

Free Economic Zones' Influence on Regional Development in Baltic States

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Abstract:

Purpose and Originality: The purpose of this research was to identify how Free Economic Zones (hereinafter – FEZs) influence regional development process and to give some evidences from Baltic States (Lithuania, Latvia and Estonia). The value of the research is achieved by revealing what kind of challenges FEZs are dealing with participating in the regional development. This research is presenting results of the original empirical research made in Baltic States.

Method: The purpose of the study was achieved by using approaches of Theory of Economic Development and System Theory to explain how Free Economic Zones are acting (in relations with other regional actors) to influence the regional economic development in Baltic States. The data was collected by applying the explanatory qualitative research. The main method was the semi-structural interviews with representatives of FEZs in Lithuania, Latvia and Estonia. The method of qualitative content analysis was used for the analysis of research data.

Results: Results of this research has shown that FEZs actively interact with regional actors of host region such as public administration bodies, NGOs, businesses, universities and EU Commission in certain regions. It was revealed that although at different level in each investigated region, FEZs in Baltic States make influence on the regional development, providing new economic activities, investments in infrastructure, attraction of advanced businesses as well as formation of new businesses creates an impact on the regional development.

Society: The research results give some ideas for regional actors (stakeholders of FEZs, public administration bodies) what are main challenges for FEZs and what is needed to be done to exploit their potential to gain more added value for regions.

Limitations / further research: As the empirical research was conducted in three FEZs, results can not be generalized for all FEZs in Baltic States. But in the future the sample could include all FEZs from Baltic States and more representatives of them. More over a comparative analysis of countries with similar economic and social development level is recommended.

Keywords: free economic zone, regional development, economic development, local government, Baltic States.

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1 Introduction

Contemporary trend of globalization raise many challenges for regions and their development. Regions are essential dimension of the development process, not just in the more advanced but also in less-developed (developing) countries (Scott & Storper, 2003). The regions' development in science literature is defined as the development of the integral community life's aspects such as social, economic, environmental, health care, technology, culture and recreation in the concrete territory (Tamošiūnas, 2009). On the other hand as the pieces of a system, the economic success of a country in national level relies on competitive and dynamic regions to achieve their development objectives in following fields; political, economic, social, technological, environmental and legal. Also it is possible to find researches suggesting governments to put more emphasis on adapting subsidies to specific entrepreneurial activities and promoting the emergence of common linkages between different sectors (i.e. enterprises and universities) (Stejskal et. al., 2016). Therefore zones with economic incentives (including Free Economic Zones (hereinafter - FEZ)) together with the Industrial Clusters have become more and more popular in order to bring dynamism to the country economy through regional economy.

Economic zones phenomena got very popular when policy-making institutions become conscious with the fact attracting new investments bring along new economic activities. New economic activities mean creation of new jobs which has a vital affection on successful economic development. Although in general, such zones are considered to be "promoted by national, regional, and local governments to spur economic growth and competitiveness" (UNIDO, 2015). Due to the fact that every region has divergent development goals and characteristics, policy makers have used different FEZs policies in order to achieve the specific regional development goals.

Baltic States (Lithuania, Latvia and Estonia) became members of European Union (hereinafter - EU) on the 1st May, 2004. Since then, EU is working with these three states to achieve regional development goals as one developing region. Baltic States share the history of being occupied by several foreign powers. This separated the Baltic States from Western Europe and the rest of the world. Naturally the states had to adapt the changes of the political reforms. This led the states to look for ways to catch up with the global economy and achieve the economic development goals. OECD published "Policy insights from a decade of Baltic transition" which is mainly pointing out that "The observation of a decade of transition in the Baltic and in other transition countries reported in several OECD Surveys provides solid evidence that macroeconomic stabilization is not an end in itself. It is a necessary condition to start the reform process" (OECD, 2000). Baltic States were far behind Western EU member states in development level perspective which is why they needed solid strategic planning on development goals and sustainable solutions to the economic issues they had. One of the policies Baltic States used in order to catch up with the other developing members was to work on attracting foreign investors to lagging regions. So the Baltic States were racing two

battles at a time; trying to catch up with EU level and trying to implement micro economic stabilization policies along the regions. However stable economic development of all countries' regions is still remaining as a huge challenge for all three Baltic States. That is the main reason these research and thesis focused on Baltic States and the influence of FEZs on regional economic development.

The analysis of previous studies of FEZs revealed that some studies were focusing on main policy issues and presented FEZ as the tool for the use of policy makers (Akinci & Crittle, 2008; Gauthier, 2011; Farole, 2011; Farole & Akinci, 2011; Pakdeenurit et. al., 2014; Daru, 2016; Zeng, 2016), some were analyzing issues of the policy debate (governments policy on economic zones) (Aggarwal, 2011; Bernstein et. al., 2012; Sosnovskikh, 2017), some presented results of case studies from countries (Kocaman, 2007; Yeung et. al. 2009; Fakroun, 2012; Zeng, 2012; Zeng, 2014; Hamed, 2014), or the social perspective of the FEZs and its labour consequences (Romero, 1995; UNIDO, 2015; Neveling, 2015). There are some researches focused on FEZs and its sustainable development in Lithuanian regions (Auruškevičienė et al., 2007; Navickas et al., 2008; Navickas, 2008); FEZs and their peculiarities in Latvia (Krodgers & Strazds, 2000; Rankevica, 2006; Ziedina & Piese, 2017; Gulbis, 2018; Ziedina & Piese, 2019), FEZs and their development issues in Estonia (Zoubir & Lhabitant, 2003; Skorobogatova, 2008). However, there was still a lack of the research presenting FEZ as a tool for regional development in all three Baltic States, revealing FEZs' similarities and differences.

