

THE POTENTIAL FOR REGIONAL DEVELOPMENT IN THE BALTIC STATES: CASE STUDY OF REGIONS WITH FREE ECONOMIC ZONES

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ABSTRACT

In modern society, a region has been considered not only a territory, but a system of different economic and social interconnected participants as well. Regional development as a form of systematic progress, including social, economic, environmental, cultural and other aspects, is becoming less dependent on public policy implemented on the European level and requires more national or regional efforts. Therefore, development is closely connected to the activity of all regional players (participants in the regional institutional system). Free Economic Zones (hereinafter FEZs) aim to function as the catalyst for economic activity in regions; however, some zones are more successful and create greater potential for regional development than others. The main problem of this article can be seen in the following question: how can regions which have FEZs enhance their potential in terms of regional development? The main aim of this paper is to reveal how regional development potential is enhanced in regions with FEZs in the Baltic states. It presents the results of empirical research which was undertaken in three regions with FEZs (Šiauliai in Lithuania, Liepāja in Latvia and Sillamäe in Estonia) by using scientific methods such as statistical data analysis and interviews with three representatives of the executive administration of the analysed FEZs. The research has revealed that, even given the favourable socio-economic environment (on both national and regional scales) for FEZs, all three FEZs in the Baltic states cannot guarantee the realisation of the full potential of FEZs. The analysis has disclosed that FEZs face certain challenges – infrastructural, attracting resources (investment and professionals), and even political ones - in their activities. All those challenges have to be dealt with, which can lead the FEZ to make a successful contribution to the growth of regional development potential.

KEY WORDS

Regional development, region, free economic zone, Baltic states.

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Introduction

While FEZs are discussed in the literature in the context of capitalist development from a macro-economic perspective, the socialist and post-socialist world con-

tinues to play an understated but significant role in their historical trajectory (Bach, 2019). As post-Soviet states, Estonia, Latvia and Lithuania have adopted FEZs

so as to boost economic activity and attract FDI within their borders.

The Baltic states (Lithuania, Latvia and Estonia), as members of the European Union (hereinafter the EU) since 1 May 2004, are facing challenges which relate to the achievement of regional development goals as one developing Baltic region. The Baltic states had to adapt to changes brought about by political reforms after gaining independence at the beginning of the 1990s, which led the states to look for ways to catch up with the rest of the world in order to strategise their economic development goals. As the Baltic states were trying to draw level with the EU and implement microeconomic stabilisation policies among the regions, they experienced success by creating the conditions for strong economic growth (a market economy was established, the standard of living improved and a high level of macroeconomic stability was attained) until the onset of the global financial crisis (Staehr, 2015: 274). During the global financial crisis, the Baltic states experienced an economic recession, which had "severe effects in this region as well as a direct impact on these societies, forcing them to rethink the fundamental aspects of their economic models and policies" (Pataccini et al., 2019: 403). The crisis produced inequality in social security and well-being and revealed other socio-economic challenges such as insufficiencies in the education system, a lack of institutional quality, production and export oriented towards low-tech goods, and the ageing population in the Baltic states (Aidukaite and Hort, 2019; Staehr, 2015). These challenges have to be dealt with nationally and internationally as well as regionally.

The modern economy requires a rapid developmental process in all regions; however, "regions thus have different preconditions to compete, innovate, and stimulate economic growth" (Grillitsch and

Sotarauta, 2018: 2). Regional development, as the integral system of aspects of community life such as social, economic, environmental, health care, technological, cultural and recreational aspects in a particular territory (Tamošiūnas, 2009), needs more effort from regional actors in order to achieve competitive advantage, although it is stated that different actors are not directly interconnected in terms of their key activities in the regional system (Mishenin et al., 2018). Even though governments invest via various programmes and instruments in specific regional entrepreneurial activities and promote the emergence of common linkages between different sectors (i.e. enterprises and universities) (Stejskal et al., 2016), the basic potential of regional development is created by regional actors, who contribute via the growth of their direct activities, the growth of differentiation of their interests as well as collaboration projects between different actors (Blažek and Hampl, 2009). Specific zones with economic incentives (including Free Economic Zones - hereinafter FEZs), along with industrial clusters, have become popular in order to create an attractive region for investors. Regional, local and national governments invest in the infrastructure of the region (connecting the FEZ with its surroundings to create a favorable environment in the FEZ) to attract potential businesses and investment in the zones. This helps the regions to promote economic activities and create greater potential for regional development.

