# INTERNATIONAL TRADE OF ROMANIA IN THE CONTEXT OF ITS LOW ECONOMIC POTENTIAL

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**Abstract:** *The study provides a view on Romanian economy in terms of its competitiveness and potential for sustaining an efficient foreign trade. After reviewing literature and the reports of prestigious institutions and bodies in the area, the author presents several elements providing an accurate image on current quantitative and qualitative parameters of Romanian foreign trade, the internal and foreign processes influencing it and its main trends. The theoretical, legislative and institutional background of the paper was developed earlier by the author in his monograph - "The legal and financial regime applicable to international foreign trade" published in 2008 by ArtPress Publishing House after Romania joined the European Union. In this study, however, the focus is placed on major changes that have occurred in Romania's foreign trade after it joined the European structures.*

**Keywords:** import; export; intra-communitarian trade; competitiveness; trade balance
**JEL Classification**: A10; F10; F49

## 1. Views on Competitiveness of National Economy

In any stage of society's evolution, the increase of society's competitiveness aims to provide economic sustainability, foreign trade development and the increase of the living standards of the population irrespective of current global challenges (Bostan, 2008). The most important challenges refer to „globalization of economy, opening of international markets, quick technological changes, challenges that should be transformed by Romanian economy into opportunities" (Government of Romania, 2007). A significant importance should be given to the analysis of competitiveness and the identification of solutions for problems faced by Romanian economy. Normally, competitiveness is analyzed based on factors, such as „technology, institutional framework, and the macroeconomic environment, leaving from the premise that a high standard of living cannot be maintained on long-term only by the accumulation of capital without technology (...)" (Government of Romania, 2007). The Global Competitiveness Report (2016-2017) (WEF, 2016) ranked Romania 62 in the top of 138 most competitive countries in the world, dropping 9 places compared to the previous year when it ranked 53, with 4,32 points (Lupitu, 2016).

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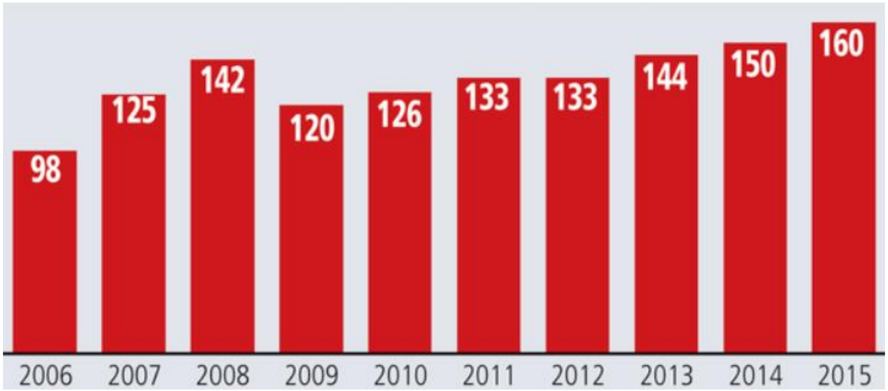
Switzerland is ranked the first [followed by the USA (5,70 points), the Netherlands (5.57 points), Germany (5.57 points), Sweden (5.53 points) and Great Britain (5.49 points)] and out of neighboring countries, Bulgaria ranks 50, Hungary – 68, Republic of Moldova– 100. The general score of Romania is 4.30 points (compared to 4.32 points last year) on a scale from one to seven. Romania scored low in indicators linked to innovation (position 93 out of 138), business sophistication (ranking 104 in the world) and to institutions (position 92 in the world) and infrastructure (position 88 in the world). It ranked higher in macroeconomic environment (position 28 in the world, the best position of Romania) and market size (position 42). Most difficulties are due to: access to funding, beaurocracy/ governmental inefficiency, taxation, less educated labor force and tax legislation (Soare, 2016).

As generally macroeconomic concerns have been focused on „promotion of competitiveness and employment, continuation of structural reform implementation, improvement of European funding, consolidation of public funding (...)", it helped Romania (also due to monetary policy and implemented structural reforms) make progress in reducing its macroeconomic imbalances, so it has to maintain its macroeconomic and financial stability (The Romanian Government, 2016). After years of economic crisis, the economic recovery amounted to annual increases of up to 1%, then the growth of GDP during 2013-2015 went back to its annual rate of 3.4%. The increase in 2015 of 3.8% was due to positive impact of domestic demand (in accordance with  the previously mentioned source, based on the growth of final spending, private spending grew by 6.1% under conditions of low inflation, interests rates reached a record low and real salary grew significantly; governmental spending increased by 17.6%. In nominal terms, after joining the EU, the GDP of Romania grew significantly (Anghel, 2016a) by 63% during 2006-2015 (Figure **1**).

