registered companies.

Note: More recent figures are unavailable as the CSO in Hungary stopped collecting data on the sectoral distribution of FDI in this form in mid-1998.

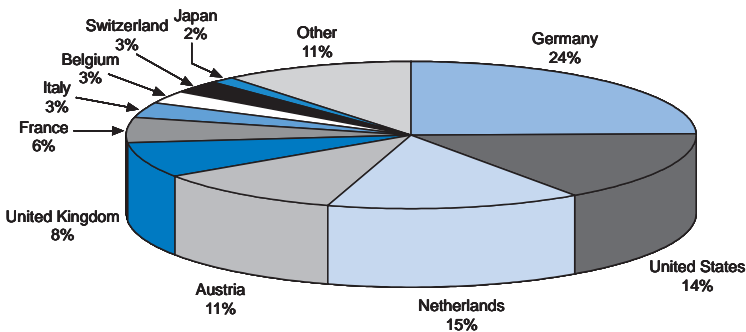
Source: CSO Hungary.

Foreign capital also plays a very major role in the retail trade sector. Ten shopping centres with 268 thousand square metres had been erected by the end of 1998. Four out of the ten were built outside Budapest in the largest rural towns. By 2000 the total value of investment in the retail trade sector is expected to reach around US\$ 800 million and the total shopping area is projected to increase to 1.5 million square metres.

### c) *Countries of origin*

Statistical data on the stock of inward FDI by investor countries are available on the foreign share in the registered capital of companies incorporated in Hungary. According to these data – compiled by the CSO – (Graph 2), the leading investors to date have come from Europe (Germany, the Netherlands, Austria, the United Kingdom, France) and the United States. However, the available data cover only the country of direct origin; therefore they need to be carefully interpreted. Multinationals often transact their investments through their foreign affiliates or through the banks of other than the sending country for tax or other reasons. For example, Siemens of Germany undertook its investment project in Hungary through its Austrian subsidiary. Similarly, one may assume that US companies have invested a large amount of capital in Hungary through their European subsidiaries or affiliates. Accordingly, available statistics are likely to underestimate the role of the US (and, to a lesser extent, Germany) as the ultimate source of FDI in Hungary.

**Graph 2. FDI stock by country of origin, end-1997**  
As a percentage of total



Source: Foreign Direct Investment in Hungary, 1996-1997, Central Statistical Office, Budapest, 1999.

In terms of the amount invested, multinationals account for most of the US and German investments in Hungary, whilst in terms of the number of investing firms, German and Austrian investors are the most active.

Until the end of 1997 according to the same statistical source, manufacturing and the energy sectors dominated German investments in Hungary (accounting for one-third, each from total German investments,), while US investors opted overwhelmingly for manufacturing (61 per cent of their total investments), more specifically for the engineering and chemical industries.

Manufacturing industry attracted 46 per cent of Austrian and one third of the Dutch capital invested in Hungary. Half of French and Belgian, and 25 per cent of British capital was invested in the energy sector. The major part of Italian investments was directed into the financial sector.

Traditionally cautious Japanese investors invested moderately until 1997 and tend to prefer greenfield projects. In recent years there has been an influx of Japanese investors to Hungary, which is a unique phenomenon in the region.

#### **d) Impact on the Hungarian economy**

FDI flows to Hungary have played a crucial role in enhancing economic efficiency and industrial restructuring, and contributed to high rates of productivity gains in industry, reaching a yearly average of 10 per cent between 1992-1999.

FDI played a particularly significant role in the Hungarian economy in the period between 1995-1999. Overall, FDI inflows into Hungary rose from around 4 per cent of GDP in 1994 to a peak of 10 per cent in 1995, and then fell to 4-5 per cent in 1996-99. FDI inflows more than financed the current account deficit, and represented also a significant share of total fixed investment, on average 27.4 per cent over the period 1995-1999, with a peak of over 50 per cent in 1995 and around 20 per cent over the following three-year period. Table 3 shows foreign direct investment trends in Hungary and the other new OECD member countries in the period 1993-1998.

Table 3. **Comparative Indicators of Foreign Direct Investment<sup>6</sup>**  
(in million US\$)

	1993	1994	1995	1996	1997	1998
Czech Republic	654	869	2 562	1 429	1 301	2 540
Hungary	2 339	1 146	4 453	1 983	2 085	1 935
Poland	1 715	1 875	3 659	4 498	4 908	6 365

Source: *International Direct Investment Statistics Yearbook*, 1999, OECD.

There are approximately 35 000 companies with foreign participation operating in Hungary at present. In 1998, companies with foreign participation produced over 39 per cent of GDP, accounted for 53 per cent of manufacturing value added and 30 per cent of private sector employees. The share of these companies rose to around 80 per cent in Hungary's gross exports.<sup>7</sup> Productivity, levels of employment and standards of technology have risen more quickly among these companies than those without foreign participation. Companies with foreign participation tend to be more export- and import-oriented than their domestic counterparts. In the automotive industry, for example, productivity in Hungary has been higher than in Austria since 1997, a unique development among the countries of central and eastern Europe.<sup>8</sup>

Compared to other OECD countries, Hungary experienced an extremely rapid growth in exports between 1993 and 1999. These developments can be directly linked to the presence and impact of foreign direct investments. The progressively competitive position of companies has boosted exports considerably and Hungary's share in the world trade doubled between 1989 and 1999. During the same period there was a geographic reorientation of the outflow of goods from the former COMECON to OECD countries, which now represent almost 88 per cent of total exports.

There are some foreign investors who aim primarily to produce more competitively for export by relocating their production to Hungary and availing of the pool of attractive semi-skilled or skilled labour resources in the country. Affiliates of well-known multinationals account for the bulk of Hungarian exports at present, together with joint ventures or companies that were acquired and restructured by foreign companies in the framework of the privatisation process (Table 4).

Correspondingly, companies with foreign participation produce the most important export products, most of which belong to the engineering sector and usually incorporate high technology (Table 5).

Table 4. **Top ten exporting companies in Hungary (1998)**

Company	Foreign participation	In industrial free trade zone
Audi Hungária Motor Ltd.	Yes (greenfield)	Yes
IBM Storage Products Ltd.	Yes (greenfield)	Yes
Philips Végszerelő Kp. Hungary Ltd.	Yes (greenfield)	Yes
Opel Hungary Ltd.	Yes (greenfield)	Yes
Zöllner Elektronik Vác Ltd.	Yes (greenfield)	Yes
General Electric Lighting Tungsram	Yes (privatisation)	No
MOL	Yes (stock exchange)	No
Videoton Holding Ltd.	No	Partly
Alcoa-Köfém Ltd.	Yes (privatisation)	No
Philips Monitorindustry Ltd.	Yes (greenfield)	Yes

Source: KOPINT-DATORG and other press articles.

Table 5. Top ten Hungarian export products in 1998

SITC	Product	Value of exports (US\$ thousand)	Percentage of total exports	Exporting company with foreign participation?
71 322	Reciprocating piston engines	2 104 555	9.2	Yes
7 527	Storage units (computers)	1 235 681	5.4	Yes
75 997	Parts, access. for automatic data processing machines	678 844	3.0	Yes
76 381	Video recording or reproducing apparatus	659 870	2.9	Yes
7 812	Motor vehicles for the transport of persons	546 868	2.4	Yes
7 526	Input or output units	492 241	2.1	Yes
7 611	Television receivers	330 276	1.4	Yes
71 323	Compression-ignition engines	300 416	1.3	Yes
77 314	Other electric conductors	246 652	1.1	Yes
82 119	Parts of seats	246 337	1.1	Yes

Source: FTS (foreign trade statistics of the OECD), newspaper articles on foreign participation.

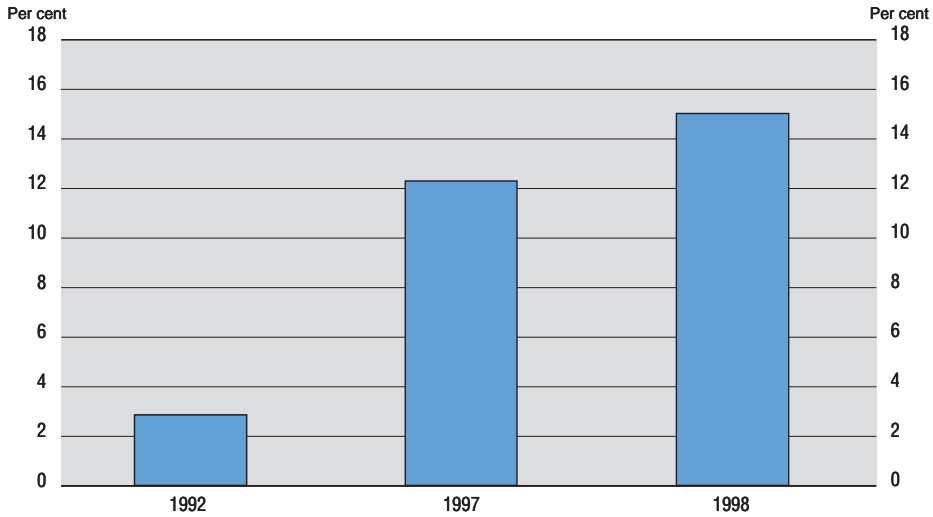
The most important exporting companies and export products belong to the machinery sector (SITC7), the share of which has been growing steadily in the analysed period. In 1998, this sector represented more than half of Hungarian exports.

Similarly, the share of high tech products in exports has been growing significantly in the second half of the nineties. This process resulted in a more than 16 per cent share of high tech products (in SITC) and a more than 23 per cent share of high technology industries (in ISIC) in Hungarian exports by 1998.<sup>9</sup> (Graphs 3 and 4) It is also an important development, that at the same time, the share of medium-high technology industries has been growing even more rapidly, which reflect the realisation of the comparative advantages of a country well equipped with skilled labour.

The role of the newly established and existing restructured companies with foreign participation is reflected in the export trends. Compared to the structure of exports in 1992, new export products had appeared alongside the traditional ones in 1998. At the same time, the major export products of 1992 were able in most cases to retain their foreign markets, which is reflected by similar absolute values of their exports in 1998 (Graph 5).

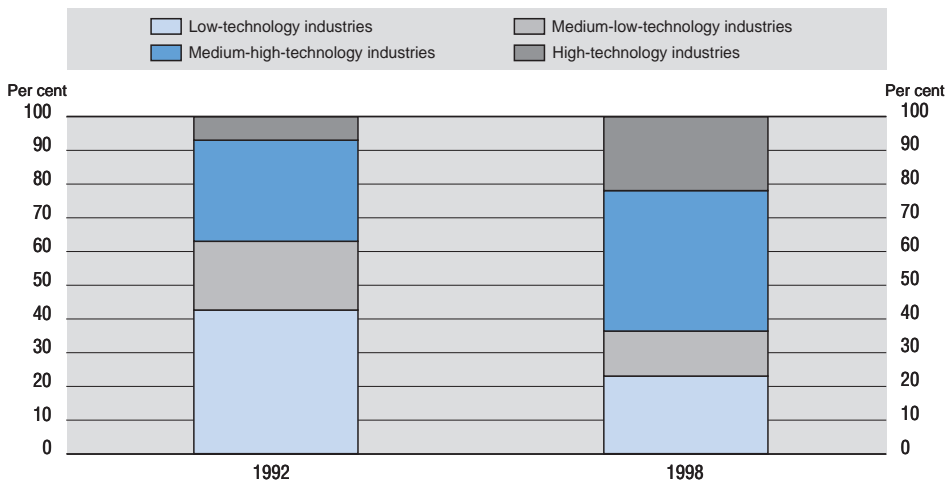
The role of industrial free trade zones in Hungarian exports is increasingly important. In the first 11 months of 1999, they accounted for 43 per cent of Hungary's total exports, compared to 36 per cent in 1998 and 26 per cent in 1997. Large, export-oriented, and usually greenfield investors are attracted to the industrial free trade zones, like most of the automotive manufacturers and their suppliers, and some newly established electronics plants.

**Graph 3. The share of high tech products in Hungarian exports**



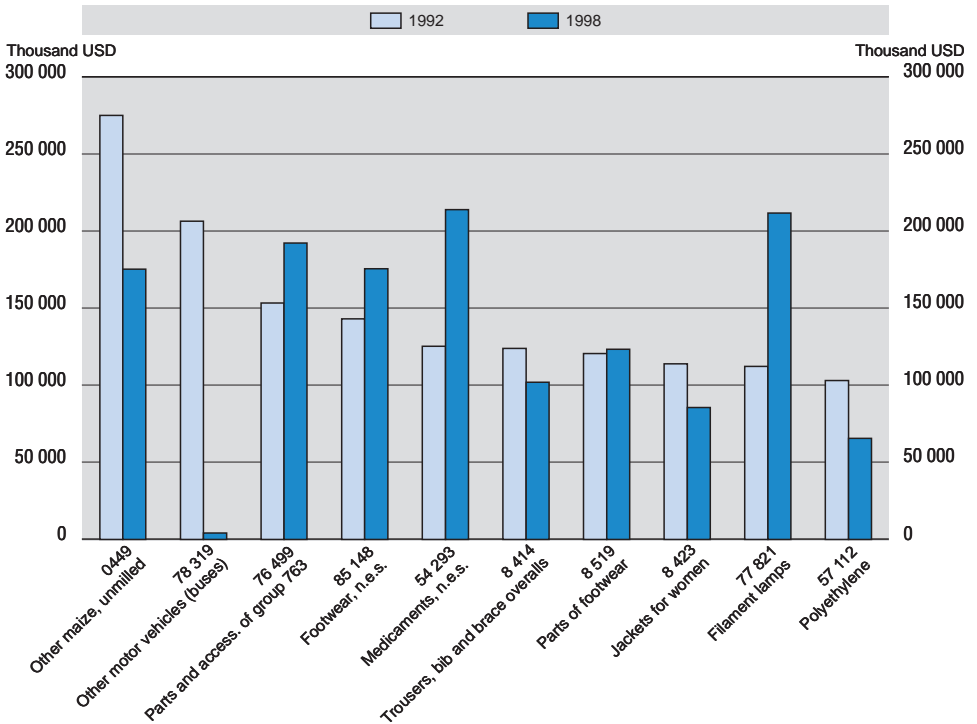
Source: FTS (foreign trade statistics of the OECD).