An analysis of previous studies of FEZs in the Baltic states revealed that many studies were focused on the main regional policy issues and had presented the FEZs as tools for the use of policymakers (Akinci and Crittle, 2008; Farole, 2011; Farole and Akinci, 2011; Pakdeenurit et al., 2014; Song, 2015; Daru, 2016; Matushevskaya, 2018). Nevertheless, there are some stud-

ies which focus on the FEZs and sustainable development in Lithuanian regions (e.g. Clark, 2000; Auruškevičienė et al., 2007; Navickas et al., 2008; Navickas, 2008; Sakiene, 2011); the FEZs in Latvia and their peculiarities (Krodgers and Strazds, 2000; Rankevica, 2006; Ziedina and Pelse, 2017; Gulbis, 2018; Ziedina and Pelse, 2019), and the FEZs in Estonia and their developmental issues (Zoubir and Lhabitant, 2003; Skorobogatova, 2008). However, the research gap in terms of presenting the FEZs as a source of regional development in all of the three Baltic states, revealing regional features of FEZs, needed to be filled. Therefore, the scientific problem can be expressed in the form of the following question: How can regions with FEZs enhance their potential for regional development? The main aim of this paper is to reveal the use of the enhanced potential for regional development in regions with FEZs in the Baltic states. The objectives are: (1) to present the concept of the potential for regional development; (2) to present the situation as it pertains to regional development in regions with the FEZ in Baltic states; (3) to reveal the approach of FEZ representatives to their contribution to regional development; (4) to identify the main activities by which FEZs contribute to the potential for regional development.

This paper presents the results of empirical research implemented in three regions with FEZs (Šiauliai in Lithuania, Liepaja in Latvia and Sillamae in Estonia) in 2018-2020. The scientific methods used in the paper are scientific literature analysis, descriptive statistics analysis, semi-structured interviews and content analysis. The paper is structured as follows: the introduction, followed by the review of the literature, then the presentation of methods used in the empirical research, the research results and the discussion sections. The conclusions are presented last.

1. Literature review

1.1. The potential for regional development

The Theory of Development explains that development (its socio-economic approach) refers to long-term changes in systems of production and distribution of goods and services affecting human welfare (Copestake, 1999). The regions are essential dimensions of the developmental process, not just in the more advanced countries but also in the less developed parts of the world (Scott and Storper, 2003). The goals of regional development require the regions to look for new ways to create competitive advantage and to attract investors, in order to realise their potential.

Potential is considered to be a combination of factors, opportunities and resources, firstly in the socio-economic sphere, then the environmental, i.e. institutional, geographical and historical, which can be activated while achieving the particular development goals (Cheymetova, Nazmutdinova, 2015; Rivera, 2012). The economic potential of the region is "largely determined by its social and environmental components and reflects the level of the region's productive forces development, its ability to produce goods, to perform work and to provide services" (Poledníková, 2017: 31). Potential is determined by the opportunities for growth, innovation and accessibility, and is affected by local externalities such as those related to local human capital and local innovation; therefore, it can be strengthened by the advantages of co-location in the neighbourhoods of other firms (working in the FEZ) (Guastella and Timpano, 2016; Kubiniy et al., 2019). The components of said potential include management potential, the potential of trust, the educational, productive, natural, innovative, and human potential, and the potential of the form and the process

(Ďurková et al., 2012). Factors which affect the economic level of the regions (the economic potential of the regions) include the localisation of enterprises in the region and their frequency (business companies' localisation in the FEZ); the structure of the sector; economic stability (on the regional and national levels); the intensity of the intra-regional economic relations; the types of organisational forms; networking and clustering; the quantitative and qualitative characteristics of the population and its movement (the structure of the workforce and its level of professionalisation); the technical and social infrastructure in terms of complexity, quality and quantity; the available natural resources and their utilisation; and the direct and indirect impact of state economic policy and support (Ďurková et al., 2012; Poledníková, 2017).

There are several factors and indicators (economic, social or environmental) that can be used to assess the potential for regional development; however, the socio-economic features of the region play a crucial role in terms of future development. Moreover, institutional closeness and cohesion (which may be possible within FEZs) can contribute to the potential of regions.

1.2. Free Economic Zones and their role in regional development

New economic activities mean the creation of new jobs which have a significant impact on successful economic development. As a result, zones with economic advantages have become popular in most countries, as they are used in order to attract greater capacity in export or import, to create a better environment in terms of industrial activities, and also to attract and control Foreign Direct Investment (hereinafter FDI) to the region. Despite the fact that 19 different terms are used to label these

zones (such as Free Economic Zones, Special Economic Zones, Free Zones, etc.) (Long, 1986), zones which enjoy particular tax relief from public administration in order to attract FDI have been part of the international economy for a significant period of time. This research is focused on Free Economic Zones.

A Free Economic Zone (hereinafter FEZ) is defined as a regional industrial zone with special incentives set up to attract foreign investors (using a single system of management or administration, tools and policy), where imported materials undergo a certain degree of processing before being exported again (ILO, 2014; Zeng, 2016). The FEZs are often used to create a policy base for regional development purposes in the lagging behind regions to create a competitive and attractive economic activity zone. The main features of the FEZs are the encouragement of export-oriented industrial development; support for entering foreign markets through foreign capital gained and the contribution of capital and industry; the creation of employment opportunities; and the increase in the domestic demand for raw materials.

To embody a successful case, the FEZ has to pay systematic attention to certain factors (Table 1). A zone that is well controlled by a suitable administrative body and profit-focused operation would face minimal danger. Potential threats can emerge at different levels of intensity and quality that depend on the type of FEZ as well as the region in which the FEZ operates.

