

# THE MAIN FEATURES OF THE FLOWS OF FOREIGN DIRECT INVESTMENTS IN ROMANIA

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**Abstract:** *A distinctive characteristic of The Global Economy over the last few decades has been the rising rate and the impressive increase in the Foreign Direct Investment (FDI globally). Due to the potential role that foreign direct investments may play in accelerating the growth rate and re-shaping the economy, many developing countries are seeking such types of investments that can multiply the efforts being made towards the growth of their economy. The purpose of this research is to analyze the flows of foreign direct investments in Romania between 2003 and 2010. The results of the research highlight the negative balance between the trade balance and the enterprises with FDI in 2007-2010, due to the financial crisis, to the fragile budget balance, due to the low competitiveness of the imports, the low quality of the Romanian products and the macroeconomic risk determined by the rate of inflation, the unemployment and the instability in the exchange rate.*

**Keywords:** foreign direct investment, growth economy, development

**JEL Classification:** E22, F14, F43

## INTRODUCTION

Occurring in the world economy since the period of the great geographical discoveries, the direct foreign investments have been perceived, in the last few decades, as a veritable explosion in the international transactions, which has generated a surprising number of studies and analyses. The investments, with the participation of the foreign capital, are controversial, although, it is generally recognized that they have a certain preponderance of positive functions, especially at the level of the macro systems (the national economy, the geographical areas, etc.).

In Romania FDI contributes to the growth formation of the capital, in particular in the private sector and, at the same time, they have a beneficial role in putting into value the qualified manpower through the creation of new jobs. FDI constitute leverages for consolidation of international ties and the economic interdependence. This creates competitive advantages given by the volume of the exports on the world market, as well as the ability to generate drive effects on the adjacent industries (Anghel, 2002).

## 1. THE CHARACTERISTICS OF FDI

Foreign Direct Investments are defined as the Long-term investments made by one enterprise in another enterprise which functions within another national economy (OECD, 2008). Also, according to UNCTAD (1999), FDI is defined as a long-term investment by a dominant company in its country of origin, in a subsidiary, a controlled enterprise or sector of an enterprise in a foreign host country. It includes the equipment, the land used and/or investment capital (a percentage greater than 10% of the total holdings of a company), capital for re-investment (which may come from the retained-undistributed profits of a controlled company or from inter-company loaning), and debit transactions (long-term loaning or other loans) between the enterprise and its subsidiaries.

Kirkilis, Nikolopoulos and Pantelidis (2009) show that multinational companies under foreign direct investment are now the most dynamic factor in economic globalization. The internationalization of the production process, with the establishment of subsidiaries of the same parent company in different countries and the cross-border transport of goods and inputs, deepens the integration of the global market. At the same time, these transfers of goods and inputs are carried out within the global network of the parent company. Thus, they replace the markets and their distributional role with the internal system of management, decision-making and resource allocation of the multinationals.

Foreign Direct Investments have become one of the most important factors in modern-day economies, since they first began to appear in a global context at the beginning of the 20<sup>th</sup> century. It is interwoven with the existence of Multinational Companies, while, historically the increase in the number of the latter, worldwide, coincides with the general establishment of FDI as a method of funding their operations.

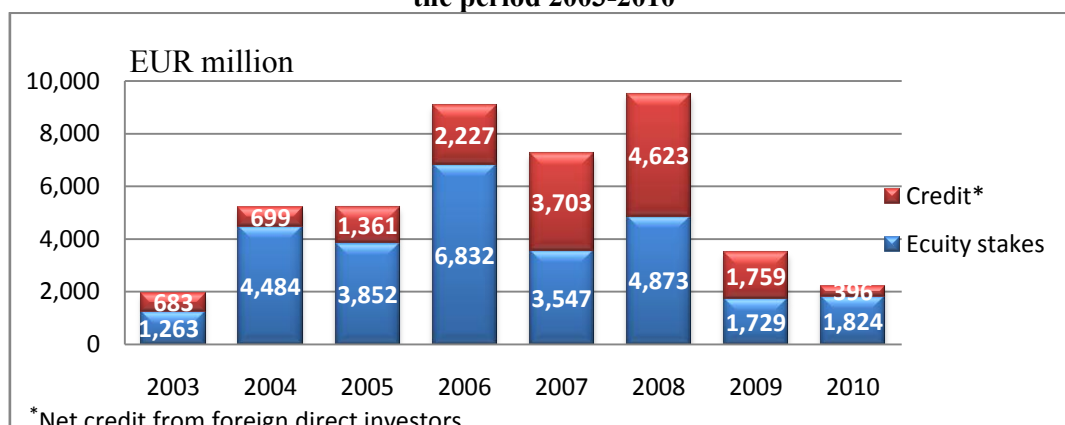
FDI include the transportation, beyond national borders, of a package of productive resources/inputs. These inputs may be either intangible (know-how, marketing, etc), or physical (share capital, raw materials, etc.). The transfer of inputs/resources occurs without the intervention of the market, that is, it takes place between two companies which are linked by ownership (Joong - Wan, 2003).