**Figure 1 - Evolution of nominal GDP of Romania during 2006-2015 (bln. Euro)**




Source: Anghel, 2016a

However, the rate of poverty and social exclusion in Romania have been high in Romania compared to other states of the EU (2014) – 40.2% against 24.4% on the whole in the EU-28.

In terms of real convergence, assessed as gaps in GDP/per capita compared to European average, reflected as standard purchasing power, Romanian economy made some progress reaching around 55% of the EU28 average (the same parameter in 2010 was only 52%).

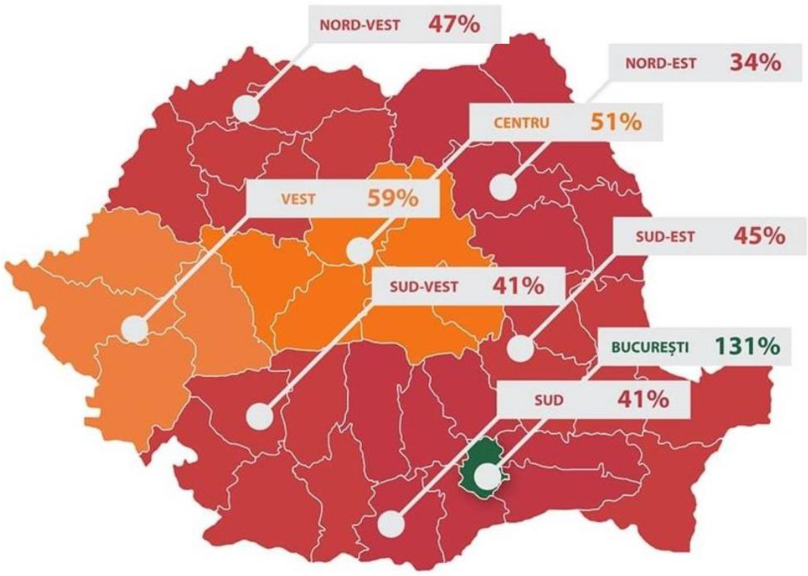
**Table 1 - Average GDP annual growth rate during 2010 – 2015 (%)**

| | UE28 | Romania |
|---|---|---|
| Real growth | 1,1 | 1,8 |
| Deflating | 1,8 | 3,7 |
| Nominal growth | 3,0 | 5,7 |
| GDP growth per capita in PPS (Purchasing power standard) | 2,4 | 5,0 |

Source: Government of Romania, 2016

As mentioned above, Romania still lags behind European competitors in terms of economic development; it is clearly seen in the level of GDP. On the other hand, the situation seems to be aggravated by the level of regional development in Romania (Figure **2**), GDP/per capita varies greatly (Infografic Monitorul Social, 2015). In accordance with the above mentioned source, Bucharest is above other European capitals that have lower GDP/per capita (relative to EU average): Athens (98%), Madrid (128%), Berlin (113%) or Budapest (108%).