One of the many factors that affects the success of these zones is the development of a FEZ, a process which takes time and requires strategic planning on the part of both the public and private sectors. The success, or at least the results, can be seen only in the long term. From a policy-based perspective, this means that governments need to be patient and to provide consist-

ent support for the zone programmes over long periods of time, which is a peculiar challenge in countries whose political cycles are rather shorter (Farole and Akinci, 2011). From a business perspective, it is

also very important that the companies obtain a view of the results and the outcomes; the long-term period can be a deterrent to investors as well as policymakers.

Table 1. Advantages of FEZs which affect regional development

Factor	Effect on regional development
Positive influence on unemployment	As new investors are attracted to the zone, new employers are required.
Policy for lagging regions	New economic activities create a boost in the economy of the lagging regions which also accelerates the development of the region.
Higher level of FDI	One of the most important aims of the FEZs is to attract foreign investors as well as local investors, which brings about the inflow of foreign currency to the economy.
Clusters	Universities and businesses work together in order to improve the quality of the main product or labour. This creates an optimal atmosphere for regional development.
Encouraging innovation activities	Competition in the FEZ creates competitive businesses; in order to produce the highest quality products and to add value to the brand, businesses tend to invest more in innovation activities.
Regional/National added value – reputation	Many examples prove that, if implemented correctly, FEZs add value to the economies of regions and nations (one such example could be Shenzhen FEZ in China).
Spill-over effect	The businesses that operate within the FEZ are keen to have more advanced innovation strategies, and so spread this knowledge among other companies in the same industry by means of research and development activities.

Source: Own elaboration.

Another aspect worth considering is the business environment. The zones are entitled to create a desirable work environment for their workers. There are specific acts and regulations for the FEZs. Each country has its own FEZ regulations or laws. Those who work in the FEZ may not be covered by the national labour regulations, or the regulations may not be in the best interest of the workers, which can lead to conflicts in the zone between the workforce and the administrative body or businesses. Chaos in the relationship between workers and businesses leads to an undesirable zone that can eventually fail to attract local or foreign investors. Therefore, the FEZ has to pay attention to certain issues that may lead to failure (Table 2).

Another element is the infrastructural background in the region in which the FEZ is located. The production process takes place in the zone and products are transported to the domestic or international mar-

ket, so it is important that the region meets the infrastructural requirements to achieve success by means of having a more attractive zone. The strategic location of the zone, the international gateways and the road network, the railway network, bridges, the distance to the airports or ports, and sometimes also the distance to raw materials, the geopolitical location as well as the population, the supply of electricity, water or gas, the costs of production as well as the costs of labour are just some of the factors which affect the success of the FEZ.

Table 2. Disadvantages of FEZs which affect regional development

Factor	Effect on regional development
Results can only be seen in the long term	Attracting new businesses and creating new economic activities are a process, and to see the results of this process takes time, which can lead to impatience on the part of the national government.
Loss of national revenue	The national government offers incentives and special tax conditions in the FEZ, thus renouncing its right to taxes in part or in full.
Increased national expenditure	Governments are required to invest in the infrastructure to create an attractive zone for local or foreign investors. It takes time for the results to be visible, and the governments invest over the long term without being certain of the results.
Labour abuse	Many countries deal with immigrants in many different contexts. In terms of labour, immigrants with low expectations bring about economic outcomes such as a decline in income. The employment of low-income immigrants in the FEZ is an issue which has been discussed over time.
Pollution	The industrialisation and the inconsiderate usage of technology have been proven to have a negative impact on the environment, which is the reason why many countries have signed agreements to try to prevent environmental pollution. On the other hand, FEZs mostly encourage industrialisation. For that reason, it could be construed as a disadvantage.
Labour standards	Low labour costs can create low standards in the labour market in the FEZ, which in turn has a negative impact on workers as a consequence.
Loss of land	Agriculture is the leading sector of the economy in underdeveloped or developing countries. Providing land that could otherwise be used for agricultural activities is seen as a disadvantage in many countries.

Source: Own elaboration.

Alongside other components, the success of the FEZ depends on the success of the businesses' markets. The competitiveness of the business environment helps to grow the businesses and the market which is the focus of the zone, as it also provides a proper environment for innovation activities. The businesses learn the weaknesses and strengths and they become capable of identifying the potential threats which can affect them. The businesses that are capable of eliminating the potential threats help to ensure that the FEZ will achieve the established goals in the short term rather than the long term.

All the abovementioned factors (strategic planning, the business environment, the infrastructural background and market success) are closely connected to the opportunities and the resources needed for regional development and the realisation of its potential. The FEZs act differently according to the laws and regulations of the country; however, a FEZ acts as a system with its own actors and linkages

to the other systems. As the direct activity of the FEZ matches the objectives of regional economic development (attracting FDI, creating new employment opportunities, increasing the level and the quality of exports and the growth of local added value), outputs of the FEZ have an influence on the regional development process (socio-economic progress). The particular situation of the FEZs and their activity can be determined by the deeper analysis of environmental and internal factors in the Baltic states.