## 2. THE FLOWS OF THE FOREIGN DIRECT INVESTMENTS IN ROMANIA IN THE PERIOD 2003-2010

The investments in Romania recently allowed the ranking of this country in the statistics that analyze the flows of foreign direct investments in the South-East Europe, ranking it on notable places sometimes. Other statistics that relate to Romania in the perspective of membership of the European Union, points it somewhere to the medium volume of the direct investments attracted. The factors that led to the advent of the direct investments in the period 2003-2010 have been represented by its position in Europe, by the availability of the material and human resources, and last but not least, by the low wage costs. The largest volume of the foreign direct investments was attracted by Bucharest, followed by the counties from Transylvania and Wallachia, and at the opposite pole there were the counties Vrancea, Galați, Tulcea, Constanța and Brăila, where the highest rate of unemployment is recorded.

In the period 1990-2011, the volume of FDI has risen relatively rapidly in Romania, on one hand, due to their almost non-existent level during the beginning period of transition and on the other hand, to the relatively large profit opportunities that the foreign investors have been able to valorise in Romania, either through the Greenfield investments, or through purchases (mergers and acquisitions) or portfolio investments on emerging capital markets.

**Figure 1 - Trends in the FDI flows in the form of participating to the capital and credit in Romania in the period 2003-2010**



Source: [www.bnr.ro](http://www.bnr.ro)

Under the conditions of the Government programs and strategies of economic and social reform insufficiently grounded as a strategic vision of the priorities in time, of the privatization of the inefficient and effective assets or of various types of privatizations in sectors, the most part of

the FDI are focused on the privatisations of the effective assets, with the state remaining loser. On the other hand, the type of the greenfield investments that would be meant a „de novo” training for the private sector in Romania, were less practiced and agreed to by the foreign investors, whereas they would have cost a management and economic-financial effort larger than buying at a low price for the active investors, in service of the State or with minimum effort, that could be made functional.

**Table 1 - The flows of the FDI in Romania in the period 2003-2010**

<b>FDI FLOWS</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
<b>FDI flows - total</b>								
Eur million	1,946	5,183	5,213	9,059	7,250	9,496	3,488	2,220
percentage change from previous year	60,6	166,3	0,6	73,8	-20,0	31,0	-63,3	-36,4
<b>FDI flows with no significant privatisation operations **</b>								
Eur million	1,805	3,503	4,413	6,860	7,250	8,623	3,488	2,220
percentage change from previous year	48,9	94,1	26,0	55,4	5,7	18,9	-59,6	36,4