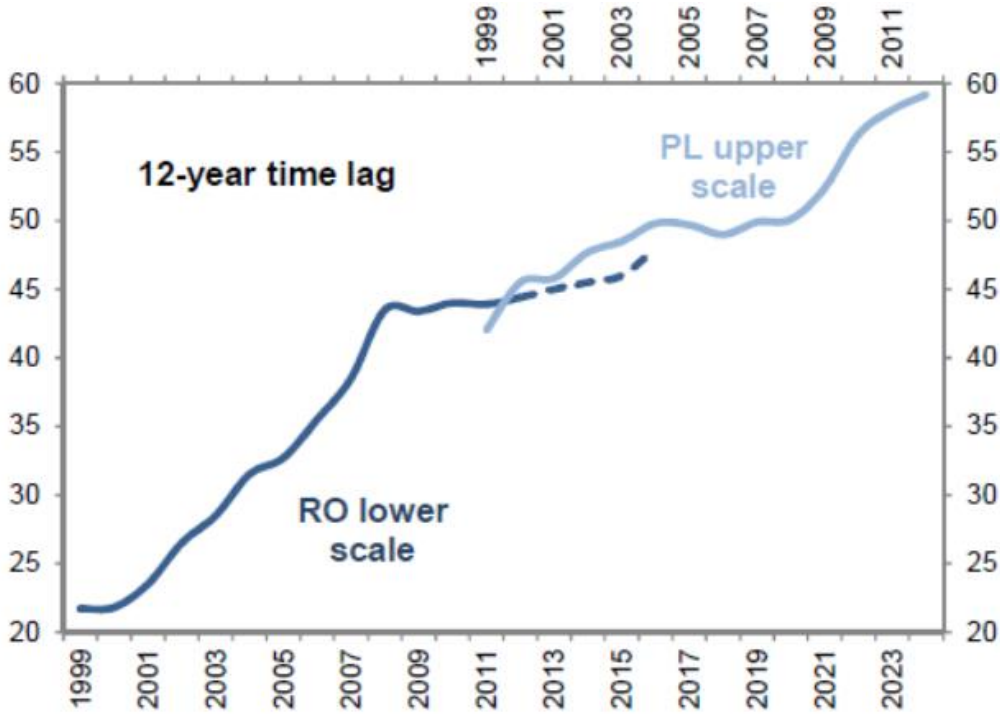
**Figure 2 - GDP/per capita by regions of development relative to EU average (2014)**




Source: Infografic Monitorul Social, 2015

The development of labor productivity – GDP to PPP (purchasing power parity)/ the employed - has grown but the productivity of Romanian economy is less than half of the average productivity in the EU. In particular, labor productivity in Romania is 45% against the European average; we are 12 years behind Poland (Figure **3**). Precisely, we grew from a productivity of 22% compared to European average at the beginning of 2000 to 45% – the level Poland had 12-13 years ago (ERSTE, 2015). Meanwhile, the Polish economy reached labor productivity of around 60% compared to European average.

**Figure 3 - Labor productivity in Romania and Poland compared to European average (EU 100%)**

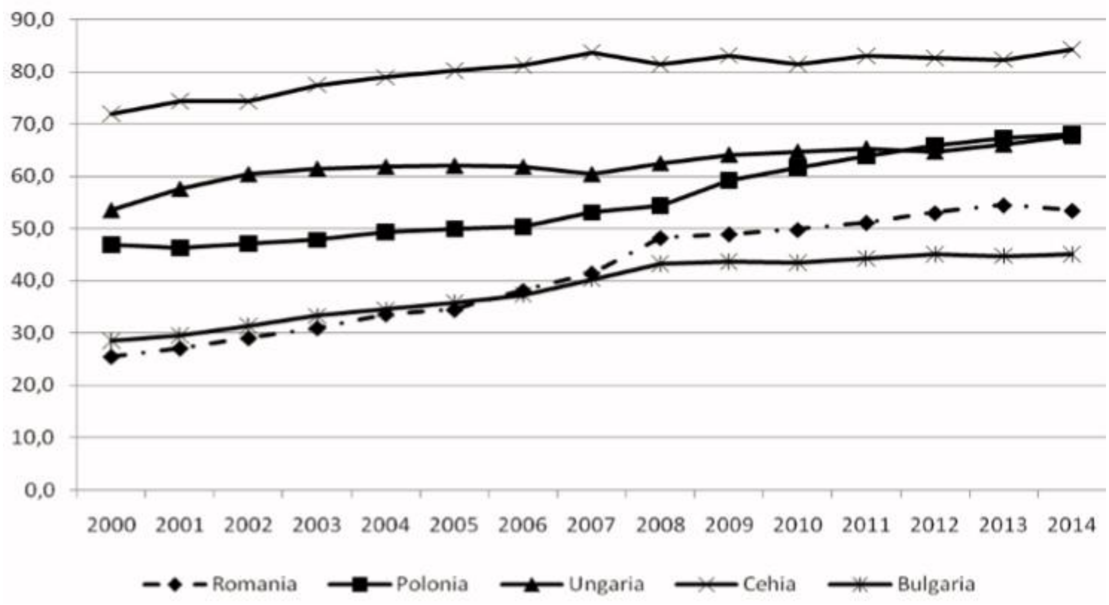



Source: ERSTE, 2015

Similarly, the relative gap between Romania and Hungary was 19%in 2007 (Ghizdeanu, 2015); however, it dropped to 14% in 2014 (Figure 4).