2. Methods

The paper presents results from both quantitative and qualitative research based on statistical data analysis and the semi-structured interviews with representatives of the FEZs in the Baltic states. There are numerous FEZs in various locations in the Baltic states (Lithuania has six FEZs, Latvia five, and Estonia three), so the authors determined a sample group on which research was focused. The au-

thors chose one FEZ from each state from which data was collected. The FEZs were selected according to their socioeconomic backgrounds. A purposive selection sampling strategy was chosen for the research. The main motive in selecting the FEZs from the Baltic states could be expressed as follows: the authors believe that, in order to address the research aim correctly, the FEZs should be selected from cities that are not capital cities (to avoid data and statistics which may be misleading), with areas of a strongly urban character which are also known as the business centres of the Baltic states also excluded. The authors chose FEZs in less developed regions (when compared to other regions in their home countries) to understand the importance of the FEZs in those regions and cities. Finally, three FEZs were selected for the sample: the Šiauliai Free Economic Zone (Šiauliai city, Šiauliai County, Lithuania), the Liepāja Special Economic Zone (Liepāja city, Kurzeme County, Latvia), and the Sillamäe Free Zone (Sillamäe city, Ida-Viru County, Estonia).

Quantitative research allows authors to focus on the economic perspective of the regions in Baltic states and the FEZs in these regions. According to Simon and Andrej (2006), the potential for regional development can be measured by using a set of indicators of the demographic structure, the socio-economic structure, the settlement structure, the countryside, the quality of life, the infrastructure, the use of the land and all the protected, degraded and endangered areas. However, such a detailed comparative analysis in the case of the selected FEZs and their regions could not be performed due to the lack of access to statistical data. To construct the quantitative part of the research, the authors collected accessible data pertaining to socio-economic indicators on two levels: data pertaining to the population, including the

share of youth (population aged 15-34), the net migration and the average gross salary were collected at the local level, while GDP per capita and the unemployment rate were calculated at the regional level. The main source of data was statistical data calculated by statistical institutions (Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020). The research focuses on the indicators in the period of 2005-2019 (a time span of 14 years), to reflect the situation in cities and regions where the FEZs are located. However, some data are not available. Each indicator is presented according to the availability of data. The analysis is also visualised via graphs.

Qualitative research was conducted in order to create an understanding of the underlying causes, conditions and problems of the FEZs in the Baltic states and their influence on regional development potential. The main reason for choosing the scientific method of semi-structured interviews was the optimality of the method for data collection from each representative who provided the latest data along with the individual experiences from each state and zone. For the qualitative research, the authors used guidelines of the semi-structured interview for the research instrument. The structure of the guidelines was carefully designed by the authors. It was based on the research problem and the need to find out about the real situation of FEZ activity in the Baltic states. The guidelines consisted of 25 questions oriented towards the establishment of the FEZs, their direct activity and influence on regional development, interaction with public administration bodies, challenges and the future of the FEZs; however, the paper presents the partial results of broader empirical research ("Free economic zones' impact on regional economic development: comparative analysis of FEZ's in Baltic states", conducted by

Büşra Demirelişçi and supervised by Vita Juknevičienė in 2016-2018). The interview sample consists of three interviewees (one from a FEZ in each analysed Baltic state). The interviewees were selected according to the following criteria: 1) The interviewee has to be part of an administrative body of the FEZ; 2) The interviewee has to have no less than six months' work experience in the field; 3) The interviewee has to have managerial experience in the FEZ. According to those criteria, three interviewees were selected (according to which the answers were coded as I_{LT} , I_{LV} and I_{EE}). The qualitative research was conducted from January to May 2018. The authors contacted interviewees from each selected zone via e-mail or telephone and provided important information about the research. Each interview was intended to last approximately 20-40 minutes. In some cases, the conversation was more in-depth and the interview took longer than intended. Due to the convenience of online channels and the distances between the countries, two interviews were organised via online video calls, while one was organised face-to-face. The interviews were recorded and the usage of the data collected by means of the qualitative research was limited to scientific purposes. To conduct a systematic analysis of the collected data, the authors used the categorisation method and the interpretation method in order to understand the findings.

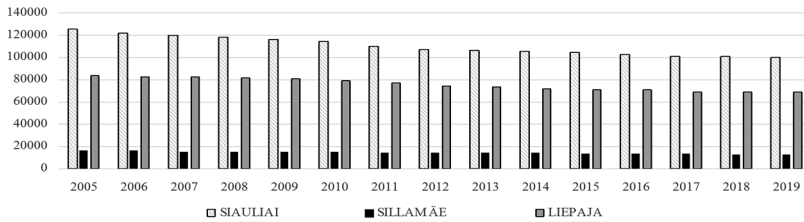
3. Research results

3.1. Socio-economic potential of the Baltic regions

In order to understand the potential for regional development, the socio-economic situation of regions where the FEZs function should be evaluated. To begin assessing problems inherent in regional development and to determine appropriate strategies and policies pertaining to them,