Therefore, *the scientific problem* can be expressed by a question: how Free Economic Zones are acting (in relations with other regional actors) to influence the regional economic development? *The aim* of this research is to identify how Free Economic Zones (hereinafter – FEZs) influence regional development process and to give some evidences from Baltic States (Lithuania, Latvia and Estonia). *Research objectives* are: 1) to present the concept of FEZs; 2) to identify specifics of FEZs' activity in Baltic States (goal, structure, peculiarities of activity and connections to other regional actors); 3) to discover challenges for the activity of FEZs in Baltic States to strengthen regional economic development. *Scientific methods* as scientific literature analysis, systematization, semi-structured interviews and content analysis are used in this research.

By this research, authors aim to understand the systematic insights of the FEZs and their influence to the host country/region. The study also lays stress on economic point of view, when analysing the impacts of FEZs on regional development. Furthermore the research explains the Baltic States FEZ policies and their connection to the regional development actors. The research is an informative guideline for the public policy too; in view of the fact that it gives insights to FEZs and how they interact with the public policy actors.

2 Theoretical framework

Many regions in are looking for new ways of acting to create the competitive advantage and to attract investors. It is based on the Theory of Development, where the term “economic development” refers to long-term changes in systems of production and distribution of goods and services affecting human welfare (Copestake, 1999). In common usage, development is usually assumed to be a definition of a good thing, however, economic development seeking for long-term benefits usually is led by short-term “pain”: local government investments (funds from tax payers), adaptation of infrastructure network, social changes in labour market (need of special group of professionals, strategies for their attraction, accommodation, network for social services’ supply, etc.).

The zones with economic advantages have been a phenomenon in most of the countries in history. These zones sometimes were used to attract greater capacity in exports or imports, sometimes create a better environment in industrial activities and sometimes they were used to attract and control the Foreign Direct Investment (hereinafter - FDI) to the region or the country.

The current literature has number of titles and translations for this type of zones. A study led by ILO (Long, 1986) states that there are 19 different terms used in order to express such zones. Most popular ones are as following: Free Economic Zone (hereinafter - FEZ), Special Economic Zone (hereinafter – SEZ), Free Trade Zone (hereinafter - FTZ), Free zone (hereinafter - FZ), Export Processing Zone (hereinafter - EPZ) and Industrial Free Zone (hereinafter - IFZ). Those types of zones differ according to the establishment goal, the market orientation and features of activity, however, they have similarities too. In order to maintain the integrity and not to cause further confusion, the term “Free Economic Zone (FEZ)” is used along the outline of this research. This research was following the definition of the FEZ where it can be defined as regional industrial zone with special incentives set up to attract foreign investors (a single management or administration, tools and policy), in which imported materials undergo some degree of processing before being exported again (ILO, 2014; Zeng, 2016). This definition reflected all important features for the research: zone of industry in a region, attraction of foreign investments, policy formation and implementation.

Although there are many definitions to the term FEZ as it was used in many countries and in many languages but zones with particular tax relieves from public administration in order to attract FDI, has been a part of international economy for a long time. Especially in developing countries, the need of procuring the capital for development goals pushes policymakers to maximize the exports and also to minimize the imports as this is the way to procure the capital. Although the developed countries are providing assistance and funds to developing countries, such provisions have some limits with regulations and effectiveness. In such situations countries require policies to achieve the development goals by procuring the capital.

The need of regional policy and decisions can be attributed to large and persistent differences in economic development across sub-national regions in European Union countries (Beugelsdijk et al., 2018). In EU FEZs are used generally in order to create a policy base for regional development purposes in the lagging regions to create a competitive and attractive economic activity zone.

EU uses NUTS regional classification system* to determine the eligible regions that can benefit from various funding options supplied by EU including Regional Development Fund. As the zone structure requires incentives from each government, EU aims to prevent the organizational crimes in the member states and institutional difficulties in the public administration bodies and highlights the importance of sufficient regulatory supervision in such zones. Grounds for establishing FEZs may differ in zones, as each region and country has various goals of development, but the literature review has revealed five main goals of establishment in FEZ policy (see Figure 1).

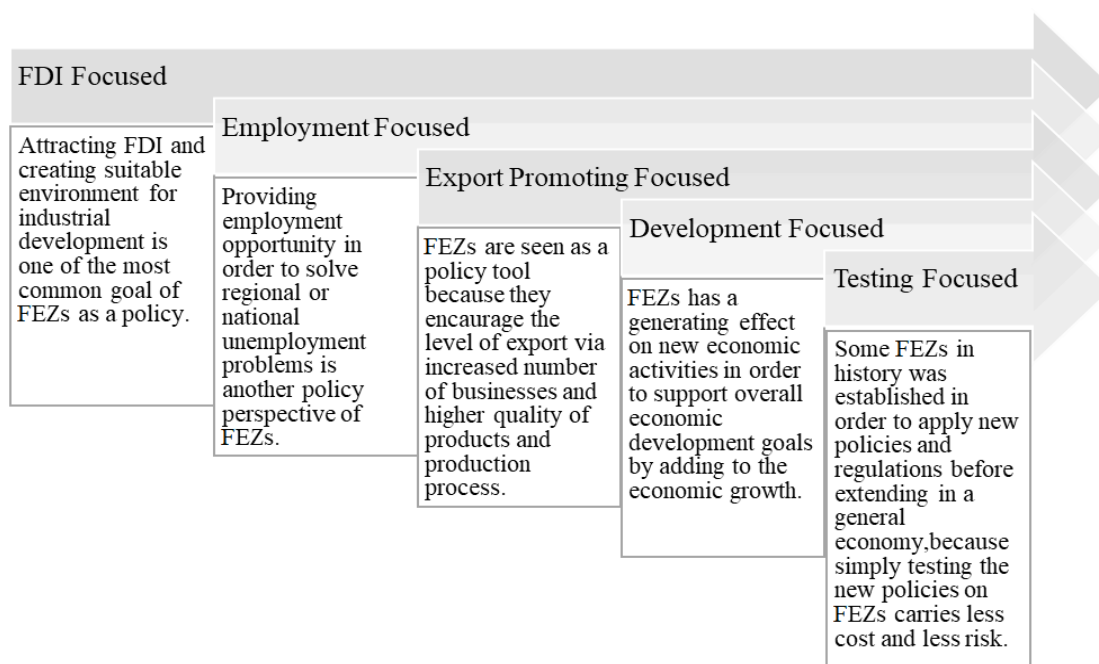


Figure 1. The common policy goals when establishing FEZs. Authors' conducted based on Madani (1999); Akinci & Crittle (2008); Farole & Akinci (2011); Zeng (2016).