**Graph 4. The technology composition of Hungarian manufacturing exports**



Source: FTS (foreign trade statistics of the OECD).

Graph 5. Exports of the top ten products of 1992 in 1998



Source: FTS (foreign trade statistics of the OECD).

While the inflow of foreign investments was very high in regional terms and companies with foreign participation play a dominant role in the Hungarian economy, there is concern on the part of policy-makers that backward linkages with the local economy have remained below expectations. Performances of domestic companies and those with foreign participation tend to vary considerably in certain areas such as wage levels, gross value added, net sales, capital base, research and development expenditures and export orientation. This has given rise to fears that a “dual economy” could develop in Hungary, with a more successful “foreign” sector operating in isolation from other parts of the economy.



On the basis of available empirical evidence, however, the picture is not so discouraging. A gradual increase in local value added is reflected in the fact that, compared to 15 per cent in 1997, in 1998 21 per cent of the total supplies of companies operating in customs free zones were sourced from 2500-3000 Hungarian-based manufacturers. The four car companies that invested in Hungary have considerably increased the share of input they buy locally and have at present about 250 Hungarian-based suppliers (see Box 1).

There are differences in local value added and use of local suppliers, according to the type of investment. Understandably, some of the privatised companies have retained their original domestic suppliers since restructuring, particularly if their main focus is on the domestic market, as for example, General Electric-Tungram with over 60 per cent local supplies in its production. In the case of greenfield investments, it can take considerable time to build up a local network of suppliers. Practice has shown that many greenfield investors have tended to build up this network as the company became established over time. Because of the number of preferential trade agreements concluded by Hungary, Japanese and United States investments mainly oriented towards EU or CEFTA markets tend to use more local suppliers than EU investors. On a sectoral basis, the automotive, electronics, food and chemical industries have a higher proportion of domestic suppliers. In addition to the small and medium-sized Hungarian suppliers, some former large state-owned companies were able to survive by becoming suppliers to multinationals with production capacities in Hungary, such as Bakony Művek Rt., Videoton.

In order to foster better linkages with local industry, the government and 49 multinationals signed a "Suppliers' Charter" in March 1998 to strengthen relations between them and domestic small and medium-sized suppliers. This involved the creation of an information network for Hungarian companies, which provides data on 1400 audited suppliers in the automotive, electronics and chemical industries. It is planned to extend the database to include other sectors. Other projects to integrate small and medium-sized domestic companies into the supplier network of foreign-owned plants are also being undertaken.

### **Hungarian investment abroad**

Up to the end of 1995, the Ministry of Foreign Economic Relations and its successor institutions issued permits to domestic companies wishing to invest abroad and the Ministry of Finance provided the exchange permit for these transactions. In 1996, when the new Foreign Exchange Act (Code) came into force, these transactions came under the jurisdiction of the Hungarian National Bank. The 1996 Code lists the conditions governing investments abroad and permission is required only

**Box 1. The automotive industry in Hungary**

The automotive industry, which was almost non-existent in Hungary before the transition period, developed rapidly throughout the 1990s and has become one of the fastest growing sectors due mainly to greenfield and brownfield foreign investments. Opel/General Motors and Suzuki were the first foreign companies to set up car assembly plants in Hungary, followed by Audi in 1998. Other local joint ventures and foreign-owned companies produce car parts and components, some of them following the car manufacturers to Hungary as their suppliers. Opel, Ford, Audi, Denso, Knorr-Bremse are some of the major companies producing automotive components in Hungary, mostly operating in industrial free trade zones.

At present, on the basis of its business performance in 1999, the Audi affiliate is the top Hungarian company. The German company founded its first engine and component production plant in Hungary in 1992 and its Győr assembly plant will produce over a million engines in 2000 and has set up an assembly operation for the new Audi sports coupe with a projected output of 55 000 vehicles this year. The total amount invested by Audi in Hungary has exceeded 1.2 billion DM to date and the company currently employs 5,000 workers.

Ford Motors opened its first spare parts subsidiary in Székesfehérvár, north western Hungary, in 1990. In 1992, Ford Hungaria Kft. began production of fuel pumps, magnetic starters and gears for Ford cars assembled abroad. The investment exceeded 130 million US\$, and about one hundred Hungarian companies supply Ford Hungaria with spare parts and components.

General Motors/Opel established its first car assembly, engines and spare parts plant in Szentgotthárd and was the country's biggest exporter in 1997. Last year, four-fifths of the output was exported. Opel is currently building a new gearbox plant in Hungary that will start production in 2001 with an annual output of 250 000 gearboxes for Opel, Vauxhall and Saturn cars. The company plans to raise local value added in the production of special gearboxes (continuously variable transmission) from 30 to 50 per cent. The total value of investments realised by GM/Opel in Hungary to date is 965 million-DM.

Suzuki established its plant in Esztergom (northern Hungary) in 1990 and is the only Japanese carmaker present in the region. It is Suzuki's principal European production site, manufacturing the company's Swift and Sedan models. This year the Hungarian plant will start assembling the Suzuki Mikro, developed in co-operation with GM/ Opel. Additional investments in the course of the nineties enabled the company to increase its production capacity and to introduce new models. This year the annual output of cars will reach 80 000.

Denso embarked upon a 100 million US\$ investment last year with the erection of a new plant in Székesfehérvár employing 400 people and producing 200 000 diesel fuel injectors annually. The local value added will be 43 per cent and 22 per cent will originate from the EU, in order to reach the 60 per cent required for duty-free exports to the EU.

### Box 1. The automotive industry in Hungary (*cont.*)

Knorr Bremse undertook a brownfield investment project by acquiring and restructuring existing production capacities in Kecskemét and Budapest. The company specialises in braking systems.

More recently, highly skilled labour resources, moderate wage costs and a special government incentives programme have attracted foreign automotive companies to move research and development activities to Hungary, as in the case of Audi and Knorr Bremse. Audi established its third research and development centre in Hungary which will concentrate on engines. Knorr Bremse's Hungarian research and development centre will carry out projects in co-operation with other affiliates of the company in Europe.

The multinationals that invested into the Hungarian automotive industry have developed many linkages with the domestic economy. At present, about 250 local companies supply parts and components to the companies in the automotive industry. This must be considered in the light of the fact that most of these affiliate companies operate in an industrial free trade zone. The shares of local suppliers in total inputs vary in the four automotive companies. At present, in the case of Opel and Audi it remains below 5 per cent. The other extreme is represented by Suzuki, which has the largest network of over 40 suppliers, and an overall local value-added of 53 per cent. Indirectly, Suzuki's role is even greater as many companies that were able to supply Suzuki with spare parts and components also became suppliers to other automotive companies. For example, the Hungarian Kunplast company supplies both Suzuki and suppliers of three other automotive companies (BMW, Ford, Opel), creating a "supplier to suppliers" network which is common in Hungary. Hungarian-owned domestic companies are usually second-tier suppliers and sell parts and components to those foreign suppliers that established a base in Hungary to supply their original customers' local affiliate. This approach was also adopted by many first-tier suppliers such as VAW (aluminium car parts), Lear Seating (car seats) and Peguform (plastic car components), which followed Audi to Hungary. Other examples here are Knorr-Bremse and Denso. About half of the small and medium-sized companies producing parts and components for the automotive industry in Hungary, are in majority foreign ownership.

The Székesfehérvár company of Ford is between the two extremes: the share of local suppliers is estimated to be about 20 per cent. The gradual increase is indicated by the fact that these shares were in most of the cases significantly lower 3 years ago. Thus, in the case of Opel and Ford investments the share of local suppliers was about 8 per cent, and for Audi it remained below 1 per cent. In the case of Suzuki, the share of local suppliers slightly exceeded 30 per cent. Local suppliers can be domestic Hungarian companies, but in most of the cases, are foreign suppliers that have followed the automotive investors to Hungary and supply their customers through joint venture or greenfield productions. Many Hungarian companies can link up with these first-tier suppliers and become part of the extended supply chain of the big automotive companies operating locally.

*Source:* Articles from HVG (Hungarian economic weekly newspaper)

when the investing company fails to meet these conditions. Otherwise, the Hungarian company only has to declare its intention to invest abroad.

While outward direct investment from Hungary was negligible until the mid-1990s, it has recently increased considerably. It amounted to US\$431 million in 1997 and US\$481 million in 1998, and slowed down in 1999 to US\$184 million in the period from January-November (according to the figures of the balance of payments, Table 6). The stock of outward FDI was US\$1.7 billion in November 1999.

Table 6. **Outward investments from Hungary**  
(million US\$)

	1993	1994	1995	1996	1997	1998	1999
Investments abroad	11	49	43	-3	431	481	249

Source: Hungarian National Bank.

The most important investment destinations are European Union member countries (particularly for market entry purposes), other countries with favourable tax regimes (for capital investment purposes) and more recently the neighbouring countries (mainly for the establishment of production facilities and pursuit of trade relations with the host country). The average amount of invested capital varies from US\$10 000 and 50 000 per transaction and the main sectors targeted are trade, services, tourism, and the manufacturing industry. Some of the flows are attributable to Hungarian affiliates of multinationals.

In 1999, there was a particularly marked increase in productive investments in neighbouring countries. Romania, for example, accounted for 40 per cent of outward Hungarian investment. This trend is in line with a recent focus of economy policy to encourage domestic companies to expand into and invest in the neighbouring countries.

### Statistical data and methods

In Hungary, there are differing sources of data on foreign direct investments. The National Bank of Hungary registers the money (cash) inflows. Non-cash contributions ("contribution in kind") are recorded by the Registration Court as part of the establishment of new companies or that of an official capital increase. The Ministry of Trade and Industry gives estimates on the basis of the data of the National Bank (cash inflows) and the customs statistics (contribution in kind). The Hungarian Central Statistical Office compiles its data on the basis of the balance sheets of compa-

nies with foreign participation and the data on newly established business entities. The database of the Central Statistical Office covers companies with more than 10 per cent foreign participation.

The most timely and frequently available figures related to FDI in Hungary is reported in the balance of payments statistics, compiled and published by the National Bank of Hungary. The statistical methodology for compiling these data is as follows:

**Flows:** for monthly figures, the primary source of information is an international transactions reporting system (ITRS), a coding system for credit institutions with transaction-by-transaction reporting above the threshold of US\$50 000 effective since January 1999. Below this threshold, cumulative monthly turnover must be reported by currencies. Banks' reports also include transactions on behalf of their clients. Directly reporting enterprises (having a bank account with a non-resident credit institution) also report their transactions. There is no recording of re-invested earnings and non-cash equity contributions.<sup>10</sup>

There are two main sub-components within FDI in the balance of payments: 1) abroad and 2) in Hungary, both with a sub-classification according to *a*) equity capital (10 per cent or more, corresponding to the OECD Benchmark Definition of FDI) and *b*) other capital (inter-company loans), which in turn includes *a*) assets and *b*) liabilities. All figures are published in net terms.

**Stocks:** the primary source of information is the credit institutions' monthly report on their own outstanding end-of-month positions (equity capital and subordinated loans). Directly reporting enterprises also report on their own outstanding end-of-month positions (equity capital and inter-company loans). Stock data for other enterprises are derived from ITRS as cumulative flows. Re-invested earnings and non-cash contributions are not accounted for in the figures on International Investment Position. Stock data are broken down into the same categories as flows.

A new enterprise survey was launched for FDI flows (quarterly) and stocks and re-invested earnings (annually) in January 1999. The survey results are to be published for the first time in 2000 with 1999 as a reference period.

## General legal framework

### a) FDI Regulation

After a series legislative changes throughout the eighties and nineties, Hungary now has a liberal FDI regulatory regime. There are no screening procedures for the entry and establishment of foreign firms. Non-resident investors may establish partly or wholly-owned companies in almost any sectors and operate their companies on National Treatment conditions. The main regulatory change in the field of FDI since accession to the OECD concerns the establishment of branches of non-resident enterprises which has been permitted since 1 January 1998 (see Box 3). A chronological overview of legislation governing FDI is given in Box 2.

The 1988 Law on Non-Resident Investment, together with other statutes governing business activities provides the legal framework concerning the operations of foreign investors in Hungary. It allows foreigners to create or expand a wholly owned enterprise, subsidiary, representative office or branch or to acquire full or partial ownership of an existing enterprise. Legislation provides for the repatriation of both capital and profits and prompt compensation for investments at real market value in the case of expropriation.

For the incorporation of a local entity, it is sufficient to have it entered in the local Register of Companies. Documents needed for registration include, where relevant, an attestation from a credit institution of completion of the foreign exchange transactions in relation to the investment. Once established, enterprises with foreign participation are entitled to operate on the same conditions as Hungarian enterprises.