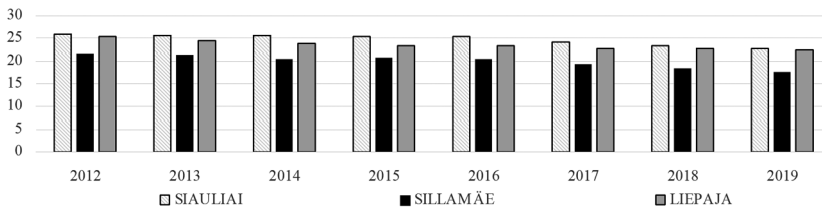
population trends and characteristics must be evaluated (Raitz et al., 2019). It is important to analyse their demographic evolution over the years so as to understand the potential of the cities which comprise the research sample (Figure 1). All three cities listed above were in a period of economic decline throughout the economic crisis. However, the population alone is not enough sufficient to analyse the social potential of the sample. In demographic terms, the ageing population is an important factor to touch upon while trying to understand the FEZs and their impact on the potential for regional development. The ageing population is not a desirable factor in terms of the overall attractiveness of FEZs. The cities must be able to offer potential investors and businesses a dynamic work force, due to the fact that the FEZs are often associated with innovative activities, which certainly puts the emphasis on youth (the 15-34 age group) (Figure 2). However, the share of youth in the population of the cities studied declined during the analysed period (not exceeding 25 percent in recent years in all regions) as a result of the ageing society and migration. As the statistics suggest, in cases in which the FEZ policy is implemented successfully, it is possible to increase the share of youth in the cities thanks to the creation of a favourable environment for attracting youth - good job opportunities for qualified professionals, higher wages, a network of social and family services, good infrastructure and options for cultural life. Such areas require investment in the region in the short term (international, national and regional); however, they will bring revenues into the region in the long term.

Figure 1. Population in the cities studied (2005-2019)



Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

Figure 2. The percentage share of youth (15-34 years old) in the population of the cities studied (2012-2019)

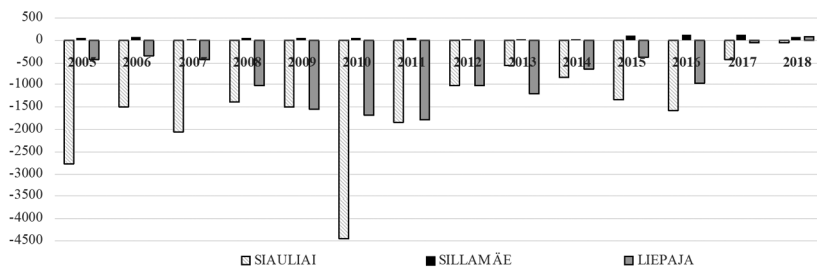


Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

The conventional understanding from neo-classical economics, as modelled by regional science, views net migration flows mainly as people responding to labour market “signals” (primarily better prospects for well-paid work) (Coombes, 2010). Based on the trajectory of the following graph (Figure 3), it is possible to state that none of the cities’ regional policies are enough to stimulate the local economy, even

though over the study period these three cities reached a neutral level in terms of net migration. The data strongly indicates that skilled workers have been leaving for other regions or countries in the hope of finding well-paid jobs. This means that the skilled labour pool has become narrower due to negative levels of net migration in all three cities, and so the FEZs are therefore less attractive.

Figure 3. Net migration in the cities studied (2005-2018), in units

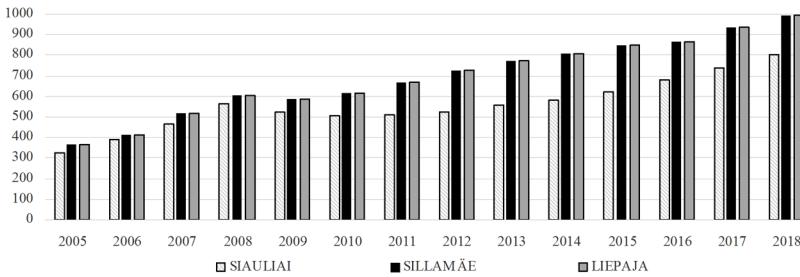


Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

Although income tax regulations in the three Baltic states differ, gross salaries are directly related to income expectation in the regions. The comparison is vital in order to understand the region and the cost of the workforce for any new business

that is planning to operate within the zone. While the three cities had similar levels of gross salaries for a time during 2005-2009, during the post-crisis period, Sillamäe and Liepāja continued to progress at a greater rate than Šiauliai (Figure 4).

Figure 4. The average gross salary in the cities studied, in EUR (2005-2018)



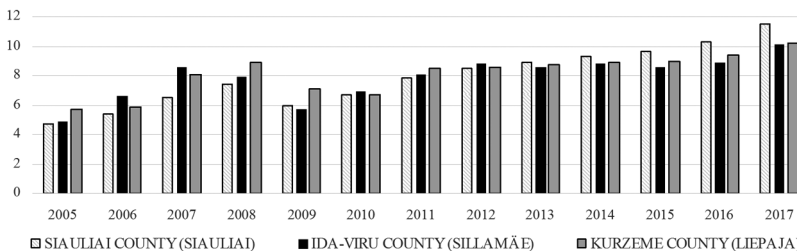
Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

At first glimpse, it might seem as if this is a disadvantage for Šiauliai. Nevertheless, once new businesses or investors look for a zone in which to invest, one of the first concerns is the cost of labour. In light of the data from the graph, the Šiauliai FEZ has great potential in terms of attracting investments when gross salaries are compared across all regions.