These five policy goals are shared by many countries, which makes it desired and popular among the countries in need of new policies. Through FEZs, governments aim to develop and diversify exports while maintaining protective barriers, to create jobs, and to pilot new policies and approaches in various areas (Akinci & Crittle, 2008). Giving incentives on taxes

* The Nomenclature of Territorial Units for Statistics (hereinafter - NUTS) was drawn up in 1988 in order to provide a single uniform breakdown of territorial units for the production of regional statistics for the European Union (Commission Implementing Regulation (EU) 2052/88 1988).

and advantageous regulations governments are capable of controlling economy more efficiently.

Based on the System Theory it is emphasized that FEZs are acting like an open system (a group of interconnected elements (having clear relations between elements and with the whole system) and having links with other subjects (other systems or their subjects)) (Laszlo & Krippner, 1998; Casey, 2006; Bawden, 2010). To understand the institutional structure (system) of the FEZs, knowing the actors taking role is significant. The roles of the FEZs could be divided in three: FEZ unit, developer/operator and the end users (for key responsibilities and relationships in a FEZ, see Figure 2). The FEZ unit is basically the government or public side of the zone and carries out many details including supervisory of the operations in the zone. The developer is the private side and is the actor that carries out the development of the zone. Lastly end users are the companies that are actively operating in the Zone and are entitled to the zone incentives supplied by FEZ unit.

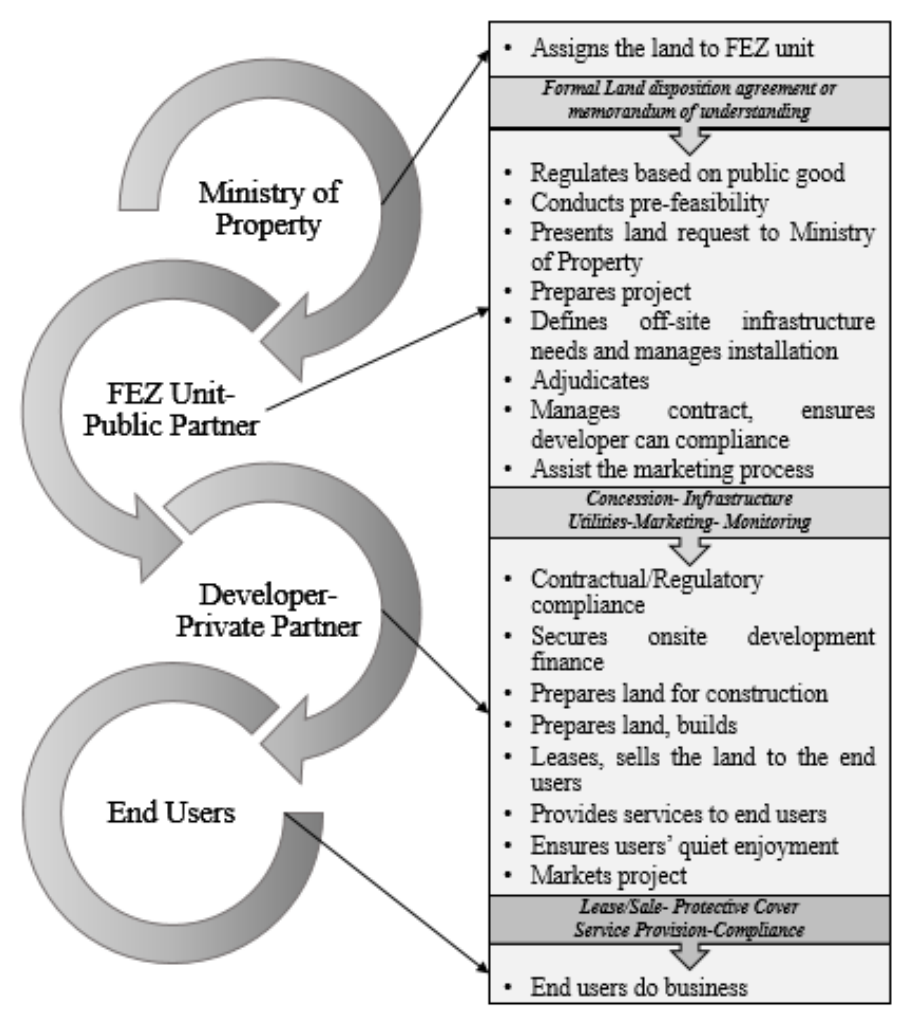


Figure 2. Key Responsibilities and Relationships in FEZ. Adapted by authors from Gauthier (2011).

It is understandable that there are confusions about FEZs and public-private partnerships (hereinafter - PPP). Although there are FEZs in PPP format, it would be a mistake to consider

all FEZs as PPPs. The institutional structure of FEZs is very well alike independent from the fact that FEZ is a PPP or not. The structure includes two sides; public and private. There is an agreement between sides regulating the terms and conditions. The public side undertakes number of responsibilities; the land assignment through it's' allocation function, strategic planning of the zone and its operations, legislative and enforcement role of the regulations (Gauthier, 2011). Also public side is responsible from providing goods and services when the private side is not or cannot provide. FEZ as a policy tool for government is a complex and time consuming process. That is why it requires experts in their fields to work on each and every step along the implementation of the FEZ as a policy tool.