There are no restrictions on foreign firms employing Hungarian citizens. Non-Hungarian executive employees do not require work permits. In accordance with the Association Agreement between the EU and Hungary, since February 1999 work permits are automatically issued – on the basis of reciprocity – to key EU personnel of companies provided that they have been previously employed by the company for a period of at least one year. In line with the relevant provisions of the GATS agreement this measure has been extended to key personnel in the services sector of all GATS signatory countries. With effect from 1 January 2000, the permit application procedure for the employment of foreigners in Hungary became easier and

**Box 2. FDI regulation**

- 1972 Legislation permitting the establishment of companies with foreign participation subject to approval by the authorities.
- 1988 National treatment for foreign investments guaranteed without general restrictions or sectoral prohibitions (except for financial institutions). 50 per cent foreign ownership permitted without prior agreement, a license being required for larger interests.  
The law guarantees free and full repatriation of profits and exemption from customs duties for in-kind contributions. Companies with foreign participation permitted to set up their own customs-free zones and tax allowances are granted depending on the foreign share, size and the sector of investment.
- 1990-93 Introduction of incentives for foreign investors (tax relief, repayable or non-repayable grants, special-purpose incentive programmes, etc.).
- 1991 Reduction of the allowances given to foreign investors in 1988 and introduction of specific tax incentives to encourage activities in selected sectors (R&D) and regions with high unemployment.  
Legislation passed allowing the state to grant concessions with time and renewal limits in exchange for investments in infrastructure.
- 1992 Complete foreign ownership made possible without prior agreement.
- 1993 Abolition of tax incentives exclusively for companies with foreign participation. Existing concessions are grandfathered.
- 1994 Amendment to maintain the prohibition of the ownership of arable land by companies with the introduction of licensed purchasing of non-agricultural land by foreigners.
- 1995 Revised privatisation law introduced to accelerate the process. Abolition of duty-free treatment for in-kind contribution connected to FDI.
- 1996 Financial support programmes consolidated in the „Targeted Allocation for the Development of the Economy” programme, managed by the Ministry of Industry, Trade and Tourism. Removal of prior requirements for foreign investments in financial institutions.
- 1998 Legislation permitting branches introduced.

faster as the range of persons eligible for automatic permits was extended (8/1999 Decree of the Ministry of Social Affairs). Filling certain posts continues to be exempt from the requirement of a work permit including management positions in foreign-based companies’ Hungarian branches and offices and chief executive positions and supervisory board membership in partly foreign-owned companies. Automatic permits will be granted to key personnel and foreign spouses and both individual and group work permits can be issued for non-Hungarian employees.

### Box 3. The 1997 Act on Branches

The 1997 Act CXXXII on Hungarian branch offices and commercial representation offices of foreign-registered companies provides the general legal framework for the establishment of branches in Hungary. A non-resident enterprise must enter a branch in the Register of Companies. Branches are treated the same way as other resident enterprises: domestic rules governing auditing, accounting, employment, market practices, membership in chambers of commerce, bankruptcy and liquidation apply. Exception from national treatment may be made only by law or by Government decree for reasons strictly specified in Section 9 of the Act, such as public order and security and stability of the financial system. International agreements binding Hungary prevail over the provisions of the Act should a conflicting requirement arise. Hungary's adherence to the OECD Codes qualify as such an international agreement.

The foreign company may run its business operations in Hungary through its branch registered in the country. The branch may not act as an agent or representative in the name of its foreign parent company or any other foreigner. Under its own name, the foreign parent company may have access to the assets and rights acquired and liabilities assumed under the branch office's company name only in the case of the dissolution of the branch office, during insolvency proceedings as described in this Act, or during proceedings initiated abroad in connection with the assets and rights obtained and liabilities assumed under the branch office's company name. The foreign company is obliged to maintain sufficient assets in the branch to operate and meet its obligations. All assets of the foreign company in Hungary may be subject to a stay of execution to satisfy debts incurred by the operation of its branch. For the purpose of Act XCV of 1995 on Foreign Exchange, a branch is considered as resident; this ensures that branches can acquire foreign exchange under the same conditions as residents. The movement of goods between a non-resident company and its branch is regarded as foreign trade. If permission is required to carry out a foreign trade transaction, the branch must acquire the necessary approvals. Capital transfers by foreign investors for the purpose of increasing the local capital of their branches are not subject to special prior approval but must only be reported. A branch may acquire domestic securities which are not available to non-residents; however the proceeds from the liquidation of these securities is not convertible as such into foreign currencies, but is freely available for all forms of current account payments. However, the amount of forints resulting from the liquidation of these securities is not convertible as such into foreign currencies but it is freely available for all kinds of current account payments.

In order to pursue its activities, a branch can freely acquire proprietary rights to real estate other than arable land or a nature conservation area – the acquisition of such land being reserved to natural persons – in accordance with the terms of international treaties (including Hungary's obligations under the OECD Codes) or if there is reciprocity between Hungary and the home country. In the absence of a treaty or reciprocity, the acquisition of real estate by branches is regulated by the 1996 Government Decree on the Acquisition of Real Estate by Foreigners. Once the branch is dissolved, the real estate must be sold within a year by the non-resident parent company unless it is exempt from such an obligation by the head of the county's public administration office. Such exemption may be granted in accordance with the conditions and rules of procedure stipulated in the legislation on the acquisition of real property by foreigners. The exemption must be granted if the real estate is necessary for the operation of a company or another branch or commercial representation established partly or entirely by the non-resident parent company.



**Box 3. The 1997 Act on Branches** (*continued*)

In the event of bankruptcy, liquidation or comparable insolvency proceedings being initiated against the foreign company abroad, it may be extended to the Hungarian branch, if this is stipulated in an international treaty or there is reciprocity. In the absence of a treaty or reciprocity, the county's court having jurisdiction over the branch initiates its liquidation *ex officio*.

**b) Real estate**

Hungary has no restrictions on the acquisition of real estate in connection with foreign direct investment. A foreign enterprise – subsidiary or branch – established in Hungary may acquire real estate when it registers. According to the 1997 Act, a branch can, in order to pursue its activities, acquire proprietary rights to real estate available to resident legal entities without any permission in cases stipulated by international treaties or if there is reciprocity between Hungary and the home country. In the absence of a treaty or reciprocity, the acquisition of real estate by branches is regulated by the 1996 Government Decree on the Acquisition of Real Estate by foreigners. Hungary's adherence to the OECD Codes of Liberalisation of Capital Movements is considered an international treaty in this respect. The reciprocity requirement goes beyond a bilateral or multilateral agreement and refers to the practice, which has been established between Hungary and the home country. The Foreign Minister and the Minister of Justice published a memorandum regarding existing international treaties and the state of practice concerning reciprocity. In all events, reciprocity, in the usual meaning of this term, is not applicable to OECD investors as a result of Hungary's accession commitments.

Acquisition of arable land and nature conservation areas is reserved to resident natural persons and, in specified cases, to resident mortgage banks – including subsidiaries of foreign mortgage banks.<sup>11</sup> However, under the 1997 Act on mortgage banks and mortgage bonds, branches of foreign mortgage banks cannot own arable land. The Hungarian government has indicated its willingness to explore the possibility of appropriate legislative changes to rectify the legislation as soon as possible.

**Investment incentives**

Hungary operates a comprehensive incentives programme which is oriented both towards attracting foreign investment and diverting it to selected sectors,

<sup>11</sup> 34

activities or regions. The programme encompasses fiscal and financial incentives and other schemes such as industrial free trade zones and parks and local and regional incentives.

The majority of the **fiscal incentives** will be phased out in the coming years. The corporate tax law specifies the rate, duration and conditions for obtaining tax relief. Investments in production facilities or hotels that exceed HUF 1 billion may receive a 50 per cent tax allowance (100 per cent for investments in priority regions or in entrepreneurial zones) for 5 years, provided that the increase in sales revenues exceeds a set minimum level. Priority regions are classified as those with an unemployment rate of over 15 per cent in June of any preceding tax year. Full corporate tax relief for 10 years is available to investments that exceed HUF 10 billion (HUF 3 billion in underdeveloped regions). Underdeveloped regions are defined as those with an unemployment rate in excess of 15 per cent in the two-year period prior to the investment project. The same allowance is available for companies undertaking an infrastructure project in such regions in the year when the project is put into operation. This preferential treatment is granted subject to achieving a pre-determined minimum sales revenue and an increase in the number of jobs created. A corporate tax allowance is available for research and development and provides for the deduction from the tax base of 20 per cent of the direct costs incurred in connection with such activities.

The overall tax regime offers a high degree of transparency and is being constantly developed in line with OECD standards and EU legislation. The range of tax incentives specifically for investors has been reviewed and modified accordingly over the past 10 years. In particular, former incentives favouring solely foreign investors were made either available to Hungarian owned companies or discontinued.

**Financial incentives** are provided for within the framework of the targeted allocation for economic development, the central basic technological development programme, the targeted allocation for rural (regional) development, the labour market fund, in schemes for the development of tourism, environmental protection and agricultural activities. They take the form of grants and preferential credit schemes and are available through a tendering process.

Access to investment incentives is open equally to national and foreign-owned enterprises, with the exception of two facilities, available only to resident persons, that aim to promote the creation of small businesses by individuals and the participation of resident entrepreneurs in the privatisation of smaller state-owned properties. As the privatisation process is almost completed, the use of these facilities is declining.

The regulation of **industrial free trade zones** is unique in Hungary. Any company may set up its own zone without geographical restrictions of any kind. This is

an attractive regulation for assembly companies using only local labour as it enables them to bring in high-value equipment free of duty for their own use. Given the preferential trade agreements with the EU and other countries, providing for duty-free trade in industrial products, the importance of these zones has been diminishing for most companies.

**Industrial parks** offer developed infrastructure, services and local tax allowances. The Ministry of Economic Affairs operates a special programme supporting the establishment of industrial parks relying on local initiatives. Industrial park status has been awarded to 75 applicants so far which are relatively evenly distributed in the country. About four-fifths of the businesses are SMEs, but several multinational companies also benefit from the services offered by the industrial parks.

Incentives and tax holidays offered by **municipalities** play an important role in diverting investment flows to the regions in question. Act LXV on Local Municipalities and Act C of 1990 on Local Taxes provides the legal background for the numerous municipalities to offer incentives and tax holidays for investors. Incentives include exemption from local tax for a given period of time, preferential real estate prices for newly built production facilities, a complete infrastructure for local government industrial parks, local authority contributions to road and sewage network development, local tax allowances in proportion to the size of the investment and/or the rate of new employment, special land prices and property acquisition conditions.

#### **a) SME development**

The economic development programme of the Hungarian Government places special emphasis on the promotion of domestic small and medium-sized enterprises. A specific bill on SME development was passed by the Hungarian Parliament in November 1999. Its aim is to provide a comprehensive legal framework for measures designed to facilitate the development of the SME sector in Hungary, reduce competitive disadvantages, improve employment capacities and achieve gradual compliance with standards and practices of the European Union.

#### **b) FDI promotion in Hungary**

Investment promotion is a prominent element of the economic development strategy of the Hungarian Government. Objectives include the achievement of a lasting investment ratio of 20 to 25 per cent, support of research and development activities, development of supplier networks and the strengthening the spillover effect from FDI on the general economic performance of the country.

#### Box 4. FDI Incentives in other OECD countries in the region

In the other OECD member countries in the region (the Czech Republic and Poland), the structure of FDI incentives is similar to the Hungarian one at present. Fiscal incentives dominate, while the role of financial incentives is relatively insignificant.

The Czech Republic introduced an incentive package in April 1998. The incentives are offered to greenfield or brownfield investments in the manufacturing industry involving a minimum amount of 10 million US\$ invested in fixed assets. At least 50 per cent of the production line must consist of machinery listed under a Czech government-approved list of high-tech machinery, and investment in machinery must account for at least 40 per cent of the total investment and the production technology must meet all Czech environmental standards. The most important elements of the package are a corporate tax holiday of up to 10 years and duty-free importation of machinery and equipment for newly established companies. They can be located in a duty-free zone and low-cost building land and/or infrastructural facilities can be provided. Job-creation grants are offered in regions with high unemployment and up to 50 per cent of total training costs in regions with high unemployment may also be covered by government grants.

Local authorities offer special incentives consisting of job-creation grants, training and retraining grants and provision of low-cost building land and/or infrastructural facilities which are negotiated on a case-by-case basis.

In Poland, the present programme of incentives has been in force since January 1st 1999. Tax allowances are available for investors on revenue earned, start-up investments, exports, machinery purchases for the exploitation of patents and domestic research and development implementation projects, production equipment for pharmaceutical start-ups, projects with a recycled materials content; equipment purchases for ISO 9000 implementation and jobs created for disabled persons. Minimum requirements in terms of capital or performance apply to some of these allowances.

At present there are 15 special economic zones throughout Poland under the jurisdiction of the Minister for Economics who determines their activities, the conditions for and duration of tax holidays and other incentives and eligibility for these incentives.

Sources: <http://czechinvest.com/> and <http://www.paiz.gov.pl/h>.

At government level, investment promotion falls primarily under the responsibility of the Ministry of Economic Affairs (MoEA). Apart from undertaking the necessary co-ordinating and regulatory functions, the MoEA puts a special emphasis on meeting the information demands of potential investors and, in 1993, founded a specialised agency for this purpose, the Investment and Trade Development

Agency (ITDH), which has offices throughout Hungary, and in 37 countries abroad. It serves as a one-stop information and advisory centre for existing and potential foreign investors. There are a number of other organisations (chambers of commerce, non-profit associations, local governments) involved in investment promotion activities in specific areas. In order to maintain close contacts and a forum for consultations with foreign investors operating in Hungary, the MoEA has established an Investors' Council. Its members represent about 70 per cent of the current level of FDI in Hungary.