**Figure 4 - GDP per capita in new member states**

- % compared to EU28 -




Source: Ghizdeanu, 2015

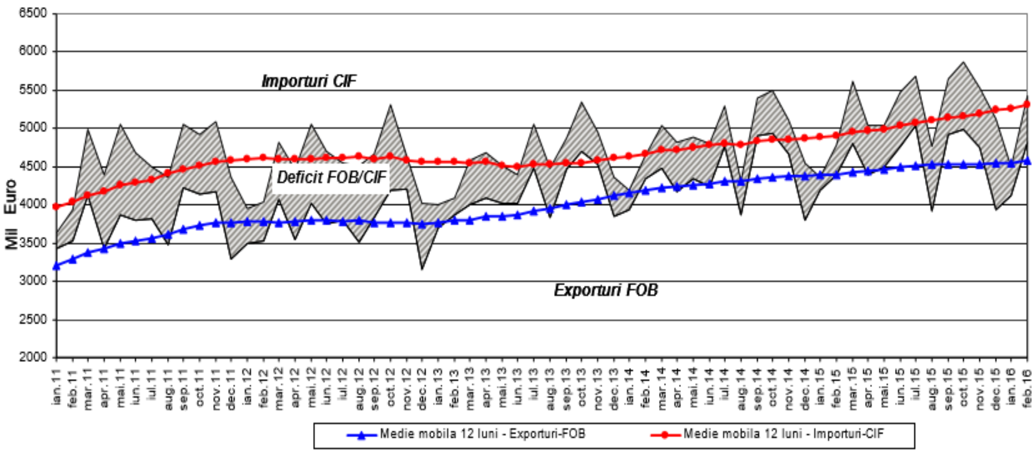
Although, we made references to positive developments, as the earlier mentioned author states „Romania is still below 60% of the EU average, similar only to Bulgaria and Croatia, even if Romania has recorded after 2007 the highest growth rate of GDP to PPS" (Ghizdeanu, 2015).

However, we should note that in accordance with economic development set out in the Convergence Program for 2016-2019 „the real convergence of Romania may get to around 65% in 2018 and the GDP per capita to PPS may reach the level of 70% of the European average by year 2020" (The Romanian Government, 2016); this is the reason why we should observe that „Romania has been improving its real convergence expressed as GDP/capita to PPS even if in a more moderate pace. Currently, the gap is approaching 55% of the European average. Considering that the states which have recently adopted the Euro had their GDP expressed in PPS of over 60% of the European average, it results that the process of real convergence should be accelerated so that the objective to adopt euro be realistic" (Ghizdeanu, 2015). It should be noted that most productivity (added value growth) directly depends not only on technological development but also on increasing product quality, marketing and applying the results of research.

## 2. Current quantitative and qualitative parameters of Romanian Foreign Trade.

As it has been shown earlier, the economic potential of Romania is medium from several perspectives, we will dedicate next section to foreign trade and its evolution. Its traditional forms include (Popa, 1997) **import of goods** (a set of trade operations used to purchase goods from third countries that are brought into the domestic space for productive/non-productive consumption; obviously, services purchased by a specific country from other countries in the area of transportation, insurance, financing, tourism or licensing) and **export of goods** (also trade operations by which a part of produced or processed goods in one country are sold in other countries; services included). Foreign trade development is based on the production of material goods and state's active policy in encouraging, liberalizing and protecting foreign trade (Bostan, 2008, 2016). Long-term development shows that after 1990 foreign trade has had a constant positive development of the following elements: on-going liberalization of trade, especially by reducing customs duties; strengthening regional trade groupings; investment growth in developing countries; revival of foreign trade in Eastern Europe and Russia. On the other hand, economic forecasts show that the tendency for foreign trade growth will continue in the next years in the context of acceleration of global trade integration and the growth of global foreign trade two-fold compared to global economy. It is well-known (Bostan, 2008), *the export and investments* have been in the past years the catalyzes of economic growth. The export of Romania has gone through a positive evolution since 2000 but it has been mainly based on products with low added value. The highest volume of export was recorded in textile industry dominated by the lohn system, followed by metallurgy producing low-alloy steel. Lately, the export of low technology and low resources products decreased, while the export of medium-technology grew significantly. The chart below presents an accurate image on the evolution of exports, imports and trade balance during January 2011-february 2016 (INSSE, 2016) (Figure 5).