The private side undertakes the other share of the FEZ process; business and business administration. Through the agreement private side and its roles are assigned by the government as well as the land for the zone to be established. The agreement simply includes a part where government expects to see development in the specific period of time from the developer. Developer should come up with realistic and achievable goals and government should approve the development goals. Government supervises the compliance of the development goals and ensures that there are legal enforcements following in case of a failure in the end of the period which was specified in the contract.

While government takes the off-site infrastructure investment share, private partner takes the onsite infrastructure investments. Private partner makes sure that the onsite of the zone is ready to be designed and planned for buildings for the potential investors and businesses. Private partner is responsible from the marketing and the advertising of the zone through many channels to the potential investors and businesses; foreign or local.

Moreover, FEZs have close connections to other actors in regions. *FEZs 2 Public Administration*. Public sector has a crucial role starting from pre-establishment process. Not only because the government is the authorized legislative and executive body within the country borders, but also representatives from government are always a part of its operations as members of the administrative board of the FEZs. This makes public administration closely associated with the FEZs. *FEZs 2 Businesses*. In many cases local businesses take FEZs as threat against their business. Because FEZs are known by FDI that they attract. For the local businesses having foreign investors means competition in many levels from labour to production and product cost. But also there are many cases that the FEZs affect the local businesses in positive way via raw material merchandising, knowledge spillovers and regional absorptive capacity. *FEZs 2 NGOs*. Many FEZs from around the world are known to be working with non-governmental organizations such as trade unions and chambers of commerce of the host government. These non-governmental institutions, has no direct role in the writing and passage of laws and regulations that affect businesses (these are handled by the public sector). Even they do not have direct influence on the FEZs, the relationship between non-governmental organizations and FEZs is that they create the optimal atmosphere for FEZs to be able to seen by the foreign direct investors. They hold some events and

conferences in order to bring related businesses and potential investors together. Although it seems like it does not have a big impact, NGOs help FEZs to be more recognizable within their target field group.

In summarizing it should be emphasized that FEZs is acting differently according to the type of the zone and laws and regulations of the country, however, FEZ is acting like a system with its actors and linkages to other systems. As direct activity of FEZs is matching objectives of regional economic development (attracting Foreign Direct Investments, creating new employment opportunities, increasing the level and quality of exports and the growth of local added value), outputs of FEZs are making the influence on the regional development process. The particular level of influence can be determined by environmental and internal factors and the situation of the Baltic States.

3 Method

This research is a part of the bigger study. The methodology of the study included both quantitative and qualitative approaches according to a framework of the empirical research (see Figure 3). The study was conducted in 2016-2018.

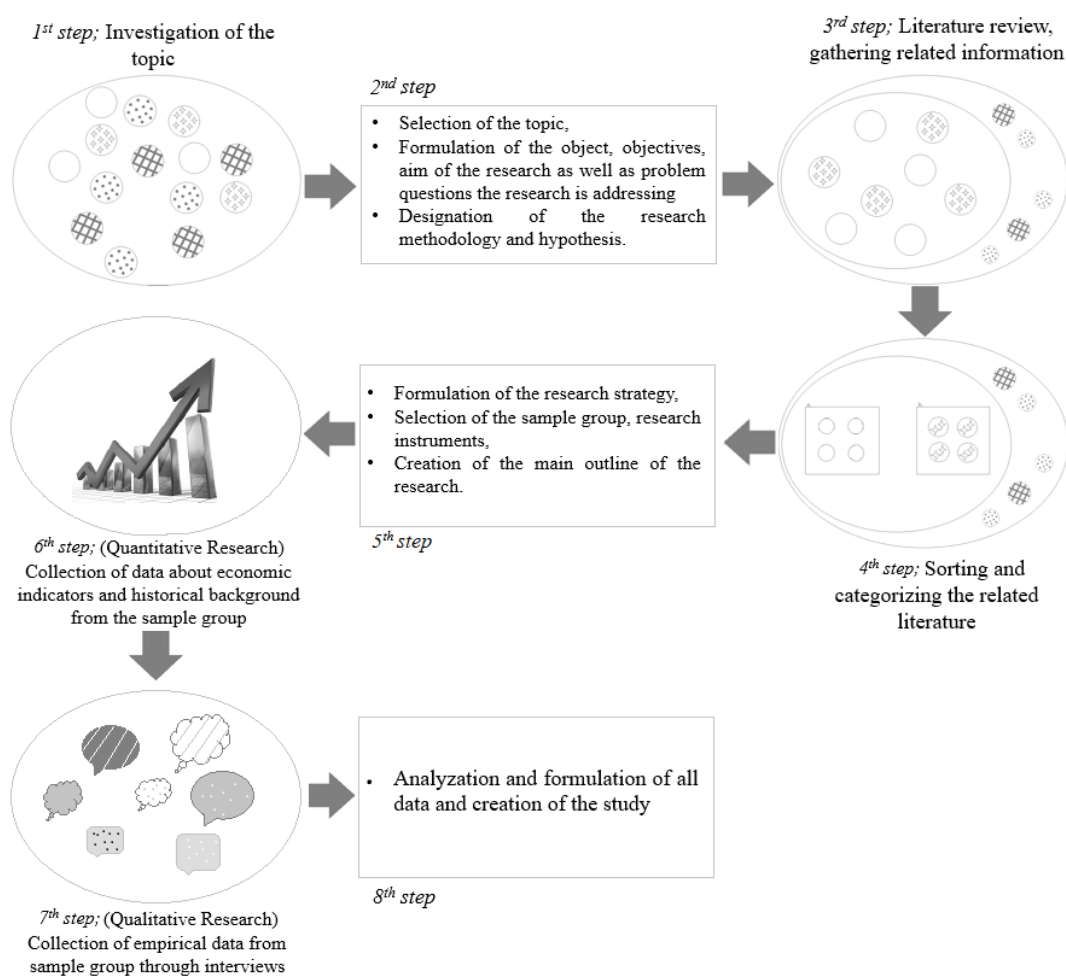


Figure 3. Visualization of the research strategy and design. Authors' conducted.