### **Bilateral investment protection, double taxation and other international agreements**

Hungary has concluded bilateral agreements on the promotion and protection of investment with the majority of OECD countries and holds double taxation agreements with 23 OECD member states. Since accession to the OECD, three new double taxation agreements have come into force (Ireland, Poland and Turkey). A complete list of these agreements is attached as Annex 3.

Hungary ratified the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions in 1998. (See Note 2.)

Prior to its accession, Hungary ratified in April 1994 the OECD Declaration and Decisions on International Investment and Multinational Enterprises.

## Sectoral measures

Hungary has few sectoral restrictions under item I/A of the Capital Movements Code and exceptions to the National Treatment instrument. These concern certain transportation sub-sectors, asset management services provided by branches of foreign financial institutions and preferential credit facilities, guarantees and subsidies for small and medium-sized enterprises and are detailed in Annex I.

Within the context of the 1997 Act on Branches which became effective on 1 January 1998, a limited number of restrictions also remain regarding:

- a) the provision of custodial and asset management services by foreign branches to Hungarian investment funds;<sup>12</sup>
- b) the provision of asset management services by foreign branches to voluntary private pension funds;<sup>13</sup>
- c) the ownership of arable land by foreign branches in relation to mortgage banking.<sup>14</sup>

### a) *Banking*

The privatisation process of banks was largely completed by the end of 1997. As a result, the share of private ownership in the Hungarian banking sector was almost 80 per cent, with foreign participation representing more than 60 per cent of the capital of the banking sector. (Table 7). The share of foreign and private equity participation in the banking sector is significantly higher in Hungary than in the other new European OECD member countries. The Hungarian Bank for Development and the Eximbank are the only institutions, which will remain under 100 per cent state ownership. The acceleration of privatisation contributed to developing and upgrading the Hungarian banking sector.

This process started with the sale of the Hungarian Foreign Trade Bank (MKB) in 1994 and continued in 1995 with the sale of Budapest Bank to the United States investor GE Capital and EBRD and in 1996 with the sale of another big retail bank, Hungarian Credit Bank (MHB), to ABN AMRO of the Netherlands. In 1997, the authorities decided to sell Takarékbank, K&H, Mezobank, PK Bank (Pénzüntézeteki Központ) and the Polgári Bank. An Irish insurance firm (Irish Life) and a Belgian bank

Table 7. Ownership structure of Hungarian banks

Owners of shares 30.09.1999	Value of shares	
	HUF billion	per cent
ÁPV Rt. (Hungarian Privatisation and Holding Co.)	68.4	20.7
<i>State ownership, total</i>	68.9	20.8
Financial institutions	20.1	6.1
Insurance firms, investment funds	1.7	0.5
Other	22.7	6.9
<i>Domestic private ownership, total</i>	44.5	13.5
<b>Domestic ownership, total</b>	<b>113.4</b>	<b>34.3</b>
Foreign financial institutions	153.0	46.3
Other foreign investors	53.1	16.1
<b>Foreign ownership, total</b>	<b>206.2</b>	<b>62.4</b>
Preference shares	7.3	2.2
Own shares	3.7	1.1
<b>TOTAL</b>	<b>330.5</b>	<b>100.0</b>

Source: National Bank of Hungary.

(Kredietbank) acquired one of the largest Hungarian banks (K&H). Takarékbank was sold to the German DG bank. The French Cetelembank and Hungarian MFB together established a new bank specialising mainly in consumer credit services. A Hungarian bank (MHB), which was privatised in late 1996, merged with the Hungarian subsidiary of ABN AMRO (Table 8). In addition, 25 per cent of stake held by the State in the National Savings Bank (OTP) was also sold, with only one golden share remaining in the state's hand, and the National Bank of Hungary sold its 34 per cent stake in the Central European International Bank to COMIT Holding, a fully-owned subsidiary of Banca Commerciale Italiana.

At present, the total number of banks in Hungary is 39. Foreign-owned banks have a majority share in 29 (of which 16 are 100 per cent owned by foreign investors) and a minority share in 2. The foreign investors come from a wide range of countries. In the period of 1995-1999, German, American, Dutch, Austrian, French, Russian, South Korean, Japanese, Belgian and Irish financial institutions invested in the Hungarian banking sector.

According to the new banking law – the 1996 Act on Credit Institutions and Financial Enterprises – the old provisions concerning the special right of the Government to pre-authorise the establishment of banks and acquisition of share-holdings by foreigners, and the reciprocity requirement were abolished in accordance with the timetable indicated by the Hungarian authorities during the 1995-96 accession examination. These requirements were repealed from 1 July 1996.

Table 8. Most recent bank privatisation transactions

	Shares sold (to strategic investors)		Privatisation price (price per share as per cent of face value)
	As per cent of registered capital	In HUF million	
MHB (1996)	89.23	6 378	222
K&H Bank (1997)	14.67	1 520	567
PK Bank (1997)	61.67	3 855	160
Mezőbank (1997)	83.66	2 874	172
Takarékbank (1997)	60.98	818	532

Source: Hungarian authorities.

The law stipulates a two-step-licensing regime for the establishment of banks, including branches of non-resident banks, which is the same for both domestic and foreign investors. Banks already established are not subject to the new licensing procedure. The procedure begins with an application for a founding license and then an operating licence has to be obtained to commence operations. The Hungarian Banking and Capital Markets Supervision (HBCMS) is responsible for granting these licenses.

During the first stage, i.e. the application for the founding license, the supervisory authorities clarify, *inter alia*, whether the candidate is reliable, has adequate capital resources and sufficient number of qualified professionals to start its operation. This first step could be considered as a codification of the consultations with the authorities, which used to take place on an informal basis before establishment.

The maximum length of the licensing procedure is three months for each of the phases, the founding and the operating licence, which can be prolonged by three months if necessary. The HBCMS provides early advice on the status of an application for the founding licence, so that the applicant can decide to initiate the procedure for the operating licence without waiting for the granting of the founding licence. Since the enactment of the banking law, four banks, two savings co-operatives, two mortgage banks and one home savings and loan association have been established under the new licensing procedure. No legal or practical difficulties emerged during the procedure.

Prior approval of the HBCMS is necessary if an investor, whether foreign or domestic, acquires a proprietary interest or voting right equivalent to or exceeding 10 per cent. Any change in the controlling share which reaches the limits of 15, 33, 50 or 75 per cent, requires an application for license to the HBCMS. Each of these



thresholds corresponds to a different degree of potential influence by a single investor on the conduct of a bank. There are no differences in the authorisation procedure at each of these percentage thresholds.

Another authorisation by the HBCMS is necessary for the election or the appointment of the bank executives. The law stipulates that, among the members of the board of directors of a financial institution, two persons have to be employees of the credit institution and two members have to be Hungarian citizens, qualified as residents and having had a permanent residence in Hungary for at least one year. However, the total number of members of the board of directors is unlimited.

Banks may only operate as joint stock companies or branches. The minimum registered capital of a bank operating as a joint stock company must be HUF 2 billion. For the establishment of a bank, the subscribed capital must be paid in cash to an account held at a credit institution with a registered office in Hungary and which is not involved in the establishment.

Subject to the general provisions of the Act on branches discussed above, since 1 January 1998, it is possible for non-resident investors to directly establish branches in Hungary. The establishment requires a license from the HBCMS.

Non-resident investors are granted treatment equivalent to that given to domestic financial institutions, with exceptions only to the extent justified by technical or legal differences in the notion of capital between a branch and an incorporated entity. No higher financial guarantees and regulatory, material and personal requirements are imposed for the establishment and operation of branches than for domestic institutions. Non-resident financial enterprises cannot engage, through their branches established in Hungary, in activities they would not be authorised to carry out in their home country.

Mortgage banks can, under the relevant law, acquire real estate up to the value of 5 per cent of their guarantee capital. In the case of a non-performing loan through a real estate-for-loan swap or of a liquidation process against a borrower, there is no such limit but this real estate will have to be sold in three years. Under the 1997 Act on mortgage banks and mortgage bonds, branches of mortgage banks cannot, unlike subsidiaries, own arable land.

Prior to the granting of a licence to a branch in the banking sector, a “mutual recognition” agreement must be established between the home country’s relevant supervisory authorities and the HBCMS. These agreements consist of an acknowledgement that both supervisory bodies have the authority to licence and supervise these institutions and the independence to do so, and should be more precisely defined as “acceptance agreements”. The relevant provisions on these agreements do not constitute a requirement which would go beyond the framework of normal relations between supervisory authorities of different countries and are consistent with internationally accepted principles, in particular the recommendations of the

Basle Committee on Banking Supervision. The first agreement is now being drafted and the Hungarian Banking and Capital Markets Supervision is willing to consider similar agreements with any other OECD country.

The Act on Credit Institutions and the Securities Act also provide that the regulatory framework of the country where the applicant for establishment of a branch is established should be deemed to ensure that financial institutions under its jurisdiction operate prudently and correctly. In the context of OECD member countries, this provision is not meant to call for some form of unilateral and arbitrary judgement on the part of Hungary about the effectiveness of the overall supervisory regime of another OECD country, which could lead to systematic rejection of any applications by institutions originating from the respective country and outright discrimination among OECD member countries. Rather it is one of the purposes of the co-operative arrangements mentioned in the previous paragraph to assess the extent to which a particular institution applying for a branch license in Hungary can be adequately supervised in its home country.

The regulation of the banking sector (and the financial services industry in general) has recently been changed in an important aspect. Until the end of 1998, banks were not allowed to provide investment services in equities (with some minor exemptions). However, from the beginning of 1999, a new overall legal framework was put in place – through an amendment to the items of legislation regulating this field – and the legal basis for the universal banking system was created. The detailed rules for banks' – and other players' – investment activities are currently being drafted (regulation on trading book and other related rules).

## **b) Insurance**

The development of a private insurance market to international standards has also been a Government priority. The Hungarian insurance sector has attracted major foreign investors. Currently, 13 out of 21 insurance companies operating in Hungary are fully foreign-owned. Six of these are foreign-majority owned and only two remain exclusively under Hungarian ownership. The total of the equity capital of the insurance companies was 46 billion HUF in 1998, in which direct foreign participation was 68 per cent and Hungarian participation was 32 per cent. Indirect foreign participation was 11 per cent. In addition to insurance companies, there are 35 insurance associations. They are set up voluntarily, operating on the basis of mutuality, *i.e.*, they render pre-determined services exclusively to their members on a non-profit basis. In Hungary, these are mainly associations dealing with agricultural insurance, established to meet special demands. Thus, they are not important from the perspective of foreign direct investment.

Under the amended 1995 Act on Insurance Institutions and Insurance Activities, it is possible for non-resident insurers to establish direct branches in Hungary, sub-

Table 9. **Ownership structure of Hungarian insurance companies, 1996-1999**

	1996		1997		1998		1999	
	HUF bn	Per cent	HUF bn	Per cent	HUF bn	Per cent	HUF bn	Per cent
Equity capital	36.4	100.0	44.3	100.0	46.0	100.0	47.6	100.0
<i>of which:</i>								
Foreign	23.5	64.6	26.4	59.7	31.3	68.2	30.5	64
Domestic	12.9	35.4	17.9	40.3	14.6	31.8	17.1	36

Source: Hungarian Insurance Supervisory Authority.

ject to a licensing requirement, with no higher financial, regulatory, material and personal requirements than those applicable to resident insurers. The Insurance Act also contains a provision by which “mutual recognition” agreements between the Hungarian supervisory authority and the home country counterparts are required as a pre-condition to authorise the establishment of branches. These agreements can be more precisely better characterised as “acceptance agreements”. Acceptance of the “recommendation concerning Mutual Assistance, Co-operation and Sharing of Information” constitutes an appropriate starting point for the conclusion of bilateral co-operation agreements – required by the Insurance Act – with OECD member countries signatories of the “Recommendation”. This Recommendation has been compiled within the framework of the International Association of Insurance Supervisors and over 60 members of the Association (including the insurance supervisory authorities of the majority of the OECD member countries) have signed this Recommendation which is designed to strengthen mutual co-operation and support among its members.

All the Hungarian insurance companies have already been privatised, except for the Hungarian Export Credit Insurance Corporation, which is owned by the Hungarian state and conducts export credit insurance. This type of insurance is also regulated in 45 other countries, members of the Bern Union. Because of its special functions, the Hungarian Export Credit Insurance Corporation is expected to remain 100 per cent state-owned in the long term.

### c) *Other financial services*

The 1996 Act on Securities, Investment Services and the Stock Exchange, and the 1991 Act on Investment Funds regulate the provision of investment services in Hungary. Commission brokers, securities dealers, investment companies, investment funds and fund managers fall under the scope of these Acts.

Prior approval of the Hungarian Banking and Capital Markets Supervision is necessary, if in such companies, an investor, whether foreign or domestic, acquires a proprietary interest or a voting right equivalent to or exceeding 10 per cent. As in the case of the banking sector, any change in the controlling share which reaches the limits of 15, 33, 50 or 75 per cent, requires an application for licence to the HBCMS. Pursuant to the Securities Act, a natural person, legal entity or any other economic association may have direct ownership exceeding 10 per cent in only one investment enterprise at the same time.

The Act on Investment Funds stipulates that, in order to hold a substantial share or vote (in excess of 25 per cent) in an investment company, an individual person or legal entity members have to have an excellent business and professional reputation. This requirement applies equally to domestic and foreign investors.