Due to the financial crisis during 2007-2008, the Baltic states were impacted on both macro- and microeconomic levels.

Although all three regions had been making positive progress in terms of GDP per capita, the crisis set this progress back significantly (Figure 5). Following the crisis, it took over four years for the three regions to catch up with the speed of development which had been visible during the pre-crisis period. It is possible to state that all three regions have been consistent when it comes to GDP per capita in the post-crisis period.

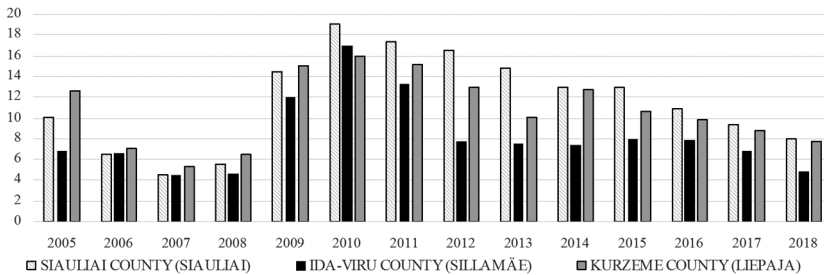
Figure 5. GDP per capita in regions, in thousands EUR (2005-2017)



Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

The financial crisis has affected the unemployment rate in the regions as well (Figure 6). Before the crisis, all three re-

gions had low unemployment rates, but the crisis brought about a peak in the unemployment rate, which rose to over 10 %.

Figure 6. Unemployment rate by regions, in percent (2005-2018)

Source: Own elaboration based on data from the Official Statistics Portal, 2020; CEIC, 2020; Centrālā statistikas pārvalde, 2020; Eesti Statistika, 2020.

The three regions only recently reduced the unemployment rate to pre-crisis levels. Nowadays, the three regions continue to battle with unemployment. Therefore, if implemented successfully, the regions studied may enjoy the best of both worlds by promoting and developing activities of the FEZs, at the same time providing new employment opportunities and economic activities through new investors and companies.

The socio-economic situation of the regions where the FEZ are located (including the cities) revealed that the financial crisis has significantly affected their potential; however, regional development trends are positive in all three regions, meaning that the possibility of utilising the strengths of regional development depends on FEZ activity and the contribution to socio-economic progress in the regions.

3.2. The situation of the FEZ in the Šiauliai region

The Šiauliai Free Economic Zone was established in 2015, which makes it the newest of the three in the research sample. In 2011 the parliament decided to establish five new FEZs, including one in Šiauliai. The establishment of the FEZ in Šiauliai was postponed until 2015, when the contract was signed, and funding of 2 million EUR was provided so as to clean

the land of pollution in order for the zone to operate properly. Although the contract was signed in 2015, requirements such as infrastructural investments took a long time, meaning the zone has not been fully active since.

Šiauliai is in an ideal location, i.e. with access to the international airport right next to the FEZ, and railways, seaports, international roads and an industrial park located nearby; however, infrastructural difficulties have had a negative effect on operations and on the attractiveness of the FEZ, and thus its potential. The Šiauliai FEZ is not yet operating to its full potential; at the end of 2019 when the research was conducted, three companies were already actively operating in the FEZ and negotiations with a big potential foreign investor were continuing. The main employer in the zone is the industrial sector, such as metals and plastics.

The Šiauliai FEZ has been working non-stop to be able to attract FDI and implement infrastructure for new businesses. Both national and international markets seem to be the target market, as the FEZ aspires to attract the attention of potential investors from the Scandinavian states, Denmark and Finland. Šiauliai has potential in terms of providing residents with employment in the upcoming years; nevertheless, the Šiauliai FEZ has not success-

fully attracted any significant FDI yet. Many potential investors were lost in the period of the establishment of the FEZ, because of the lack of infrastructure. The administrative body of the zone, a company from Lithuania, is constantly working on this and investing in marketing. The zone is expected to be promoted more actively at national and international events in order to establish contacts with prospective foreign investors.

The zone is a member of the Lithuanian Chamber of Commerce, which helps the zone to be more active at international and national conferences and events, as well as creating a web of contacts for its members that are good for the reputation of the zone. The I_{LT} states *“In short, this membership helps the zone to be seen and recognised”*. The other collaboration is between the zone and a non-profit organisation called “Invest in Lithuania” which promotes business opportunities and consulting services to potential investors.

The interview with I_{LT} has revealed that it is possible to specify the number of challenges when discussing the contribution of the FEZ to the Šiauliai region. The I_{LT} 's biggest concern is that the process of improving infrastructure is moving slower than expected. Although in 2018 the zone obtained its first investor, it took a long time for the municipality and the government to invest in the infrastructure of the zone.