However, this research presents results of the qualitative approach, therefore only issues on this part are described here.

The method. Qualitative research was chosen in order to create an understanding to underlying causes and motivations of the FEZs in Baltic States and their influence on the regional development to their host region. Through qualitative research authors aimed to provide insights to the conditions and problems of the implementation of the FEZs policy in Baltic States and to develop ideas for the quantitative research. Authors followed oral survey method in order to collect the empirical data from sample group in Baltic States. The main reason for choosing *the scientific method of semi-structured interviews* was that this method was optimal one for collecting data for each representative who provided the latest data along with individual experiences from each state and zone. This method allowed authors the chance to look for deeper information if necessary and it entitled authors with the freedom to follow a new line of inquiry regarding to the direction of the interview.

Instrument of the research. For the qualitative research authors used the research instrument – *guidelines of the semi-structured interview*. The structure of guidelines was carefully designed by authors regarding the research problem and seeking to find out about the real situation of FEZs activity in Baltic States. The guidelines consisted of 25 questions oriented to the establishment of FEZ, FEZ direct activity and influence on regional development, interaction with public administration bodies, challenges and the future of FEZs.

The sample. As the FEZs in Baltic States are located in various locations and the quantity of the FEZs is relatively large (Lithuania had 6 FEZs, Latvia - 5 FEZs, Estonia - 3 FEZs), authors determined a sample group which research was focused on. Authors chose one FEZ from each state to collect the data about. The FEZs were selected according to their socioeconomic backgrounds. Purposive selection sampling strategy was chosen for the research. It made it useful as there were many types of FEZ, authors worked on the same types of FEZs from each state. Main motive while selecting the FEZs from Baltic States were expressed as follows: authors believed in order to address the research aim correctly, FEZs should be selected from cities which are not capitals, not the most urban areas also not known as the business centres of the Baltic States. Cause in that case the data and statistics may have been misleading in terms of population change, GDP, levels of export and import, unemployment level, FDI. So authors preferred FEZs in regions which are less developed comparing to the other regions in their home country in order to understand the importance of the FEZs in those regions, cities. So, finally 3 FEZs were selected for the sample: Šiauliai Free Economic Zone (Lithuania), Liepāja Special Economic Zone (Latvia), Sillamäe Free Zone (Estonia). Sample consisted of three informants from each Baltic States FEZs. The interviewees were selected following the method of criteria selection: 1) Informant had to be a part of administrative body of the FEZ; 2) Informant had to be working in the field not less than 6 months; 3) Informant had to have the managing experience in FEZs. According to

those criterias, *three informants* were selected (answers of informants were coded I_{LT}, I_{LV}, I_{EST}).

Research organizing. The empirical research was conducted in January-May of 2018. This first author of this scientific article conducted interviews. Author connected informants from each FEZ through e-mail or phone call. The author gave the important information about the research. The intended period of one interview was in between 20-40 minutes. In some cases the direction of the questions became deeper and the interview took longer than intended. Due to the convenience of the online channels and distances between the countries, 2 interviews were organized through Skype video calls and one was organized as a face-to-face interview in the office of the informant. The interviews were recorded and the usage of the collected data through the qualitative research was limited within scientific basis and only used for the scientific purposes.

Research ethics. Informants were fully obtained by the knowledge of the scope of the research and they are ensured that the data collected by the interview would only be used for scientific purposes within the research ethics frame. Before, after or during the interview, the interviewees have not been harmed physically, psychologically or via their vocation or future employment. Interviewees were given the required information in order to make an informed decision about whether or not they wish to participate in this study. In order not to cause invasion of privacy, each informant is given the chance to decide if they prefer to be preserved in terms of their privacy (seeking to ensure the confidentiality for informants) answers of informants were coded I_{LT}, I_{LV}, I_{EST}.

Results' analysis. In order to conduct a systematic analysis for the collected data, authors used firstly categorisation method of the data. And later the categorised data was analysed through the interpretation method in order to understand the findings and linking the findings to the data conducted by the quantitative research method.

4 Results

4.1 Situation of Lithuanian FEZ

Šiauliai Free Economic Zone was established in 2015 which makes it newest in the sample. History is separating Šiauliai from others as actually during 1997-1998 period the first FEZ was established in Šiauliai, but the operator who won the bid gave up on right to manage the FEZ because the infrastructure was not installed during that time and there was a problem with the land pollution. Then the government had to choose two other locations to establish new FEZs. The government has faced difficulties with land plan plots of these two new locations. The landowners gave very high prices and government decided to minimize the areas given to two FEZ areas in Klaipeda and Kaunas. Instead of the minimized areas in 2011, parliament decided that there would be 5 new FEZs established. One of them was decided to be established in Šiauliai, again. Thus the establishment of the FEZ in Šiauliai was postponed

until 2015, when the contract was signed between tender and Ministry of Economy. For zone to operate properly, 2 million Euros were funded in order to clean the land from pollution. Although the contract was signed in 2015, requirements such as infrastructural investments from both sides took long time. That is why the zone is not operating yet to its full potential.

Although Šiauliai has a perfect location and access to international airport right next to the FEZ, railways, sea ports, international roads and an industrial park located next to the FEZ; infrastructural difficulties decelerates the operation and attractiveness of the FEZ. Main sector the zone is promoting is industry sector such as metal plastic and furniture industries because trade is not supported by the law yet. International and national markets are seen as target market. Along with local investors, the potential investors are from Scandinavian States, Denmark and Finland.

