

## INVESTMENT ACTIVITY AND ITS POSTPONING IN THE CZECH REPUBLIC IN THE CRISIS PERIOD

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**Abstract.** This article should discuss corporate investment activity and its postponing in the Czech Republic in the crisis period. This topic has become again important how the second wave of a crisis is discussed nowadays. Reaction of business units during the first crisis period is demonstrated thanks to results of several surveys done by the Faculty of Business Administration in Prague in the Czech Republic. Each survey had sample of nearly 100 companies. Answers show change in investment mood and chosen reaction steps which should have helped companies in the crisis period. Reduction of investment activity was chosen as one of the most effective steps which companies did. On the other hand business units do not see that as a factor of negative impact on their competitive position. As the most negative signs companies saw short-term troubles such as decrease in demand which is typical for sales crisis or exchange rate volatility which was caused by global financial turbulences. It could be very dangerous if double-dip recession comes. It is forecasted that next cutting cost is coming.

**Keywords:** corporate investment activity, postponing or reducing investment, Czech Republic, economic crises, survey.

**Jel:** E22, G01, G11 and M20.

### 1. Introduction

This paper describes investment activity of Czech firms during the crisis. Results which are communicated were got as a part of surveys done by researchers of the Faculty of Business Administration in Prague. Targets of surveys were wider at the time of realization but now we have chosen only the question of corporate investment. This topic is actual because the second wave of crisis is foreseen.

Companies reduced or postponed investment in the past because it was necessary for their surviving on the market. Although the recovery of whole economy came in-

vestments are still low. It could be very dangerous if the second wave of the crisis comes. Because companies have not invested, modernized, thought about innovations and launching new products. The future will show which companies were prepared the best and it is a target for the next survey of the Faculty of Business Administration.

## **2. Investment**

Investment activities are important on the macroeconomic level as well as on the microeconomic level. Regular investment in company development or at least in recovery of assets and technologies is the only possibility how to ensure a sustainable company growth. It is same with the whole national economy.

In macroeconomic theory investment is the amount of assets which are not consumed but are to be used for future production of consumer goods or other capital goods (Synek, 2011). According to Scholleová (2009) in a narrower sense investment is an asset which is not directly consumed but used to creating additional assets, the company then sells on the market. Difficulty could be that each investment is connected at the beginning with one-off (short-term) cash outlay (Scholleová, 2008).

The investment decision is crucial for each company. Managers make decision whether to invest or not and they should consider when the right time for the investment is. Basic approaches how to measure effectiveness of investment are described in Hyršlová and Klečka (2008) or Jordan et al. (2011) or Anthes (2008). Managers decide on one hand between investment activities which do not have the same aim on the other hand between investment activities which should fulfil the same target. Investment decisions are very important because wrong choice can even cause bankruptcy. An interesting research in this field was done by Scholleová et al. (2010) which demonstrate that not all Czech companies use “sophisticated” methods for economic evaluation of investment. For some company’s net present value or payback period are only empty words. They decide more spontaneous and do not use evaluation investment process. It is necessary to emphasize that we cannot imagine any company which is able to exist for a long time without any investment. The importance of innovations which are off course at the beginning connected with the need of cash outlay is stressed in the articles Nečadová and Scholleová (2011a or 2011b). According to innovation cycles or product life cycle shorten the importance of coming with new ideas, improvements which are followed by investments is stronger and stronger. Further discussing of innovations and shortening of cycles can be found in Kislingerová et al. (2010b).

How the investment activity is important we can shown by classical production function which is described for example by Soukup et al. (2007). Classical production function is based on dependency between production quantity and the amount of

capital. The amount of capital is independent variable in this case and we can increase the amount by investment process. The dependent variable production quantity is on the axis y and the more capital the greater production quantity how the figure 1 shows us.