With respect to the securities business, foreign firms enjoy non-discriminatory access to brokerage licenses issued by the HBCMS. Non-resident shareholding represents 21 per cent of the capital of the brokerage sector. Taking into account shares held by foreign-controlled institutions established in Hungary, foreign ownership amounts to more than 50 per cent of the capital of the sector.

Since 1 January 1998, it is possible for non-residents to provide investment services through branches, subject to a licensing requirement. As in the case of banking and insurance, non-resident investors are granted equivalent treatment to domestic financial services enterprises in accordance with the Code requirements, with exceptions being justified by technical or legal differences in the notion of capital between a branch and incorporated entity. In particular, no higher financial guarantees and material and personal requirements are imposed for the establishment and operation of branches than for domestic financial institutions.

As in the case of banking, prior to the granting of a licence to a branch in the securities sector, a “mutual recognition” agreement, which corresponds to an “acceptance agreement” (see above) is required between the home country’s relevant supervisory authorities and the Hungarian supervisory bodies. The Hungarian Banking and Capital Markets Supervision has concluded memoranda of understanding on co-operation with its German, Austrian, Italian, French, Portuguese, Czech and Polish counterparts and with the competent Luxembourg authorities and is willing to negotiate and conclude similar agreements with other OECD countries.

#### **d) Pension funds**

A pension reform introducing a new three-pillar pension system was adopted on 15 July 1997.<sup>15</sup> The first pillar is the pay-as-you-go social security system. The second and newly introduced pillar is a fully funded, privately managed, pre-defined contributory pension scheme, financed from mandatory employee contributions. Participation in the second pillar is mandatory for new entrants to the labour mar-

ket. Older workers had an option to voluntarily the join the multi-pillar system, the two-year switching period was closed on 31 August 1999. The third pillar, introduced in 1993, is a voluntary private pension scheme, where participation is encouraged by a tax concession.

The State Private Fund Supervisory Authority was established in 1994. It is an independent agency under the supervision of the Minister of Finance responsible for safeguarding the interests of participants in both mandatory and voluntary pension funds, and also for supervising health and voluntary mutual benefit. The Guarantee Fund for Private Pension Funds, financed from members' contributions, is responsible for guaranteeing a minimum benefit to second pillar participants. Investment activities of the various types of funds are strictly regulated by Government decrees, which impose quantitative investment restrictions.

## Privatisation

### a) *Status*

Privatisation was given priority in government policy beginning in 1989. By November 1999 more than 90 per cent of the companies belonging to the privatisation organisation (APV Rt.) existing at the beginning of the privatisation process and as the companies established during the corporate restructuring process had been privatised. This involved a total of 1 267 companies. (Table 10).

Privatisation is estimated to have raised the private sector share in GDP to 85 per cent by the end of 1999 and, in line with the Government's policy, had at that time practically reached its final stage. The sale of the bulk of state-owned assets had been completed with extensive foreign participation.

By the end of the same period, the private sector held the majority of the Hungarian retail and commercial banking system, the pharmaceutical and the chemical industries. The insurance sector, the building and construction industries, the tobacco, brewing and the food processing industries, the leisure and hotel industry, the printing, paper and packaging industries and the food and general retail network were almost fully privatised. A significant part of the public utilities sector has also been privatised, including MOL (Hungarian Oil Company), the majority of electricity supply companies and the electricity generating capacities. The sale of the Hungarian Telecommunications Company, MATÁV was completed in 1999.

The above results could not have been achieved without FDI involvement, which so far accounts for two-thirds of the privatisation returns. Between the beginning of 1990 and November 1999, the value of foreign investments through privatisation was US\$12.6 billion, of which 25 per cent originated from Germany, 13 per cent from United States, 9 per cent from France. Foreign investors' interest has centred mainly on larger firms. The successful completion of the privatisation of MATÁV resulted in revenues of US\$315 million in the first half of 1999. In the second half, the shares of several electricity supply companies were sold off for more than US\$60 million.

Since the process of privatisation began, cash sales have prevailed over other privatisation methods. This was considered the best way to involve responsible (strategic) investors and raise money in a relatively short period of time. Competi-

Table 10. Expenses and incomes of ÁPV Rt. (1990–November 1999)  
(HUF billion)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	November 1999	Total
<b>EXPENSES</b>											
Preparation and fees due for the sale of the assets	0	1.14	6.16	7.56	25.26	5.27	11.22	12.02	4.87	5.24	78.74
Asset management	0	0	0	0	0	4.59	2.06	2.07	1.34	1.41	11.47
Internal operating expenses	0	0	0	0	0	4.50	4.00	3.05	3.30	3.00	18.30
Reorganisation	0	0	8.70	19.53	4.03	8.89	20.08	12.14	13.38	12.76	99.51
Establishing companies	0	0	0	20.00	4.00	8.31	14.36	18.01	35.96	0.00	100.64
Other priv. related expenses	0	0	0	0	0	0	4.74	0.57	1.37	0.00	6.68
<i>Privatisation expenses total</i>	0.00	1.14	14.86	47.09	33.29	31.56	56.46	47.86	60.22	22.41	315.34
Budget-related <sup>1</sup>	0.51	25.33	63.88	70.18	168.69	222.66	304.00	265.51	91.03	52.82	1 264.61
<b>Total expenses</b>	<b>0.51</b>	<b>26.47</b>	<b>78.74</b>	<b>117.27</b>	<b>201.98</b>	<b>254.22</b>	<b>360.46</b>	<b>313.37</b>	<b>151.23</b>	<b>75.23</b>	<b>1 579.48</b>
<b>REVENUES</b>											
Cash revenues	0.67	29.42	55.58	128.22	38.56	437.80	119.46	318.18	99.06	108.53	1 335.48
<i>Of which: hard currency</i>	0.53	24.61	40.98	110.67	10.95	411.48	92.73	208.64	39.02	69.53	1 009.14
E-credit and instalments pay.	0.00	1.01	9.07	21.72	29.27	3.99	2.47	0.31	0.99	0.00	68.83
Compensation vouchers	0.00	0.00	2.26	14.56	64.20	30.15	40.70	23.20	4.5	0.30	179.87
<i>Totals sales</i>	0.67	30.43	66.91	164.50	132.03	471.94	162.63	341.69	104.55	108.83	1 584.18
Dividend	0	0.93	7.41	5.41	7.80	5.07	7.86	5.77	5.07	5.56	50.88
Other revenues	0	0	2.91	0	16.84	4.03	6.02	2.92	2.22	10.03	44.97
<b>Total revenue</b>	<b>0.67</b>	<b>31.36</b>	<b>77.23</b>	<b>169.91</b>	<b>156.67</b>	<b>481.04</b>	<b>176.51</b>	<b>350.37</b>	<b>111.84</b>	<b>124.42</b>	<b>1 680.03</b>

Note: "Total expenses budget-related" are subject to Parliamentary approval and only used for repayments (including pre-payment) of the Government debt.

1. Includes payments, such as transfers to local governments, guarantees, etc.

Source: ÁPV Rt.

tive tender procedures were established with the approval of the Government to ensure fairness and transparency of transactions. In some cases multinational companies and multilateral organisations (IFC, EBRD) were invited to participate. The stock exchange also played an important role in public offerings of shares of enterprises to be privatised. International public offerings of equity amounted to altogether 30 per cent between 1990 and 1999. Part of the shares has been earmarked for institutional and small investors. The Government also used employee stock ownership plans, management buyouts, small preferential financing schemes (such as E-loans, compensation vouchers, leasing, instalment payments) to promote Hungarian entrepreneurship. Special (simplified) privatisation methods were applied for smaller companies, *i.e.*, with an equity capital under HUF 600 million and/or with less than 500 employees.

At the end 1999 the value of assets still saleable was estimated at US\$1.6 billion.

### **b) Legislation**

A transparent legal framework was created for the privatisation process, reinforced in particular by the 1995 Act on the Sale of State-Owned Entrepreneurial Assets (Privatisation Act). At the same time, a single privatisation agency, the Hungarian Privatisation and State Holding Co. (ÁPV Rt.) was established in order to implement in a simple and effective way the Government's strategy and the accompanying institutional changes. This Act enabled the privatisation process to be substantially accelerated.

#### **Box 5. The Hungarian Privatisation and State Holding Company – ÁPV Rt.**

Under the terms of the 1995 Privatisation Act, the assets of the Hungarian State Holding Company (ÁV Rt., formerly in charge of the long-term state assets), the State Property Agency (ÁVÜ, formerly responsible for administering the state assets for sale) and a portion of those belonging to the Treasury Asset Management Organisation were placed under the authority of a single institution, the Hungarian Privatisation and State Holding Company (ÁPV Rt.). In accordance with the Privatisation Act, the statutes of ÁPV Rt. were adopted by the Government. It is operated as a joint stock company with the ownership functions (shareholders' rights) exercised by the minister responsible for privatisation (at present the minister, in charge of the Prime Minister's Office). The company's strategic decision-making body is its board of directors, whose powers of authority cannot be revoked by the minister. The State Audit Office, the supervisory board and an independent auditor monitor the operation of the company. The Government is obliged to report annually to Parliament on the activity of ÁPV Rt. which is the proprietor and manager of the entrepreneurial assets of the state with additional responsibility for the privatisation of companies at the best possible conditions.



### c) *Restrictions and the composition of assets remaining in permanent state ownership*

The Privatisation Act of 1995 clarifies the rules applicable to enterprises currently under state control. It identifies general categories of enterprises that may remain under full or partial permanent state ownership. The categories in question include the following: *a)* a national public utility provider; *b)* a company of “strategic significance with regard to the national economy”; *c)* a company responsible for national defence or other special duties and/or similar functions; *d)* any company share required to safeguard the ownership of the state and its voting rights as provided for by the law on concessions.

As a general rule, the Privatisation Act stipulates that, under normal circumstances, the mandatory stake of the State cannot fall below 50 per cent plus 1 voting right in relation to permanent state ownership. In exceptional cases, however, it allows the State to remain permanently in a so-called strategic minority position (25 per cent plus 1 vote, a blocking minority) within the company. In addition, there is legal provision for exercising the rights related to the State ownership – limited to certain strategic decisions – through the so-called golden share (for details see Box 6).

#### Box 6. **The golden share**

Based on the Act on Business organisations, the Privatisation Act also provides for which the representation of the permanent interest of the State through a single share conferring the special right of a priority vote. The rights attached to what is known as “the golden share” are defined in the company’s deed of foundation/statutes. The owner of the golden share has a veto right in the matters listed below. The presence of the owner of the golden share is needed for a resolution to be made on these matters at the shareholders’ meeting. The golden share actually means that (generally) the following matters can only be decided with the approval of the holder of the share:

- the increase or decrease of the equity capital;
- modification of the rights attached to specific types of shares;
- changes in the business organisation’s relationship with another company, such as joining, merging or separation of interests, as well as its transformation into another business organisation form or its termination without a successor in title;
- when the right representing the asset value required for the operation of the business organisation is transferred, waived or leased or in any other manner assigned for long-term use to another management organisation, or is pledged or tied up as a guarantee;
- the election or recall of any member of the board of directors or supervisory board representing the owner of the priority voting right.

The Privatisation Act also defines the level of authority at which the privatisation of individual companies is to be determined. The Privatisation Act entitles the Government to decide on the privatisation strategy of the companies deemed significant for the national economy. This group of companies is defined by the Parliament.

According to the Privatisation Act, the Government – on recommendation of ÁPV Rt., the minister responsible, the employers concerned and the representative bodies of the employees – can make a proposal to Parliament for classification into or declassification from permanent state ownership, so that the list can be changed as appropriate. The final decision lies with the Parliament.

Pursuant to the regulations in force, the sectors remaining in total, majority or significant state ownership are limited essentially to those of a strategic nature. Currently 172 companies are considered to fall within the category identified above according to the Appendix of the Privatisation Act. Of these companies, 93 belong to ÁPV Rt. – among them 3 banks, 19 forestry companies which are to remain in 100 per cent state ownership, and 27 agricultural companies, most of which are to remain in 75 per cent state ownership. As far as MVM (Hungarian Electricity Works), owner of the national electricity grid and responsible for the nuclear energy industry and the 24 Volán regional transport companies are concerned, 50 per cent + 1 vote is to remain in state hands in the long-term. The others (e.g. research institutions) fall within the competence of the relevant ministries.

Of the companies of strategic importance to long-term national interest, the state has one golden share in 30 companies (Table 11).

The government is currently reviewing the tasks to be fulfilled directly by the state in the economy. The December 1999 amendment of the Privatisation Act was an outcome of this review. Changes affected the extent and scope of long-term state ownership in terms of specifying the companies as well as the size of the stake to be retained, although the number of companies affected was only marginally reduced from 98 to 93 as a result.

A change in the main tasks of ÁPV Rt. is also expected due to the progress of the privatisation process and the reduction in the number of companies still for sale. Greater emphasis is likely to be placed on asset management and the fulfilment of obligations from former sales agreements. The amendment of the Privatisation Act also permitted ÁPV Rt. to take a more active asset-management role which may involve non-transparent cross-subsidies between profitable and loss-making state-owned enterprises.