Šiauliai Free Economic Zone is not yet operating full-potential (in the spring of 2018, when the research is conducted). It has 2 investors soon to finish the project design for the plan of factory, and many potential investors were lost because of lacking infrastructure. Until the operations of the investors begins (one expected to start within 2018, other 2019), there is no employment provided to the local labour market yet. But the city has around 100 000 population and an industrial park located within the region. Šiauliai is a promising zone in terms of providing employment to the residents in the following years. Even the zone has two investors, who are working on their designs for their buildings, Šiauliai Free Economic Zone has not yet successfully attracted FDI yet. The administrative body of the zone, which is a company from Lithuania, is constantly working and investing into its marketing. The zone is expected to be seen more actively in the national and international events in order to create contacts with the foreign investors.

Šiauliai Free Economic Zone is mostly focused on attracting foreign investors to the zone. Because in many cases it is known that new businesses attract other new businesses as zone becomes more attractive. Other case is that the businesses attract other businesses because before or after production process they need side businesses for example for packaging or logistics of the product. Also Šiauliai FEZ aspires to be in the same page with the education institutions in terms of creation of high-skilled labour force pool. Also it is possible to state that the local businesses are feeling the need to be threatened by the FEZ in Šiauliai because the common presumption is that new businesses will be attracted and local businesses have fewer opportunities. This is just a minor issue but still impacts the relations of the zone.

Šiauliai Free Economic Zone right now has one worker which is the director. It has a board consists of 7 people including city mayor and minister of economy. Governmental influence on the zone is not very big. Because Lithuanian FEZ law states that the administration of a FEZ belongs to the private partner. The governmental representatives are still members of the board and connection is always there. The zone also has two shareholders companies from region. The zone is a member of Lithuanian Chamber of Commerce which helps the zone to

be more active in international and national conferences and events also it creates a web of contacts for its members which are good for the reputation of the zone. I_{LT} states *“In short words this membership helps the zone to be seen and recognized”*. Other collaboration is between zone and a non-profit organization promoting the business opportunities to foreign investors *“Invest in Lithuania”*. It provides consultant services to the potential investors.

The interview with I_{LT} has revealed that it is possible to specify number of challenges when discussing the contribution of FEZ to the Šiauliai region. One of the most important challenge is that the lack of infrastructure. Although in 2018 the zone plans to have the first investors, it took long time for municipality and government to invest in infrastructure of the zone.

I_{LT} implies that the second and third ones at first does not seem as problem, but *“when investors are interested in the zone, they ask for statistics about the demographics and number of students who are enrolled in educational institutions, and when we provide this information to them it doesn’t seem very attractive to them”*. As it was mentioned, Šiauliai city is giving emigration and the number of students enrolled in higher educational institutions within region is getting lower each year. This creates a big drawback for the FEZ to be able to contribute to the regional development, because new companies need the work force which mainly will be provided from the region. It is also mentioned by I_{LT} that the educational institutions, businesses as well as FEZ may work on the needs of region as a group, maybe a cluster. The reason to that is the expert states that; *“If we can develop a well-educated labour force within the region meeting the needs of the foreign investors, which will make the region more attractive for investors”*.

4.2 Situation of Latvian FEZ

Liepaja Special Economic Zone is located within Latvian borders, is a zone located next to Baltic Sea. The Liepaja port is located within the borders of the zone. The zone was established in 1997, which makes is the oldest one in the sample group. During the period under Soviet occupation, economy of Liepaja got more active with the construction sector and import of labour force from other Soviet Republics. Also the city was a Soviet military city. Government worked particularly hard on the transformation process of the zone after Latvia gained its independence with other Baltic States. Liepaja also provides infrastructural advantages such as railways, seaways, international roads as well as 3 airports located within 200 km radius. The main sectors in zone are; production, industry, logistic services, cargo storage and real estate development. The zone is actively operating in international market and its main investors are from Scandinavian States, Denmark, Finland, Russia, Belarus and other countries.

With its 47 companies operating within the zone, Liepaja could be considered as a success story. It provides approximately 2000 employment opportunities. It became the second region with biggest share of GDP contributions after capital Riga. State labour agency provides

trainings for the employees prior to employment or to the unemployed at the employer's request and also provides grants for job creation for specific support groups. This provides a pool of employees with high skills for the investors. Through its successful implementation, Liepaja Special Economic Zone was able to attract investors which made almost 3 billion Euros of investment that were subject to the tax incentives in 2015 by their statistical estimations.

Liepaja Special Economic Zone also has development projects which are focused on the regions' infrastructural improvements. Since 2011-2012, each 1-2 years, the zone works on these projects. The field of the projects span from street construction to railway and airport improvements. Also zone is focused on the environmental issues and has an environmental plan for future activities and with reports analysing the state of the environment in the territory of the Liepaja Special Economic Zone and the possible impact of the implementation of the planning document on the quality of the environment.

I_{LV} states particularly that "*Liepaja Special Economic Zone has a positive impact on the region socially and economically*". The zone is partners with Latvian Chamber of Commerce and Industry which is the biggest association of entrepreneurs in Latvia. Liepaja Special Economic Zone participates in activities, seminars and events the Chamber of Commerce and Industry is holding. Via these events and seminars the zone is able to promote their economic incentives and attract new businesses to the zone. Also local administrative body is promoting the zone to possible investors because region benefits the new businesses.

Other interaction of FEZ of Liepaja is that it has 9 Board members that include 3 members representing the state so they direct connection the administration and decision making of the zone. In the other hand as they have direct connection too, zone can also give suggestions and requests to these ministries. Other members are consists of 3 members representing the Liepaja City Council and last 3 members are representing entrepreneurs in Liepaja. Board includes all three levels of actors from national government, local government and the regional entrepreneurs. The structure of the Board is well-thought as it helps the zone to have stronger development goals focusing on the interests of all three groups as well as the society.

Liepaja Special Economic Zone achieved the goals of establishment. The zone is now providing employment opportunities to many regional inhabitants and Liepaja comes as a second city after Riga in terms of production of entities such as goods and services. In order for the zone to attract FDIs and improve regional economic development region must have advanced facilities and should be seen as a promising zone in terms of operation.