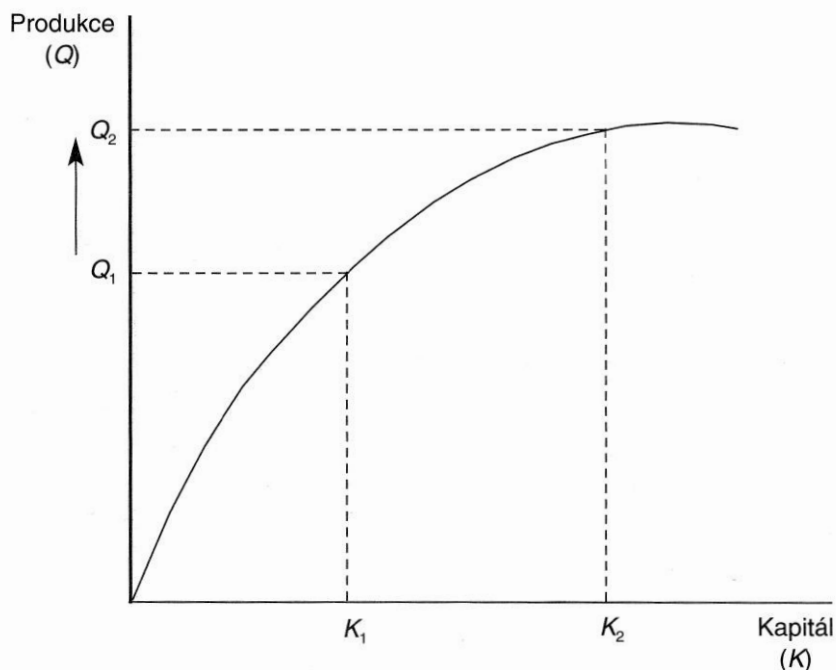


Fig. 1. Classical production function (Source: Soukup et al., 2007)

### 3. Postponing or reducing investment in crisis period

Many papers recent months were devoted to economic crisis. We do not want to discuss sources and beginnings of crisis itself but we want to look at the development of investment during the crisis period. The Czech Republic as well as other national economies has been affected by the crisis since 2008. For a laugh we can demonstrate example of the American billionaire Donald Trump. Carrell (2011) writes that Donald Trump has been forced to postpone his plan to create the "world's greatest" golf resort in Scotland, complete with five-star hotel and luxury villas, because of the global financial crisis.

Czech macroeconomic data are displayed in the table 1. All data except inflation are written in million CZK in current prices. Until 2008 Czech gross domestic product

rose. At the end of the year 2008 the crisis caused decrease in the production of machinery and connected industry branches but we have not seen deterioration in the whole economy if we look at the indicator GDP. Decrease in all indicators is typical for the year 2009 in the Czech Republic. Very sensitive part of GDP is investment which fell dramatically down in 2009, the recovery came in 2010 but it was not dramatic change. Gross investment in 2010 was insufficient. If we compare GDP 2008 and 2010 with gross investment 2008 and 2010 the difference is higher for gross investment which means that other components such as consumption, government expenditures or net export have to cover dramatic decrease in investment activities.

**Table 1.** Selected Czech macroeconomic data (Source: Makroekonomická predikce, 2011a and Makroekonomická predikce, 2011b)

	2007	2008	2009	2010
GDP (mil. CZK)	3 662 573	3 848 411	3 739 225	3 775 237
Gross investment (mil. CZK)	1 091 542	1 113 805	898 373	947 100
Gross fixed investment (mil. CZK)	989 608	1 031 182	927 465	922 952
Inventories (mil. CZK)	98 487	79 050	-32 957	20 110
Inflation (%)	2,8	6,3	1,0	1,5

### 3.1. Postponing or reducing investment in the crisis period in business units

Each crisis period requires appropriate behaviour of economic subjects. It does not matter if it is the government, households or businesses. The crisis period since 2008 was no exceptions. Basic recommendation according Synek and Kislingerová (2010) is cutting costs. Businesses should reduce costs which are not necessary in times of sales crisis. We can discuss costs such as extra benefits, education of employees, finding savings in manufacture process and of course investment. Always the recommendation list contains investments.

We have already seen the reaction of the whole Czech economy in the table 1 which shows us how gross fixed investment decreased dramatically since 2008. Researchers of the Faculty of Business Administration did two phases of a survey – one in March 2009 and the second in June 2009. In the first phase of survey 80 Czech companies were included and in the second phase 200 business units. The survey contained more than 30 questions but this article will represents only answers connected with investment activity. It is obvious that companies in the crisis period postponed or reduced investment.

Results say that conditions and investment mood at companies in March and June 2009 were comparable and almost same. Nearly 70% of business units in our survey

reduced their investment how figures 2 and 3 illustrate. On the other hand we have to admit that market conditions for investment were too disadvantageous. Experience of companies confirms low availability of bank loans etc. For further information we recommend surveys of researchers of the Faculty of Business Administration. Deeper analysis of credit lines in America is to found in the article Campello et al. (2011). Their sample consisted 1050 business units and they distinguished the difference between internal sources and credit lines during the economic crises.