\*\*more than Eur 10 million

Source: www.bnr.ro

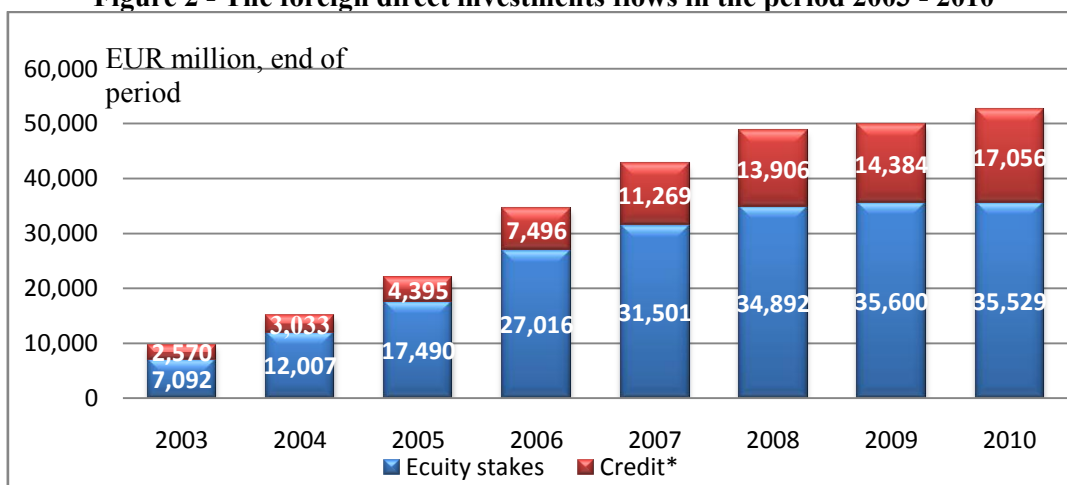
The annual FDI flows in the form of the loans and the equity holdings in the period 2003-2010, in Romania (Table 1) had a development characterized by the following sub periods: - 2003-2006, when the total annual flows of FDI increased from 1,94 billion euro to 9,05 billion euro, due to the major privatizations in Romania of the banking and industrial sectors (the petroleum and the petro chemistry, the metallurgy, the construction machinery); - 2007-2008, when the privatization in the banking sector and in the field of energy and utilities continued, the year 2008 being the peak year of FDI, with a volume of 9,49 billion euro; - 2009-2010, the annual total volume of FDI decreased dramatically compared to the previous years, reaching to 54,54 billion euro in 2010, as a result of the impact of the financial and economic crisis.

An analysis of each year in part leads to the following conclusion: the year 2003 registered a value of investments of about 1950 million. Increasing the value of the foreign investments in Romania exceeded by the year 2004 when the level reached 5183 million. In 2005, an amount roughly equal to that of the previous year. In 2006 the number of FDI increases, reaching 9059 million Euros, but the highest value being registered in 2008. The year 2007 attracts investments of 7250 million in Romania; this number was lower than in the previous year, but higher than in the previous years of the period considered. In 2009 the investments are half, compared to 2008 and in 2010 a decrease in the flow of FDI is noted, the loss is due to the financial crisis. High values of the foreign direct investments in Romania in 2006-2008 can be explained through the fiscal policy

adopted by the Government. The highest growth of the investments is in 2004 when they have a value of 2, 6 times higher compared to the year 2003.

During the 2003-2010, starting with the year 2008 with the economic and financial crisis, a balance of accumulated FDI with very small increases. The participations in the capital in the years 2009 and 2010 remained practically at the same level (Figure 2). The volume of the loans has increased, which indirectly leads to the conclusion that, in this period, the foreign firms have reduced the substantial or even ceased their net incomes from the investments made, some being strongly affected by the loss.

**Figure 2 - The foreign direct investments flows in the period 2003 - 2010**



Source: Foreign direct investment in Romania, BNR, 2010.

We note that the foreign direct investments did not achieve a leap of the productivity, nor did they make the Romanian economy an innovative player in the European market, because the foreign capital flows were not targeted to those sectors of the economy that produced sustainable economic growth, but by the speculative sectors such as the real estate and the retail.

The period 2003-2010 is characterized by a domestic demand more than by the internal offer of goods and services (gross domestic product). During this period, Romania has applied a set of economic policies which focused on reducing the domestic demand in order to reduce the gap between these two fundamental parameters of the general economic equilibrium.

On December 31st 2010, the final balance of the FDI was 52,585 million euro, more with 5,2% than of the ending balance of FDI in 2009, representing a rate of less than 50% in relation to the size of the GDP in the same year from Romania. The shares to the social capital (including reinvested profits) of the enterprises with FDI was 35,5 billion the euro in 2010, meaning 67,5% of the ending balance of FDI.

