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Tiivistelmä-Referat-Abstract <p>The paper focuses on unveiling the determinants affecting the volumes of FDI inflows to the transition countries. Particular attention is devoted to the macroeconomic and institutional factors in host economies, in terms of economic development, which serve as incentives for investors to enter a certain market. In particular, the paper concentrates on exploring regional characteristics of different 'blocks' across transition countries and finding out in which way these characteristics affect FDI inflows.</p> <p>The data for the research have been assembled from various publicly available sources – namely from World Bank World Development Indicators, World Bank World Governance Indicators, European Bank for Reconstruction and Development, Heritage Foundation, United Nations Conference on Trade and Development and United Nations Economics Commission for Europe. The research is undertaken in two steps. First, cluster analysis is applied, through which countries are grouped by their common features. The detailed description of each cluster is presented with the focus on the legal framework of the countries in the clusters. Based on the results of the cluster analysis, dummy variables representing clusters are included in the dataset. Panel regression analysis is further employed to all transition countries over the period from 1996 to 2007, except Montenegro, which is excluded due to the lack of data.</p> <p>Through the Cluster analysis, the four distinct groups are determined across the sample, mostly based on the institutional framework and market size of the countries. The first group represents countries with the strengthened legal framework, where transition process is at the advance stage. That is why it is chosen to be the reference group. The second one consists of the countries with the middle size markets and institutions that require certain improvements. Countries with quite weak institutions and small market size are included in the third cluster. This group is characterised by the relatively high GDP growth rates. The fourth group consists of the countries with the largest market size, which represents the main driving force for the foreign investments.</p> <p>Results of the regression analysis suggest that main determinants of Inward FDI in transition countries are market size presented by the GDP per capita and institutional variables, namely Rule of Law and Business Freedom. In addition, Openness of the Economy has shown to be significant determinant of Inward FDI. It has been proved that dummy variable for the third group is statistically significant, which means that belonging to a certain cluster has an impact on the FDI inflows. Significance of the dummy variable for the second group is not robust. Overall, results confirm the thesis hypothesis that determinants of FDI inflows differ across the clusters.</p>			
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