

Letter of Invitation to meeting with CzechInvest – investment and business development agency of the Czech Republic’s government

“Seminar on European Union market opportunities and the Czech Republic that has become major business partner for Taiwan in Europe”

Over thirty Taiwanese companies set up their presence in the Czech Republic and their projects are expanding despite increasing costs and shortage of labour in Europe. Mr Jaromir Cernik from CzechInvest’s Hong Kong office will explain the reasons why the Czech Republic still attracts companies to do business there and what are the prospects for future collaboration. Mr Cernik has worked with one break for six years for the Czech government and assisted dozen Taiwanese companies to set up in the Czech Republic. He also ran a business in Hong Kong. He speaks English, German, Czech and a little Chinese.

Organized by Industrial Development and Investment Promotion Committee of Taichung City and Kaohsiung County Government Economic Development Bureau and co-organized by CzechInvest, the seminars will be held on 10 – 12 November 2008.

Seminar is focused on Taiwanese companies and entrepreneurs that plan to set up in Europe.

We have the pleasure to invite you/ your representatives to participate in the said “Seminar”. Attached with this letter please find the Reply Slip of the Seminar.

Agenda:

- 1) Introduction to economy of the Czech Republic and investment environment
- 2) Investment Incentives and governmental policy to support foreign investors and entrepreneurs in the Czech Republic
- 3) Services of CzechInvest – governmental investment agency
- 4) Q and A

Abstract:

C Z E C H R E P U B L I C

Investment Environment

Reform of Science and Innovation Policy from March 2008

Reform of Public Finance from January 2008

The Czech Republic Has Reached Another Cycle

Shortage of Workforce?

October 2008

Will the Czech Republic be hit by credit crunch?

Czech economy continued very strong performance in 2007 and 2008 driven by private consumption and investments with growth rates exceeding 6 % while keeping inflation down (2.8 % in 2007, but 6 % in 1H2008). Czechs have reached already 87 % of European Union GDP per capita (17,000 USD per capita in 2007). The country has built its reputation mainly for its logistic convenience, unique infrastructure, transparent and pro-business oriented government and on-site support to foreign investors, no matter if during governments of Social Democrats or Civic Democrats.

Relatively small country with little more than 10 million people has very open economy based on export industries – automotive, electronics, ICT and mechanical engineering – and with high industrial concentration. The country has built entire supply chain within automotive industry including small suppliers and research and development facilities. Today, you can assemble the whole car just from the Czech parts. The country is well positioned within automotive and electronics cluster of companies that naturally attract additional investors to participate in this supply chain.

But the global financial crisis has already slashed share prices at the Prague Stock Exchange (PSE) by almost a half. It may freeze the flow of money from banks and weaken in particular small and medium-sized Czech enterprises. Global recession is looming and may also hit the Czech economy. CzechInvest has already felt repercussions of the financial crisis on the operations of foreign investors. The current developments are expected to have in the near future a negative effect on subcontractors in the automotive industry, glass and porcelain industry, textile industry, property development and in connection with this, in the long run on the construction industry. What is happening in the financial markets will leave a mark on the entire economy, including firms' willingness to invest. CzechInvest keeps a close watch on decisions of the biggest car maker Skoda Auto on its further expansion, for instance. They have not yet decided whether they should or should not go on with the expansion of the plant in East Bohemia.

With extremely strong Koruna, more voices arise for quick adoption of Euro. Obviously, such huge swings on the FX market are negative for the very open Czech economy. On the other hand, with Euro the economy would suffer higher inflationary pressures from convergence of the price level of the European Monetary Union. Czech government has abandoned old target for Euro adoption (2010) but has not set another one.

Any investment is becoming more expensive with the strengthening Koruna. We have to cope with this as we try to convince potential investors. Of course, it is hard to counterbalance the strengthening crown. On the other hand, it makes inputs cheaper. We therefore look for new openings for our activities. The market for direct investments is becoming saturated, and there's more room for technological centres needing less capital and manpower. These centres are often associated with an existing assembly shop and to develop it, but even in these cases it is necessary to encourage the investors. To do so we have a framework program in support of technological centres and centres of strategic services. Aftercare on-site assistance is even more important.