The FEZ aspires to be on the same page with educational institutions in terms of creating a highly-skilled labour pool. The I_{LT} implies that *“when investors are interested in the zone, they ask for statistics about the demographics and the 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”*. Šiauliai city still has negative net migration and the number of students enrolled in higher educational institutions

within the region is lower each year, which creates a significant drawback for the FEZ in terms of being able to contribute to regional development, because new companies require a workforce which will mainly be provided from within the region.

The I_{LT} also mentioned that educational institutions and businesses, as well as the FEZ, may work on the needs of the region as a group, perhaps in the form of a cluster. The reason for this is stated by the I_{LT} as follows: *“If we can develop a well-educated labour force within the region which meets the needs of foreign investors, we will make the region more attractive to investors”*. Even if the circumstances are not as advanced as the other zones in the research sample, the I_{LT} is certain that the Šiauliai FEZ is already transforming into a very important regional player, thus contributing to regional development.

3.3. The situation of the SEZ in the Liepaja region

The Liepaja Special Economic Zone (hereinafter SEZ) is located within Latvian borders next to the Baltic Sea. The port of Liepaja is located within the borders of the zone. The zone was established in 1997, making it the oldest one in the sample group. The government worked particularly hard on the transformational process of the zone after Latvia gained independence along with the other Baltic states (because of the history of the city as a Soviet military city and major economic activity within the construction sector).

Liepaja provides infrastructural advantages such as railways, seaways, international roads as well as three airports located within a 200km radius. The main sectors in the zone are production, industry, logistics services, cargo storage and real estate development. The zone actively operates on the international market and its main investors are from the Scandinavian

states, Denmark, Finland, Russia, Belarus and other countries.

With 43 companies operating within the zone, Liepaja could be considered a success story. It provides approximately 2100 employment opportunities, and has become the second-largest region in terms of GDP contributions after the capital Riga. The Liepaja SEZ was successfully able to attract investors.

The Liepaja SEZ also has development projects which are focused on the region's infrastructural improvements. Since 2011-2012, the zone has worked on these projects for a period of one or two years. The scope of the projects span from street construction to railway and airport improvements. The zone is also focused on environmental issues and has an environmental plan for future activities, together with reports analysing the state of the environment on the territory of the Liepaja Special Economic Zone and the possible impact of the implementation of the planning document on the environment.

The I_{LV} particularly states that *the Liepaja Special Economic Zone has a positive impact on the region socially and economically*". The zone has partnered with the Latvian Chamber of Commerce and Industry, which is the biggest association of entrepreneurs in Latvia. The Liepaja SEZ participates in activities, seminars and events held by the Chamber of Commerce and Industry. Through these events and seminars, the zone is capable of promoting their economic incentives and attracting new businesses to the zone. The local administrative body also promotes the zone to possible investors, because of the regional benefits from new businesses.

The Liepaja SEZ has achieved the goals which were set during its establishment. The zone provides employment opportunities to many inhabitants of the region, and as the I_{LV} states: *"It has also helped the re-*

gion to become the second most productive in Latvia in terms of the production of entities" such as goods and services. For the zone to attract FDI and to improve regional economic development, the region must possess advanced facilities and should be perceived as promising in terms of its operation.

Being proud of the fact that the zone has been successful in terms of attracting FDI and new economic activities in Liepaja, the I_{LV} is certain that the zone has had a positive impact on regional development. However, the I_{LV} still emphasises the importance of investments and funding, the availability of which could further improve the impact of the zone on regional development.

3.4. The situation of the FZ in the Sillamäe region

The Sillamäe Free Zone (hereinafter FZ) is a port located next to the Baltic Sea in the very east of Estonia, close to the Russian border. The zone started operating in 1999 and was redesigned later in 2008. It was established to support cargo handling within the Port of Sillamäe. The area of the port is located within the FZ territory. The aim of the Sillamäe FZ is to support cargo deliveries by offering long-term storage without the need to pay any customs fees or taxes.

It has infrastructural advantages with connections via railways, seaways and highways as well as a connection to the Russian border. There are four terminals operated by different investors within the zone. The main activities are focused on imports and exports, and the main sector in terms of economic activities within the zone is transit cargo handling. The most frequent customers are local businesses, factories, traders and logistics companies that either rent warehouses from the zone or use other services provided by the zone.

The zone actively operates in the international market.

10 companies operate within the Sillamäe FZ and the total size of the labour force including port employees and employees of the companies operating therein is approximately 1000. More than half of the labour force is comprised of locals from Sillamäe town, and around 90 percent of employees are residents of the Ida-Viru region which in Sillamäe city is located. The zone is part of the cluster within Sillamäe. The cluster helps the zone to reach more of the labour force and to provide them with jobs. According to their own statistics, every seventh person in the region is employed by businesses within the cluster. The I_{EE} states that *“the customs personnel of the Sillamäe Free Zone are quite competent and well educated”*. This doubtless helps the zone to function smoothly in terms of bureaucracy, making it easier to provide a better service to the end client. The zone actively creates new employment opportunities for the local and regional labour market, and also attracts new investments, making it easier to improve the infrastructural facilities within the region.

New companies are attracted to the region, and the zone provides new export and import alternatives to local businesses. Furthermore, even when there are tax incentives, the companies are supposed to pay taxes to the government, which allows the government to draw up a budget based on higher public revenue. The I_{EE} states: *“I would say, yes, our goals have been achieved and the zone is developing even further. Our cargo grows year by year”*.