#### **d) Opportunities**

As previously indicated, at the end of 1999 the value of the remaining saleable assets for privatisation purposes was estimated at HUF 400 billion (US\$1.6 billion). In 2000 APV Rt. will have the task of selling the assets (shares and property) of the

Table 11. Companies with golden shares at the end of 1999

1	AES-Tiszai Erőmű Rt.	AES Tisza Power Plant Ltd.
2	Bakonyi Erőmű Rt.	Bakony Power Plant Ltd.
3	Budapesti Elektromos Művek Rt.	Budapest Electricity Plc.
4	Budapesti Erőmű Rt.	Budapest Power Plant Ltd.
5	Dél-Alföldi Gázszolgáltató Rt.	Southern Lowlands Gas Supplying Ltd. (DÉGÁZ Ltd.)
6	Dél-Dunántúli Áramszolgáltató Rt.	South West Hungarian Electricity Supply Company Ltd
7	Dél-Dunántúli Gázszolgáltató Rt.	South Transdanubian Gas Supply Ltd.
8	Dél-Magyarországi Áramszolgáltató Rt.	South Hungarian Electricity Supply Company Ltd.
9	Dunamenti Erőmű Rt.	Dunamenti Power Plant Ltd.
10	Észak-Dunántúli Áramszolgáltató Rt.	North West Hungarian Electricity Supply Company Ltd
11	Észak-Dunántúli Gázszolgáltató Rt.	North Transdanubian Gas Distribution Plc. (ÉGÁZ Plc.)
12	Észak-Magyarországi Áramszolgáltató Rt.	North Hungarian Electricity Supply Company Ltd.
13	Közép-Dunántúli Gázszolgáltató Rt.	Middle Transdanubian Gas Distribution Company Ltd.
14	Mátrai Erőmű Rt.	Mátra Power Plant Company Ltd.
15	Országos Villamos Távfűtési Rt.	National Power Line Company Ltd.
16	Paksi Atomerőmű Rt.	Paks Nuclear Power Plant Ltd.
17	Pécsi Erőmű Rt.	Pécs Power Plant Ltd.
18	Tiszántúli Áramszolgáltató Rt.	East Hungarian Electricity Supply Company Ltd.
19	Tiszántúli Gázszolgáltató Rt.	Tiszántúli Gas Supply Corporation (TIGÁZ Corp.)
20	Vértesi Erőmű Rt.	Vértes Power Plant Ltd.
21	CD Hungary Ingatlanforg. És Szolg. Rt.	CD Hungary Ltd.
22	Magyar Távközlési Rt.	Hungarian Telecommunications Company Ltd.
23	Herz Szalámigyár Rt.	Herz Salami Company Ltd.
24	Hungaropharma Gyógyszer-kereskedelmi Rt.	Hungaropharma Ltd.
25	Kalocsai Fűszerpaprika Rt.	Kalocsai Spices Ltd.
26	Pick Szegedi Szalámigyár Rt.	Pick Szeged Salami Factory and Meat Processing Corp.
27	Zsolnay Porcelán Rt.	Zsolnay Porcelain Factory Plc.
28	Országos Takarékpénztár és Kereskedelmi Bank	OTP National Savings and Commercial Bank
29	HUNGEXPO Vásár és Reklám Rt.	HUNGEXPO Exhibition and Advertisement Co.
30	Magyar Olaj- és Gázipari Rt.	Hungarian Oil and Gas Plc MOL

social security fund, a process which was started in 1999. Plans for the coming years are expected to include the sale of the state's interest in Hungaropharma (a pharmaceutical wholesale company), CD Hungary (a real estate management company), MALÉV (Hungarian Airlines), and Antenna Hungaria (a broadcasting and telecommunications company), as well as other items of real estate.

Generally, as further infrastructure investments take place in Hungary, further potential for investors is seen in the eastern part of the country which is only now being developed and offers attractive labour resources. Sectoral opportunities present themselves in the areas of environmental protection where the preparations for EU membership require considerable investment. Other opportunities for foreign investors are expected in the tourism sector and particularly in the areas of congress management services, spa facilities and hotel developments.

### **Monopolies and concessions**

The Hungarian legislation on monopolies and concessions is outlined in Annex 2. A number of activities have been earmarked by the privatisation legislation to remain under “permanent” state control. Some of these areas will continue to be the “exclusive” preserve of the state and could be considered as public monopolies. Designated public monopolies concern mainly transportation, postal and certain telecommunications services, utilities, nuclear energy and narcotic substances.

The 1991 Concession Act specifically provides for the possibility for foreign investors to engage in these activities on a national treatment basis. This is done by way of a concession contract awarded on the basis of a public tender. In the case of concession tenders, equal treatment is granted to domestic and foreign participants and a foreign investor is not obliged to be part of a legally incorporated entity in Hungary to participate in the public tender procedure. However, once the concession has been awarded, the beneficiary must incorporate a company to exercise the concession rights. Concessions may be awarded for terms of at least five, and not more than thirty-five years. These rules apply to concessions granted by the central government or by sub-national authorities.

The Concession Act also governs the acquisition access to natural resources by foreigners. It stipulates that foreigners, including non-residents, can be considered for concession contracts in mine exploration and exploitation and related secondary activities on the same conditions as resident nationals. Concessions are granted through competitive tendering procedures.

The organisation of gambling, betting, lotteries and other similar activities is subject to a Government monopoly.

### **National security**

The Hungarian Government has not invoked public order or essential security interests to restrict the access of foreign investors in any field. A clause providing for the introduction of measures for national security and public order reasons exists in the 1997 Act on Branches.

## Notes

1. Source: OECD Privatisation Database.
2. Refer to the following website for further information: <http://www.oecd.org/daf/nocorruption>.
3. According to data on cumulative net FDI inflows between 1989-1998 – published by the EBRD – the FDI per capita was US\$1,627 in Hungary, US\$967 in the Czech Republic and US\$389 in Poland. From among other countries in the East Central European region Estonia performed the best (US\$953), while in the rest of countries this figure varied between US\$130 and 600.
4. However similar peaks strongly influenced by privatisation revenue are unlikely to be achieved in the foreseeable future, given the fact that the bulk of the state assets had been privatised by the end of 1998 (for details see Chapter 4 on Privatisation).
5. It should be noted though that financial data on geographical location might be slightly misleading since often only headquarters (particularly in the case of service companies) are registered in the capital or in Pest County and the actual economic activities are carried out in other parts of the country.
6. Regional comparison of inflows of foreign direct investments is made difficult by the fact that in the three countries, balance of payments data on foreign direct investment differ in their coverage. In the Czech Republic, this coverage includes only equity capital, the basic source of information being the quarterly enterprise survey conducted by the Czech National Bank. The number of respondents is insufficient and therefore the data obtained are supplemented from the National Property Fund on non-resident investment in existing Czech enterprises and from commercial courts on newly established joint ventures. Information from the media is also used. Hungarian data are more comprehensive. However, data on reinvested earnings are not available, and the existing data cover only transactions made through the resident banking system. (Thus, contribution in kind and other transactions bypassing the domestic banking system are not included.) Poland's data on foreign direct investment have the most complete coverage. In the annual balance of payments, the banking system data that cover payments made through the banking system are supplemented with information from surveys of all direct investment enterprises in Poland. Data from the surveys cover flows in currency, contributions in kind, reinvested earnings and other claims and liabilities. (Source: Balance of Payments Statistics Yearbook, IMF, 1998.)
7. Preliminary figures based on data from tax files for 1998.
8. Source: "Development and Prospects of the Transport Equipment Sector in the Central and Eastern European Countries", by Doris Hanzl, Vienna Institute for international Economic Studies – WIIW Industry Studies, No. 4, December 1999.
9. For details on high technology sector and product classification see: STI Working Papers 1997/2, Thomas Hatzichronoglou: Revision of the high-technology sector and product classification. OECD/GD(97)216.

10. Figures related to the latter are obtainable from the foreign trade statistics compiled by the Ministry of Economic Affairs.
11. Mortgage banks may own the arable land – obtained as a collateral for non-performing loans – only for a limited period of time. They have to sell it within three years.
12. This restriction will be reviewed in due course in the light of regulatory regimes in other OECD countries.
13. Legislative changes are to be proposed to correct this situation as soon as possible.
14. Legislative changes are to be proposed to correct this situation as soon as possible.
15. Act LXXX of 1997 on Persons Entitled to Social Security Benefits and Private Pensions, as well as the Coverage of these Services, Act LXXXI of 1997 on the Social Security Pension and Act LXXXI of 1997 on Private Pension and on Private Pension Funds.

## **Hungary's current position under the Code of Liberalisation of Capital Movements and under the National Treatment Instrument**

### **Introduction**

As a signatory to the OECD Code of Liberalisation of Capital Movements (the Code) and the National Treatment Instrument (NTI), Hungary has undertaken a number of obligations in the FDI field. This annex and Annex 2 highlight the main provisions of these instruments as well as Hungary's position under them.

### **The OECD Commitments**

The Code and the NTI are the two main instruments for co-operation among OECD member countries in the field of foreign direct investment.

The Code, which has the legal status of OECD Council Decisions and is binding on all Member countries, covers the main aspects of the right of establishment for non-resident enterprises and requires OECD members to progressively liberalise their investment regimes on a non-discriminatory basis and treat resident and non-resident investors alike.

The NTI is a "policy commitment" by Member countries to accord to established foreign-controlled enterprises treatment no less favourable than that accorded to domestic enterprises in like situations. While the NTI is a non-binding agreement among OECD Member countries, all measures constituting exceptions to this principle and any other measures which have a bearing on it must be reported to the OECD.

Member countries need not, however, liberalise all their restrictions upon adherence to the above instruments. Rather, the goal of full liberalisation is to be achieved progressively over time. Accordingly, members unable to fully liberalise are permitted to maintain "reservations" to the Code of Capital Movements and "exceptions" to the NTI for outstanding foreign investment restrictions. These limitations to the liberalisation obligations may be lodged at the time a member adheres to the Codes, whenever specific obligations begin to apply to a member, or whenever new obligations are added to the instruments.

The investment obligations of the Code and the NTI are, in fact, complementary, both dealing with the laws, policies and practices of Member countries in the field of direct investment. However, the Code addresses the subject from the point of view of non-resident investors in an OECD host country, while the NTI is concerned with the rights of established foreign-controlled enterprises. Limitations on non-resident (as opposed to resident) investors affecting the enterprises' operations and other requirements set at the time of entry or establishment are covered by the Code. The investment operations of foreign-controlled

enterprises after entry, including new investment, are covered by the National Treatment Instrument.

Measures pertaining to subsidiaries fall under the purview of the Code or the NTI depending on whether they set conditions on entry/establishment or concern the activities of foreign-controlled enterprises already established. As to branches, the 1991 Review of the OECD Declaration and Decisions on International Investment and Multinational Enterprises introduced a distinction between “direct” branches of non-resident enterprises and “indirect” branches, that is branches of already established foreign-controlled enterprises. The latter are subject to all the five categories of measures covered by the NTI (investment by established enterprises, government procurement, official aids and subsidies, access to local financing and tax obligations). The investment activities of “direct” branches of non-resident enterprises, which concern the category of measures covered by the NTI, fall however, exclusively under the purview of the Code.

The Committee on Capital Movements and Invisible Transactions and the Committee on International Investment and Multinational Enterprises together conduct country examinations of every Member country measures covered by these OECD commitments. These examinations involve a face-to-face discussion between representatives of the two Committees and experts from the country being examined. The discussion is based on submission by the Member concerned and a document prepared by the Secretariat. The objective is to clarify the nature and purpose of remaining restrictions and to identify possible areas for further liberalisation. The examinations usually conclude with modifications to the Member country’s position and recommendations by the OECD Council to the Member’s authorities concerning the future direction of the country’s foreign direct investment policies.

**a) Hungary’s reservations on inward direct investment under the Code of Liberalisation of Capital Movements**

List A, Direct investment:

I/A

– In the country concerned by non-residents.

Remark: The reservation applies only to:

- i) Acquisition of a license for domestic air transportation;
- ii) Acquisition of a shipping license to operate in international waters;
- iii) The provision of asset management services by branches of non-resident investors to domestic compulsory private pension funds.

**b) Measures reported as exceptions to the National Treatment Instrument**

A. *Exceptions at the national level*

I. Investment by established foreign-controlled enterprises

**Air transport**

Licenses for the domestic transport of persons or goods may be granted only to companies with Hungarian majority both in terms of capital and management control.

(Law on commercial aviation)



***International waterways***

Shipping licenses may be granted only to Hungarian nationals or enterprises with majority Hungarian ownership.

(Decree 17/1992. Minister of Transport.)

## II. Official aids and subsidies

Preferential credit facilities and credit guarantees for promoting small enterprises may be reserved for Hungarian nationals and companies with majority Hungarian ownership.

(Government decree No. 59/1992; Act XI of 1993)

## III. Tax obligations

None

## IV. Government purchasing

None

## V. Access to local finance

None

B. *Exceptions by territorial subdivisions*

None

## Hungary's Transparency Measures regarding National Treatment

### A. Monopolies and Concessions\*

- National public roads and related engineering structures, railways, canals and sewage (including the main waterworks for the agricultural sector), designated public ports of national interest, public airports, and regional public utilities;
- Frequencies for telecommunications;
- Public electricity works, the national transmission network for the supply and conveyance of energy;
- Local public roads and engineering structures forming part of the assets of local governments and the operation of local public utilities;
- Mining research and exploitation and related secondary activities;
- Conveyance and storage of products through pipelines;
- Production and sale of fissile material and radioactive matter;
- Production and sale of drugs and psychotropic substances;
- Basic postal services (services related to consignments of letter post and cash remittances);
- Telecommunications services (public telephone, public mobile telephone, public national paging, distribution and broadcasting national or regional radio and television programmes excluding specialised programmes);
- Passenger and goods rail transportation;
- Scheduled passenger road transportation;
- Organisation of gambling, betting, lotteries and other similar activities.