After interview with I_{LV}, it is possible to state that the main and biggest challenge which zone is facing is in his words "*insufficient investment and funding for infrastructure*". The funding of the infrastructure is quite important for any potential investor because the main idea is to

create new economic activities. So when the potential investors and the zone interact the most important attraction is the infrastructure and facilities.

4.3 Situation of Estonian FEZ

Sillamäe Free Zone is a port located next to Baltic Sea and it is in the very east of Estonia, which makes it the most eastern FEZ in EU and closest to the Russian border. The Port started operating in 1999 and it was redesigned later in 2008. The zone was established in order to support cargo handling within the Port of Sillamäe. Area of the port is located within the free zone territory. Aim of the Sillamäe Free Zone is to support cargo deliveries via offering long term storage without need to pay any customs fees or taxes. It has the infrastructural advantages with connections via railways, seaways and highways as well as connection to the Russian border. The capital of the zone is shared 50 percent by Estonian government and 50 percent of Russian government. There are 4 terminals operated by different investors within the zone. The number of licensed operators in Sillamäe Free Zone is 10 with around 1000 employees. Main sector that is subject to economic activities within the zone is; transit cargo handling. The zone is actively operating in international market.

10 companies are operating within the Sillamäe Free Zone and total number of labour force including port employees and employees of the companies which are operating is approximately 1000. More than half of the labour force need is met by the locals of Sillamäe town, and around 90 percent of employees are the residents of the Ida-Viru region which Sillamäe city is located within. The zone is a part of the cluster within Sillamäe. Cluster helps the zone reach more labour force and provide them with jobs. According to their own statistics, every 7th person on the region is provided with a job by the clustering businesses.

Sillamäe Free Zone has main activities focused on imports and exports. The zone does not have direct connections to the public administration. But the most common customers are the local businesses, factories, traders and logistic companies that are either renting warehouses from the zone or they use other services provided by the zone.

Although there is no direct influence of public administration bodies to the administration of the zone, Government of Estonia is already taking an active part on the investment process of the Sillamäe Free Zone. One of the recent investment policies on the zone was built with the help or with the investments from EU, Government of Estonia and the owners of the port. The project consisted of creating a preliminary waiting area for the trucks that are passing to border and an electronic registration which allows the trucks to book a date and time for exact border passing. This area as well is located within the zone as the zone is very close to border.

The I_{EST} states “*We have excellent relations with the local public administration bodies and they are very supportive. We have regular meetings with them and we are discussing different projects related to for example different cargo handling within the zone. We feel that local public administration bodies should take a part in the process even though it is not a necessity*”

because it is a privately administrated zone". Also in some cases the projects that Sillamäe Free Zone is working on need coordination or confirmation from the local public administration. It is possible to state that the zone administration and the local public administration body is working harmoniously on these projects.

Another important point which was touched upon during interview, in I_{EST}'s own words: *"The customs personnel of the Sillamäe Free Zone are quite competent and well educated"*. No doubt this makes the zones' work function smoothly in terms of bureaucracy. This makes it easier to provide a better service to the end-client. As Estonia is one of the most advanced countries due to their e-government activities, possible difficulties are avoided by the use of document providing via electronic channels to the related institutions.

Sillamäe Free Zone positively impacts on regional economic development of Sillamäe region. The zone actively creates new employment opportunities to the local and regional labour market and also attracting new investments which make it easier to improve the infrastructural facilities within the region. The new companies are attracted to the region and the zone provides new export and import alternatives to the local businesses. Also even when there are tax incentives, the companies are supposed to pay some taxes to the government which allows government to make budget with higher public revenue. I_{EST} states *"I would say, yes, our goals have been achieved and the zone is developing even further. Our cargo volumes are growing year by year"*.

In order to facilitate new business development in Sillamäe Free Zone has established a Business Incubation Centre that provides companies with some services for improvement. It makes it easier for the zone to assist the new businesses along the beginning period. The zone is improving the regional economic development of Sillamäe while it is boosting the economic activities handled within the zone.

Although I_{EST} mentions that the zone does not have big challenges to face, there is an aspect which could be improved by the government. *"It is a challenge for us that there are some conflicts including host country and Russia. Better political connections and relations between neighbouring countries would improve our chances while attracting new economic activities. Because whether we want it or not the political situation affects our work as Russia is our main partner. A huge part of the transit cargoes handled by our zone either comes into the zone from or travels from the zone to Russia"* states I_{EST}.

5 Discussion

Despite of FEZs' environment (national, regional) all three FEZs in Baltic States meet some problems and challenges in their activities to use their full potential, to implement the FEZ's policy and to contribute to the regional economic development.

The individual governments while setting FEZs in these regions aimed that these regions would become business hubs and attract more businesses via becoming more and more developed. Zones in Liepaja and Sillamäe have more experience, better implementation of FEZ policy than the zone in Šiauliai. Liepaja and Sillamäe has successfully attracted FDI, provided region with new employment opportunities, focused on the attractiveness of the region and worked on infrastructure through their years of operation and it seems Šiauliai FEZs is on the beginning of the similar process.

Liepaja Special Economic Zone still needs the financial assistance from the government. As the zone gets the support from government it may add to its' successful operations by achieving the goal of attraction of the workforce to Liepaja region. Liepaja Special Economic Zone could be seen as a success story. Because, no doubt, the zone played an important role within the transformation process of a small military-related, hardly producing city into a second biggest production contributor city of the country. The zone helps the region in terms of employment opportunities and has constant connections with the local and national public administration as well as local entrepreneurs from Liepaja. This makes the zone focus on the interests of the benefits to regional society as well as the regional development in general.