**Figure 5 - Exports, imports and trade balance (2011 – 2016/Febr.)**




Source: INSSE, 2016

It may be stated that Romanian exported products are competitive due to price, but not innovation. *Low cost of labor force* is the main dominant source of competitive advantage, an advantage that is slowly decreasing and therefore shaping as the main direction for encouraging internal research and innovation. It is estimated that these will have a positive impact on the reduction of technology and equipment imports and the increase of gross added value for domestic and export products. In 2015 (BNR, 2016), the degree of coverage of imports through exports has dropped by 1.8% reaching 86.3 %. The same document states that „export of goods amounted to 49.121 million Euros, a rise of 4.9% compared to previous year (...). Compared to 2014, the structure of exports by groups of goods shows the increasing share in the export of cars, devices, equipment and vehicles (by 2.7% up to 45.3 %), agri-food products (by 0.2% up to 12%) and other goods (by 0.3% up to 8.2%). The import of goods amounted to 56.897 million Euros, an increase of 7.1% compared to 2014, by 3.755 million Euros”. In what regards *the imports,* their structure by structure of goods „reflects the increasing share in imports of cars, devices, equipment and vehicles (by 1.1% up to 37.8 %), agri-food products (by1% up to 10.6%), textiles, clothing, footwear (by 0.2% up to 5.9%) and other products (by 0.5% up to 6.%)”. The structure of exports by groups of products includes (INSSE, 2016): cars and transport equipment – 48.0%; other manufactured products - 33.2%. The above mentioned show that technology in Romania is mostly imported, local innovation is hard to promote and transfer to local businesses. The high of imports in the past years created negative trade balances („trade deficit for the first eight months in 2016 amounted to 6 133.8 million Euros, approximately 28% higher than in the same period last year; coverage of imports carried out on the basis of exports dropped below 90%, this threshold has been exceeded every year during 2013 – 2015” (Pana, 2016) mainly due to import of cars and industrial equipment aimed to upgrade industrial capacities and to purchase from abroad chemical products, fuel and food. In 2015, the deficit of current account of balance of payments amounted to 1828 million Euros (Table **2**), representing 1.1% of GDP compared to 0.5% of GDP in the previous year.

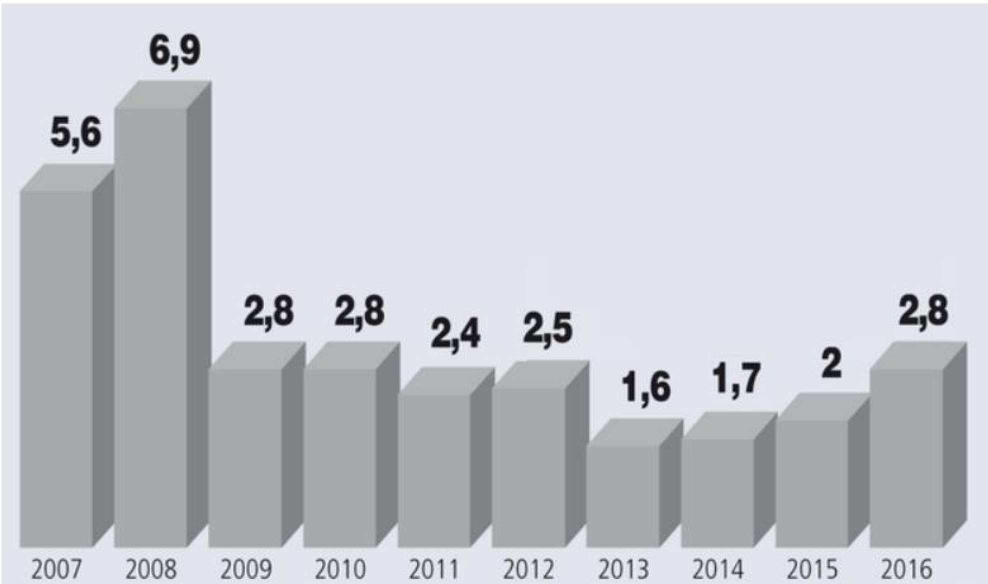
**Table 2 - Current account**

| | milioane euro | |
|---|---|---|
| | 2014 | 2015 |
| Bunuri | -6 335 | -7 776 |
| – export (FOB) | 46 807 | 49 121 |
| – import (FOB) | 53 142 | 56 897 |
| Servicii, net | 5 867 | 6 936 |
| Venituri primare, net | -1 904 | -3 806 |
| Venituri secundare, net | 1 686 | 2 818 |
| Sold cont curent | -686 | -1 828 |

Source: BNR, 2016.