### B. Transparency Measures at the Level of National Government

#### I. Measures based on public order and essential security considerations

- None

#### II. Other measures reported for transparency

- None

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\* These activities may be open to the private sector on a National Treatment basis under the Hungarian Law on Concessions.

Annex 3

## Hungary's Investment Protection and Double Taxation Treaties with OECD Member States

	Agreement on the promotion and protection of investments		Agreement on the prevention of double taxation	
	Signature	Effective date	Signature	Effective date
Australia	15.08.1991	10.05.1992	29.11.1990	01.01.1993
Austria	26.05.1988	26.09.1989	25.02.1975	1.1.1976-77
Belgium	14.05.1986	23.09.1988	1 907.1982	01.01.1985
Canada	03.10.1991	21.11.1993	15.04.1992	01.01.1995
Czech Republic	14.01.1993	15.05.1995	14.01.1993	01.01.1995
Denmark	02.05.1988	18.10.1988	24.10.1978	01.01.1980
Finland	06.06.1988	13.05.1989	25.10.1978	01.01.1982
France	06.11.1986	30.09.1987	28.04.1980	01.01.1982
Germany	30.04.1986	07.11.1987	18.07.1977	01.01.1980
Greece	27.05.1989	01.02.1992	25.05.1983	01.01.1986
Ireland	–	–	25.04.1995	01.01.1997
Italy	17.02.1987	06.09.1989	16.05.1977	01.01.1981
Japan	–	–	13.02.1980	01.01.1981
Korea	28.12.1988	01.02.1989	29.03.1989	01.01.1991
Luxembourg	14.05.1986	23.09.1988	15.01.1990	–
Mexico	–	–	Under negotiation	
Netherlands	02.09.1987	01.06.1988	05.06.1986	01.01.1988
Norway	08.06.1991	04.12.1992	21.10.1980	01.01.1982
Poland	23.09.1992	16.06.1995	23.09.1992	01.01.1996
Portugal	28.02.1992	–	16.05.1995	–
Spain	09.11.1989	01.08.1992	09.07.1984	01.01.1988
Sweden	21.04.1987	21.04.1987	12.10.1981	01.01.1983
Switzerland	05.10.1988	16.05.1989	09.04.1981	01.01.1983
Turkey	14.01.1992	01.11.1994	10.03.1993	01.01.1996
United Kingdom	09.03.1987	28.08.1987	28.11.1977	01.01.1979
United States			12.02.1979	01.01.1980

Source: Ministry of Finance.

*Annex 4*

## **Foreign Direct Investment Statistics\***

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\* Comparative foreign direct investment statistics were provided by Ayse Bertrand and Jean-Marc Salou of the Financial Statistics Unit.

Table 1. **Direct Investment from abroad in OECD Countries: Inflows**  
Million US dollars

	Cumulative flows		Inflows								
	1971-1980	1981-1990	1990	1991	1992	1993	1994	1995	1996	1997	1998 <sup>p</sup>
Australia	11 295	39 822	6 513	4 042	5 036	3 007	3 951	12 729	5 106	8 724	6 494
Austria	1 455	3 274	647	359	940	982	1 314	1 904	4 429	2 656	5 917
Belgium-Luxembourg	9 215	27 986	7 966	9 292	11 326	10 751	8 313	10 812	14 061	12 451	20 887
Canada	5 534	33 409	7 562	2 870	4 717	4 748	8 204	9 255	9 405	11 465	16 500
Czech Republic	..	..	..	..	1 004	654	869	2 562	1 429	1 301	2 540
Denmark	1 561	3 467	1 212	1 453	1 015	1 681	4 890	4 176	776	2 801	6 452
Finland	376	2 838	787	-247	406	864	1 578	1 063	1 109	2 116	12 141
France	16 908	54 588	15 609	15 157	17 855	16 439	15 580	23 681	21 960	23 178	28 033
Germany	13 816	19 691	2 962	4 729	-2 089	368	7 134	12 019	5 637	9 605	19 888
Greece	..	6 145	1 005	1 135	1 144	2 583	3 081	4 272	5 888	3 586	3 709
Hungary	..	512	311	1 462	1 479	2 339	1 146	4 453	1 983	2 085	1 935
Iceland	..	74	22	18	-11	..	..	14	82	149	112
Ireland	1 659	1 371	258	1 168	1 244	850	420	621	1 888	1 676	2 236
Italy	5 698	24 888	6 344	2 481	3 210	3 746	2 236	4 817	3 535	3 698	1 212
Japan	1 424	3 324	1 806	1 286	2 755	210	888	41	228	3 224	3 193
Korea	..	4 025	789	1 180	728	588	809	1 176	2 325	2 844	5 143
Mexico	..	24 421	2 633	4 762	4 393	4 389	10 973	9 526	9 185	12 478	10 238
Netherlands	10 822	37 857	12 165	6 552	7 824	8 561	7 333	12 150	14 754	9 198	22 491
New Zealand	2 598	3 940	1 681	1 695	1 089	2 212	2 690	2 697	3 697	1 832	1 930
Norway	3 074	5 634	1 807	655	-426	2 244	2 713	2 229	3 257	3 630	3 600
Poland	..	88	88	359	678	1 715	1 875	3 659	4 498	4 908	6 365
Portugal	535	6 920	2 608	2 451	1 914	1 550	1 265	695	1 315	2 520	1 773
Spain	7 060	46 158	13 839	12 445	13 352	8 073	9 425	6 217	6 468	5 540	8 680
Sweden	897	8 619	1 971	6 351	-41	3 843	6 346	14 448	5 076	10 905	18 900
Switzerland	..	14 068	5 485	2 644	411	-83	3 368	2 224	3 078	5 028	4 781
Turkey	228	2 434	778	910	911	746	636	935	913	852	953
United Kingdom	40 503	130 469	32 889	16 027	16 214	15 468	10 497	22 738	26 084	37 051	63 545
United States	56 276	365 084	48 422	22 799	19 222	50 663	45 095	58 772	84 455	105 488	188 960
<b>TOTAL OECD</b>	<b>190 934</b>	<b>871 105</b>	<b>178 158</b>	<b>124 035</b>	<b>116 299</b>	<b>149 190</b>	<b>162 628</b>	<b>229 885</b>	<b>242 621</b>	<b>290 989</b>	<b>468 608</b>

p Provisional.

Break in series: Australia 1995, France 1988, Greece 1992, Ireland 1990.

Source: *International Direct Investment Statistics Yearbook*, 1999, OECD.

Table 2. **Direct Investment abroad from OECD Countries: Outflows**  
 Million US dollars

	Cumulative flows		Outflows								
	1971-1980	1981-1990	1990	1991	1992	1993	1994	1995	1996	1997	1998 <sub>p</sub>
Australia	2 510	22 266	265	3 001	951	1 779	5 291	3 844	5 921	5 913	671
Austria	578	4 132	1 663	1 288	1 871	1 467	1 201	1 131	1 935	1 948	3 013
Belgium-Luxembourg	3 213	20 984	6 130	6 493	10 389	4 693	1 205	11 712	8 065	7 742	23 111
Canada	11 335	42 337	5 222	5 813	3 586	5 868	9 293	11 462	12 877	22 044	26 577
Czech Republic	..	..	..	..	21	101	120	37	153	25	55
Denmark	1 063	6 292	1 509	1 844	2 225	1 373	4 041	3 069	2 518	4 210	3 868
Finland	605	11 577	2 708	-124	-753	1 409	4 297	1 498	3 596	5 292	18 643
France	13 940	101 365	36 220	25 115	30 416	19 732	24 381	15 760	30 419	35 591	40 578
Germany	27 830	94 239	24 233	22 947	18 596	17 197	18 858	39 052	50 830	40 284	86 641
Greece	..	..	..	..	..	..	..	..	..	..	..
Hungary	..	..	..	..	..	11	49	43	-3	431	481
Iceland	..	26	10	27	3	11	23	24	62	51	99
Ireland	..	..	..	..	..	..	..	..	..	..	..
Italy	3 597	28 707	7 612	7 326	5 948	7 221	5 109	5 732	6 465	10 619	15 591
Japan	18 052	192 410	50 774	31 688	17 301	13 916	18 117	22 629	23 424	25 991	24 159
Korea	..	2 406	1 052	1 489	1 162	1 340	2 461	3 552	4 670	4 449	4 756
Mexico	..	..	..	..	..	..	..	..	..	..	..
Netherlands	27 829	65 771	15 288	13 577	14 366	12 343	17 745	20 002	31 646	19 955	35 942
New Zealand	375	4 556	2 358	1 472	391	-1 386	2 015	1 751	-1 260	-1 602	343
Norway	1 079	8 995	1 478	1 840	-80	791	2 098	3 140	5 901	5 016	2 546
Poland	..	..	..	..	13	18	29	42	53	45	316
Portugal	21	374	165	474	687	141	283	689	749	1 918	2 923
Spain	1 274	8 793	3 442	4 424	2 171	2 648	3 900	3 608	5 222	10 142	15 427
Sweden	4 597	48 074	14 743	7 053	409	1 357	6 698	11 214	4 664	12 641	21 231
Switzerland	..	33 553	6 709	6 212	6 050	8 765	10 798	12 214	16 152	18 023	14 225
Turkey	..	97	88	127	133	175	78	163	110	251	367
United Kingdom	55 112	185 581	18 636	15 972	19 156	25 573	28 251	44 329	34 125	63 734	114 957
Unites States	134 354	175 985	30 982	32 696	42 647	78 164	73 252	92 074	84 426	99 517	121 644
<b>TOTAL OECD</b>	<b>307 364</b>	<b>1 058 520</b>	<b>231 287</b>	<b>190 754</b>	<b>177 659</b>	<b>204 707</b>	<b>239 593</b>	<b>308 771</b>	<b>332 720</b>	<b>394 229</b>	<b>578 163</b>

p Provisional.

Break in series: Australia 1995, France 1988.

Source: *International Direct Investment Statistics Yearbook*, 1999, OECD.

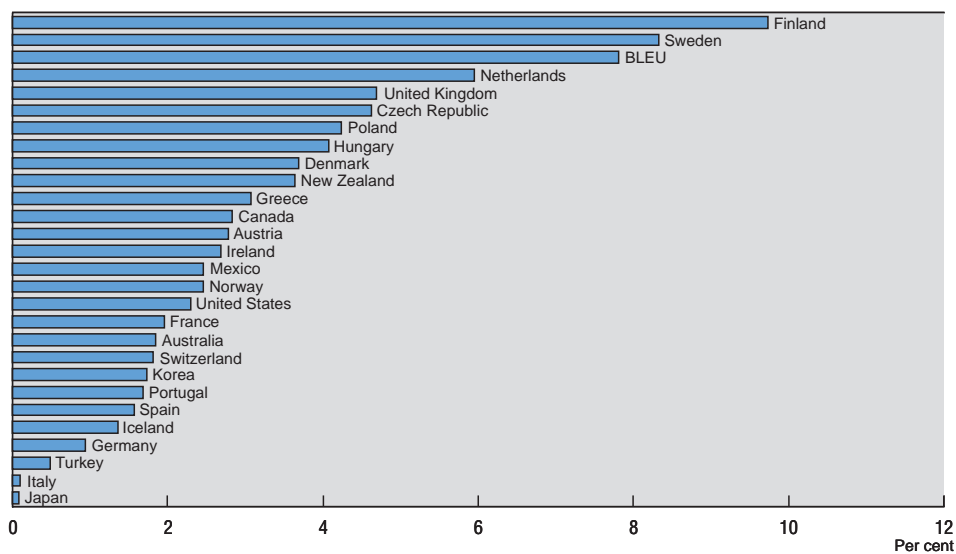
Table 3. **Direct Investment from abroad in OECD Countries: Inflows**  
As a percentage of GDP

	1990	1991	1992	1993	1994	1995	1996	1997	1998 <sub>p</sub>
Australia	2.20	1.36	1.72	1.05	1.21	3.60	1.29	2.22	1.85
Austria	0.41	0.22	0.50	0.54	0.67	0.82	1.94	1.29	2.78
Belgium-Luxembourg	3.86	4.38	4.77	4.74	3.37	3.72	4.93	4.82	7.82
Canada	1.32	0.49	0.83	0.86	1.49	1.61	1.59	1.89	2.84
Czech Republic	..	..	3.36	1.90	2.18	5.04	2.53	2.50	4.62
Denmark	0.91	1.08	0.69	1.21	3.22	2.31	0.42	1.65	3.69
Finland	0.58	-0.20	0.38	1.02	1.61	0.84	0.89	1.77	9.73
France	1.31	1.26	1.35	1.32	1.17	1.54	1.43	1.66	1.96
Germany	0.18	0.28	-0.11	0.02	0.35	0.50	0.24	0.46	0.93
Greece	1.21	1.27	1.16	2.80	3.12	3.68	4.77	2.99	3.08
Hungary	0.87	4.37	3.97	6.06	2.76	10.06	4.43	4.60	4.08
Iceland	0.35	0.27	-0.16	..	..	0.20	1.12	2.01	1.37
Ireland	0.57	2.53	2.38	1.73	0.77	0.95	2.62	2.17	2.69
Italy	0.58	0.22	0.26	0.38	0.22	0.44	0.29	0.32	0.10
Japan	0.06	0.04	0.07	0.00	0.02	0.00	0.00	0.08	0.08
Korea	0.31	0.40	0.24	0.18	0.21	0.26	0.48	0.64	1.73
Mexico	1.00	1.51	1.21	1.09	2.61	3.33	2.79	3.10	2.46
Netherlands	4.29	2.26	2.43	2.73	2.17	3.05	3.72	2.53	5.96
New Zealand	3.90	4.07	2.72	5.06	5.24	4.49	5.65	2.82	3.63
Norway	1.57	0.56	-0.34	1.93	2.21	1.52	2.06	2.37	2.46
Poland	0.15	0.47	0.80	1.99	2.02	3.07	3.34	3.62	4.24
Portugal	3.77	3.13	2.03	1.85	1.44	0.66	1.21	2.49	1.67
Spain	2.81	2.35	2.31	1.69	1.95	1.11	1.11	1.04	1.57
Sweden	0.86	2.65	-0.02	2.07	3.20	6.25	2.02	4.79	8.33
Switzerland	2.40	1.14	0.17	-0.04	1.29	0.72	1.04	1.97	1.81
Turkey	0.52	0.60	0.57	0.41	0.49	0.55	0.50	0.45	0.48
United Kingdom	3.37	1.58	1.55	1.64	1.03	2.05	2.26	2.89	4.68
United States	0.87	0.40	0.32	0.80	0.67	0.84	1.14	1.35	2.30

p Provisional.