Sillamäe Free Zone is successfully contributing to the development of the Sillamäe region. The zone is actively working on some future projects as well as development plans. Their development plans firstly includes establishing a passenger terminal within the zone and they aim to enlarge the territories by creating additional terminals to already existing 4 terminals. Zone is actively creating new employment opportunities to residents of the region and attracts investments on the infrastructure of the region which adds to the value of the region. The relationship of the zone with local public administration bodies as well as the national government functions well. Also is important to state that the leader (representatives of FEZ) improving the political connections and relations carries the big importance while attracting new economic activities. Resulting from successful relationships with other regional actors such as local businesses the zone functions as a tool of regional development and it generates employment opportunities, investments on the regional infrastructure, an attractive area for the new economic activities and new companies, lastly the alternatives for the imports and exports of the local businesses.

Šiauliai Free Economic Zone is facing number of difficulties. Indeed Šiauliai has a good potential of becoming a more productive region within the country, especially if the regional actors could be able to provide the needed support to the Šiauliai Free Economic Zone. The reason authors believe that the city has a potential even with no operations yet is; the fact the city still has relatively lower labour costs than other regions within the country may be able to create the boost which is needed. If the zone could commercialize that point and give emphasise on the already mentioned location related characteristics, it has great chance becoming the next business centre and FDI-related production region. The case of Šiauliai Free Economic Zone is a very clear example that the infrastructure means the most when it

comes to the attraction of the investors. The most important step for Šiauliai Free Economic Zone is to work on the infrastructure as intensely as possible. Most importantly, the region is in need of collaboration between businesses, zone, education institutions and local public administration bodies in order to look out for the biggest benefit that could be provided to the Šiauliai region. Authors believe via achieving the goal of creating well-educated labour force in the sectors which Šiauliai FEZ is promoting not only will create a more attractive region, but also it will create a more attractive region for the inhabitants of other regions, even countries as it will initiate a cycle for the inflowing brain drain in long term. Possible to state that only then they as regional actors can create a more efficient development for the region

The most common the three zones are identifying in terms of their future development is the improvements of the infrastructure. In order to implement the FEZ policy as good as possible, government has to take some risks and not expect the zone administration to handle everything. Most important future activities may be considered as to contact and be seen as more companies as possible.

6 Conclusion

In summary it should be emphasized that according to results of this research, although at different level in each investigated region, FEZs in Baltic States make the influence on the regional economic development, providing new economic activities, investments in infrastructure, attraction of advanced businesses as well as formation of new businesses creates an impact on the regional economic development.

Another important finding is that FEZs actively collaborate with the local public administration bodies in order to include them into the development process of the region. Local public administration bodies are very supportive to the activities of the zone as well as the national government. National government continuously invests in the infrastructure improvements and this makes zones function even more successfully. Thus, zones are actively collaborating with the other regional actors and national government; they are included to the development process by their board membership.

Analysis of results from free FEZs in Baltic States revealed that the FEZ can contribute (influence) significantly the processes of regional (economic) development just when it is enough developed (using fully its potential by allocating companies and having employees, FDIs, strategy and marketing policy). This was approved by successful examples of zones in Liepaja and Sillamäe (with fully working infrastructure, governmental support, national development strategy), and the beginner example of Šiauliai Free Economic Zone (with no appropriate infrastructure, no funding and lack of national and local government support).

As the empirical research was conducted in three FEZs, results can not be generalized for all FEZs in Baltic States. But in the future the sample could include all FEZs from Baltic States

and more representatives of them (not only from administration, but from business companies too). More over a comparative analysis of countries with similar economic and social development level is recommended.

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Povzetek:

Vpliv prostih gospodarskih con na regionalni razvoj v baltskih državah

Namen in izvirnost: Namen te raziskave je bil ugotoviti, kako proste gospodarske cone (v nadaljevanju PGC) vplivajo na proces regionalnega razvoja in podati nekaj dokazov iz baltskih držav (Litva, Latvija in Estonija). Vrednost raziskave je dosežena s tem, ko razkrijemo, s kakšnimi izzivi se proste gospodarske cone ukvarjajo pri sodelovanju v regionalnem razvoju. Ta raziskava predstavlja rezultate izvirnih empiričnih raziskav v baltskih državah.

Metoda: Namen študije je bil dosežen z uporabo pristopov teorije gospodarskega razvoja in teorije sistemov, da se razloži, kako proste gospodarske cone (v odnosih z drugimi regionalnimi akterji) vplivajo na regionalni gospodarski razvoj v baltskih državah. Podatki so bili zbrani z uporabo pojasnjevalnih kvalitativnih raziskav. Glavna metoda so bili polstrukturalni razgovori s predstavniki PGC v Litvi, Latviji in Estoniji. Za analizo raziskovalnih podatkov smo uporabili metodo kvalitativne vsebinske analize.

Rezultati: Rezultati te raziskave so pokazali, da PGC-ji dejavno sodelujejo z regionalnimi akterji gostiteljske regije, kot so organi javne uprave, nevladne organizacije, podjetja, univerze in Komisija EU v nekaterih regijah. Odkrilo se je, da PGC v baltskih državah, čeprav so na različnih ravneh v vsaki preiskani regiji, vplivajo na regionalni razvoj, zagotavljajo nove gospodarske dejavnosti, naložbe v infrastrukturo, privlačnost naprednih podjetij in oblikovanje novih podjetij, kar vpliva na regionalni razvoj.

Družba: Rezultati raziskav ponujajo nekaj idej za regionalne akterje (zainteresirane strani PGC-ov, organe javne uprave), kateri so glavni izzivi za PGC in kaj je treba storiti, da bi izkoristili njihov potencial za pridobivanje večje dodane vrednosti za regije.

Omejitve / nadaljnje raziskave: Ker je bila empirična raziskava izvedena v treh PGC-jih, rezultatov ni mogoče posplošiti za vse PGC-je v baltskih državah. V prihodnosti pa bi lahko vzorec vključeval vse PGC-je iz baltskih držav in več njihovih predstavnikov. V prihodnjih raziskavah se priporoča primerjalna analiza držav s podobno stopnjo gospodarskega in socialnega razvoja.

Ključne besede: proste gospodarske cone, regionalni razvoj, gospodarski razvoj, lokalna uprava, baltske države.

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