The chart below shows the evolution by year of trade deficit (2007-2015) (Anghel, 2016b – since year 2016, only data for the first four months were considered) (Figure 6).

**Figure 6 - Evolution of trade deficit (2007-2015) (since 2016, only data for the first four months were considered)**




Source: Anghel, 2016b

### 3. Internal and International Events that Influenced Foreign Trade of Romania

International trade is highly influenced by two events: internal and external events. Under their influence, Romania was characterized by exports, such as (main products) (Oprea, 2016): cars and related products, wire, cables; oil products; chairs, paintings, panels, consoles, control panels/electricity distribution panels; pneumatic tires; telephones; wheat and corn; pumps (...); compressors, ventilators, aspirating hoods; tobacco; drugs, etc. Also, main imported products include, on first position, car parts and accessories, then, crude oil, drugs, telephones, cars, wires, cables and other insulated electrical conductors; oil products, etc.

Concerning internal documents, we will refer to *trade regulatory framework.* Considering the context of our country after 1989, the most important undertaking that had to be made was the development of a new trade legislative framework which was generally mad, the most significant measure, to begin with, was the adoption of Law 31/1990 on the set-up and operation of companies that ensured the legal framework for the set-up of new entities: public limited liability companies, limited liability companies, limited partnerships, partnerships limited by shares, family associations. Until the accession to the European Union, the main package of specific regulations allowing the continuation of foreign trade and providing conditions needed to attract foreign investors had already been implemented, as well as the main mechanisms for the operation of Stock Exchange and Secondary Market Stock Exchange (RASDAQ). Then, foreign currency regulations had been changed and improved by successive amendments so that today there are adequate mechanisms supporting in good conditions Romania's foreign trade.

*Besides regulatory framework, we should also consider the framework regulating the tax system.* It also had a contradictory and sinuous evolution with almost 100 types of different taxes that companies have to pay but the introduction of 16% flat income tax in 2005 resulted in significant positive changes. In terms of internal events, *foreign investments* also had a significant impact on foreign trade of Romania. In 2015, the foreign direct investment net inflow (ISD) reached 3 461 million Euros (BNR and INSSE, 2015), out of which (i) 3 595 million Euros own equity (ownership interests in FDI of enterprises amounting to 3 085 billion Euros and reinvested earnings in FDI of enterprises worth 510 million Euros) and (ii) 134 million Euros net credit from foreign investors. The final balance of ISD at the end of the same year amounted to 64 433 million Euros, out of which: (i) 45 098 million Euros own equity, including reinvested profit (70,0%) and (ii) 19 335 million Euros net credit from foreign investors (30.0%). The need for foreign investments is obvious as the country cannot ensure its development only using its internal resources. On the other hand, it may provide, besides the injection of capital, transfer of technology, improvement of management strategy and the revigoration of export production.

*Global division of labor* is among foreign events influencing Romania's foreign trade; it is the process of international specialization in the production of national economies developed over time and which sets the basis for their relations (Clipa, 1998). It indicates the place of different economies in global economy and represents the material foundation for international economic flows. In the post-war period, the formation and deepening of the global division of labor has been significantly influenced by at least two events: the collapse of the colonial rule which led to the creation of more than new states, as well as the modern scientific and technical revolution. The latter is the most driving factor for global economy and foreign trade with all its aspects (Suta, 2000). Romania, as the member of international community is no exception to what has been mentioned above, it has been actively engaged in international exchange of material and spiritual values benefitting from the advantages provided by global division of labor. Also, we cannot elude the existence of *globalization* manifested by (Gilpin, 2004): production and technology internationalization; stock exchange globalization, internationalization of services markets and integration of global financial markets. *International and regional economic integration* is extremely important for our discussion as it involves the absence of discrimination and its progressive elimination in the relations among countries, thus contributing to the stability and economic efficiency of these relations. In accordance with the previously cited author, the stages and types of economic integration include the following: preferential trade agreement, free trade area, customs union and the economic union. The main effect of economic integration is that it may lead to trade development or deflection, in other words, integration creates both the element of trade liberalization, at least between neighboring countries, and also leads to a discriminatory effect.