Czechs maintain financial discipline

The Czech Republic has very conservative and strong central bank (CNB) with aim to target inflation. The country has maintained relatively low interest rates (3.87 %, 3-months PRIBOR) that make financing of the projects more affordable. The Czech banks have also avoided to certain extent possession of toxic assets connected to the mortgage-linked stocks

that would hit the banks' liquidity. But as Czech commercial banks are now owned by Western banks (KBC, Societe Generale, Erste), we will have to wait if there is any impact coming from Western Europe. We will expect the banks to be even more conservative in financing speculative investments.

Czechs reform its applied science and innovation policy from March 2008: “Science makes from money knowledge; innovation makes from the knowledge the money.”

Czech government has started the reform of system of science, research and innovation policy since 26 March 2008. The reform has increased the Czech budget expenditures for applied science (0.92 billion Euro in 2008, 0.99 billion Euro in 2009, 1.07 billion Euro in 2010). It also brings more flexibility to start projects between Czech universities and private companies (investors) within the 7th framework programme of EU (FP7). Despite the fact that Taiwan is unfortunately not listed by the European Union as a member country for FP7 projects, the Czech operations may well cooperate with Taiwan on contract research or by engaging their researchers into international teams. Taiwanese investors in manufacturing sectors in Europe should utilize local manpower (PhDs) to develop their outputs up to demanding European market. This is also a role of CzechInvest to assist these companies in these intentions.

There are extensive resources to build infrastructure for applied research projects and through European Union programmes we are able to co-finance the hard infrastructure (buildings, lab equipment) up to 60 %. From the European Union funds the Czech Republic will receive payments over 5 billion Euro in between 2007 – 2013 for research and development infrastructure.

The Czech Republic has also reformed its public finance since January 2008

The reform decreases the corporate income tax down to 21 % in 2008, 20 % in 2009, 19 % in 2010. For individuals the flat rate of 15 % has been introduced in 2008 and 12.5 % flat is proposed for 2009. The reform also changes tax base calculation. For individuals the tax base includes social and health contributions. For corporations the reform brings advantages of multiple asset depreciations. The entrepreneur may deduct 100 % of research and development eligible costs from the tax base and at the same time amortize the machinery and equipment used for this research and development if not contracted from the third parties.

In addition, the investor may apply for standard investment incentives through CzechInvest for manufacturing projects offering 5-year tax relief and job creation grants according to the Czech law. Also CzechInvest offers grants from the European Union through its programmes – namely programme “Potential” and “Innovation”. It may take longer time and investor has to find its own financing to the project, though. But it finally works - and mostly on infrastructure projects and on investments into older industrial installations (Brownfields).

The Czech Republic has reached another cycle

Czech Republic has attracted foreign investors due to its transparent law and stability, both economic and political, and predictability. The current problems are unquestionably transient, and we expect some work force to be released so in the next phase of the economic cycle investors here can again look for qualified workers, which they are now a bit short of. But CzechInvest has been recently successful at attracting investments in projects with higher added value.

It is the first time in history when investments in research and development and services account for most of the projects attracted by us. This is clear evidence of our country's transition toward a knowledge-based economy. We expect this trend to continue.

And this is also the way the number of projects increases and not their volume because such investments demand less capital and also create fewer jobs. This is a good thing, though, because there's no need for a high number of new jobs in the Czech Republic now. On the contrary, these investments stimulate demand for people with specialized education, which has a knock-on effect on education, from colleges to universities. It has a positive influence on overall cultivation of the economy. When compared to its competitors in the region, the Czech Republic performs well in terms of shifting the economy into higher gear due to its relatively small size, infrastructure (schools) and immigration (Germany, USA, Ukraine, Slovakia). Today, Czech cities attract expatriates from both Eastern and Western Europe to work for subsidiaries of foreign companies due to relatively flexible Czech labour market and expanding economy. We think this talent pool will be crucial for attracting new projects in the near future. And the story is not only about Prague City.