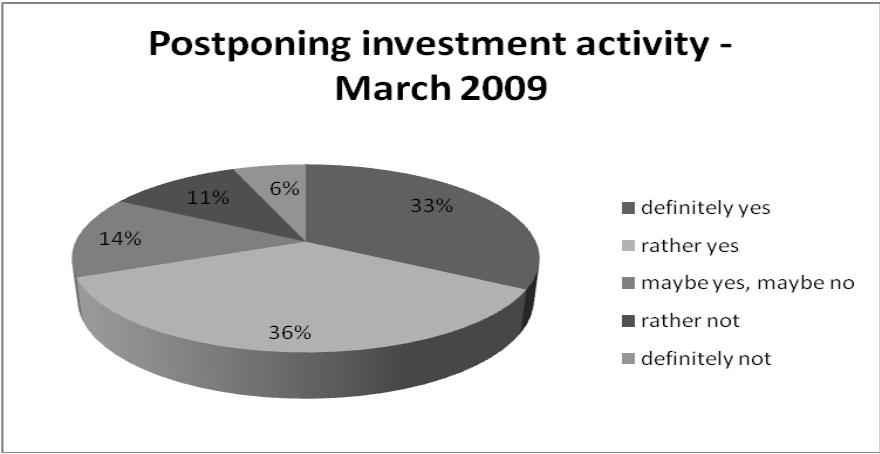


Fig. 2. Postponing or reducing investment in March 2009 (Source: Kislingerová,2009a)

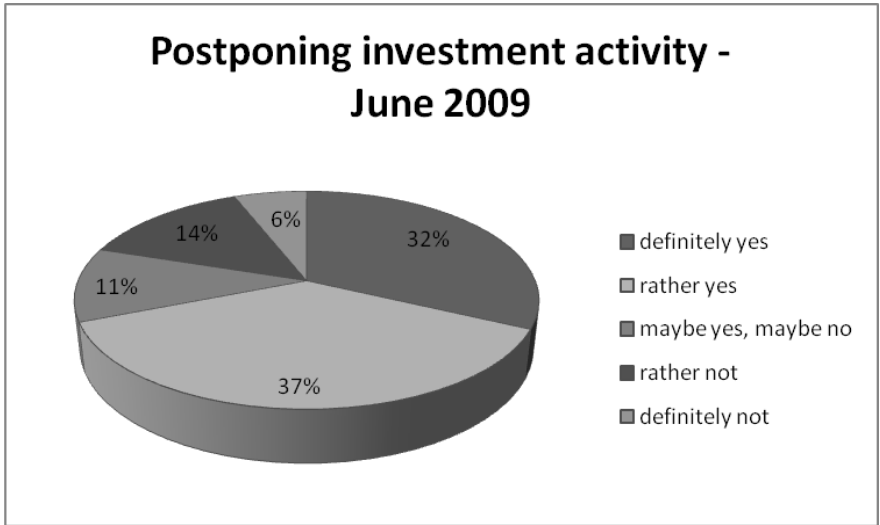


Fig. 3. Postponing or reducing investment in June 2009 (Source: Kislingerová, 2009b)

Nowadays we speak about post-crisis period and therefore it is possible to discuss which steps companies realized as a response to a market change during the crisis period. Business units usually did more things but with the time distance they can choose the most effective ways how to react. In November 2010 researchers of the Faculty of Business Administration realized its last survey in this research field. This survey contains questions which should provide evidence how companies overcame recent crisis. Financial executives of companies answered for example the question “Which steps for your business have proved very effective in last two years?”. They could choose more options or the most effective one. The list contained following steps – postponing implementation (reduction) of investments; gaining new key employees such as managers and experts; innovation (high order) of existing products or services; complete change of business strategy; strengthening the position of mergers, acquisitions or asset enters; change of marketing strategy, enlargement of company's product portfolio; narrowing of company's product portfolio; change in motivation of employees; change of organizational structure and others which should have been specified by a respondent. Results are contained in the figure 4.



**Fig. 4.** Very effective steps in last two years (Source: Kislingerová, 2010)

Firms due to crisis changed their performance and had to react. Detailed information could be found in the article Breňová and Nečadová (2010).