*Integration of Romania to the European Union.* Our country started its relations with the European Union in 1980, it was the first agreement signed with a country in the East (Diaconescu, 2003). The next trade and cooperation agreement was signed in 1991 and the negotiations for signing the Association Agreement with the European Union began in 1992, the agreement signed in the same year together with Bulgaria, the Czech Republic, Hungary and Poland.

Based on the Strategy aimed to prepare the accession of the associated countries in Central and Eastern Europe and to implement measures stipulated in the White Book of the European Commission on the support provided for these countries in the process of integration, Romania implemented its integration into European structures through four means: the implementation of the

Association Agreement and the national programs aimed to harmonize the internal and communitarian development and the creation of institutional structures facilitating access to the internal market of the European Union, participation in the structured dialogue with the institutions of the European Union, management of the integration process. All 31 chapters, which Romania had undertaken to open, were finalized during 2004 and it became the member of the European Union on January 1, 2007 after signing the Accession Treaty on April 25, 2005. Obviously, various trade policies had been operating during this period that included all legal, administrative, tax, budgetary, financial, banking, foreign currency regulations adopted by the state promoting or limiting foreign trade or protecting national economy against foreign competition (Rainelli, 2004; Miron, 2003). These regulations developed in three directions: promotion of foreign economic relations, (export boosting), national economy protection against foreign competition (control of exports) and achievement of a dynamic equilibrium between trade and payment balance together with strengthening the state's foreign currency reserve. Trade policies under GATT and OMC are put into practice using instruments and measures of tariff (customs duties), non-tariff and promotional nature. Certainly, we may also mention here budgetary measures for stimulating exports (related to increasing the competitiveness of exports and increasing the degree of attractiveness for producers and exporters as to boost the delivery of goods to be exported) and financial and banking measures related to: export credits and provision of insurance and guarantee for export credits.

The main changes that appeared in foreign trade of Romania after its accession to the European Union refer to the following (Oprea, 2016): (1) The countries to which Romania has exported/imported intensely compared to the period before 2006, prior to its entry to the European Union are the member states of the European Union. Therefore, „Intra-communitarian trade (with 27 partner member states of the EU) increased its share amounting to 73.7% in export and 77.2% in import in 2015. In 2015, the first 10 partner countries account for 64.1% out of total value of exports, highest share belonging to Germany, Italy, France, Hungary, the United Kingdom, Turkey, Bulgaria, Spain, Poland and the Netherlands."; (**2**) The exports of Romania to Russia also decreased reaching „the highest level in 2014 (almost 1.5 billion Euros) and since 2015, the exports have decreased by 31.7% compared to 2014". In terms of imports from the Russian Federation, these amounted in the same year to „2.0 billion Euros, a decrease of 12.6% compared to 2014. The highest share of imports from the Russian Federation were in crude oil (50.7%), followed by oil products (25.6%), with 2.4% in natural gas out of total imports with the Russian Federation 2015. Romania's imports of crude oil from the Russian Federation amounted to 34.8% in 2014 and 43.8% in 2015".

## Conclusions

The literature review enabled us discover that currently two phenomena lie at the basis of the growing integration of global economy: the technological one, due to explosive development of the speed and efficiency of communications and international transportation along with their cost reduction, and the economic phenomenon, represented by the reduction and elimination of national barriers to international flows of goods, services, technology and capital. Although Romania has made progress lately, it is still behind its main international/European competitors in terms of economic development. The Romanian export has had a positive development since 2000, although it has been mainly focused on products with low added value. It may be stated that often exported Romanian products were competitive in terms of their price and not innovation. Specific improvements have been noticed after the year 2007 when Romania joined the European Union. Although the progress has been limited, there may be noticed a positive tendency in the improvement of foreign trade structure. We believe that with a more vigorous economic growth, Romanian products will become more competitive abroad. The more acceptable structure of imports and exports may provide positive results. But, a real growth in the competitiveness of Romanian economy is needed, as well as the development of a secure and dynamic e-business environment, so that SMEs may benefit from multiple opportunities, as it is well-acknowledged that e-business depends on progress that leads to cost reduction and access to internal and foreign markets.

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