Research and development surpasses manufacturing investments in the first half of 2008. Two-thirds of investors entering the Czech Republic establish the technology centres or shared-services centres.

With CzechInvest's assistance the Czech Republic attracted 124 new investments worth nearly CZK 20 billion (1 Euro = 25 CZK) in the first half of this year. More than 65 % of these investments involve research and development or services. The new investors plan to create 9,669 new jobs, 34 % of which will be intended for university-educated specialists.

Software development dominates the investment projects

The largest numbers of new investments were prepared by firms engaged in software development. With CzechInvest's contribution, 16 programming centres worth CZK 233.35 million will be established, eventually employing 2,561 specialists. Carmakers and automotive-component manufacturers account for another thirteen investments, and yet another 13 companies will focus on research and development in the area of mechanical engineering.

Such investments profit from a trend where firms endeavour to innovate their products, increase their utility value, instead of increasing production capacity, which may be affected by declining demand in world markets.

Tables

Country of origin

Investment projects mediated by CzechInvest in 1H 2008 (1 Euro = 25 CZK)

Investment projects mediated by CzechInvest in 1H 2008

Type of investment	number	jobs	investment amount (CZK mil.)
Manufacturing	44	4,542	17,043
Shared services	26	4,587	1,294
Technology centres	54	540	1,424
Total	124	9,669	19,761

Country of origin	Number of firms	Investment amount (CZK mil.)	Jobs	Jobs for univ. graduates	Proportion of univ. graduates
Belgium, Luxembourg, Netherlands	8	1,512.73	1,472	696	47%
Czech Republic	78	5,426.93	4,023	1,857	46%
Denmark, Finland, Sweden	1	125.00	30	2	7%
France	3	843.55	354	30	8%
Ireland, Great Britain	2	48.37	211	151	72%
Italy, Cyprus, Spain	5	1,482.75	727	72	10%
Japan	2	749.26	324	2	1%
Korea, Taiwan	4	401.82	373	14	4%
Germany	12	4,602.44	1,117	65	6%
Austria, Switzerland	1	234.00	150	145	97%
USA	4	470.45	340	160	47%
Other	4	3,863.74	548	54	10%
TOTAL	124	19,761.04	9,669	3,248	34%

But is shortage of highly educated specialists one of the most acute problems of the Czech economy?

The situation is changing. It is to a great extent a question of supply and demand, and mergers that take place with CzechInvest's assistance between firms creating technological centres and universities. This has been a success for instance in the Cities of Liberec (North Bohemia) and Prague. A special requirement has been received from German company Bosch Diesel (auto technology firm), where we mediate contacts with universities, so that the investor can influence the number of students of certain disciplines. This is a direction we want to follow, as we see much room for CzechInvest there.

Qualified staff will be also available from existing companies that will suffer from global pressures in glass industry, textile machinery industry, for instance. We expect the shift of this labour into progressive industries. The employers have to monitor the situation of the labour market closely though. Thus we always consult with investors their human resources strategy in order to hire local Czech managers to help them recruiting. It is very key point, especially nowadays. Of course, investors should comply with local conditions and offer appropriate compensations. This will eliminate the fluctuations of the staff in the future, though. The Czech nominal wages surge at 7 % rate annually. The average wage in very general has increased up to 1,000 Euro a month in the country.

CzechInvest attracts foreign investors into the Czech Republic and assists their investment projects. CzechInvest also assists Czech companies with their investments onto foreign markets. For more information please visit www.czechinvest.org

Contact:

Mr **Jaromir Cernik**
Executive Director, Southeast Asia Operations

CzechInvest

Room 2207-9, Tower II, Lippo Centre
89 Queensway, Admiralty
HONG KONG

Phone: (852) 2530 8806, IP Phone: (420) 2 96 34 905

Fax: (852) 2530 8136

E-mail: southeast-asia@czechinvest.org

www.czechinvest.org