### **3.2. Other recommendations**

Reducing investment itself does not solve difficulties of companies. Kislingerová (2009c) finds a response to sales crisis in new products and services. At least mobilization of internal sources could help increase competition force of a company if they do not modernise. These expert suggestions of Kislingerová (2009c) are confirmed by companies themselves because 55% of business units in spring 2009 saw their opportunity in innovations of products or services. New products or services are general topic and it is not specified how to react or what to realize. Because we live in conditions which are constantly changing classical approaches are sometimes not enough efficient. Kislingerová et al. (2008) came with the book *Inovace nástrojů ekonomiky a managementu organizací*. They discussed new approaches and methods or tools in business economics and management. Although this work came before crisis many ideas could be used after modification also for changed conditions. Nowadays the most important thing for businesses is flexibility because it is necessary to react when the environment is changing. The study of Lee and Makhija (2008) is showing the advantage of real options investment of Korean firms. Real options are discussed in Kislingerová (2008) as well. But the study of Lee and Makhija (2008) contributes to the literature by showing that companies with real options investments in place have a greater ability and flexibility adapt their overall operations in line with unforeseen negative environmental change, in contrast to firms without such investments.

We would find many other specific approaches as an example we can use Pavelka (2011) who finds specific recommendations in the field of employees. His suggestions could be based on the activity of foreign employees who bring new “blood” in the company. Other way could be financial support programmes which use European funds for financing. Financial contribution of these programmes could be used as an additional source of investment financing (Čámská, 2011a). On the other hand government incentives in the Czech Republic could be supported with mobilization of public private partnership projects which have not already started on the national level how Čámská (2011b) writes. One possibility for Czech companies could be also incentives of foreign countries as Mevald (2011) points out.

### **4. Post crisis period**

As Kislingerová (2009c) wrote the end of economic crises is connected with new wave of investments. As we already know business units reduced dramatically their investments in the period of crises. Figure 4 introduced reducing investments on the first

place of the most effective steps. It does not mean that all businesses reduced investment activity as a world example we can introduce the motorcycle producer Honda. Mitra (2010) shows the strategy of Honda during the global financial crisis 2008-2009. Pawan Munjal, managing director of Honda, says that they did not postpone their investment plans during the slowdown and did not cut investments from their advertising, promotions or events. Honda has been updating their motorcycle model line-up, particularly with premium products. It means that we are back to innovations which have been already discussed. But table 1 does not support it that businesses are coming with innovations following by investments in 2010.

#### 4.1. Opinions of businesses

Postponing or reducing investment in the crisis period was seemed as one of the most effective steps by businesses. We are standing in front of a question if this behaviour is not dangerous, if company competitive position cannot be worsen. Although the crisis period is over nowadays recovery of investment is too mild. In November 2010 researchers of the Faculty of Business Administration realized their last survey in this research field. This survey contains questions which should provide evidence how companies overcame recent crisis. Financial executives of companies answered for example the question “Which of the following factors lead to negative change in competitive position of your company (or affect downside way your company competitive position in the market or prevent strengthen company position?)”. The list of factors included narrow product portfolio, low share of innovations; problems with operational financing; low availability of bank loans; decrease in investment; decrease in demand; insolvency customers and exchange rate volatility. Respondents could choose as many options as they wanted but they also calculated the importance of the factor by numbers (1 – very important, 2-4, 5 – less important). The results are shown in the table 2. As the most important factors which had negative impact on competitive position were chosen decrease in demand, exchange rate volatility and insolvency customers.

**Table 2.** Factors leading to negative change in competitive position (Source: Kislingerová, 2010a)

	1	2	3	4	5
Narrow product portfolio, low share of innovations	8	7	9	12	33
Problems with operational financing	6	5	9	13	26
Low availability of bank loans	6	4	12	11	26
Decrease in investment	4	12	18	8	19
Decrease in demand	31	15	9	2	6
Insolvency customers	8	18	16	10	9
Exchange rate volatility	11	15	13	7	15



Companies chose factors of the recent economic crisis. It seems that they are “blind” and do not forecast future because low share of innovations or decrease in investment are limitation for potential growth. Figure 5 illustrates unimportance of decrease in investment.