Source: Foreign Direct Investment database, 1999, OECD.

**Graph A1. Direct investment from abroad in OECD countries: inflows**  
As a percentage of GDP: 1998



Source: OECD.



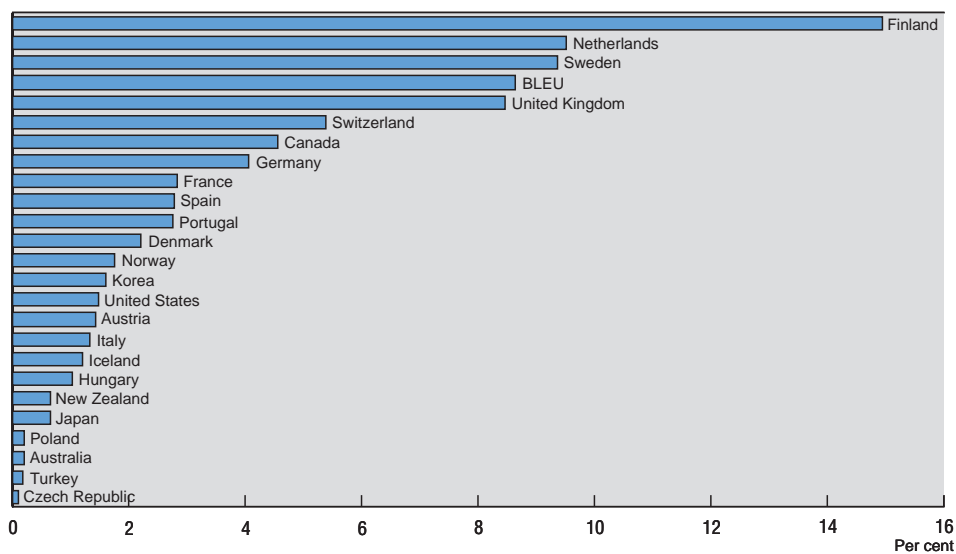
Table 4. **Direct Investment abroad from OECD Countries: Outflows**  
As a percentage of GDP

	1990	1991	1992	1993	1994	1995	1996	1997	1998 <sub>p</sub>
Australia	0.09	1.01	0.33	0.62	1.62	1.09	1.50	1.50	0.19
Austria	1.04	0.77	1.00	0.80	0.61	0.49	0.85	0.94	1.42
Belgium-Luxembourg	2.97	3.06	4.38	2.07	0.49	4.03	2.83	3.00	8.65
Canada	0.91	0.99	0.63	1.06	1.69	2.00	2.17	3.63	4.57
Czech Republic	..	..	0.07	0.29	0.30	0.07	0.27	0.05	0.10
Denmark	1.13	1.38	1.51	0.99	2.66	1.70	1.37	2.48	2.21
Finland	2.01	-0.10	-0.71	1.67	4.39	1.19	2.88	4.42	14.94
France	3.03	2.09	2.30	1.58	1.83	1.03	1.98	2.55	2.83
Germany	1.48	1.33	0.94	0.90	0.92	1.63	2.17	1.93	4.06
Greece	..	..	..	..	..	..	..	..	..
Hungary	..	..	..	0.03	0.12	0.10	-0.01	0.95	1.01
Iceland	0.16	0.40	0.04	0.18	0.37	0.34	0.85	0.69	1.21
Ireland	..	..	..	..	..	..	..	..	..
Italy	0.70	0.64	0.49	0.73	0.50	0.53	0.53	0.93	1.33
Japan	1.71	0.93	0.47	0.33	0.39	0.44	0.51	0.62	0.64
Korea	0.41	0.51	0.38	0.40	0.65	0.78	0.96	1.01	1.60
Mexico	..	..	..	..	..	..	..	..	..
Netherlands	5.39	4.68	4.46	3.94	5.26	5.02	7.97	5.49	9.52
New Zealand	5.47	3.53	0.98	-3.17	3.93	2.92	-1.93	-2.47	0.65
Norway	1.28	1.56	-0.06	0.68	1.71	2.14	3.73	3.27	1.74
Poland	..	..	0.02	0.02	0.03	0.04	0.04	0.03	0.21
Portugal	0.24	0.61	0.73	0.17	0.32	0.66	0.69	1.89	2.76
Spain	0.70	0.84	0.38	0.55	0.81	0.64	0.90	1.91	2.79
Sweden	6.42	2.95	0.17	0.73	3.38	4.85	1.85	5.55	9.36
Switzerland	2.94	2.67	2.48	3.70	4.13	3.97	5.47	7.06	5.39
Turkey	0.06	0.08	0.08	0.10	0.06	0.10	0.06	0.13	0.18
United Kingdom	1.91	1.58	1.83	2.71	2.77	4.00	2.96	4.97	8.47
United States	0.56	0.57	0.71	1.23	1.09	1.31	1.14	1.27	1.48

p Provisional.

Source: Foreign Direct Investment database, 1999, OECD.

Graph A2. **Direct investment from abroad in OECD countries: outflows**  
As a percentage of GDP: 1998



Source: OECD.

Table 5. Direct Investment from abroad and in OECD Countries: Inward and Outward Position

At year-end

Million US dollars

	Inward					Outward				
	1990	1992	1994	1996	1998 <sup>p</sup>	1990	1992	1994	1996	1998 <sup>p</sup>
Australia	75 801	78 592	86 974	107 615	96 881	31 153	34 712	39 857	51 237	55 599
Austria	9 976	11 209	13 092	18 258	24 943	4 498	6 862	9 282	12 781	17 111
Belgium-Luxembourg	..	..	..	..	..	..	..	..	..	..
Canada	112 844	108 503	110 204	131 071	141 822	84 808	87 870	104 302	132 416	156 655
Czech Republic	..	1 606	3 077	7 061	..	..	..	..	..	..
Denmark	..	..	..	..	..	..	..	..	..	..
Finland	5 132	3 689	6 714	8 797	16 455	11 227	8 565	12 534	17 666	28 037
France	86 508	100 209	123 887	143 937	..	110 119	140 679	163 075	192 973	..
Germany	119 618	129 970	160 128	188 502	..	148 456	170 867	213 654	271 241	..
Greece	..	..	..	..	..	..	..	..	..	..
Hungary	569	3 424	7 087	14 690	18 255	..	..	291	493	1 286
Iceland	147	124	128	197	457	75	97	146	241	361
Ireland	..	..	..	..	..	..	..	..	..	..
Italy	57 996	48 474	58 846	72 482	..	59 039	65 816	81 383	107 441	..
Japan	9 850	15 511	19 211	32 675	26 647	201 441	248 058	275 574	282 257	267 584
Korea	..	..	..	..	..	2 339	4 511	7 623	13 796	20 433
Mexico	7 613	11 453	6 234	5 975	..	..	..	..	..	..
Netherlands	73 824	81 191	103 359	131 146	..	109 094	124 746	149 023	203 248	..
New Zealand	..	..	19 849	33 584	35 735	..	..	5 167	8 925	5 784
Norway	17 712	15 206	16 305	20 519	..	10 278	13 144	16 909	25 442	..
Poland	109	1 370	3 789	11 463	22 479	..	101	461	735	1 165
Portugal	..	..	..	18 945	21 616	..	..	..	4 725	9 842
Spain	65 917	79 203	86 161	98 431	118 794	15 654	20 911	28 331	36 616	68 461
Sweden	12 461	13 773	22 247	34 202	..	49 491	47 707	59 237	70 877	..
Switzerland	34 245	32 990	48 667	53 919	..	66 086	74 413	112 586	141 591	..
Turkey	..	..	..	..	..	..	..	..	..	..
United Kingdom	218 213	185 925	218 211	228 642	326 731	230 824	223 774	286 394	330 432	498 506
United States	394 911	423 130	480 667	598 021	811 756	430 521	502 063	612 893	795 195	980 565
<b>TOTAL OECD</b>	<b>1 303 447</b>	<b>1 345 551</b>	<b>1 594 838</b>	<b>1 960 132</b>	<b>1 662 572</b>	<b>1 565 103</b>	<b>1 774 896</b>	<b>2 178 722</b>	<b>2 700 328</b>	<b>2 111 390</b>

Note: Data are converted using the end-of-year exchange rates.

p. Provisional.

Break in series: Australia 1994, Germany 1992, Japan 1995, Poland 1993.

Source: International Direct Investment Statistics Yearbook, 1999, OECD.

Table 6. **Direct Investment from abroad:**  
**Inward Position by Industrial Sector**  
 Forint million

	1992	1993	1994	1995	1996	1997
<b>Agriculture and fishing</b>	<b>2 668</b>	<b>7 559</b>	<b>9 914</b>	<b>15 400</b>	<b>18 700</b>	<b>19 000</b>
<b>Mining and quarrying</b>	<b>5 920</b>	<b>8 850</b>	<b>8 859</b>	<b>11 300</b>	<b>19 900</b>	<b>22 900</b>
<i>of which:</i> Extraction of petroleum and gas	..	..	..	..	1 000	2 400
<b>Manufacturing</b>	<b>198 002</b>	<b>319 265</b>	<b>402 087</b>	<b>558 800</b>	<b>598 900</b>	<b>803 200</b>
<i>of which:</i>						
Food products	72 339	106 735	131 970	157 400	146 700	211 500
Textile and wood activities	22 665	34 781	42 453	64 000	68 500	88 100
Petroleum, chemical, rubber and plastic products	46 481	60 566	85 690	149 800	131 400	170 300
Metal and mechanical products	22 497	35 285	41 105	54 600	70 600	101 100
Office machinery, computers, radio, TV and communication equipment	11 770	47 118	59 313	80 100	79 400	89 800
Vehicles and other transport equipment	19 850	29 880	36 056	46 900	38 400	75 600
<b>Electricity, gas and water</b>	..	..	..	..	<b>229 200</b>	<b>281 000</b>
<b>Construction</b>	<b>16 218</b>	<b>25 743</b>	<b>39 215</b>	<b>45 900</b>	<b>59 600</b>	<b>51 100</b>
<b>Trade and repairs</b>	<b>54 394</b>	<b>87 751</b>	<b>114 285</b>	<b>155 900</b>	<b>183 100</b>	<b>263 700</b>
<b>Hotels and restaurants</b>	..	..	..	..	<b>36 700</b>	<b>50 700</b>
<b>Transport and communication</b>	<b>6 632</b>	<b>57 479</b>	<b>65 917</b>	<b>117 000</b>	<b>141 500</b>	<b>157 400</b>
<i>of which:</i>						
Land, sea and air transport	5 710	13 921	17 107	17 700	10 200	11 200
Telecommunications	922	43 558	48 810	99 300	121 900	135 600
<b>Financial activities</b>	<b>71 837</b>	<b>101 660</b>	<b>143 214</b>	<b>188 000</b>	<b>144 400</b>	<b>216 400</b>
<i>of which:</i>						
Monetary institutions	..	..	..	..	..	..
Other financial institutions	..	..	..	..	..	..
<i>of which:</i>						
Financial holding companies	..	..	..	..	..	..
Insurance and activities auxiliary to insurance	..	..	..	..	..	..
Other financial institutions and insurance activities	..	..	..	..	..	..
<b>Real estate and business activities</b>	..	..	..	..	<b>110 100</b>	<b>170 400</b>
<i>of which:</i> Real estate	..	..	..	..	48 700	68 600
<b>Other services</b>	<b>18 773</b>	<b>35 287</b>	<b>39 911</b>	<b>209 900</b>	<b>7 400</b>	<b>16 000</b>
Unallocated	2	11	40	-	-4 800	-
<b>TOTAL</b>	<b>374 446</b>	<b>643 605</b>	<b>823 442</b>	<b>1 302 200</b>	<b>1 544 700</b>	<b>2 051 800</b>
<i>of which:</i>						
<b>PRIMARY</b>	<b>8 588</b>	<b>16 409</b>	<b>18 773</b>	<b>26 700</b>	<b>38 600</b>	<b>41 900</b>
<b>MANUFACTURING</b>	<b>198 002</b>	<b>319 265</b>	<b>402 087</b>	<b>558 800</b>	<b>598 900</b>	<b>803 200</b>
<b>SERVICES</b>	<b>167 854</b>	<b>307 920</b>	<b>402 542</b>	<b>716 700</b>	<b>912 000</b>	<b>1 206 700</b>

Source: International Direct Investment Statistics Yearbook, 1999, OECD.

OECD PUBLICATIONS, 2, rue André-Pascal, 75775 PARIS CEDEX 16  
PRINTED IN FRANCE  
(21 2000 02 1 P) ISBN 92-64-176330-X – No. 51 145 2000