As revealed in the interview with the I_{EE}, it is clear that the strategic location of Sillamäe near the Russian border has ensured an initial boost in visibility to investors. However, the I_{EE} expressed concerns about Russian-Estonian relations and

mentioned that *“the improvement of the relationship could have a positive impact on regional development”*.

To facilitate new business development in the Sillamäe FZ, the zone has established the Business Incubation Centre, which provides companies with professional services, making it easier for the zone to assist new businesses within the launch period. The zone also aspires to maintain well-functioning relations with other regional development actors so as to support regional development.

4. Discussion

The quantitative analysis of social and economic indicators of the cities and the regions where the FEZ are located revealed the growing potential of the regions, even if they were highly affected by the financial crisis. Despite new threats in the global economy, the regions have shown positive socio-economic tendencies in recent years.

The Šiauliai FEZ (Lithuania) is facing a number of difficulties. Indeed, the Šiauliai region has the potential to become a more productive region, especially if the regional actors were able to cooperate and support the Šiauliai FEZ. If the zone were to advertise the region's relatively lower labour costs and emphasise the location-related characteristics, it could have a great chance of becoming an FDI-related production region. The case of the Šiauliai FEZ is a very clear example that infrastructure is most important when it comes to attracting investors. However, the region still requires collaboration between the FEZ and businesses, science and education institutions and local public administration bodies in order to better capitalise on the benefits that could be provided to the Šiauliai region.

The Liepāja SEZ (Latvia) still needs financial assistance from the government to

ensure successful operation by achieving the goal of attracting the workforce to the Liepaja region. The Liepaja SEZ could be seen as a success story, because it has played an important role in the process of transforming a small city, focused mainly on the military sector rather than on production, into the second-biggest production location in the country. The zone helps the region in the terms of employment opportunities and has constant connections with other regional actors. This makes the zone's contribution important to regional development and its potential.

The Sillamäe FZ (Estonia) successfully contributes to the development of the Sillamäe region, continuing to work on future projects as well as development plans. The improvement of political connections and relationships is hugely important in terms of attracting new economic activities. As a result of successful relationships with other regional actors, the FZ functions as a tool of regional development, generates employment opportunities and investments in regional infrastructure, offers an attractive area for new economic activities and new companies, creates alternatives for the imports and exports of local businesses, and helps to enhance the potential of regional development.

In spite of the favourable infrastructural environment and socio-economic potential of the FEZs (national and regional), all three zones in the Baltic states are faced with certain challenges in their activities when it comes to using their full potential and contributing to regional development. While setting up the FEZs in the regions, the respective governments aimed for these regions to become business hubs, which would attract more businesses and would contribute to the regional development processes. The zones in Liepaja and Sillamäe have seemingly implemented FEZ activity better than the zone in Šiauliai.

Liepaja and Sillamäe have successfully attracted FDI, provided their regions with new employment opportunities, focused on the attractiveness of the region and worked on the infrastructure over the period of their operation – while it seems that the Šiauliai FEZ is only just beginning a similar process.

Conclusions

The potential for regional development as a combination of various opportunities and resources, which can be activated while achieving particular development goals, requires contributions from the national government, international investment, as well as the involvement of all regional actors, including Free Economic Zones. The FEZs in the Baltic states contribute to regional development by means of their own resources (internal potential) and activities (regional potential), although at a different level of development in each region investigated. The FEZs offer new economic activities, attract investments and advanced businesses, and create better opportunities for new businesses to establish or base themselves in the region.

Theoretical and empirical research has revealed the main ways by which the FEZs can contribute to the (socio-economic) potential for regional development: attracting investment (local, regional, and national) in favourable conditions and based on modern networks of infrastructure; attracting FDI flows; creating jobs for highly competent staff and greater opportunities for the employment of residents; creating added value (especially focused on the high-tech industry); ensuring the contribution of FEZ representatives and active participation in the planning and implementation of regional development plans; launching trust-based collaboration with other regional actors (including cross-sectorial collaboration); and directing marketing initiatives

and maintaining constant communication with potential external investors. The paper has contributed to the development of scientific knowledge about the role of FEZs in regional development. It has identified ways for FEZs to contribute to and enhance the potential for regional development. However, the need to measure each identified tool or process which affects regional development would require further research.

As the empirical research was conducted in three FEZs, the results cannot be generalised for all FEZs in Baltic states, which constitutes a limitation of the research. Therefore, in future research, the sample should include all FEZs from the Baltic states to create the possibility for a scientific generalisation. Another limitation for this research appears to be the lack of the statistical data in the analysed regions on the local and regional levels. Therefore, the next direction for future research could be to measure the potential for regional development as a whole by using multicriteria methods (such as SAW, etc.) and to compare regions during a particular period. Such research would require developing a finite list of indicators and a precise selection of statistical data from all the sample regions – gathering them not only from public databases, but rather directly from official institutions. Data collection would enable researchers to prepare a deep comparative analysis of the potential for regional development.

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