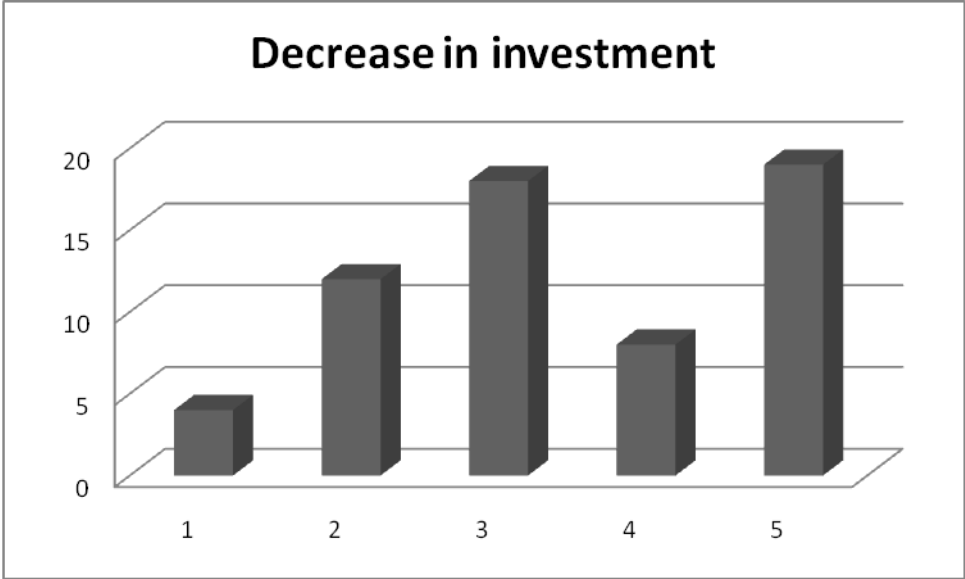


Fig. 5. Importance of decrease in investment for competitive position (Source: Kislingerová, 2010a)

**5. Conclusions**

Investment activity is crucial for each company because it is the only possibility how to ensure a sustainable company growth. The global crisis caused dramatic decrease in corporate investments. Significant recovery has not yet come. During the crisis period majority of companies decreased or postponed their investment how macroeconomic data as well as our surveys prove. The second wave of a crisis which is discussed nowadays could be a disaster for businesses which survived the first wave but their sources have been exhausted and innovations have been limited. The first response will be cutting costs because companies saw that as the most effective step in the past. New reducing of investment can have serious impact on competitive positions.

We as a part of the research team of the Faculty of Business Administration are planning next survey with targets if companies are prepared and how. It is obvious that problem of investment activity will be included and we will go on in this research.

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## INVESTICINĖ VEIKLA IR JOS ATIDĖJIMAS ČEKIJOS RESPUBLIKOJE KRIZĖS LAIKOTARPIU

**D. Čámská, D. Kula**

Santrauka

Šiame straipsnyje analizuojama įmonių investicinė veikla ir jos atidėjimas kriziniu laikotarpiu Čekijos Respublikoje. Ši tema vėl tapo aktuali, kadangi vis dažniau kalbama apie antrąją krizės bangą. Pirmosios finansų krizės rezultatai ir verslo reakcija į tai, jau buvo ištirta Verslo administravimo fakultete Prahoje, Čekijos Respublikoje. Kiekvieno tyrimo metu buvo tiriama beveik 100 įmonių. Atsakymai rodo investavimo nuotaikų pasikeitimus ir reakciją, kuria buvo siekiama padėti įmonėms krizės laikotarpiu. Investicinės veiklos sumažinimas buvo pasirinktas kaip vienas iš labiausiai efektyvių priemonių, kuriomis bendrovės siekė sumažinti krizės poveikį. Kita vertus, verslo vienetai nemato, kokią poveikį tai būtų turėję jų konkurencingumui, jeigu tos priemonės nebūtų taikomos. Tarp labiausiai negatyvių požymių, su kuriais bendrovės susidūrė, tai buvo tokie trumpalaikiai rūpesčiai, kaip, pavyzdžiui, paklausos sumažėjimas, kuris yra tipiškas atsakas į krizės pardavimų srityje arba valiutų kursų svyravimus, rezultatas. Šie pokyčiai gali būti labai pavojingi, jeigu recesija užkluptų antrą kartą, kas prognozuojama, gali įvykti.

**Reikšminiai žodžiai:** įmonių investavimas, investavimo atidėjimas arba sumažinimas, Čekijos Respublika, ekonominė krizė, tyrimas.

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