**Table 2 - The foreign direct investments stock in 2003-2010**

<b>FDI STOCK</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
<b>Total</b>								
Eur million	9,662	15,040	21,885	34,512	42,770	48,798	49,984	52,585
percentage change from previous year	...	55,7	45,5	57,7	23,9	14,1	2,4	5,2
<b>Equity stakes (including reinvested earnings*)</b>								
Eur million	7,092	12,007	17,490	27,016	31,501	34,892	35,600	35,529
percentage change from previous year	...	69,3	45,7	54,5	16,6	10,8	2,0	-0,2
<b>Credit**</b>								
Eur million	2,570	3,033	4,395	7,496	11,269	13,906	14,384	17,056
percentage change from previous year	...	18,0	44,9	70,6	50,3	23,4	3,4	18,6

\*in 2008, 2009 and 2010 equity stakes are consolidated with the net loss

\*\*net credit from foreign direct investors

Source: Foreign direct investment in Romania, BNR, 2010.

Throughout the period 2003-2010, the shares of FDI to the capital, including the reinvested profits in Romania increased 5 times, while the volume of the loans increased 6,3 times, which means a greater need of the subsidiaries discography, particularly during the years of crisis, but also the additional interest of parent company to achieve net revenue from the interest on the financial market of Romania, are relatively high when compared with those of the origin country or in the other countries.

In 2010, the net flow of FDI was 54,54 billion euro, of which: 1,82 billion euro (meaning 82,2% from the net flow of FDI) the net holdings of foreign direct investors in the capital of enterprises with FDI. The net credit of 396 million euro received by the firms with FDI from direct foreign investors in 2010, including within the group represented a rate of 17,8% in the net flow of FDI.

The most important results of the economic policy focused on the Romania's access to the foreign markets of the capital in favourable conditions of the interest, the health of the public finances, by strictly budget deficit and improving the degree of completion the collection of the revenue, the financial reform, so that the financial policy should become a stimulating factor of the economic growth, of the macroeconomic stabilization and the enhance of the economic growth.

## CONCLUSIONS

The foreign direct investments (FDI) bring their contribution to the growth. They create employment and optimize the allocation of resources, the technology transfer and stimulate the trade.

Doing business in Romania requires an economic freedom and a friendly taxation for the entrepreneurs, including to the foreign investors. GDP per capita, the labour productivity, the exports and the average salary in Romania are among the lowest in the European Union. The accession of Romania to the European Union has brought about an improvement in the business environment in Romania, thus becoming an attractive target for foreign investment.

Foreign direct investments can have an important function in the economic restructuring and recovery on a sustained increase in Romania. At the same time, they can play a significant role in the restructuring of the enterprises and the institutions that have an effect on them. Foreign direct investments are spread out across all the sectors of the economy, and investors come mainly from Europe. Romania attracts foreign investors because of the low wage costs and well-trained workforce. Multinational companies can use their already formed links to import and export products in and from Romania, in this way the Romanian economy increases in the world economy. The potential of the investment of Romania was always attractive to the foreign investors. With the changes of the legislation of Romania and the beginning of the reform of privatization of State-owned companies in various industries have resulted opportunities for penetrating the Romanian market, starting with the year 1997.

In the recent years, there has been an upward flow of investments in Romania, which could mean that our country is on a path of increasing. Of course, the effects of the recession have had a negative impact on the foreign investments, which were down by almost half compared to the so-called boom and Romania has a record in 2007 and 2008. However, the flow of the foreign investments, in addition to the positive effects, produces the widening disparity among the developed regions of Romania.

Whereas, in the past few decades, between the countries of the world there is a red-hot competition for creating the most favourable conditions for attracting FDI, the world experience shows that the improvements in the investments climate is the main condition for attracting foreign investors.

FDI represents an important part of any country's economy development and the functioning of its market economy principles. They have a great importance for the strengthening of the economy of the countries in transition and the integration of this category of countries into the world economy. Using FDI, the process of modernization of the national economies takes place, in particular for those in transition, through the implementation of the advanced technologies, the know-how, the equipment, the most powerful of the new standards of quality, by switching to a higher type of the economic growth.

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